CURRENT ECONOMIC CONDITIONS IN THE U.P., & THE ROLE OF LABOR FORCE IN FUTURE GROWTH

August 18, 2022 **Ron Wirtz** Regional Outreach Director



FEDERAL RESERVE BANK OF MINNEAPOLIS

DISCLAIMER

The views expressed here are the presenter's and not necessarily those of the Federal Reserve Bank of Minneapolis or the Federal Reserve System.



TODAY'S TALK

- Current state of the economy
 - Demand has softened, but hiring demand still solid
 - Lots (and *lots*) of challenges for UP companies
 - Prices, supply chains, Ukraine, interest rates
 - Covid/variants = disruption, uncertainty & volatility
 - Labor force big key to long-term economic growth
 - Outlook is softer across the UP
- Fast-paced, lots of data. Will share PPT for those wanting a closer look at individual slides



MEASURING THE ECONOMY: THE BIG PICTURE

GROSS DOMESTIC PRODUCT

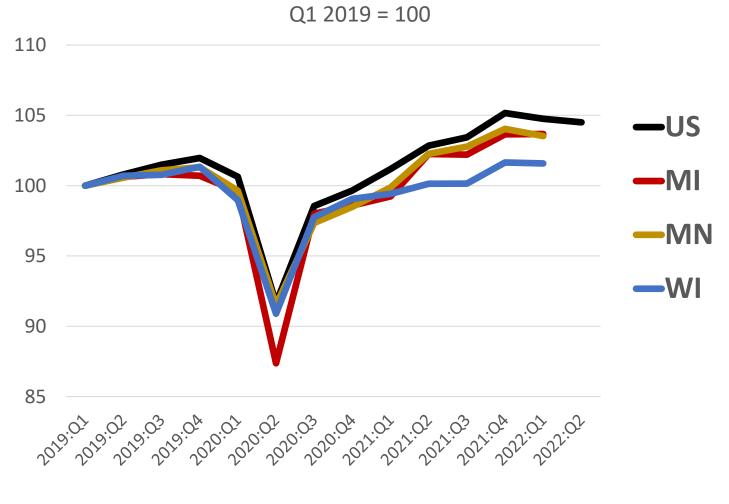
Real GDP = total output, adjusted for inflation

US: Negative GDP last two quarters

Typically = recession

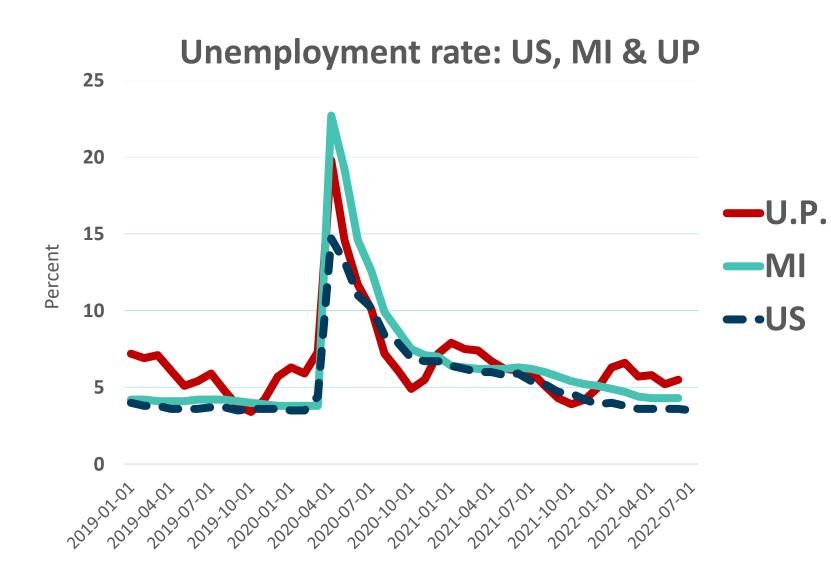
But 'official' recessions also require other economic events, like job loss

Michigan: Bigger drop and bigger recovery



Real gross domestic product

UNEMPLOYMENT



U-3 rate = 'official' rate not yet below pre-pandemic for MI or UP

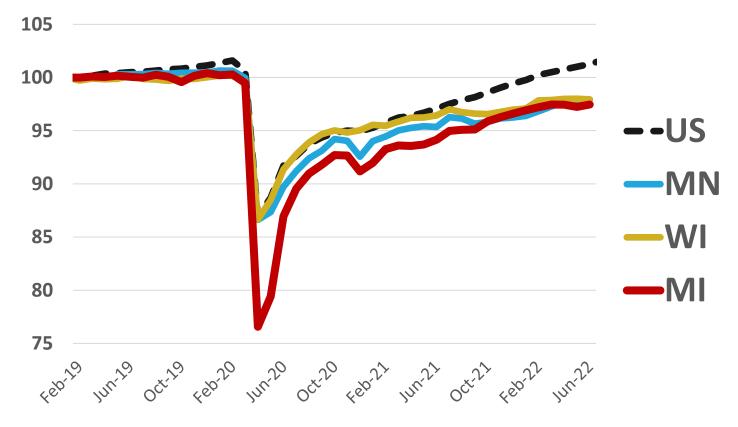
U-6 rate = "realworld" labor slack; also still significantly higher



TOTAL EMPLOYMENT

Total employment index

January 2019 employment =100



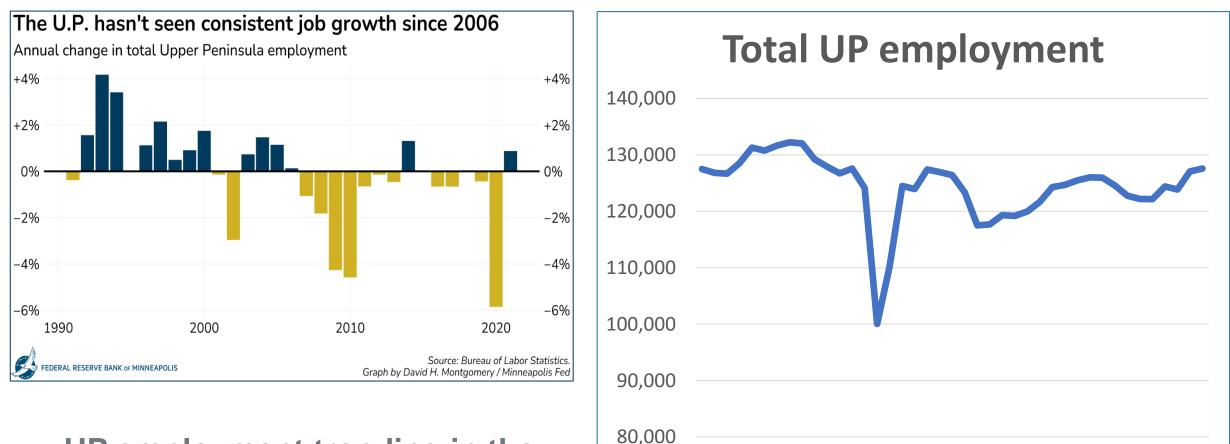
Jobs definitely recovering ... but trajectory much flatter compared with national trend

Still 2-3 percent below prepandemic levels

Michigan = 125,000 fewer jobs



UP EMPLOYMENT



Feb

2019

Jun

2019

Oct

2019

Feb

2020

Jun

2020

Oct

2020

Feb

2021

Jun

2021

Oct

2021

Feb

2022

RESERVE BANK OF MINNEAPOLIS

Jun

2022

UP employment trending in the right direction, but seasonal job loss also about to set in

DRILLING INTO CURRENT CONDITIONS HOW WOULD YOU CHARACTERIZE RECENT BUSINESS ACTIVITY?

MINNEAPOLIS FED: PANDEMIC SURVEYS

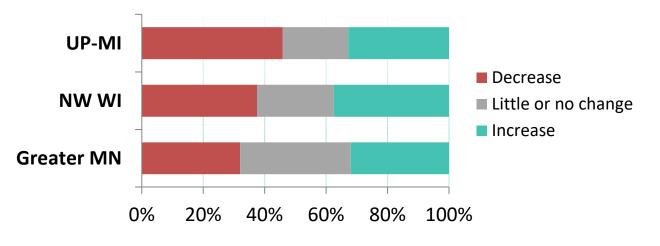
• During pandemic, needed ways to gauge real-time business conditions = more outreach to businesses

• General Business survey

- Closed at the end of July
- About 440 responses, including 60 from Upper Peninsula
- What'd they say about current business conditions?

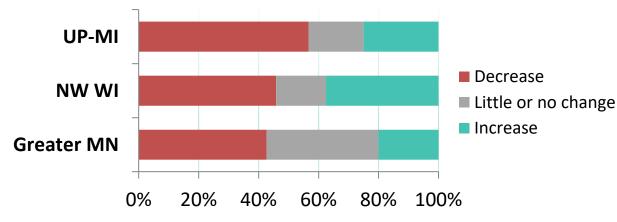


RECENT BUSINESS ACTIVITY IN U.P.



Quarterly revenue compared with last year

Quarterly profits compared with last year



Recent revenues and (esp) profits declining across Ninth District, but a bit more so in UP

Composition matters *a lot*

UP sample =

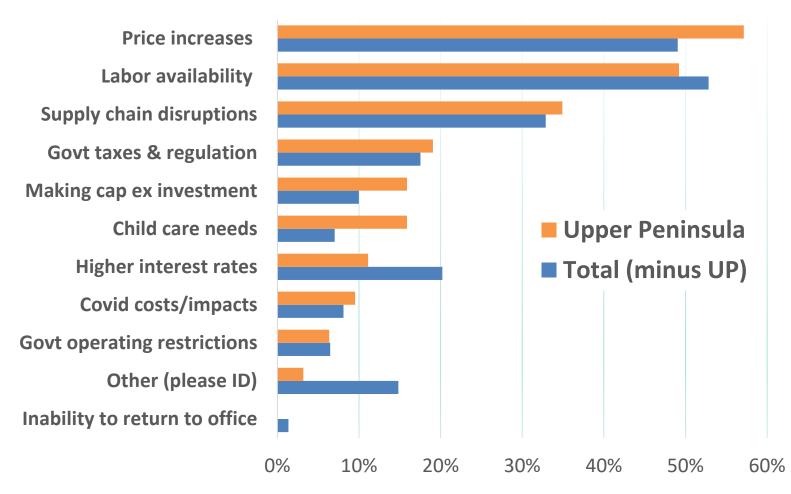
- More small firms
- More food-drink & retail
- Fewer manufacturing, finance and profess-sci-tech



LOTS OF CHALLENGES

CHALLENGES TO OPERATIONS

Top TWO challenges to your business



General Business Survey The Big Three:

- Inflation
- Labor availability
- Supply chain

Higher interest rates also now on the radar

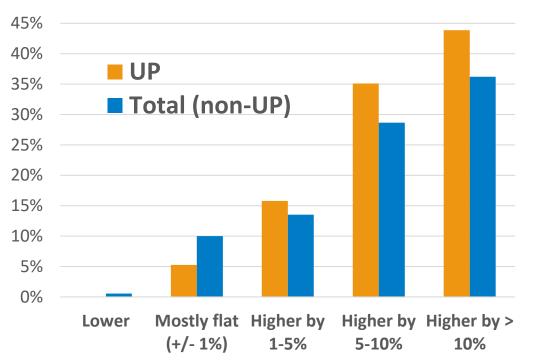
Covid falling on the radar (% cut in half from January survey)



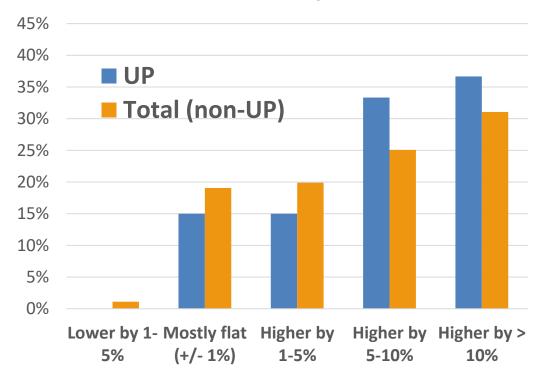
Source: Federal Reserve Bank of Minneapolis, General Business Survey, January 2022



Wholesale and retail prices rising more steeply in the UP



Wholesale priced from vendors

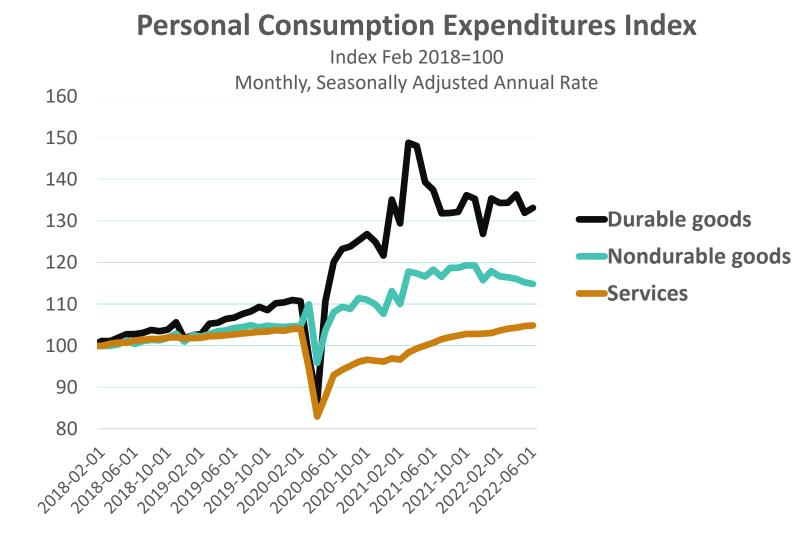


Final retail prices

FEDERAL RESERVE BANK OF MINNEAPOLIS

Source: Federal Reserve Bank of Minneapolis, General Business Survey, July 2022

INFLATION: NOT ALL GOODS & SERVICES CREATED EQUAL



Inflation driven by pandemic shift into goods (esp. durables),

Shortages occurred, compounded by supply chain problems, and covid's impact on labor

Inflation for services very modest overall

Very gradual rebalancing of demand back toward services



Source: Bureau of Economic Analysis

NEEL KASHKARI'S TAKE ON INFLATION AND THE FED'S RECENT MOVE

- "When inflation accelerated last year, I argued that it was likely due to **transitory factors** which would soon pass. That hasn't happened."
- Google: "Kashkari inflation Medium" (great read)
- Vaccine effects were not long-lasting; e.g, labor increases did not relieve pressure on supply chains and wages; workers also did not return as quickly as expected
- Covid continues to be global disruptor
- Unexpected: Consumer demand has not moderated
 - "Good" news: Sustained demand from rising disposable income
- Fed increased rates by 25 basis points in March, 50 bps in early May, 75 bp in June; 75 bp in July; more expected



IMPACT OF INFLATION AND HIGHER INTEREST RATES ON YOU!

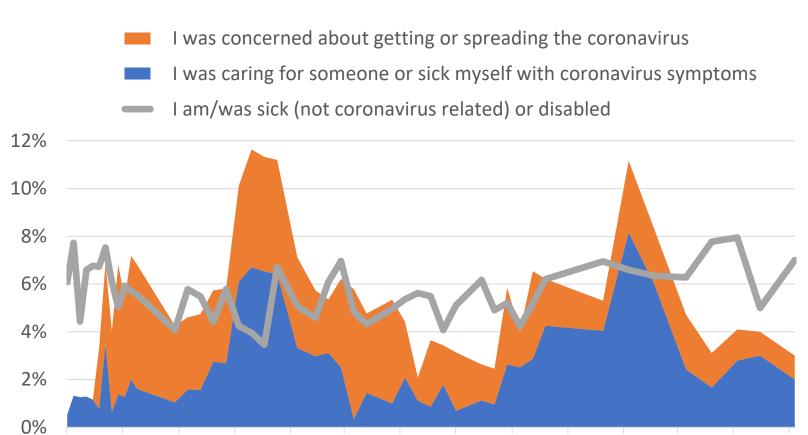
CHALLENGE #2: SUPPLY CHAINS

- Pandemic demand shifted toward goods = low inventories
- Producers trying to meet *new* demand *and* rebuild inventory
 - Having problems sourcing some materials for their products (= delays and higher costs), AND
 - Facing labor constraints in production and delivery
 - Present *before* pandemic, & worsened significantly by pandemic and repeated covid surges
- **Lesson:** Hyper-efficient, global supply chain is vulnerable in a pandemic because there is no latent capacity
- *Covid surges prevent repair:* More people out of work; production and supply chains don't get fixed; slower consumer rotation back to services (and fewer goods)



COVID'S IMPACT ON WORKFORCE/STAFFING

Reason for not working



512020 1512020 1512020 1512022 1512022 1512022 1512022 1512022 1512022 1512022 1512022 1512022

Covid surges spill into labor force, which spills into everything else

Catch-up is hard when you're at 85-90 percent of optimal capacity (and not counting unfilled jobs!)

Source: Household Pulse Survey, Census Bureau

Note: Survey and resulting data are still in experimental phase



A NEW CHALLENGE: UKRAINE & RUSSIA CONFLICT

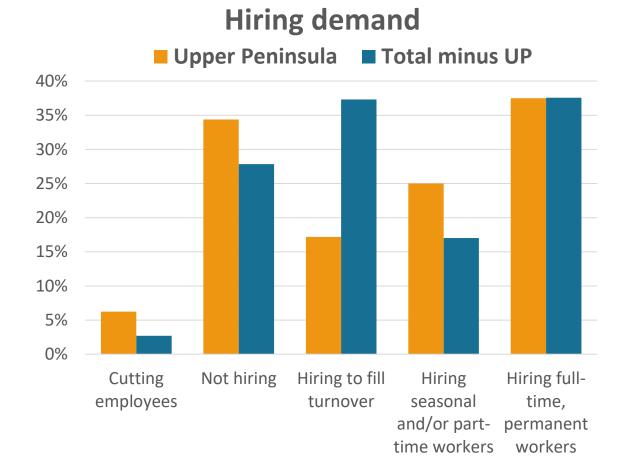
- Direct trade effects to businesses are likely small;
 Ukraine and Russia are not big trade partners with U.S.
 - **Top three U.S. trade partners:** China, Mexico, Canada; Russia not among top 30; Ukraine not in top 50
- However, the war having notable effects on energy and ag markets; worsens existing inflationary pressures for everyone, everywhere
- **Overall:** war in Ukraine introduces more uncertainty; uncertainty = caution = slower growth

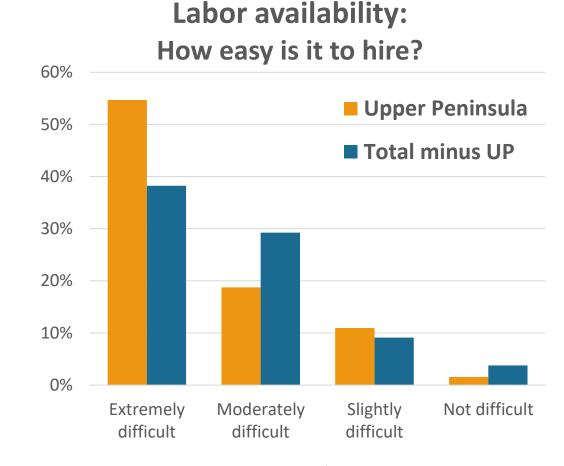


PIVOTING TO LABOR MARKETS AND HIRING DEMAND

LABOR DEMAND AND SUPPLY (AVAILABILITY)

UP businesses are trying to hire, but having difficulty



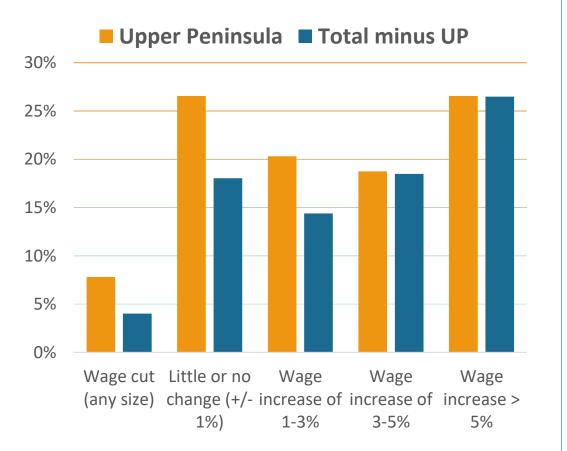


FEDERAL RESERVE BANK OF MINNEAPOLIS

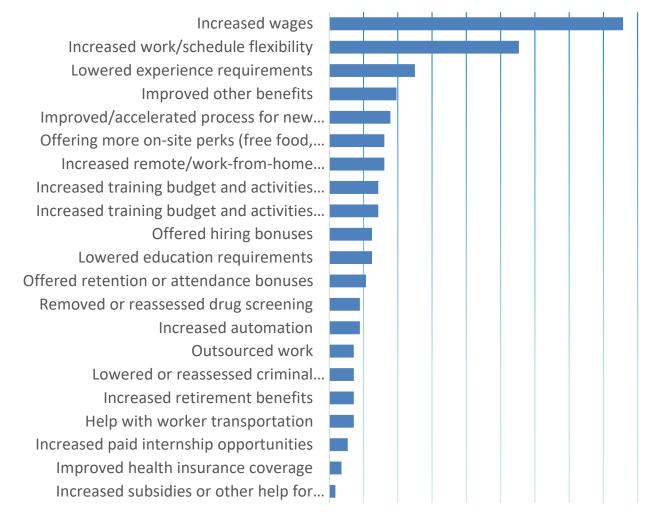
Source: Federal Reserve Bank of Minneapolis, General Business Survey, July 2022

EMPLOYER RESPONSES

Wage growth over the last year



U.P. employer responses to labor shortage



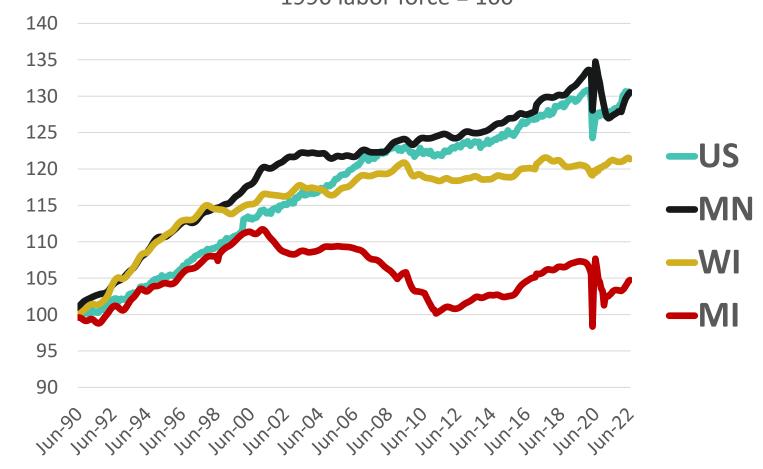
 $0\% \ 10\% \ 20\% \ 30\% \ 40\% \ 50\% \ 60\% \ 70\% \ 80\% \ 90\%$



Source: Federal Reserve Bank of Minneapolis, General Business Survey, July 2022

LABOR FORCE POPULATION: SLOWING

Labor force population index 1990 labor force = 100



Labor force population: Those employed or unemployed and looking (counted only once regardless of jobs held)

Labor force growth slowed dramatically since 2000

- Slowing population growth
- Lower labor force participation



LABOR FORCE PARTICIPATION

Labor force participation index 1990 labor force = 100LFP definition = 78 Share of those over 16, working, 76 or looking for work 74 72 70 MN Percent 68 WI 66 -US 64 62 M 60 58 56 1417-22 111,90

FEDERAL RESERVE BANK OF MINNEAPOLIS

LFP rates in decline since late 1990s

Finally started to pivot higher ... and then pandemic hit

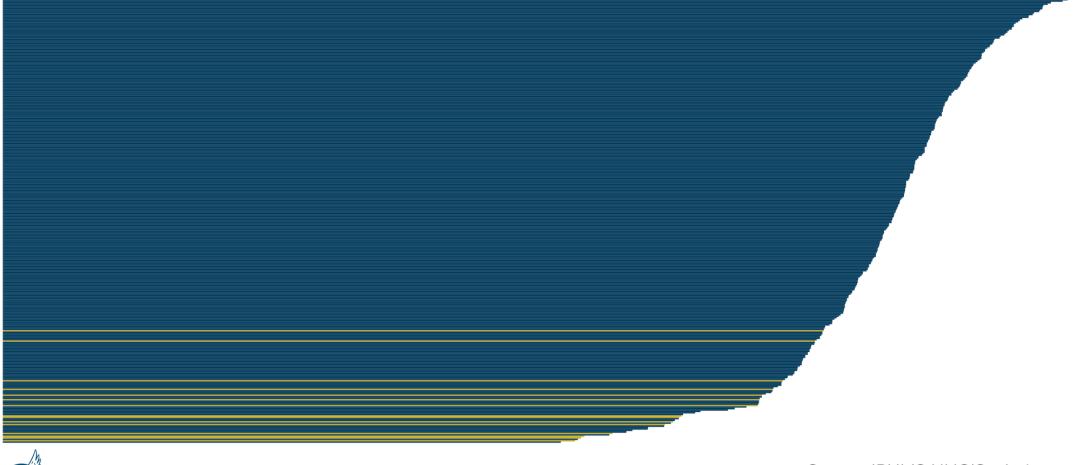
Unlikely to 'bounce' back to pre-pandemic levels

Source: Bureau of Labor Statistics

UP LABOR FORCE PARTICIPATION

The Upper Peninsula has low labor force participation

Labor force participation for Ninth District counties, with Michigan counties highlighted

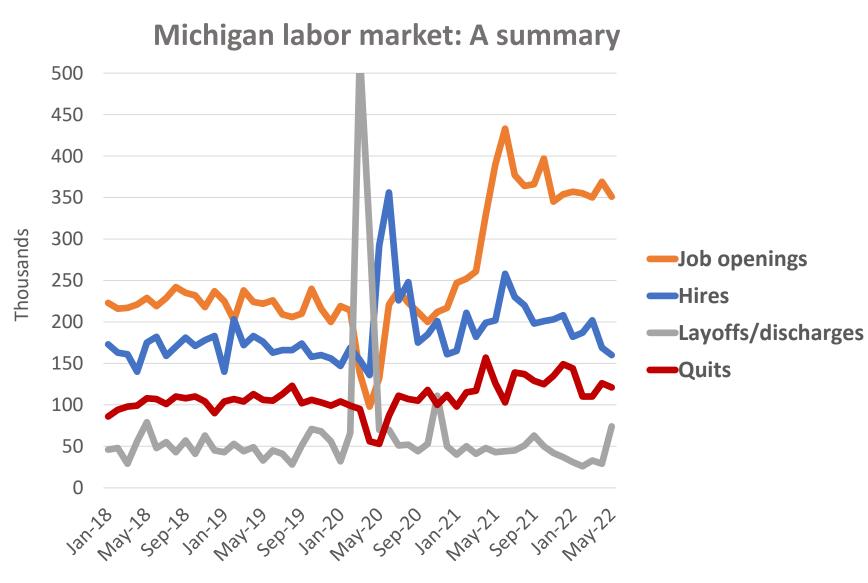




Source: IPUMS NHGIS, nhgis.org Graph by David H. Montgomery / Minneapolis Fed

Slide 26

JOB OPENINGS AND LABOR TURNOVER SURVEY



Hiring demand up strongly

Actual hires lower, and falling

Voluntary quits still higher than normal; compounds labor problem

Layoffs low & stable, except...?



WHY ARE SO MANY JOBS GOING UNFILLED?



TODAY'S LABOR FORCE NARRATIVE From business surveys and other outreach

- "Nobody wants to work any more; workers are lazy; Government benefits are too generous"
- These things likely true to some extent
- But it's also a too-simple generalization; likely fits only small share of non-working population
 - Misses much more complicated labor picture
 - Research shows most people want to work, but job-matching faces lots of obstacles and friction
 - By over-generalizing, we're misdiagnosing real problems and overlooking real solutions



WORKER EXPERIENCE INITIATIVE

- Federal Reserve has always tracked the economy
- Typically done via outreach to businesses
 - Offer good insights on aggregate activity, as well as insights across geography, industry, etc.
- But business-centric view is very one-sided, esp. regarding labor market environments



WORKER EXPERIENCE INITIATIVE

- New effort: Understand current labor market from worker point of view – their objectives, job search experience
- WHY? Labor force participation arguably the single most important factor in long-term economic growth
 - Started research with intermediaries organizations that provide job-search services
 - 6 surveys in first year in three states



THE FLIP SIDE OF LABOR AVAILABILITY: WORKER VIEW

Extreme challenge

Significant challenge

Moderate challenge

Not applicable / Unsure

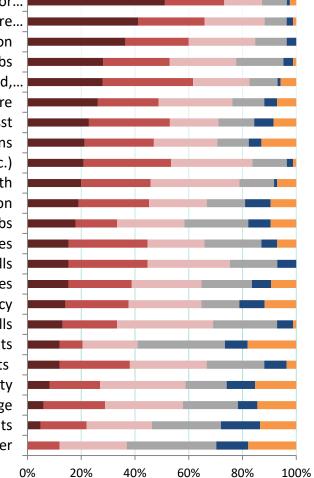
Slight challenge

Not a challenge

Perceptions of job obstacles faced by Minnesota job seekers

Survey of staff, Minnesota Employment Services Coalition

Affordability of day care (children or... Affordability of housing where jobs are... Lack of transportation Low pay at available jobs Background issues (e.g. record,... Concern over COVID-19 exposure Potential loss of govt asst Lack of a telework options Access to technology (computer etc.) Mental health Lack of employer response to application Low benefits at available jobs Pre-existing health/medical issues Lack of 'hard' skills Employer screening/HR practices English proficiency Lack of 'soft' skills Occupational licensing requirements Excessively high job requirements Bias - race/ethnicity Bias - age Unemployment benefits Bias - gender



Multitude of potential obstacles to labor force participation

Some worker-based

Some employer-based

Some related to economic environment, government policy

Source: Minneapolis Fed, October 2021



SO WHAT? WHY DOES THIS MATTER?

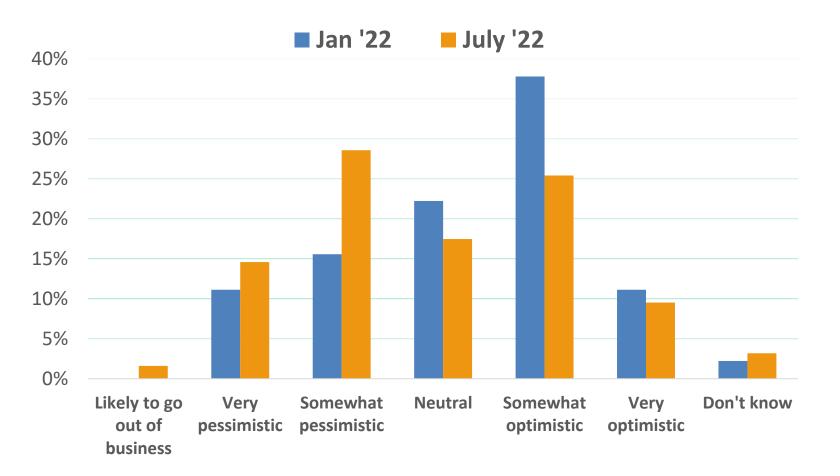
- In the past: Labor <u>surplus</u> meant businesses could be choosey
 should be choosey to find best workers
- Present: Labor <u>shortage</u> means *workers have leverage*, and we have to treat obstacles that workers face from a problem-solving POV *if we want more people to work*
- Clearly already happening (e.g. higher wages). Will it continue?
- We can decide to do nothing, keep status quo; but then we have to accept slower growth



OUTLOOK



Outlook for the coming six months



Outlook has turned more pessimistic Again, partly a 'respondent composition' issue But hard to dispute the downturn in overall sentiment

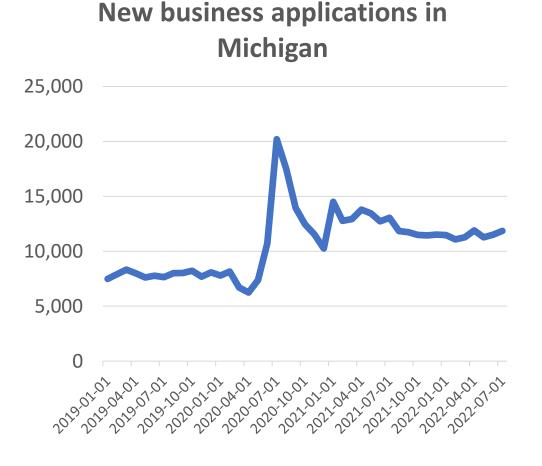


Source: Federal Reserve Bank of Minneapolis, General Business Survey, January and July, 2022

LET'S END ON A MORE UPBEAT NOTE, YES?

GOOD VIBRATIONS

- Recent data suggests some macro improvements in the economy of late (prices, supply chains)
- Still very early, and the Federal Reserve is committed to bringing inflation back to target, hopefully without damaging hiring demand
- Some evidence that pandemic has sparked innovation & entrepreneurship
- Pandemic has proven (again, and again) the resilience of U.S. & MI & U.P. businesses





THANK YOU! QUESTIONS? SPEECH/WEBINAR REFERRALS WELCOME! **TWITTER: @RONWIRTZ @MINNEAPOLISFED CONNECT VIA LINKEDIN** RON.WIRTZ@MPLS.FRB.ORG