John C Williams: There and back again

Remarks by Mr John C Williams, President and Chief Executive Officer of the Federal Reserve Bank of New York, at the Long Island Association Regional Economic Briefing, Garden City, New York City, 28 February 2024.

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As prepared for delivery

Introduction

Good afternoon, everyone. Thank you for having me here today. I always enjoy meeting with business and community leaders in the Federal Reserve's Second District. And it's a real treat to join you here at the Cradle of Aviation Museum. It's a great reminder of Long Island's rich history in aeronautics and innovation.

If only I had time to visit some of the space exhibits today. Alas, maybe next time....

Instead, in my remarks, I will focus on how the Federal Reserve is working to achieve our goals of maximum employment and price stability. I'll also discuss the significant progress we've seen in restoring balance to the economy and bringing inflation down to the Federal Open Market Committee's (FOMC's) 2 percent longer-run goal. And I'll talk about what we still need to see for a full and sustained return to price stability. Finally, I'll give my economic outlook.

Before I get into all of that, I need to provide the standard Fed disclaimer that the views I express today are mine alone and do not necessarily reflect those of the FOMC or others in the Federal Reserve System.

Falling Inflation, Low Unemployment

In thinking about the state of our economy today, and what that means for the future, it's important to start from where we've been.

As business leaders, you know all too well the impacts of the pandemic. In many ways, Long Island's economy mirrors New York City's. Both were hit especially hard in 2020-in fact, much harder than what we saw nationally. And in 2023, both reached an important milestone, returning to the number of jobs we had before the pandemic.

Last year was also a turning point for the U.S. economy. Global supply chains, which were severely disrupted during the pandemic and early in the recovery, returned to normal.[1] Demand came into better balance with supply. And the economy grew far faster than anyone expected a year ago, boosted by increases in the labor force and productivity.

At the same time, the labor market remained strong, with the unemployment rate under 4 percent-a mark it's held for the past two years, the longest stretch in five decades. And inflation-as measured by the personal consumption expenditures (PCE) price index-

continued to decline from its 40-year high of about 7 percent in mid-2022, reaching about 2-1/2 percent last year.

Given that we are in a museum that houses an *actual* Lunar Module-and all eyes are on plans to return to the moon-I cannot resist the temptation to use the mission to send astronauts to the moon as a metaphor for the economy.

Like traveling to the moon and back, inflation shot up, then came back down. And as with the Apollo missions, it's the safe return home that's essential. While we've seen great progress toward achieving our goals, the journey is not yet over, and I am very focused on making sure we complete this mission successfully.

A Strong, More Balanced Labor Market

I'm going to spend some time digging deeper into the trends behind both sides of our dual mandate goals. I'll start with employment.

As you'll recall, when the economy recovered from the pandemic, the labor market turned red hot. Demand for workers far exceeded supply, and that imbalance contributed to rapid wage growth and high inflation.

Now, the labor market-both in the nation as a whole and here in the Second District-has shown signs of returning to something closer to normal. Nationally, many indicators-such as quits rates and surveys of perceptions of availability of workers and jobs-have returned to around pre-pandemic levels.

Throughout this process of getting into better balance, the labor market has remained strong. The current unemployment rate of 3.7 percent is near my estimate for the unemployment rate that is likely to prevail over the longer run. And job growth continues to be solid.

Despite the very real progress in restoring balance, two important indicators point to lingering tightness in the labor market: job openings and wage growth. Job vacancies, which reached all-time highs in the red-hot labor market of 2022, have trended lower since then, but are still quite elevated relative to pre-pandemic norms. And while we have seen measures of wage growth come down from their pandemic-era peaks, they remain above pre-Covid averages.

The Return Trip of Inflation

That leads me to the other side of our mandate, price stability. As I mentioned, inflation has declined significantly over the past year and a half. This drop has been broad-based, encompassing decreases in inflation rates for food, energy, goods, and services. The decline in inflation has benefited from a reduction in demand and supply imbalances, both here and internationally, and the resolution of global supply-chain bottlenecks.

One way to illustrate the dynamics of inflation is through the New York Fed's measure of underlying inflation, called the Multivariate Core Trend inflation (MCT).[2] Before the pandemic, this measure was 1.8 percent, slightly below the FOMC's 2 percent inflation

target. As inflation rose following the pandemic and the onset of Russia's war on Ukraine, it climbed sharply, peaking at about 5-1/2 percent in June of 2022.

Since then, the MCT has fallen significantly, reaching 2.3 percent in December, reflecting declines in all the major categories of core inflation. Like the flight path the Apollo missions took to the moon and back, the MCT's return trajectory is a mirror image of its rise. But, we still have a ways to go on the journey to sustained 2 percent inflation.

You see a similar round trip in measures of near- and medium-term inflation expectations. According to the New York Fed's monthly Survey of Consumer Expectations, one- and three-year-ahead inflation expectations rose as inflation surged. Since then, these measures have come back to Earth.

One-year-ahead expectations are within the range seen in the years prior to the pandemic, and three-year-ahead expectations are now actually a bit *below* their 2014-2019 average.[3] Other measures of inflation expectations show similar round-trip trajectories.

Monetary Policy and the Economic Outlook

In summary, the economy is strong, imbalances are diminishing, and inflation has come down but remains above our 2 percent longer-run target.

What does that mean for monetary policy?

Over the past two years, the FOMC has put in place a restrictive stance of monetary policy with the aim of bringing inflation back to 2 percent on a sustained basis. Given the progress we have seen, the risks to achieving our maximum employment and price stability goals are moving into better balance.

At its January meeting, the FOMC kept the target range for the federal funds rate unchanged at 5-1/4 to 5-1/2 percent. In announcing that decision, the Committee said it "does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent."[4]

Taking into account the effects of restrictive monetary policy, I expect GDP growth to slow to about 1-1/2 percent this year, and the unemployment rate to rise modestly, peaking at around 4 percent.

I expect inflation to continue its return journey to 2 percent, although there will likely be bumps along the way, as we saw in the most recent Consumer Price Index data. To be specific, I expect PCE inflation to be around 2 to 2-1/4 percent this year and 2 percent next year.

The risks to this forecast are two-sided. Inflation may surprise on the upside, or consumer strength-a major driver of the robust growth we saw in 2023-may fade more quickly than I anticipate.

Conclusion

Price stability is the bedrock upon which our economic prosperity stands. While the economy has come a long way toward achieving better balance and reaching our 2 percent inflation goal, we are not there yet. I am committed to fully restoring price stability in the context of a strong economy and labor market.

As we navigate the remainder of this journey, I will be focused on the data, the economic outlook, and the risks, in evaluating the appropriate path for monetary policy that best achieves our goals.

Or, to paraphrase the words of the astronaut Alan Shepard, we'll assess incoming data until it's clear all systems are go.

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[1] Federal Reserve Bank of New York, Global Supply Chain Pressure Index.

[2] Federal Reserve Bank of New York, Multivariate Core Trend Inflation.

[3] Federal Reserve Bank of New York, Consumers More Optimistic about Their Financial Situation and Credit Access, February 12, 2024.

[4] Board of Governors of the Federal Reserve System, Federal Reserve issues FOMC statement, January 31, 2024.