ECONOMIC UPDATE
REGIONS
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January FOMC Meeting: "Patient" And "Flexible" But Not Necessarily Done

- The FOMC left the Fed funds rate target range unchanged, with the mid-point of the target range remaining at 2.375 percent
- The Committee will be patient in terms of any further increases in the funds rate, and flexible in its approach to balance sheet management

To the surprise of no one, the FOMC made no changes to the Fed funds rate target range at the conclusion of their two-day meeting, leaving the mid-point of the target range at 2.375 percent. With virtually no chance of a change in the funds rate target range and no updates to the Committee's economic and financial projections, the main questions going into the meeting pertained to the Committee's post-meeting policy statement – the assessment of current economic conditions, and forward guidance around the path of the funds rate – and Chairman Powell's post-meeting press conference. The two main takeaways from the statement and Chairman Powell's press conference are patience and flexibility – patience in terms of future changes in the funds rate, and flexibility in its approach to managing the Fed balance sheet.

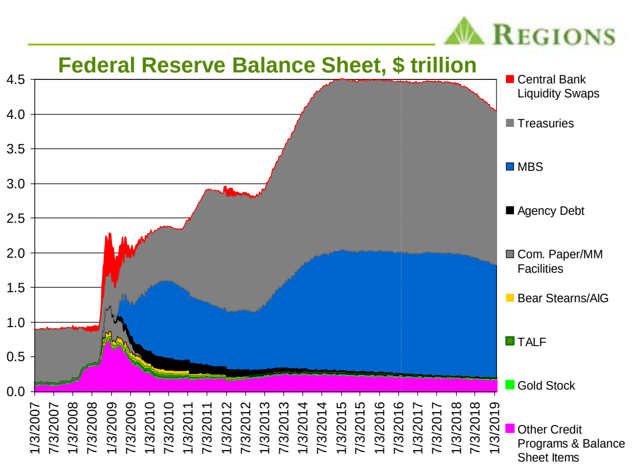
The Committee's assessment of current economic conditions was virtually unchanged from the December 19, 2018 statement. Economic activity is characterized as rising at a "solid rate." Given the sizeable hole left in the body of economic data by the partial government shutdown, it was unlikely that the Committee's assessment of economic conditions would have changed materially, particularly given that the labor market data, which were undisturbed by the partial shutdown, continue to show the labor market remains solid.

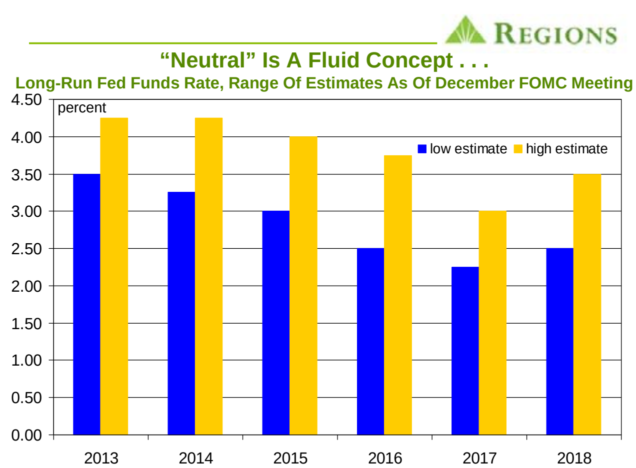
One material change in the post-meeting statement is the elimination of the passage stating "some further gradual increases" in the funds rate will be consistent with the Committee's objectives for growth and inflation. Instead, today's statement notes that "the Committee will be patient as it determines what future adjustments" to the funds rate will be necessary to achieve the Committee's objectives for growth and inflation. This is consistent with the FOMC's messaging over the past several weeks, in which the word "patient" has been featured prominently. It is interesting that the Committee dropped its assessment of the balance of risks in the post-meeting policy statement, whereas statements in the recent past have noted the risks to the economic outlook were "roughly balanced." We would not have been surprised had the Committee assessed the risks as being weighted to the downside, particularly given tighter financial conditions, and it is worth noting that in his post-meeting press conference Chairman Powell noted "the case for raising rates has weakened somewhat."

The Committee also issued an additional statement regarding the Fed balance sheet, noting that it intends to conduct monetary "with an ample supply of reserves," while further noting that it is "prepared to adjust any of the details for completing balance sheet normalization in light of economic and financial developments." In other words, the FOMC is signaling they will be flexible in the process of balance sheet normalization. Chairman Powell made it clear in his post-meeting press conference that the Committee has not reached any firm conclusions as to the ultimate size of the Fed balance sheet and when that will be reached, but also noted that balance sheet normalization will be completed "sooner with a larger balance sheet" than previous estimates.

Chairman Powell noted that the current situation "calls for patience," and that "the length of this patient period will depend entirely on the incoming economic data." That said, Chairman Powell stated that only in hindsight will we know whether this current period is the end of the rate hike cycle or just a pause in it. This statement becomes more interesting in conjunction with the elimination of an assessment of the balance of risks to the Committee's economic outlook. There are clearly downside risks to the outlook, but what remains fairly subdued inflation gives the FOMC the latitude to see "how these cross currents resolve themselves" before deciding on the appropriate path of the Fed funds rate going forward.

This is clearly the appropriate stance to take at this time, but to us the danger in this approach is that the financial markets confuse "patient" and "flexible" with "done." Our sense is that while the FOMC may not have much further to go in normalizing monetary the funds rate, they aren't quite there yet. It isn't clear that the markets see it that way, which could mean the FOMC will have yet another communications challenge on their hands somewhere down the road.





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