A View of the U.S. Economy and Rural and Urban Labor Market Dynamics

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- Atlanta Fed President and CEO Raphael Bostic speaks November 14 at Auburn University at Montgomery on current economic conditions as well as economic prospects in rural and urban areas.
- Bostic's economic forecast for the foreseeable future is of GDP growth continuing a bit above 2 percent, the unemployment rate in the low 4s, and modest increases in real wage growth.
- Bostic thinks it will be appropriate for interest rates to rise gradually over the next couple of years.
- Bostic notes that the Great Recession and the subsequent recovery have intensified labor force disparities between urban and rural areas.
- Bostic says Atlanta Fed research suggests that differences in health and disability account for a large part of the disparity among regions for less-educated workers.
- Bostic believes the Federal Reserve System can play an important role as a facilitator to help local and state business, community, and government leaders find ways to maximize economic opportunity in both rural and urban communities.

Good afternoon, everyone, and thank you for that kind introduction.

This is my first trip to Montgomery. I'm excited to be here and to get to know the city and region better. Later today, I'll be meeting with some local experts in workforce development—a topic I'm especially interested in. It's a big focus of our community development efforts at the Atlanta Fed.

I want to acknowledge the thought leadership we have gotten from Alabama through your Alabama Industrial Development Training program. The leader of the AIDT effort, Ed Castile, sits on the advisory council for the Atlanta Fed's Center for Human Capital Studies.

I've been learning a lot about the Southeast in the past few months, and it's my honor to bring that information to the monetary policy table when we meet every eight weeks or so.

This afternoon, I'd like to share my views on current economic conditions and talk a bit about how my team and I arrive at a policy outlook. Then I'll turn to an issue that is coming up in my discussions with my staff and local leaders more and more—namely, the differences we are seeing in economic prospects between rural and urban areas.

Before I begin, let me offer a familiar disclaimer. I'll present only my personal views today. I'm not speaking for the Federal Reserve or for the Federal Open Market Committee.

Economic update
So let's begin with where the national economy stands in the fourth quarter. Despite the series of recent hurricanes that hit the South, economic activity has grown at a reasonably solid pace in recent months. Gross domestic product, or GDP, is estimated to have increased by a little over 2 1/4 percent during the past year, and the unemployment rate now sits at 4.1 percent—down more than half a percentage point from a year ago.

In my view, the national economy is nearing full employment, meaning that a spike in demand could push the economy beyond its sustainable capacity. This would put pressure on labor costs, as businesses would have to compete more aggressively for an increasingly limited pool of available workers.

That said, I do not get much of any signal from the boots on the ground that a large, generalized expansion of business activity is in the offing. The Atlanta Fed has an extensive information-gathering network with business contacts in the Southeast. The feedback I have been getting is that businesses overall do not expect a surge in growth. Neither do they expect to see an upshift in growth for cost pressures, including labor costs.

When we ask business owners about their prospects over the short to medium term, the dominant view is that business is good, and that acquisitions and market-share capture remain the go-to growth strategies.

It is possible that tax reform, if it's enacted, could be one of the needle-movers on economic activity. We've started conversations with our contacts to see how changes to the structure of corporate taxes might change their thinking about investment and business expansion. But, as everyone knows, the devil is in the details, and it's too early to know how we would incorporate the impact of fiscal policy changes into our outlook until we see those details.

In short, all of this anecdotal information convinces me that a reasonable economic forecast for the foreseeable future is more of the same: GDP growth continuing a bit above 2 percent, the unemployment rate in the low 4s, and modest increases in real wage growth.

Under my baseline scenario, I think it will be appropriate for interest rates to rise gradually over the next couple of years, as our policy position is still very accommodating rather than neutral. How gradual that pace will be depends on the strength of the incoming macroeconomic data and what it implies for the economic outlook.

And, as you may know, inflation has softened since the beginning of the year. While I'm still holding to the view that the recent weakness largely reflects idiosyncratic noise, I'll be watching the next few inflation reports closely for signs of a pickup.

The path to a policy outlook
I'd like to take a moment to explain how we develop the narrative I just shared. As you can imagine, my staff and I pore over many data releases and reports and run sophisticated econometric models to determine how the economy has performed in the recent past and predict how the economy is likely to perform in the near future.

Several of the data points we use are developed at the Atlanta Fed—tools such as GDPNow, the Wage Growth Tracker, and the Business Inflation Expectations survey, for example. I hope you all check out those tools on a regular basis.

Other data points for our models come from regular surveys we conduct of businesses in our region that span the nation's major economic sectors.

And, importantly, we continually test the narrative that emerges using anecdotal input from businesses and community leaders to get their sense of how the economy is performing and is likely to perform in the near future.

I can assure you, the Federal Reserve is no ivory tower. We make it a priority to listen to input from throughout the region.

We accomplish this through an innovative organizational structure that we call the Regional Economic Information Network. Through this network, we have a team of regional executives whose job it is to talk with business and community leaders across the Sixth District. I'd like to take this opportunity to introduce our regional executive for Alabama, Lesley McClure, who is here today. Lesley, could you please stand? I encourage you to share your thoughts with her. Our dialogue with our communities is central to everything we do.

When combined with the insight and expertise of my staff, these inputs—data, models, and stories from Main Street—help develop narratives such as the one I shared a moment ago. I hope this gives you a better sense of how we do our work to fulfill our mission.

I believe that meeting the Federal Reserve's dual mandate of price stability and maximum employment is a primary way we can help improve economic opportunity for workers and families in this country. However, expanding economic opportunity and striving for maximum employment require going beyond monetary policy alone, and beyond aggregate statistics on GDP growth and employment.

For instance, while the overall unemployment rate has declined substantially since 2010, some measures of labor market performance reveal divergences between regions and types of workers. These differences paint a picture of a very complex economy, one that includes many different economic realities. I believe policymakers across government should consider the sources of these differences when thinking about ways to expand economic opportunity.

Rural versus urban differences
I would like to focus the remainder of my remarks on one dimension of difference—the difference in labor market and economic outcomes in rural and urban communities. The urban-rural economic divide, particularly the increasingly difficult plight of rural communities, has come up repeatedly as I've spoken with many business and community leaders. It is clearly an issue that merits attention.

At the outset, I should say that defining what is rural versus urban is not straightforward. There are no objectively delineated boundaries between the two. Rather, there is a progression such that population densities gradually decline. Different people have varied ideas about how to best draw the line.

For today, I will distinguish between urban and rural places by relying on official designations of metropolitan and nonmetropolitan areas. As a rule, a metropolitan area consists of one or more counties that include a core urban area with at least 50,000 people, plus adjacent counties that have a high degree of social and economic integration with the urban core, as measured by commuting times to work. I will call metro counties urban places. Nonmetro areas are what I will refer to as rural.

Secular forces, such as technological change and globalization, have been at work for several decades and have been particularly difficult for rural places. The Great Recession exacerbated this trend.

This difficulty is evident when we compare the demographics of urban and rural populations. For example, the rural population is older on average. This is due in part to the migration of younger people to urban areas for better education and job opportunities. As an aside, the older demographic is also associated with the in-migration of people planning to retire for lifestyle reasons.

The rural population also has less formal education on average, earns less income, has a higher poverty rate, is less racially and ethnically diverse, and has poorer health. The rural population is also less geographically mobile overall.

The picture is a little more nuanced when one considers labor force attachment. Among people in their prime working ages who have a college degree, the participation rate is actually higher in rural areas versus urban areas. By contrast, the rate of participation for those without a college degree is much lower in rural areas than in urban areas, which is an issue of particular concern here in the South.

The Great Recession and the subsequent recovery have intensified labor force disparities between urban and rural areas, even for people with less formal education, for whom recovery has been slow. Here in the South, the prime-age urban-area participation rate for those without a college degree, while still below its prerecession level, has been recovering over the past two years. In contrast, participation is more than 6 percentage points lower in southern rural areas than it was in 2007, and it shows no sign of improvement.

Research by my staff at the Atlanta Fed suggests that differences in health and disability account for a large part of this disparity among regions for less-educated workers. Diabetes and heart disease lead the list of negative health factors. The underlying reasons for these differing trends are not clear. However, the more limited access to health care services and higher incidence of poverty in some rural communities may be an important contributing factor.

Differences in the characteristics of businesses in urban and rural areas also affect regional labor markets. On the one hand, rural businesses tend to be older, more stable, and more profitable on average. The rate of new business formation is lower, but so is the probability of business failure. Evidence from a 2016 Fed survey of small businesses suggests that this relative stability means that rural businesses are less likely to be financially distressed. However, these businesses also tend to be smaller and not as well positioned to engage in regional or global markets.

This reality has shaped perceptions of the opportunities that rural areas can provide, prompting many to leave rural areas for the promise of better jobs and incomes in urban places.

So what does all this mean for the relative performance of rural labor markets? I think there is an interesting paradox.

Because of low population density and greater distance from population centers, rural businesses often face a more limited pool from which to hire workers who have the needed education, skills, and experience.

Preliminary survey data we have compiled indicate that rural employers are currently having relatively more difficulty filling positions and are having to raise wages to attract workers. Data on average wage rates confirm that wages in rural areas have increased more rapidly in recent years, especially for less-skilled workers. As a result, the traditional urban wage premium for low-skilled workers has shrunk in recent years.

This evidence, when combined with the decline in labor supply noted earlier, suggests that the rural labor market, particularly for less-educated workers, has tightened more than in urban areas. While jobs requiring less education may be more plentiful in urban areas, the supply of labor has kept up with this demand. In rural areas, the supply of labor appears to be lagging behind demand.

Ensuring access to opportunity and resources
You might be thinking that this is an unusual topic for the Fed to be concerned about, and perhaps the Fed should be worrying only about inflation. I think differently. We have a dual mandate: maintaining a stable-price environment and maximizing employment in a sustainable way. The challenges facing rural communities, and urban communities for that matter, *may* impede our ability to achieve our employment mandate, and we need to keep a focus on these issues.

That said, I recognize that expanding economic opportunity involves many domains beyond monetary policy, including education policy, workforce and economic development policy, public health policy, and even migration policy.

I believe the Federal Reserve System can play an important role as a facilitator to help local and state business, community, and government leaders find ways to maximize economic opportunity in both rural and urban communities.

For example, we recently launched the Center for Workforce and Economic Opportunity. Every Reserve Bank has staff engaging in workforce development, and our Center can help advance and elevate this work to policy experts and practitioners alike. I see this effort as a way to find practical solutions to help ensure that all people have the opportunity and resources to enhance their economic circumstances.

Thanks for your attention. Now I'll be glad to take some of your questions.

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