For release on delivery
11:00 a.m. EST
November 20, 2024

Economic Outlook

Remarks by

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at the

University of Virginia

Charlottesville, Virginia

November 20, 2024

Thank you, Christa. It is wonderful to be with you here on the University of Virginia's beautiful campus. This is my first visit here as an adult. As a child, I was fortunate enough to be able to attend the commencement ceremony of my aunt and uncle, who received their doctoral degrees from UVA several decades ago. My family and I are grateful to the University of Virginia for all the educational opportunities it has afforded us over the years. I look forward to connecting with many of the exceptional students and faculty during my visit.[1]

As a member of the Federal Reserve Board, I always find it a pleasure to hear from people in communities across the country and to share some views of my own. At the Fed, I am committed to pursuing the best policy to achieve the dual-mandate goals given to us by Congress of maximum employment and price stability. Today, I would like to share with you my outlook for the economy, including some international comparisons of productivity and inflation, and offer my views on U.S. monetary policy.

Broadly, I view the economy as being in a good position. Inflation has substantially eased from its peak in mid-2022, though core inflation remains somewhat elevated. Unemployment remains historically low, but the labor market is no longer overheated. Economic growth has been robust this year, and I forecast the expansion will continue. Looking ahead, I remain confident that inflation is moving sustainably toward our 2 percent objective, even if the path is occasionally bumpy. Meanwhile, I see employment risks as weighted to the downside, but those risks appear to have diminished somewhat in recent months.

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[1] The views expressed here are my own and not necessarily those of my colleagues on the Federal Open Market Committee.

Inflation

Inflation, as measured by the personal consumption expenditures (PCE) price index, has eased notably from a peak of 7.2 percent in June 2022. Estimates based on the consumer price index and other data released last week indicate that total PCE prices rose 2.3 percent over the 12 months ending in October. Core PCE prices—which exclude the volatile food and energy categories—increased 2.8 percent, down from a peak of 5.6 percent in February 2022.

Despite this significant progress on disinflation, the elevated core figure suggests that we have further to go before credibly achieving our inflation target of 2 percent. Although most price indicators suggest that progress is ongoing, I anticipate bumps along the road. For instance, when measured on a monthly basis, estimated core PCE inflation stepped up in September and October after four months of lower readings. Even so, I still see headline and core inflation falling to 2.2 percent next year and to lower levels after that. Moreover, disinflation has been widespread across a broad range of goods and services. Taken together, recent data support my view that the disinflationary process is continuing.

Thinking of the components of inflation, core goods and core services inflation excluding housing are now at rates consistent with previous periods when inflation averaged about 2 percent. As a result, housing services account for most of the excess of core inflation over our target. Despite a slowing in rent increases for new tenants over the past two years, recent research from the Federal Reserve Bank of Cleveland suggests that existing rents for continuing tenants may still be notably below new tenant rent

levels.[2] Existing rents rising toward market rent levels is keeping housing services inflation temporarily elevated. My view is that housing services inflation will come down gradually over the next two years as the earlier slowing of growth in new tenant rent feeds through into the overall rate.

Recently, other inflation factors have been subdued. Core import prices have continued to step down from the surprisingly strong pace in the first half of the year. Global oil prices have fluctuated, largely in response to developments in the Middle East, but are back near the lows reached in late summer.

My confidence in continued disinflation is further reinforced by the moderation in wage growth. The employment cost index report showed that hourly compensation for private-sector workers rose at a 2.9 percent annual rate in the third quarter, the lowest since 2021. The 12-month change in average hourly earnings in October was 4 percent, down from 4.3 percent during the previous year. The wage premium for job switchers, a significant contributor to wage growth early in the pandemic recovery, has largely disappeared, according to data from the Federal Reserve Bank of Atlanta.

Labor Market

Turning to the labor market, on balance, recent data suggest that it remains solid. Monthly increases in firms' payrolls have slowed from earlier this year but are consistent with only a gradual cooling in the labor market. The October employment report did

[2] See Lara Loewenstein, Jason Meyer, and Randal J. Verbrugge (2024), "New-Tenant Rent Passthrough and the Future of Rent Inflation," Economic Commentary 2024-17 (Cleveland: Federal Reserve Bank of Cleveland, October), https://www.clevelandfed.org/publications/economic-commentary/2024/ec-202417-new-tenant-rent-passthrough-and-future-of-rent-inflation.

show a sharp slowdown in job creation, but that was largely due to the temporary effects of recent hurricanes and a labor strike.

While economists and forecasters often focus on aggregate data for the national economy, it is important to acknowledge that hurricanes Helene and Milton resulted in the tragic loss of life and devastating destruction in many parts of the country, including some here in the state of Virginia. My thoughts remain with those affected communities. The Federal Reserve System remains in touch with these communities to help the financial institutions that serve them in any way we can.[3]

The broader trend I see is that national job growth is solid but perhaps not quite strong enough to keep unemployment at the current low rate. Net hiring so far this year is running somewhat below estimates for what economists call the breakeven pace, or the rate of hiring needed to keep the unemployment rate constant, when accounting for changes to the size of the labor force. With job growth coming in below the breakeven pace, which was likely more than 200,000 jobs a month over the past year, the unemployment rate has risen from a historical low of 3.4 percent in April 2023 to 4.1 percent in October.

Other data are also consistent with a gradual cooling in labor demand. The vacancies-to-unemployment ratio has fallen from a peak of 2.0 in 2022 to 1.1 in

[3] See Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of the Currency, and State Financial Regulators (2024), "Federal and State Financial Regulatory Agencies Issue Interagency Statement on Supervisory Practices regarding Financial Institutions Affected by Hurricane Helene," joint press release, October 2, https://www.federalreserve.gov/newsevents/pressreleases/other20241002a.htm. See also Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Florida Office of Financial Regulation, National Credit Union Administration, and Office of the Comptroller of the Currency (2024), "Federal and State Financial Regulatory Agencies Issue Interagency Statement on Supervisory Practices regarding Financial Institutions Affected by Hurricane Milton," joint press release, October 15, https://www.federalreserve.gov/newsevents/pressreleases/other20241015a.htm.

September, slightly below where it stood just before the pandemic. The rate at which workers are quitting their jobs continued to slide in recent months to well below its pre-pandemic level, which could indicate that workers are less optimistic about finding a better job should they leave their current role. Notably, firms' hiring rates and hiring plans remain subdued, while workers report reduced availability of jobs. Although layoffs remain low, less hiring makes it harder for labor market entrants and reentrants to find jobs. Also, our contacts report that employers are being more selective, waiting to find workers with the skills they seek, rather than pursuing a hire-and-train strategy.

Overall, I see a labor market that has largely normalized after being overheated because of pandemic disruptions and dislocations. The labor market is in a good position—with the supply and demand for workers being roughly in balance—such that it is no longer a source of inflationary pressure in the economy. I will continue to watch incoming data carefully and remain attuned to signs of undesirable further cooling in the labor market.

Economic Output and Productivity Growth

Along with generally solid labor market data and moderating inflation, recent indicators show economic activity moving along at a strong pace. Real gross domestic product (GDP) increased at a 2.8 percent annual rate in the third quarter, consistent with the solid growth recorded in the first half of the year.

American consumers remain resilient, with broad-based gains in household spending on both goods and services. This supports broader economic growth because consumer spending constitutes roughly two-thirds of GDP. Spending at retailers and restaurants rose 2.8 percent in October from a year earlier, a faster 12-month rate of

increase than the prior two months. Recent data revisions show that household income and savings have been higher than previously thought, improving the outlook for consumer spending and GDP growth.

It is remarkable that the U.S. economy has been growing rapidly even as inflation has been declining significantly over the past two years. One reason why this solid growth could be occurring is that potential growth, or the maximum rate at which an economy can grow without causing inflation over the medium term, may have increased.

One factor that appears to have supported both potential and actual growth is a faster pace of productivity gains. Recent data indicate labor productivity has grown at a 1.8 percent annual rate since the end of 2019, surpassing its 1.5 percent growth rate over the previous 12 years. Several forces could have boosted productivity in recent years. As I discussed in a recent speech in South Carolina, the U.S. experienced a surge in new business formation since the start of the pandemic.[4] These newer firms are more likely to innovate and adopt new technologies and business processes, thus boosting productivity.

Two other factors boosting productivity relate in part to changes in the U.S. economy during and after the pandemic. Worker reallocation across jobs and locations surged early in the pandemic and remained high for some time. There is some research suggesting that such reallocation resulted in better and more productive matches between some workers and jobs, thus raising labor productivity.[5] At the same time, severe labor shortages during the post-pandemic recovery spurred many businesses to invest in labor-

[4] Lisa D. Cook (2024), "Entrepreneurs, Innovation, and Participation," speech delivered at the 2024 Women for Women Summit, Charleston, S.C., October 10, https://www.federalreserve.gov/newsevents/speech/cook20241010a.htm.

[5] See David Autor, Arindrajit Dube, and Annie McGrew (2023), "The Unexpected Compression: Competition at Work in the Low Wage Labor Market," NBER Working Paper Series 31010 (Cambridge, Mass.: National Bureau of Economic Research, March; revised May 2024), https://www.nber.org/papers/w31010.

saving technologies and to restructure aspects of production more efficiently, which may also have given at least a one-time boost to productivity.

More broadly, the continued sizable investment in new technologies may promote ongoing strength in productivity growth. Much of this investment has gone toward artificial intelligence (AI), which has the potential to transform many aspects of the economy and job market, as I discussed in speeches earlier this fall.[6,7]

International Comparisons

Compared with productivity abroad, recent U.S. productivity growth looks quite exceptional. As shown in figure 1, before the pandemic, the U.S. had faster productivity growth—as shown by the green portion of the bars—than other advanced economies, but the difference was small. Since the pandemic, however, U.S. productivity growth has far exceeded that of Europe, Canada, and Australia, as shown in figure 2. To explain this notable outperformance, some have highlighted our country's relatively flexible labor market and greater business dynamism compared with these other economies.[8] Moreover, to the extent that investment in technology has been a driver of cross-country differences, it is notable that private investment in AI has been much higher in the U.S. than abroad.[9]

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[6] See Lisa D. Cook, "Artificial Intelligence, Big Data, and the Path Ahead for Productivity," speech delivered at "Technology-Enabled Disruption: Implications of AI, Big Data, and Remote Work," a conference organized by the Federal Reserve Banks of Atlanta, Boston, and Richmond, Atlanta, Georgia, held in Atlanta, Ga., October 1, https://www.federalreserve.gov/newsevents/speech/cook20241001a.htm.
[7] See Lisa D. Cook, "What Will Artificial Intelligence Mean for America's Workers?" speech delivered at The Ohio State University, Columbus, Ohio, September 26, https://www.federalreserve.gov/newsevents/speech/cook20240926a.htm.
[8] See François de Soyres, Joaquin Garcia-Cabo Herrero, Nils Goernemann, Sharon Jeon, Grace Lofstrom, and Dylan Moore (2024), "Why is the U.S. GDP Recovering Faster than other Advanced Economies?" FEDS Notes (Washington: Board of Governors of the Federal Reserve System, May 17), https://doi.org/10.17016/2380-7172.3495.
[9] See Chirag Chopra, Ankit Kasare, and Piyush Gupta (2024), "How Venture Capital is Investing in AI in the Top Five Global Economies—and Shaping the AI Ecosystem," *World Economic Forum,* May 24.

This productivity outperformance is likely a main reason why U.S. GDP growth has been stronger than that of foreign economies; the path of inflation, however, has largely been similar across the globe. As shown in figure 3, inflation in the U.S. and abroad rose sharply in 2021 and 2022, amid supply bottlenecks and a post-pandemic recovery in demand. Inflation reached a higher peak in European economies that were most directly affected by the energy price shock from Russia's war in Ukraine. Inflation has since declined globally as supply normalized and monetary policy tightening restrained demand. U.S. inflation, as shown by the black line, is nearly back to its 2 percent target level, while core inflation, as shown in figure 4, has come down but remains somewhat above 2 percent.

Monetary Policy

As I stated, the totality of the data suggests that a disinflationary trajectory is still in place and that the labor market is gradually cooling. As such, I view the risks to achieving the Federal Reserve's dual mandate of maximum employment and price stability as being roughly in balance. Consistent with those balanced risks, in my view, it likely will be appropriate to move the policy rate toward a more neutral stance over time.

My colleagues on the Federal Open Market Committee and I acted earlier this month to lower the target range for the federal funds rate by 1/4 percentage point. That action came after we reduced the rate by 1/2 percentage point in September. Together, these moves were a strong step toward removing policy restriction.

Going forward, I still see the direction of the appropriate policy rate path to be downward, but the magnitude and timing of rate cuts will depend on incoming data, the evolving outlook, and the balance of risks. I do not view policy as being on a preset

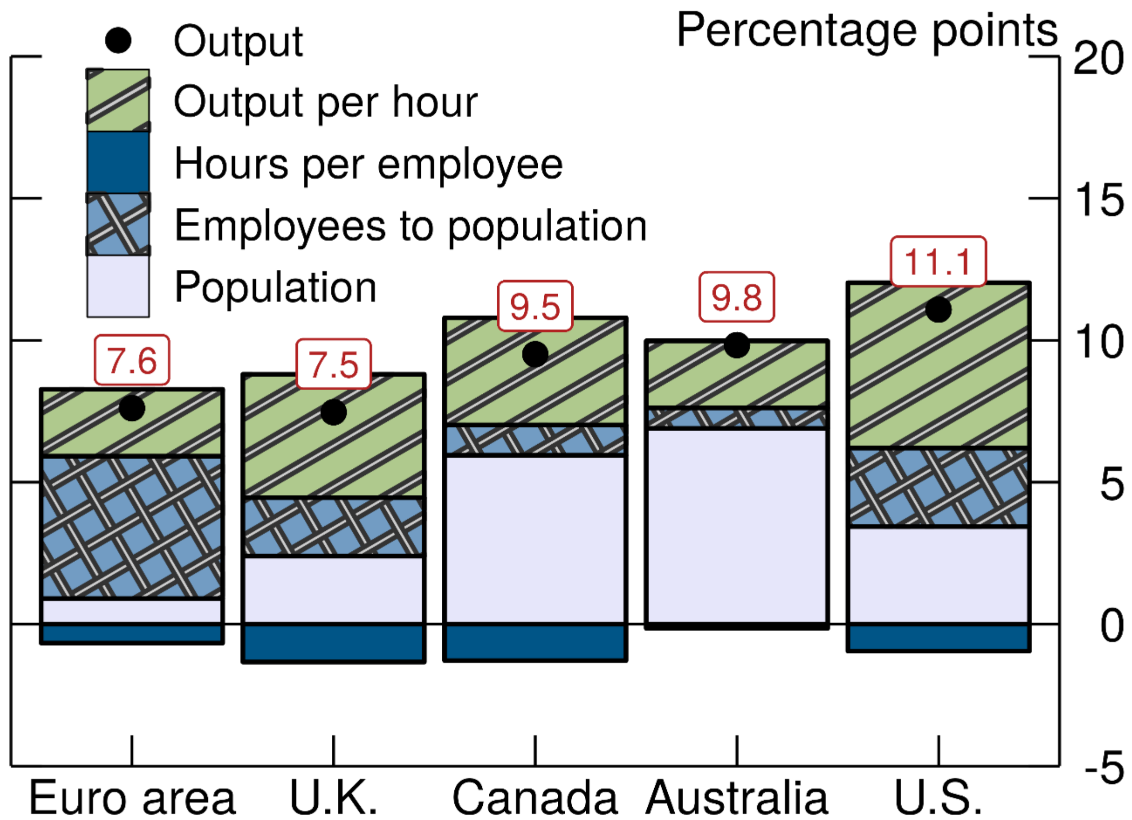
course, and I am ready to respond to a changing outlook. In fact, I find it helpful to consider a range of scenarios when thinking about the path of policy.

If the labor market and inflation continue to progress in line with my forecast, it could well be appropriate to lower the level of policy restriction over time until we near the neutral rate of interest, or the point when monetary policy is neither stimulating nor restricting economic growth. However, if inflation progress slows and the labor market remains solid, I could see a scenario where we pause along the downward path. Alternatively, should the labor market weaken in a substantial way, it could be appropriate to ease policy more quickly.

My policy decisions will be guided by our dual mandate of maximum employment and stable prices, and I know delivering on those goals will produce the best economic outcomes for all Americans.

Thank you for having me here today. I look forward to your questions.

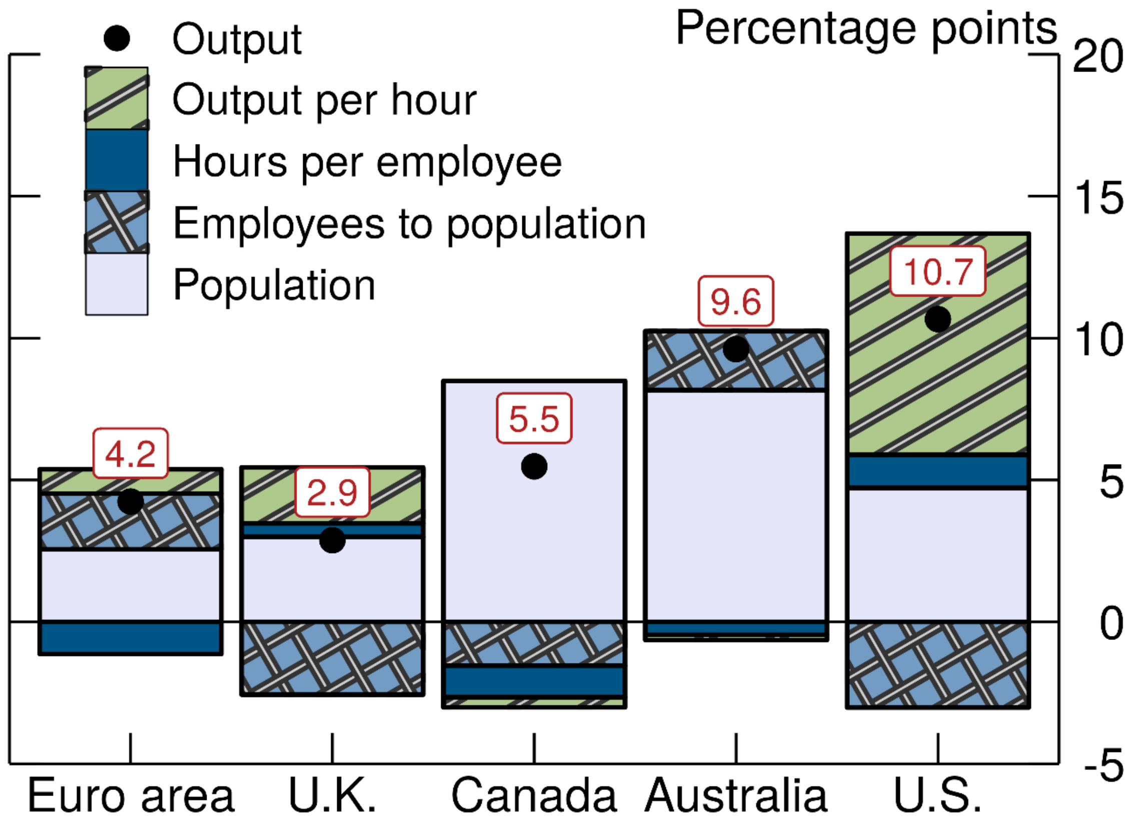
Contribution to Cumulative GDP Growth from 2015:Q4 to 2019:Q4



Note: GDP is gross domestic product. Output per hour is GDP divided by total hours worked. Hours per employee is the total number of hours worked divided by employment. Employment and population includes those aged 15 years or older in Australia, Canada, and the euro area and those aged 16 years or older in the U.K. and the U.S.

Source: Haver Analytics; Federal Reserve Board staff calculations.

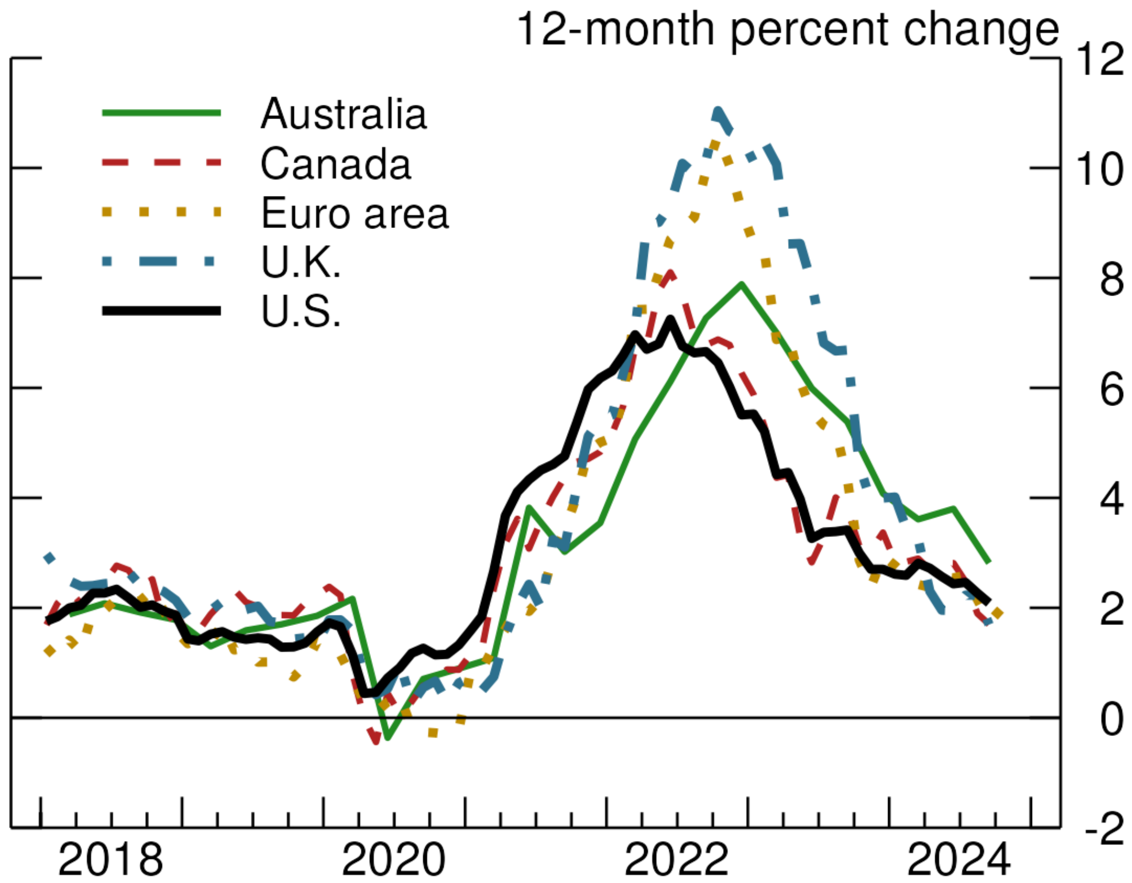
Contribution to Cumulative GDP Growth from 2019:Q4 to 2024:Q2



Note: GDP is gross domestic product. Output per hour is GDP divided by total hours worked. Hours per employee is the total number of hours worked divided by employment. Employment and population include those aged 15 years or older in Australia, Canada, and the euro area and those aged 16 years or older in the U.K. and the U.S.

Source: Haver Analytics; Federal Reserve Board staff calculations.

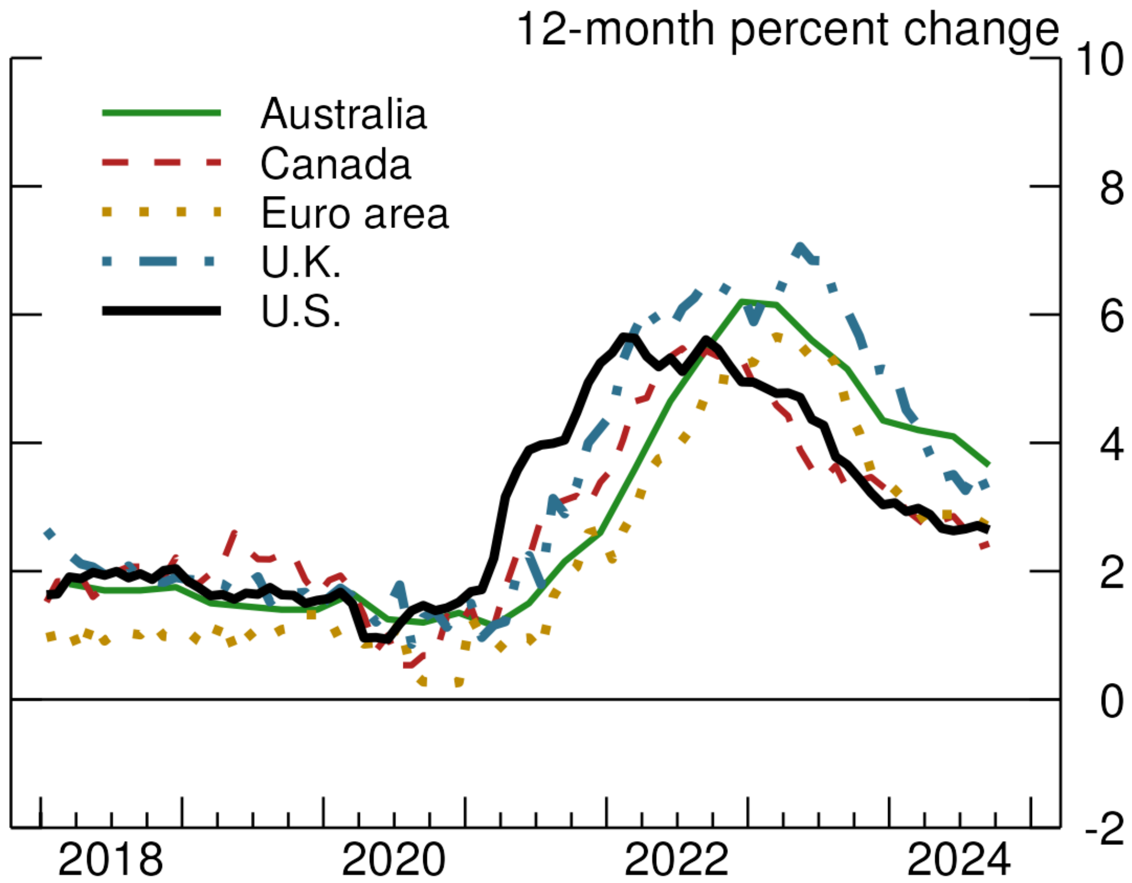
Headline Inflation



Note: Data are quarterly for Australia and monthly for all other economies. Data extend through the third quarter for Australia, October for the euro area, and September for the U.K., the U.S., and Canada.

Source: Haver Analytics; Federal Reserve Board staff calculations.

Core Inflation



Note: Data are quarterly for Australia and monthly for all other economies. Data extend through the third quarter for Australia, October for the euro area, and September for the U.K., the U.S., and Canada.

Source: Haver Analytics; Federal Reserve Board staff calculations.