First Trust
ECONOMIC RESEARCH REPORT
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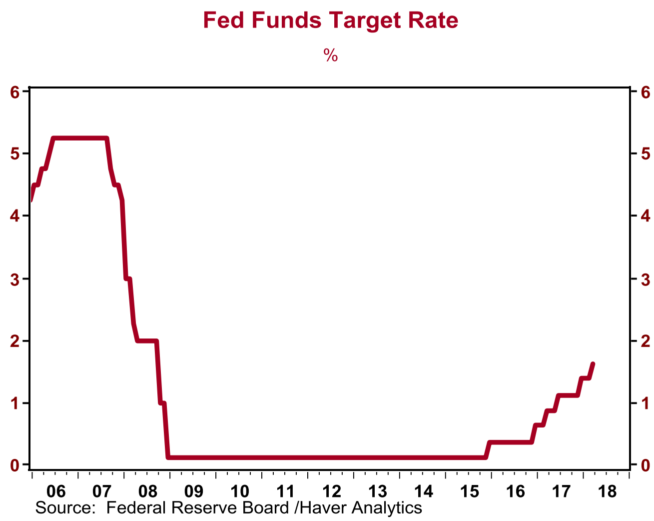
Powell Takes Charge

In his first meeting as Chair of the Federal Reserve, Jerome Powell and company delivered what almost everyone had been expecting, a 25 basis point hike in the federal funds rate, and raised expectations for economic activity in the months and years ahead. While the hike (which we expect is the first of four in 2018) needs little more than passing mention given its essentially shoe-in status heading in to today's meeting, the Fed Statement and projection materials warrant closer inspection.



Start with the statement, where the Fed upgraded the outlook on jobs growth to "strong" from "solid", while continuing to note that the unemployment rate remains low. And while they made a point to note a moderation in growth in household spending and business fixed investment from their fourth-quarter readings, they added new language noting that the economic outlook has strengthened in recent months. This pickup in activity is likely due in large part to the passage of tax reform in late December that the FOMC has now had time to digest and work into their outlook.

On the inflation front, the Fed took a more hawkish tone, changing their expectations for inflation to move to the Fed's 2% objective "in coming months", up from "this year" as was used in the January statement. With inflation closing in on the Fed's target and unemployment already low, the summary of economic projections released today provide more guidance on how the Fed expects both economic growth and monetary policy to develop in the years ahead.

The Fed raised the outlook for GDP growth to 2.7% in 2018 and 2.4% in 2019, up from 2.5% and 2.1%, respectively, in their December projections. At the same time, they lowered the projected year-end level for the unemployment rate in the comings years and moderately raised their inflation outlook.

What is most notable from the projections is that the Fed expects both inflation and the Federal Funds rate to overshoot the long-term targets in 2020, with inflation forecast to exceed the 2% objective at 2.1%, while the federal funds rate is forecast at 3.4%, a full 50 basis points above the 2.9% that the Fed believes appropriate over the long term.

For 2018, the Federal Funds rate is still projected to end the year in the 2.0-2.25% target range (representing three rate hikes), but a look at the "dot plot" shows a notable change in the distribution of forecasts in-line with what we noted in this week's [Monday Morning Outlook](). Back in December, twelve of sixteen participants forecast a year-end rate at or below 2.25% for 2018, while today's projections show a near even split with eight participants expecting three or fewer hikes and seven expecting four or more. In other words, if economic data points continue to show a pickup in the pace of growth – and we expect they will – a shift towards a Fed consensus of four hikes in 2018 looks likely.

In addition to the Fed statement and projection materials, Chair Powell also made a few comments of note during his first press conference. When asked about concerns regarding trade policy and the trade tariffs recently announced by President Trump, the Chair noted that the FOMC does not expect these policies to impact the Fed's economic outlook. At the same time, he expressed expectations that the tax cuts signed into law last December should provide a positive tailwind to the economy for at least the next few years.

These were not groundbreaking statements by any means, but they reinforced the hawkish outlook from the Fed and provide some insight into the thinking of an FOMC that voted unanimously on today's rate hike and changes to the Fed statement. Chair Powell appears to have a "coalition of the willing" behind him as the Fed seeks to avoid falling behind the curve in an economy that's heating up.

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Text of the Federal Reserve's Statement:

Information received since the Federal Open Market Committee met in January indicates that the labor market has continued to strengthen and that economic activity has been rising at a moderate rate. Job gains have been strong in recent months, and the unemployment rate has stayed low. Recent data suggest that growth rates of household spending and business fixed investment have moderated from their strong fourth-quarter readings. On a 12-month basis, both overall inflation and inflation for items other than food and energy have continued to run below 2 percent. Market-based measures of inflation compensation have increased in recent months but remain low; survey-based measures of longer-term inflation expectations are little changed, on balance.

Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. The economic outlook has strengthened in recent months. The Committee expects that, with further gradual adjustments in the stance of monetary policy, economic activity will expand at a moderate pace in the medium term and labor market conditions will remain strong. Inflation on a 12-month basis is expected to move up in coming months and to stabilize around the Committee's 2 percent objective over the medium term. Near-term risks to the economic outlook appear roughly balanced, but the Committee is monitoring inflation developments closely.

In view of realized and expected labor market conditions and inflation, the Committee decided to raise the target range for the federal funds rate to 1-1/2 to 1-3/4 percent. The stance of monetary policy remains accommodative, thereby supporting strong labor market conditions and a sustained return to 2 percent inflation.

In determining the timing and size of future adjustments to the target range for the federal funds rate, the Committee will assess realized and expected economic conditions relative to its objectives of maximum employment and 2 percent inflation. This assessment will take into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments. The Committee will carefully monitor actual and expected inflation developments relative to its symmetric inflation goal. The Committee expects that economic conditions will evolve in a manner that will warrant further gradual increases in the federal funds rate; the federal funds rate is likely to remain, for some time, below levels that are expected to prevail in the longer run. However, the actual path of the federal funds rate will depend on the economic outlook as informed by incoming data.

Voting for the FOMC monetary policy action were Jerome H. Powell, Chairman; William C. Dudley, Vice Chairman; Thomas I. Barkin; Raphael W. Bostic; Lael Brainard; Loretta J. Mester; Randal K. Quarles; and John C. Williams