

Weekly Economic Commentary



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Extending the Extended Period?

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ECONOMIC CALENDAR

Tuesday, Apr 27 Consumer Confidence <i>Apr</i>	Friday, Apr 30 Employment Cost Index <i>Q1</i>
Wednesday, Apr 28 FOMC	Real GDP <i>Q1</i>
Thursday, Apr 29 Initial Claims <i>wk 04/24</i>	Chicago PMI <i>Apr</i>
	U of Mich Consumer Sentiment <i>Apr</i>

Although there are several notable economic reports due out this week, including the first look at real gross domestic product (GDP) growth in the first quarter of 2010, market participants are likely to be focused on the outcome of the Federal Reserve's (Fed) FOMC meeting. The meeting (which is on Wednesday, April 28) is not likely to result in an immediate change in the fed funds interest rate set by the FOMC—the rate at which banks lend to each other overnight.

However, the FOMC may change the language in the statement that is released at the conclusion of each FOMC meeting, which occurs eight times a year. Each FOMC statement since March 2009 has included the phrase “economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period.”

Beginning in November 2009, the FOMC slightly modified the “extended period” language by adding a conditional statement to the phrase: “economic conditions, including low rates of resource utilization, subdued inflation trends, and stable inflation expectations, are likely to warrant exceptionally low levels of the federal funds rate for an extended period.”

In recent public appearances, Fed Chairman Ben Bernanke and Fed Vice Chairman Don Kohn, have hinted that the FOMC may be moving away from a time-based (i.e. rates low for an extended period) promise to a more data-dependent (i.e. is inflation or economic growth or inflation expectations tracking to the Fed's forecast) promise on rates. In short, while the FOMC may leave “extended period” in the next FOMC statement, it may modify the phrase, making low rates for an “extended period” dependent on continued low inflation readings, low and stable inflation expectations and slack resource utilization, as well as the economy continuing to track the FOMC's forecast.

Thus, in our view, the economic forecast made by FOMC meeting participants at this week's FOMC meeting may take on some importance for financial markets. The FOMC may establish new forecast ranges for key economic variables at the April 28 FOMC meeting including:

- GDP growth,
- The unemployment rate,
- Overall inflation, and
- Core inflation-inflation excluding food and energy prices.

Those forecasts will be made available to the public on May 19, along with the minutes of the meeting.

Highlights

This week will be dominated by the Federal Open Market Committee's (FOMC) decision on monetary policy.

Fed policymakers are unlikely to raise interest rates at the April 28 FOMC meeting, but may adjust the language of the policy statement.



Two aspects of the new forecasts:

- How they changed since the last time the FOMC published a forecast, which was on February 17, 2010 for the forecast made at the January 26-27 FOMC meeting, and
- How the updated forecasts jive with the latest consensus forecast for each of those variables may be the next key event for monetary policy.

Economic Projections of Federal Reserve Governors and Reserve Bank Presidents, Made at the January 2010 FOMC Meeting

Variable	Central Tendency				Range			
	2010	2011	2012	Longer run	2010	2011	2012	Longer run
Change in real GDP	2.8 to 3.5	3.4 to 4.5	3.5 to 4.5	2.5 to 2.8	2.3 to 4.0	2.7 to 4.7	3.0 to 5.0	2.4 to 3.0
November Projection	2.5 to 3.5	3.4 to 4.5	3.5 to 4.8	2.5 to 2.8	2.0 to 4.0	2.5 to 4.6	2.8 to 5.0	2.4 to 3.0
Unemployment Rate	9.5 to 9.7	8.2 to 8.5	6.6 to 7.5	5.0 to 5.2	8.6 to 10.0	7.2 to 8.8	6.1 to 7.6	4.9 to 6.3
November Projection	9.3 to 9.7	8.2 to 8.6	6.8 to 7.5	5.0 to 5.2	8.6 to 10.2	7.2 to 8.7	6.1 to 7.6	4.8 to 6.3
PCE Inflation	1.4 to 1.7	1.1 to 2.0	1.3 to 2.0	1.7 to 2.0	1.2 to 2.0	1.0 to 2.4	0.8 to 2.0	1.5 to 2.0
November Projection	1.3 to 1.6	1.0 to 1.9	1.2 to 1.9	1.7 to 2.0	1.1 to 2.0	0.6 to 2.4	0.2 to 2.3	1.5 to 2.0
Core PCE Inflation	1.1 to 1.7	1.0 to 1.9	1.2 to 1.9		1.0 to 2.0	0.9 to 2.4	0.8 to 2.0	
November Projection	1.0 to 1.5	1.0 to 1.6	1.0 to 1.7		0.9 to 2.0	0.5 to 2.4	0.2 to 2.3	

Source: Federal Reserve, March 2009

IMPORTANT DISCLOSURES

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The discount rate: The rate at which member banks may borrow short term funds directly from a Federal Reserve Bank. The discount rate is one of the two interest rates set by the Fed, the other being the Federal funds rate. The Fed actually controls this rate directly, but this fact does not really help in policy implementation, since banks can also find such funds elsewhere.

PCE inflation and core PCE inflation are the percentage rates of change in, respectively, the price index for personal consumption expenditures (PCE) and the price index for PCE excluding food and energy. Projections for the unemployment rate are for the average civilian unemployment rate in the fourth quarter of the year indicated. Each participant's projections are based on his or her assessment of appropriate monetary policy. Longer-run projections represent each participant's assessment of the rate to which each variable would be expected to converge under appropriate monetary policy and in the absence of further shocks to the economy. The November projections were made in conjunction with the meeting of the Federal Open Market Committee on November 3-4, 2009.

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