MILLENNIALS, WORK, AND THE ECONOMY

William R. Emmons

For most young people, earnings from work constitute virtually all of their income.[1] Research shows that the trajectory of most individuals' lifetime wage and salary earnings is heavily influenced by labor-market conditions when they enter the workforce.[2] Entering a bad job market with relatively less education exacts an especially large and long-lasting toll on an individual's health and life satisfaction.[3] Clearly, then, the difficult job market facing Millennials during and after the Great Recession poses a significant challenge to the current and future well-being of today's young adults, especially those with low levels of education or training.

Current Conditions

The Millennial Job Market has been Historically Bad

The unemployment rate for men aged 25-34 peaked at 11.4 percent during the second quarter of 2009 (this corresponds to birth years between about 1975 and 1984, combining late Gen-Xers and early Millennials). Among men aged 20-24, unemployment peaked at 18.9 percent during the first quarter of 2010 (corresponding roughly to birth years 1986-90). Women had lower and somewhat delayed unemployment peaks: 9.5 percent in the third quarter of 2010 for those aged 25-34 and 13.9 percent in the first quarter of 2011 for women aged 20-24. The unemployment rate for young workers during the last seven years has traced out a path very similar to the one experienced during 1979-86, which had been the worst job market in the post-WW II period prior to the Great Recession. The job market that Millennials inherited has been historically weak.

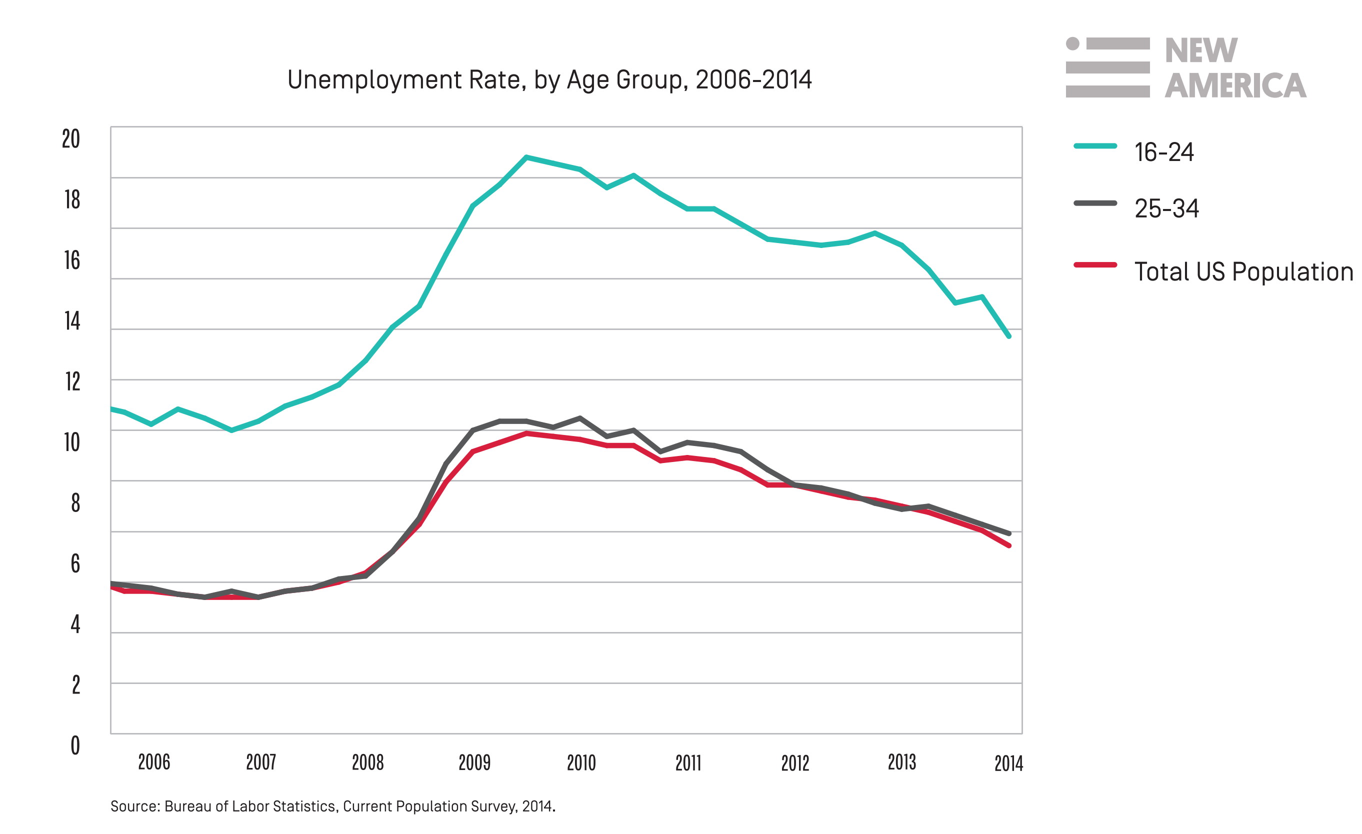
More recently, the unemployment rate for men and women aged 25-34 (birth years 1980-89) had fallen to 6.7 percent and 6.5 percent respectively, as of the second quarter of 2014. However, these rates were still noticeably above the rates for those aged 45-54 (birth years 1960-69), at 4.5 percent.[4] Among those aged 20-24, the unemployment rate in the second quarter of 2014 had fallen only to 11.9 percent for men and 9.4 percent for women. Again using the unemployment rates among 45-54-year old men and women as benchmarks, the gap between the unemployment rates of the 20-24-year old groups and 45-54-year olds remained slightly elevated for women but substantially higher among young men.[5]

A Deep Malaise among Young Workers

Arguably more consequential than the unemployment rate is the employment rate—the fraction of all members of an age group that is employed. While the unemployment rate ignores everyone who drops out of the labor market for any reason, the employment rate takes this category into account. The distinction between the unemployment rate and the employment rate is particularly important for people in their late 20s and 30s, who would be expected to have relatively low non-participation rates, especially among men.

Why is non-participation normally lower among young adults? People in their late 20s and early 30s are much less likely to be full-time students than people under 25; they are much less likely than older people to be unable to work due to disability; and they are extremely unlikely to have retired early due to unusually high career earnings or having received a windfall such as an inheritance or winning the lottery. Hence, reasons for nonparticipation that are important in other age groups are not as relevant for young adults.[6]

The most likely reason for a man to drop out of (or never to have entered) the labor market in his late 20s or 30s is a lack of marketable skills or other impediments to continuing employment (criminal record, resident status). Very few men are primary caregivers for children; even when they are, many continue to work, at least part-time. Among young women, a somewhat larger group is taking care of children full-time.



In terms of the employment rate, the Great Recession and its aftermath have pushed young adults into new territory. During the 1950s and 1960s, the employment rate among men aged 25-34 was in the low 90-percent range. Indeed, this group's employment rate exceeded 90 percent as late as 2000, and it reached a cyclical peak of 88.4 percent in early 2007. After falling as low as 79.6 percent during the Great Recession (first quarter of 2009), five full years of recovery have brought this key employment indicator back only to 82.7 percent (second quarter of 2014). Even at its worst point during the severe 1981-82 recession, the employment rate for 25-34-year old men fell only as low as 83.4 percent. Thus, 2014 will mark the sixth consecutive year during which the employment rate for men aged 25-34 remained continuously below the lowest quarterly level previously recorded.[7] Young Americans are participating in the economy and working at historically low rates.

The post-WW II employment rate for young women increased steadily until about 2000. Since that time, the employment rate for 25- to 34-year-old women has fluctuated by similar magnitudes as those experienced by 25- to 34-year-old men since about 2000, although it declined less sharply during the Great Recession. Together, the employment rate for both sexes aged 25-34 was only 75.5 percent in the second quarter of 2014, down 6.4 percentage points from its peak in the second quarter of 2000.

A New (and Tough) Economy for Young Adults

In addition to the worst cyclical downturn in the post-WW II period—from which recovery has been notably weaker for young workers, especially young men—today's young adults may be facing a long-term decline in the demand for high-skilled workers.[8] For successive cohorts of college graduates beginning in about 2000, the share of each cohort that is employed in jobs that require a college degree has declined and inflation-adjusted wage profiles have flattened and slipped lower.

Even though this downshift in the demand for college-educated workers directly affects only the (increasingly numerous) people with those skills, the ripple effects are being felt throughout the labor market. A "cascading" effect transfers downward pressure on wages from the highest-skilled young workers, who struggle to find skill-appropriate jobs, to other workers on lower-skill rungs of the job ladder. This is because lower-skill young workers face increasing competition from underemployed higher-skill workers suffering a paucity of opportunity in high-paying occupations. At the very bottom of the skill distribution, some potential workers are pushed out of the job market altogether as employers are able to fill even low-wage positions with relatively higher-skilled applicants.[9]

The downshifting of demand for cognitive skills, and the ensuing cascading effect on lower-skilled workers, appears to affect young adults the most because entry-level wage rates are the most flexible for many employers. The evidence to date suggests that occupational downgrading and the resulting market-wide downward wage pressure since about 2000 may exert permanent effects on young adults' earnings trajectories. For the least-skilled and least-experienced workers, obtaining a foothold on the job ladder has become increasingly difficult.

Policy Landscape

Four widely-touted policy responses to the weak job market are unlikely to solve the problems unique to young adults. Indeed, each of these policy tools is in use today, yet the employment outlook for young adults remains discouraging. While current policy debates focus on supporting the economy, they are not addressing the specific employment problems of young adults. From the perspective of young workers, much of the current policy discussion amounts to the prescription, "The medicine isn't working; increase the dosage!"

Response #1: Redouble macroeconomic stimulus

By some measures, fiscal policy and monetary policy have been more stimulative since 2008 than in many previous decades. There is broad consensus that expansionary fiscal and monetary policy stabilized an economy in free-fall in 2008 and 2009, but there is less agreement on how effective (or how expansionary) they have been during the recovery, which began in mid-2009. A growing chorus within and outside policy circles points to the need to "normalize" macroeconomic policy, moving away from emergency settings toward more sustainable stances for fiscal and monetary policy. *Bottom line*: We should not expect macroeconomic policy to become more stimulative in the years to come.

Response #2: Raise the minimum wage

The Congressional Budget Office projected that an increase in the federal minimum wage to $10.10 per hour by 2016, with annual inflation adjustments thereafter, would raise the incomes of some 16.5 million workers.[10] However, the CBO estimated that total employment would decline by about 500,000 workers. The most likely to be squeezed out of the job market are the least-skilled and least-experienced workers, who are disproportionately young and members of historically disadvantaged minority groups. *Bottom line*: An increase in the minimum wage does not address the problems facing the most vulnerable young workers.

Response #3: Expand education and training opportunities

Providing current and future workers with greater skills is a goal endorsed by virtually everyone; as always, the devil lies in the details. Small-bore efforts to increase the efficiency with which education and training are delivered should and will be continued. But large-scale, transformative efforts to bring the American labor force into the globally competitive 21st century—an education and training "moon shot"—appear to be pipe dreams in an era of near-total dysfunction in Congress. Moreover, the "skills cascade" that is affecting young workers even more than older workers would—paradoxically—be exacerbated by an expanded supply of college graduates. *Bottom line*: More education is not the answer—at least, not in the foreseeable future.

Response #4: Expand the Earned-Income Tax Credit

Strictly speaking, the EITC is not an employment policy. It is an income supplement for lower-wage workers that is delivered as a tax refund. Initially, it rises in value as earnings increase, but then phases out beyond a certain earnings threshold. Some economists argue that it can impose a relatively high marginal tax rate in the form of the phase-out schedule and thus dampens work incentives on the margin. Others emphasize its role as a means to transfer cash resources to those with low-incomes and to improve their economic outlook. Regardless of its impact on work effort, the EITC and other elements of the social safety net should be part of any discussion of the job-market challenges facing young adults. *Bottom line*: The EITC is a way to improve the current job prospects of young adults who are already employed, rather than a means to create new job opportunities.

The Challenges to Address

Perhaps the most difficult challenge policymakers face when it comes to addressing the employment situation of Millennials is accepting that the unique problems facing young workers may be due to forces beyond policymakers' control. These forces include the declining demand for skilled workers in the face of a rising supply of such workers, disproportionately affecting young adults of all skill levels;[11] an increasingly competitive and connected global economy; a rapidly aging population that will reduce the economy's potential growth rate; and a damaged domestic economy that will continue to convalesce for many years, perhaps never regaining the growth trajectory it once followed.[12]

Considering both the intractable nature of the forces underlying generally poor short-term job prospects for young adults and the need for policy reforms to ensure the sustainability of growth for economy as a whole, it makes sense to consider how the "generational risk" can best be shared.

Perhaps Millennials have "drawn the short straw" in a generational lottery. Current federal policies have a generational bias, to be sure; the beneficiaries are older Americans. Considering only Medicare, for example, the CBO estimates that the median person born in the 1960s will consume benefits in excess of the taxes they paid (both in inflation-adjusted terms) of about $200,000.[13] A new inter-generational social contract that recognizes the undiversifiable risk borne by young Americans should be the beginning of the conversation.

William R. Emmons is senior economic adviser at the Center for Household Financial Stability and an assistant vice president and economist at the Federal Reserve Bank of St. Louis.

Endnotes

[1] Among people aged 25-34 in 2012, 94.4 percent of total income came from employment or self-employment (i.e. earnings from work). Among all people 35 or older, the share of earnings from work was 77.7 percent (Bureau of the Census and Bureau of Labor Statistics, Current Population Survey).

[2] Joseph G. Altonji, Lisa B. Kahn, and Jamin D. Speer, "Cashier or Consultant? Entry Labor Market Conditions, Field of Study, and Career Success," Yale University working paper, September 2013.

[3] David Cutler, Wei Huang, and Adriana Lleras-Muney, "When Does Education Matter? The Protective Effect of Education for Cohorts Graduating in Bad Times," NBER working paper 20156, May 2014.

[4] The age-related unemployment gap has returned close to normal for women but remains elevated for men. In particular, the average annual difference in the unemployment rate among men aged 25-34 and men aged 45-54—about 2.0 percentage points during the past four quarters—ranged between 1.3 and 1.7 percentage points during the previous economic expansion (2002-07). Among women, the gap during the most recent four quarters of 1.8 percentage points lies within the range of 1.4 to 2.2 percentage points during the previous expansion (2002-07).

[5] The range of average annual gaps between the unemployment rate of 20-24-year old men (women) and 45-54-year old men (women) was 5.6 to 6.2 (4.1 to 5.6) percentage points between 2002 and 2007. During the four quarters ending in the second quarter of 2014, the average unemployment gap was 7.8 percentage points for men and 5.4 percentage points for women.

[6] Melinda Pitts, John Robertson, and Ellyn Terry, "Reasons for the Decline in Prime-Age Labor-Force Participation," Federal Reserve Bank of Atlanta Macroblog, April 10, 2014.

[7] It should be pointed out that employment rates for men in all but the oldest age groups have plumbed new depths since the Great Recession.

[8] Paul Beaudry, David A. Green, and Benjamin M. Sand, "The Declining Fortunes of the Young Since 2000," *American Economic Review* 104 (2014), No. 5, pp. 381-86; and Paul Beaudry, David A. Green, and Benjamin M. Sand, "The Great Reversal in the Demand for Skill and Cognitive Tasks," NBER working paper, March 2013.

[9] Perversely, minimum-wage laws may harm the lowest-skilled, least-experienced workers in the presence of a skills "cascade."

[10] Congressional Budget Office, "The Effects of a Minimum-Wage Increase on Employment and Family Income," February 2014.

[11] See Beaudry, Green, and Sand (2013, 2014).

[12] Robert E. Hall, "Quantifying the Lasting Harm to the U.S. Economy from the Financial Crisis," NBER working paper, April 2014.

[13] Congressional Budget Office, "Medicare and Social Security Payroll Taxes and Benefits for People in Different Birth Cohorts," September 2013.