

Remarks on the Outlook and Monetary Policy

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The views expressed by the author are his own and do not necessarily reflect those of the Federal Reserve System, its governors, officers or representatives.

Thank you for participating in the Kansas City Fed's Agricultural Summit and, for those of you who have travelled, welcome to Omaha. I am a Nebraska native, growing up just down the road in Papillion, and I spent much of my career as a banker here, working with the businesses and farmers that contribute so much to the region and to the nation's economy. I now bring this perspective to my role at the Kansas City Fed, and I am honored to represent the region and the people and businesses that reside here at the Federal Open Market Committee, which sets the nation's monetary policy.

This event continues our tradition of bringing together leaders in the agricultural and food industries to share insights and keep the Bank up to date on the current conversation in the sector. This year the theme of the summit is "Investment in Food Production and Distribution." In keeping with this theme, the Kansas City Fed has long invested in understanding and monitoring the farm economy. Many of these efforts are organized out of our Omaha Branch and have benefited from the leadership of our Omaha Branch Executive Nate Kauffman.

Today I will provide a high-level view of the Fed's relationship with agriculture before turning to my outlook for the overall economy and monetary policy.

Agriculture and the Fed

Agriculture is important to the seven states of the Tenth Federal Reserve District. In addition to the production of crops and cattle, the region is concentrated in food processing as well as the ancillary industries that support and grow out of the agriculture sector.

Agriculture is also important to the Federal Reserve. The Fed was created in 1913 in part because farmers demanded it. The agricultural sector, and the local community banks that served farmers, had grown tired of having to rely on money center banks in Chicago and New York to supply needed liquidity. They found that these banks were unresponsive to seasonal changes in

credit demand inherent to the agricultural economy. Demands for a more elastic currency that could flex to changing conditions underpinned much of the early support for the Federal Reserve System.

The role of farmers in the creation of the Fed also played a role in how the system was structured. This same structure persists today and continues to play an important role in the Fed's ability to serve the public. A demand for national representation in monetary policy supported a system of 12 distinct geographically defined Reserve Banks, which along with the Board of Governors in Washington, makes up the Federal Reserve System. The Reserve Banks reflect the belief that monetary policy decisions are too important to be left to Washington and New York alone, but instead require input from all the varied industries, geographies, and communities that make up the United States. This distribution of decision-making power has served the nation well.

Agriculture and the KC Fed

At the Kansas City Fed we are invested in understanding the agricultural and food markets and making sure that we communicate that understanding to a larger audience.

Some of what we do relates to the collection and distribution of data, with an emphasis on banking and credit. Earlier this month we released the most recent results of our quarterly Survey of Agricultural Credit Conditions. We produce this report in collaboration with many of our Reserve Bank peers. In the survey, agricultural lenders are asked about the demand for agricultural loans as well as loan availability, repayment rates, farm income, and other indicators of farm sector financial health, including recent changes in farmland values.

Results for the first quarter show signs of stress in the farm economy. Low crop prices are pulling down farm incomes and leading to low loan repayments and increased demand for

extensions and credit. Farmland prices, which have seen strong growth in recent years, slowed across much of the country, and have fallen slightly in the Kansas City Fed's territory for the first time this decade.

This data, collected and distributed by the Fed, provides important insights that inform monetary policy but also benefits industry, farmers, and other policymakers concerned about the farm economy.

Food Prices and Inflation

In addition to regular reports and data, staff at the Kansas City Fed also produce research on the agricultural sector. A relevant example for monetary policy is a research piece examining the role of food prices in inflation.¹ I would like to review their argument, which builds on a speech I delivered earlier this year at the USDA, because I think it is important for how the Fed thinks and talks about inflation.²

Inflation is of course one of the Fed's primary concerns. It is one half of the dual mandate that Congress has established for the Fed, along with maximum employment. To achieve its mandate the Fed aims to keep inflation at 2 percent. This inflation objective is measured as the change in the price of overall personal consumption expenditures (or headline PCE). However, in discussing the outlook for prices, Fed policymakers and other economic forecasters often refer to core inflation, which excludes energy and food prices. The recent research by our staff argues that excluding food prices from core inflation might have made sense in the past, but doing so now provides little benefit and comes with potential costs.

¹ See Scott, Mustre-del-Rio, Lusompa, and Nichols, "[Is it Time to add Food-at-Home Inflation to Measures of Core Inflation?](#)" Kansas City Fed *Economic Bulletin*. June 6, 2025.

² See remarks at the USDA's 2025 Agricultural Outlook Forum in Washington, D.C., "[Agriculture and the Federal Reserve](#)," Feb. 27, 2025.

Backing up, if the Fed’s target is headline inflation, why do policymakers often speak about core inflation? It is because food and energy prices historically have been volatile — so volatile that core inflation is often thought to be a better predictor of trend inflation.

For energy, it is not hard to find examples where outsized spikes or declines in oil prices led to temporary changes in inflation that were clearly not informative to the trend. But is the same true for food prices?

When the idea of core inflation was first introduced in the mid-1970s, the contribution of food to overall inflation was in fact very volatile — much more so than most other prices consumers faced. But this is no longer true. Since the 1990s food prices are no more volatile than most other prices. In contrast, energy prices remain far more volatile than food prices and other prices in the economy.

Moreover, research at the Kansas City Fed has shown that food prices are increasingly behaving like other prices in the economy. Commodity prices are having less passthrough to food prices, and food prices are reacting more to labor market tightness and other factors that are common across many other prices in the economy.³

In summary, excluding food prices provides little additional understanding of inflation but comes at a cost. Although the Fed’s objective is headline inflation, discussing core inflation, and excluding food prices, can lead to communication challenges given the importance of food in the average household budget. While these communication challenges are not insurmountable,

³ See Cowley, Scott, Lusompa, Rodziewicz, and Dice; “[The Passthrough of Agricultural Commodity Prices to Food Prices](#).” Kansas City Fed Research Working Paper 24-16. December 2024. For factors driving food prices, see Scott, “[Commodity Prices Have Limited Influence on US Food Inflation](#).” Kansas City Fed *Economic Bulletin*. Sept. 23, 2022; and Scott and Kreitman, “[Tight Labor Markets Have Been a Key Contributor to High Food Inflation](#).” Kansas City Fed *Economic Bulletin*. April 19, 2023.

why invite them if there is little benefit to excluding food prices? My preference is to replace the current definition of core inflation with a measure of inflation excluding only energy prices.

Outlook

Now, I would like to turn to a discussion of the outlook coming out of last week's FOMC meeting. First, to level-set the discussion, my starting point when I think about the outlook and policy is the Fed's dual mandate for maximum employment and price stability. Congress has given the Fed its objectives and it is our job as monetary policy makers to use the tools available to us to achieve those objectives. Of course, the primary tool of the Fed is short-term interest rates, but by adjusting interest rates the Fed can affect the scarcity or abundance of liquidity in the economy, which in turn influences the pace of economic activity and the path of prices.

Currently we are as close to meeting our mandate as we have been in quite some time. In May, the 12-month inflation rate looks to be running just a touch above the Fed's 2 percent objective. This represents considerable progress relative to the 40-year highs that we were hitting just a couple of years ago. The spike in inflation that peaked in 2022 was importantly driven by imbalances in the economy that developed during the pandemic. The supply of goods was constrained by production and distribution bottlenecks. At the same time, demand was boosted by expansive fiscal policy that pushed up disposable income, improved household balance sheets, and encouraged spending. With demand exceeding supply, prices rose. Food prices experienced a similar pattern over this time with food inflation also reaching multi-decade highs in mid-2022.

Responding to these imbalances, the Fed rapidly tightened monetary policy, increasing short-term interest rates by 525 basis points. Higher rates helped ease demand growth as households responded to the incentive of greater interest returns by keeping their savings in the

bank or decreasing their demand for borrowing. At the same time, and helped by the easing in demand, supply conditions improved as pandemic-era disruptions faded. As imbalances in the economy closed, inflation eased.

An important contributor to this trajectory in prices were conditions on the other side of the Fed's mandate, the labor market. Disruptions to labor supply during the pandemic had led to a historically tight labor market, with the number of advertised jobs exceeding the number of unemployed job seekers by a ratio of over two to one. An important, though not always agreed-upon, point is that the labor market can in fact be too tight. By my eye, the tightness in the labor market in 2022 and 2023 contributed to the bottlenecks that pushed up prices. Also, a historic pace of labor market churn with workers rapidly switching jobs sent training costs skyrocketing and damaged productivity.

However, as in product markets, the imbalance in the labor market has closed. The ratio of job openings to jobseekers has returned to one-to-one, about where it was before the pandemic. The return to equilibrium in the labor market reflects an easing of demand, but also an improved supply of workers, especially as women returned to the labor force in historic numbers. All in all, the labor market now appears to be in a good place, with the unemployment rate at 4.2 percent, very close to many estimates of an equilibrium rate where labor market conditions are neither contributing to nor subtracting from inflation.

To summarize, in my view we are currently very near to meeting both sides of our mandate. However, monetary policy works with a considerable lag. Policy must be set not in relation to where the economy is as much as where the economy is going. This is never easy. And it is not easy now.

Many measures of economic uncertainty remain near historic highs, although they are down from two months ago. Speaking to contacts in the region, much of this uncertainty stems from changes in trade, fiscal, and other federal policies. And the uncertainty is not only over the course of these policies but also over their ultimate effect on the economy. Focusing on tariffs, contacts almost uniformly expect increased tariffs to push up prices and to weigh on activity, but with less agreement or conviction on the timing or ultimate magnitude of these effects. While it seems likely that the two sides of the Fed's mandate will come into conflict, there is far less clarity on when and by how much.

There are two reasons why it is difficult to know what the effect of higher tariffs will be. First is the size of the changes that are being discussed. We have no modern experience with such a significant change in trade policy. Many of the estimates that are being shared on the potential effects are calculated with models that are based on historical averages. The farther away from historical experience you get, the less faith you should have in these estimates.

Second, the pricing of each tariffed product is determined by the action and interaction of many different actors, from the foreign producer to the domestic importer, to the domestic supply chain and the retailers that ultimately deliver that product to the consumer. Which of these actors bears the cost of the tariff will be determined by a complex chain of negotiations that importantly will be affected by the availability and costs of substitutes along the entire path to the final consumer. This chain of interactions will vary for each product. Hence, it is almost impossible to anticipate exactly what the effect of tariffs will be on final consumption prices. Considering the additional complication that these decisions are likely to be dynamic and change over time, it becomes apparent that it is not only hard to know how prices will change but also when prices might change.

With all this uncertainty, the current posture of monetary policy, which has been characterized as “wait-and-see,” is appropriate. Certainly, with the inflation of the past couple of years still in people’s minds, I will be carefully watching the monthly price data for signs of broad-based price increases that might further challenge an already fragile price-setting psychology. The resilience of the economy gives us the time to observe how prices and the economy develop. Policy will need to remain nimble as the FOMC balances the two sides of its mandate.