FOMC Meeting 12-16-15

Sung Won Sohn

California State University CI

213-247 5012

- After six and half years, today's lift-off was an anti-climax. Chair Yellen made it very clear a December hike was highly likely. If the rate hadn't gone up, more uncertainty and volatility in the financial markets would have ensued. It wanted to start raising the rate now. If waited longer, they believe, future rate increases could be steeper and more abrupt.

- The central bank expects "gradual" increases in coming months allowing it to gauge the impact of small increases on the economy and financial markets. The FOMC wanted to leave some wiggle room in the future by not committing itself to a predictable series of rate increases.

- Today's move is greatly based on Yellen's belief in Phillips's Curve. She believes lower jobless rate and a tighter labor market will usher in more inflation. The data does not support lift-off today, however. While employment gains have been good, the overall economic growth as measured by GDP is moderate at best. As the economy approaches full employment, the room for future economic improvements is limited.

- Inflation has been lagging below the FOMC's projections and is unlikely to reach the target growth rate of 2 percent in the medium term. Global deflationary psychology, not the unemployment rate is the reason behind it. Higher interest rates will lower inflation expectations raising the real interest rate. The real interest rate, the difference between nominal rate and inflation expectation, will hurt already modest economic growth.

- The forces which caused the central bank to delay the hike in September has gotten worse not better. Commodity prices, the value of EM currencies and turbulence in the credit markets are some examples. Tightening moves by the Federal Reserve will further accelerate capital outflows from emerging markets, weaken their currencies and slow economic growth there. Countries including Brazil, Turkey, India, South Africa, etc. have been suffering from capital outflows, low commodity prices, slow economic growth etc. Higher interest rates by the FOMC Would exacerbate the economic problems. Even China, the second largest economy in the world, is experiencing significant economic slowdown and uncertainties in the financial markets.