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What the Federal Reserve Is Doing to Promote a Stronger Job Market

I am here today to talk about what the Federal Reserve is doing to help our nation recover from the financial crisis and the Great Recession, the effects of which were particularly severe for the people and the communities you serve.

Part of that effort has involved strengthening the financial system. New rules are in place to better protect consumers and ensure that credit is available to help communities grow. The Federal Reserve also plays a role in communities by fostering dialogue that promotes community development. I will highlight some initiatives around the Federal Reserve System that I believe are making a real difference. Later today, I will visit the Manufacturing Technology Program at Daley College, on Chicago's south side, where adult students are acquiring the skills they need to connect to good-paying jobs in that sector.

The Fed supports the work you do in communities because *you* make a difference. You help ensure that credit is available for families to buy homes and for small businesses to expand. Your organizations sponsor programs that help make communities safer and families healthier and more financially secure. One of the most important things you do is to help people meet the demands of finding a job in what remains a challenging economy. And that help *is* crucial, but I also believe it can't succeed without two other things.

The first of these is the courage and determination of the people you serve. The past six years have been difficult for many Americans, but the hardships faced by some have shattered lives and families. Too many people know firsthand how devastating it is to lose a job at which you had succeeded and be unable to find another; to run through your savings and even lose your home, as months and sometimes years pass trying to find work; to feel your marriage and other relationships strained and broken by financial difficulties. And yet many of those who have suffered the most find the will to keep trying. I will introduce you to three of these brave men and women, your neighbors here in the great city of Chicago. These individuals have benefited from just the kind of help from community groups that I highlighted a moment ago, and they recently shared their personal stories with me.

It might seem obvious, but the second thing that is needed to help people find jobs…is jobs. No amount of training will be enough if there are not enough jobs to fill. I have mentioned some of the things the Fed does to help communities, but the most important thing we do is to use monetary policy to promote a stronger economy. The Federal Reserve has taken extraordinary steps since the onset of the financial crisis to spur economic activity and create jobs, and I will explain why I believe those efforts are still needed.

The Fed provides this help by influencing interest rates. Although we work through financial markets, our goal is to help Main Street, not Wall Street. By keeping interest rates low, we are trying to make homes more affordable and revive the housing market. We are trying to make it cheaper for businesses to build, expand, and hire. We are trying to lower the costs of buying a car that can carry a worker to a new job and kids to school, and our policies are also spurring the revival of the auto industry. We are trying to help families afford things they need so that greater spending can drive job creation and even more spending, thereby strengthening the recovery.

When the Federal Reserve's policies are effective, they improve the welfare of everyone who benefits from a stronger economy, most of all those who have been hit hardest by the recession and the slow recovery.

Now let me offer my view of the state of the recovery, with particular attention to the labor market and conditions faced by workers. Nationwide, and in Chicago, the economy and the labor market have strengthened considerably from the depths of the Great Recession. Since the unemployment rate peaked at 10 percent in October 2009, the economy has added more than 7-1/2 million jobs and the unemployment rate has fallen more than 3 percentage points to 6.7 percent. That progress has been gradual but remarkably steady--February was the 41st consecutive month of payroll growth, one of the longest stretches ever.

Chicago, as you all know, was hit harder than many areas during the recession and remains a tougher market for workers. But there has been considerable improvement here also. Unemployment in the city of Chicago is down from a peak of nearly 13 percent to about 9-1/2 percent at last count. That is about the same improvement as in the larger Chicago metro area, where unemployment has fallen to 8-1/2 percent. Metro Chicago has added 183,000 jobs since 2009, just below the rate for job gains nationwide.[1]

But while there has been steady progress, there is also no doubt that the economy and the job market are not back to normal health. That will not be news to many of you, or to the 348,000 people in and around Chicago who were counted as looking for work in January.[2] It will not be news to consumers or to owners of small and medium-sized businesses, who surveys say remain cautious about the strength and durability of the recovery.

The recovery still feels like a recession to many Americans, and it also looks that way in some economic statistics. At 6.7 percent, the national unemployment rate is still higher than it ever got during the 2001 recession. That is also the case in Chicago and in many other cities. It certainly feels like a recession to many younger workers, to older workers who lost long-term jobs, and to African Americans, who are facing a job market today that is nearly as tough as it was during the two downturns that preceded the Great Recession.

In some ways, the job market is tougher now than in any recession. The numbers of people who have been trying to find work for more than six months or more than a year are much higher today than they ever were since records began decades ago. We know that the long-term unemployed face big challenges. Research shows employers are less willing to hire the long-term unemployed and often prefer other job candidates with less or even no relevant experience.[3]

That is what Dorine Poole learned, after she lost her job processing medical insurance claims, just as the recession was getting started. Like many others, she could not find any job, despite clerical skills and experience acquired over 15 years of steady employment. When employers started hiring again, two years of unemployment became a disqualification. Even those needing her skills and experience preferred less qualified workers without a long spell of unemployment. That career, that part of Dorine's life, had ended.

For Dorine and others, we know that workers displaced by layoffs and plant closures who manage to find work suffer long-lasting and often permanent wage reductions.[4] Jermaine Brownlee was an apprentice plumber and skilled construction worker when the recession hit, and he saw his wages drop sharply as he scrambled for odd jobs and temporary work. He is doing better now, but still working for a lower wage than he earned before the recession.

Vicki Lira lost her full-time job of 20 years when the printing plant she worked in shut down in 2006. Then she lost a job processing mortgage applications when the housing market crashed. Vicki faced some very difficult years. At times she was homeless. Today she enjoys her part-time job serving food samples to customers at a grocery store but wishes she could get more hours.

Vicki Lira is one of many Americans who lost a full-time job in the recession and seem stuck working part time. The unemployment rate is down, but not included in that rate are more than seven million people who are working part time but want a full-time job. As a share of the workforce, that number is very high historically.

I have described the experiences of Dorine, Jermaine, and Vicki because they tell us important things that the unemployment rate alone cannot. First, they are a reminder that there are real people behind the statistics, struggling to get by and eager for the opportunity to build better lives. Second, their experiences show some of the uniquely challenging and lasting effects of the Great Recession. Recognizing and trying to understand these effects helps provide a clearer picture of the progress we have made in the recovery, as well as a view of just how far we still have to go.

And based on the evidence available, it is clear to me that the U.S. economy is still considerably short of the two goals assigned to the Federal Reserve by the Congress. The first of those goals is maximum sustainable employment, the highest level of employment that can be sustained while maintaining a stable inflation rate. Most of my colleagues on the Federal Open Market Committee and I estimate that the unemployment rate consistent with maximum sustainable employment is now between 5.2 percent and 5.6 percent, well below the 6.7 percent rate in February.

The other goal assigned by the Congress is stable prices, which means keeping inflation under control. In the past, there have been times when these two goals conflicted--fighting inflation often requires actions that slow the economy and raise the unemployment rate. But that is not a dilemma now, because inflation is well below 2 percent, the Fed's longer-term goal.

The Federal Reserve takes its inflation goal very seriously. One reason why I believe it is appropriate for the Federal Reserve to continue to provide substantial help to the labor market, without adding to the risks of inflation, is because of the evidence I see that there remains considerable slack in the economy and the labor market. Let me explain what I mean by that word "slack" and why it is so important.

Slack means that there are significantly more people willing and capable of filling a job than there are jobs for them to fill. During a period of little or no slack, there still may be vacant jobs and people who want to work, but a large share of those willing to work lack the skills or are otherwise not well suited for the jobs that are available. With 6.7 percent unemployment, it might seem that there must be a lot of slack in the U.S. economy, but there are reasons why that may not be true.

One important reason relates to the skills and education of people in the workforce. It is no secret that America faces some daunting challenges in educating people and preparing them to work in a 21st century, globalized economy. Many of you in this audience are helping workers address this challenge, but you also know that the economy continues to change very rapidly.

To the extent that people who desire to work lack the skills that employers are demanding, there is less slack in the labor market. This is an example of what economists call "structural" unemployment, and it can be difficult to solve. Even understanding what workers need to appeal to employers is difficult in a fast-changing economy. For government, effective solutions for structural unemployment, beginning with improved education, tend to be expensive and take a long time to work. The problem goes deeper than simply a lack of jobs.

But a lack of jobs *is* the heart of the problem when unemployment is caused by slack, which we also call "cyclical unemployment." The government has the tools to address cyclical unemployment. Monetary policy is one such tool, and the Federal Reserve has been actively using it to strengthen the recovery and create jobs, which brings me to why the amount of slack is so important.

If unemployment were mostly structural, if workers were unable to perform the jobs available, then the Federal Reserve's efforts to create jobs would not be very effective. Worse than that, without slack in the labor market, the economic stimulus from the Fed could put attaining our inflation goal at risk. In fact, judging how much slack there is in the labor market is one of the most important questions that my Federal Reserve colleagues and I consider when making monetary policy decisions, because our inflation goal is no less important than the goal of maximum employment.

This is not just an academic debate. For Dorine Poole, Jermaine Brownlee, and Vicki Lira, and for millions of others dislocated by the Great Recession who continue to struggle, the cause of the slow recovery is enormously important. As I said earlier, the powerful force that sustains them and others who keep trying to succeed in this recovery is the faith that their job prospects *will* improve and that their efforts will be rewarded.

Now let me explain why I believe there is still considerable slack in the labor market, why I think there is room for continued help from the Fed for workers, and why I believe Dorine Poole, Jermaine Brownlee, and Vicki Lira are right to hope for better days ahead.

One form of evidence for slack is found in other labor market data, beyond the unemployment rate or payrolls, some of which I have touched on already. For example, the seven million people who are working part time but would like a full-time job. This number is much larger than we would expect at 6.7 percent unemployment, based on past experience, and the existence of such a large pool of "partly unemployed" workers is a sign that labor conditions are worse than indicated by the unemployment rate. Statistics on job turnover also point to considerable slack in the labor market. Although firms are now laying off fewer workers, they have been reluctant to increase the pace of hiring. Likewise, the number of people who voluntarily quit their jobs is noticeably below levels before the recession; that is an indicator that people are reluctant to risk leaving their jobs because they worry that it will be hard to find another. It is also a sign that firms may not be recruiting very aggressively to hire workers away from their competitors.

A second form of evidence for slack is that the decline in unemployment has not helped raise wages for workers as in past recoveries. Workers in a slack market have little leverage to demand raises. Labor compensation has increased an average of only a little more than 2 percent per year since the recession, which is very low by historical standards.[5] Wage growth for most workers was modest for a couple of decades before the recession due to globalization and other factors beyond the level of economic activity, and those forces are undoubtedly still relevant. But labor market slack has also surely been a factor in holding down compensation. The low rate of wage growth is, to me, another sign that the Fed's job is not yet done.

A third form of evidence related to slack concerns the characteristics of the extraordinarily large share of the unemployed who have been out of work for six months or more. These workers find it exceptionally hard to find steady, regular work, and they appear to be at a severe competitive disadvantage when trying to find a job. The concern is that the long-term unemployed may remain on the sidelines, ultimately dropping out of the workforce. But the data suggest that the long-term unemployed look basically the same as other unemployed people in terms of their occupations, educational attainment, and other characteristics. And, although they find jobs with lower frequency than the short-term jobless do, the rate at which job seekers are finding jobs has only marginally improved for both groups. That is, we have not yet seen clear indications that the short-term unemployed are finding it increasingly easier to find work relative to the long-term unemployed. This fact gives me hope that a significant share of the long-term unemployed will ultimately benefit from a stronger labor market.

A final piece of evidence of slack in the labor market has been the behavior of the participation rate--the proportion of working-age adults that hold or are seeking jobs. Participation falls in a slack job market when people who want a job give up trying to find one. When the recession began, 66 percent of the working-age population was part of the labor force. Participation dropped, as it normally does in a recession, but then kept dropping in the recovery. It now stands at 63 percent, the same level as in 1978, when a much smaller share of women were in the workforce. Lower participation could mean that the 6.7 percent unemployment rate is overstating the progress in the labor market.

One factor lowering participation is the aging of the population, which means that an increasing share of the population is retired. If demographics were the only or overwhelming reason for falling participation, then declining participation would not be a sign of labor market slack. But some "retirements" are not voluntary, and some of these workers may rejoin the labor force in a stronger economy. Participation rates have been falling broadly for workers of different ages, including many in the prime of their working lives. Based on the evidence, my own view is that a significant amount of the decline in participation during the recovery is due to slack, another sign that help from the Fed can still be effective.

Since late 2008, the Fed has taken extraordinary steps to revive the economy. At the height of the crisis, we provided liquidity to help avert a collapse of the financial system, which enabled banks and other institutions to continue to provide credit to people and businesses depending on it. We cut short-term interest rates as low as they can go and indicated that we would keep them low for as long as necessary to support a stronger economic recovery. And we have been purchasing large quantities of longer-term securities in order to put additional downward pressure on longer-term interest rates--the rates that matter to people shopping for a new car, looking to buy or renovate a home, or expand a business. There is little doubt that without these actions, the recession and slow recovery would have been far worse.

These different measures have the same goal--to encourage consumers to spend and businesses to invest, to promote a recovery in the housing market, and to put more people to work. Together they represent an unprecedentedly large and sustained commitment by the Fed to do what is necessary to help our nation recover from the Great Recession. For the many reasons I have noted today, I think this extraordinary commitment is still needed and will be for some time, and I believe that view is widely shared by my fellow policymakers at the Fed.

In this context, recent steps by the Fed to reduce the rate of new securities purchases are not a lessening of this commitment, only a judgment that recent progress in the labor market means our aid for the recovery need not grow as quickly. Earlier this month, the Fed reiterated its overall commitment to maintain extraordinary support for the recovery for some time to come.

This commitment is strong, and I believe the Fed's policies will continue to help sustain progress in the job market. But the scars from the Great Recession remain, and reaching our goals will take time. In the meanwhile, the Federal Reserve will continue to expand its efforts to promote community development. The Board and each of the 12 Reserve Banks have community development staff members who focus on improving the availability of financial services in low- and moderate-income communities. They help bankers comply with the Community Reinvestment Act, but they are also a source of research and a facilitator of communication among financial institutions and practitioners to identify and share best practices.

This conference is one example of how the Fed pursues those goals, and I would like to mention a few of the Fed's other community development initiatives that I find particularly promising. In 2012, The Federal Reserve Bank of San Francisco partnered with the Low Income Investment Fund (LIIF), a community development financial institution that bridges the gap between low-income neighborhoods and private capital sources, to publish the book *Investing in What Works for America's Communities*. This book cited innovative and effective community development initiatives across the country and advocated for a "Community Quarterback" model to coordinate initiatives and better leverage funding among groups with similar goals.

In a similar way, the Federal Reserve Bank of Boston has been the catalyst for the Working Cities Challenge, inspired by its own research on cities that managed to diversify away from a declining, manufacturing-based economy. The research found that one key to success is "collaborative leadership," when governments, businesses, and nonprofits unite behind one focused approach. The Working Cities Challenge promotes that principle by inviting smaller Massachusetts cities to consider how they would use collaborative leadership to unite their communities to address a major challenge for lower-income residents. Twenty cities competed for $1.8 million in funding from the state and other sources. Six cities were awarded funds this past January, but many more will benefit from the spread of a new approach to capacity building that Fed research shows helps communities thrive.

Leadership recruitment is also at the heart of a grassroots-oriented program called Economic Avenue that was developed by the Kansas City Fed. In Northeast Kansas City, Kansas, residents and neighborhood leaders are forming a leadership council that will have responsibility for managing the program, which aims to create and grow local businesses, create jobs, and promote homeownership. The bank's community development staff is providing education and training to get the council off the ground, will measure and evaluate its progress, and assist in connecting leaders to resources and other programs.

These examples are just a few among many throughout the Federal Reserve System. By testing ideas, developing better measurement tools, convening interested parties, and sharing the Federal Reserve's skills and knowledge with our partners at the national and local levels, we aim to serve as a catalyst to improve lives.

Through these initiatives, together with the use of monetary policy and steps to safeguard the financial system, the Federal Reserve is committed to strengthening communities and restoring a healthy economy that benefits all Americans. It is my hope that the courageous and determined working people I have told you about today, and millions more, will get the chance they deserve to build better lives.

1. According to the Bureau of Labor Statistics, total nonfarm employment for the Chicago-Joliet-Naperville metropolitan division has increased 183,000 since December 2009, or about 5 percent. Over this period, employment nationally has increased about 6 percent. Return to text

2. Bureau of Labor Statistics Local Area Unemployment Statistics for the Chicago-Joliet-Naperville metropolitan division. Return to text

3. See Kory Kroft, Fabian Lange, and Matthew J. Notowidigdo (2013), "Duration Dependence and Labor Market Conditions: Evidence from a Field Experiment," *Quarterly Journal of Economics*, vol. 128 (3), pp. 1123-67; and Rand Ghayad (2014), "The Jobless Trap (PDF)," unpublished paper, Northeastern University, Department of Economics. Return to text

4. See, among others, Louis S. Jacobson, Robert J. LaLonde, and Daniel G. Sullivan (1993), "Earnings Losses of Displaced Workers," *American Economic Review*, vol. 83 (September), pp. 685-709; Steven J. Davis and Till von Wachter (2011), "Recessions and the Costs of Job Loss (PDF)," *Brookings Papers on Economic Activity,* Fall, pp. 1-55; Till von Wachter, Jae Song, and Joyce Manchester (2009), "Long-Term Earnings Losses due to Mass Layoffs during the 1982 Recession: An Analysis Using U.S. Administrative Data from 1974 to 2004 (PDF)," unpublished paper, April; and Daniel Cooper (2014), "The Effect of Unemployment Duration on Future Earnings and Other Outcomes (PDF)," Working Paper No. 13-8 (Boston: Federal Reserve Bank of Boston, January). Return to text

5. From 2010 to 2013, average annual growth in compensation per hour, hourly compensation as measured in the Employment Cost Index and average hourly earnings for all employees in private industries--all independent estimates of wage and compensation growth--increased annually, on average, no more than 2-1/4 percent. Return to text