

The Progressive Benefits and Retreating Risks of High-Pressure Labor Markets

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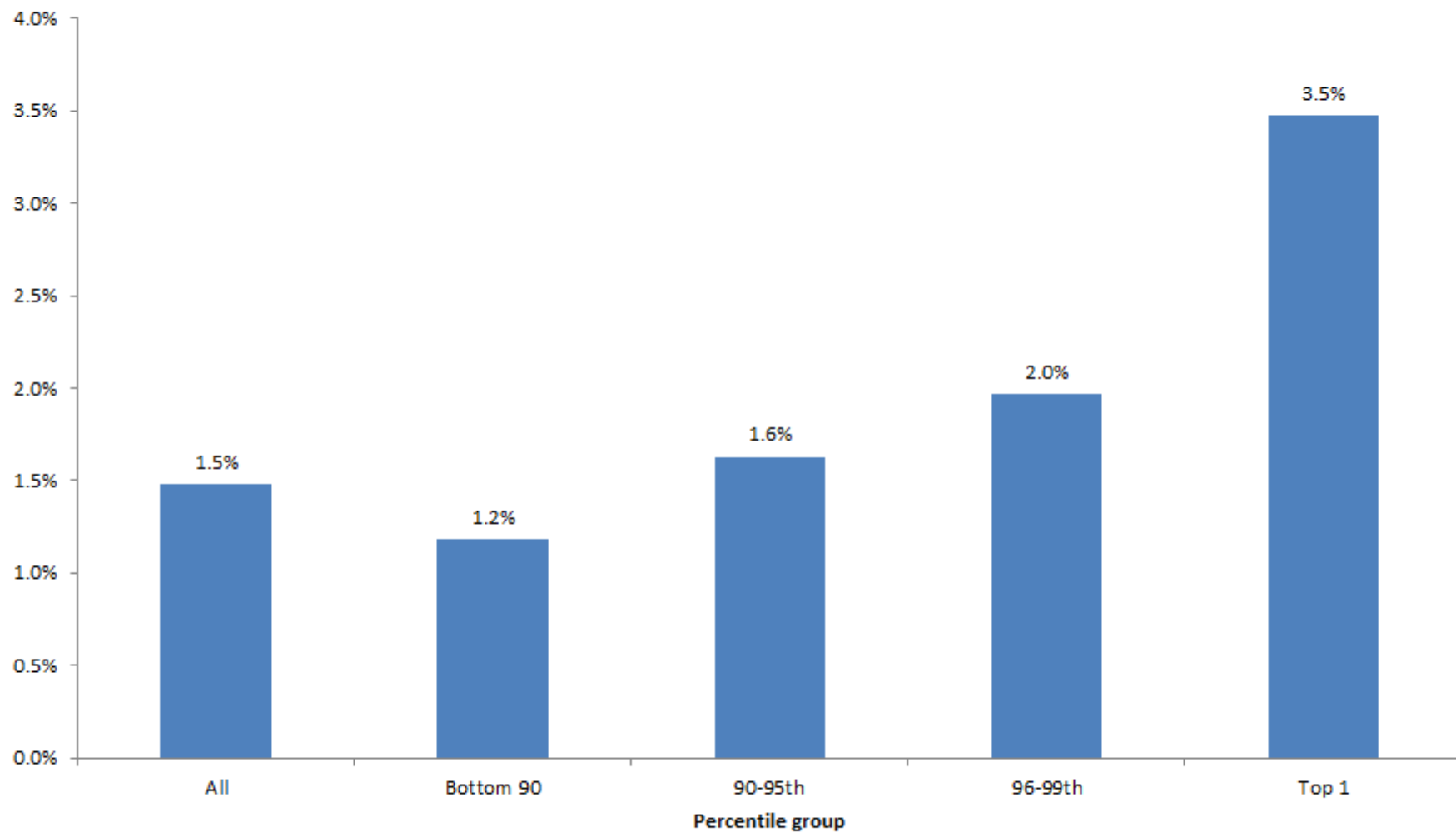
Remarks for a conference at the
Minneapolis Federal Reserve Bank's
Institute for Opportunity and Inclusive Growth

Macroeconomic stabilization policy has played a significant role in the rise of inequality

- Failing to hit an already too-conservative NAIRU target contributed to sluggish wage growth for low/middle wage workers
- These workers – and others lacking strong bargaining power and leverage (especially workers of color) – benefit more when labor markets get tight
- While the benefits of high-pressure labor markets are hence large and progressive, ample evidence that the risks of targeting high-pressure labor markets have relented in recent decades
- Reduced bargaining power and leverage of workers (even aside from too-loose labor markets) has removed potential tinder that could have supported a wage-price spiral

(I) Role of macroeconomic stabilization failures in generating inequality

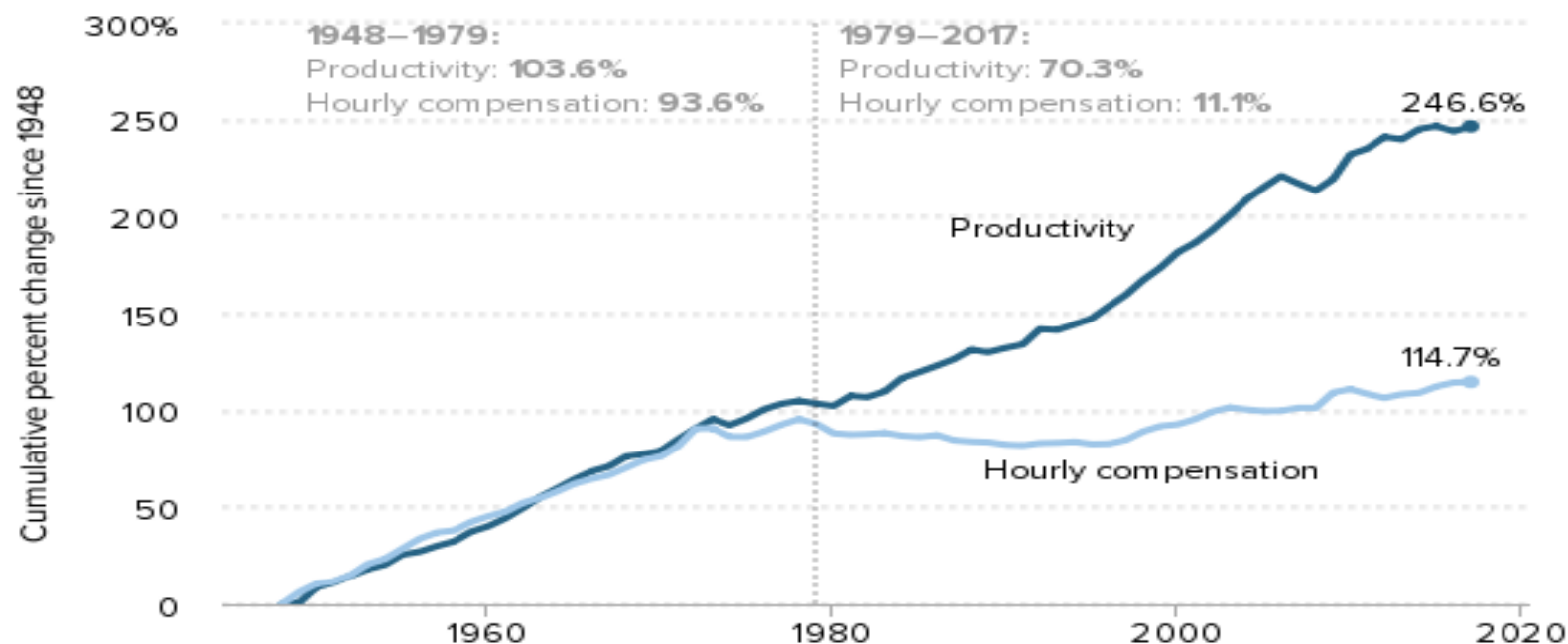
Familiar stair-step of income growth, Average annualized growth rate of comprehensive, post-tax income, 1979-2015



Note: Author's analysis of data from the Congressional Budget Office (2018), The Distribution of Household Income, 2015

Productivity grew six times faster than hourly compensation between 1979 and 2017

Productivity growth and hourly compensation growth, 1948–2017

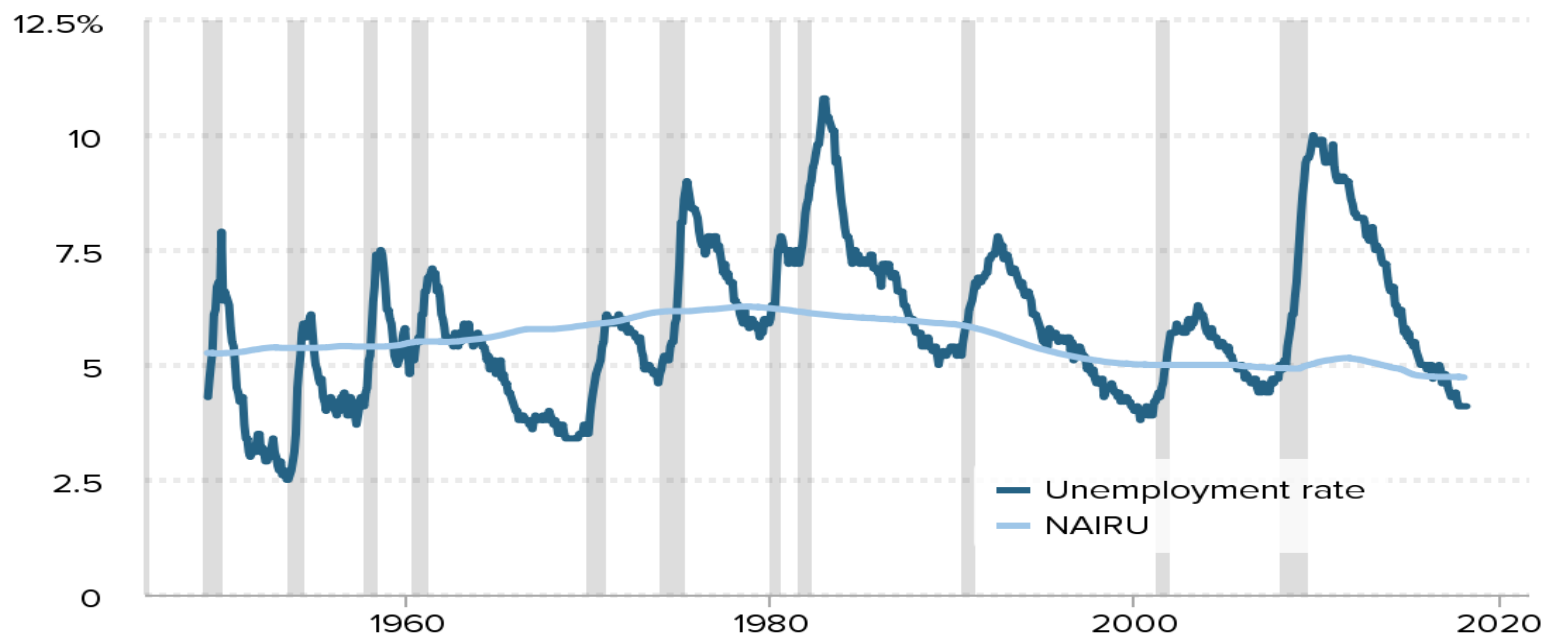


Notes: Data are for compensation (wages and benefits) of production/nonsupervisory workers in the private sector and net productivity of the total economy. “Net productivity” is the growth of output of goods and services less depreciation per hour worked.

Source: EPI analysis of Bureau of Labor Statistics and Bureau of Economic Analysis data. Updated from Figure A in Bivens et al. 2014.

There has been insufficient vigilance in fighting unemployment since the late 1970s

Estimate of the natural rate of unemployment and actual unemployment, 1949–2018

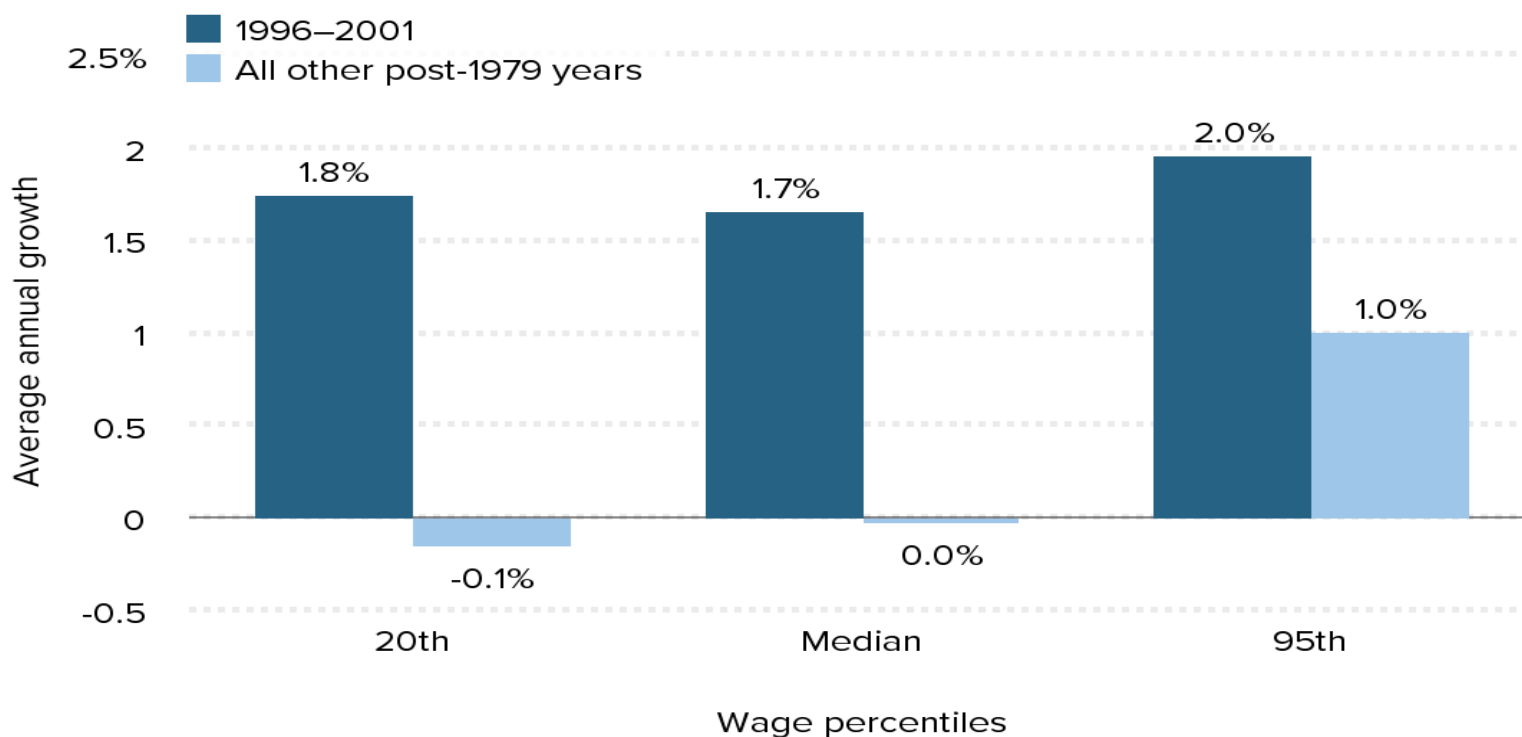


Note: NAIRU refers to the nonaccelerating inflation rate of unemployment (another term for the natural rate of unemployment).

Source: Data on the natural rate of unemployment from the Congressional Budget Office (2018); data on actual unemployment rate from the Bureau of Labor Statistics (2018). Shaded areas represent recessions.

The only period of high pressure in the labor market since 1979 led to rapid wage gains

Average annual wage growth from 1996–2001 vs. all other years between 1979 and 2017



Note: Wage growth is inflation-adjusted.

Source: Authors' calculations from data obtained from the State of Working America Data Library from the Economic Policy Institute (EPI 2018)

(II) Progressive benefits of high-pressure labor markets

Low- and middle-wage workers' wages grow more quickly in response to an improving labor market than high-income workers' wages

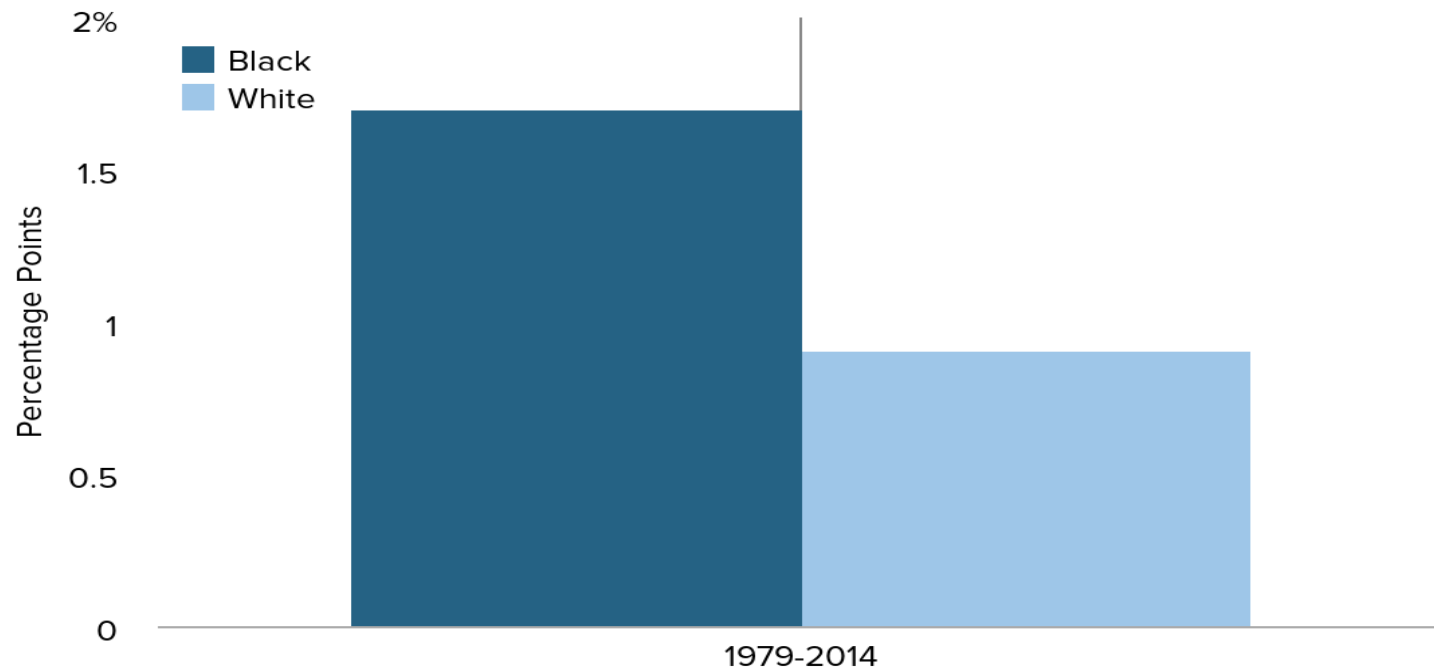
Change in average annual real wage growth in response to a 1-percentage-point increase in unemployment or employment rates over the 1980–2016 period, by wage percentile



Notes: Each bar is the coefficient from the regression of the real annual percent change in a given percentile's wage on the measure of labor market tightness. Regressions include state and year fixed effects. Additional details and estimates are in the appendix. EPOP refers to the employment-to-population ratio; prime-age refers to adults ages 25–54.

Source: Authors' analysis of annual, state-level aggregations of Current Population Survey Outgoing Rotation Group microdata, 1979–2016

Percentage Point Change in Black and White Unemployment Rates for a 1 Percentage Point Change in the National Unemployment Rate, 1979-2014

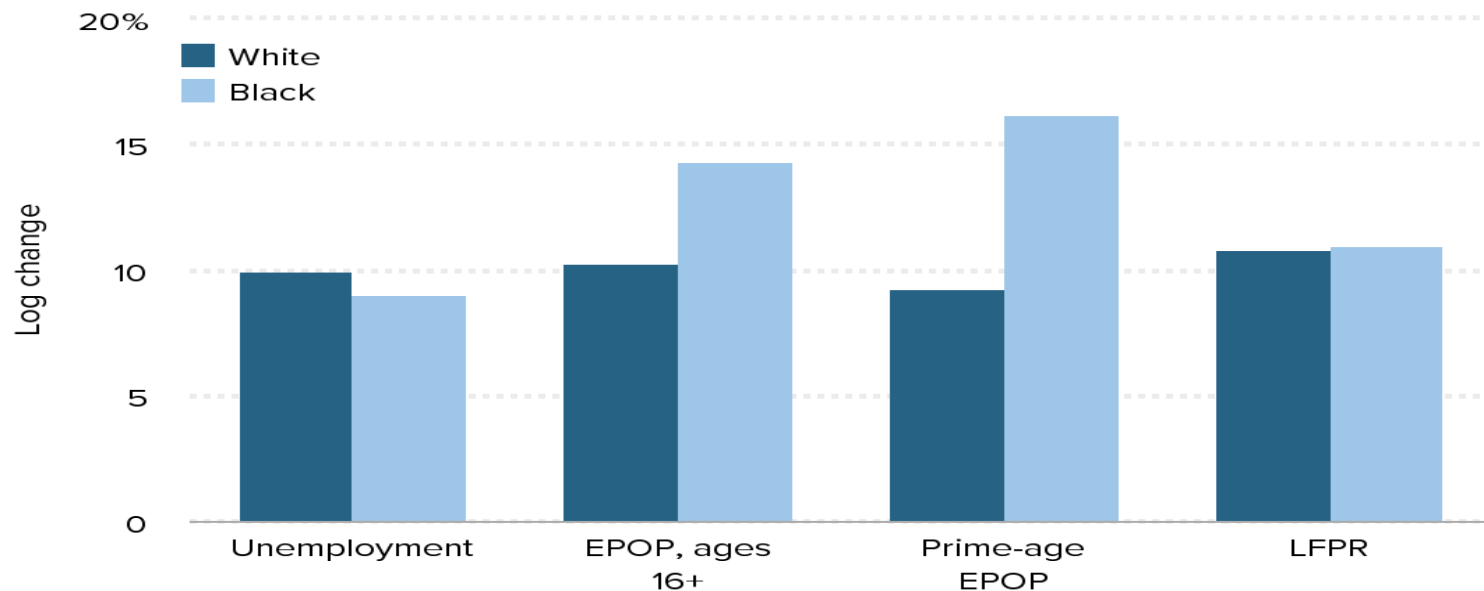


Source: Author's analysis of Bureau of Labor Statistics' Current Population Survey.

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High-pressure labor markets erode race-based gaps in employment-to-population ratios

Changes in race-specific labor market indicators stemming from a 10-percent change in the overall indicator

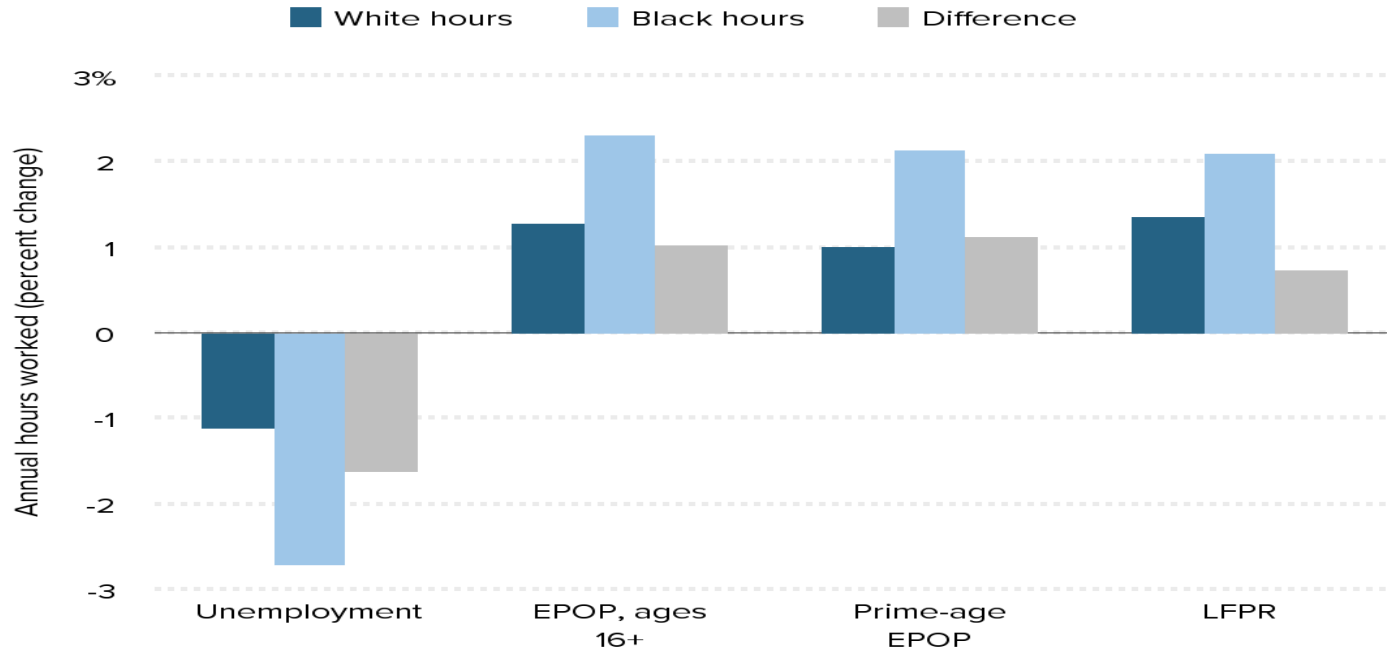


Notes: Each bar shows the coefficient from the regression of the log of a group-specific labor market outcome on the log of the overall labor market outcome. Regressions include state and year fixed effects. Additional details and estimates are in the appendix. EPOP refers to the employment-to-population ratio; prime-age refers to adults ages 25–54; and LFPR refers to the labor force participation rate of people ages 16 and older.

Source: Authors' analysis of annual, state-level aggregations of Current Population Survey data, 1979–2016

High-pressure labor markets narrow race-based gaps in hours worked

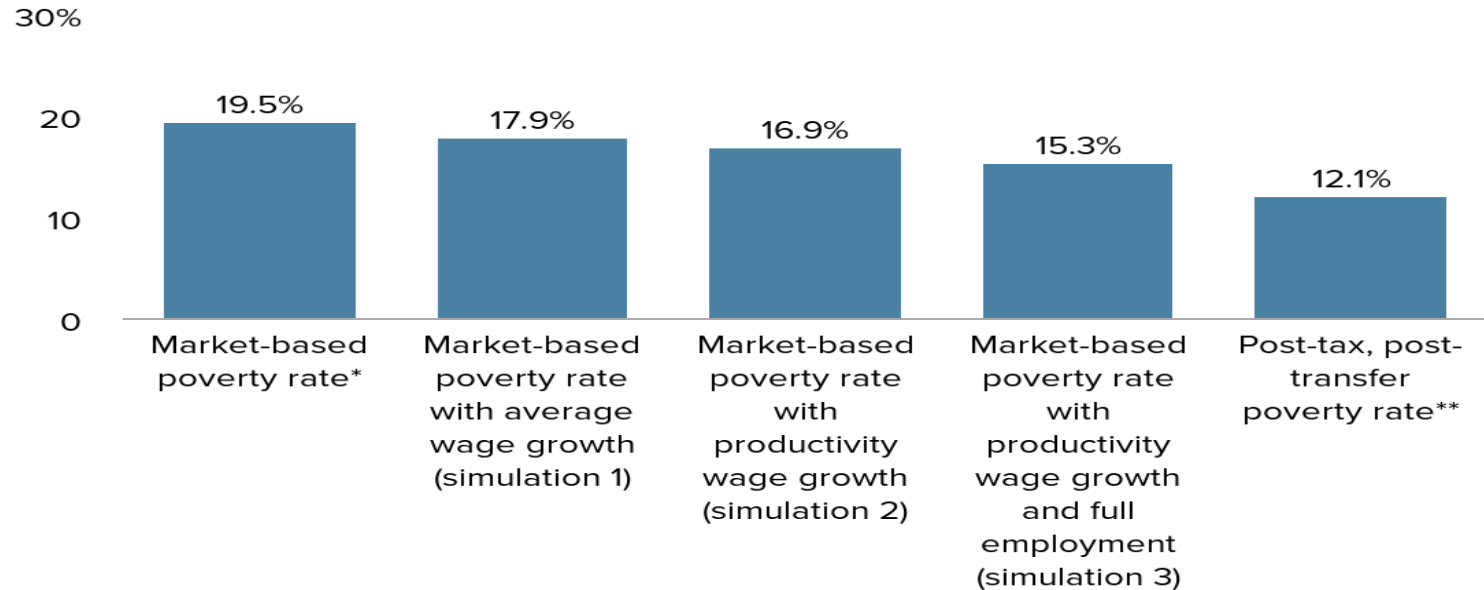
Changes in annual household hours worked in response to a 1-percentage-point increase in the specified labor market indicator, by race



Notes: Each bar is the coefficient of the regression of the race-specific log of average annual household-level hours worked on the overall labor market tightness outcome. Regressions include state and year fixed effects. Additional details and estimates are provided in the appendix. EPOP refers to the employment-to-population ratio; prime-age refers to adults ages 25–54; and LFPR refers to the labor force participation rate of people ages 16 and older.

Source: Authors' analysis of annual, state-level aggregations of Current Population Survey data, 1979–2016

Market-based non-elderly poverty rate in various scenarios, 2013



* Measurement of market poverty rate with income excluding the following income components: veterans payments, public assistance, supplemental security, Social Security, workers compensation, and unemployment compensation.

** Measurement of post-tax, post-transfer poverty rate that adds the following variables to income: EITC credits, SNAP benefits, housing subsidies, and energy subsidies (LIHEAP).

Source: EPI analysis of Bureau of Labor Statistics unpublished Total Economy Productivity data, Bureau of Economic Analysis National Income and Product Accounts Table 1.7.6, and Current Population Survey Annual Social and Economic Supplement data

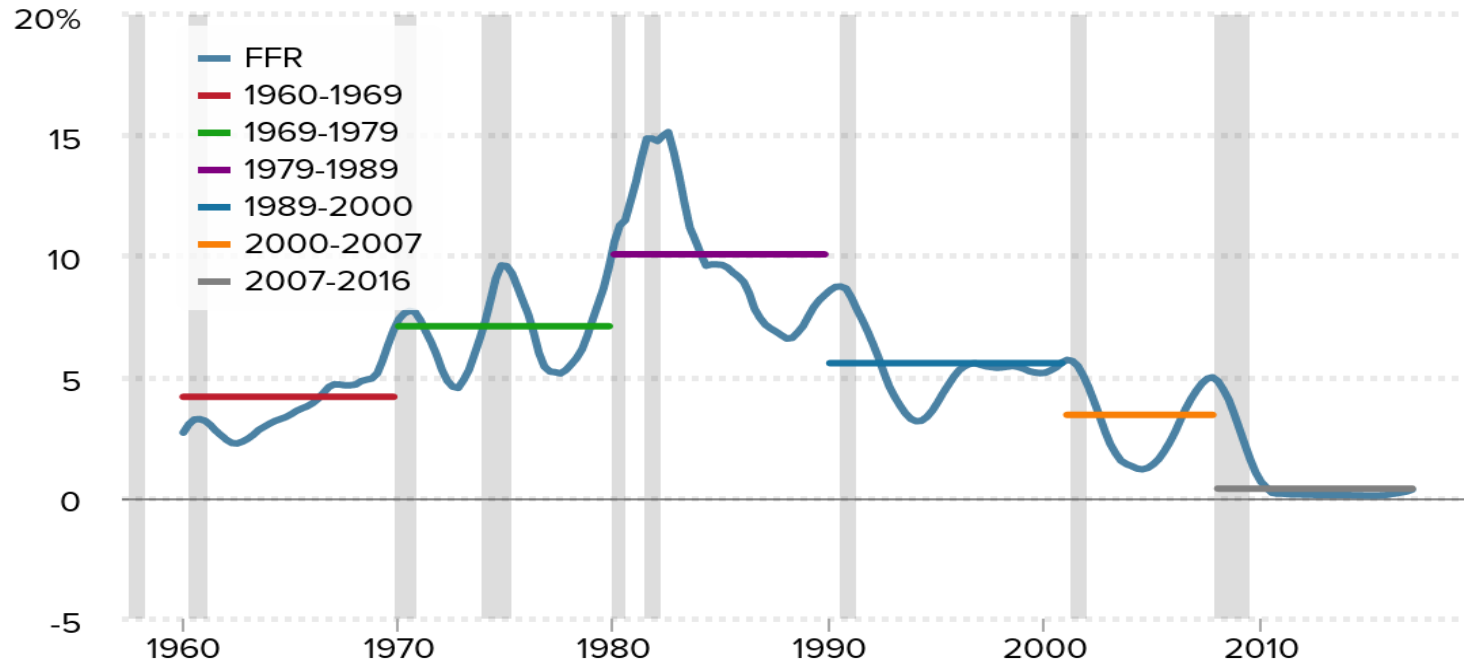
(III) Retreating risks from pursuing
high-pressure labor markets

Not that 70s show: Far less tinder for wage-price spirals

	1965-1969	1979-2007	2007-2018
Productivity growth, 10-year average	2.9%	1.5%	1.4%
Real wage growth, 10-year average	2.5%	0.2%	0.6%
Unemployment, period average	3.8%	6.1%	6.9%
Unionization rates, period average	26.9%	16.2%	12.6%
Unionization rates, average annual % change over period	1.2%	2.6%	1.2%
Federal minimum wage, % of AHE	46.5%	36.5%	35.2%
LDC import share	< 0.9%	3.9%	6.3%

Clear decline in interest rates signals Fed is coping with slowing demand growth

Effective federal funds rate, actual and business cycle averages, 1960–2016

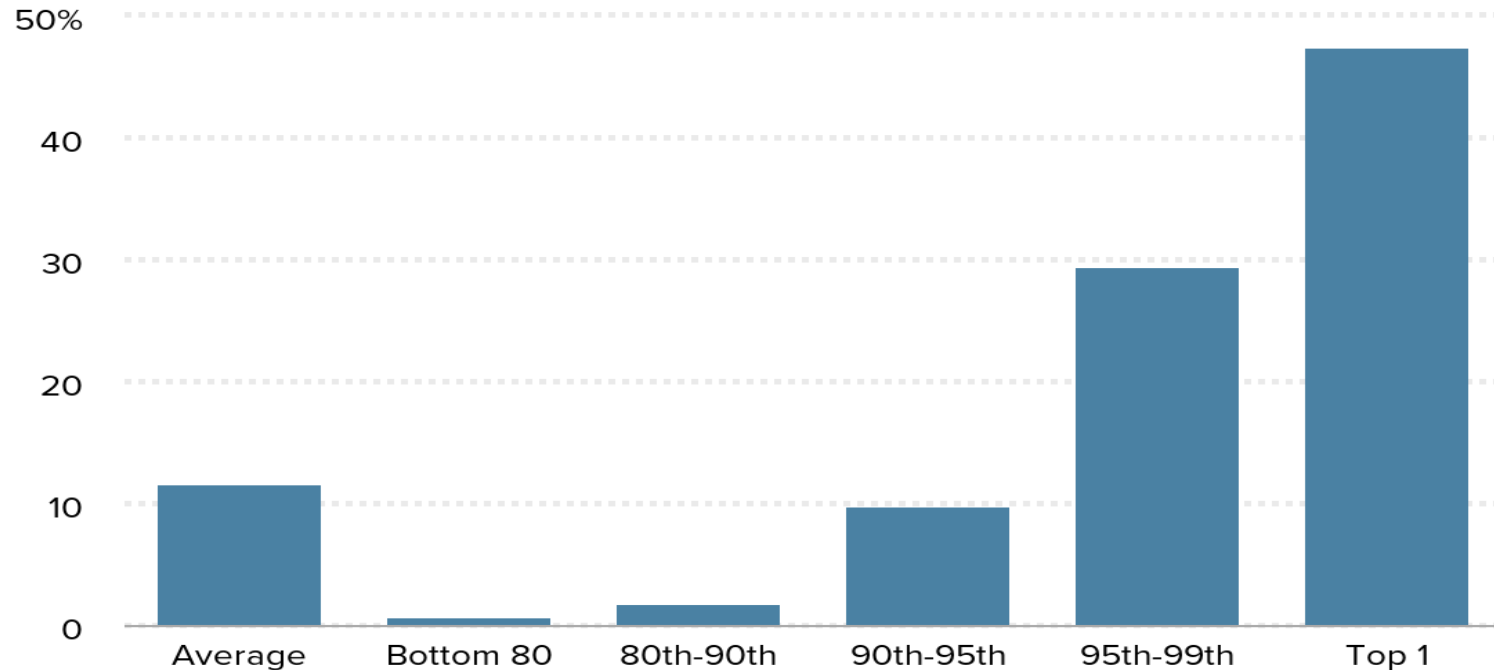


Notes: Data are quarterly averages. Horizontal lines are averages over dates indicated. Shading indicates recessions.

Source: Author's analysis of [Effective Federal Funds Rate data](#) accessed from [FRED database](#) in [September, 2017](#)

Higher-income households have much higher savings rates

Savings as share of income by income percentiles, 1989-2013 averages



Notes: Construction of the data is described in the appendix.

Source: Author's analysis of data from the Federal Reserve Board's Survey of Consumer Finances (SCF), the Federal Reserve Board's Financial Accounts of the United States (FAUS), and Congressional Budget Office data on household income and effective tax rates (CBO 2016)

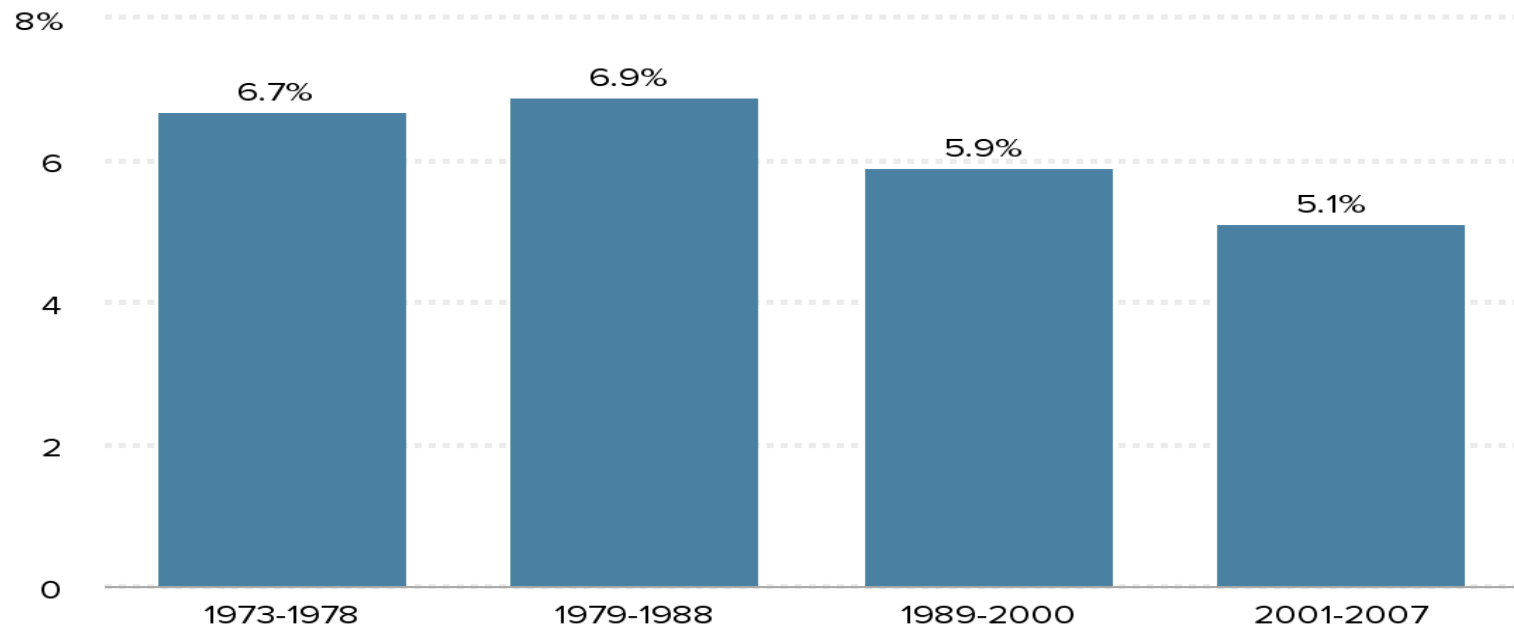
Should macro policymakers care about a decline in workers' leverage and bargaining power?

“Another consideration concerns the effect of declining worker bargaining power on wages and prices. If weaker nominal wage growth is being passed through in the form of lower prices, then the price stability mandate would call for a more accommodative monetary policy in response to declining worker bargaining power.”

Krueger (2018, Jackson Hole)

American workers have needed ever-tighter labor markets since the 1970s to achieve decent wage growth

Estimates of the unemployment rate consistent with zero real wage growth (URCZWG) over the 1973–1978, 1979–1988, 1989–2000, and 2001–2007 periods

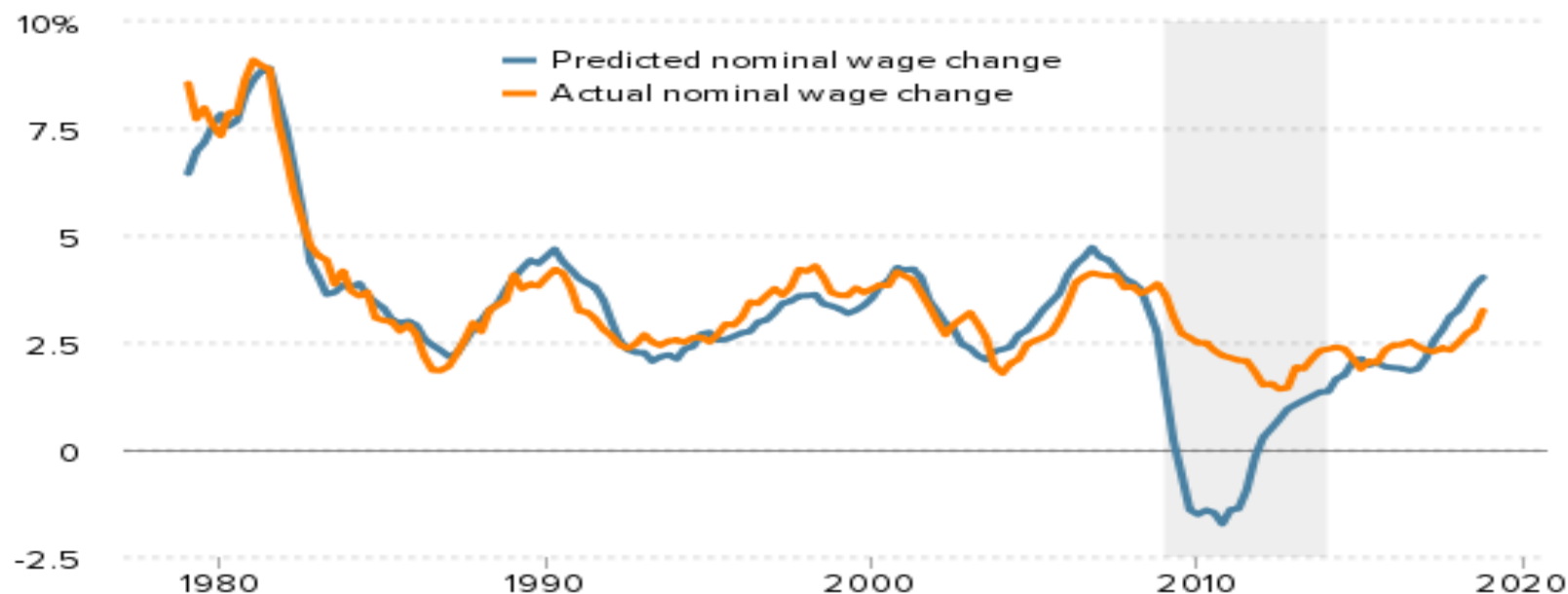


Notes: Estimates stem from regression using percent wage change as the dependent variable and the unemployment rate as the independent variable, along with dummy variables for the time periods shown. The estimated URCZWG is the constant from this regression divided by the coefficient on unemployment.

Source: Authors' replication and extension of results from Katz and Krueger (1999)

Immediate post–Great Recession period explains the declining predictive power of unemployment on wages

Predicted nominal wage changes and actual nominal wage changes, 1979–2018

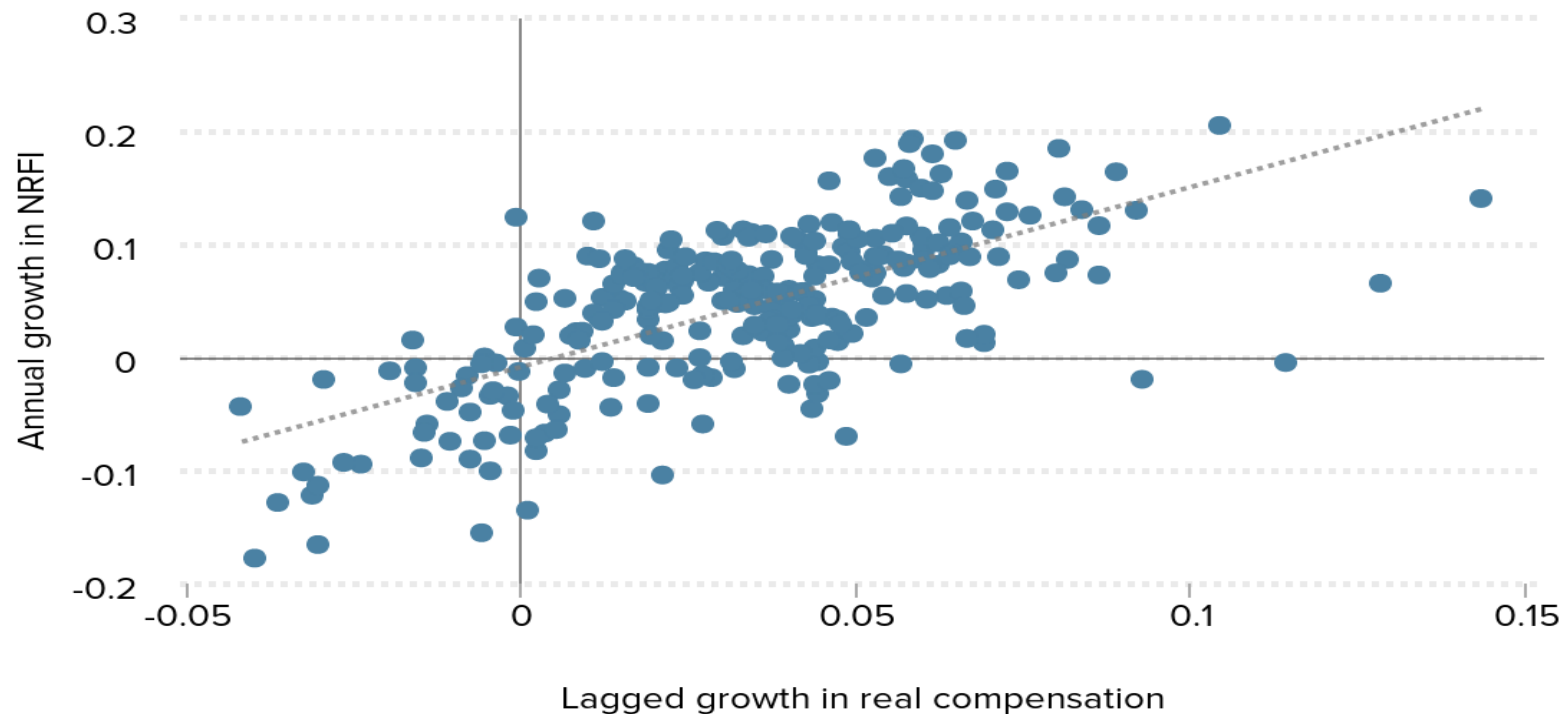


Note: The predicted nominal wage change is obtained from a regression of nominal wage changes on expected inflation and the unemployment rate for the years 1979–2007. The predicted nominal wage changes from this regression fit very tightly with actual nominal changes until the immediate post–Great Recession period (shaded in the figure).

Source: Unemployment rates are from the Bureau of Labor Statistics (BLS) Current Population Survey and wages are the average hourly earnings of production and nonsupervisory workers from the BLS Current Employment Statistics.

Faster real wage growth followed by greater nonresidential fixed investment in the United States

Lagged change in average real wages and growth of NRFI, 1979–2016



Source: Bureau of Economic Analysis (BEA) National Income and Product Accounts (NIPA) series, Table 1.16 and the Bureau of Labor Statistics total economy productivity database.

What is policymakers' obligation to take risks in pursuit of equalizing effects of high-pressure labor markets?

“Would it be legitimate to tolerate a somewhat greater chance of inflation while maintaining a strong demand for labor because doing so also manages to hold the unemployment rate of black youth at humane levels for the first time in a half-century? Can we reckon that this is a good policy because it contributes to overcoming racial stigma, draws blacks more fully into the mainstream of society, and permits them to earn the respect of their fellow citizens? (Here I mean to suggest that, but for this racial benefit, a different decision might be taken.) In other words, can we explicitly count as a benefit to society what we calculate to be the racially progressive consequences (reducing black economic marginality) of what is a race-blind action (electing to take a greater risk of inflation)?”

Loury (2000)