ECONOMIC PREVIEW

REGIONS

Week of July 9, 2018

Indicator/Action Economics Survey:	Last Actual:	Regions' View:
Fed Funds Rate: Target Range Midpoint *(After the July31-August1 FOMC meeting):* Target Range Midpoint: 1.875 to 1.875 percent Median Target Range Midpoint: 1.875 percent	Range: 1.75% to 2.00% Midpoint: 1.875%	Recent months have seen considerable angst over trade wars, geopolitical tensions, diminishing monetary accommodation, and other factors that pose risks to the economic expansion. At this point, however, this has all been little more than background noise to a U.S. economy that keeps humming along. This could change, of course, but our view is that it will take much more than this to trigger a significant slowdown in an economy amped up on fiscal stimulus. To that point, while FOMC members have expressed concern over the potential adverse impacts of tariffs – though, somewhat oddly, these concerns have focused more on the growth aspect than on the inflation aspect – at this point it seems highly unlikely that such concerns will alter the path of the Fed funds rate, at least this year. Thanks largely to the high degree of fiscal stimulus, the economy is growing at a well above-trend rate, which will help insulate the economy from any adverse impacts stemming from trade in the near term. The longer the trade disputes run, and the deeper they run, the risks to the economy rise, making it more likely the FOMC acts on their concerns.
June PPI: Final Demand Wednesday, 7/11 Range: 0.0 to 0.3 percent Median: 0.2 percent	May = +0.5%	Up by 0.2 percent, for a year-on-year increase of 3.2 percent.
June PPI: Core Wednesday, 7/11 Range: 0.1 to 0.3 percent Median: 0.2 percent	May = +0.3%	Up by 0.2 percent, leaving the core PPI up 2.6 percent year-on-year.
June Consumer Price Index Thursday, 7/12 Range: 0.1 to 0.3 percent Median: 0.2 percent	May = +0.2%	Up by 0.2 percent, good for a year-on-year increase of 2.9 percent, which would be the highest rate of CPI inflation since February 2012. Gasoline should be a very slight drag on the June CPI, with shelter and medical care costs the main factors behind the increase in the headline index. While headline CPI inflation could have a 3-handle in the July data, we think that will mark the peak, at least for now, with headline CPI inflation settling in around 2.5 percent for the remainder of 2018.
June Consumer Price Index: Core Thursday, 7/12 Range: 0.1 to 0.2 percent Median: 0.2 percent	May = +0.2%	Up by 0.2 percent, which would yield a year-on-year increase of 2.3 percent. For some time we've referred to rents, core goods prices, and medical care costs as the "Big Three" drivers of core inflation in 2018. Growth in market rents is slowing, but at a very gradual pace, while growth in owners' equivalent rent is rising at a faster rate, which we believe reflects a prolonged period of robust house price appreciation. As owners' equivalent rent is weighted much more heavily than market rents, this means growth in overall rents will likely hold up better than our forecast had anticipated at the start of the year. With rents accounting for over 40 percent of the core CPI, firmer rent growth will be a persistent support for core CPI inflation. It should be noted that rents carry a much lower weight in the core PCE deflator, which is the FOMC's preferred measure of inflation. Medical care costs have been all over the map for some time now, but our forecast anticipates a larger increase in June than that seen in May. Year-on-year growth in medical care costs is again accelerating but remains far short of the better than four percent pace seen over the back half of 2016. After mounting a brief but uninspired rally earlier in 2018, core goods prices are falling again, which makes sense in light of the strong run of the U.S. dollar over recent months. As such, our forecast anticipates yet another (the 61st in the past 63 months) year-on-year decline in core goods prices in the June data. Going forward, the big wild card here is whether, or to what extent, core goods prices will be pushed higher over coming months due to tariffs. If the U.S. and its trading partners continue down the tariff path, it seems only a matter of time until firms begin, or at least attempt, to pass along at least some portion of tariffs on to consumers in the form of higher goods prices, particularly should tariffs become increasingly focused on consumer goods as opposed to raw and intermediate goods as in the initial rounds. Apparel prices are shaping up to be a source of uncertainty in our core CPI forecasts. Having apparently taken umbrage at not being included in our short list of key drivers of core inflation, apparel prices have been acting out by defying the pattern seen over recent years, i.e., post-holiday increases in January and February followed by declines over the remainder of the year. While our June forecast anticipates a decline in apparel prices, we're not all that convicted and won't be too surprised if apparel prices go in the opposite direction. Though "only" accounting for just under four percent of the core CPI, a big enough swing in apparel prices can push the core CPI up/down by one-tenth of a point when all is said, done, and rounded.

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