ECONOMIC UPDATE

REGIONS

December 14, 2022

December FOMC Meeting: Pushing Back Hard, Or Hardly Pushing Back?

- The FOMC raised the Fed funds rate target range by 50 basis points, with the mid-point of the target range rising to 4.375 percent
- The updated dot plot implies a terminal Fed funds rate target range mid-point of 5.125 percent, up from 4.625 percent in the September edition

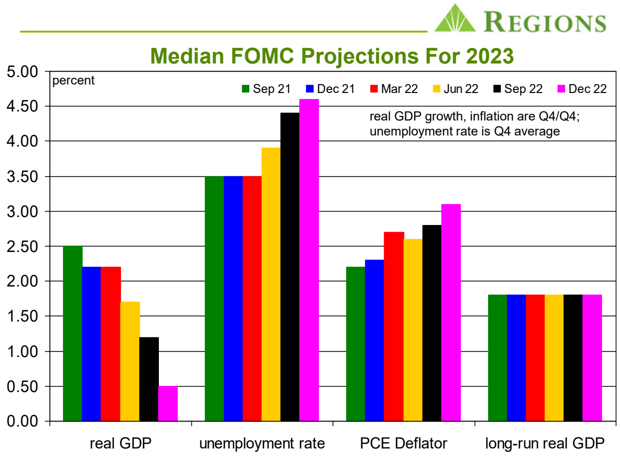
As was widely expected, the FOMC raised the Fed funds rate target range by 50 basis points at their December meeting after having moved at 75-basis point increments in their prior four meetings. At the same time, however, the updated dot plot implies a "higher for longer" course for the Fed funds rate than had been messaged in the September projections while the updated economic projections include a meaningful downgrade in the forecast for 2023 real GDP growth, a higher unemployment rate, and higher rates of headline and core inflation. While the updated dot plot can be seen as consistent with the higher inflation forecast, it could also be part of an effort to push back on further easing in financial conditions and the perception held by many market participants that, wherever the terminal funds rate proves to be, rate cuts will be soon to follow. Whether that message is getting through remains an open question.

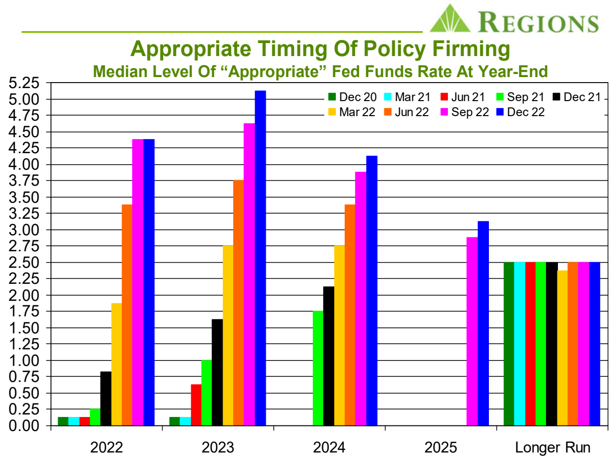
There was virtually no change in the FOMC's assessment of current economic conditions as conveyed in the post-meeting statement. Perhaps the biggest question around the statement ahead of the meeting was whether the passage noting "the Committee anticipates that ongoing increases in the (Fed funds rate) target range will be appropriate . . ." or whether that would be softened to "further increases." Today's statement retains the prior language, and Chairman Powell reinforced that point in his post-meeting press conference, noting that "the inflation data for October and November show a welcome reduction, but it will take more evidence to give confidence that inflation is on a downward path."

The updated economic projections show a meaningful downgrade to expected 2023 real GDP growth; on a Q4/Q4 basis, the median forecast now shows growth of 0.5 percent for 2023, compared to growth of 1.2 percent in the September projections, with real GDP growth expected to remain below the Committee's estimate of its longer-run trend rate through 2024. At the same time, the median forecast of the Q4 average unemployment rate for 2023 is now 4.6 percent, compared to 4.4 percent in the September projections. The median forecast for headline inflation, on a Q4/Q4 basis, is higher for both 2023 and 2024, at 3.1 percent and 2.5 percent, respectively, than was the case in the September projections, and the same is true of the median forecast for core inflation. Perhaps not significant but nonetheless noteworthy is that one Committee member assesses the risk to their inflation forecast as being to the downside, the first such instance of this since the March 2021 projections. The Committee as a whole, however, continues to see the risks to their inflation forecast as being weighted to the upside despite the higher forecast. This goes to the point made by Chairman Powell at his press conference, which is that despite recent signs of progress, the FOMC is not close to being convinced inflation is on a one-way path lower.

The updated dot plot implies an additional seventy-five basis points worth of funds rate hikes in 2023, whereas the September edition implied 25-basis points of incremental tightening in 2023. This leaves the implied year-end 2023 target range mid-point at 5.125 percent (or, a range of 5.00 to 5.25 percent), which is higher than many had expected. The updated dot plot implies a year-end 2024 target rate mid-point of 4.125 percent, up from 3.875 percent in the September projections. It is interesting to note that the highest year-end 2023 dot is at 5.625 percent (two instances) while in the September edition the highest year-end 2023 dot was at 4.875 percent. It is also notable that while there is a narrower dispersion of the 2023 dots, with a high/low spread of only seventy-five basis points, the dispersion of the 2024 dots is, at 225 basis points, wider than shown in the September dot plot. Finally, the median year-end 2025 dot now stands at 3.125 percent, up twenty-five basis points from the September edition and quite a bit higher than the estimate of the "neutral" funds rate, which remains at 2.50 percent. One interpretation is that despite having slowed, many Committee members fear inflation could be more entrenched and not return to the 2.0 percent target rate for a very long time

While Chairman Powell noted that monetary policy will "soon" be sufficiently restrictive, he also noted that there is "more work to do." As he has done on several occasions, Chairman Powell stated that there is no painless way to get inflation down and that the worst pain would be allowing inflation to become entrenched. What constitutes clear and convincing evidence of progress on inflation is not clear, and it is also not clear how much of the dot plot/Chairman Powell's press conference is policy and how much is messaging aimed at the financial markets.





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