February 2016

QUEST Monthly Economic Update

Fourth quarter real GDP growth revised upward to 1.0%

Economists expect no increase in federal funds rate until at least June

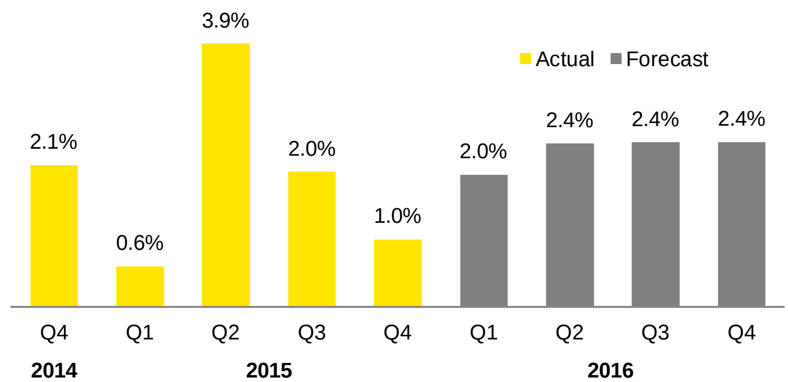
Ernst & Young LLP's Quantitative Economics and Statistics (QUEST) group has developed the following monthly publication summarizing the latest key economic and employment trends in a short, easy-to-read format. Developments such as growth trends in US gross domestic product (GDP), US employment and Federal Reserve activity are highlighted, as are economic trends outside the United States that may affect US businesses.

US economic trends

The February 26 GDP release indicated that real GDP in the fourth quarter grew at a real annualized rate of 1.0%, an upward revision of the estimate cited in January's Economic Update.

Annualized real GDP growth of 2.0% is expected for Q1 2016, according to *The Wall Street Journal Economic Forecasting Survey*. In the prior forecast, cited in January's Economic Update, annualized real GDP was predicted to increase by 2.4% in Q1 2016. The survey also indicates that real GDP is expected to increase at an annualized growth of 2.4% in Q2 2016.

Figure 1. US quarterly real GDP growth at annualized rates



Source: Bureau of Economic Analysis and *The Wall Street Journal Economic Forecasting Survey.*

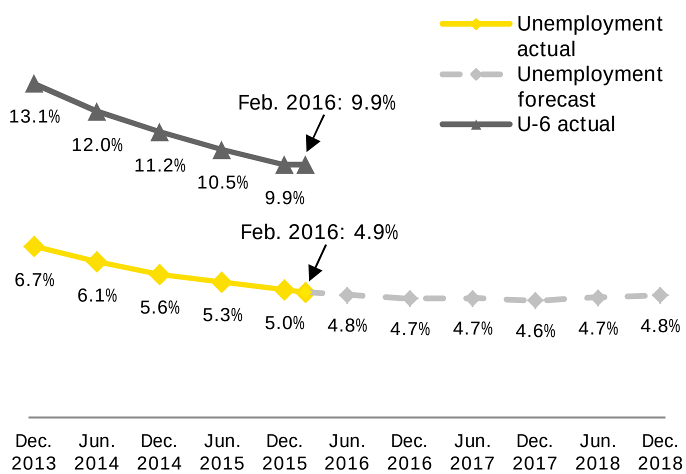
Building a better working world

The latest US jobs report indicated that employment grew by 242,000 jobs in February and the unemployment rate stayed flat at 4.9%.

The Bureau of Labor Statistics' underemployment U-6 rate, another closely watched measure of slackness in labor markets that includes the total unemployed, marginally attached workers and workers employed part-time for economic reasons, also remained unchanged at 9.9%. (Note: A forecast of the U-6 rate is not available.)

Employment gains for the months of December and January were revised to +271,000 and +172,000 jobs, respectively. Combined, job gains were 30,000 greater for these two months than previously reported.

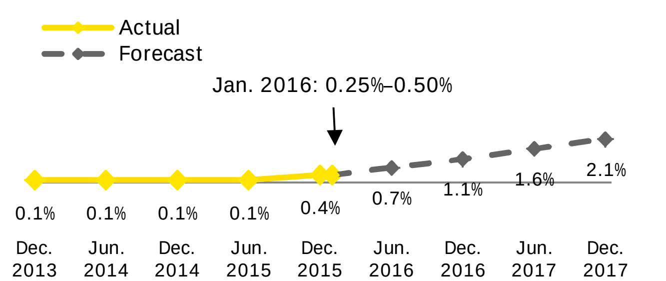
Figure 2. US unemployment rate



Source: Bureau of Labor Statistics and *The Wall Street Journal Economic Forecasting Survey.*

The federal funds rate is currently set to a target range of 0.25% to 0.50%. The Federal Reserve Board (FRB) will meet next on March 15-16. Changes to the federal funds rate will depend on the FRB's assessment of economic conditions relative to its goals of full employment and a 2% inflation rate target.

Figure 3. US federal funds rate

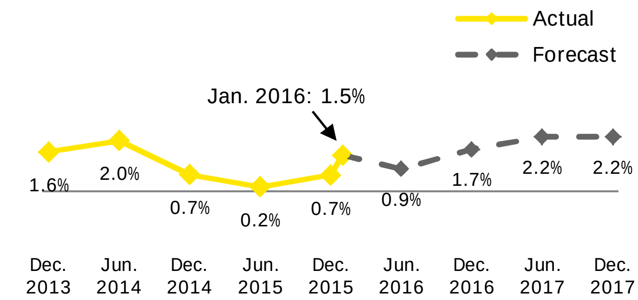


Note: The federal funds rate was set between 0.00% and 0.25% from December 2008 until December 2015.

Source: Bureau of Economic Analysis and *The Wall Street Journal Economic Forecasting Survey*.

As shown in Figure 4, the inflation rate, as measured by the change in the Consumer Price Index (CPI), was 1.5% in January 2016 – the highest level since December 2014. The inflation rate is expected to decrease to 0.9% by June 2016 and then increase toward the FRB's target of 2% by the end of 2016.

Figure 4. US CPI year-over-year growth rate



Source: Bureau of Labor Statistics and *The Wall Street Journal Economic Forecasting Survey.*

Economic trends outside the United States

- The International Monetary Fund (IMF) predicts real Russian GDP will decline by 1.0% in 2016 due to persistent low oil prices and sanctions. Oil prices have declined by more than 66% from their 2014 high to around $30/barrel as worldwide daily supply exceeds demand by 2 million barrels. Low prices may also put pressure on Russian government spending because roughly 50% of Russian government revenue comes from oil and gas taxes.
- The IMF continues to predict 2.2% growth in UK real GDP for 2016 and 2017 despite uncertainty surrounding the June 23, 2016 referendum on whether to stay in the European Union. UK Prime Minister David Cameron has pushed for concessions on migration and financial regulation that would help keep the UK in the EU.

Source*:* EY, Bloomberg and the IMF.

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