Federal Reserve Bank of Boston®

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Perspectives on the Economy from Susan M. Collins

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Points shared while meeting stakeholders and assessing economic conditions in the Massachusetts towns of Fall River, New Bedford, Centerville, and Plymouth

Please note, these views are my own and may not reflect the views of colleagues at the Board of Governors, on the Federal Open Market Committee, or at other Reserve Banks.

Economic Resilience, Amid Elevated Tariffs and Uncertainty

Economic conditions remain resilient; however, the outlook is still clouded by significant uncertainty, especially as it relates to trade policy. Focusing on the Fed's congressionally mandated goals of price stability and maximum employment, I see monetary policy as currently well positioned, and I supported last week's FOMC decision to maintain the target range for the federal funds rate at 4¼ to 4½ percent. I believe a careful, patient, and highly attentive approach to monetary policy remains appropriate at this point, as we learn more about tariffs and other changes in government policies, and actively assess their implications for the economy.

The U.S. Economy Remains Solid, Overall

The data show an economy that remains solid overall. Labor market conditions point to a modest deceleration in activity, but are generally healthy: unemployment is low, layoff indicators are around pre-pandemic levels, and job gains – while moderating – are close to their trend pace. Balance sheets of both firms and households are also in good shape: first-quarter earnings of nonfinancial corporations were solid, while household fundamentals are favorable overall, supported importantly by robust real disposable income growth. And after rising at the beginning of this year, inflation has recently continued its slow, uneven decline back to the Fed's 2 percent target, and underlying price pressures appear contained. But there are some early signs of tariff-induced price increases.

The Economic Outlook Depends Importantly on Trade Policy

Tariff policy continues to be the main driver of my outlook for the economy in the near to medium term, with higher tariffs leading to a rise in inflation, slower output growth, and a higher unemployment rate relative to current conditions. The reduction in tariff rates relative to April has lowered my assessment of the likely size of tariff-induced price hikes. But an effective tariff rate around 15 percent is still significant, and is likely to boost inflation by about one percentage point, pushing core PCE inflation somewhat above 3 percent by the end of this year. In turn, higher tariffs are likely to reduce household purchasing power and increase firms' input costs, slowing demand and hiring. But the associated rise in the unemployment rate could be tempered by more subdued labor supply growth from less immigration. Over the coming months, I expect the effects of tariffs to show through more significantly, as inventory frontloading wanes and tariffed goods hit the shelves and enter firms’ production processes. Most of the ensuing price and demand adjustments are likely to take place over a few quarters, before disinflation resumes and growth picks up. But uncertainty – including about the ultimate size and impact of tariffs – remains elevated, clouding the outlook.

Attuned to Cautionary Signals and Risks

I continue to see upside risks to my outlook for inflation and downside risks to my outlook for economic growth and the labor market. And I do not rule out scenarios with larger and more persistent tariff effects on inflation. At the same time, there are signs that it is taking longer for some new entrants in the labor market to find jobs, and that firms are becoming more cautious and selective in their hiring. I also continue to hear about businesses pausing or delaying projects, especially large ones, in the face of high uncertainty. This “wait-and-see” approach could slow activity further, especially if risk sentiment in financial markets deteriorates. Geopolitical risks have also risen. And it is too soon to assess the likely impacts of other changes in government policy – including immigration, fiscal policy, and the regulatory environment – on the evolution of the economy in the near term. I will also note that reduced funding for education and scientific research could have longer run effects on innovation and the growth rate of the economy.

An “Actively Patient” Monetary Policy Approach Is Appropriate for Current Challenges

From a policy perspective, it is essential that longer-term inflation expectations remain anchored, a critical sign of the Fed’s credibility with the broader public. At the same time, calibrating appropriate policy is challenging in contexts when projections of inflation call for a tighter policy stance while forecasts of real activity call for a looser one. The overall solid current conditions enable the Fed to take the time to carefully assess the incoming data and their implications for the economic outlook and the balance of risks to inflation and economic activity. Indeed, the recent back-and-forth in tariff policy, and the potential for more changes to come, validate the careful approach I call “active patience” that the Fed has taken since the beginning of the year. While I continue to expect it will be appropriate to resume gradual policy normalization later this year, my outlook could change significantly as events unfold, and the economic impact of changes in various government policies comes into sharper focus. Much will depend on whether the “price shock” from tariffs dissipates quickly, without derailing inflation expectations, and on whether the associated slowdown in real activity is limited. For now, however, I see the current monetary policy stance as modestly restrictive, and well positioned to address a range of possible outcomes.

Engaging with New Englanders to Learn About Challenges & Opportunities

Connecting with people across New England is central to the Boston Fed's overarching mission of a vibrant economy that works for everyone, and a vital part of responsible policymaking. Hearing directly from a range of stakeholders, from a variety of sectors and locations, helps us uncover current and emerging realities in the local economy and beyond. This complements our on-going, formal analysis of economic and financial data and deepens our understanding of the challenges, as well as the opportunities and strengths, in the region's economy. Often cited strengths include a highly skilled and educated workforce; a tradition of innovation; our institutions, such as universities and hospitals; strong and innovative companies in many industries; and leading cultural institutions and nonprofits. On the other hand, challenges include a high cost of living, limited availability and affordability of housing and childcare, slower rates of population and labor force growth compared with other regions, and changes in research and medical funding.

Meetings with Southcoast Stakeholders this Week Will Illuminate Economic Conditions

This week, I will travel through southeastern Massachusetts to engage with a wide range of stakeholders in the economy. Transportation and infrastructure play important roles in labor force participation and economic activity, so I am eager to speak with MBTA leaders, while riding the new South Coast commuter rail line to Fall River. In New Bedford, I'll connect with business leaders to discuss the challenges and opportunities in their industries and the region. In Centerville, I'll hear from individuals in the hospitality industry, which is so important to Cape Cod and many other parts of New England and the country. In Plymouth, I'll tour the Aviation-Maintenance Technology program at Cape Cod Community College – a great example of a "win-win" skill-development program, benefitting workers and the companies that need them. I'll also meet with bankers from across the state, to exchange perspectives on economic, financial, and credit conditions.