Congressional Research Service
Informing the legislative debate since 1914

INSIGHT

Labor Market Tightness and the Economic Recovery, Part 1

October 5, 2021

Recently, many businesses have reportedly complained of challenges posed by labor market "tightness"—workforce shortages and difficulties in hiring to reduce them. This is generally considered unusual when employment is still low by historical standards—one of the many unusual economic phenomena that have occurred during the Coronavirus Disease 2019 (COVID-19) pandemic. If long-lasting, these shortages could hold back the economic recovery and potentially contribute to inflationary pressures. This Insight examines evidence of tightness. A companion Insight (Part 2) discusses potential causes and policy implications.

Evidence of Tightness …

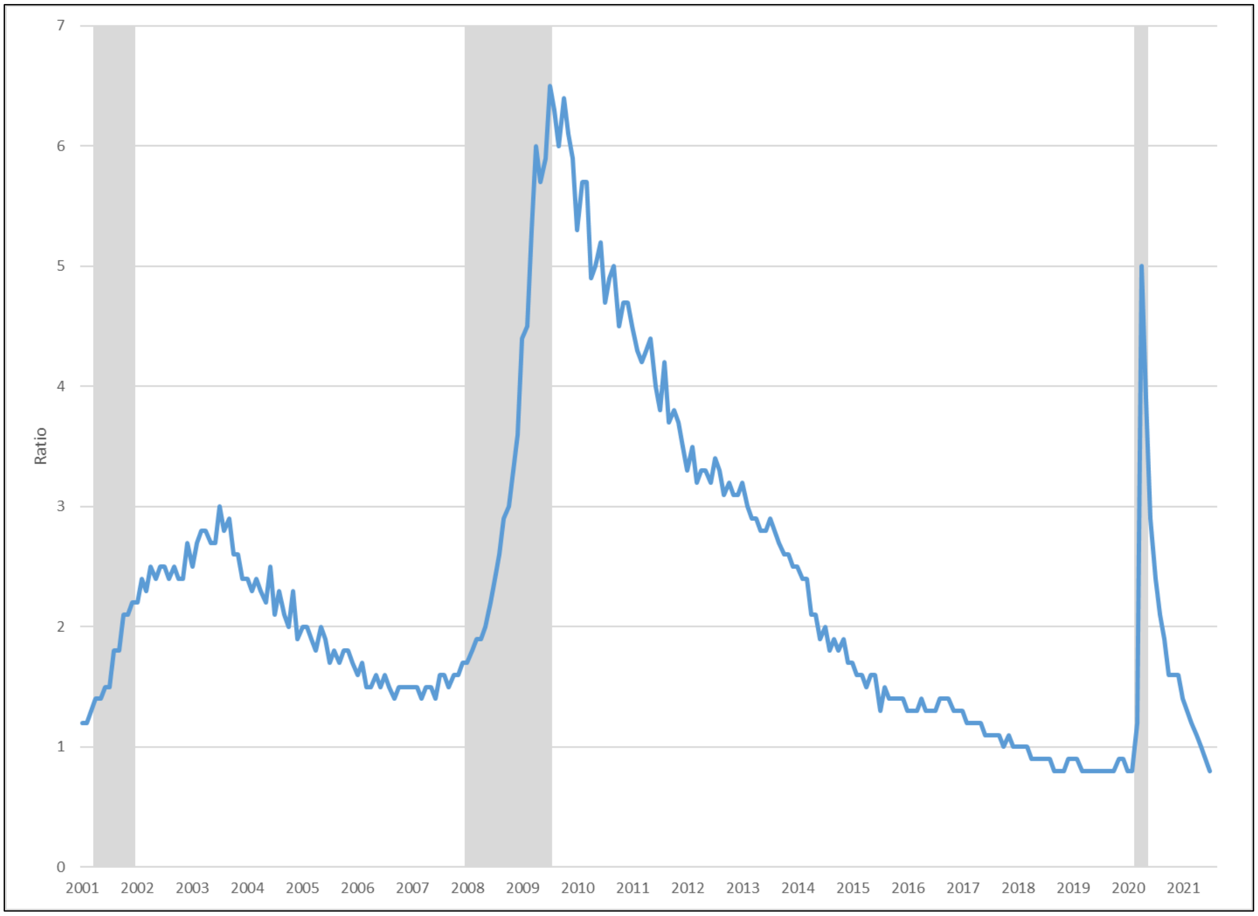
There is no single, direct measure of labor market tightness, but one popular proxy measures the ratio of unemployed workers to job openings (see **Figure 1**). This measure provides a comparison of how many workers are unemployed and actively looking for jobs with how many positions employers are looking to fill. In July 2021, there were fewer than one unemployed worker per job opening. This ratio, which rises in recessions and declines in expansions when the labor market tightens, is lower than in previous expansions and similar to the level reached before the pandemic, when the unemployment rate was 3.5%.

Congressional Research Service
https://crsreports.congress.gov
IN11770

CRS INSIGHT
Prepared for Members and
Committees of Congress

Figure 1. Ratio of Unemployed Workers to Job Openings

1/2001-7/2021



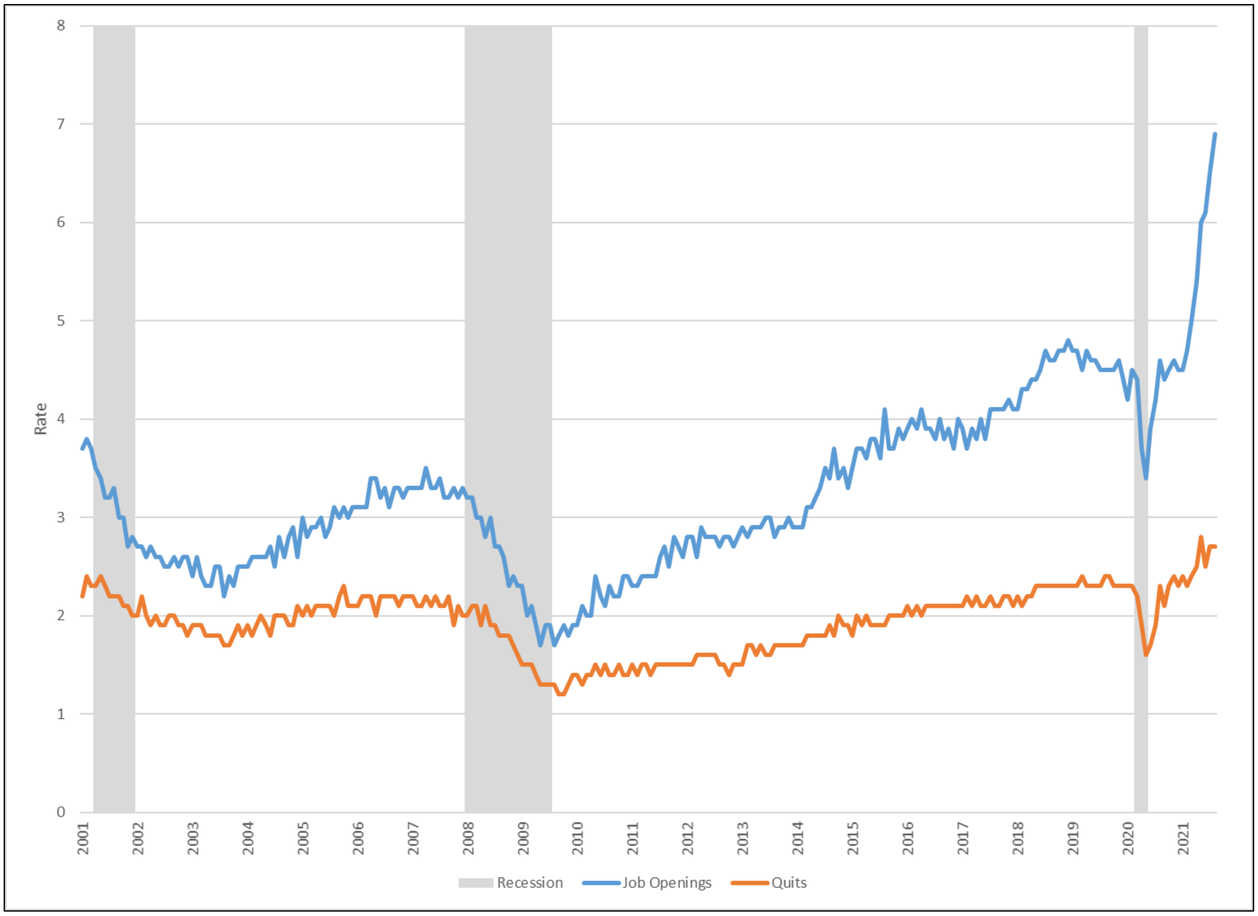
Source: Bureau of Labor Statistics (BLS).

Notes: Gray bars denote recessions.

This ratio has fallen quickly in the recovery because unemployment has fallen and job openings have risen to the highest rate in the history of the data series (see **Figure 2**). At the same time, the rate of workers quitting their jobs—which they tend to do when alternative job opportunities are abundant—is also at a series high. After dipping early in the pandemic, the rise in both of these series in the recovery points to tighter labor markets.

Figure 2. Job Openings and Quits Rates

1/2001-7/2021



Source: BLS.

Labor shortages may be less of an economy-wide phenomenon than one specific to certain industries, however. This would also be consistent with a rise in the job openings rate and quits rate. The pandemic caused changes in demand that necessitated job reallocation across industries, resulting in an outsized decline in employment in certain industries and occupations during the recession. Now that the economy is expanding, jobs are being added back quickly—some in the industries that were hardest hit, others in industries that have benefited from the shift in spending patterns—creating a temporary surge in openings. For example, employment in the leisure and hospitality industry declined from 16.9 million in February 2020 to 8.7 million in April 2020. Many of these workers moved on to other industries after they lost their jobs. When health restrictions on leisure and hospitality were lifted, the industry needed to add back workers quickly, but those workers were no longer available or willing to return to work. As of August 2021, the industry is 1.7 million jobs below its February 2020 level and is one of the industries that has anecdotally struggled most with labor shortages.

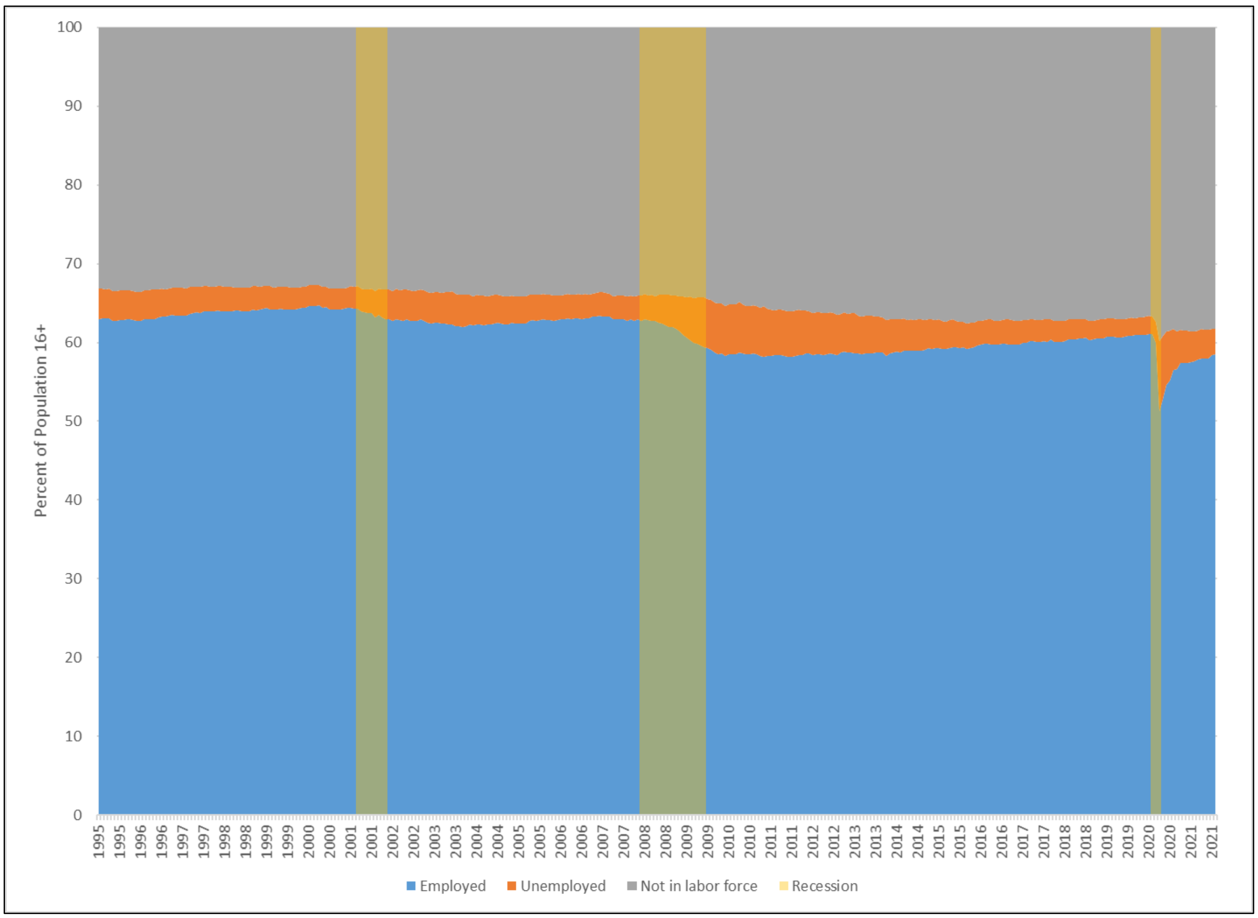
Some point to wage increases as more evidence of labor market tightness—employers unable to attract applicants at prevailing wages may be responding by increasing wage offers. However, wage increases are noticeably pronounced only in certain industries, and even those industries have not seen any significant gains in wages after adjusting for inflation. For more information, see CRS Insight IN11711, *The Post-Pandemic Labor Market and Rising Inflation*, by Lida R. Weinstock.

… Despite Low Employment Rates

In the past, labor market tightness has been associated with high rates of employment. It is unexpected now when employment is still low—the percentage of the population working fell from 61% before the pandemic to 51% in April 2020 and has rebounded to only 58.5% today. As **Figure 3** shows, this is still low by historical standards, including compared to during the past two recessions. Initially, the sudden drop in employment caused many workers to become unemployed (i.e., out of a job but looking for work), while others left the labor force (i.e., were not actively seeking work). In the subsequent recovery, the share of the population that is unemployed fell quickly and is now one percentage point higher than before the pandemic. The labor force participation rate (LFPR) is the sum of employed and the unemployed as a share of the population, which can be seen by combining the blue and orange areas in **Figure 3**. The LFPR has recovered less than unemployment has. It is 61.7% today, which is still lower than at any time pre-pandemic in recent decades. Before the pandemic, the lowest it reached was 62.4% in 2015, and it was 63.4% immediately before the 2020 recession.

Figure 3. Population by Work Status

1/1995-8/2021



Source: CRS calculations based on BLS data.

Notes: This chart measures unemployment as a percentage of the population, not the official unemployment rate.

The low LFPR provides ambiguous evidence of how long labor markets may remain tight, because it is unclear whether workers exited the labor force permanently. It could mean that there are many individuals waiting on the sidelines to re-enter the labor force once economic or public health conditions improve. Alternatively, it is possible that many former workers either cannot or do not want to come back to work—or will no longer have the right skills when they do want to come back. Labor market tightness would be relieved under the former scenario but not the latter. To interpret which of these scenarios better matches current conditions, Part 2 looks at reasons why people have remained out of the labor force during the recovery.

Author Information

Marc Labonte
Specialist in Macroeconomic Policy

Lida R. Weinstock
Analyst in Macroeconomic Policy

Disclaimer