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Statement by

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Chairman

Board of Governors of the Federal Reserve System

before the

Committee on Banking, Housing, and Urban Affairs

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Good morning. Chairman Crapo, Ranking Member Brown, and other members of the Committee, I am happy to present the Federal Reserve's semiannual *Monetary Policy Report* to the Congress.

Let me start by saying that my colleagues and I strongly support the goals Congress has set for monetary policy--maximum employment and price stability. We are committed to providing transparency about the Federal Reserve's policies and programs. Congress has entrusted us with an important degree of independence so that we can pursue our mandate without concern for short-term political considerations. We appreciate that our independence brings with it the need to provide transparency so that Americans and their representatives in Congress understand our policy actions and can hold us accountable. We are always grateful for opportunities, such as today's hearing, to demonstrate the Fed's deep commitment to transparency and accountability.

Today I will review the current economic situation and outlook before turning to monetary policy. I will also describe several recent improvements to our communications practices to enhance our transparency.

Current Economic Situation and Outlook

The economy grew at a strong pace, on balance, last year, and employment and inflation remain close to the Federal Reserve's statutory goals of maximum employment and stable prices--our dual mandate.

Based on the available data, we estimate that gross domestic product (GDP) rose a little less than 3 percent last year following a 2.5 percent increase in 2017. Last year's growth was led by strong gains in consumer spending and increases in business investment. Growth was supported by increases in employment and wages, optimism among households and businesses,

and fiscal policy actions. In the last couple of months, some data have softened but still point to spending gains this quarter. While the partial government shutdown created significant hardship for government workers and many others, the negative effects on the economy are expected to be fairly modest and to largely unwind over the next several months.

The job market remains strong. Monthly job gains averaged 223,000 in 2018, and payrolls increased an additional 304,000 in January. The unemployment rate stood at 4 percent in January, a very low level by historical standards, and job openings remain abundant. Moreover, the ample availability of job opportunities appears to have encouraged some people to join the workforce and some who otherwise might have left to remain in it. As a result, the labor force participation rate for people in their prime working years--the share of people ages 25 to 54 who are either working or looking for work--has continued to increase over the past year. In another welcome development, we are seeing signs of stronger wage growth.

The job market gains in recent years have benefited a wide range of families and individuals. Indeed, recent wage gains have been strongest for lower-skilled workers. That said, disparities persist across various groups of workers and different parts of the country. For example, unemployment rates for African Americans and Hispanics are still well above the jobless rates for whites and Asians. Likewise, the percentage of the population with a job is noticeably lower in rural communities than in urban areas, and that gap has widened over the past decade. The February *Monetary Policy Report* provides additional information on employment disparities between rural and urban areas.

Overall consumer price inflation, as measured by the 12-month change in the price index for personal consumption expenditures (PCE), is estimated to have been 1.7 percent in December, held down by recent declines in energy prices. Core PCE inflation, which excludes

food and energy prices and tends to be a better indicator of future inflation, is estimated at 1.9 percent. At our January meeting, my colleagues and I generally expected economic activity to expand at a solid pace, albeit somewhat slower than in 2018, and the job market to remain strong. Recent declines in energy prices will likely push headline inflation further below the Federal Open Market Committee's (FOMC) longer-run goal of 2 percent for a time, but aside from those transitory effects, we expect that inflation will run close to 2 percent.

While we view current economic conditions as healthy and the economic outlook as favorable, over the past few months we have seen some crosscurrents and conflicting signals. Financial markets became more volatile toward year-end, and financial conditions are now less supportive of growth than they were earlier last year. Growth has slowed in some major foreign economies, particularly China and Europe. And uncertainty is elevated around several unresolved government policy issues, including Brexit and ongoing trade negotiations. We will carefully monitor these issues as they evolve.

In addition, our nation faces important longer-run challenges. For example, productivity growth, which is what drives rising real wages and living standards over the longer term, has been too low. Likewise, in contrast to 25 years ago, labor force participation among prime-age men and women is now lower in the United States than in most other advanced economies. Other longer-run trends, such as relatively stagnant incomes for many families and a lack of upward economic mobility among people with lower incomes, also remain important challenges. And it is widely agreed that federal government debt is on an unsustainable path. As a nation, addressing these pressing issues could contribute greatly to the longer-run health and vitality of the U.S. economy.

Monetary Policy

Over the second half of 2018, as the labor market kept strengthening and economic activity continued to expand strongly, the FOMC gradually moved interest rates toward levels that are more normal for a healthy economy. Specifically, at our September and December meetings we decided to raise the target range for the federal funds rate by 1/4 percentage point at each, putting the current range at 2-1/4 to 2-1/2 percent.

At our December meeting, we stressed that the extent and timing of any further rate increases would depend on incoming data and the evolving outlook. We also noted that we would be paying close attention to global economic and financial developments and assessing their implications for the outlook. In January, with inflation pressures muted, the FOMC determined that the cumulative effects of these developments, along with ongoing government policy uncertainty, warranted taking a patient approach with regard to future policy changes. Going forward, our policy decisions will continue to be data dependent and will take into account new information as economic conditions and the outlook evolve.

For guideposts on appropriate policy, the FOMC routinely looks at monetary policy rules that recommend a level for the federal funds rate based on measures of inflation and the cyclical position of the U.S. economy. The February *Monetary Policy Report* gives an update on monetary policy rules. I continue to find these rules to be helpful benchmarks, but, of course, no simple rule can adequately capture the full range of factors the Committee must assess in conducting policy. We do, however, conduct monetary policy in a systematic manner to promote our long-run goals of maximum employment and stable prices. As part of this approach, we strive to communicate clearly about our monetary policy decisions.

We have also continued to gradually shrink the size of our balance sheet by reducing our holdings of Treasury and agency securities. The Federal Reserve's total assets declined about \$310 billion since the middle of last year and currently stand at close to \$4.0 trillion. Relative to their peak level in 2014, banks' reserve balances with the Federal Reserve have declined by around \$1.2 trillion, a drop of more than 40 percent.

In light of the substantial progress we have made in reducing reserves, and after extensive deliberations, the Committee decided at our January meeting to continue over the longer run to implement policy with our current operating procedure. That is, we will continue to use our administered rates to control the policy rate, with an ample supply of reserves so that active management of reserves is not required. Having made this decision, the Committee can now evaluate the appropriate timing and approach for the end of balance sheet runoff. I would note that we are prepared to adjust any of the details for completing balance sheet normalization in light of economic and financial developments. In the longer run, the size of the balance sheet will be determined by the demand for Federal Reserve liabilities such as currency and bank reserves. The February *Monetary Policy Report* describes these liabilities and reviews the factors that influence their size over the longer run.

I will conclude by mentioning some further progress we have made in improving transparency. Late last year we launched two new publications: The first, *Financial Stability Report*, shares our assessment of the resilience of the U.S. financial system, and the second, *Supervision and Regulation Report*, provides information about our activities as a bank supervisor and regulator. Last month we began conducting press conferences after every FOMC meeting instead of every other one. The change will allow me to more fully and more frequently explain the Committee's thinking. Last November we announced a plan to conduct a

comprehensive review of the strategies, tools, and communications practices we use to pursue our congressionally assigned goals for monetary policy. This review will include outreach to a broad range of stakeholders across the country. The February *Monetary Policy Report* provides further discussion of these initiatives.

Thank you. I am happy to respond to questions.