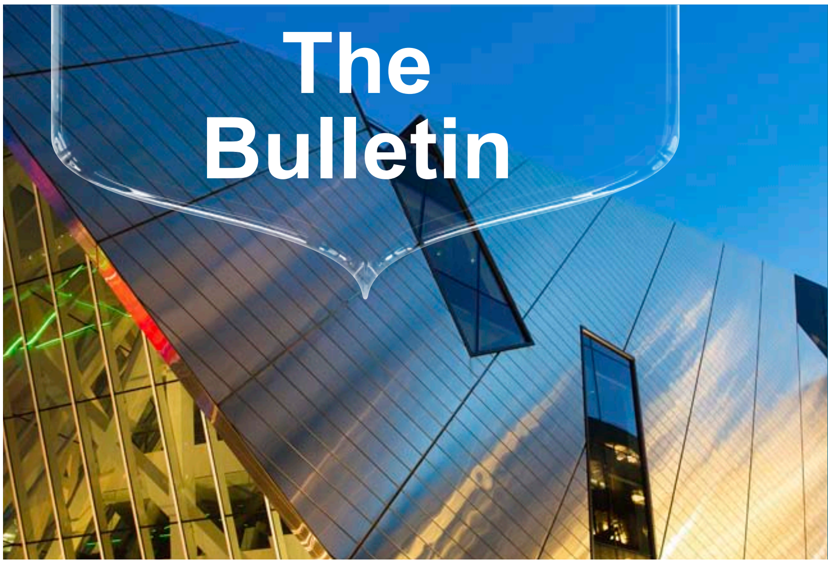
Bank of Ireland

Economic Research Unit



November 2015

Fed 'lift off' in December

Overview The Fed left interest rates unchanged in October but said it would assess whether an increase is 'appropriate' at its December 15/16 meeting. The Chair of the Fed, Janet Yellen, subsequently stated that a rate rise next month is a 'live possibility' if labour market conditions continued to improve. In this regard, the October employment report showed job gains reaccelerating, unemployment falling and earnings growth picking up, which would seem to copper-fasten a December hike. Meanwhile, the ECB has said it will examine the need for further stimulus for the Euro are economy at its next meeting (December 3) in light of 'downside risks' to the growth and inflation outlook, indicating that this could include a cut in interest rates and/or an expansion of its asset purchases (QE) programme (a slight easing in GDP growth in Q3 according to the preliminary estimate will have added to the ECB's concerns). The stark divergence in the monetary policy outlook in the respective economies has contributed to a sharp decline in the euro/dollar exchange rate over the past month. It has fallen by the best part of 7% - from almost $1.15 to $1.07 - and is likely to lose some further ground over the coming months.

Euro Area growth eases a little

UK PMI rebounds in October

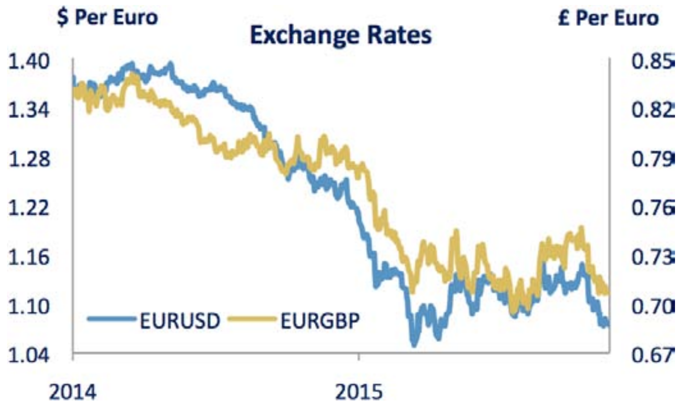
US unemployment falls further

Diary	Euro Area	UK	US
Central Bank Meetings	Dec 3	Dec 10	Dec 15/16
GDP	Dec 8	Nov 27	Nov 24
Inflation	Dec 2	Dec 15	Dec 15
Labour Market	Dec 1	Dec 16	Dec 4

Forecasts	End Dec 2015	End Mar 2016	End Jun 2016	End Sep 2016
Exchange Rates				
€/$	1.07	1.06	1.05	1.05
€/£	0.71	0.70	0.69	0.70
£/$	1.52	1.51	1.52	1.50
Swap Rates (5 year)				
Euro Area	0.25	0.35	0.50	0.65
UK	1.60	1.80	2.00	2.20
US	1.70	1.90	2.20	2.40

Euro Area growth eases a little

The economy expanded again in Q3 athough the pace of growth eased to 0.3% q-o-q from 0.4% in Q2. Amongst the largest economies, growth in Germany and Italy slowed a little, but picked up in France (after a weak second quarter). On an annual basis, the Euro area economy grew by 1.6% in Q3 and averaged 1.4% over the first three quarters of 2015, after expanding by 0.9% in 2014 as a whole. The OECD is forecasting full year growth of 1.5%, strengthening to 1.8% in 2016 (the EU Commission is projecting 1.6% and 1.8% respectively). The ECB left interest rates unchanged in October, but said it would 're-examine' its monetary policy stance in December in light of 'downside risks to the outlook for growth and inflation'. This could entail the ECB lowering interest rates and/or expanding its current asset purchases (QE) programme. The prospect of further policy action has resulted in a fall in the euro over the past month.



UK PMI rebounds in October

GDP growth eased in Q3 (to 0.5% q-o-q) with a reacceleration in services activty offset by falls in manufacturing and construction. This may prove short-lived as the composite PMI rebounded to 55.4 in October from 53.3 at the end of Q3. The OECD is forecasting annual GDP growth of 2.4% for both 2015 and 2016, in line with the projections in our new UK Outlook (click here to view). Headline inflation is subdued at -0.1%, though the core rate is running at 1.1%. Unemployment fell to 5.3% in Q3 on the back of continued job gains, while the growth in annual earnings ex bonuses softened (to 2.5%). The MPC left interest rates unchanged in November. Its latest Inflation Report sees continued growth in 2016-2017, with unemployment falling further and inflation rising to slightly above the 2% target by end-2017. Given this outlook, we expect the MPC to raise rates over the first half of 2016, though the market is not 'pricing in' a full 25bps hike until late Q4.

US unemployment falls further

GDP growth fell back to 0.4% q-o-q in Q3 from 1.0% in Q2. However, this was due largely to a slower rate of inventory building, as domestic spending grew strongly. On an annual basis, GDP rose by 2.0% and averaged 2.5% over the first 9 months of 2015. The OECD expects full year growth of 2.4%, rising a little to 2.5% in 2016. Job gains picked up strongly in October (to 271,000 from 137,000 in September) and the unemployment rate fell to 5.0%, the lowest since April 2008. The Fed kept rates unchanged in October, but stated it would assess whether a hike is 'appropriate' at December's meeting. Chair Yellen subsequently said an increase next month is a 'live possibility', and the continuing fall in the unemployment rate would seem to cement such a move. The market now sees a much greater chance of a hike than was the case up until recently, which has contributed to a rise in bond yields and a strengthening of the dollar over the past month.

Contact us at:
economics@boi.com

Dr. Loretta O'Sullivan
Chief Economist
+353 (0) 766 244 267

Michael Crowley
Senior Economist
+353 (0) 766 244 268