FedListens

A primer: Transitioning to the Post-Pandemic Economy

This material supports the Federal Reserve Bank of Boston's May 31 Fed Listens event, "*Transitioning to the Post-Pandemic Economy,*" which has engaged a diverse set of leaders from a cross section of the New England economy to discuss their experiences with challenges and opportunities following the disruptions of the COVID-19 pandemic. The conference is part of the Federal Reserve Board's Fed Listens series.

As part of today's event, we want to hear your thoughts and perspectives on how labor markets, housing markets, and state and local public finance have changed and are changing based on the pandemic experience. To facilitate this conversation, we are sharing this brief, high-level overview material that profiles our understanding of current conditions and relevant trends.

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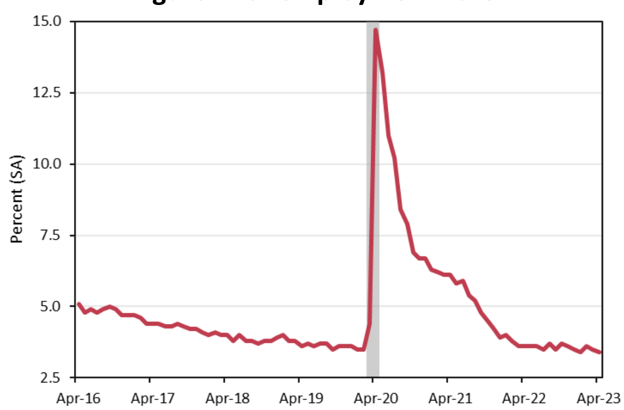
Transitioning to the Post-Pandemic Economy: Overview of Labor Market Conditions

1. Labor market recovery since the start of the pandemic

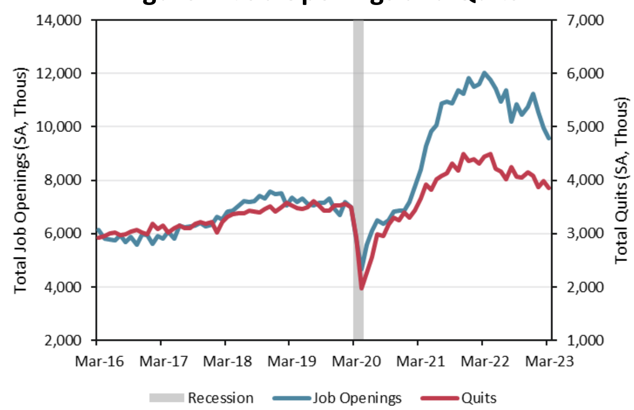
The unemployment rate—the share of the labor force that does not have a job but is looking for one—typically rises sharply in recessions, and the COVID-19 pandemic recession of 2020 (denoted by the vertical gray bar in both figures below) was no exception. The unemployment rate reached 14.7 percent in April 2020, the highest it has been in the postwar era (**Figure 1**). After April 2020, businesses reopened from pandemic shutdowns, and the unemployment rate fell rapidly. By mid-2022, it had returned to its pre-pandemic level of 3.5 percent, which was among the lowest unemployment rates since the late 1960s. The most recent jobs report, covering April 2023, placed the unemployment rate at 3.4 percent.

Figure 1. Unemployment Rate



Note: *Civilian population aged 16 and older*
Sources: *Bureau of Labor Statistics, NBER, Haver Analytics*

Figure 2. Job Openings and Quits



Sources: *Bureau of Labor Statistics, JOLTS, NBER, Haver Analytics*

Data on job openings and on workers quitting their jobs indicate that the current labor market is even better for job seekers than it was before the pandemic. For example, the total number of job openings (also called job vacancies) reached 12 million in early 2022 (**Figure 2**). This was by far the highest level since December 2002, when the US Bureau of Labor Statistics began collecting official data on vacancies. Job openings and quits have been declining since early 2022, but they remain well above pre-pandemic levels.

2. Employment and labor force participation for different groups of workers

During the pandemic era, labor market experiences have varied markedly across different groups of workers. One key labor market statistic is the participation rate, which is the fraction of people in a given population who are "participating" in the labor market—that is, who either have a job or are looking for one. In **Figure 3** on the next page, the blue bars depict participation rates just before the pandemic for demographic groups defined by education, age, and race/ethnicity. Participation tends to be higher for people with a college education and for people in their "prime" working years (aged 25 to 54). Participation also tends to be higher for white people than for Black people, although Hispanic people (either white or Black) had the highest participation rate of any racial/ethnic group on the eve of the pandemic. The unemployment rate can also be used to analyze the experience of individual demographic groups. The red bars in **Figure 3** show that unemployment tends to be higher among less educated people and is especially high for people aged 16 to 24. (Because young workers are just starting their careers, they are more likely to quit their jobs in search of better ones.) The unemployment rate among Black workers has traditionally been much higher than the rate among white workers. The rate among Hispanic workers is somewhere in between, and the rate among Asian workers is the lowest of all racial groups.

Figure 3. Pre-Pandemic Participation and Unemployment Rates

Average values from November 2019 to February 2020

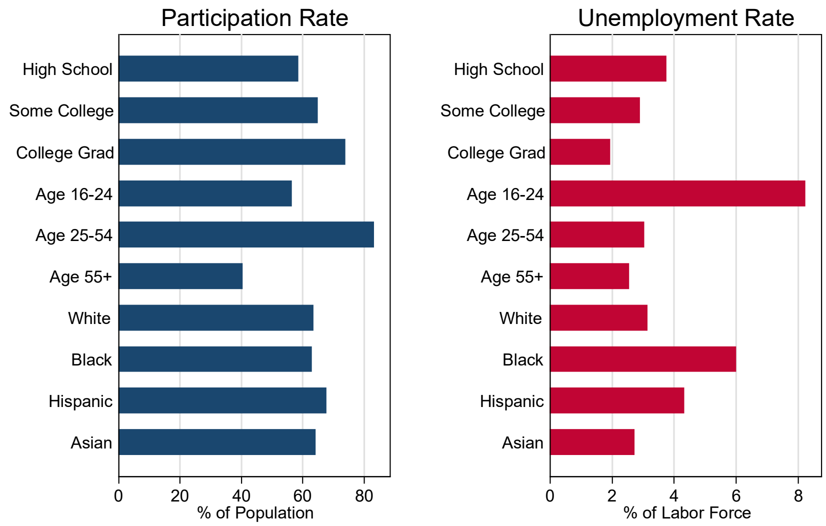


Figure 4. Changes in Participation and Unemployment Rates

November 2019-February 2020 to January-April 2023

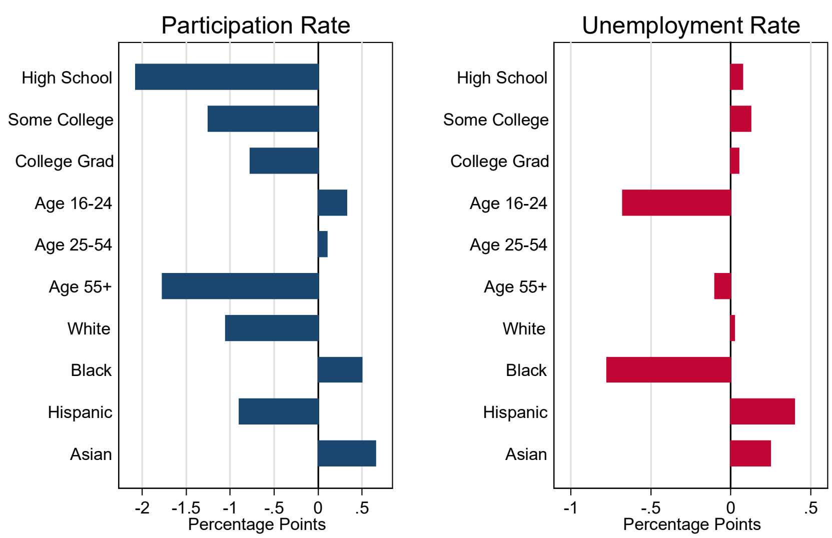


Figure 4 shows *changes* in labor force participation and unemployment since the pandemic began. Participation has declined for all educational groups but has fallen most among people with only a high school education. Older workers (aged 55-plus) have experienced a striking drop in participation, which could reflect early retirements brought on by the pandemic. For young and prime-age workers, participation is now higher than before the pandemic, which argues against the notion that a so-called Great Resignation fundamentally altered the American labor supply. Across racial/ethnic groups, participation among white and Hispanic people has fallen, while the rates for Black and Asian people have increased.

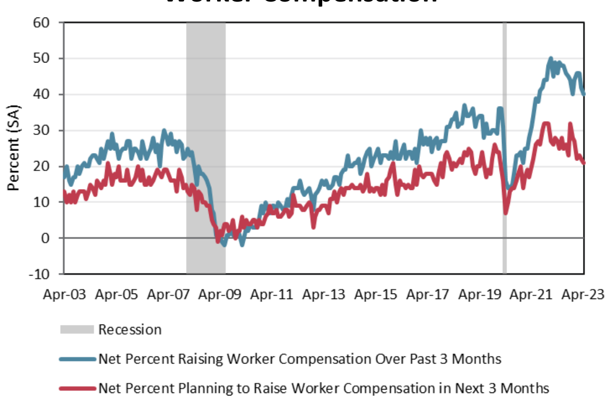
The red bars in **Figure 4** indicate one possible reason why the participation rate for Black people has increased: Black workers are far *less* likely to be unemployed today than before the pandemic. A tight labor market—where there are more available jobs than unemployed workers willing and able to fill them—tends to favor demographic groups that have relatively high unemployment rates; note that young workers have also seen their unemployment rates decline. As the economy has continued to grow following the COVID-19 crisis, the unemployment rate for Black workers has fallen to historic lows, hitting 4.7 percent in April 2023. The difference in unemployment rates between white and Black workers has also fallen to historic lows; after averaging 4 percentage points over the preceding 10-year period, the difference in unemployment rates between white and Black workers is now just 1.6 percentage points. Unemployment for Hispanic workers has been somewhat higher over the past four months than before the pandemic, but the month-to-month data for 2023 (not shown in the graphs) indicate that the rate may be trending lower this spring.

3. Employers' efforts to recruit and retain workers

The tight labor market has forced employers to work harder to attract and retain workers. They have raised wages and adopted more flexible work practices. Before the pandemic, wage increases became increasingly common as the economy expanded steadily for many years (**Figure 5**). Wage increases nearly disappeared with the onset of the pandemic, but as the economy recovered and the labor market grew tighter, pressure on employers to raise wages returned even stronger than it was before the pandemic. In late 2021, half of the small businesses surveyed by the National Federation of Independent Businesses reported that they had raised their workers' wages over the preceding three months, and one-third indicated that they planned to do so over the next three months. The share of small businesses raising wages has declined only slightly since then and remains well above pre-pandemic levels today.

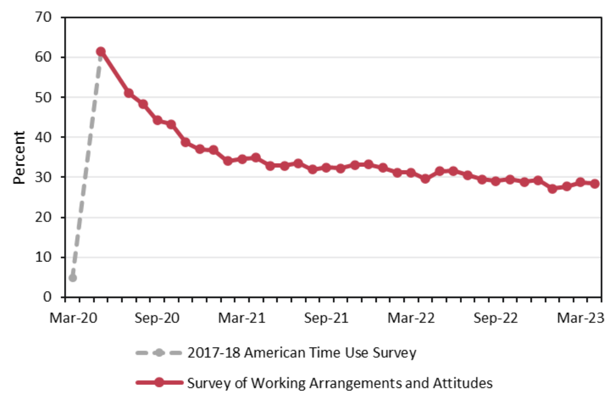
Increased remote work is also likely to be a lasting feature of the US labor market. During the early stages of the pandemic, remote work was critical to the continued operation of many businesses; in May 2020, 60 percent of all paid working days took place at home (**Figure 6**). The extent of remote work has receded as the pandemic has faded; since mid-2021, the share of total paid work taking place at home has remained about 30 percent.

Figure 5. Small Business Economic Trends: Worker Compensation



Sources: *National Federation of Independent Business, NBER, Haver Analytics*

Figure 6. Percentage of Paid Full Days Worked from Home



Note: *The survey question changed in November 2020.*
Source: *Barrero, Jose Maria, Nicholas Bloom, and Steven J. Davis. 2021. "Why Working from Home Will Stick." National Bureau of Economic Research Working Paper 28731.* *www.wfhresearch.com*

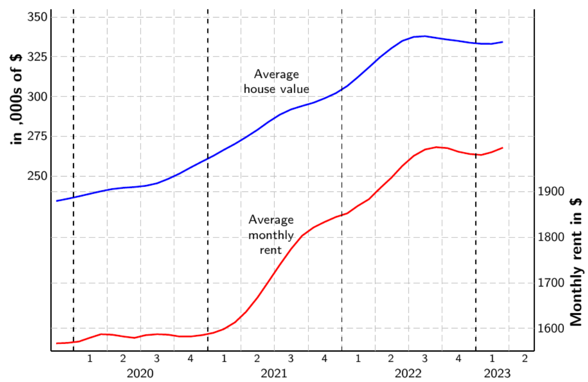
Transitioning to the Post-Pandemic Economy: Overview of Housing Market Conditions

1. National housing market conditions: prices, rents, listings, and sales

The COVID-19 pandemic had diverse impacts on housing markets across the country. Initially, widespread job losses made it challenging for many households to meet rent and mortgage obligations. Furthermore, house sales and construction activities were disrupted. As the pandemic persisted, the shift to remote work, as well as some residential migration, brought about significant changes in housing requirements, leading to substantial increases in house prices and rents. More recently, the increase in mortgage rates has presented additional hurdles for some families aspiring to purchase homes.

The most recent data show that house prices and rents have stabilized at a high level, roughly 40 percent and 25 percent above their pre-pandemic levels, respectively **(Figure 1a)**. The strength of the housing market is surprising given how much interest rates have risen. Indeed, since the start of 2021, mortgage rates have climbed 3 percentage points, and the median home buyer is spending more than $2,100 per month versus about $1,500 at the end of 2021 and less than $1,400 in 2020 **(Figure 1b)**.

Figure 1a: Average House Prices and Rents



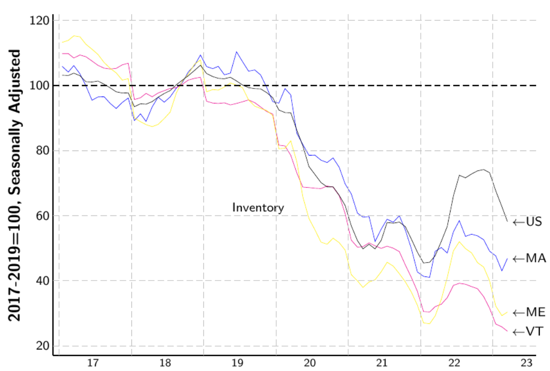
Source: *Zillow*

Figure 1b: Mortgage Rates and Monthly Payments

Source: *Optimal Blue*

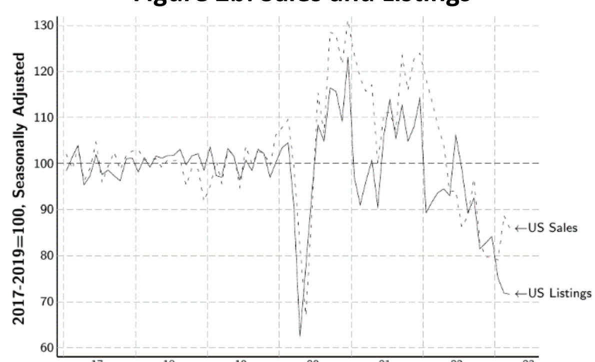
In addition, the inventory of homes on the market is about 40 percent below its pre-pandemic level nationally and is even lower in New England **(Figure 2a)**.

Figure 2a: Inventory of Homes on the Market



Source: *Redfin*

Figure 2b: Sales and Listings



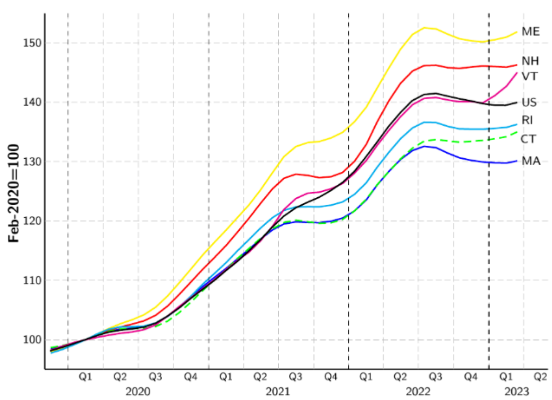
Source: *Redfin*

The low inventory reflects the surge in mortgage rates. As rates have increased, homeowners have chosen to retain their low-interest mortgages and postpone listing their properties for sale **(Figure 2b)**. With few new listings to replenish the inventory, home sales, which are only about 10 percent below their pre-pandemic level, have drained the market.

2. Prices in New England

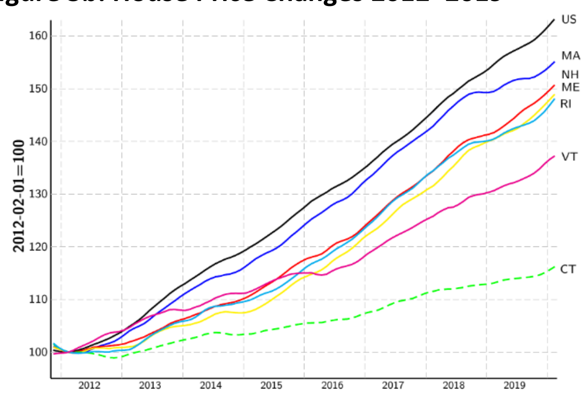
The pandemic brought about a shift in the patterns of house-price growth in New England, with rural-area prices rising much more significantly than urban-area prices. In Maine, prices have surged by more than 50 percent since 2020, whereas in Massachusetts, the increase has been only 30 percent **(Figure 3a)**. This price-change pattern deviates from longer-term trends in many states **(Figure 3b)** and has likely been influenced by household-migration patterns in the region. For example, from 2012 through 2019, the year before the onset of the pandemic, Massachusetts saw relatively strong price growth compared with the more rural New England states of Maine and Vermont, where prices increased at a rate that was well below the national average.

Figure 3a: House Price Changes since 2020



Source: *Zillow*

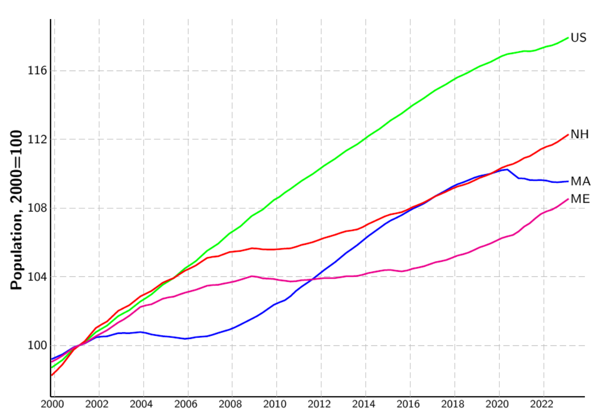
Figure 3b: House Price Changes 2012–2019



Source: *Zillow*

Moreover, recent house-price changes have been tied to population gains. States with faster population growth since the start of the pandemic period, such as Maine and New Hampshire, have seen more rapid price increases **(Figure 4)**. In Massachusetts, where population growth has been flat, price increases have been the slowest in New England over this time.

Figure 4: Population Growth

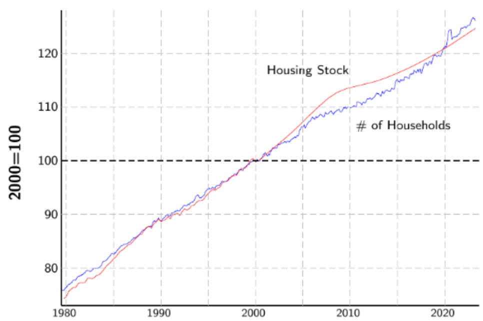


Source: *US Census*

3. Why are prices so high?

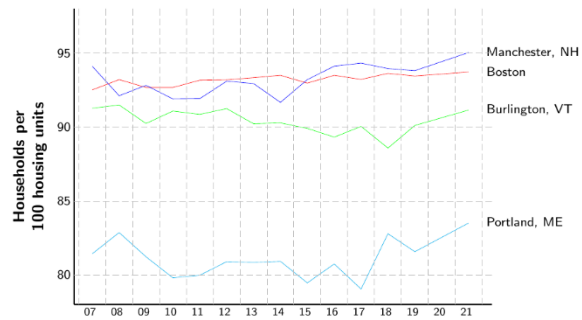
The housing market is out of balance. Before 2020, the combination of new construction and a large inventory of vacant properties left from the speculative boom of the 2000s enabled the market to keep pace with the increase in the number of households in New England **(Figure 5a)**. However, the market has been unable to cope with the accelerated growth in households that started in 2020, particularly outside the region's major metropolitan area of Boston **(Figure 5b)**.

Figure 5a: Housing Supply, 1980–Present



Source: *Housing Vacancy Survey*

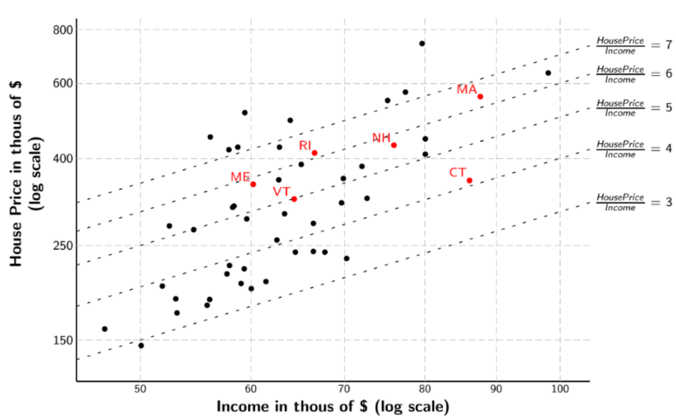
Figure 5b: New England, 2007–Present



Source: *US Census*

Indeed, one of the significant challenges with housing in New England is the presence of low-income areas in an overall high-income region. New England is home to some of the highest-income metropolitan areas in the United States and is adjacent to New York City. The high-income households in these cities contribute to increasing local property prices, and this trend spills over to the rest of the region through the second-home market **(Figure 6)**. The New England states of Maine, Rhode Island, and Vermont have much higher house prices when compared to most other states with comparable levels of income.

Figure 6: House Prices vs. Income



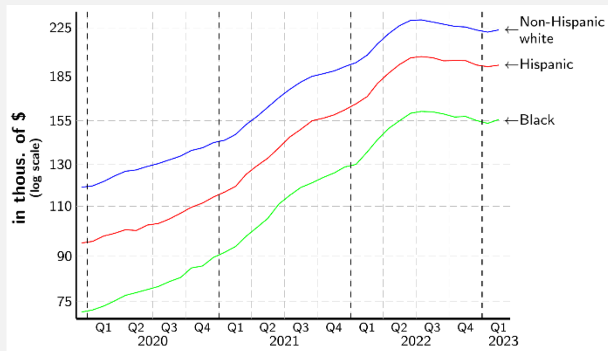
Sources: *Zillow, US Census*

4. Housing wealth

Increasing house prices have had a positive impact on household balance sheets, benefiting a broad range of individuals. The rise in median home equity among mortgage borrowers has been observed across various regions **(Figure 7a)** and demographic groups throughout the country **(Figure 7b)**. Within New England, the gains in equity have been greater in the smaller and more rural states. Nationally, equity gains have been relatively larger for Black, and to some extent Hispanic, homeowners than for white homeowners. This difference by race is due primarily to the fact that sharp increases in house values result in larger equity gains for homeowners with relatively higher mortgage balances.

Figure 7a: Housing Equity by State

Figure 7b: Housing Equity by Race



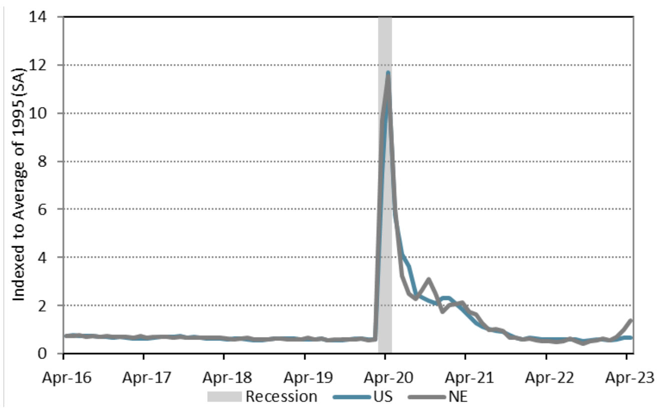
Sources: *McDash, Equifax, HMDA, and CoreLogic*

Transitioning to the Post-Pandemic Economy: Overview of State and Local Government Fiscal and Economic Policy Conditions

1. Federal revenue transfers to state and local governments in the early part of the pandemic

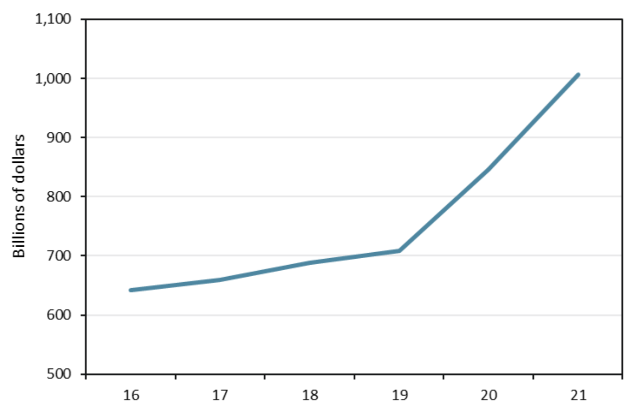
In response to the COVID-19 pandemic, the federal government implemented unprecedented policy initiatives that had a dramatic impact on state and local governments. These initiatives included discretionary fiscal policy and the supplementation of unemployment insurance and other existing programs. The number of initial claims for unemployment insurance surged from 900,000 in February 2020 to a historic level of more than 18 million in April 2020 (**Figure 1**). The number of claims did not fall below 1 million again until December 2021. In addition to providing financial assistance directly to households and businesses, the federal government transferred an unprecedented amount of more than $1 trillion in revenue to state governments in 2021. By contrast, revenue transfers were about $700 billion in 2019, the year before the onset of the pandemic (**Figure 2**).

Figure 1. Initial Claims for Unemployment Insurance



Sources: *Department of Labor, NBER, Haver Analytics, Federal Reserve Bank of Boston*

Figure 2. Federal Revenue Transfers to State Governments



Sources: *Bureau of the Census, Haver Analytics*

The American Rescue Plan Act, which was signed into law in March 2021, included $350 billion in emergency funding for state, local, and territorial and tribal governments. Known as the Coronavirus State and Local Fiscal Recovery Funds, this money has been used to replace lost revenue, increase human services and health-care services, strengthen unemployment insurance, and promote economic development. As of December 1, 2022, states collectively had yet to appropriate more than $25 billion of this funding. Policymakers face important decisions regarding how to best use these remaining federal funds.

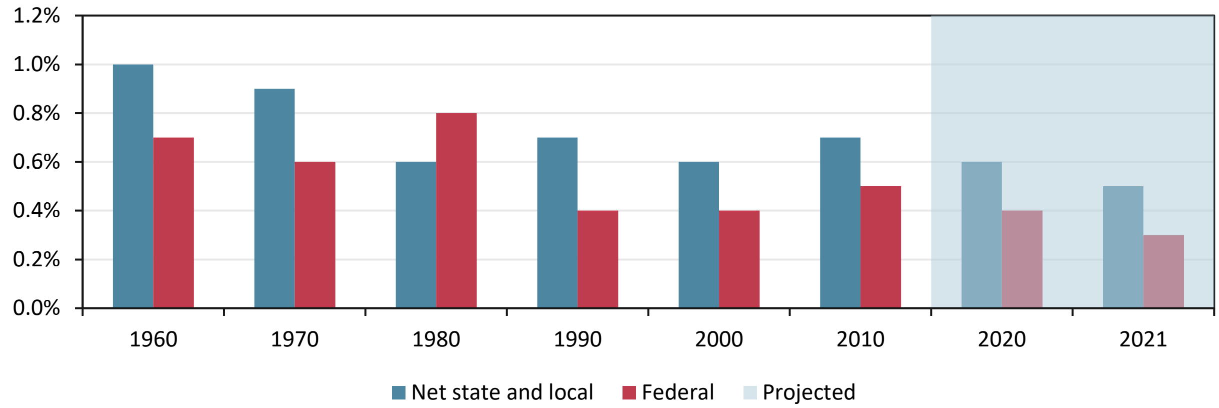
2. Infrastructure funding

After the onset of the COVID-19 pandemic, the federal government also authorized major infrastructure investments for state and local governments to implement. The $1.2 trillion Infrastructure Investment and Jobs Act was signed into law in November 2021 with the goals of rebuilding America’s roads, bridges, and rails; expanding access to clean drinking water; increasing access to broadband internet; and addressing energy- and power-infrastructure needs. The law included $550 billion in funding for new investments and programs.

For several decades, the rate of infrastructure investment has been declining or stagnant at best (**Figure 3**). The Volcker Alliance estimated in 2019 that the cost of delayed repairs and maintenance that had accumulated nationally over the preceding 50 years was close to $1 trillion, or about 5% of the US gross domestic product. Funds from the Infrastructure Investment and Jobs Act will help to address this gap in infrastructure investment.

Figure 3. Rates of Government Infrastructure Spending, Selected Years 1960-2021

Capital investments as a percentage of gross domestic product



Note: *Projected portion for each category of spending for 2020 and 2021 indicates Pew estimates using federal data.*
Sources: *Subset of Pew analysis of economic data from the Federal Reserve; Federal Highway Administration data; and data and analysis from the Congressional Budget Office report "Public Spending on Transportation and Water Infrastructure, 1956 to 2017"; © 2023 The Pew Charitable Trusts*

3. Challenges and opportunities highlighted during the pandemic

During the pandemic, many federal, state, and local agencies faced significant challenges managing new and large federal aid programs, especially considering the need to distribute aid quickly. Many had outdated IT and financial-management systems and encountered difficulties with inter-agency coordination and conducting adequate oversight. Such factors increased the risk of fraud and misuse of these funds.

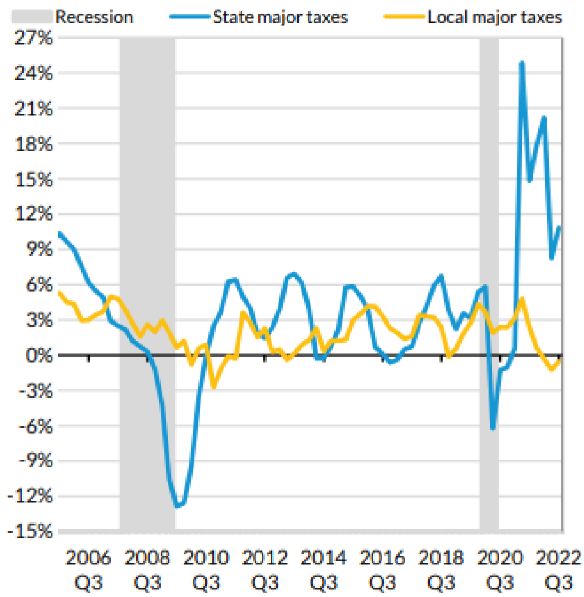
These challenges were evident in, but not limited to, the unemployment insurance program. The US Department of Labor and state governments were not adequately prepared to handle unemployment insurance fraud risks when the pandemic began. The expedited rollout of COVID-19 relief funding further exacerbated the improper-payment problem. The US Government Accountability Office estimates that states collectively made more than $60 billion in fraudulent unemployment insurance payments during the pandemic.

4. State taxes and revenue

Contrary to expectations, state tax collections dipped only briefly early in the pandemic before surging to unprecedented levels (**Figure 4**). Stronger-than-expected tax revenues alongside federal transfers have allowed state policymakers to contemplate a range of potential investments and to substantially increase financial reserves. State rainy day funds reached new heights in fiscal years 2021 and 2022 and are projected to increase further in fiscal year 2023. In 2022, state rainy day fund balances reached $134.5 billon, which amounted to 12.4 percent of state general fund spending (**Figure 5**).

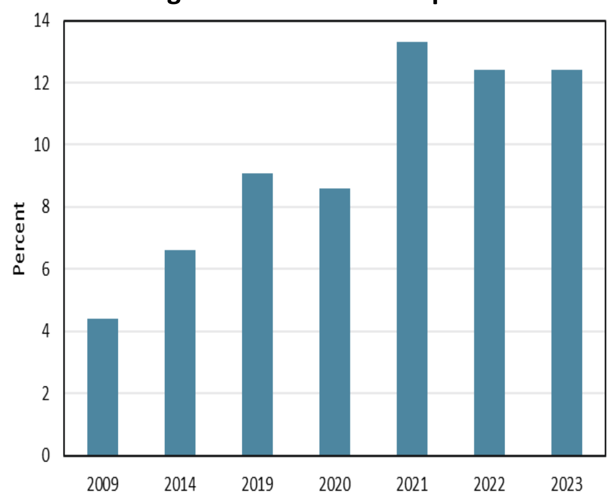
Figure 4. State and Local Major Tax Revenues Weakened in the Third Quarter of 2022

Year-over-year inflation-adjusted percentage change in state and local taxes from major sources



Sources: *Urban Institute: US Census Bureau (tax revenue) and Bureau of Economic Analysis (GDP)*
Notes: *Year-over-year change is the percentage change of four-quarter moving averages. Data are adjusted for inflation. Data are for four major tax categories only: personal income, corporate income, general sales, and property.*

Figure 5. Rainy Day Fund Balances as a Percentage of General Fund Expenditures



Sources: *National Association of State Budget Officers, Fall 2022 Fiscal Survey of States*

In this environment, many states have pursued tax cuts. In fiscal year 2023, according to the National Association of State Budget Officers, 31 states enacted net decreases in taxes and fees, while just five adopted net increases, resulting in a projected net revenue decline of $16.2 billion for all state funds. However, state and local tax revenues have weakened since mid-2022, while major federal relief measures related to the pandemic are also winding down. There is ongoing debate among policymakers and fiscal watchdog groups as to whether tax cuts are prudent—particularly permanent ones—or whether states should further strengthen rainy day funds and unemployment insurance funds, increase long-term investment in education and infrastructure, and protect public services from a potential economic downturn.