

The Federal Reserve and Outlook for the Economy 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 having me today. I appreciate the opportunity to talk with you, and I look forward to our discussion. I will start with a few words about the Federal Reserve and what we do before turning to the outlook for the economy and monetary policy.

The Federal Reserve System

The Federal Reserve is America's central bank. It was established by an act of Congress in 1913. The structure of the system, with a seven-member Board of Governors in Washington, D.C., and 12 independent and geographically defined district banks across the country, owes much to the state of Oklahoma. Sen. Robert L. Owen, one of Oklahoma's first senators, sponsored the Federal Reserve Act.

Sen. Owen believed that the United States would be best served by a central bank directly engaged with communities across the United States. As such, the Act established a regional structure for the Federal Reserve, with each district bank serving its region and representing its geography in the national discussion of monetary policy. That is what we do at the Kansas City Fed. It is what we do from our office here in Oklahoma City, and what we do across our district's seven-state region of western Missouri, Kansas, Oklahoma, Nebraska, Colorado, Wyoming, and northern New Mexico. The regional structure of the Fed allows for voices across the nation to inform the setting of policy, and staff from our bank, including Oklahoma City Branch Executive Cortney Cowley, are in regular contact with business and community leaders throughout the district, collecting information and views that can be brought to the national conversation. For me, meetings such as this one are an opportunity to collect insights that I can bring to Washington, and I look forward to our conversation.

More generally, we should remember that much of the early support for the creation of Fed came from this region and in particular from farmers throughout the Midwest. Prior to the Fed, small agricultural lenders in the Midwest relied on large money center banks in New York and Chicago for credit. One common complaint was that the supply of liquidity provided by these large banks was inelastic, such that it did not flex to accommodate seasonal changes in credit demand.

By providing flexibility in the supply of liquidity, the Fed was able to meet the economy's needs and the farmers' demand for currency and credit, while providing more stability in interest rates and less financial volatility. Notably, the Fed, and the stability it provided, also underpinned the growth of the dollar as the central currency of global commerce.

But despite the impression of the headlines, the Fed is not only monetary policy. The Fed engages in monetary operations through the regional Reserve Banks, supervises financial institutions, acts as the Bank for the United States Treasury, and works to maintain the safety and security of the nation's payment system.

To focus on one of these areas, it would be hard to overstate the importance of a well-functioning, secure, and efficient payment system for the health of the overall economy. Payments are often compared to the circulatory system of the economy. They are the ledger that determines how decisions are made and how resources are allocated in a market economy. Payments can take many different forms, including cash, check and wire transfer; and the Fed plays a role in ensuring the security and efficiency of all of these. Fedwire, for example, transfers and processes more than \$4 trillion on average each business day.

Payments are also an area of tremendous innovation, both for the private sector and for the Federal Reserve. In 2023, the Fed introduced FedNow, a 24/7/365 instant payments system

and the Fed's first major new payment rail in over 40 years. FedNow aims to bring instant payments technology to all financial institutions, no matter their size or location, and has a multitude of uses that are just now being explored, including allowing employees to be paid daily, speeding the availability of funds to small businesses, and quickening the delivery of disaster-assistance payments.

Another aspect of payments where the Fed plays an essential role is in its interaction with the U.S. Treasury. As the Treasury's fiscal agent, the Fed is responsible for distributing payments to individuals throughout the economy, including Social Security and disaster relief payments.

In addition to maintaining the nation's payments infrastructure, a contingent of employees in our office in Oklahoma City as well as our offices in Kansas City, Denver, and Omaha are responsible for supervising financial institutions in the Tenth District and contributing to the health, strength and resilience of the country's financial system. A well-supervised banking system is in everyone's interest as it promotes the public trust that allows financial institutions of all sizes to flourish rather than just the largest and most well-known.

The Outlook for the Economy and Monetary Policy

Now, I would like to turn to the outlook for the economy and monetary policy. Overall, I am optimistic when it comes to the outlook for the United States. We have the strongest and most dynamic economy in the world. Our economy weathered the pandemic shock better than any of our international peers. Relative to the end of 2019, output—after taking into account inflation—has increased 13 percent. In comparison, the euro area grew only 6 percent over the same period, or half as much, and the United Kingdom and Japan were flatter still. Looking ahead,

technological change and increased labor productivity promise further strong growth in the years to come.

Currently, the economy continues to show strong momentum. Output bounced back in the spring after a dip at the start of the year, and consumption, the backbone of the U.S. economy, picked up as well. Speaking to business contacts across the 10th District, I am hearing increased optimism as some of the uncertainty and concern around trade policy that spiked in April recedes. Overall, my expectation is that the economy will show continued resilience.

Consumption will continue to benefit from growing disposable income, supported by both low unemployment and solid wage increases. Another support is the strength of household balance sheets. While certainly not true for all households, in the aggregate household net worth remains historically high.

What does this mean for monetary policy and interest rates? To set monetary policy the Fed is guided by its congressionally determined dual mandate of full employment and price stability. By my assessment, the Fed is as close to meeting its mandate as it has been for quite some time. The unemployment rate in July was 4.2 percent, very close to what many economic forecasters would estimate as the full employment rate. While it is true that payroll growth was weak over the summer, a broader set of indicators suggest a labor market that is in balance. The unemployment rate remains low, wage growth remains solid, and the ratio of reported job vacancies to available unemployed workers is about one-to-one, a matching that suggests a labor market close to balance.

With many different labor market indicators sometimes sending contradictory messages, the Kansas City Fed has created an index that combines the information from multiple series and

sources into a consolidated read on the health of the labor market.¹ By this comprehensive measure, the labor market, while cooling, remains in good health.

On the other side of the mandate, inflation remains too high. Over the 12 months ending in June, prices increased 2.6 percent, a pace above the Fed's 2 percent inflation objective, but far lower than the 7 percent-plus rate seen during the pandemic-related surge in inflation.

The design of the Federal Open Market Committee, with voices from the Board of Governors in Washington and the presidents of the regional Reserve Banks, supports a range of independent and diverse views. My own view, guided by the dual mandate, is that with the economy still showing momentum, growing business optimism, and inflation still stuck above our objective, retaining a modestly restrictive monetary policy stance remains appropriate for the time being. Though of course this is a position that I will continually reassess as we receive new data and information on inflation, the labor market, and the economy more generally.

My support for a patient approach to changing the policy rate is based on two connected arguments. First, while monetary policy might currently be restrictive, it is not very restrictive. And second, given recent price pressures, a modestly restrictive stance is exactly where we want to be.

Returning to the first point, how much is the current stance of policy restricting the economy? My assessment is not very much. As I said, we are as close to meeting our dual mandate objectives of price stability and full employment as we have been for quite some time. And while uncertainties abound, I do not see strong evidence of a trend movement away from our mandates at this point. This all suggests to me that the stance of monetary policy is not far

¹ The [Kansas City Fed's Labor Market Conditions Indicators](#), or LMCI, provide summary measures for the level of activity and momentum in the U.S. labor market based on 24 labor market variables.

from neutral. More generally, looking at financial markets, with stock prices near record highs and bond spreads near record lows, I see little evidence of a highly restrictive monetary policy.

Turning to my second point, I view a modestly restrictive policy stance as appropriate given the recent inflation data. While increased tariffs seem to be having a limited effect on inflation, I view this as a rationale for keeping policy on hold rather than an opportunity to ease the stance of policy.

From my perspective, the most important lesson of the pandemic inflation surge is that inflation should be discussed and analyzed in terms of the balance and imbalance of supply and demand rather than supply or demand independently. Let me be more specific. During the pandemic, disruptions in production, logistics, and the labor market impeded the supply of goods and services to the economy, while at the same time a historic fiscal transfer supercharged demand. When strong demand ran into weak supply, prices spiked and inflation climbed to a 40-year high in mid-2022. As supply recovered and demand growth slowed, partly in response to the Fed's aggressive tightening of monetary policy, imbalances in the economy eased and inflation fell back towards the Fed's 2 percent objective.

How does this experience inform my policy views now? Similar to the pandemic disruptions, the recent increase in tariffs has the prospect of pushing up the price of goods and services in the economy. With the lessons of the pandemic inflation in the background, my view is that the strength of demand will be absolutely central in determining how much of the increase in tariffs will eventually show up in inflation.

Currently, the relatively moderate pace of demand growth and the cooling labor market are working against the passthrough of tariffs to inflation. The current environment is one where aggressively boosting demand could raise the risk of an outsized increase in prices, as firms gain

pricing power and increase the passthrough of tariffs to consumers. During the pandemic it was often said that the Fed could not heal supply chains and bring down prices, and that was true. But it turned out what the Fed could do was moderate demand growth, provide the space for the economy to adjust, and eventually bring inflation down. Today, the Fed cannot offset the effect of higher tariffs on prices, but what the Fed can do is monitor demand growth, provide space for the economy to adjust, and keep inflation on a path to 2 percent. Overall, I am anticipating a relatively muted effect of tariffs on inflation, but I view that as a sign that policy is appropriately calibrated rather than a sign that the policy rate should be cut.

Importantly, I would not characterize my view on tariffs and inflation as “wait-and-see.” As I’ve said earlier this summer, I am not confident that we will ever be able to identify the exact (or even general) contribution of tariffs to inflation given the complexity of the problem. 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 an intricate 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.

While economic forecasting is notoriously difficult, I will confidently forecast that a decade from now economists will still be arguing over exactly what impact the tariffs had on

inflation. As such, I see no possibility that we will know the effect of the tariffs on prices, either as a one-off shock to the price level or a persistent inflation impetus, over the next few months. Also, I promise that you will not hear me talking about inflation excluding tariffs, which I think is neither a meaningful nor a measurable concept.²

Instead of puzzling over potential tariff effects, I intend to remain data dependent. In my view, and in discussion with my contacts, growth remains solid, inflation remains too high, and therefore policy should remain modestly restrictive. That said, as I stated earlier, inflation is determined by the balance of supply and demand, and if I see indications that demand growth is weakening significantly, I will adjust my views accordingly.

²More generally, I am not a big believer in speaking about inflation ex. anything, and I have been vocal in my opinion that economic commentators should stop excluding food prices from their discussion of inflation. See my remarks at the USDA's 2025 Agricultural Outlook Forum in Washington, D.C., "[Agriculture and the Federal Reserve](#)," Feb. 27, 2025. For related research on the topic of adding food inflation to measures of core inflation, 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.