

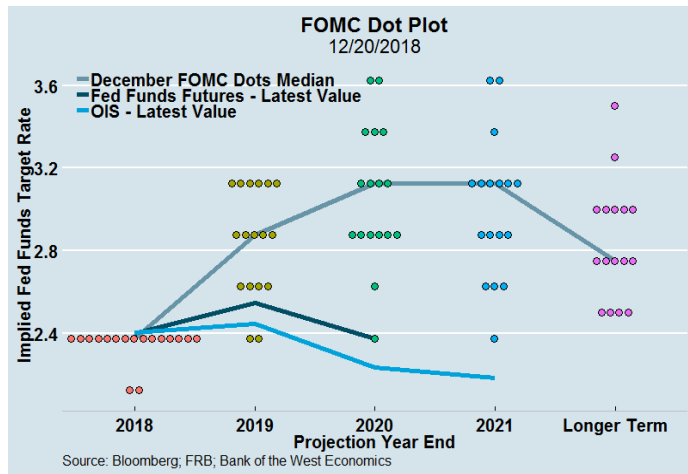
Date	Indicator	For	Estimate	Consensus*	Previous Period
24-Dec-2018	Chicago Fed Nat Activity Index	Nov	NA	NA	24.0%
26-Dec-2018	S&P CoreLogic CS 20-City MoM SA	Oct	0.2%	0.3%	0.3%
26-Dec-2018	Richmond Fed Manufacturing Index	Dec	12.0	16.0	14.0
27-Dec-2018	Initial Jobless Claims	22-Dec	217k	NA	214k
27-Dec-2018	FHFA House Price Index MoM	Oct	0.2%	0.3%	0.2%
27-Dec-2018	New Home Sales	Nov	575k	569k	544k
27-Dec-2018	Conf. Board Consumer Confidence	Dec	135.0	133.2	135.7
28-Dec-2018	Advance Goods Trade Balance	Nov	-\$76.0b	-\$75.5b	-\$77.0b
28-Dec-2018	Wholesale Inventories MoM	Nov P	0.5%	NA	0.8%
28-Dec-2018	Chicago Purchasing Manager	Dec	60.0	61.0	66.4
28-Dec-2018	Pending Home Sales MoM	Nov	1.0%	1.0%	-2.6%
31-Dec-2018	Dallas Fed Manufacturing Activity	Dec	15.0	17.6	17.6
2-Jan-2019	Markit US Manufacturing PMI	Dec F	53.9	NA	53.9
3-Jan-2019	ADP Employment Change	Dec	170k	175k	179k
3-Jan-2019	Initial Jobless Claims	29-Dec	NA	NA	NA
3-Jan-2019	Construction Spending MoM	Nov	0.2%	0.3%	-0.1%
3-Jan-2019	ISM Manufacturing	Dec	57.8	58.0	59.3
3-Jan-2019	Wards Total Vehicle Sales	Dec	17.30m	17.40m	17.40m
4-Jan-2019	Change in Nonfarm Payrolls	Dec	175k	180k	155k
4-Jan-2019	Change in Manufacturing Payrolls	Dec	19k	23k	27k
4-Jan-2019	Unemployment Rate	Dec	3.7%	3.7%	3.7%
4-Jan-2019	Average Hourly Earnings MoM	Dec	0.3%	0.3%	0.2%
4-Jan-2019	Average Weekly Hours All Employees	Dec	34.5	34.5	34.4
4-Jan-2019	Markit US Composite PMI	Dec F	NA	NA	53.6
4-Jan-2019	Markit US Services PMI	Dec F	53.5	NA	53.4

\*Consensus from Bloomberg

## Dissecting the Dots

Every newspaper article on the Fed decision this week cited the downward migration of the median dot-plot from 3 hikes next year to just 2 hikes. But just looking at the median forecast gives one a false sense of precision about the future of U.S. interest rates. If you dig a little deeper into the dots, you see just how divided the FOMC members really are about the future course of monetary policy today.

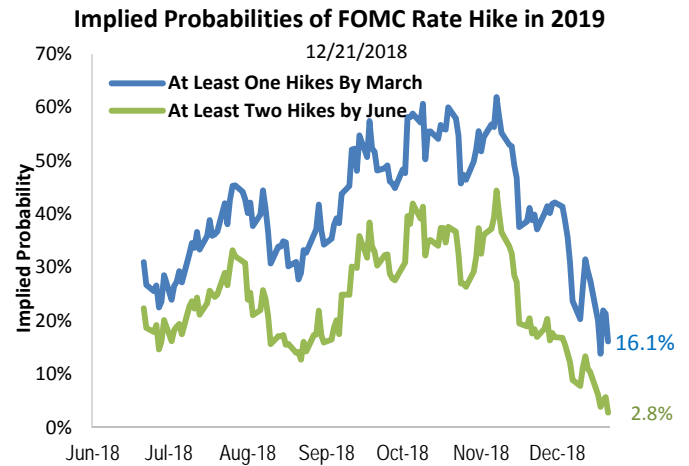
Fed Funds Forecasts Are All Over the Map at the Moment



The FOMC members neatly divide into three distinct camps when it comes to interest rate expectations for 2019. About 1/3 of the members expect one hike or less in 2019, 1/3 expect two hikes, and 1/3 expect three hikes in 2019. Of the 1/3 that expect one hike or less, only two FOMC members see no rate hikes in 2019. And the dots keep rising into 2020 too. So, a pretty wide distribution of rate expectations over the near-term, but the bottom-line from the FOMC seems to be “What me worry?” despite a substantial amount of market volatility rocking your portfolio. The downward adjustments to the FOMC’s GDP, inflation, and Fed funds rate forecast since the September FOMC meeting was relatively minor.

The market appears to have come to a far different conclusion than the FOMC about the proper stance of monetary policy and interest rates. As the end of trading today, the Fed funds futures market was placing only a 16% probability of a Fed rate hike in March and only a 2.8% probability that the Fed would follow up a March hike with another one in June.

Still Pricing Out Fed Rate Hikes in 2019



Source: Bloomberg

But even more chilling is what is happening in the overnight index swap futures (OIS) market. Not only is this market not pricing in any rate hikes for 2019, but it is actively pricing in Fed rate cuts in 2020 and 2021. This means a lot of investors are positioning themselves for a Fed monetary policy mistake, perhaps an impending recession that will necessitate the Fed to reverse course and start cutting interest rates again by 2020. Another way to view this is to look at the inversion of the 5 Yr and 2 Yr Treasury note yields. The differences in these interest rate projections reveal fundamental differences in the near-term outlook for the U.S. and global economy, and both can’t be right.

It is important to note that markets get things wrong sometimes, they can overreact especially during times of market panic like we seem to be going through right now, but sometimes markets see our economic future before analysts do, or even the Fed does. Also financial panics have a nasty way of morphing into a self-fulfilling prophecy. Market pessimism and wealth declines can lead to changes in consumer and business behavior that create the next downturn. Which are we in today? My belief is closer to the FOMC’s that this is just an overreaction to the stock selloff and other potential downside risks lurking out there, but only time will tell for sure. Happy Holidays!

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**Key Economic and Interest Rate Forecasts**

<b>Economic Data</b>	<b>2018.1</b>	<b>2018.2</b>	<b>2018.3</b>	<b>2018.4</b>	<b>2019.1</b>	<b>2019.2</b>	<b>2019.3</b>	<b>2019.4</b>	<b>2020.1</b>	<b>2020.2</b>	<b>2020.3</b>	<b>2020.4</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>
Real GDP*	2.2	4.2	3.4	2.5	2.1	2.0	1.8	1.7	1.0	0.6	0.5	0.5	2.2	2.9	2.4	1.1
Personal Consumption Expenditures*	0.5	3.8	3.5	3.5	2.3	2.3	2.1	1.9	1.5	1.0	1.0	1.0	2.5	2.7	2.7	1.5
Non-residential Fixed Investment*	11.5	8.7	2.5	5.7	3.8	4.1	3.7	3.4	1.5	1.5	1.5	1.5	5.3	6.9	4.4	2.3
Private Housing Starts (000s units)	1,317	1,261	1,234	1,250	1,260	1,240	1,220	1,210	1,190	1,185	1,180	1,175	1,208	1,266	1,233	1,183
Vehicle Sales (mill. Units, annualized)	17.1	17.1	16.9	17.4	16.9	16.8	16.7	16.5	16.2	15.9	15.6	15.9	17.2	17.1	16.7	15.9
Industrial Production*	2.5	5.3	4.7	2.7	2.1	2.0	1.7	1.5	-0.5	-1.0	-1.0	-1.0	1.6	3.9	2.6	0.1
Nonfarm Payroll Employment (mil.)	148.1	148.7	149.3	149.8	150.3	150.7	151.1	151.4	151.5	151.1	150.7	150.5	146.6	149.0	150.9	151.0
Unemployment rate	4.1	3.9	3.8	3.7	3.6	3.5	3.5	3.6	3.8	4.2	4.5	4.8	4.4	3.9	3.6	4.3
Consumer Price Index* (percent)	3.5	1.7	2.0	2.8	2.5	2.0	2.1	2.1	1.8	1.8	1.7	1.6	2.1	2.5	2.3	1.9
"Core" CPI* (percent)	3.0	1.8	2.0	1.9	2.2	2.1	2.1	2.1	2.0	1.9	1.8	1.8	1.8	2.1	2.1	2.0
PPI (finished goods)* (percent)	3.6	2.9	2.0	2.8	2.0	1.9	1.7	1.7	1.3	1.4	1.4	1.4	3.2	3.2	2.1	1.5
Trade Weighted Dollar (Fed BOG, major)	86.2	88.2	90.2	91.3	91.0	90.6	89.6	88.5	88.3	88.0	87.5	87.0	91.1	89.0	89.9	87.7
Crude Oil Prices -WTI (\$ per barrel)	63	68	70	63	52	52	51	51	50	50	46	47	51	66	52	48

\*Quarterly Data Percent Change At Annual Rate; Annual Data Year-on-Year % Chg, or Annual Average.

<b>Financial Data</b>	<b>History</b>				<b>Forecast</b>								<b>Annual Average</b>			
	<b>2018.1</b>	<b>2018.2</b>	<b>2018.3</b>	<b>2018.4</b>	<b>2019.1</b>	<b>2019.2</b>	<b>2019.3</b>	<b>2019.4</b>	<b>2020.1</b>	<b>2020.2</b>	<b>2020.3</b>	<b>2020.4</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>
S & P 500	2,733	2,703	2,850										2,449			
Dow Jones Industrial Average	25,127	24,556	25,595										21,745			
Federal Funds Rate (effective)	1.45	1.74	1.92	2.19	2.46	2.71	2.88	2.88	2.79	2.54	2.29	2.04	1.00	1.83	2.73	2.42
Treasury-3 Month Bills (yield)	1.58	1.87	2.07	2.32	2.58	2.79	2.95	2.91	2.70	2.35	2.10	1.84	0.95	1.96	2.81	2.25
Treasury-2 Year Notes (yield)	2.16	2.48	2.67	2.83	2.91	3.00	2.98	2.95	2.90	2.65	2.40	2.15	1.40	2.53	2.96	2.53
Treasury-5 Year Notes (yield)	2.53	2.77	2.81	2.89	3.09	3.19	3.21	3.15	3.05	2.80	2.60	2.35	1.91	2.75	3.16	2.70
Treasury-10 Year Notes (yield)	2.76	2.92	2.92	3.08	3.22	3.32	3.38	3.31	3.21	3.00	2.80	2.65	2.33	2.92	3.31	2.92
Treasury-30 Year Notes (yield)	3.03	3.09	3.06	3.30	3.43	3.56	3.64	3.55	3.45	3.40	3.20	2.95	2.90	3.12	3.55	3.25
Prime Rate	4.53	4.80	5.01	5.25	5.50	5.75	6.00	6.00	5.90	5.60	5.35	5.10	4.10	4.90	5.81	5.49
Libor 3-Mo. U.S. Dollar	1.93	2.34	2.34	2.57	2.79	3.01	3.12	3.13	2.95	2.70	2.42	2.13	1.26	2.29	3.01	2.55
Mortgage-30 Year (yield)	4.28	4.54	4.57	4.84	4.92	5.03	5.09	5.02	4.95	4.75	4.60	4.50	3.99	4.56	5.02	4.70
BAA Corporate (yield)	4.47	4.78	4.81	5.15	5.40	5.60	5.80	6.10	6.30	6.40	6.35	6.20	4.44	4.80	5.73	6.31

Source: Bank of the West Economics, Bloomberg, Federal Reserve