Highlighting the Labor Market's New Complexities; Listening to Worker Voices

National Association for Business Economics (NABE)
Monetary Policy and Outlook Webinar
Philadelphia, PA (virtual)

June 1, 2023

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Good afternoon, everyone. It is a pleasure to join you in this series on monetary policy and our economic outlook.

And I thank NABE for the invite and Dr. Elaine Buckberg for moderating.

You heard from my colleague, Richmond Fed President and CEO Tom Barkin, on Tuesday, so I am honored to provide a Fed bookend to this webinar.

I look forward to having a useful and engaging dialogue. But please allow me to open with my thoughts on the direction in which we are heading.

And I must lead with the standard Fed disclaimer: The views I express today are my own and do not necessarily reflect those of anyone else on the Federal Open Market Committee or in the Federal Reserve System.

While headline PCE inflation has come down from its peak of 7 percent last year, it is still running at over 4 percent year over year — way above the Fed's long-run target of 2 percent annually. Disinflation is under way, but it is doing so at a disappointingly slow pace.

This persistently high inflation comes with real costs for American families — cutting into purchasing power and household wealth. And the pain isn't being felt equally.

The toll is falling most heavily on those least able to bear it. I'm especially concerned about the elevated costs of housing, food, and health care — life's true necessities.

To combat this inflation, the Fed has been working to slow the economy modestly and bring demand more in line with supply. We have increased the target range for the federal funds rate — our primary monetary policy tool — by 500 basis points since March 2022. Ongoing balance sheet reduction is also tightening financial conditions.

We're already seeing promising signs that these actions are working; for example, house price indexes are cooling.

And it is encouraging that even as we have raised rates, the national economy remains relatively healthy overall. Since January, we've experienced modest growth in economic activity.

There are also still a record number of Americans employed, with more than 1 million jobs created, on net, so far this year. While there are some signs that labor market tightness is beginning to ease a bit, the unemployment rate remains near record lows — 3.4 percent in April.

We're also paying close attention to the banking system. The recent failures of Silicon Valley Bank, Signature Bank, and First Republic ignited an understandable wave of anxiety among banks, depositors, and investors. But I can assure you that the U.S. banking system remains sound and resilient.

We know that problems in a few banks, if left unattended, can undermine confidence in healthy banks. That's why the Treasury, the FDIC, and the Fed acted quickly to protect the U.S. economy and its banking interests. The Federal Reserve also led a thorough, transparent, and swift review of the events surrounding Silicon Valley Bank so we could learn what went wrong.

So, of course, I know the question on everyone's mind: OK, Pat, where do we go from here?

The Fed's monetary policy actions are guided by our dual mandate: to promote full employment and price stability. On the jobs front, things look quite good; we are, effectively, at full employment. But when it comes to inflation, there is still significant room for improvement.

It will take some time to evaluate how recent events may impact overall economic activity and inflation. I expect to see tighter credit conditions for households and businesses that may slow economic activity and hiring, but the full extent is still unclear.

What is clear is that the Fed remains fully committed to return inflation to its 2 percent target. To do this, the policy stance needs to be restrictive enough — but what is "enough" is not written in stone somewhere.

Instead, I am closely monitoring incoming data, listening to our contacts and audiences, and evaluating economic conditions to assess whether additional tightening will be needed.

I do believe that we are close to the point where we can hold rates in place and let monetary policy do its work to bring inflation back to the target in a timely manner.

Along this path, I project that we will see modest growth this year, with real GDP coming in a bit below 1 percent.

I expect inflation to decline to somewhere around 3.5 percent this year, before falling to 2.5 percent in 2024, and leveling out at our 2 percent target in 2025. Unemployment is also likely to tick up slightly, hitting around 4.4 percent this year.

But this is just a snapshot of what conditions look like today. We're operating in a very uncertain environment, and I will be closely monitoring our dashboards of economic indicators and assessing their implications.

Now, as I've said before, survey data are an important tool in the economic business. At the Fed, we look at everything from big broad numbers like GDP and employment growth to more granular figures like restaurant reservations and mobility data.

These data — hard data — tell us a lot. But even hard data have their limits. The numbers can point in a certain direction, yet there may be a lot going on underneath those numbers, which is not as easily visible but is just as vital to drawing a complete picture.

Take, for example, the employment picture.

Throughout the past year, each interest rate hike was predictably followed by voices warning that we were about to tank the labor market and spike unemployment. That hasn't happened, but we monitor these trends to see how workers will be impacted if it does.

Given the tight labor market, there's obviously something deeper happening. We continually hear from some employers that certain tools aren't working as they once did. Simply offering higher wages still isn't attracting the workers some need, and some efforts to increase the productivity of current workers is instead leading to increased turnover.

These cases are especially true at the lower end of the wage scale, and this may be why some have groused that, "No one wants to work anymore." But I think we all would agree there's more going on under the surface.

Now, I'm not strictly an economist. I'm a civil engineer. And that background is what is forcing me to look at this issue in a different way.

And this is what we at the Philadelphia Fed are doing. And I'd like to spend a few moments on this before we get to our Q&A.

Over the past year, our Community Development and Regional Outreach team, along with colleagues at the Atlanta Fed and elsewhere, engaged with low-wage and non-degree-holding workers nationwide in a series of focus group conversations.

We've been listening to them and to their reasons why they may have exited the labor market at the onset of the pandemic to reenter from an entirely different door on the other side of it or are quitting jobs at such a high rate.

We're calling this effort the Worker Voices Project. And we released our first report — "Shifting Perspectives and Expectations on Employment" — one week ago.

Yes, workers want to be paid what they believe they are worth and bring to the table, but it's not only about wages. And, yes, they want to be somewhere they can be productive and contributing employees, but not if they don't believe their contributions are appreciated, let alone rewarded.

What we increasingly heard is that workers want something that we, as economists and civil engineers, don't yet have a metric for: being treated with dignity.

As one participant told me recently, "Work is not the end-all, be-all." Or, in the words of another, "We're looking for a place where we belong."

The factors going into the decisions of where to work, or whether to go in an entirely different direction, are increasingly complex. And these complexities may make us rethink what we thought we knew about labor markets.

I encourage everyone to take a look at our initial Worker Voices Project report.

For us as policymakers, soft data are perhaps equally important to get a full understanding of our economic situation. And the soft data we're getting through Worker Voices are what will help us chart a course for a strong and growing — but also a more inclusive — American economy.

I know that's a lot to start with, but I also know it's what is going to lead us to a great conversation.

And, Elaine, to that end, let's get right to it.