

ECONOMIC PREVIEW



Week of March 20, 2023

Indicator/Action

Economics Survey:

Last

Actual:

Regions' View:

Fed Funds Rate: Target Range Midpoint

(After the March 21-22 FOMC meeting):

Target Range Mid-point: 4.375 to 4.875 percent

Median Target Range Mid-point: 4.875 percent

Range:
4.50% to 4.75%
Midpoint:
4.625%

In the wake of Fed Chair Powell's recent Congressional testimony, the question was whether the FOMC would hike the Fed funds rate by twenty-five basis points or by fifty basis points at this month's meeting, as stronger than expected economic data had opened the door for a fifty basis point hike. The question today as we write this is whether the FOMC will change the funds rate at all in light of the stress in the banking system and lingering questions around how much more is to come. The dilemma for the Committee is that, though decelerating, inflation remains much too high for their comfort, which is an argument in favor of a 25-basis point funds rate hike at this week's meeting, particularly given uncertainty over how the FOMC holding steady would be interpreted (i.e., a sign of unspoken worry). The other side of that argument is that holding the Fed funds rate steady until there is more clarity around the degree of and potential fallout from the stress in the banking system while holding out the option of subsequent hikes if warranted will not change the ultimate path of inflation. Many are pointing to last week's decision by the ECB to raise their policy rate by fifty basis points as a roadmap for the FOMC, though we're not sure the FOMC would see a connection. Unlike the ECB, which punted on forward guidance, the FOMC is due to issue a set of updated economic and financial projections, including an updated dot plot, which we still expect to imply a higher terminal funds rate than did the December edition. Many are arguing that there is a clear distinction between the FOMC's ongoing fight against inflation and their seeking to foster financial stability, which would imply that the stress in the banking system is not grounds for the FOMC to forgo raising the funds rate as part of its fight against inflation. We do not believe it is that clear cut, however, given that the more aggressive the FOMC is in its battle against inflation, the greater the likelihood that the FOMC will have to act more aggressively to preserve financial stability.

February Existing Home Sales

Range: 3.700 to 4.480 million units

Median: 4.200 million units SAAR

Tuesday, 3/21

Jan = 4.000 million units SAAR

Up to an annualized rate of 4.480 million units. On a not seasonally adjusted basis, we look for total sales of 265,000 units, up 14.7 percent from January. While January sales were, to the surprise of no one, weaker than is normal for month, our forecast anticipates a stronger than normal February. Recall that existing homes are booked at closing, so February closings will mainly reflect sales contracts signed from late-December through January, a period when mortgage interest rates were still falling after having peaked at over seven percent last October. To that point, the increase in not seasonally adjusted pending home sales – a measure of signed sales contracts – in January was larger than is normal for the month, even with mortgage rates well above they'd been over the prior several Januarys. This goes to a point we've made since mortgage rates took off last year, which is that there is still a considerable degree of pent-up demand for home purchases after the market having been so chronically undersupplied over the past several years, and that there would be some buyers who would respond to any improvements in affordability, whether those came from lower mortgage rates or lower prices, if not both. We saw this when new home sales, which are booked at the signing of the sales contract, jumped in January, so the increase we expect in February existing home sales would simply be the counterpart of that increase in new home sales.

The more relevant question, however, is even if our above-consensus forecast is on or near the mark, where would that leave the market, and our answer is not in a good place. After all, our forecast would still leave unadjusted sales down 24.7 percent year-on-year. Moreover, even with sales having dropped so sharply over the past several months, the market remains undersupplied, even if to a lesser degree than had been the case prior to mortgage rates taking off. Even if we are correct in expecting a typical February increase in inventories (February is the month in which listings typically begin rising ahead of the spring sales season), the months supply metric will continue to hover around three months, far below the 5.5-6.0 months consistent with a balanced market. To be sure, constrained inventories pose a downside risk to our sales forecast. Additionally, any bounce in sales in February will prove short-lived given the reversal in mortgage interest rates seen in February, which we think will have dented new home sales (see Page 2). While the median existing home sales price should show a year-on-year increase, we look for that increase to be only around one percent and it won't surprise us at all if the March data bring the first over-the-year decline in the median existing home sales price since 2012.

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Q4 Current Account Balance Range: -\$219.7 to -\$186.0 billion Median: -\$213.3 billion	Thursday, 3/23	Q3 = -\$217.1 billion	<u>Narrowing</u> to -\$207.8 billion.
February New Home Sales Range: 605,000 to 698,000 units Median: 650,000 units SAAR	Thursday, 3/23	Jan = 670,000 units SAAR	<u>Down</u> to an annualized rate of 612,000 units. On a not seasonally adjusted basis, we look for total sales of 55,000 units, down 6.8 percent from January. As noted in our discussion of our existing home sales forecast, falling mortgage rates contributed to a jump in new home sales in January, with the 25.5 percent increase second to only 2019 as the largest January increase over the past thirty-one years, which is notable even if coming off a lower base. With mortgage interest rates having reversed course in February, we expect some payback in new home sales. It is interesting that units on which construction had not yet started accounted for the bulk of the increase in new home sales in January, a month which saw a significant decline in spec inventories of new homes for sale. Still, spec inventories remain meaningfully higher than had been the case before mortgage rates began rising last year, with completed units accounting for a rising share of overall spec inventories. So, even with sales having jumped in January, builders remain uncomfortable with current levels of spec inventories, and with mortgage rates having turned higher in February, builders may have had to be more accommodating in terms of concessions in order to move units. It does seem, given how far below the consensus our forecast is, that the risks to our forecast are to the upside, but that's the beauty of the ever-volatile new home sales data – one just simply never knows.
February Durable Goods Orders Range: -7.4 to 2.8 percent Median: 0.8 percent	Friday, 3/24	Jan = -4.5%	<u>Down</u> by 3.6 percent. Boeing booked only two net orders in February, and even though we look for another increase in motor vehicle orders, we expect transportation orders to be a drag on headline orders. This is contrary to the consensus forecasts, in which the increase in total orders is easily above the forecast for ex-transportation orders. Some are pointing to the February ISM Manufacturing Index, which shows that even though new orders declined, orders for transportation goods increased, to support their call. Either way, as we frequently note, the single most important number in any month's report on durable goods orders is core capital goods, and we expect a weak February print (see below). Recall that core capital goods orders jumped by 0.8 percent in January after a string of weak prints over prior months. What went largely unnoticed, however, is that the reported January increase was a gift from seasonal adjustment, as not seasonally adjusted core capital goods orders fell by 9.9 percent. This puts the data on durable goods orders in the same camp as almost all of the rest of the January data, i.e., a smaller than typical January decline in the not seasonally adjusted data yielding an implausibly strong reading in the seasonally adjusted data. We look for the February data to fall back into the trend of weakening business investment in equipment and machinery evident over the prior several months, including the decline in real outlays reported in the Q4 GDP data.
February Durable Goods Orders: Ex-Trnsp. Range: -1.3 to 1.2 percent Median: 0.2 percent	Friday, 3/24	Jan = +0.8%	We look for <u>ex-transportation</u> orders to be <u>down</u> by 0.3 percent with orders for <u>core capital goods</u> (non-defense capital goods excluding aircraft & parts) <u>down</u> by 0.4 percent.

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