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"The National and Regional Economy: Navigating Near-term Changes and Long-term Challenges"

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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. Restoring price stability remains the imperative for monetary policymakers, and there is more work to do. I anticipate the need for further rate increases, perhaps at a slower pace, depending on incoming data, before holding rates at a sufficiently restrictive level for some time. More measured rate adjustments will better enable us to address the competing risks that monetary policy now faces.

2. While realistic about the risks and uncertainties, I remain reasonably optimistic that there is a pathway to reducing inflation without a significant economic downturn. I see ongoing resilience in the economy, evidenced by many firms' continued hiring plans, and household and business spending that is holding up relatively well.

3. New England's economy has many strengths to nurture, and some key challenges to address. This is an opportunity to take stock, look ahead, and assess long-term trajectories, opportunities, and imperatives – especially related to the availability of both workers and housing.

4. The Fed's mandate and mission involve an economy with opportunities for all – but outcomes persistently differ in certain places, and for certain people or groups. The region's economy is healthiest when it's providing opportunities for all to contribute and prosper, not leaving some people and places behind. Today's conference will explore the challenges – and opportunities – presented by the post-pandemic economy for New Englanders.

5. Since 2014, the Boston Fed has been leading promising work focused on encouraging local efforts to find economic resurgence – in smaller cities where manufacturing once flourished, and rural areas facing challenges. We call it the Working Places Challenge – and the model is proving effective.

6. "Working Places" is based on research that showed a key to resilience, through waves of economic change and challenge, is cross-sector collaboration among local individuals willing to take on shared leadership. The program is structured as a competition for grant money (not from the Fed but from the private sector, philanthropy, and states). Local leaders are building cross-sector vision and priorities, and working on them together. It helps communities weave together many small individual approaches into one, coherent system – and then improve the system. The Fed hosts, convenes, and supports these efforts.

7. Working Places helps the Fed encourage economic progress in local economies, grounded in our mission of a vibrant and inclusive economy, and our mandate to achieve price stability and maximum employment – for all not just some. It is one example of strategic partnerships the Boston Fed creates to improve New England's economy. Like other community development efforts of the Boston Fed, it complements our monetary policy, research, payments, and supervision work as we seek to fulfill our mission and mandate.

Good morning, and thank you for joining us. I want to thank our organizers: my colleagues at the Boston Fed's New England Public Policy Center – part of our Research department – as well as our partners at the New England Economic Partnership, and the Donahue Institute at the University of Massachusetts.

This gathering provides an opportunity to explore key aspects of the future of the New England economy, especially given the pandemic effects that are still with us, and still evolving. It is important to study the shifts we are seeing – in work, commuting, housing, and economic activity – with an eye to navigating them effectively, and ensuring a vibrant regional economy with opportunities for all.

In my remarks, I'll speak briefly about monetary policy, then touch on what I've seen in the New England economy during my first six months in this role, and finally talk about an approach we at the Fed have found helps local community efforts to coalesce around challenges, in support of economic resurgence.

The National Context: The Macroeconomy and Monetary Policy

My comments about monetary policy and the national economy focus on recent developments related to the Fed's dual mandate of maximum sustained employment and price stability. Of course, these comments are my own; I'm not speaking for my fellow policymakers.

With the inflation rate well above the 2 percent target, the Federal Open Market Committee (or FOMC) has been resolute in its goal of restoring price stability – raising interest rates aggressively since last March. High inflation takes a toll on households, especially the most vulnerable ones. And it complicates investment and planning decisions for firms. Price stability is essential for a well-functioning inclusive economy that works for all, and for healthy labor market conditions that are sustainable over time.

We are starting to see some effects of the cumulative policy actions the FOMC has taken so far. Less demand (from higher interest rates), combined with lower input costs (from easing supply bottlenecks), are contributing to noticeably slower inflation for goods – with the prices for some goods actually declining. These developments, together with decreasing energy prices, are at the root of the inflation improvement we saw in the last quarter of 2022. But households consume far more services than goods, and services inflation remains persistently high.

A key piece of this has been sizeable increases in shelter costs. However, monetary policy tightening has slowed new rent growth considerably, which should lead to a moderation in shelter inflation starting in the spring of this year. For services outside of shelter, labor tends to be the most important input – so developments in this component of services inflation are ultimately tied to the behavior of wages.

Bringing labor market conditions into better balance will therefore be critical to achieving our inflation target. While labor market activity has shown some signs of moderating, there is still a long way to go. Indeed, high job vacancies and "quit rates" are signs that labor demand remains strong. And while the latest average hourly earnings data suggest some softening of wage pressures, labor costs continue to grow more rapidly than is consistent with 2 percent inflation. (I'll note that workers do not benefit from nominal wage gains that are eroded by too-high inflation. What matters for workers are gains in real wages.)

While it is promising to see the effects of higher rates starting to spread from the most interest-sensitive sectors to the broader economy, more is required to ensure a steady path toward our inflation target. As monetary policymakers, restoring price stability remains our imperative. Thus, I anticipate the need for further rate increases, likely to just above 5 percent, and then holding rates at that level for some time.

Now that rates are in restrictive territory and we may (based on current indicators) be nearing the peak, I believe it is appropriate to have shifted from the initial expeditious pace of tightening to a slower pace – though appropriate policy will, of course, depend on a holistic review of available data. More measured rate adjustments in the current phase will better enable us to address the competing risks monetary policy now faces – the risk that our actions may be insufficient to restore price stability, versus the risk that our actions may cause unnecessary losses in real activity and employment. I am well aware that, as with inflation, the costs of higher unemployment are disproportionately borne by people of color and economically vulnerable groups.

I'll conclude my comments about monetary policy by noting that I continue to be what I call a "realistic optimist." The ongoing resilience of our economy – from many firms continuing to increase their payrolls, to business and household spending still holding up relatively well despite an uncertain economic environment – make me reasonably optimistic that there is a pathway to reducing inflation without a significant economic downturn. But I also recognize risks and uncertainties to that outlook, including the possibility of a more substantial downturn driven by a self-fulfilling loss of confidence in the economy.

These are among the many considerations for both determining and communicating monetary policy. I'll shift now from national policy to some of the longer run opportunities and challenges with a focus on New England – the Fed's First District, which the Boston Fed serves.

New England's Economy… and the Issue of Gaps

New England's economy has many strengths to nurture, and some key challenges to address. The conference today provides an opportunity to take stock, to look ahead, and to assess long-term trajectories, opportunities, and imperatives – especially around the availability of both workers and housing.

Some of the greatest strengths of New England can be found in our workforce, and the innovative institutions located here. Our workforce is among the most highly skilled and educated in the world.[1] The region also hosts many organizations leading in healthcare, technology (including biotechnology), clean energy, and higher education.[2]

These enviable characteristics suggest New England is favorably positioned for the future. I see the Fed's mandate and mission, however, as encompassing an economy with opportunities for *all* – not just those with advanced degrees, and not just the cities and towns that are thriving. When we look across New England, we see places and communities that are not fully participating in the region's overall prosperity. For example, some small cities, and rural areas with dwindling employment, struggle to sustain local schools and services.

And we see some demographic groups – particularly when looking by race and ethnicity – with lower levels of income, wealth, and educational achievement than their white and Asian peers. For instance, students in New England perform better on math and reading tests than most other states, but there are large gaps by race and income.[3,4] And household incomes differ widely by race.[5]

The region's economy is healthiest when it is providing opportunities for *all* to participate, contribute, and prosper, not leaving some people and places behind. As we head into a future of slowing population growth and likely continued labor challenges, we need the contributions and capabilities of all communities and places across the region. So this conference is timely and important, as we think together about the challenges – and opportunities – presented by the post-pandemic economy for people and places.

Working Places: Local Successes from a Productive Model

I'll turn now to an effort the Boston Fed has been involved with for nearly a decade, begun under the leadership of my predecessor, Eric Rosengren. Since 2014, staff here have focused on encouraging local efforts to find economic resurgence in smaller cities and rural areas facing long-term struggles. We call it the Working Places Challenge.

These places were once centers of the manufacturing and natural resource economies in New England. With the employment decline in those industries, many of these communities have struggled to reimagine and rebuild their economies. They face myriad challenges: aging housing stock and infrastructure, a dwindling tax base, and often high rates of poverty. Of course, they also have strengths and potential.

"Working Places" is based on research that showed the key to economic resilience, through waves of change and challenge, is cross-sector collaboration among local individuals willing to take on shared leadership.[6] This collaborative leadership seems to be the "secret sauce" in resurgent communities. The Working Places model helps it blossom.

The program is structured as a competition for relatively modest grant money (not from the Fed but rather from the private sector, philanthropy, and states). Local leaders – now in 30 communities across 5 states – are building cross-sector vision and priorities, and working on them together. The Fed hosts, convenes, and supports these efforts.

It starts with teams choosing a shared goal for improving the economy that benefits low-income people. Many teams focus on improving conditions and capabilities for the local workforce, or for locally owned businesses. If the independent jury (not the Fed!) selects a community in the competition, that team receives several hundred thousand dollars over three years (again, not from the Fed), to use in coordinating efforts and creating new interventions.

I'll share some examples:

- The team in rural **Lamoille County in northern Vermont** is newly focused on responding to the need for housing voiced by low- and moderate-income residents and the employers in need of workers. The county has low-income areas of poverty alongside higher income and second-home communities associated with skiing. The need for housing is made more acute by the influx of new residents – many working elsewhere, remotely – and the growth of the short-term rental market, which squeezes out long-term renters. Locals from a variety of sectors are working together to move the needle on housing, by experimenting with novel approaches such as extending water and sewer infrastructure to enable new development, and creating a landlord liaison to facilitate rental housing for local residents.

- In **East Hartford, Connecticut,** people across sectors saw the need to align job opportunities for local residents with local employers' workforce needs. East Hartford is a diverse community. Compared to nearby towns and the state as a whole, it has higher poverty rates, more working poor, fewer with college degrees, and more female-led single-parent households. The Working Places team focused on local-resident job training, local recruiting and placement with major employers, and summer jobs for high school students.[7] For example, the Professional Skills Academy has now trained three cohorts of local residents for placement with local employers, in cooperation with a local college – including relatively well paid, career-ladder jobs.

- **Lawrence, Massachusetts,** once a textile manufacturing powerhouse, has been one of the lowest-income cities in the Commonwealth for decades, with deteriorating services and high rates of poverty. People in city government, nonprofits, the school department, the community college, and local firms decided to focus on raising the income prospects of parents with children in the public schools. They provided job training and wraparound services for more than 600 parents, assisted 200 families with job placements (with an average wage increase of 25 percent), created new training pipelines with employers and the local community college, and integrated some long-term interventions into the school system, aimed at improving family well-being.[8]

In sum, we see progress, and promise. Working Places helps communities weave together many small individual approaches into one, coherent system – and then improve the system. It has been wonderful to see relatively limited awards be followed by substantial private and public investment, capitalizing on new cross-sector frameworks and creating new hubs of economic activity. For example, in Fitchburg, Massachusetts, work by the local team was a key factor in now more than $100 million in new investment downtown and in surrounding neighborhoods. In Massachusetts, the Executive Office of Economic and Housing Development created the Urban Agenda grant program, modeled partially on Working Places, which has now invested in collaborative economic growth projects in over 50 communities over 5 years, including Lawrence – and a national funder[9] created a small-city investment fund for follow-on investment.

Independent outside evaluations cite progress such as heightened involvement of anchor institutions like educational and health care organizations, and other private employers; evaluations also find city government spending more aligned with local priorities.[10] And from 2011 to 2016, poverty dropped and high school graduation rates improved faster and more dramatically in our Round 1 winning "working cities" (Lawrence, Fitchburg, Holyoke, Chelsea) than in the state as a whole and other similar cities.

There are important lessons from Working Places. Complex issues cannot be solved by one sector, one organization, or one person. Successful collaboration requires attention to process, and new voices at the table to expand insight. It requires the flexibility to seize opportunities – and to change along the way, including admitting when efforts need to be rethought. A neutral, trusted convener can help. The most successful Working Places teams have robust community engagement, local government supporters, and an urgent shared purpose.

While still unfolding, it's a great story that deserves to be told – and hopefully replicated as well as studied.

Concluding Observations

The Working Places initiative helps the Fed encourage progress in local economies. It is grounded in our mission of a vibrant and inclusive economy, and our mandate to achieve price stability and maximum employment for all, not just some. Like other community development efforts of the Boston Fed, it complements our monetary policy, research, payments, and supervision work, as we seek to fulfil our mission and mandate.

If we are to move toward a more inclusive economy over time, the capacity for low-income places to adapt to economic change, which Working Places supports, is ever more important. This is particularly true in the context of the kinds of changes in housing and work we are discussing at today's conference.

I'll conclude my remarks there. We have important topics to cover today, and some terrific experts to share their perspectives. I look forward to hearing from our panelists about shifting economic conditions, and invite moderator John Ballantine to begin that session.

Again, thank you all for joining us today.

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[1] Forty-seven percent of Massachusetts residents 25 and older hold a bachelor's or advanced degree, the highest among states (although bested by Washington, D.C.). Three other New England states – Connecticut, New Hampshire, and Vermont – are also in the top ten for educational attainment. American Community Survey, one-year sample for 2021.

[2] New England "punches above its weight" in higher education, with many standout institutions. The higher education sector directly accounts for 3.4 percent of total employment in New England, compared to 2.5 percent nationally. Quarterly Workforce Indicators (QWI) US Census Bureau; Integrated Public Education Data System (IPEDS), National Center for Education Statistics, FY2018.

[3] Bradbury, Kathy, "Racial and Socioeconomic Test-Score Gaps in New England Metropolitan Areas: State School Aid and Poverty Segregation." NEPPC Research Report 21-2, February 2021. https://www.bostonfed.org/publications/new-england-public-policy-center-research-report/2021/racial-and-socioeconomic-test-score-gaps-in-new-england-metropolitan-areas.aspx

[4] Black students in New England score 6/10 of a standard deviation below white students and Hispanic students score half of a standard deviation below.

[5] In 2021, incomes were $111,000 for Asian households, $88,000 for white households, $62,000 for Black households, and $55,000 for Hispanic households. American Community Survey, 1-year estimate for 2021.

[6] See the Federal Reserve Bank of Boston's "Public Policy Discussion Papers, No. 13-3: 'Economic Distress and Resurgence in U.S. Central Cities: Concepts, Causes, and Policy Levers'" by Yolanda K. Kodrzycki and Ana Patricia Muñoz: https://www.bostonfed.org/publications/public-policy-discussion-paper/2013/economic-distress-and-resurgence-in-us-central-cities-concepts-causes-and-policy-levers.aspx

[7] Many of these efforts focused on jobs in manufacturing or the service industry that could not be done remotely when COVID hit. In the wake of COVID-19, the team realized that over 50 percent of adult education participants – largely Black and Latino people – in Hartford and East Hartford do not have regular access to the Internet, which is hindering learning, the ability to apply for employment, and access to remote jobs. As a result, the team is now gathering data to better understand the need and create new strategies, which is critical to improving employment opportunity for their residents.

[8] Prior to the disruptions created by the COVID-19 pandemic, affecting schools everywhere, the Lawrence school turnaround – which included the Working Cities team, and also extended beyond it – included progress in math scores in younger grades, increases in English proficiency, and increases in the graduation rate.

[9] The Kresge Foundation

[10] Local systems like the job market and school system are also beginning to deliver better outcomes for residents, though it's important to say that Working Places teams are just one part of those efforts.