ECONOMIC UPDATE

REGIONS

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September FOMC Meeting: A Strong Signal Of An FOMC On Hold For Some Time To Come

- The FOMC left the Fed funds rate target range unchanged, leaving the mid-point of the target range at 0.125 percent
- The updated dot plot implies no change in the Fed funds rate target range through 2023

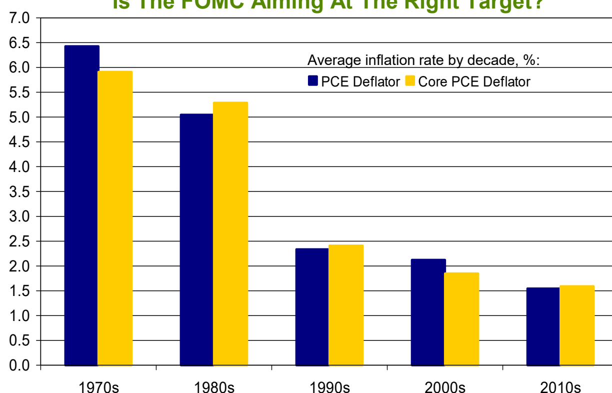
As was widely expected, the FOMC made no changes to the Fed funds rate target range, while strongly reinforcing the point that it will be some time before they consider a funds rate hike. The forward guidance component of the post-meeting policy statement was altered to be compatible with the recent shift in the Committee's inflation strategy, though does not offer any clarity on a potential trigger for a funds rate hike. The updated economic projections are quite a bit different from those issued in June, reflecting the improvement seen in the economy since then. The updated "dot plot" implies no changes in the Fed funds rate target through 2023, but it is worth once again stressing that the path of the funds rate implied in the dot plot is based on how Committee members see the economy evolving as they look ahead today, as that view changes, the path of the funds rate implied by the dot plot will change accordingly. The main takeaway for now, however, is that with the recent shift in the FOMC's inflation strategy and with a pre-defined notion of "full employment" no longer their guide to assessing labor market conditions, the bar for a funds rate hike is higher now than has been the case, even if that bar was already set high.

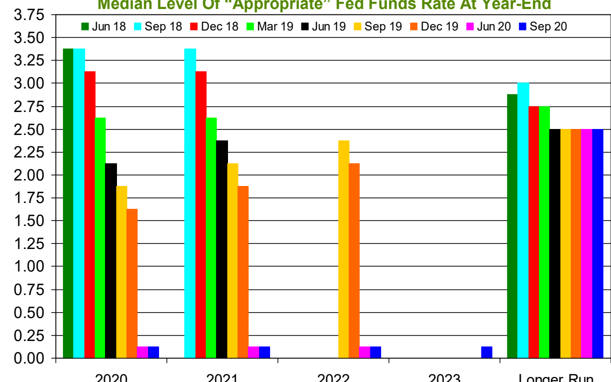
In their post-meeting policy statement, the Committee once again noted that the pandemic "is causing tremendous human and economic hardship across the United States and around the world." Though acknowledging that economic activity and employment have picked up in recent months, the Committee noted that both remain well below their levels at the beginning of 2020. It was noted that "the public health crisis will continue to weigh on economic activity, employment, and inflation in the near term and poses considerable risks to the economic outlook over the medium term."

Recall that in his address to the Jackson Hole conference, Chairman Powell discussed the shift in the FOMC's inflation strategy, moving away from a target inflation rate of 2.0 percent at any point in time to targeting an average rate of inflation of 2.0 percent over time. The forward guidance passage reflects this shift, noting that "the Committee will aim to achieve inflation moderately above 2 percent for some time so that inflation averages 2 percent over time." Left undefined is the specific meaning of "moderately above 2 percent" and the specific meaning of "some time." As forward guidance goes, that doesn't seem like much guidance but, as Chairman Powell made clear in his post-meeting press conference, that is intentional on the FOMC's part, as they seek to retain flexibility in setting the course of monetary policy.

Still, it is worth noting that inflation has run below the FOMC's 2.0 percent target since that target was formally adopted in 2012. Keep in mind that this time period has largely been characterized by a Fed funds rate target range of 0.00 to 0.25 percent and an expanding Federal Reserve balance sheet. Over the past two-plus decades, the main drivers of inflation have been technology, demographics, and globalization, each of which on its own would work to push inflation lower, but which combined have exerted a strong downward push on inflation. If an unprecedented degree of global monetary accommodation was a match for the factors cited above, odds are we'd have at least some evidence of that by now. This is worth considering given the implicit assumption that after "tolerating" inflation "moderately above" 2.0 percent for "some time," the FOMC – or any central bank for that matter – can simply dial inflation down without significant economic disruption.

The updated dot plot implies no change the Fed funds rate target range through 2023. While that is no surprise, what stands out is the degree to which the Committee is unified around this view. The projections for 2023 show only 4 of the 17 members see the funds rate rising by year-end 2023. Interestingly, the projections show not a single Committee member expects inflation to top 2.0 percent (on a Q4/Q4 basis) by year-end 2023 – in order for inflation to run ahead of 2.0 percent for some time, it first has to get to 2.0 percent. Again, it is important to keep in mind that perceptions of the economy will evolve over time, but as they see the world today, the FOMC is implying it will be some time after 2023 before they would need to raise the funds rate. In a sense, that was the objective, i.e., to signal that the FOMC is on hold for some time to come. On that front, the Committee hit their target.





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