Federal Reserve Bank of Boston®

Remarks as Prepared for Delivery

EMBARGOED UNTIL 11:30 A.M U.S. Eastern Time,
Wednesday, February 7, 2024 – OR UPON DELIVERY

Remarks to the Boston Economic Club:
"The Economy's Performance and Outlook, and Implications for Policy"

Susan M. Collins
President & Chief Executive Officer
Federal Reserve Bank of Boston

February 7, 2024

Held at the Federal Reserve Bank of Boston

The views expressed today are my own, not necessarily those of my colleagues on the Federal Reserve Board of Governors or the Federal Open Market Committee.

Key Takeaways

1. The U.S. economy overall performed remarkably well in 2023. Inflation slowed notably last year, while the job market remained quite favorable. These very encouraging trends have reinforced Collins' optimism that we are on a path to price stability with a healthy job market.

2. However, Collins says she will need to see more evidence that the disinflationary process will continue before beginning to carefully adjust the monetary policy stance. Recent developments in the economic data highlight that progress toward achieving the Fed's mandated goals could be uneven, and more time is needed to discern whether some of the promising economic trends we saw in 2023 will both broaden and persist, going forward.

3. In Collins' view, the threat of inflation settling persistently above the Committee's 2 percent target has receded, and risks to the economy overall are moving into better balance. Still, a sustained, durable return to 2 percent inflation will likely require demand growing at a more moderate pace this year. Collins sees the current stance of monetary policy as consistent with achieving this outcome.

4. Collins says policy should reflect the commitment to restoring price stability while also aiming to preserve the more-equitable outcomes seen in this recovery. In the current environment, appropriate policy requires an assessment of the incoming data that is holistic and increasingly focused on implications for the economic outlook. While not on a preset path, she believes it will likely become appropriate to begin easing policy restraint later this year.

5. Collins also notes that overall, the strength of an economy has many dimensions. In this regard, the Federal Reserve is involved in a breadth of activities, all in the public interest – to support a vibrant economy that works for all: monetary policymaking, economic research, bank supervision, infrastructure and services for the financial system, and supporting collaborations that expand prospects for progress in communities.

It is my great pleasure to welcome the Boston Economic Club back to the Federal Reserve Bank of Boston. I had a chance to greet you last February, for the event featuring Neel Kashkari and Roger Lowenstein, and I'm really delighted to be with you today. We appreciate that the Club chooses to hold its meetings here at the Bank each month – and certainly want the Boston Fed to be a key place for those who study the economy to gather.

Our focus here at the Boston Fed is on policies and services that support a vibrant economy that provides opportunities for everyone. And we share the Club's interest in a frank exchange of views, rigorous use of data, and focus on important topics with the potential for impact.

I should mention, as always, that my remarks represent my own views, not necessarily those of my colleagues on the Federal Reserve Board of Governors or the Federal Open Market Committee.

The Promise and Potential of New England

At the Boston Fed, our district includes just about all of New England, and I take seriously my commitment to all six states, visiting each one at least annually. Exchanging perspective with a wide range of stakeholders in the economy is vital to policymaking – and is meaningful, inspiring, and really enjoyable.

Although I lived in New England at an earlier stage of my career, I have been able to return with "fresh eyes" and note some of what makes it wonderful. Without question the talent and brainpower in so many fields – certainly economics and finance among them – make this region very special.

Today we're gathered in Boston. Extraordinary problem solving has occurred here, creating better living standards and entire industries – in medicine, technology, and financial products, to name a few. We have amazing talent and institutions here.

I mention this because we live in a world of challenges, and Greater Boston and New England face many – including housing supply and expense; transportation infrastructure; access to dependent care, and the potential for climate shifts to affect assets or expenses.[1]

But we have an immense capacity for innovation and problem solving, as we've shown. I look forward to what we can accomplish in New England to support a vibrant economy that works for all. I am optimistic about what we can accomplish when we care, collaborate, study, and act.

The Boston's Fed's Portfolio and Mission

I'd like to highlight some of the ways the Boston Fed reflects that spirit of innovation and problem-solving. As you know, the strength of an economy has many dimensions – so the Federal Reserve, our nation's Central Bank, is involved in a number of activities, all in the public interest. Most people know us for monetary policy, and the research that underpins it. We're also supervisors of some of the nation's financial institutions, and provide back-end infrastructure and services for the financial system. And we examine factors that could limit people from participating in the economy, and support research and collaborations that expand prospects for progress in communities.

I'll mention just two examples of Boston Fed innovation.

First, many parts of New England that were once centers for manufacturing or natural resources have faced long-term challenges. Our Working Places initiative,[2]

[1] See, for example, the following work by Boston Fed staff:
- The Effects of Weather on Massachusetts Municipal Expenditures: Implications of Climate Change for Local Governments in New England (bostonfed.org)
- Early Child Care for Working Parents (bostonfed.org); Podcast Season 2: A Private Crisis - Federal Reserve Bank of Boston
- Housing and rent prices with Paul Willen - Federal Reserve Bank of Boston

started under my predecessor Eric Rosengren, is based on research showing that an essential element of place-based economic resurgence is local, cross-sector collaboration. Now in 30 communities across 5 states, teams of local leaders choose a shared goal for improving the economy that benefits low-income people – for example, creatively supporting workforce development, affordable housing, or childcare supply; or removing barriers to entrepreneurship. They develop and implement strategies. The Fed hosts, convenes, and supports these efforts – but not financially. The real work is in local ingenuity and commitment.

Second, I mentioned the Fed's work on payments. It wasn't so long ago that paper checks had to be physically flown around the country to settle at the bank they were drawn on – a slow, costly necessity. The Boston Fed and others helped pioneer digital check imaging, and expanded automated clearing of electronic payments – and more recently, creation of an entirely new interbank system for instant payments, the FedNow Service.[3]

When fully available, instant payments will provide substantial benefits for consumers and businesses, including rapid access to funds, or just-in-time payments to manage cash flows in bank accounts. The FedNow Service can help workers in the gig economy get access to their wages on completing their shifts; help consumers pay a bill on its due date, avoiding a late fee; and help small businesses get instant proceeds to help cash flow.

While I'm always happy to talk more about all we do, today, I'll focus the rest of my remarks on the economy, monetary policy and my outlook, and then will look forward to taking questions.

---

[2] I discussed this work in more detail in this talk: "The National and Regional Economy: Navigating Near-term Changes and Long-term Challenges" (bostonfed.org). And one can learn more about the Bank's work to support growth in smaller cities and rural areas at https://www.bostonfed.org/community-development/supporting-growth-in-smaller-industrial-cities.aspx

[3] Learn more about the FedNow® Service at https://explore.fednow.org/about

The National Economy and Fed Policy

Economic outcomes last year surpassed most observers' expectations, including my own. Growth and the labor market remained quite strong, while inflation slowed notably.

As some of you know, I have described myself as a "realistic optimist" for well over a year now. These very encouraging trends have reinforced my optimism that we are on a path to price stability, with inflation durably at 2 percent, and a healthy labor market. However, the "realistic" part is important as well – uncertainty remains elevated, and there are risks to my outlook – although those risks are coming into better balance.

Last Friday's data release showing a surprisingly strong labor market is a case in point – and in this case, good news. Still, it helps illustrate the logic in methodically waiting for more evidence that the economy is sustainably on that desired path, before beginning a policy adjustment.

These are the issues I'd like to discuss with you today. To do so, I'll start by highlighting key aspects of recent economic performance, then discuss my outlook, and the implications for policy.

Recent Economic Performance

As I mentioned, the U.S. economy overall performed remarkably well in 2023. GDP growth, at 3.1 percent, defied widespread pessimistic forecasts made at the end of 2022. The unemployment rate remained historically low – below 4 percent – with strong overall employment gains and healthy wage increases.

These positive developments were accompanied by greater progress on inflation than most anticipated. Headline and core inflation, where the latter excludes volatile food and energy prices, were both around 2 percent over the last 6 months of 2023. They had been above 3 percent and 4 percent, respectively, in the second half of 2022.

By the way, obviously food and energy are vital, but we focus on core inflation because it has been shown to be a strong predictor of future inflation trends.

Normally, strong economic activity tends to raise inflationary pressures. The fact that this did not occur indicates significant, favorable supply-side developments, which tend to be disinflationary. In particular, last year's improvements in the economy's productive capacity were driven by further resolution of supply chain bottlenecks; a rebound in labor supply, in part driven by immigration; and increased labor productivity in some sectors.

Importantly, these positive economic developments have continued to be unusually equitable, a point highlighted by Cecilia Rouse, former chair of the Council of Economic Advisers and now president of the Brookings Institution, at our economic conference last fall, which some of you attended.[4] The rise in labor force participation among working-age individuals was widespread across racial and other demographic groups. I have heard from contacts in New England that some employers have increased efforts to train workers and are exploring ways to find untapped talent. This should continue expanding opportunities for people who typically face greater challenges finding employment.

In this strong labor market, with unemployment rates near historic lows, many workers have also moved into better jobs. Aggregate wage growth was around 5 percent in 2022 and 4 percent last year, and wage gains have been especially favorable and sustained for lower-paying occupations. While such developments cannot be taken

[4] Dr. Rouse's presentation can be found at https://youtu.be/inRU_TPE3z4. All the conference materials and videos can be found at https://www.bostonfed.org/news-and-events/events/economic-research-conference-series/rethinking-full-employment.aspx. The conference provided analysis of factors that likely prevent some people from participating fully in the labor market, even when the overall economy is thriving. Conference presenters explored past and current thinking on measuring full employment, paying particular attention to the role of long-term labor market trends as well as to more recent changes in labor market structure. Participants also discussed recent research on how monetary policy can be conducted to achieve full employment and price stability at the same time.

for granted, they represent tangible progress toward achieving a more broad-based and inclusive notion of full employment.[5]

The Outlook

Given the positive economic news, what can we expect going forward? And what can monetary policy do to achieve price stability at the 2 percent target, while maintaining a healthy labor market?

An open question is how much longer supply-side progress will continue. While we may see some more labor force growth, the prospects for additional labor supply improvements seem somewhat limited. And although there may be some further effects on consumer prices from the past resolution of supply chain bottlenecks, most of that is likely behind us. Also, productivity is always difficult to forecast. Many businesses, especially in the services sector, have learned to operate effectively with fewer workers – but there is likely a limit to how far this process can go.

So, while we may still get some positive supply-side news, a durable return to 2 percent inflation will likely require demand growing at a more moderate pace this year. I expect this slowdown will happen, but the timing is difficult to predict, and the road may well be bumpy.

To be clear, the current stance of monetary policy is consistent with achieving this outcome. However, the balance sheets of both households and businesses are stronger today than in prior periods when the Fed needed to restrain demand to achieve price stability. I will not be surprised if demand remains fairly robust in the early part of 2024. Consumer spending could remain elevated in the near term, given income from

[5] As I pointed out in remarks at the Bank's 67th Economic Conference (my remarks entitled "Full Employment: A Broad-Based, Inclusive Goal"), no one statistic can adequately characterize the labor market because aggregate numbers can mask the wide range of experiences across people, sectors, and places. Uneven labor market outcomes call for a full and focused exploration, motivated by the duty to pursue the Fed's maximum employment mandate from Congress. For some people, communities, and places, there are substantial and persistent gaps in economic outcomes – including but not limited to employment. This underutilization of the workforce adversely affects national productivity and prosperity.

the strong labor market and the wealth some households have accumulated in the aftermath of the pandemic. And many companies still have ample internal sources to finance their expenditures, although increased credit costs are starting to affect capital investment decisions. Further, the unexpected strength in recent GDP and labor market data exemplifies the on-going resilience of demand, and highlights that the anticipated slowdown in activity may take some time.

However, I do see some signs consistent with an expected demand moderation. Delinquencies on credit card and auto loans have risen briskly and are around pre-pandemic levels. And some consumers are becoming more reliant on revolving debt to finance their expenditures. Orders for capital goods excluding aircraft are slowing, suggesting that businesses are becoming increasingly sensitive to higher financing costs.

And despite the recent hiring strength, there are indications of the labor market normalizing at healthy levels. In particular, job turnover rates have declined noticeably since the first half of 2023, and job openings are down, especially in more cyclical sectors.

Overall, these developments imply that the risks related to inflation and economic activity are coming into better balance. In addition to the points I've discussed, many measures of inflation expectations have returned to pre-pandemic levels. This all suggests to me that the risk of inflation running persistently above the Committee's target, while still there, has receded.

Policy Implications

In this context, I think that policy needs to reflect a steadfast commitment to restoring price stability – following through on the progress we have made – while also aiming to preserve the more-equitable economic outcomes seen in this recovery. And I remain cognizant of the geopolitical and other risks around my baseline outlook.

This brings me to what I plan to focus on going forward, as I monitor economic developments and consider appropriate policy. I certainly believe policy should remain data dependent and that it is not appropriate to specify a pre-set path. Given the progress to date and the more balanced risk environment, my holistic assessment of available data will focus on gaining additional confidence in the baseline forecast of sustained low inflation with a healthy labor market.

It is important to recognize that the path the economy takes toward the Fed's mandated goals may continue to be bumpy and uneven, and we should not overreact to individual data points. To my thinking, that reflects the realities of a unique and challenging pandemic and the economic recovery from it. Expecting *all* indicators to be well aligned is too high a bar, but seeing sustained, broadening signs of progress should provide the necessary confidence I would need to begin a methodical adjustment to our policy stance.

To this end, here are a few of the (many!) developments I will be watching closely: I continue to look at the components of inflation – not because the composition matters for achieving our target, but because different components behave differently. Housing as well as non-shelter service price inflation are taking longer to return to their pre-pandemic trends, and I hope to see additional progress there.

I want to see evidence of wages evolving in a way that is ultimately consistent with price stability. Here I'll note interesting work by Boston Fed economists, which suggests that, given the increases in prices and labor productivity to date, there is room for wages to catch up and continue increasing at a healthy pace for some time without necessarily spurring inflationary pressures.[6]

It is also important that short- as well as long-term inflation expectations remain well anchored. And given the centrality of labor market developments to the outlook, I will continue to look for signs of labor demand moderating in an orderly way, to a healthy, sustainable balance with supply.

---

[6] See Is Post-pandemic Wage Growth Fueling Inflation? - Federal Reserve Bank of Boston

So, while heartened by the progress to date, I will need to see more evidence before considering adjusting the policy stance. Indeed, I fully support last week's FOMC policy statement. It unambiguously reaffirms the Committee's resolve to achieve and maintain our inflation target. For the moment, policy remains well positioned, as we carefully assess the evolving data and outlook.

That said, as we gain more confidence in the economy achieving the Committee's goals, and consistent with the last set of projections from FOMC participants, I believe it will likely become appropriate to begin easing policy restraint later this year. A methodical, forward-looking strategy that eases policy gradually will provide the flexibility to manage risks, while promoting stable prices and maximum employment.

Thank you for being here today, and best wishes for 2024. Now I'm happy to take some questions.