

For release on delivery  
6:00 a.m. EDT (1:00 p.m. local time)  
September 30, 2025

Monetary Policy Frameworks and the U.S. Economic Outlook

Remarks by

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at

“Monetary Policy in the Shadow of Geopolitical Tensions and Trade Conflicts,” the  
fourth International Monetary Policy Conference hosted by the Bank of Finland

Helsinki, Finland

September 30, 2025

Thank you, Governor Olli Rehn, for the invitation to visit the lovely city of Helsinki and participate in the Bank of Finland's International Monetary Policy Conference.<sup>1</sup> I highly value the opportunity to interact with, and learn from, my fellow central bankers, so thank you again for having me.

When considering the Bank of Finland, the European Central Bank (ECB), and the Federal Reserve in the U.S., it is easy to point out some differences, including our mandates and our economies. But there are also important similarities across these central banks. As independent central banks, our objective is to set policy that will result in the best outcomes for the people we each serve. Another similarity, and one I would like to focus on today, is that both the ECB and the Fed see value in establishing and clearly articulating to the public a framework on how we each approach monetary policymaking. And, in fact, both the ECB and the Fed published revisions to our individual framework documents earlier this year. Such revisions lead to more robust frameworks that help support the mission of central banks across a broad range of economic conditions, including those that are also shaped by geopolitical tensions and trade conflicts, as is the theme of this conference.

Today, I will briefly review some consistent themes that emerged from the two revised documents. Then, I will discuss in more depth the changes to the Fed's Statement on Longer-Run Goals and Monetary Policy Strategy, which Chair Powell announced in his Jackson Hole speech in August. Finally, I will offer my views on the economic outlook and its implications for U.S. monetary policy.

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<sup>1</sup> The views expressed here are my own and are not necessarily those of my colleagues on the Federal Reserve Board or the Federal Open Market Committee.

## **Consistent Themes**

Understanding the work of other central banks and speaking with their policymakers is a healthy exercise. This is particularly true when studying other banks' overarching frameworks. The ECB's Monetary Policy Strategy Statement dates to the central bank's founding in 1998. The Fed is quite a bit older, but it still took us longer to offer a formal framework to the public. The Fed's Statement on Longer-Run Goals and Monetary Policy Strategy was first issued in 2012, under Chair Ben Bernanke's leadership. At the time, Fed leaders took note that other peer central banks issued public statements of their frameworks and saw value in doing so. While the two documents differ in length and touch on some slightly different topics, reflecting each bank's unique mandate, there are several similarities. One is that the governing bodies of both the ECB and the Fed target 2 percent inflation. Another is that they both have a commitment to revisiting and revising their framework periodically. Also, both revised documents de-emphasized their previous focus on operating near the effective lower bound (ELB) of interest rates in favor of considering a broad range of economic circumstances.

Overall, both documents describe the central bank's understanding of its monetary policy mandates and its broad approach to achieving them. However, neither is a mandatory policy prescription. Indeed, each framework provides a structure within which its respective policymakers can develop their individual policy views. That is a good thing. It is a sign of a healthy, independent central bank. Robust discussions where alternative viewpoints are considered are more likely to lead to effective policies and better outcomes for the people we serve.

## **The Fed's Revised Framework**

Now, let me turn specifically to the framework document my Federal Open Market Committee (FOMC) colleagues and I finished revising in August. The Fed's dual mandate to foster maximum employment and stable prices, which was given to us by the U.S. Congress, underpins the Fed's monetary policy framework. Our commitment to delivering on our dual mandate is unwavering. The revisions to our framework will support that mission across a broad range of economic conditions.

We often refer to the framework document as the "consensus statement." We call it that because it reflects the consensus view of the FOMC—and because having a nine-word title for a two-page document is a bit verbose!

The FOMC created the revised consensus statement after conducting a public review, the second time the Committee has done so. That review consisted of three elements: first, we held *Fed Listens* events around the U.S., where members of the public could share their views with policymakers; second, we hosted an academic research conference that featured presentations from leading experts, including former Chair Bernanke; and third, we convened a series of policymaker discussions and deliberations at FOMC meetings this year, supported by staff analysis.

The statement is designed to give the public a clear sense of how we think about monetary policy, and that understanding is important both for transparency and accountability, and for making monetary policy more effective. The changes implemented as a result of this review were a logical progression, not a change in course, grounded in our ever-evolving understanding of our economy. I will make note of four adjustments to the consensus statement and discuss each in turn.

First, the revised consensus statement removed language emphasizing the ELB as a defining feature of the economic landscape. Instead, it states that our monetary policy strategy is designed to promote maximum employment and stable prices across a broad range of economic conditions. This revision, reflecting a move away from the post-financial crisis era of historically low interest rates, makes our framework more robust. It is useful to recall that at the time of the FOMC's previous framework review, during 2019 and 2020, policymakers were considering an economy that had for many years demonstrated low growth, low inflation, and a very flat Phillips curve—meaning that inflation was not very responsive to slack in the economy. The overarching concern for central bankers at that time was how to operate with interest rates near the ELB. Today, of course, we are operating in a very different environment, at least in part brought on by the economic consequences of the COVID-19 pandemic.

Second, the revised framework embraces a flexible inflation-targeting approach at all times and eliminates a “makeup” strategy that would be employed in certain circumstances. The experience since the pandemic highlights different challenges to achieving our inflation mandate, such as supply shocks, sectoral developments, and nonlinear inflation dynamics. The flexible inflation targeting in our revised framework allows us to take a balanced approach in promoting our goals, considering the extent of departures from them. The revised framework appropriately emphasizes the Committee's commitment to ensuring that longer-term inflation expectations remain well anchored.

Third, the revised consensus statement provides clarity around how the Committee thinks about maximum employment. The 2020 version of the statement

indicated that the Fed would mitigate “shortfalls” from maximum employment. The shortfalls strategy grew out of the insight that real-time assessments of the natural rate of unemployment—and hence of “maximum employment”—are highly uncertain. However, the use of the word “shortfalls” created some communications challenges, as it was not intended to be a commitment to always avoid preemption or to ignore tight labor market conditions. As a result, it was removed from the consensus statement. Instead, the revised document more precisely states that “the Committee recognizes that employment may at times run above real-time assessments of maximum employment without necessarily creating risks to price stability.”<sup>2</sup> As Chair Powell pointed out, preemptive action could well be warranted if tightness in the labor market or other factors pose risks to price stability. The revised statement defines maximum employment as “the highest level of employment that can be achieved on a sustained basis in a context of price stability.”<sup>3</sup>

Fourth, and closely aligned with the change I just discussed, the FOMC clarified its approach to monetary policy in times when the employment and inflation sides of our mandate may be at odds. The revised statement says that, in such periods, the Committee will follow “a balanced approach in promoting them, taking into account the extent of departures from its goals and the potentially different time horizons over which employment and inflation are projected to return to levels judged consistent with its mandate.” The revised language more closely aligns with the original 2012 statement. It

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<sup>2</sup> The consensus statement is available on the Federal Reserve Board’s website at <https://www.federalreserve.gov/monetarypolicy/monetary-policy-strategy-tools-and-communications-statement-on-longer-run-goals-monetary-policy-strategy-2025.htm>.

<sup>3</sup> See note 2 for the Fed’s consensus statement.

is also consistent with the Committee's actions during the 2022–24 period, when the departure from our 2 percent inflation target was the overriding concern.

While I have highlighted multiple changes, it is also important to note the continuity with the Fed's past framework statements. The document continues to explain how we interpret the mandate Congress has given us and describes the policy framework that we believe will best promote maximum employment and price stability. We also continue to believe that monetary policy must be forward looking and consider the lags in its effects on the economy. We have never set a numerical goal for employment because the maximum level of employment is not directly measurable and changes over time for reasons unrelated to policy. Likewise, we maintained our commitment to a 2 percent inflation objective because that is a key factor helping keep longer-term inflation expectations well anchored. And we remain committed to conducting a public review roughly every five years.

While the framework provides a structure through which to think about policy decisions, I will continue to determine the appropriate stance of monetary policy based on the incoming data, the evolving outlook, and the balance of risks. Consistent with such a determination, I would like to share with you my current outlook for the U.S. economy.

## **Economic Outlook**

Recent data indicate that U.S. economic growth has moderated, and the risks to both sides of our dual mandate have shifted. Employment growth has slowed because of weaker growth in labor supply and a softening in labor demand. The uptick in the unemployment rate suggests that demand has fallen by a bit more than supply and that

the downside risks to employment are rising. Meanwhile, higher tariffs are showing through to higher inflation for some goods. I expect that the effects of tariffs on inflation, employment, and economic activity will further show through in coming months.

The softening of labor market activity comes as overall economic activity has moderated this year. In the first half of 2025, U.S. GDP grew at about a 1.5 percent annual rate, which reflects a marked cooling from last year's 2.5 percent growth rate. The slowdown in economic activity in the first half of this year was primarily driven by weaker consumer spending. That said, U.S. retail spending picked up over the summer. Overall, I expect the U.S. economy to maintain the first half's rate of growth through the remainder of the year.

In terms of the labor market, there has been notable slowing in both labor supply and labor demand. Net immigration into the U.S., an important contributor to workforce growth, has dropped sharply. At the same time, total employment growth has slowed. Over the past three months, American employers have added just 29,000 jobs to payrolls a month on average. The recent pace of employment growth has been the slowest since the U.S. economy recovered from the COVID-19 pandemic recession, which is largely explained by the slower growth in the labor force. There are other measures of the labor market that also bear watching. For example, the ratio of unfilled jobs to unemployed Americans seeking work remains near 1. And measures of job openings and initial jobless claims have been mostly moving sideways.

A low level of job creation would historically put upward pressure on the unemployment rate, though so far that effect has been muted because of the decline in labor force growth. The U.S. unemployment rate in August was 4.3 percent, a still



relatively low rate, and up just 0.1 percentage point from August of the previous year. The unemployment rate could edge a bit higher this year before moving back down next year.

Turning to the other side of our dual mandate, it remains notable that inflation has slowed considerably from the highs that occurred when the economy reopened after pandemic disruptions. Inflation, however, remains somewhat above our 2 percent target, and the tariffs that have been announced and implemented so far are showing up in some goods prices. Overall, personal consumption expenditures (PCE) prices rose 2.7 percent over the 12 months ending in August. Core PCE inflation—which removes volatile food and energy prices—was 2.9 percent in August. Often, it is helpful to study the three major components of core PCE inflation. Currently, core goods prices have been rising, reflecting tariff effects. In contrast, core services inflation, outside of housing, has generally trended sideways this year, while housing inflation appears to be on a gradual downward trend.

I view the uncertainty around my baseline outlook as especially high, mainly due to the new policies being introduced by the current U.S. Administration and their effects on employment and inflation. As the changes in these policies are finalized and we have more time to judge how they are affecting the economy, I expect some of the broader uncertainty around the U.S. economy to diminish.

## **Monetary Policy**

Considering the outlook I described, I see the risks to employment as tilted to the downside and risks to inflation to the upside. It follows that both sides of our mandate are under pressure.

While tariff-related inflation is apparent in the prices of some goods, it is also notable that it so far has been lower than what many forecasters predicted this spring. Several factors—including the final tariff rates, the extent of pass-through to consumer prices, the effects on supply chains, overall economic conditions, and what happens to longer-run inflation expectations—will influence the scope and persistence of the related rise in inflation. Short-term inflation expectations have come down from the peaks reached in the second quarter, and most measures of longer-run inflation expectations have been largely stable, suggesting that the American people understand our commitment to returning inflation to our 2 percent target. As such, I expect the disinflation process to resume after this year and inflation to return to the 2 percent target in the coming years.

With the unemployment rate at 4.3 percent, the labor market is softening, which suggests that, left unsupported, it could experience stress. To balance the risk of persistent above-target inflation and the risk of a deteriorating labor market, I supported a 25 basis point cut in our target range at the last FOMC meeting. This change moved our policy rate closer to a more neutral stance while maintaining a balanced approach to promoting our dual-mandate objectives.

With respect to the path of the policy rate going forward, I will continue to evaluate the appropriate stance of monetary policy based on the incoming data, the

evolving outlook, and the balance of risks. I will also consider and assess information about government policies and their effects on the economy.

## **Conclusion**

In this room, I know that I am not alone in putting careful thought and attention into what should be the proper path of monetary policy moving forward. I have found the Fed's consensus statement to be a valuable tool in helping me organize my thinking and take a grounded approach to policymaking. I know that similar documents at your central banks also provide wise counsel to pursue your mandates.

Thank you again for the invitation to speak here and for allowing me to engage in the sharing of ideas.



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## Road Map of Talk

- Consistent Themes from Central Bank Framework Reviews
- Federal Reserve's Statement on Longer-Run Goals and Monetary Policy Strategy
- Views on Economic Outlook
- Conclusion



## Statement on Longer-Run Goals and Monetary Policy Strategy

*“The Committee’s monetary policy strategy is designed to promote maximum employment and stable prices across a broad range of economic conditions.”*

Source: Federal Reserve Board



## Four Adjustments

- A shift away from a focus on the effective lower bound
- Embraces flexible inflation targeting at all times
- A refinement of how we consider maximum employment
- Clarity on how we approach periods when employment and inflation objectives are not complementary



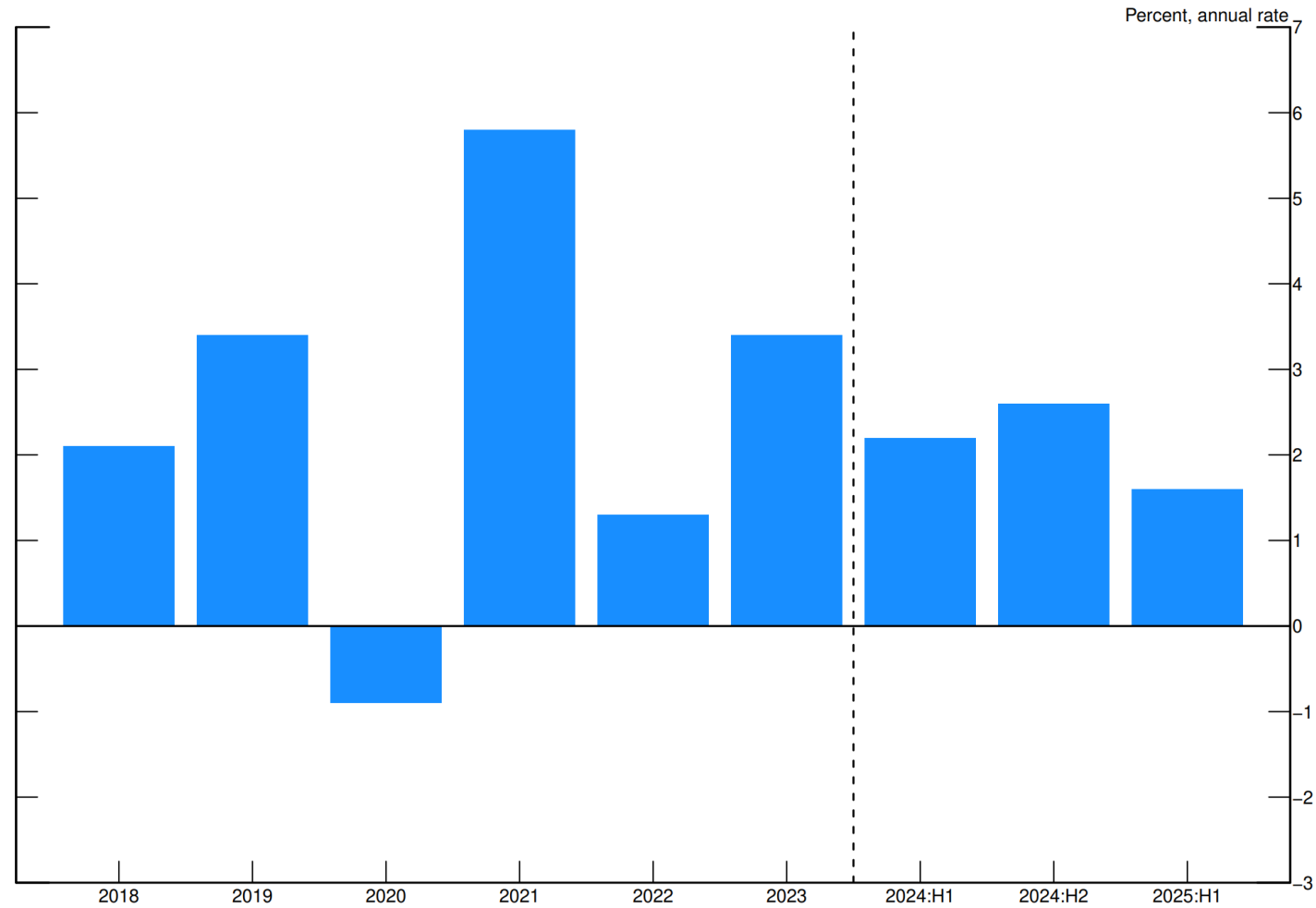
## Notable Continuity

- Explains how we interpret the dual mandate from Congress
- States monetary policy must be forward looking
- Maintains our commitment to a 2 percent inflation objective
- Committed to conducting a public review roughly every five years





## Figure 1: Real Gross Domestic Product

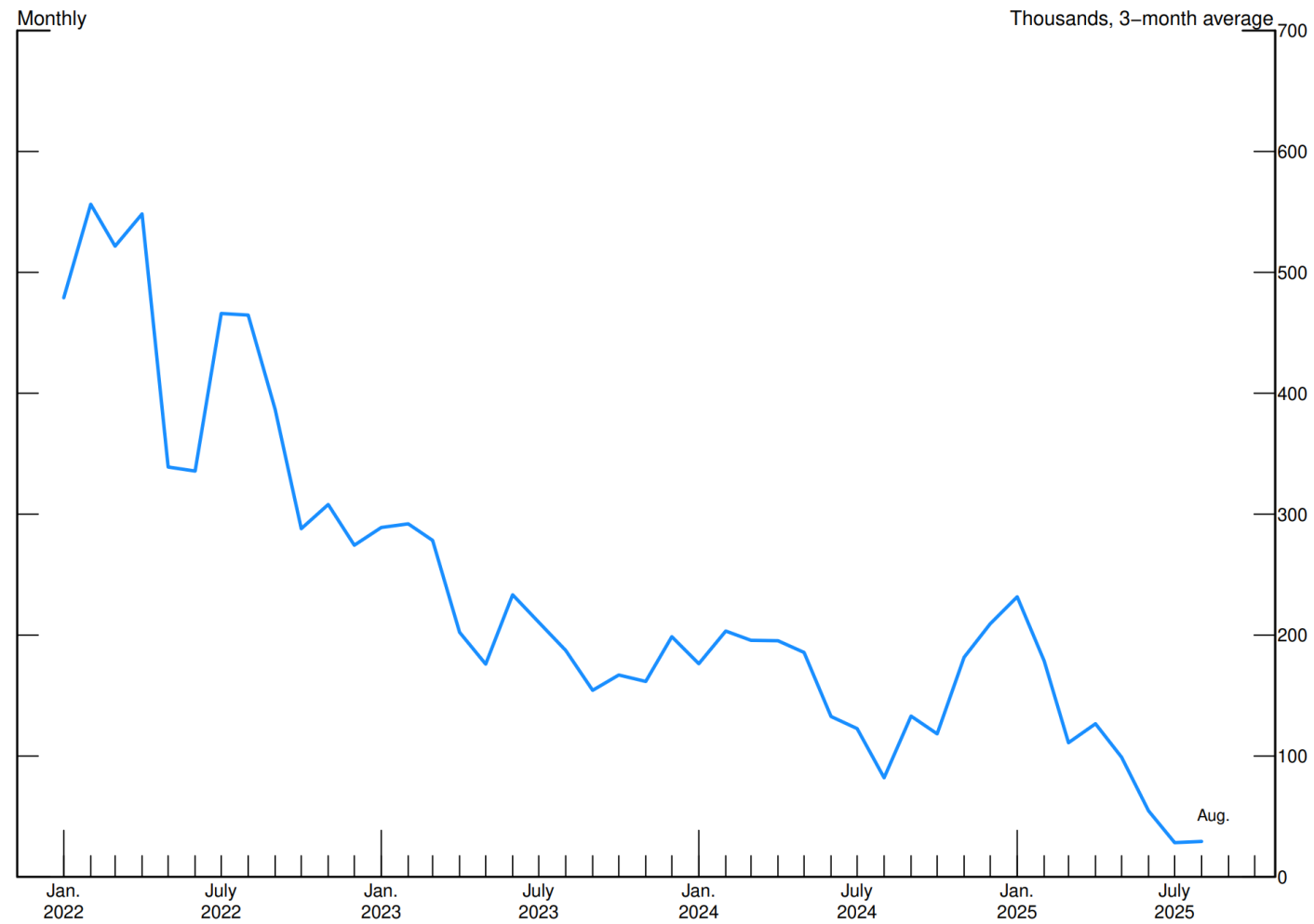


Note: Percent change from preceding period. The vertical line separates yearly GDP data from half-yearly GDP data. Annual GDP values represent Q4:Q4 comparisons, and half-year GDP values represent Q4:Q2 and Q2:Q4 comparisons. Seasonally adjusted.

Source: U.S. Bureau of Economic Analysis, Real Gross Domestic Product, retrieved from FRED, Federal Reserve Bank of St. Louis.



## Figure 2: Nonfarm Payroll Gains

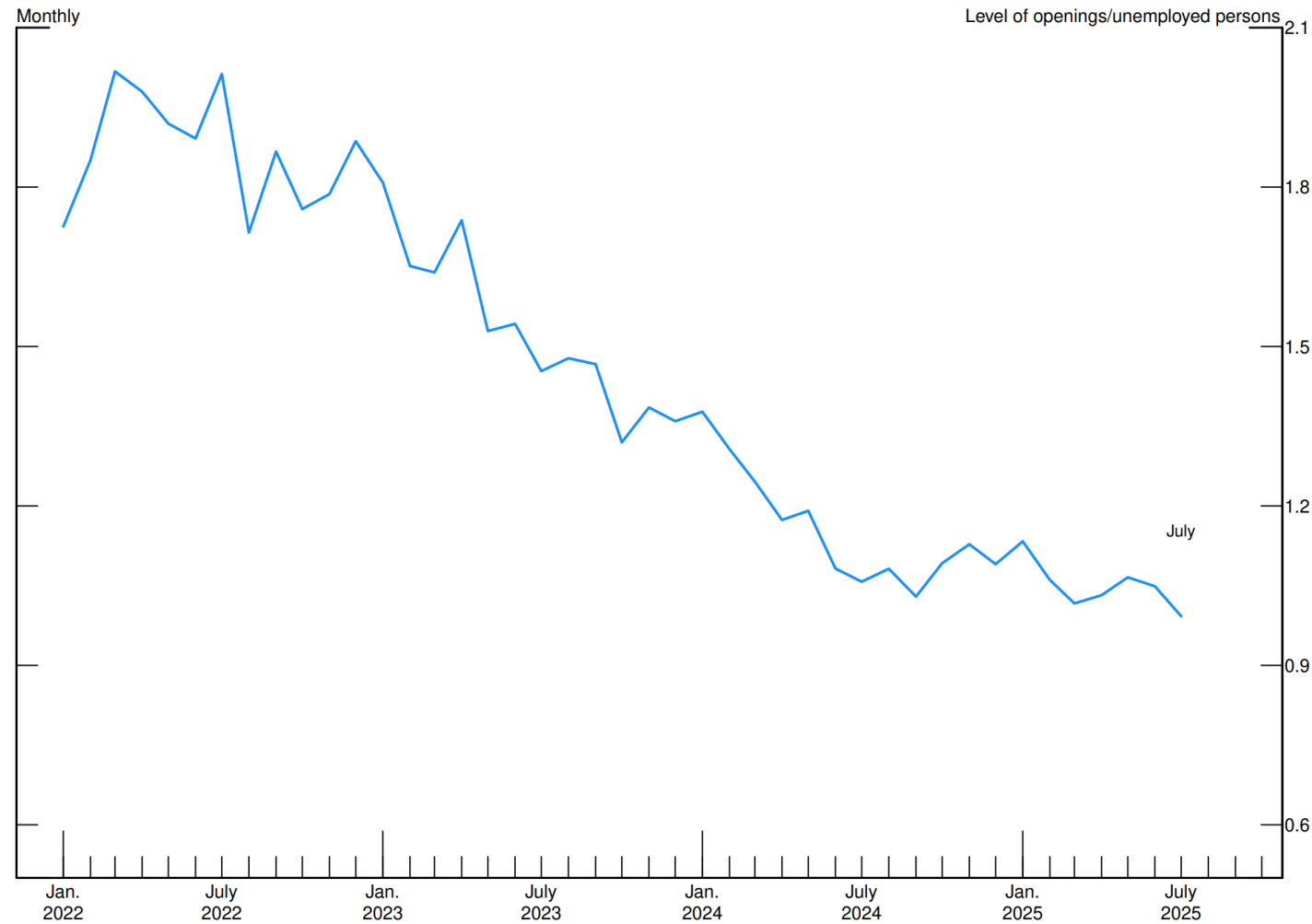


Note: Seasonally adjusted.

Source: U.S. Bureau of Labor Statistics, All Employees, Total Nonfarm, retrieved from FRED, Federal Reserve Bank of St. Louis.



## Figure 3: Nonfarm Job Openings/Unemployment Level

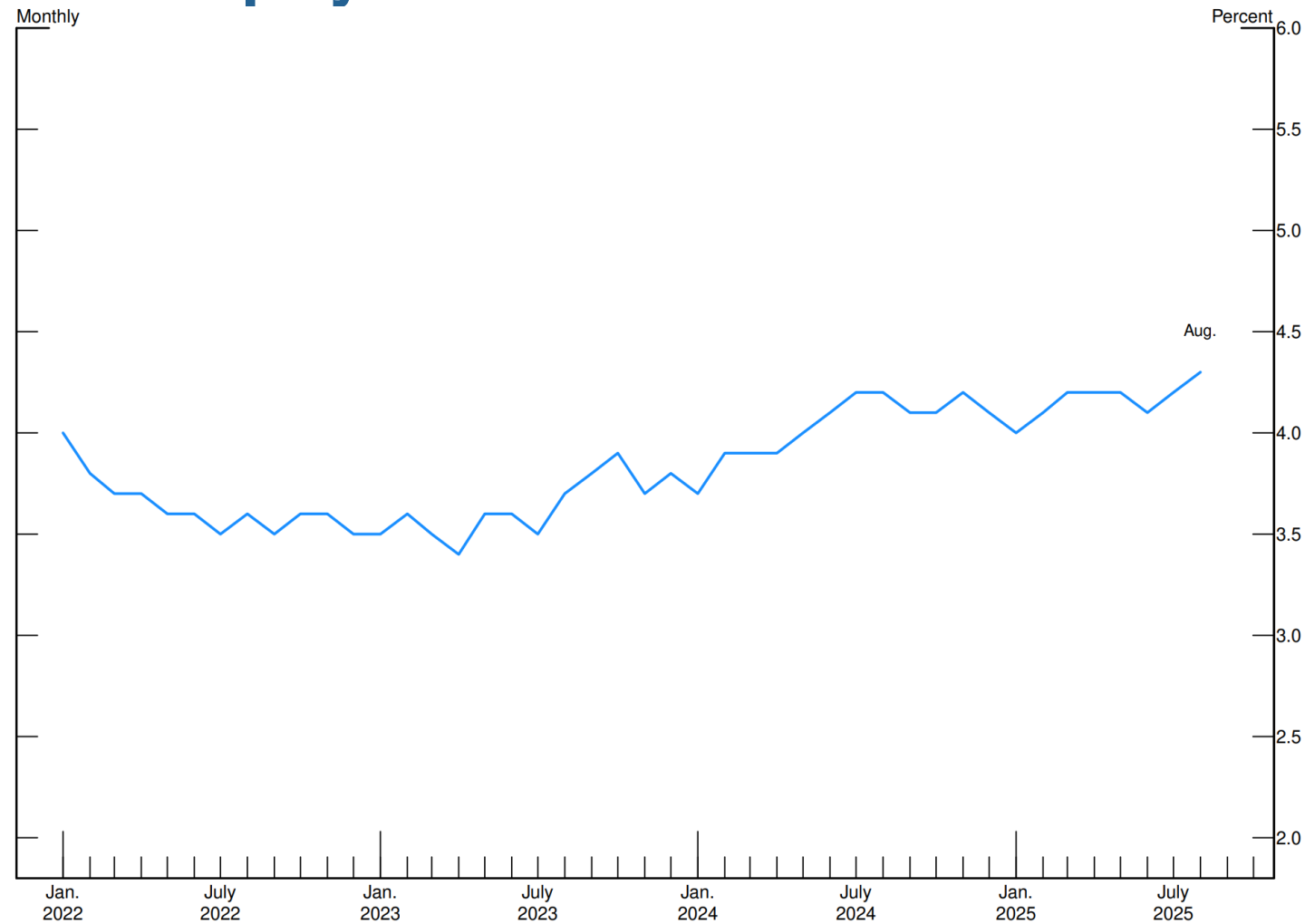


Note: Seasonally adjusted.

Source: U.S. Bureau of Labor Statistics, Job Openings: Total Nonfarm and Unemployment Level, retrieved from FRED, Federal Reserve Bank of St. Louis.



## Figure 4: Unemployment

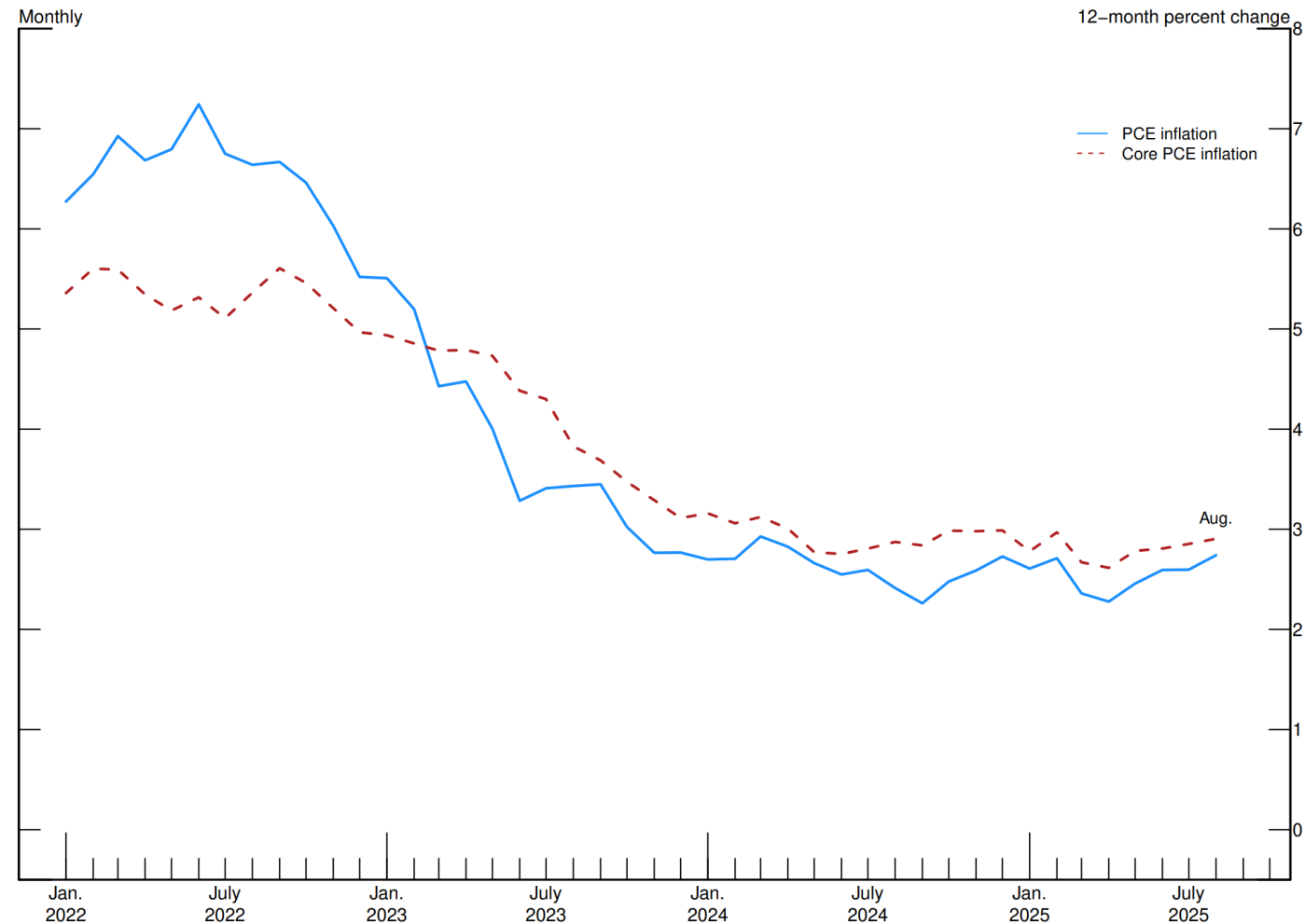


Note: Seasonally adjusted.

Source: U.S. Bureau of Labor Statistics, Unemployment Rate, retrieved from FRED, Federal Reserve Bank of St. Louis.



## Figure 5: 12-Month PCE and Core PCE Inflation

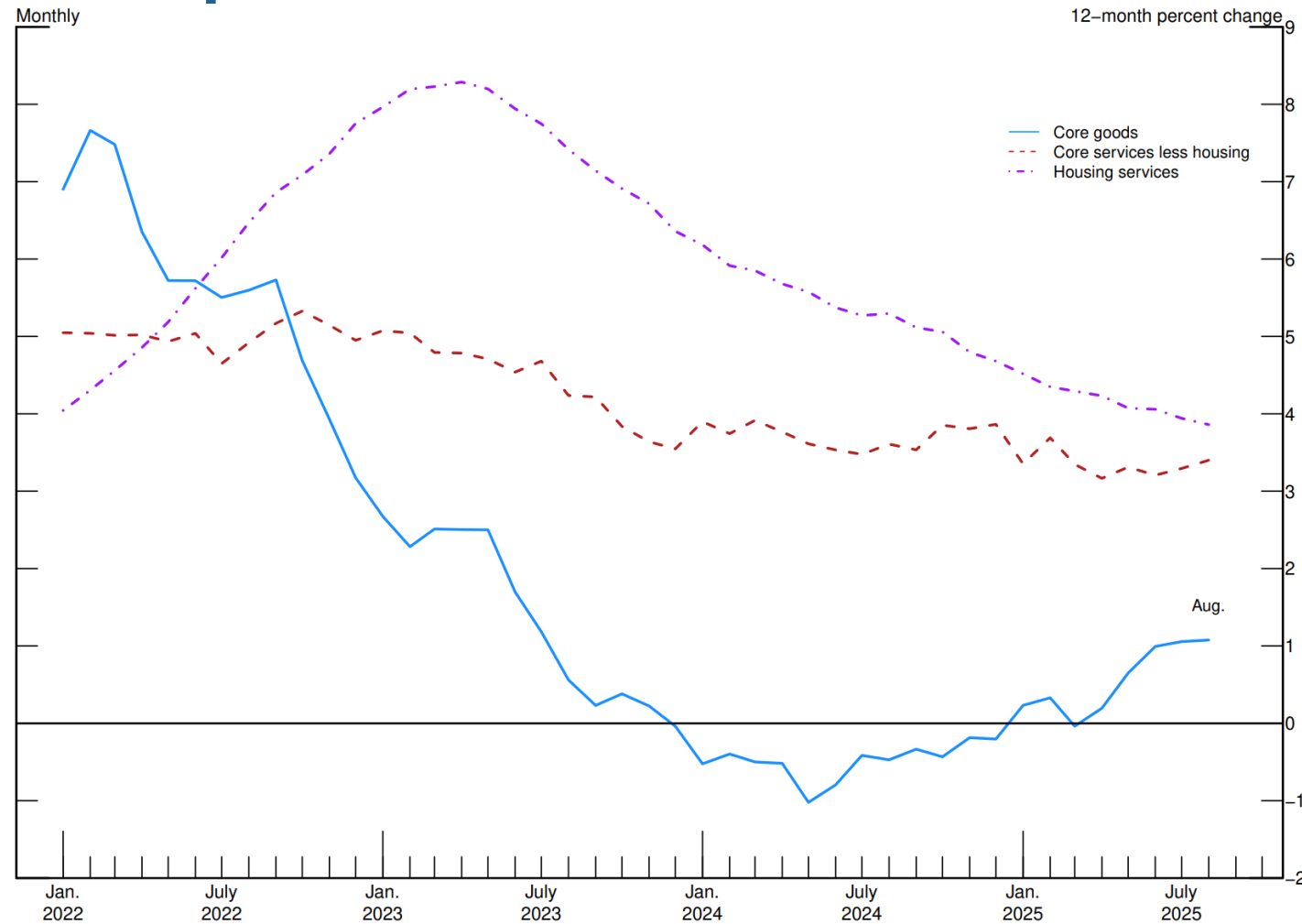


Note: PCE inflation is the change in the personal consumption expenditures price index, and core PCE inflation is the change in PCE price index excluding food and energy. PCE and core PCE are 12-month inflation percentages calculated using seasonally adjusted annual rates.

Source: U.S. Bureau of Economic Analysis, Personal Consumption Expenditures: Chain-type Price Index and Personal Consumption Expenditures Excluding Food and Energy (Chain-Type Price Index), retrieved from FRED, Federal Reserve Bank of St. Louis.



## Figure 6: Components of Core PCE Inflation

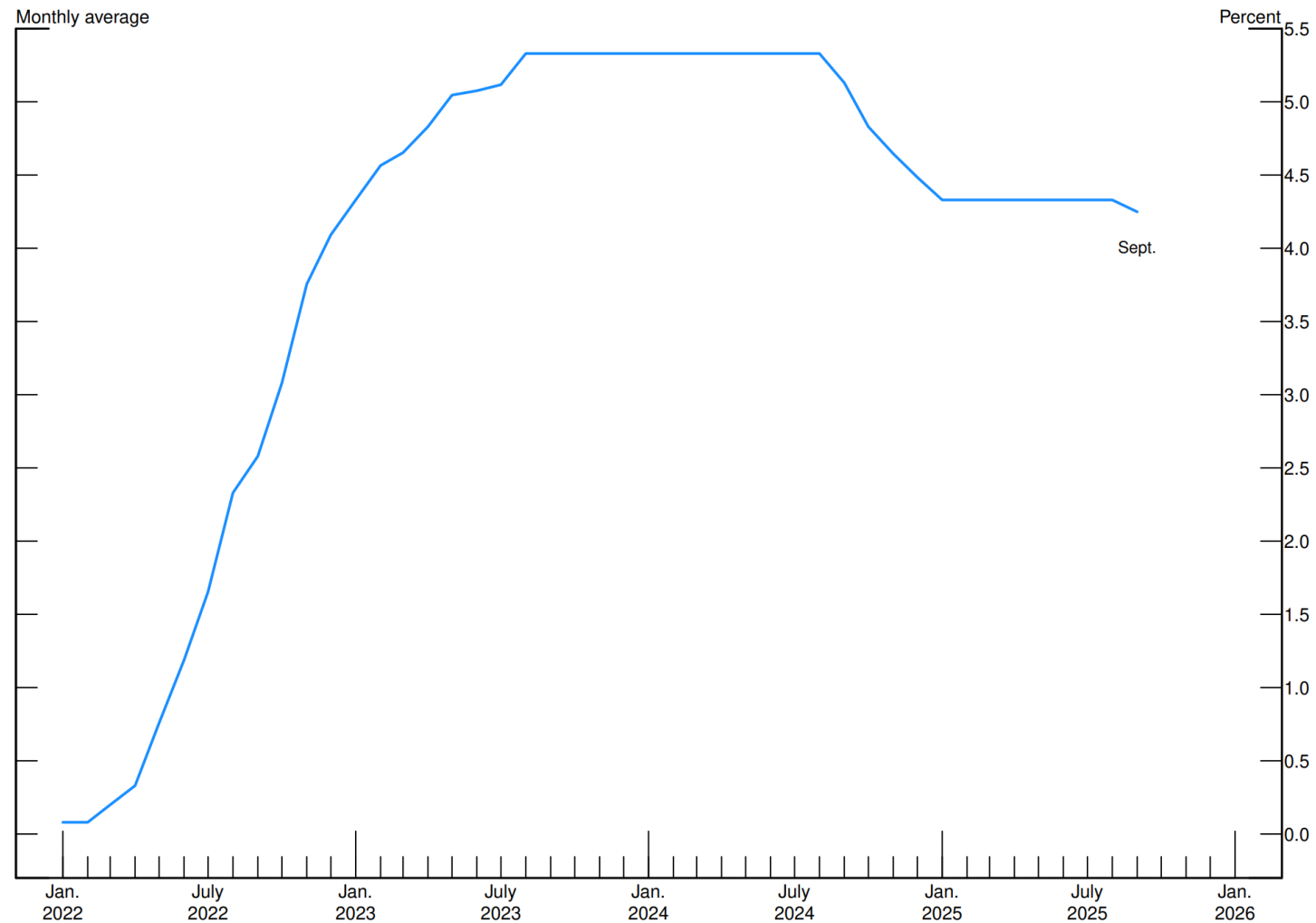


Note: Core goods inflation is the change in the personal consumption expenditures (PCE) price index excluding energy and food. Core services inflation is the change in the PCE price index excluding energy services.

Source: U.S. Bureau of Economic Analysis.



## Figure 7: Federal Funds



Source: Federal Reserve Bank of New York.



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