

It's all about the labor market*

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What's (not) up with inflation?

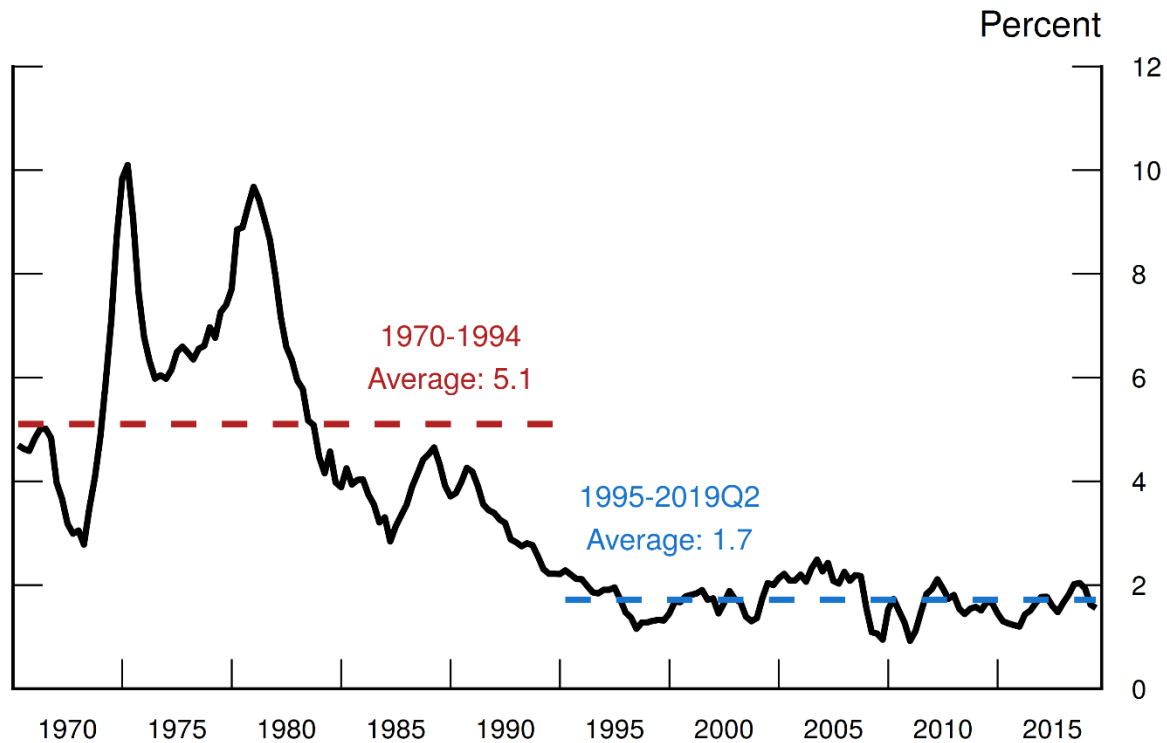
Washington, DC

October 3, 2019

* The views expressed here are my own and do not indicate concurrence with other members of the research staff of the Board of Governors or the Federal Reserve System.

U.S. Inflation Dynamics

U.S. Core Inflation

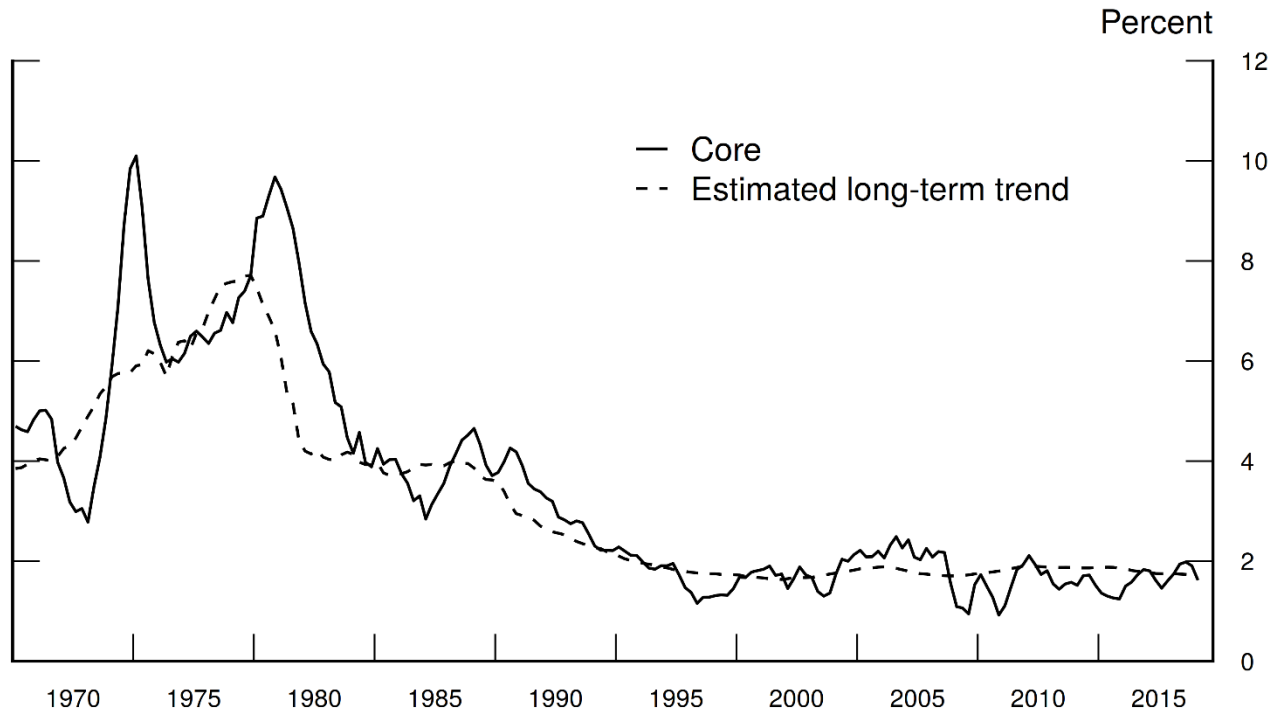


Note: Core inflation is the four-quarter change in the core personal consumption expenditures price index, with data through 2019:Q2.

Source: Bureau of Economic Analysis.

Core Inflation Over the Past 25 Years: Transitory Fluctuations Around a Stable Long-Run Trend

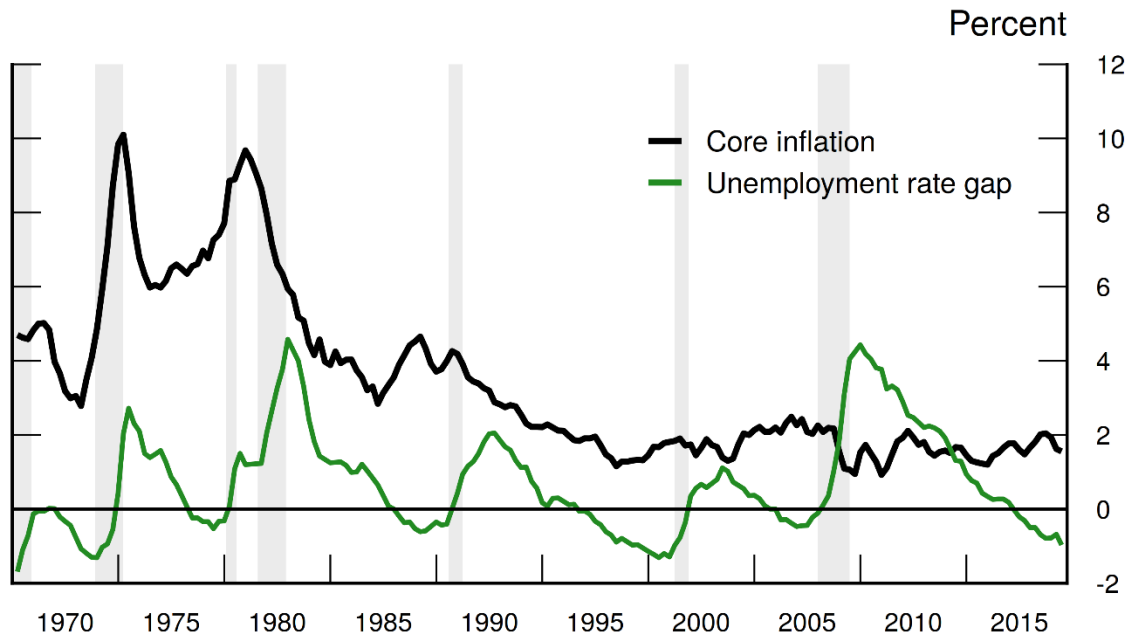
Core PCE Price Inflation Since 1970



Note: Inflation computed as four-quarter percent change.

A Change in the Price Phillips Curve

U.S. Core Inflation and Unemployment Rate Gap

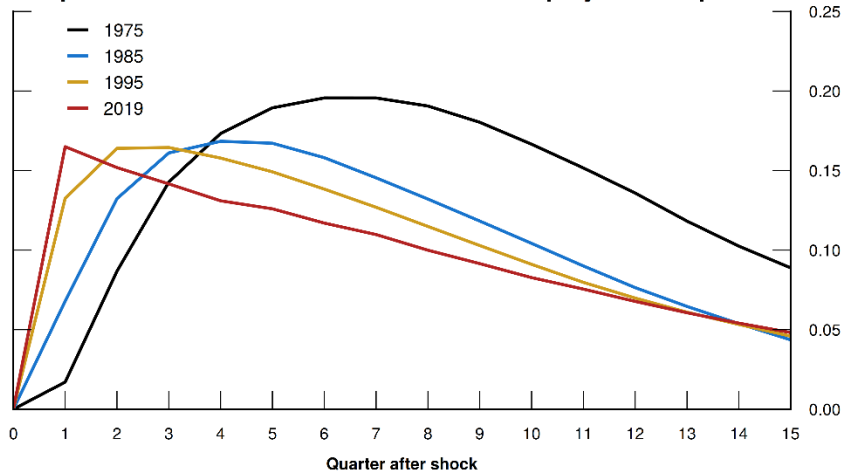


Note: Core inflation is the four-quarter change in the core personal consumption expenditures price index, with data through 2019:Q2. Unemployment rate gap is the difference between the unemployment rate and the short term natural rate of unemployment as estimated by the Congressional Budget Office.

Source: Bureau of Labor Statistics, Bureau of Economic Analysis, Congressional Budget Office.

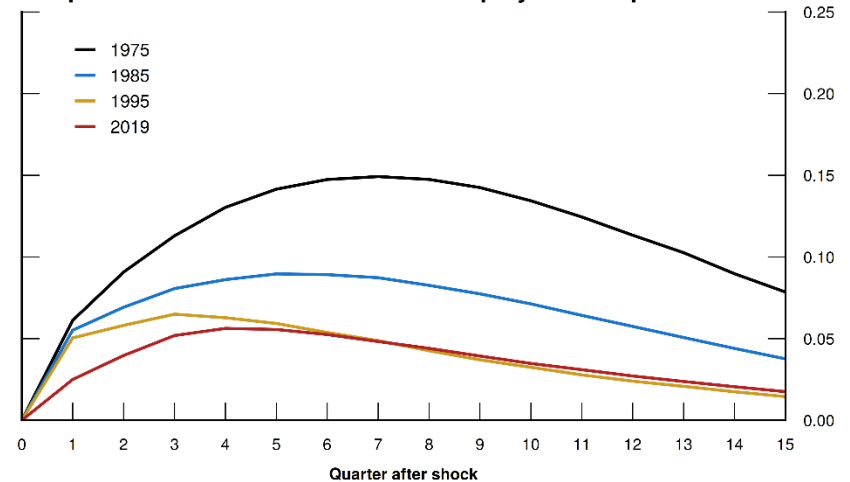
Responses of Unit Labor Costs and Core Inflation to Unemployment Gap Shocks

Response of Labor Cost Growth to an Unemployment Gap Shock



Note: Percentage point deviation from baseline; core inflation defined using market-based PCE price index.

Response of Core Inflation to an Unemployment Gap Shock

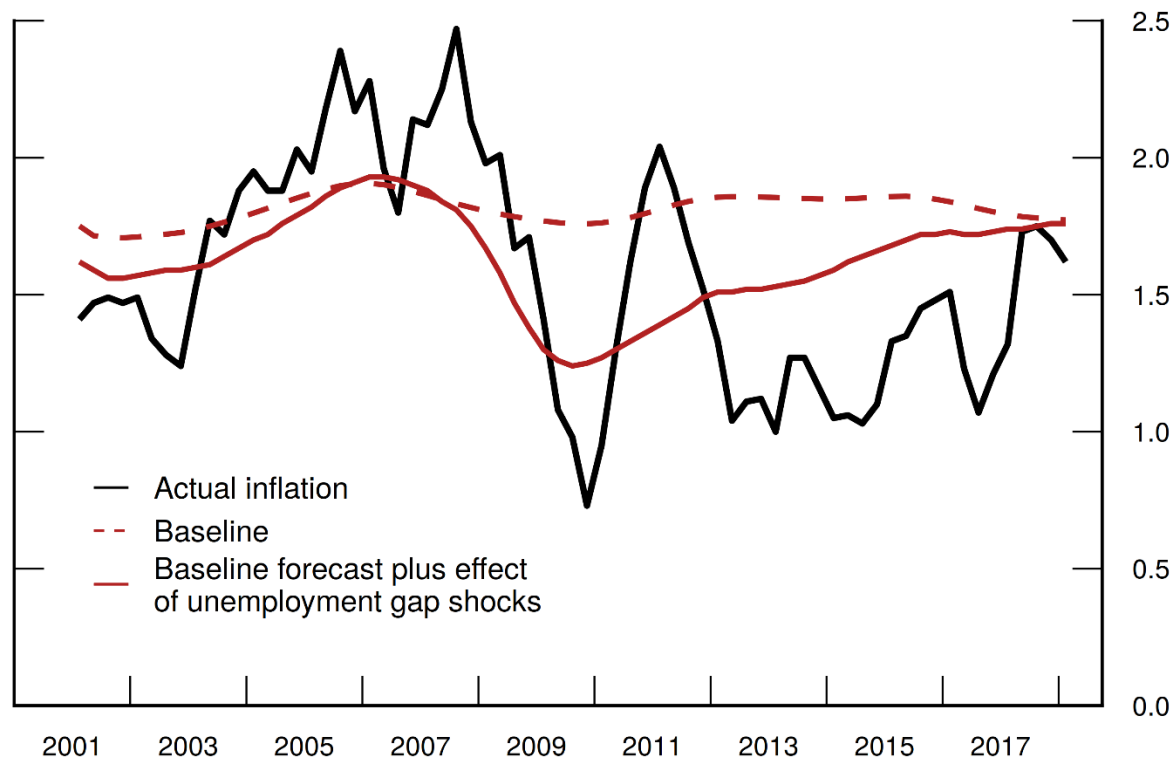


Note: Percentage point deviation from baseline; core inflation defined using market-based PCE price index.

Labor Market Slack: Still an important low-frequency driver of inflation

Decomposition of Core Market-Based PCE Price Inflation

Four-quarter log change, percent



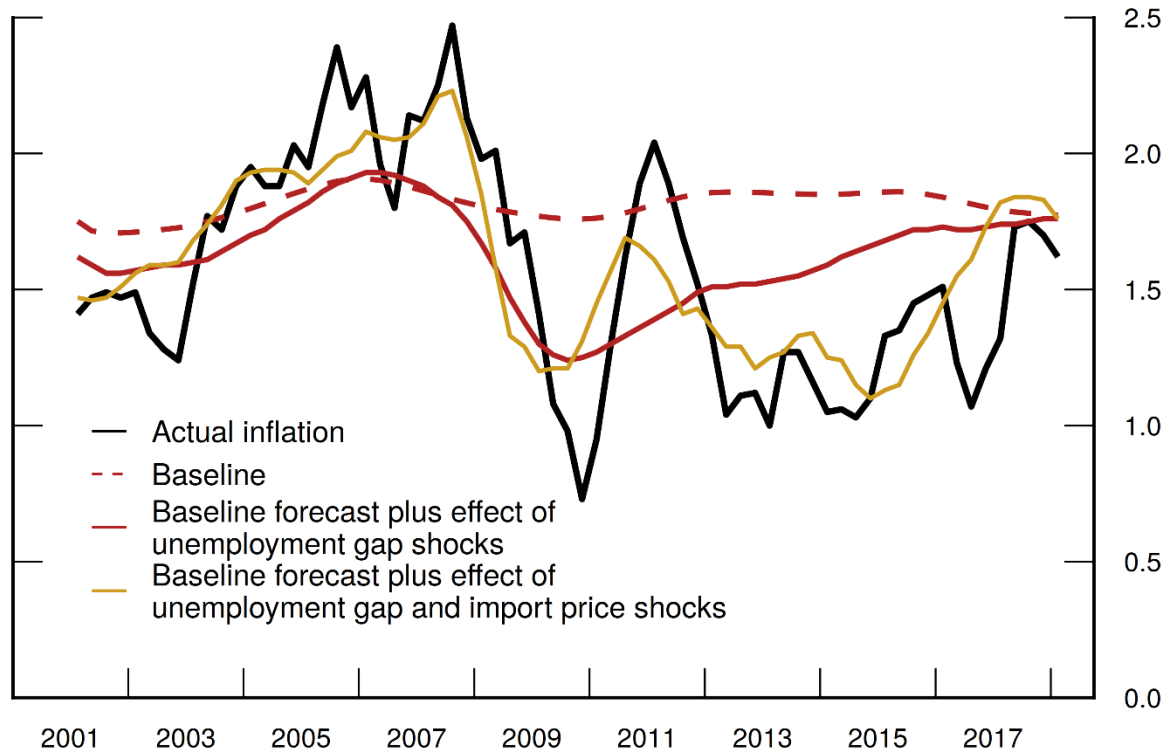
Concluding remarks

- Over the past couple of decades, we have seen two major changes in inflation dynamics:
 - Stable long-run trend
 - Flatter price Phillips curve
- The problem is that we do not have entirely convincing explanations for either change.
- From a policy perspective this is worrisome: Can we rely on these features of the inflation process going forward? Should policy makers try to exploit them?

Appendix

Decomposition of Core Market-Based PCE Price Inflation

Four-quarter log change, percent



Source: Bureau of Economic Analysis.