ECONOMIC UPDATE

REGIONS

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September FOMC Meeting: FOMC Signals Its Resolve To Stay The Course

- The FOMC raised the Fed funds rate target range by 75 basis points, with the mid-point of the target range rising to 3.125 percent
- The updated dot plot implies a terminal Fed funds rate target range mid-point of 4.625 percent, up from 3.75 percent in the June edition

The FOMC raised the Fed funds rate target range by 75 basis points at their September meeting, a move widely expected in the wake of the August CPI data showing an acceleration in core inflation. The updated economic projections show real GDP running well below "potential" through 2023 with more persistent inflation than anticipated in the June projections along with a higher unemployment rate. The updated "dot plot" implies a more aggressive path of Fed funds rate hikes than that implied in the June edition, with the mid-point of the funds rate target range topping out at 4.625 percent in 2023. Clearly, the FOMC was late to the game in responding to elevated inflation, and just as clearly, they seem intent on making up for lost time. What is far less clear, particularly in light of them now expecting inflation to be higher and more persistent than only a few months ago, is how far the FOMC will ultimately go and what the effects will be on the labor market and the broader economy.

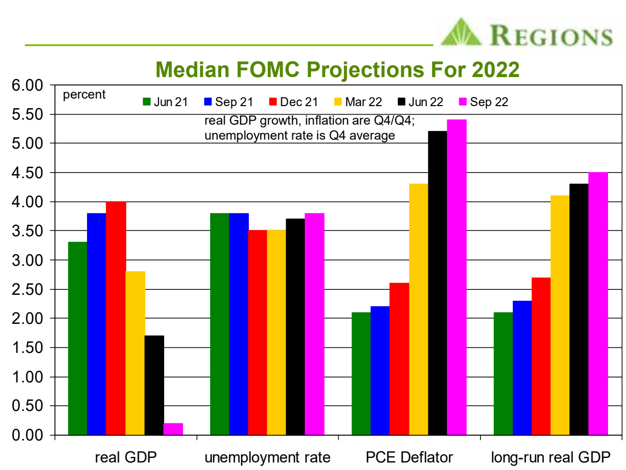
The FOMC's assessment of current economic conditions points to modest growth in spending and production, compared to the reference to spending and production having softened in the July statement. The Committee retained the characterization of inflation remaining elevated, "reflecting supply and demand imbalances related to the pandemic, higher food and energy prices, and broader price pressures." Also retained was the passage on the impacts on inflation of Russia's war against Ukraine, and the statements that "the Committee remis highly attentive to inflation risks" and is "strongly committed to returning inflation to its 2.0 percent objective."

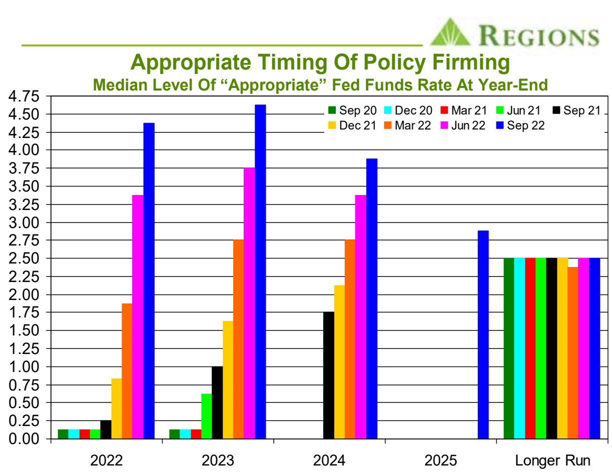
The updated economic projections show a meaningful downgrade to expected real GDP growth; on a Q4/Q4 basis, the median forecast now shows growth of 0.2 percent for 2022 compared to the June forecast of 1.7 percent, with growth of 1.2 percent for 2023, down from 1.7 percent in the June projections. Real GDP growth is 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 2022 is now 3.8 percent, rising to 4.4 percent in Q4 2023 and staying at 4.4 percent in Q4 2024, these compare to average Q4 rates of 3.7 percent, 3.9 percent, and 4.1 percent, respectively, in the June forecasts.

While it is no surprise that the Committee's inflation forecasts are higher than was the case in June, it is striking that the median forecast sees core PCE inflation at 3.1 percent in Q4 2023 (quarterly average), up from 2.7 percent in the June forecast, and remaining above the Committee's 2.0 percent target through 2024. It is also notable that 17 of the 19 FOMC members see the risks to their inflation forecasts as weighted to the upside, the most in the history of the FOMC projections. As with previous FOMC forecasts, some are questioning what seems a fairly mild expected increase in the unemployment rate, particularly in relation to the path of the funds rate implied in the updated dot plot. Keep in mind, however, that many, if not most, FOMC members see a meaningful reduction in job vacancies as a component of a reduction in the demand for labor that will contribute to an easing of wage pressures. Chairman Powell reiterated this point in his post-meeting press conference.

The updated dot plot implies an additional 150 basis points worth of funds rate hikes by year-end 2024, with 125 of that coming this year and the final 25 coming next year. The dot plot is consistent with the tone of comments from FOMC members over the past several weeks as they aggressively pushed back on the notion of a quick pivot from rate hikes to rate cuts. While the dot plot does imply rate cuts in 2024, those cuts would still leave the funds rate well above the FOMC's estimate of the neutral funds rate, i.e., 2.5 percent, with the dot plot implying this will remain the case through 2025 (added to the projections this month). So, as with inflation, the trip back down for the funds rate figures to be a slow one. Clearly, the dot plot is a projection not a commitment, but for now the FOMC remains incentivized to reinforce a hawkish message to the markets to help prevent an unwanted easing in financial conditions.

In his post-meeting press conference, Chairman Powell stressed that the FOMC is "strongly resolved" to bring inflation back down to 2.0 percent and will "keep at it" until that goal is attained. Chairman Powell noted that there is "no painless way" to get inflation down, and again stressed that the costs of prematurely loosening policy would be worse than the costs of the FOMC remaining on its present path. Not exactly inspiring, and more than a bit late, but at this point the right message to send.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com