

# Shocks and Monetary Policy: Assessing Conventional Wisdom



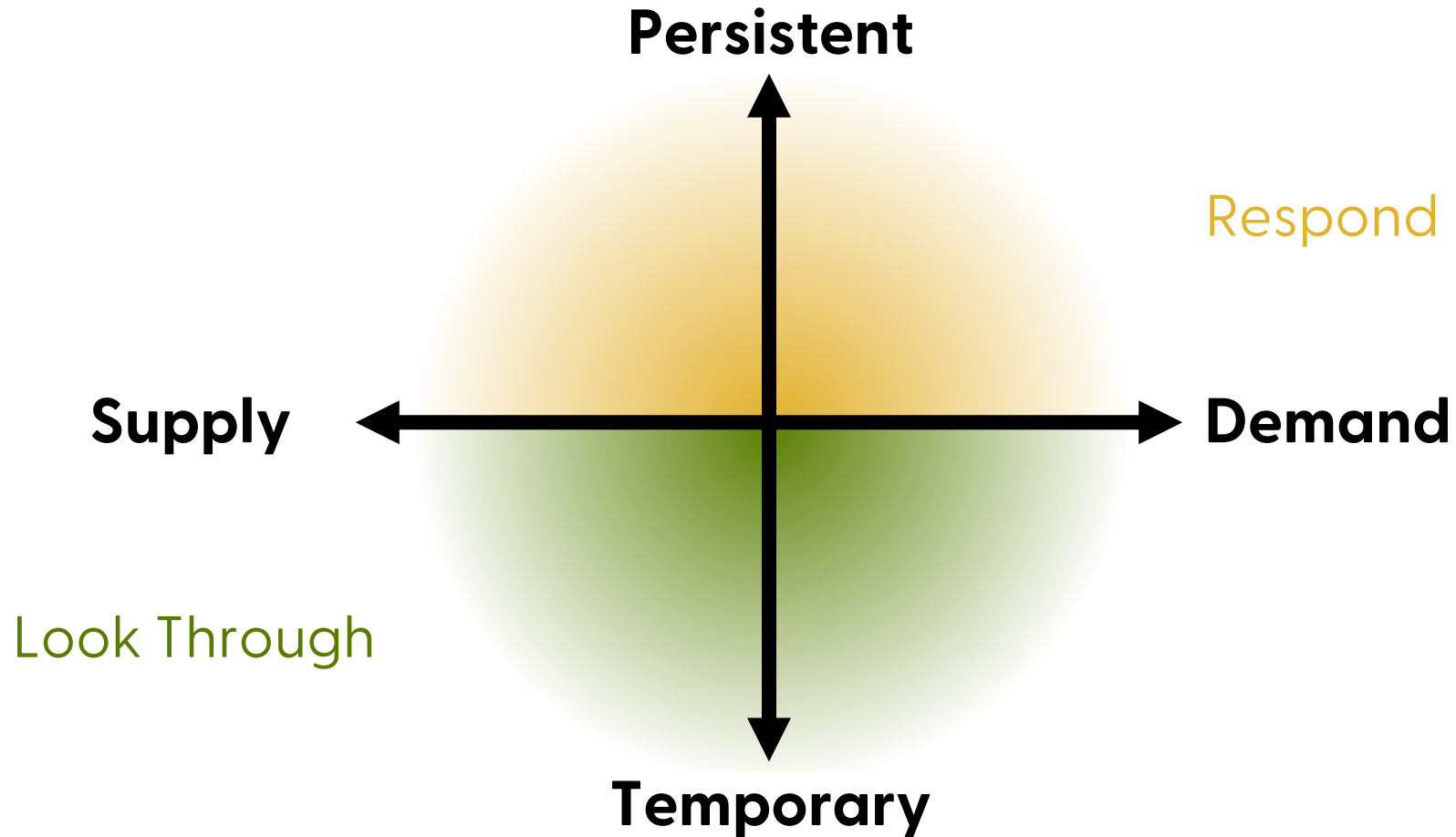
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*Views expressed are those of the presenter and not necessarily those of the Federal Reserve Bank of San Francisco or the Federal Reserve System.*

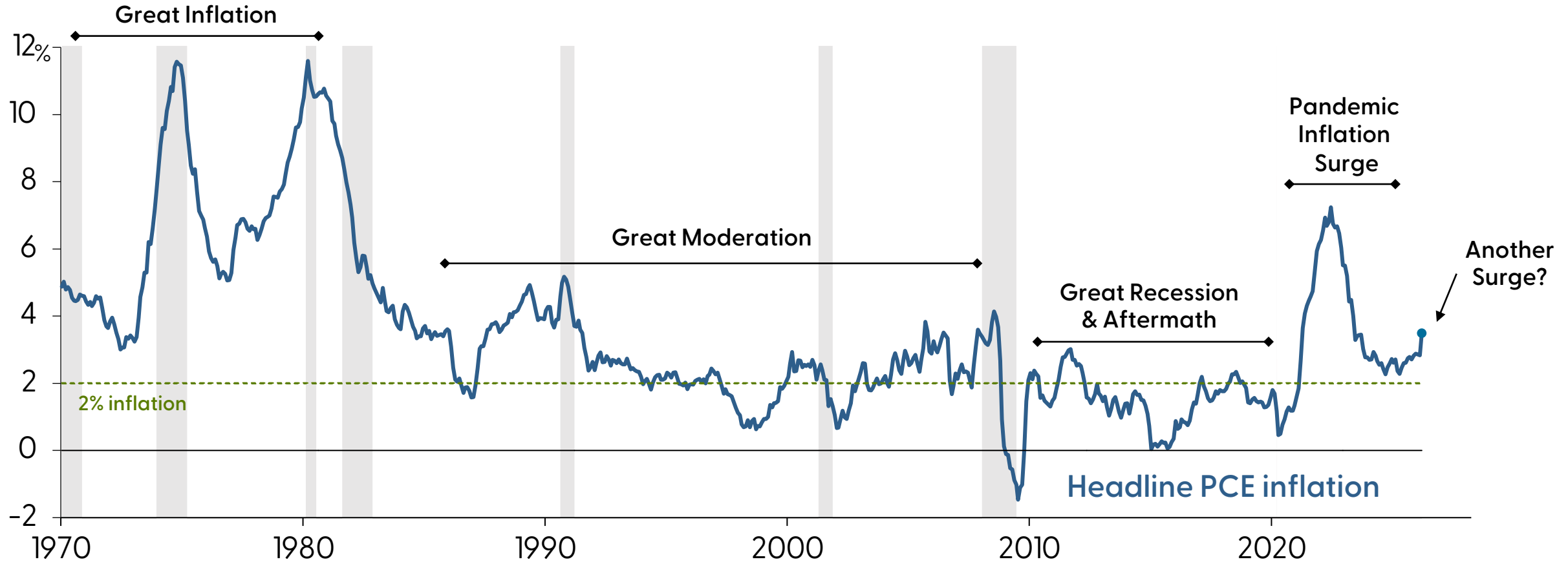
# Conventional Wisdom

## Taxonomy of Inflation Shocks



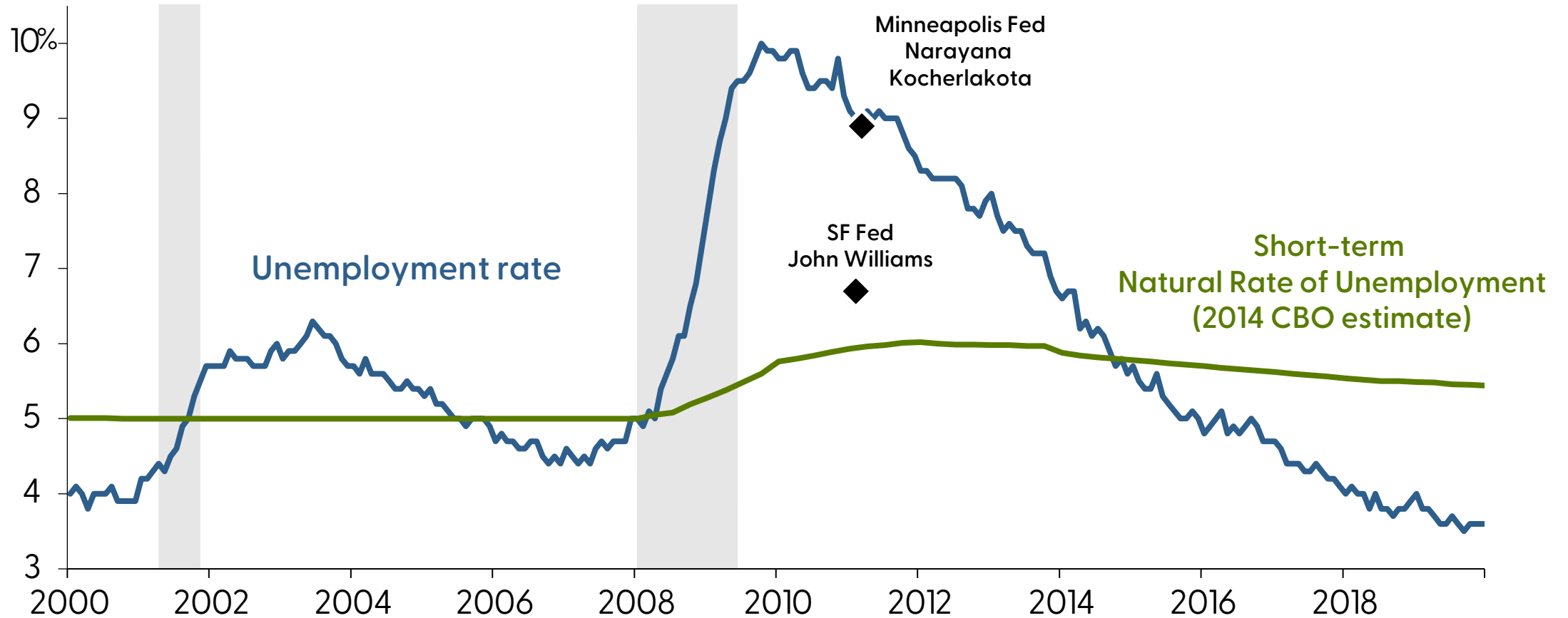
# Recent Inflation Shocks

## Headline PCE Price Index, 12-Month Change



# Labor Market: Cyclical or Secular?

## Unemployment Rate and Short-run U\* Estimate, 2014 Vintage



Note: 2014 vintage via St. Louis Fed's ALFRED. Williams and Kocherlakota both presented a range of estimates in early 2011 between 6.1-7.7% and between 5.9-8.9%, respectively.

Source: Bureau of Labor Statistics, Congressional Budget Office, San Francisco Fed, and Minneapolis Fed.

# Start with More Data

## San Francisco Fed Labor Market Heat Map

No.	Indicator	79	80	81	82	83	84	85	86	87	88	89	90	91	92	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07	08	09	10	11	12	13	14	Aug-12	Now	Date
	Recession																																							
<u>Headline series</u>																																								
1	Unemployment gap																													1.26	.38	8/14								
2	Payroll employment																													-.09	-.54	8/14								
<u>Williams' original alternative measures of slack</u>																																								
3	Employment to population gap																													1.42	1.00	8/14								
4	Jobs gap (Conference Board)																													.99	.08	8/14								
5	Capacity utilization																													.70	.12	7/14								
6	Output gap																													1.36	.35	6/14								
7	Job openings rate																													-.04	-1.43	6/14								
8	Job openings hard to fill																													.46	-.56	7/14								
<u>Survey indicators</u>																																								
9	ISM Composite Index																													.05	-1.45	8/14								
10	ISM Manufacturing: PMI Composite Index																													.11	-1.21	8/14								
11	ISM Manufacturing: Employment Index																													-.69	-1.47	8/14								
12	ISM: Nonmanufacturing: Employment Index																													-.48	-1.28	8/14								
13	NFIB Firms expanding employment next 3 months																													-.01	-.53	7/14								
14	NFIB Businesses w/ Increase in Employment in La																													-.36	-.53	7/14								
15	CB Labor market expectations - fewer jobs																													.67	-.57	8/14								
16	CB Labor market expectations - more jobs																													-.01	-.36	8/14								
<u>Unemployment insurance related</u>																																								
17	Initial Claims																													-.10	-1.07	8/14								
18	Continuing claims																													.93	-.57	7/14								
19	Insured unemployment rate																													-.14	-1.09	7/14								
<u>Labor turnover</u>																																								
20	Quits rate																													.84	.03	6/14								
21	Job finding rate (Shimer)																													1.57	.92	7/14								
22	Hires rate																													.61	.11	6/14								
<u>Payroll survey</u>																																								
23	Private payroll employment																													-.18	-.59	8/14								
24	Temp help employment																													-.11	-.47	8/14								
25	Average weekly hours																													1.14	.97	8/14								
26	Average Hourly Earnings																													1.32	.65	8/14								
<u>Household survey</u>																																								
27	Household employment																													.43	-.35	8/14								
28	Part time econ reasons (% of emp)																													1.07	.51	8/14								
29	Long-term unemployment																													2.19	1.26	8/14								
30	Labor force participation rate																													1.37	2.78	8/14								

Note: Red means level above historical mean, green means below. Units of measurement are historical sample standard deviations from mean

# Discipline with Analysis

Daly, Hobijn, Şahin, Valletta (JEP, 2013)

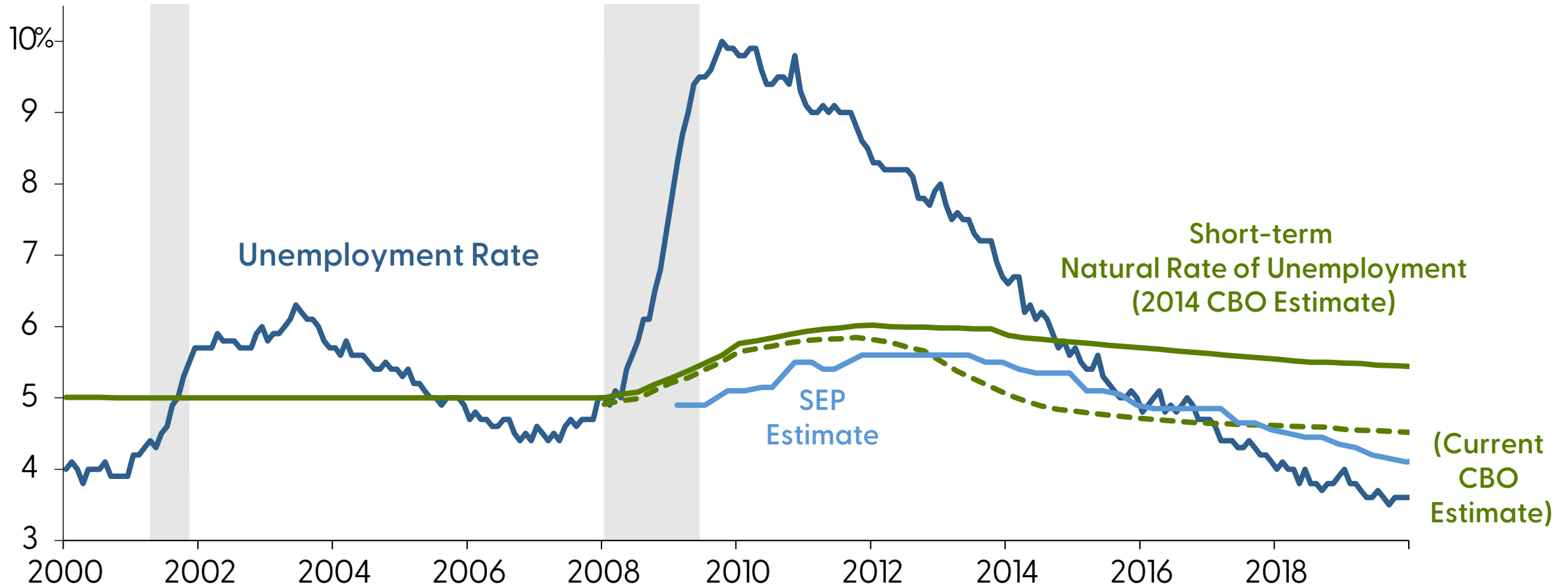
*Table 1*

**Factors that Move the Beveridge Curve (BC) and the Job Creation Curve (JCC)**

<i>Shifter</i>	<i>JCC</i>	<i>BC</i>	<i>Transitory or Permanent</i>
<i>Cyclical factors</i>			
Shortfall in aggregate demand	↓		Transitory
Elevated layoffs rate	↓	⇒	Transitory
<i>Structural/Noncyclical factors</i>			
Decrease in match efficiency (mismatch)	↓	⇒	Mostly transitory
Increased generosity of unemployment insurance	↓	⇒	Transitory
Uncertainty	↓	⇒	Transitory

# Over Time, Views Evolved

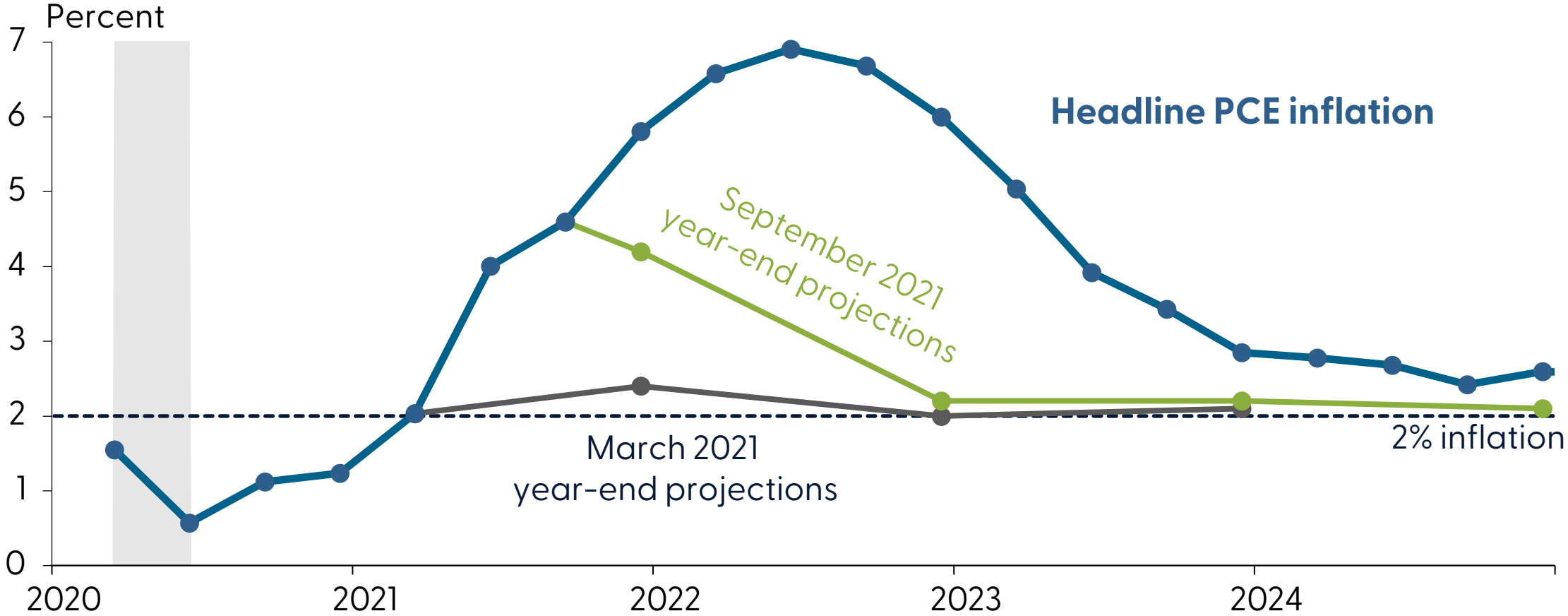
## Unemployment Rate and Natural Rate of Unemployment



Note: 2014 vintage via St. Louis Fed's ALFRED. Current CBO and SEP lines represent long-run estimates. SEP estimate is the central tendency midpoint. Source: Bureau of Labor Statistics, Congressional Budget Office, and Federal Reserve Board of Governors.

# Inflation: Temporary or Persistent?

## Evolution of Median SEP Inflation Projections

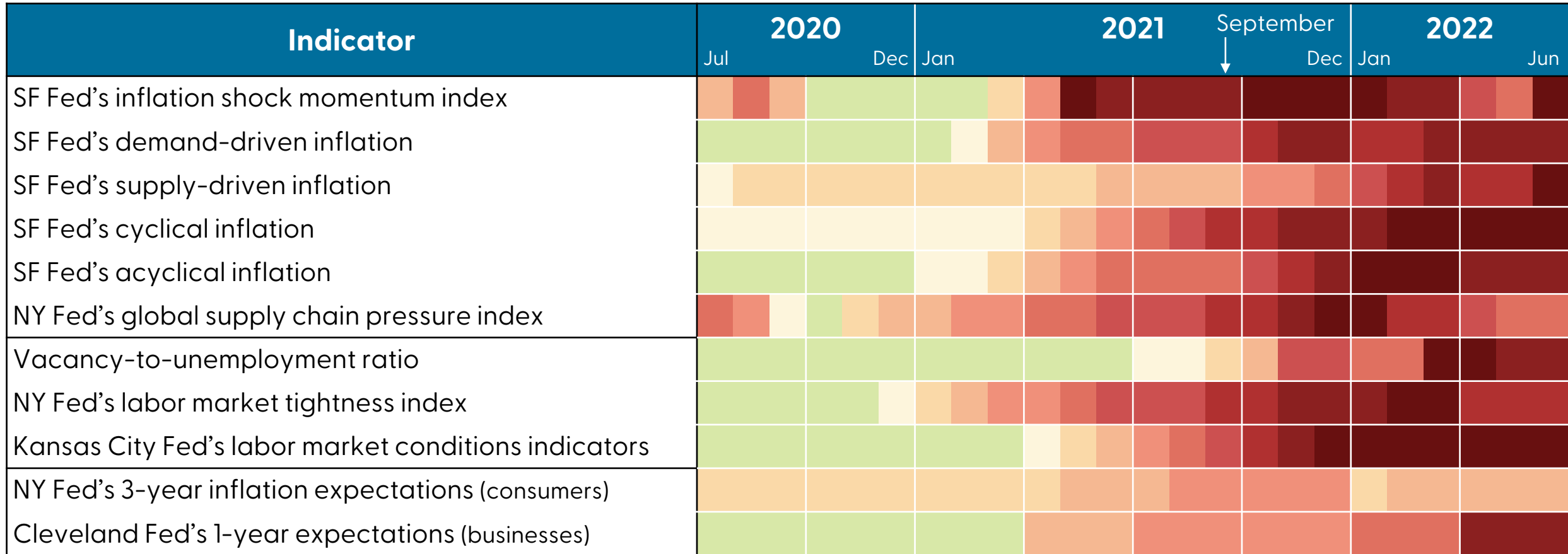


# Traditional Inflation Gauges

Inflation	Inflation Expectations
Headline and Core PCE	New York Fed Survey of Consumer Expectations
Headline and Core CPI	University of Michigan Surveys of Consumers
Dallas Fed's trimmed mean PCE	Philly Fed Survey of Professional Forecasters
Cleveland Fed's median PCE and median CPI	Cleveland Fed Survey of Firms (SoFIE)
Producer Price Index (PPI)	Financial Market Based Measures (TIPS)
Employment Cost Index (ECI)	FRB Index of Common Inflation Expectations

# Monitoring Inflation Pressures

## Inflation Pressures Heat Map, 2020-22



# Applying to Current Moment

## Inflation Pressures Heat Map, 2025-26

Indicator		2025				2026			
		Jan	Apr	Jul	Oct	Jan	Feb	Mar	Apr
Core goods as share of total PCE inflation	<b>Tariff shock</b>	Light Green	Light Green	Light Yellow	Light Yellow	Light Orange	Light Orange	Light Orange	Light Orange
Import prices index		Light Green	Light Green	Light Green	Light Green	Light Orange	Light Orange	Light Orange	Light Orange
Crude oil futures prices (3-6 months ahead)	<b>Oil shock</b>	Light Orange	Light Orange	Light Green	Light Green	Light Green	Light Green	Light Green	Light Green
NY Fed's global supply chain pressure index		Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange
SF Fed's inflation shock momentum index	<b>Both shocks</b>	Light Green	Light Green	Light Green	Light Green	Light Green	Light Green	Light Green	Light Green
Global commodities prices (e.g., aluminum)		Dark Red	Dark Red	Dark Red	Dark Red	Dark Red	Dark Red	Dark Red	Dark Red
Vacancy-to-unemployment ratio		Light Yellow	Light Yellow	Light Yellow	Light Green	Light Green	Light Green	Light Green	Light Green
NY Fed's labor market tightness index		Light Yellow	Light Yellow	Light Yellow	Light Green	Light Green	Light Green	Light Green	Light Green
Kansas City Fed's labor market conditions indicators		Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange
NY Fed's 3-year inflation expectations (consumers)		Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange
Cleveland Fed's 1-year expectations (businesses)	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	Light Orange	