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Economic Trends and Opportunities for Philadelphia

The Chamber of Commerce for Greater Philadelphia State of the Economy
Philadelphia

Anna Paulson

President and Chief Executive Officer
Federal Reserve Bank of Philadelphia

Remarks as prepared for delivery.

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Good morning! And thank you for that kind introduction. It's great to be here with you. I'd like to thank Chellie[1] and the Chamber team for the invitation to speak today.

The Chamber and the Philly Fed have a long-standing and important partnership on many programs and that includes the annual Chamber State of the Economy survey that many of you will have filled out. Your input helps us understand the economy and the range of ways organizations and individuals are experiencing and shaping it. You provide the stories behind the data that are a key input into my thinking about monetary policy.

My goal today is to leave you with a sense of the important national economic trends and how those trends are playing out here in Philadelphia. I'll also share some findings from a recent survey that our team did to identify barriers to employment for Philadelphia residents. I hope this will provide good background for the panel discussion focusing on opportunities to create great jobs here in the region.

Before I get into the details, please note that I am speaking just for myself and that my views don't necessarily reflect those of any of my Federal Open Market Committee (FOMC) colleagues.

Economic Outlook

As many of you know, Congress has charged the FOMC with delivering maximum employment and price stability. We define price stability to mean inflation of two percent, as measured by the change in the personal consumption expenditure price index, affectionately known as PCE inflation.

If I had to pick a theme for inflation for 2026 it would be "cautious optimism." I am going to focus on PCE inflation data through September of 2025 because the lack of data collection during the government shutdown complicates the interpretation of some more recent data.

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[1] Chellie Cameron, president and chief executive officer of the Chamber of Commerce for Greater Philadelphia, https://chamberphl.com/about/our-team/.

Twelve-month core PCE inflation came in at 2.8 percent in September. And it was also 2.8 percent for the 12 months ending in September of 2024. On the surface, it looks like we made little to no progress in getting inflation down last year.

However, when we dig into the components, I see some progress and reasons for my cautious optimism.

First, while goods inflation is clearly up, it seems likely to return to normal over the next 12 months. Goods prices have increased more than 1 percent over the last year or so after declining in 2024. We know why this is happening: Higher tariffs on imports are showing up in goods prices.

Based on my reading of the evidence, I expect that we've already seen a lot of the price adjustments. That being said, producers may still have some more price changes to make. The data for January will be especially useful for gauging this because the beginning of the year is a natural time for firms to change prices.

All in all, though, I see an environment where tariff-induced price adjustments are largely confined to goods, as would be the case if tariffs lead to a shift in the price level but do not create sustained inflation. I expect the shift in the price level to run its course in the first half of this year and for goods inflation to return to levels consistent with overall inflation being near 2 percent sometime in the second half of the year.

It is also encouraging that core services inflation excluding housing eased a bit last year, coming in at 3.3 percent (year over year) in September of 2025 compared to 3.5 percent (year over year) in September of 2024. It's still elevated, but it is moving in the right direction.

The remaining component of inflation is housing, and here the news is unambiguously good. Housing inflation has gone from 5.1 percent (year over year) in September of 2024 to 3.7 percent in the 12 months ending in September of 2025. And data on new market rents that feed into housing inflation mean that, going forward, it should continue its return to levels consistent with 2 percent core PCE inflation as we go through 2026.

So, I am feeling cautiously optimistic on inflation, and I see a decent chance that we will end the year with inflation that is close to 2 percent on a run-rate basis; that is, 12-month inflation may still be a little elevated, but three-month inflation will be 2 percent by the end of the year. Yesterday's CPI inflation release for December doesn't change my assessment.

I view the current level of the federal funds rate as still a little restrictive. So, the combination of past and current monetary policy restrictiveness will help to bring inflation all the way to two.

We've seen progress on underlying inflation that is likely to continue and there is no evidence to date that tariff-induced price increases are leading to broader inflation. In addition, long-term inflation expectations are anchored at levels consistent with a gradual return to 2 percent inflation. These trends, especially given labor market developments, argue against tighter monetary policy.

Turning to output and employment, I think the theme for 2026 will be “waiting for clarity.” Currently, we are receiving divergent signals on growth and the labor market. Gross domestic product (GDP) growth has been very strong, with third quarter real GDP growth coming in at an above-trend 4.3 percent, with continued strong consumption. Preliminary data point to strong growth in the fourth quarter as well. But this growth is happening against the backdrop of a slowing labor market.

In 2024, the economy created about 2 million jobs and, in 2025, we created only about six hundred thousand jobs. In addition, the base for job creation has narrowed. Nearly 95 percent of net private job creation in 2025 occurred in a single sector: healthcare and social assistance.

Here in the city of Philadelphia, about 27 percent of employment is in healthcare and social assistance, compared to 16 percent nationally. This means that we have been somewhat insulated from the national slowdown in job creation.

I see the broad deceleration in the national labor market as stemming from both supply and demand factors. On the supply side, the sharp drop in immigration has slowed the growth of labor supply. On the demand side, firms — both nationally and here in Philadelphia — tell us that uncertainty is holding back hiring as they consider a range of factors, including trade policy and the potential for artificial intelligence (AI) to transform the need for workers. Employers also point to over-hiring during the pandemic recovery as a restraint on labor demand. I expect that monetary policy restrictiveness is also playing a role. On net, the slowdown in demand appears to have outpaced the slowdown in supply, with the unemployment rate up to 4.4 percent in December. This is up somewhat from the rate of around 4 percent that we saw in the first half of last year.

While the labor market is clearly bending, it is not breaking. We can see this in the unemployment insurance (UI) claims data. Initial claims have been essentially flat over the last year. Still, labor market risks have risen and that has been an important factor in my support for the 75 basis points of cuts that the FOMC did last year. I will be monitoring labor market developments closely.

What could reconcile strong growth, with apparent momentum from consumer spending, and the slowing labor market? It’s possible that some combination of the growth data being revised down or the labor market data being revised up could move the two trends into better alignment. If the patterns of the last couple of years hold, though, I would expect job gains to be revised down and not up. And, typically, when GDP and labor market signals are in conflict, the labor market signal turns out to be more accurate.[2]

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[2] Michelle L. Barnes, Fabià Gumbau-Brisa, and Giovanni P. Olivei. “Do Real-Time Okun’s Law Errors Predict GDP Data Revisions?” Federal Reserve Bank of Boston Research Department Working Paper

Even setting aside possible data revisions and taking the very strong topline growth data for Q3 at face value, what it means for future momentum is unclear. Income growth has not kept up with consumption growth, and the savings rate fell in Q3. And, certainly, not everyone is doing great. Contacts consistently report that low-income households are struggling, pressured by high prices, and they are increasingly concerned about job security. A retailer who is active in the Philadelphia area told us they are seeing lots of headwinds for the consumer, especially for lower-income individuals. Even individuals with discretionary income to spend are being careful. For example, although people are still eating out in Philadelphia, contacts tell us that less expensive options on the menu are becoming more popular. The only exception to this trend is at more upscale restaurants. High-income households, bolstered by a strong stock market, appear to be driving elevated consumption growth.

We don't see a lot of momentum in other major spending categories like aggregate investment. While investment in high-tech equipment was strong through the third quarter, residential investment has been negative, as one might expect with restrictive monetary policy.

Another possibility that could help reconcile the conflicting GDP and labor market signals is that we are seeing the beginning stages of a step up in productivity growth, likely driven by AI and deregulation. Initial investments in AI are concentrated in things like data centers that don't require a lot of workers. And, going forward, we could see a period of strong growth where relatively few jobs are created as AI becomes fully embedded. It appears that the potential for AI to reduce the demand for workers is likely to be mostly ahead of us. For example, in the Chamber survey the vast majority of firms report using AI. But among firms who are using it, only about 10 percent reported that it had reduced their need for workers.

The type of structural change that AI could bring is challenging for monetary policymakers. Monetary policy can offset a cyclical slowdown in demand, but it can't do anything about a structural change in the demand for labor. And it is difficult to tell in real time if growth is driven by structural or cyclical forces. For instance, we've seen slowing job gains, particularly for younger, entry-level workers.[3] This could be a sign of a coming cyclical slowdown, as it often has been in the past. But these are also the types of jobs that we might expect to be very exposed to AI.

More generally, if a productivity boom does materialize, we will see high growth long before we will know with certainty what is driving it. Policymakers will likely worry that

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(2013), https://www.bostonfed.org/publications/research-department-working-paper/2013/do-realtime-okuns-law-errors-predict-gdp-data-revisions.aspx.

[3] Erik Brynjolfsson, Bharat Chandar, and Ruyu Chen. "Canaries in the Coal Mine? Six Facts about the Recent Employment Effects of Artificial Intelligence," Stanford Digital Economy Lab Working Paper, November 13, 2025, https://digitaleconomy.stanford.edu/publications/canaries-in-the-coal-mine/.

apparently above-trend growth could lead to higher inflation. Of course, this doesn't have to be the case if growth is high due to elevated productivity. But there's no way to be sure in real time.

The FOMC successfully navigated a scenario like this in the second half of the 1990s under Chairman Greenspan's leadership. Firms were investing heavily in information technology (IT) and growth was higher than what was thought to be sustainable. At Committee meeting after Committee meeting, FOMC members anticipated raising rates at the next meeting, assuming they would see inflationary pressures emerge. But inflation never came and the patience of the Committee paid off. The economy experienced strong GDP growth, a decline in unemployment, low inflation, and, eventually, a lower federal funds rate.

In my view, a key factor behind this successful outcome was the FOMC's inflation-fighting credibility. That credibility allowed the Committee to be patient, to hold rates steady, and eventually even lower them, without fueling inflation or inflationary expectations. The FOMC had earned the public's trust during earlier inflation-fighting episodes and could, therefore, afford to be patient. To be sure, some FOMC members in the 1990s worried that they might be sacrificing some of that credibility by not tightening policy.

Former New York Fed President McDonough argued that the Committee's credibility ultimately depends, not on reflexively raising rates or keeping them arbitrarily high, but on pursuing whatever policy path is most likely to achieve stable prices and maximum employment. At the July 1997 FOMC meeting, he told his colleagues: "Credibility is not the result of raising rates whether needed or not; credibility is doing the right thing."[4] Of course, we now have the benefit of hindsight in knowing that not raising rates during this period was in fact the right thing!

As we go through 2026, both of the themes I discussed will be important: cautious optimism on inflation and wanting greater clarity on what is pushing growth up and employment down and whether these trends will continue. Although I see labor market risks as somewhat elevated, my baseline outlook is pretty benign and does not take strong signal from Q3 growth. I see inflation moderating, the labor market stabilizing and growth coming in around 2 percent this year. If all of that happens, then some modest further adjustments to the funds rate would likely be appropriate later in the year.

At the same time, I will be paying close attention to both cyclical and structural influences on the economy, including AI and deregulation, and what they may mean for the health of the labor market, progress on inflation, and the restrictiveness of monetary policy.

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[4] Transcript of the Meeting of the Federal Open Market Committee, Board of Governors of the Federal Reserve System (1997): 45, https://www.federalreserve.gov/monetarypolicy/files/FOMC19970702meeting.pdf.

I suspect that it will take some time to assess all of these factors and their implications for monetary policy. No matter where we land on those assessments, or the economic circumstances that arise, I'll be focused on actions that promote price stability and maximum employment and monetary policy credibility.

In other words, I'll be striving to follow President McDonough's advice to do the right thing.

Job Creation and Economic Mobility

Let's turn now to the challenge of creating jobs, and especially family sustaining jobs here in Philadelphia. You'll hear a lot more about strategies for doing this from our panel, so I just want to highlight a few things.

First, some employers in Philadelphia struggle to find qualified workers. In the recent Chamber survey, about 30 percent of employers who were seeking to maintain or grow headcount reported that a lack of qualified applicants, or a lack of applicants generally, made it difficult to follow through on those plans.

Second, many city residents are looking for better job opportunities. Our experts partnered with an organization focused on economic mobility to survey individuals living in the poorest two-thirds of Philadelphia neighborhoods. While the survey focused on lower-income zip codes, higher-income individuals living in those neighborhoods were also included. Through these efforts, we learned that for about one-third of individuals a better paying job is the single thing that would be most helpful to them.

However, we also learned that individuals face challenges in finding better jobs. Twenty-two percent of survey respondents said that their ability to work or look for a job was limited by their health, 16 percent said it was limited by caretaking responsibilities, and another 16 percent cited lack of access to reliable transportation.[5] These percentages were all significantly higher for lower-income individuals.

So, we've got employers who are looking for qualified workers and individuals who are looking for better jobs. And we also have some sense of the challenges that would need to be overcome in order for these observations to translate into progress for employers, for residents, and for the city.

This makes it sound like it might be easy, but what I have learned from our community development experts — who focus on reducing barriers to participation in the labor market — is that success requires sustained engagement with all the relevant stakeholders; that real progress is rarely easy; and that it's important to ensure that stakeholders develop and drive progress.

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[5] Ashley Anglin, Stephanie Hoopes, Ashley Putnam, Theresa Y. Singleton, and Bryan Stuart. "Understanding Economic Stability and Economic Mobility in Philadelphia," Federal Reserve Bank of Philadelphia, April 10, 2025, https://www.philadelphiafed.org/community-development/workforce-and-economic-development/understanding-economic-stability-and-economic-mobility-in-philadelphia.

But there is another theme that came out of focus groups we did with about 10 percent of the survey respondents. And that theme really spoke to me. When participants were asked what economic mobility means to them, they made it clear that economic stability necessarily precedes economic mobility.

That speaks to me because the mission of the Philly Fed, indeed of the entire Federal Reserve System, is about stability. Monetary policy is focused on price stability and maximum sustainable employment. We strive to ensure the stability of the financial system as well as the safety and soundness of individual financial institutions. We operate the payment system, working to ensure it is safe and efficient. And, as we've been discussing, our community development efforts help us to understand what stability means for families and communities.

The type of stability that advances economic mobility has mostly happened during long economic expansions. So, I'll be thinking about the many dimensions of stability — including what they mean for families in Philadelphia — as I focus on monetary policy that advances stable prices and maximum employment.

So, thank you again for the opportunity to share my thoughts with you this morning. And now, let me hand it off to Elinor[6] who will introduce our expert panel.

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[6] Elinor Haider, senior director, Philadelphia Program, The Pew Charitable Trusts, https://www.pew.org/en/about/experts/elinor-haider.