Adriana D Kugler: Economic outlook

Speech by Ms Adriana D Kugler, Member of the Board of Governors of the Federal Reserve System, at the International Economic Symposium, co-hosted by the National Association for Business Economics and the Central Bank of Ireland, Dublin, 12 May 2025.

* * *

Thank you, Reamonn. It is an honor and a privilege to be asked to speak in the beautiful country of Ireland and here at the Central Bank of Ireland. The histories of the U.S. and Ireland are intertwined. Our friendship is enduring, and our economies are closely tied. The Irish economy and the Bank stand as examples of the benefits of being open to international connections and the sharing of the best ideas and practices. I am delighted to have the opportunity to meet with my counterparts here and continue this great friendship. It is also wonderful to see many members of the National Association for Business Economics (NABE). NABE and its members have made many important contributions to the field of economics; as such, I always enjoy speaking to this esteemed group.[1]

I am particularly delighted to contribute to this conference on trade, technology, and policy. As an academic, part of my research has investigated the link between trade and productivity. And in my current role, I have highlighted these themes in several of my recent speeches, including the role of recent advancements in technology, such as artificial intelligence, as well as the role of business formation in terms of boosting U.S. productivity over the past few years.[2] Today, I would like to focus my attention on the current outlook for the U.S. economy and how I am thinking about the path of monetary policy. Of course, given current developments, I will focus on the role played by trade policy and how it may affect the economy and productivity going forward.

While the latest data show a resilient economy, I expect growth this year to be slower than last. Labor market conditions have been mostly stable. Inflation remains above the Federal Open Market Committee's (FOMC) 2 percent target, and further progress on disinflation has been slow. Looking ahead, I am monitoring the effects of changing trade policies, as I see them as likely having a significant effect on the U.S. and global economies in the near future.

Trade policies are evolving and are likely to continue shifting, even as recently as this morning. Still, they appear likely to generate significant economic effects even if tariffs stay close to the currently announced levels, and the uncertainty associated with these tariffs has already generated effects on the economy through front-loading, sentiment, and expectations. Let me start by describing how I see current economic conditions.

Economic Activity

Regarding overall economic activity, it is currently hard to judge the underlying pace of growth of the U.S. economy, as the gross domestic product (GDP) release for the first quarter showed strong evidence of front-loading of imports ahead of tariffs. GDP contracted at a 0.3 percent annual rate in the first quarter after expanding 2.5 percent during 2024. However, the latest GDP figure likely overstates the deceleration in activity, as a 41.3 percent surge in imports apparently did not get fully picked up in the inventory data or other components of spending. The size of the swings in imports may make the measurement of activity more difficult.

It is helpful to look at private domestic final purchases (PDFP), a measure of demand in the private sector: It rose at a rate of 3 percent in the first quarter-similar to the pace recorded last year. Still, the strength in PDFP also likely reflects some pull-forward of purchases by businesses and consumers to get ahead of tariffs.

The Federal Reserve's April Beige Book and conversations with contacts also point toward front-loading in auto sales or other high-end goods. However, the Beige Book and various indicators of consumer and business confidence also point to a downbeat tone about underlying economic activity down the road. For instance, the Beige Book notes that several Districts see a deterioration in demand for travel and other nonfinancial services and indicates that businesses may put investments on hold moving forward. Several other economic indicators that I track suggest some signs of declining economic activity in the future. For instance, the Institute for Supply Management's manufacturing purchasing managers index for April shows that new orders have been declining since February.

Labor Market

On the employment side of our mandate, conditions seem to be mostly stable. The most recent employment report showed that employers created 177,000 new jobs in April, in line with the average of the previous six months. The unemployment rate was 4.2 percent-still within the narrow and historically low range of 4 to 4.2 percent-where it has remained since May of 2024. In addition, the pace of layoffs remains modest. New applications for unemployment benefits have remained relatively stable at historically low levels. However, I am carefully watching other sources of data for any signs that the labor market could be shifting, given the broader uncertainty. Some forward-looking measures of layoffs have increased, such as the number of mentions of the word "layoff" in the Beige Book.

In terms of the demand for workers, the U.S. Labor Department's Job Openings and Labor Turnover Survey (JOLTS) showed that the vacancy rate-the number of vacant jobs as a percentage of total employment and vacant jobs-declined to 4.3 percent in March, the lowest in six months. The government data showed that the ratio of vacancies to the number of unemployed Americans was 1.0 in March, below its 2019 average of 1.2-also indicating the continuing easing of U.S. labor markets. Overall, job growth remains positive, and unemployment is still low, but I am watching a broad range of incoming readings carefully.

Inflation

On the other side of our dual mandate is inflation. After two years of notable progress following U.S. inflation reaching its pandemic-era peak, progress on disinflation has slowed since last summer. Inflation remains somewhat above the FOMC's 2 percent goal. At the Fed, the inflation reading we track most closely is the personal consumption expenditures (PCE) price index. The March report, released on April 30, showed that the 12-month change in the PCE price index was 2.3 percent; the core PCE price index-which excludes food and energy prices-rose 2.6 percent over the same period.

To help me judge the path of future inflation, I pay careful attention to two subcategories of the index. One is core goods prices, which exclude volatile food and energy prices. The second is nonhousing market-based services, which are based on transactions such as car maintenance and haircuts, not imputed prices. Goods inflation was negative for most of 2024-as was the norm for several years before the pandemic-but it was positive early this year. In contrast, nonhousing market services inflation stayed elevated through March, coming in at 3.4 percent. That category often provides a good signal of inflationary pressures across all nonhousing services. Looking ahead, I find it critical to monitor not only the most up-to-date data but also the changing economic policies around the world.

Economic Effects of Global Policy Changes

To pause briefly, I would like to take a moment to discuss the Fed's structure. The Fed operates independently from the elected government in Washington. We make our policies to best achieve the goals given to us by Congress of maximum employment and price stability. As such, it is not my role to comment on the policies offered by the U. S. government or any government around the world. Rather, I make assessments of the likely effects of these policies, observe the behavior of the U.S. and world economies, and develop views about the best U.S. monetary policy to achieve our dual-mandate goals.

The U.S. is implementing policy changes in trade, immigration, fiscal policy, and regulation, and other economies are also changing their policies in the areas of trade and fiscal spending, particularly in defense, which could stimulate aggregate demand. But given that the most important changes have occurred so far in the area of trade policy, today I would like to discuss some important economic channels through which changes in tariffs may affect the U.S. economy.

Although higher tariffs on U.S. imported goods may affect our macroeconomy through many channels, some of which I will describe next, I think they will primarily act as a negative supply shock, raising prices and decreasing economic activity. While uncertainty remains about the ultimate level of the average tariff rate, currently announced average tariffs in the U.S. are still much higher than they were in the past many decades. If tariffs remain significantly larger relative to earlier in the year, the same is likely to be true for the economic effects, which will include higher inflation and slower growth.

How do I expect this to play out? In the near term, higher import costs will raise prices for both consumer goods and inputs to production. On their own, imported goods represent about 11 percent of U.S. GDP. However, given that several intermediate goods, such as aluminum and steel have been tariffed, and they affect costs in many sectors of the economy, prices of many goods and services are also likely to be affected. In addition, in conversations with business contacts, I have heard that firms are paying attention to the price sensitivity of consumers across the entire catalog of items sold and may spread price increases to less price-sensitive items to avoid reducing their profit margins. A Federal Reserve Bank of Dallas survey of Texas business executives found that 55 percent of respondents expect to pass through most or all of the costs from higher tariffs to customers.[3] Of those expecting to pass on costs, 26 percent expect to pass through the higher tariff cost upon the announcement of tariffs, and 64 percent expect this pass-through to occur within the first three months after the tariffs take effect. That would suggest that price increases may be observed soon.

Given these expected price increases, real incomes will fall, and operating costs will rise, which will lead consumers to demand fewer final goods and services and firms to demand fewer inputs. Ultimately, I see the U.S. as likely to experience lower growth and higher inflation. Over time, there could also be significant effects on productivity. As firms adjust to the higher input costs and lower demand, they may cut back on capital investment and shift to a less-efficient combination of inputs. Additionally, less-efficient domestic firms may increase their market share.[4] All of this may result in a decrease in potential output growth, lowering the underlying pace of economic activity in the U.S.

In addition to any direct effect from actual global policy changes, consumers, businesses, and market participants have reported high levels of uncertainty about which policies may be ultimately chosen and how long they will remain in place. In fact, in recent months, several measures of economic uncertainty have risen sharply.

There are several types of measures that quantify economic uncertainty, with two types having gained prominence among economists closely monitoring the U.S. economic outlook.[5] Some are based on financial market transactions, such as the Chicago Board Options Exchange's Volatility Index, popularly called the VIX. Others are based on the occurrence of certain keywords associated with the concept of uncertainty in newspapers of wide circulation, such as the economic policy uncertainty and trade policy uncertainty readings.[6] These measures of uncertainty have reached historical highs in recent months. Similarly, I also saw the word "uncertainty" being highly cited in the Beige Book I reviewed before the FOMC's policy meeting last week.[7]

In times of heightened uncertainty, businesses may delay investment decisions, and consumers may increase precautionary savings and postpone discretionary purchases. Moreover, the economic research literature has documented that these decisions from businesses and consumers reverberate through the economy, pushing down aggregate demand. Firms, anticipating lower demand for their services and products, may post fewer job openings and cut back on investments to expand capacity. While the labor market has remained broadly resilient, the JOLTS data for March showed that job openings fell. Workers, therefore, may have a more difficult time finding employment, decreasing economy-wide income and aggregate demand.[8] This lower aggregate demand may then exert downward pressure on inflation, though probably not by enough to offset the effect from the adverse supply shock that I previously mentioned. For example, recent data show that prices for accommodations and airfares have fallen, consistent with an increasing number of anecdotal reports of weaker consumer demand for discretionary travel services.

I am also monitoring the effect of policy changes on another important channel: inflation expectations. For instance, consumers and businesses have reported tariffs as an important reason for having increased their near-term inflation expectations. Several surveys, including those from the Conference Board and the Federal Reserve Banks of Atlanta and New York, have found that consumers and businesses expect higher inflation one year from now. Another closely watched survey from the University of Michigan showed that one-year-ahead inflation expectations in April were higher than in the pandemic period. This increase in short-run expectations may give businesses more leeway to raise prices.

Most longer-run measures, including those from the Philadelphia Fed's Survey of Professional Forecasters and the New York Fed's Survey of Consumer Expectations, show either stability or much smaller increases in inflation expectations, which does provide some comfort to me. Additionally, inflation compensation, which is based on yields from Treasury Inflation-Protected Securities, has increased only for short-term maturities, such as one year ahead, and has shown stability in maturities over the five years starting five years from now. Still, I have taken note of the increase in longer-term inflation expectations from the Michigan survey, which reached the highest level since June 1991. Given these developments, I am keeping a close watch on inflation, because as I have indicated in the past, I believe it is critical to keep long-term inflation expectations very well anchored at 2 percent.

Looking globally, international developments do not seem to be adding inflationary pressures to the U.S. Economic growth in most developed economies remains moderate, and domestic inflation in those countries has declined from elevated levels. In Europe, activity data point to modest growth as the region deals with headwinds stemming from past energy shocks and competitive pressures from elsewhere in the world. The New York Fed's Global Supply Chain Pressure Index has been relatively stable since the beginning of the year. Oil prices have declined significantly since January.

Monetary Policy

I have discussed a lot of data and developments with you today. To summarize, the U. S. economy has remained resilient up until now, with a still-stable labor market. Meanwhile, the disinflationary process has slowed. This comes against a backdrop of heightened uncertainty as households, businesses, and, indeed, monetary policymakers process the changes to economic policies that are happening around the world. Going forward, I will continue to closely monitor the direct effects of global economic policies on prices and employment, as well as the indirect economic effects from uncertainty, inflation expectations, and productivity.

U.S. monetary policymakers on the FOMC met last week in Washington. At that meeting, the Committee voted to maintain its policy rate at 4-1/4 to 4-1/2 percent. Given the upside risks to inflation and given that I still view our policy stance as somewhat restrictive, I supported the decision to keep rates at that level. With inflation and employment potentially moving in opposite directions down the road, I will closely monitor developments as I consider the future path of policy.

I view our current stance of monetary policy as well positioned for any changes in the macroeconomic environment. I remain committed to achieving both of our dual-mandate goals of maximum employment and stable prices.

Thank you for your attention today-and thank you very much for inviting me to speak to you here in Dublin. It has been an honor and a privilege. I look forward to your questions.

---

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

[2] See Adriana D. Kugler (2025), "Entrepreneurship and Aggregate Productivity," speech delivered at the 2025 Miami Economic Forum, Economic Club of Miami, Miami, Florida, February 7. Also, see Adriana D. Kugler (2024), "A Year in Review: A Tale of Two Supply Shocks," speech delivered at the Detroit Economic Club, Detroit, Michigan, December 3.

[3] The special questions included in the survey of Texas business executives is available on the Federal Reserve Bank of Dallas' website at https://www.dallasfed.org/research/surveys/tbos/2025/2504q#tab-all.

[4] For the effects of tariffs on productivity, see Marcela Eslava, John Haltiwanger, Adriana Kugler, and Maurice Kugler (2013), "Trade and Market Selection: Evidence from Manufacturing Plants in Colombia," *Review of Economic Dynamics,* vol. 16 (January), pp. 135–58; Marcela Eslava, John Haltiwanger, Adriana Kugler, and Maurice Kugler (2004), "The Effects of Structural Reforms on Productivity and Profitability Enhancing Reallocation: Evidence from Colombia," *Journal of Development Economics,* vol. 75 (December), pp. 333–71; and Davide Furceri, Swarnali A. Hannan, Jonathan D. Ostry, and Andrew K. Rose (2022), "The Macroeconomy after Tariffs," *World Bank Economic Review,* vol. 36 (May), pp. 361–81.

[5] For a literature review on quantifying uncertainty, see Danilo Cascaldi-Garcia, Cisil Sarisoy, Juan M. Londono, Bo Sun, Deepa D. Datta, Thiago Ferreira, Olesya Grishchenko, Mohammad R. Jahan-Parvar, Francesca Loria, Sai Ma, Marius Rodriguez, Ilknur Zer, and John Rogers (2023), "What Is Certain about Uncertainty?" *Journal of Economic Literature,* vol. 61 (June), pp. 624–54.

[6] For more details on the economic policy uncertainty index, see Scott R. Baker, Nicholas Bloom, and Steven J. Davis (2016), "Measuring Economic Policy Uncertainty," *Quarterly Journal of Economics,* vol. 131 (November), pp. 1593–1636. For more details on the trade policy uncertainty index, see Dario Caldara, Matteo Iacoviello, Patrick Molligo, Andrea Prestipino, and Andrea Raffo (2020), "The Economic Effects of Trade Policy Uncertainty," *Journal of Monetary Economics,* vol. 109 (January), pp. 38–59.

[7] The April 2025 Beige Book is available on the Federal Reserve Board's website at https://www.federalreserve.gov/monetarypolicy/beigebook202504-summary.htm.

[8] For studies documenting how uncertainty shocks may act as adverse aggregate demand shocks, see Sylvain Leduc and Zheng Liu (2016), "Uncertainty Shocks Are Aggregate Demand Shocks," *Journal of Monetary Economics,* vol. 82 (September), pp. 20–35, as well as Susanto Basu and Brent Bundick (2017), "Uncertainty Shocks in a Model of Effective Demand," *Econometrica,* vol. 85 (May), pp. 937–58.