

## **Beyond the Numbers: Inflation Concerns in the Federal Reserve's Twelfth District**

The Twelfth District of the Federal Reserve System, headquartered in San Francisco and encompassing nine western states—Alaska, Arizona, California, Hawaii, Idaho, Nevada, Oregon, Utah, and Washington, as well as U.S. territories in the Pacific—is an economic powerhouse. Its 30-plus million workers accounted for over 20% of the nation's total nonfarm employment in 2019, and its manufacturers produced almost 20% of the nation's exports in the same year.

Despite the District's strong economic foundations, its businesses and communities—like those in the rest of the country—have felt the pinch of rising prices in recent months. Acknowledging these economic pressures, San Francisco Fed President and CEO Mary Daly has made it clear that inflation is too high. She has emphasized the need for the Federal Reserve to take steps to turn the inflationary tide, including raising interest rates at the FOMC's upcoming March meeting.

To help guide her decision-making about the scale and scope of the Fed's actions, President Daly has stressed the importance of hearing the stories beyond the inflation numbers dominating the headlines. To that end, the San Francisco Fed is listening to and learning from the District's communities and businesses so we can understand how rising prices are affecting household budgets and bottom lines.

In late February 2022, we convened over a dozen listening sessions with business leaders representing the District's leading industries—information technology, professional and business services, construction, food and agriculture, leisure and hospitality—and non-profit organizations that serve and support low- and moderate-income communities and communities of color across the region.

These conversations painted a picture of an economy and households under stress. No sector or industry has been immune from rising prices and pandemic-related supply chain disruptions.

At the same time, listening session participants provided numerous examples of the District's resiliency and well-earned reputation for innovation. Whether it is by adapting logistics to work around material shortages, developing new ways to attract and retain employees, or altering service delivery to meet ongoing community needs, businesses and non-profits have found innovative ways to be flexible and meet a shifting set of challenges.



## Higher Prices across the Board

Businesses and non-profits reported facing higher prices across the board for supplies and materials essential to their operations. Wages have also increased at all points on the wage scale. The type of cost increases that participants cited as important varied from sector to sector. There was one major exception: transportation costs. Regardless of size or industry, businesses reported significant increases in the cost of shipping supplies and finished goods. The increase related to both the pandemic-related disruptions of supply chains as well as hiring challenges that have made it difficult to find drivers and other critical logistics workers.

For all participants, inflation has been a major operational challenge. For non-profits, hiring costs have made it difficult to deliver services. For example, one organization that provides reduced-cost meals noted how the rise in food prices has made it necessary to rethink what they can offer the people they serve. Other organizations have struggled with hiring and retaining staff as the job market has tightened and wages have risen.

All non-profits reported significant concerns about how rising prices are impacting the communities they serve. This is especially true for people who rely on a fixed income or public assistance programs. While their household costs have gone up, their benefits have not. Families who received expanded Child Tax Credits have lost benefits and find themselves in more difficult financial positions today than a year or two ago.

Residents of rural areas have also had a tough time navigating the economic turbulence. They have fewer options when it comes to jobs, healthcare, and utilities like affordable broadband, and they often need to make difficult decisions to prioritize where they spend their money. To illustrate these trade-offs, one leader cited the example of telehealth. For rural residents, telehealth is one of the most efficient ways to access healthcare. However, the ability to take advantage of this option depends on access to affordable broadband. When broadband is expensive, residents must make hard choices about whether to use their internet access for healthcare or to use it for other essential needs like education.

Non-profit leaders also cited the lack of affordable housing as a significant area of concern. Rents are rising at a rate where people can't keep up, and affordable housing developments have slowed due to a variety of reasons including increasing costs of construction materials and labor. Seniors are at particular risk for being priced out of their homes and unable to cover the growing cost of medication, food, and other necessities as prices continue to rise. One nonprofit leader gave an example of a senior whose rent rose \$500, a 38% increase, after remaining stable for years. The same leader noted that they are fielding numerous phone calls from seniors distressed that they may be evicted because they can't afford their rent.

All businesses reported disruptions to their industries and to their specific operations. These ranged from delayed capital investment to reduced services to closures. At the same time, the scale and scope of these disruptions varied by a number of factors, including the size and sector of the business and the level of demand for its products or services.



## Confronting Increased Costs

Large, vertically integrated businesses that could negotiate goods and services contracts have been able to successfully hedge against some of the rising prices. This option has been less frequently open to smaller businesses or start-ups. As a result, they have borne the full brunt of price increases for materials and other inputs.

While some businesses reported passing a certain percentage of the cost increases to consumers, those industries that enjoyed strong consumer demand were able to pass on a greater percentage of costs. Generally, companies noted the decisions to pass on costs had to be balanced with the competitive disadvantage price increases bring with them.

Faced with increased costs, non-profits must confront a unique set of challenges. The costs of providing services have risen. These organizations have also seen an increase in the demand for their services as more households face economic challenges. Yet unlike private companies, they cannot pass on costs to the communities they serve. Faced with this dilemma, they have sought more funding from grants and donations. They have also explored sharing services with other non-profits to meet increased demand.


## The Future of Wages and Work

The majority of session participants noted the difficulty posed by wage increases and labor shortages. At all levels of the wage scale, organizations must deal with intensified competition for talent, and it has become more difficult to attract and retain workers. Where possible, companies and non-profits have raised wages and adjusted wage scales, sometimes multiple times per year. Where this is cost-prohibitive, they have focused on other types of compensation and benefits, including allowing more remote work options, increasing training and job development, and offering retirement fund matching programs.

Looking ahead, most participants felt that the gains in wages and the changes in working conditions—especially the increase in remote work—are here to stay. While non-profit leaders noted that the wage gains were overall a very positive development, they also cautioned that they were uneven. Small or micro-business owners were less likely to see an increase in income, given the rise in prices. Low-wage workers may have seen their income go up but not enough to counteract the pressures of rising costs.

Businesses that depend on the skilled trades and other types of highly trained employees said that labor shortages had focused new attention on the long-term deficits in the country's approach to workforce development. They shared that their attempts to solve labor shortages for high-skilled workers were more difficult because younger generations of workers have not had access to apprenticeship and training programs. As a result, they lack the skills to qualify for these generally well-compensated jobs.

Non-profit leaders were especially keen to point out that the economic dislocations of the pandemic and the subsequent increases in inflation exacerbated certain other long-standing social and economic problems. The lack of affordable housing, child care, health care, and pathways to high-skilled jobs are issues that low-to-moderate-income communities and



communities of color have experienced long before the spike in inflation. While lowering prices would help address some of the immediate crises facing individuals today, leaders said the nation needs systemic solutions to create an economic system that truly works for every individual and family.

## Looking Forward

When asked about their outlook for the future, most participants felt that inflation well above the Fed's 2% target would persist for the next couple of years. When asked to look three to five years out, participant opinions were more varied. Some leaders see price increases and supply chain challenges lasting a considerable amount of time while others feel prices would stabilize more quickly.

## A Community-engaged San Francisco Fed

The San Francisco Fed succeeds when we meet the needs of the people we serve across the Twelfth District. Our recent listening sessions have been valuable, deepening our understanding of inflation's impact on operations, lives, and livelihoods. With the help of these insights, the Federal Reserve can help shape a monetary policy that addresses these inflation concerns and supports an economy that works for everyone.