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Economic Outlook and Energy Effects

Remarks by

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at

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Federal Reserve Bank of Dallas

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Thank you, Donald, for the kind introduction.¹ I am honored to be here in Dallas. I very much enjoyed my time today meeting with community members and hearing from the hardworking staff at the Dallas Fed. And I appreciate this opportunity to speak with all of you this evening.

Tonight, I would like to share with you my updated economic outlook and then discuss the possible implications of that outlook for the path of monetary policy. It is an opportune time for that discussion, just a week after our last Federal Open Market Committee meeting. Then, I will expand on the implications of elevated energy prices for the economy, particularly thinking about the effects here in the resource-rich 11th District, and finally I will be happy to answer some questions.

I see the U.S. economy continuing to grow, led by resilient consumers and healthy business investment. The labor market is roughly in balance but susceptible to adverse shocks. Unemployment is low and stable by historical standards, while hiring has slowed to a very modest pace. Inflation, meanwhile, remains above the Federal Reserve's 2 percent target. At the beginning of the year, I noted signs that inflation would return to a sustainable path toward our objective.² The ongoing uncertainty over tariff policy and the recent jump in energy prices, however, complicates, at least in the short term, the picture on both sides of our dual mandate of maximum employment and price stability. .

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

² See Philip N. Jefferson (2026), "Economic Outlook and Monetary Policy Implementation," speech delivered at the American Institute for Economic Research, Shadow Open Market Committee, and Florida Atlantic University Conference, Boca Raton, Florida, January 16, <https://www.federalreserve.gov/newsevents/speech/jefferson20260116a.htm>

Economic Activity

In 2025, gross domestic product expanded about 2 percent, as shown in Figure 1. That was just a slight slowdown from the prior year, and about in line with estimates of its potential pace. Economic activity was supported by household spending. Business investment, particularly in equipment and intellectual property, was also strong over the past year. Residential investment, meanwhile, contracted.

For this year, I see the economy expanding at a similar or slightly faster rate than last year, though the uncertainty around my outlook is high. On the positive side, I have taken note of the high pace of business formation and broad deregulation activity among federal agencies, which could stimulate growth. Additionally, increased investment in high-tech capital, particularly purchases tied to the expansion of artificial intelligence infrastructure, is promising. Those effects underpin healthy structural productivity growth, which in turn supports economic growth. That said, there are also significant headwinds to consider. If elevated energy costs persist, they can weigh on consumer and business spending. The potential for an extended conflict in the Middle East adds considerable uncertainty to the global economic outlook.

The Labor Market

Currently, labor market dynamics also present a complex picture. The unemployment rate has been relatively low and little changed in recent months. As shown in Figure 2, the unemployment rate was 4.4 percent last month, the same as September 2025. Job growth, however, has also been low. Figure 3 shows nonfarm payrolls, with the blue line representing the monthly change and the red dashed line representing the three-month moving average. After a solid gain in January, payrolls

declined in February, reflecting the effects of winter weather and a strike in the health-care sector. The three-month moving average of payroll gains in February was only 6,000. In addition to its low pace, job growth has also been concentrated in only a few sectors such as healthcare and social services. Behind these figures is that the growth in the supply of labor has significantly eased as net immigration has declined. That has allowed unemployment to hold steady even while demand for labor has cooled.

Other evidence on the health of the labor market is mixed. Job openings are gradually moving lower, and Americans' perceptions of job availability have also trended lower in recent months. But in a positive sign, alternative measures of unemployment have also changed little since September. Specifically, a measure that includes part-time workers who would like to work full time and those who are not working but have looked for a job in the past year moved down in recent months after rising sharply at the end of last year. Claims for unemployment insurance have remained low.

I see the labor market as roughly in balance and expect the unemployment rate to remain near its current level throughout this year. The risks to my labor market forecast, however, are skewed to the downside. Overall, job gains are likely to remain low. I am attentive to the pace and composition of job growth going forward in my assessment of potential fragilities in the labor market.

Inflation

Turning to inflation, progress on disinflation has stalled over the past year, mainly because of tariffs, and inflation remains somewhat elevated relative to our target.

Figure 4 shows the 12-month change in prices. Based on the latest available data, the personal consumption expenditures (PCE) price index, the blue line, is estimated to

have risen 2.8 percent for the 12 months ended in February, in line with January's reading. Core prices, which exclude the volatile food and energy categories and represented by the red dashed line, are estimated to have risen 3.0 percent. There has been little progress in lowering core inflation over the past year. Figure 5 shows the subcomponents of core PCE inflation. We have seen a notable decline in housing services' inflation, shown by the dashed purple line. This decline, however, has been partly offset by an increase in core goods inflation, shown by the blue line. Core services inflation outside of housing, the dashed red line, has largely moved sideways over the past year.

I will pause here to say that I understand why many Americans are frustrated with inflation. Following pandemic disruptions, inflation has remained above the Fed's 2 percent target for five years. The cost of many products rose sharply during the pandemic, and Americans still notice those higher prices when they shop and pay their bills. The recent jump in gasoline prices adds to those frustrations. Low and stable inflation, alongside maximum employment, is the best outcome for all Americans, and that is why I remain firmly committed to returning inflation to our 2 percent target.

It has been my expectation that the disinflationary process would resume once higher tariffs are no longer pushing up consumer prices. In addition, the strong productivity growth and deregulation efforts, which I previously mentioned, may further help in bringing inflation down to our 2 percent target. The ongoing trade policy uncertainty and geopolitical tensions, however, pose upside risk to my inflation forecast. At least in the short term I expect overall inflation to move higher, reflecting a rise in energy prices stemming from the conflict in the Middle East.

Monetary Policy

As a monetary policymaker I confront an outlook where there is downside risk to the labor market and upside risk to inflation. While that is a potentially challenging situation, I am confident that our current policy stance is well positioned to respond to a range of outcomes.

Last week, I supported the FOMC's decision to hold the target range for the federal funds rate steady. As you can see in Figure 6, over the past year and a half, the Committee lowered the target range for the policy rate 175 basis points. These changes put the rate broadly in the range of neutral while maintaining a balanced approach to promoting our dual-mandate objectives. The current policy stance should continue to support the labor market while allowing inflation to resume its decline toward our 2 percent target as the effects of tariff pass-through are completed.

Looking ahead, I believe that the current policy stance leaves us well positioned to determine the extent and timing of additional adjustments to our policy rate based on the incoming data, the evolving outlook, and the balance of risks in a timely manner.

The Energy Economy

Before I conclude, I will share a few thoughts on the energy economy, given that I have the privilege of speaking here in Dallas. I am closely monitoring the situation in both the Middle East and global energy markets. It is still too early to say with great specificity what the economic effects will be, but I can discuss broadly the implications of oil price shocks for both the global and national economy as well as in energy-producing regions.

The effects on the economy will greatly depend on how long energy prices remain elevated. A short period of disruption is unlikely to have a noticeable effect on the economy beyond a quarter or two. A sustained energy price shock, however, could have material implications. Also, regions that are more dependent on energy imports, such as Europe and parts of Asia, may see economic activity and inflation more negatively affected than the U.S.

In the U.S., the increase in energy prices to date should have relatively modest effects on inflation, though consumers are seeing higher gas prices at the pump now. The average price of a gallon of gasoline is up about a dollar compared to just before the recent conflict in the Middle East.³ When gasoline prices jump, families—especially those with lower incomes who spend a larger share on essentials—have less money for everything else. The longer energy prices remain elevated, the more households will need to confront tradeoffs. Families who depend on petroleum products to commute to jobs and school and to heat their homes may need to pull back on more discretionary forms of spending. That could potentially result in lower spending at restaurants or retailers. It could also result in households carrying elevated levels of debt.

Energy products directly represent about 7 percent of total consumer spending, but energy costs are also spread through the economy, including in transportation, manufacturing, and food production. An extended bout of elevated energy prices could put upward price pressure on a variety of other products. As a policymaker, I will monitor to see if these higher costs become embedded in prices throughout the economy.

³ See “National Average Gas Prices” on AAA’s webpage at <https://gasprices.aaa.com>.

When economists discuss oil price shocks in the U.S., the example is often the events of the 1970s. While informative, it is important to understand that the U.S. is in a very different position relative to a half-century ago. The U.S. now leads the world in crude oil and natural gas production and is a net exporter of energy; and Texas is the nation's largest producer of both commodities.

That means the overall economic effect of higher energy prices, if sustained, may be somewhat different here in Texas and in other energy-producing states. It could mean more drilling activity; more jobs in the energy sector and supporting industries, which could translate into higher wages for energy workers; and stronger profits for oil companies in this area. Crude oil and natural gas production, transportation, and processing account for about 15 percent of Texas's economic output, though those sectors account for a smaller share of jobs. About 2.6 percent of workers in this state are directly employed in the sector, with more in supporting industries like legal, accounting, hospitality, construction, and scientific and technical services. If the energy industry expands, that could support spending in other sectors as well.

That said, no family, business, or region is immune to higher energy costs. Drivers in the 11th District also face elevated prices at the pump. Texas is home to logistics and transportation hubs, and those firms face higher costs, as do school districts, small businesses, and nonprofits. It is not possible for this region to avoid the pressures that higher energy prices create, but this area may be buffered by some offsetting benefits.

As I stated, it is still too soon to tell the exact effects of higher energy prices on the economy here in Dallas, nationally, or globally. The conflict may prove to be short

lived, global oil flows could return to prior levels, and the overall effects could be very small. From a policy perspective, energy prices are one factor I monitor regularly, alongside many others. When I contemplate what policy is best to achieve our dual mandate of maximum employment and price stability, I consider the whole of the national economy rather than focus on any specific sector or region.

Uncertainty about the economy is elevated, and the rise in energy prices and the conflict in the Middle East add to that uncertainty. I continue, however, to see our current policy stance as appropriately positioned to allow us to assess how the economy evolves. Thank you again for inviting me to speak here in Dallas. I look forward to our conversation.



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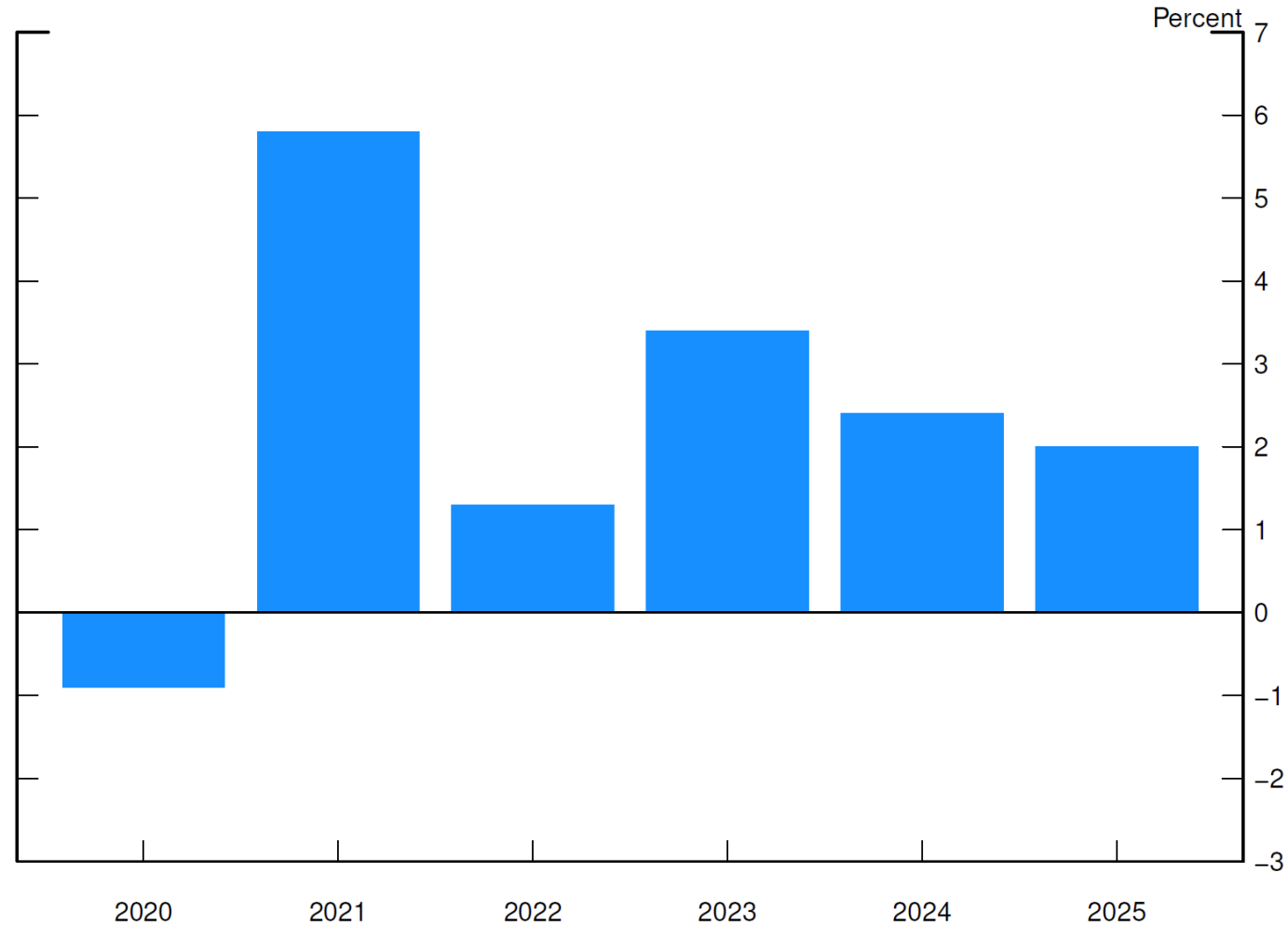
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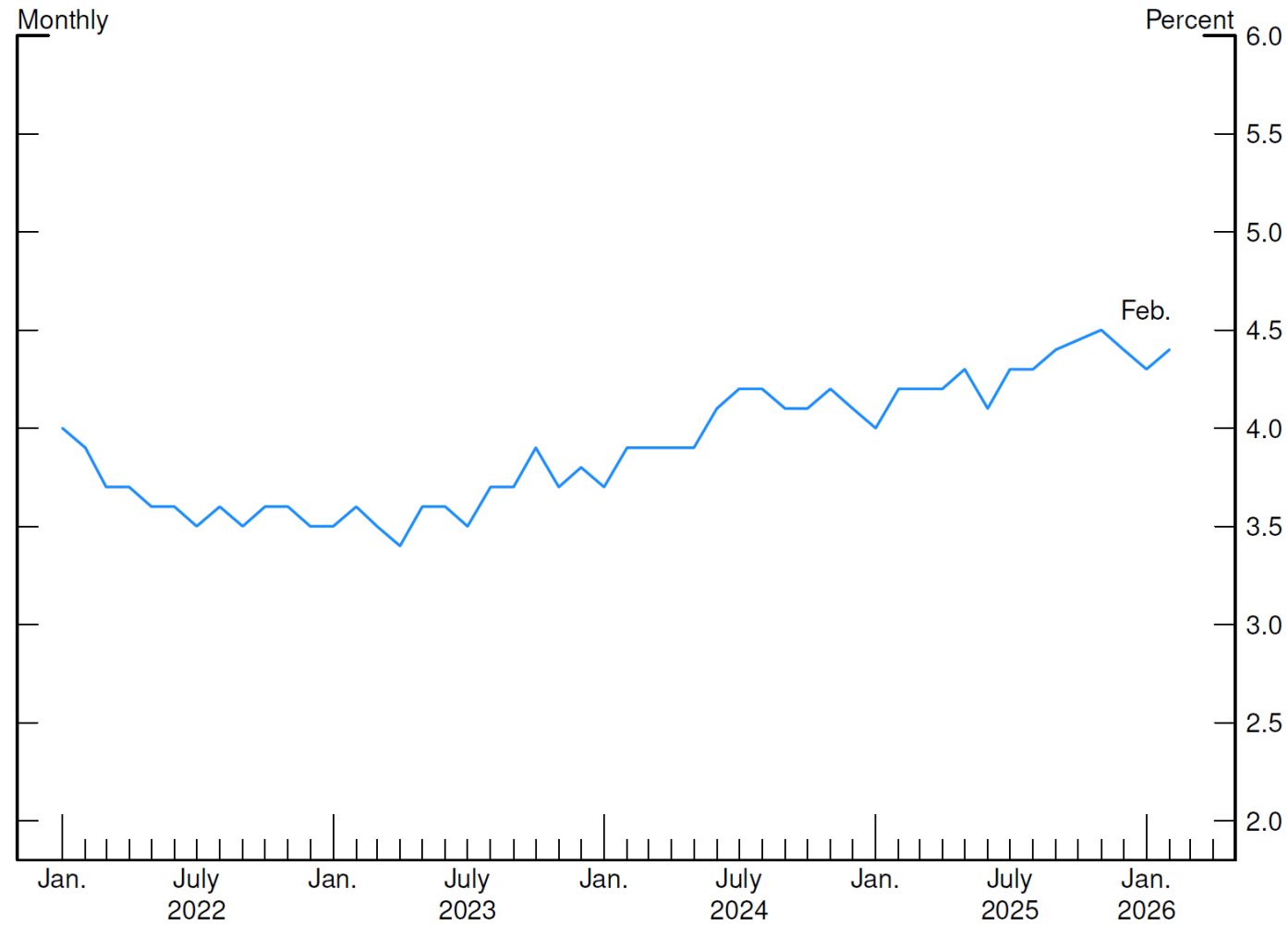
Figure 1: Real Gross Domestic Product



Note: Percent change from preceding period. Annual GDP values represent Q4: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: Unemployment Rate

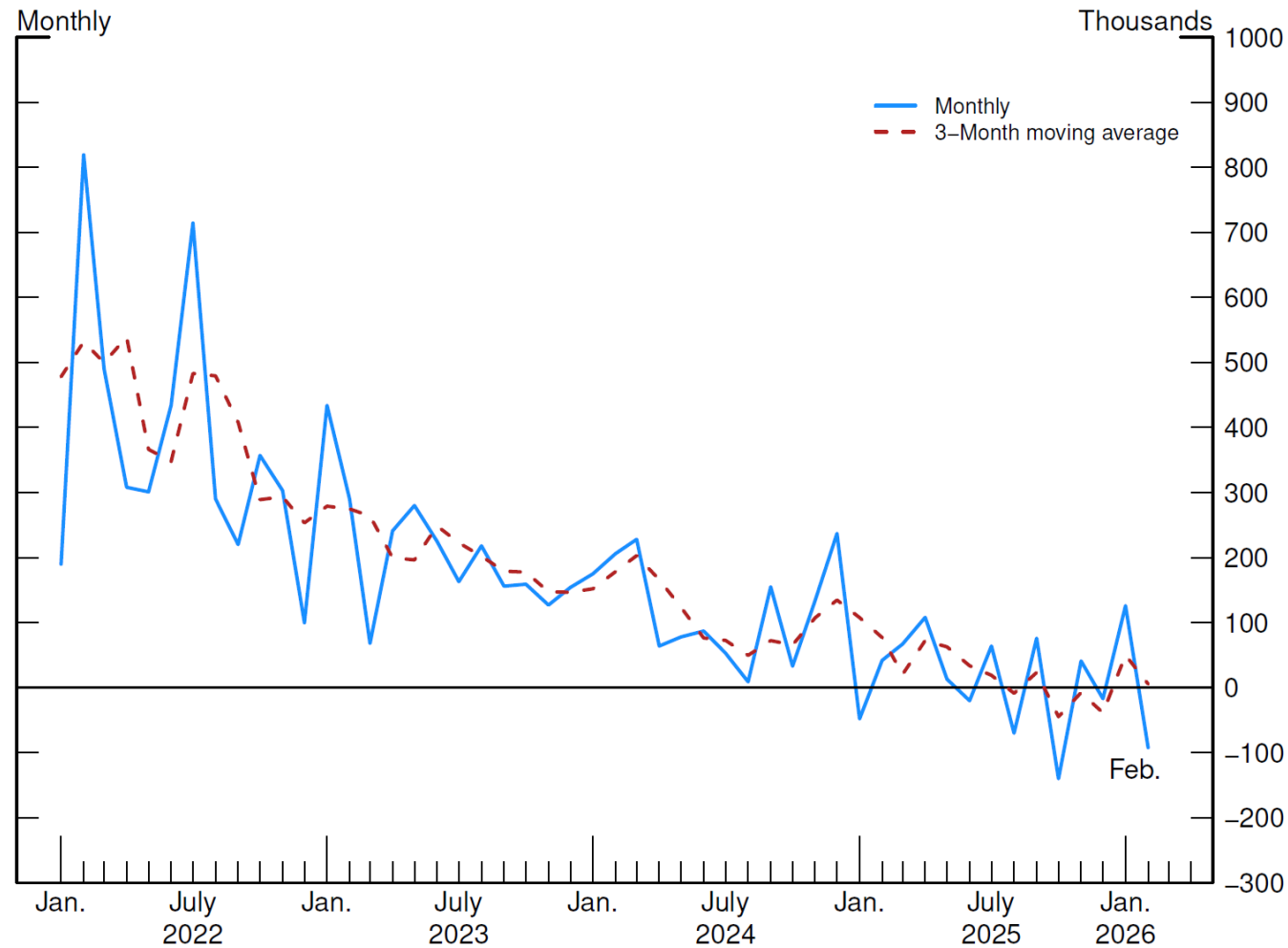


Note: There are no data for October 2025.

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



Figure 3: Monthly Nonfarm Payroll Gains

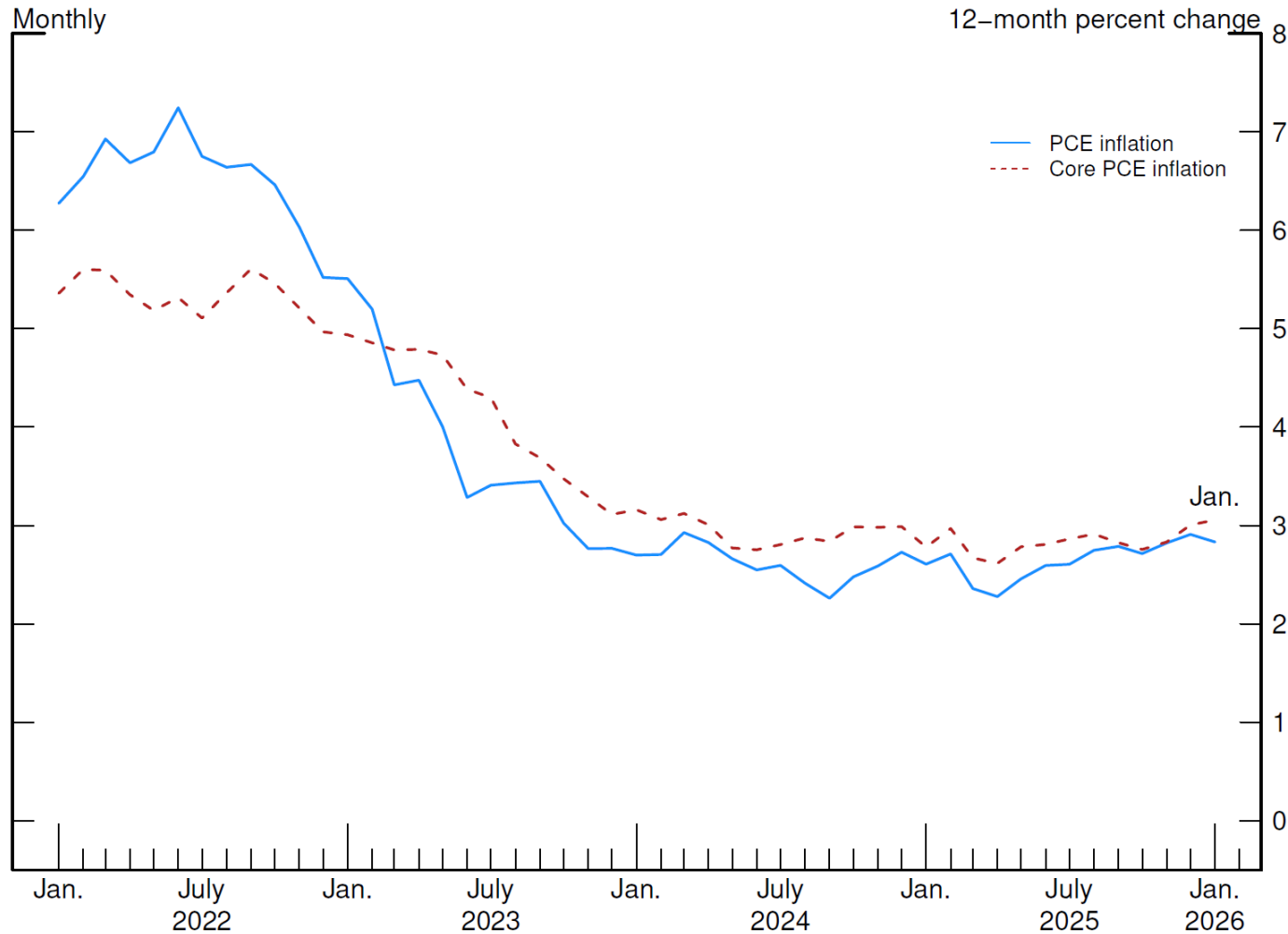


Note: Seasonally adjusted.

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



Figure 4: 12-Month PCE and Core PCE Inflation

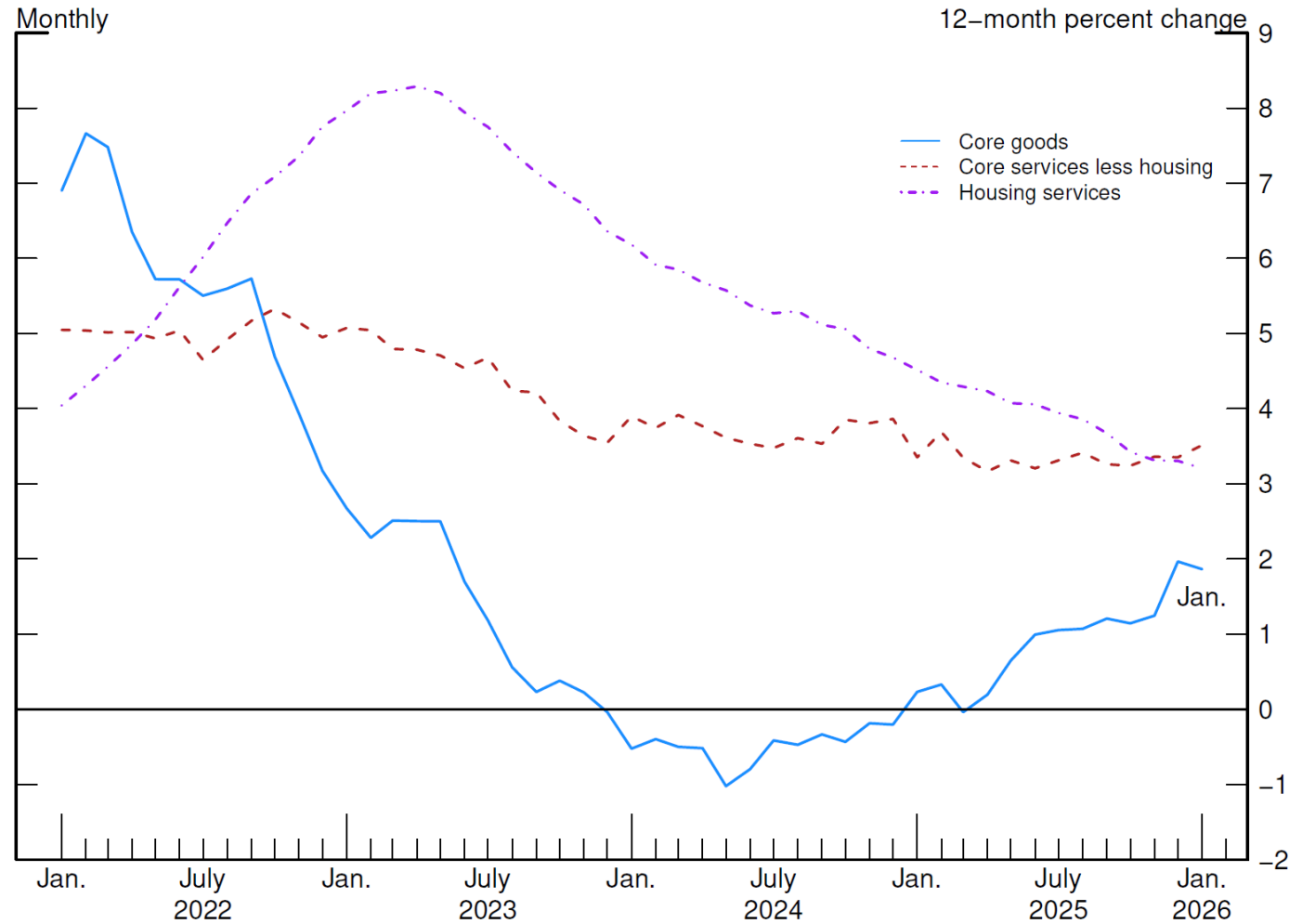


Note: PCE inflation is the change in the personal consumption expenditures price index, and core PCE inflation is the change in PCE price index excluding food and energy. PCE and core PCE are 12-month inflation percentages calculated using seasonally adjusted annual rates.

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 5: Components of Core PCE Inflation

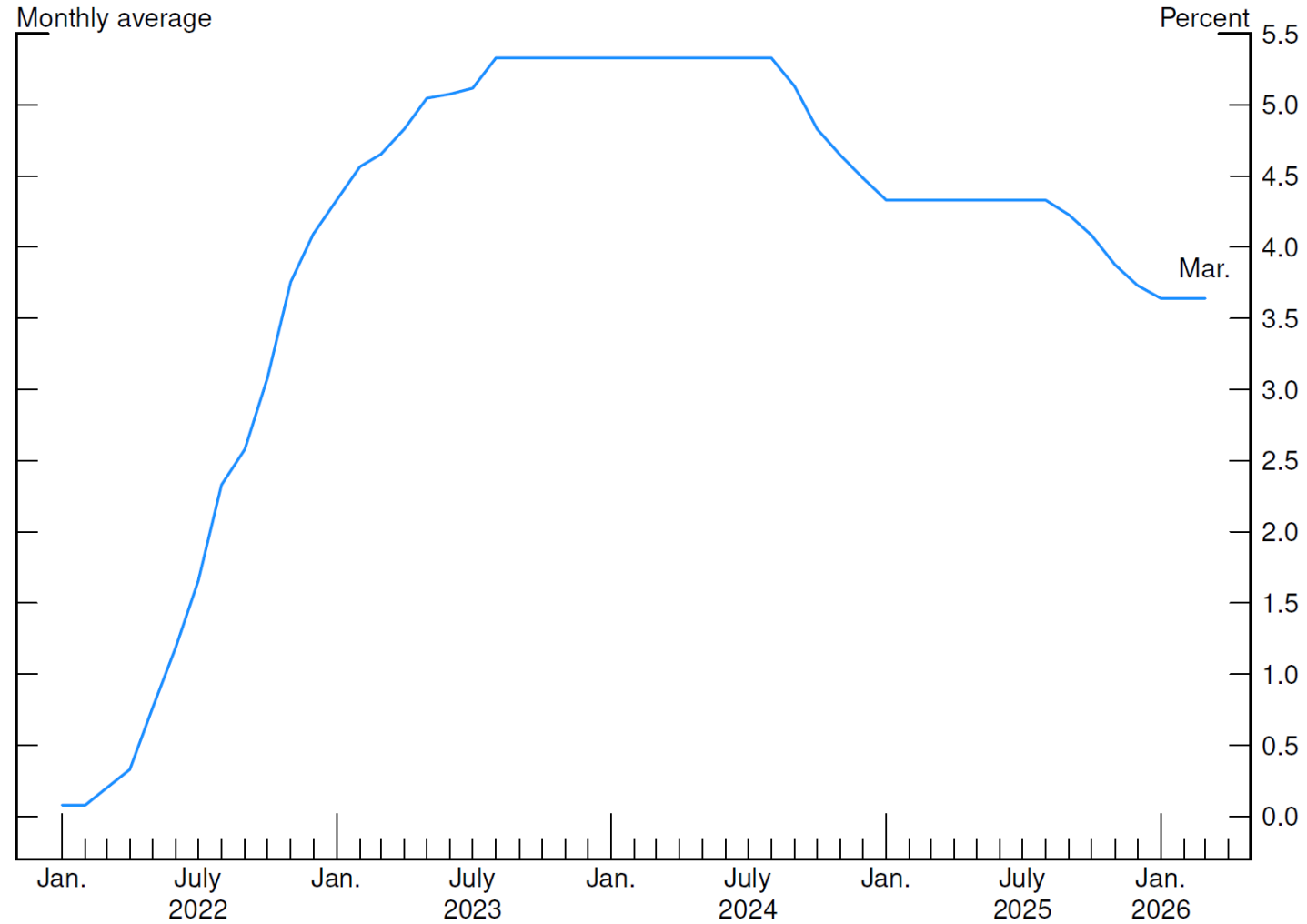


Note: Core goods inflation is the change in the personal consumption expenditures (PCE) price index excluding energy and good. Core services inflation is the change in the PCE price index excluding energy services.

Source: U.S. Bureau of Economic Analysis.



Figure 6: Federal Funds Rate



Source: Federal Reserve Bank of New York, <https://www.newyorkfed.org/markets/reference-rates/effr>.



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