ECONOMIC UPDATE

REGIONS

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March FOMC Meeting: Hawkishly Dovish, Or Dovishly Hawkish?

- The FOMC raised the Fed funds rate target range by 25 basis points, taking the mid-point to 1.625 percent
- The "dot plot" again implies three 25-basis point hikes in the target range mid-point in 2018, three in 2019, and two in 2020

To the surprise of no one, the FOMC raised the Fed funds rate target range by 25-basis points at the conclusion of their two-day meeting, putting the mid-point at 1.625 percent. The uncertainty surrounding the March meeting, however, revolved around whether the updated dot plot would imply a total of three or four such hikes in 2018 after the prior (December 2017) dot plot implied three such hikes. While the updated dot plot implies a total of three 25-basis point hikes in 2018, it was a close call – had one additional FOMC member shifted into the four-hike camp, the median dot would have shifted up. But, the implied trajectory of the funds rate in both 2019 and 2020 is now steeper than was the case in the prior projections, with the dot plot implying a total of three hikes in 2019 and two in 2020. At the same time, updated economic projections show the Committee expects faster growth and lower unemployment in 2018 and 2019 than previously had been the case but virtually no change in expected inflation. There were no dissents in today's vote to raise the funds rate.

While the specifics changed a bit, such as an acknowledgement that growth in both household spending and business investment had moderated from strong Q4 2017 readings, the assessment of current economic conditions is basically upbeat. While much of the Q1 data to date have surprised to the downside, this is the same pattern seen over recent years and did not sway the Committee's assessment of current conditions. Indeed, a new sentence in today's statement notes that "the economic outlook has strengthened in recent months." Without specifically calling out fiscal policy, the Committee clearly expects the fiscal stimulus to juice growth this year and next. The mid-point of the range of real GDP growth estimates for 2018 now stands at 2.8 percent, with the mid-point of estimates for 2019 now at 2.4 percent.

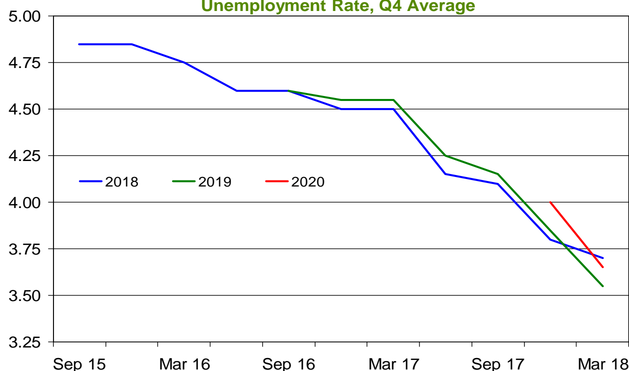
This upgrade to near-term growth stands out for two reasons. First, the median estimate of the economy's long-term (i.e., potential) rate of sustainable growth remains at 1.8 percent, meaning that on the whole the Committee sees little supply-side effects from the fiscal stimulus, specifically no lift to productivity growth as a result of firmer business investment spending. While Chairman Powell did note in his press conference that the Committee is "hopeful" the tax bill will foster supply side effects, any such hopes don't appear in the longer run growth forecast. Second, despite upgraded expectations for growth in the near-term there is virtually no change in the Committee's inflation outlook. The mid-point of the range of estimates of the PCE deflator remains at 1.9 percent for 2018 and for 2019 moved up only slightly, from 2.05 percent to 2.10 percent.

Chairman Powell did note in his press conference that "there is no sense in the data we are on the cusp" of a significant acceleration in inflation, and it is worth keeping in mind that the Committee does, collectively, expect some acceleration this year. Today's projections simply suggest the Committee has yet to see any evidence that inflation will accelerate more than they expect. At the same time, Chairman Powell did note that wage gains remain moderate, which for many Committee members is a key flash point for inflation expectations. The updated projections do show a lower expected unemployment rate for 2018 (a Q4 average of 3.7 percent) and 2019 (a Q4 average of 3.55 percent), but the median estimate of the longer run (i.e., full employment) rate stands at 4.5 percent. This seems a direct challenge to the "Phillips Curve" model that so many Committee members seem wedded to.

The median estimate of the long-run Fed funds rate stands at 2.875 percent, consistent with relatively slow longer-run growth. The dot plot implies the funds rate target range mid-point will finish 2020 at 3.375 percent; Chairman Powell characterized this as "moderately restrictive," but also cautioned against putting too much stock into forecasts three years out. It is worth noting Chairman Powell's frequent use of the term "uncertainty" regarding the effects of fiscal policy and the true value of the "full employment" value of the unemployment rate. Mr. Powell also noted downside risks from trade policy have grown. On the whole, Mr. Powell sent, at least in our view, a strong signal that the FOMC can and will respond to economic and financial conditions evolving differently than may seem likely at this point in time.

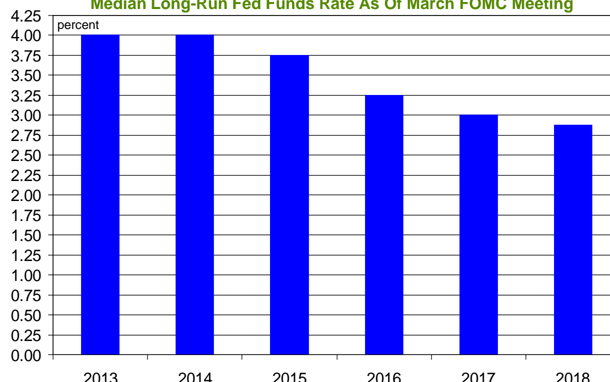
Mid-Point Of FOMC Central Tendency Forecasts

Unemployment Rate, Q4 Average



"Neutral" Just Isn't What It Used To Be . . .

Median Long-Run Fed Funds Rate As Of March FOMC Meeting



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