

Economics Group

Special Commentary

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Projecting Labor Force Participation Beyond COVID

Executive Summary

Labor force participation has cratered since the onset of the pandemic. In November, 4.1 million fewer individuals were employed or looking for work compared to February. We expect the unique challenges posed to labor force participation by COVID to abate this year, but how will the participation rate evolve in the post-pandemic world?

We expect labor force participation to improve within all age groups in the coming years. As health concerns and childcare issues subside, more individuals are expected to be available for work. Furthermore, stronger economic activity should pull workers who are discouraged over current job prospects back into the labor force. Yet the rebound in the labor force participation rate will be constrained by the rapid aging of the U.S. population.

In this note, we illustrate four scenarios for the labor force participation rate in the years ahead, which all reflect the country's aging demographics. Even under what we consider to be our most realistic scenarios, which allow for both a cyclical rebound in participation and a boost from positive secular trends (such as the ability to work from home), the labor force participation rate would not recover to its 2019 rate until the second half of the decade. The lengthy recovery underscores the prospect that the economy's potential rate of growth likely will remain constrained by slow growth in the labor supply after the pandemic.

The labor force participation rate may not recover to its pre-virus rate until the second half of the decade.

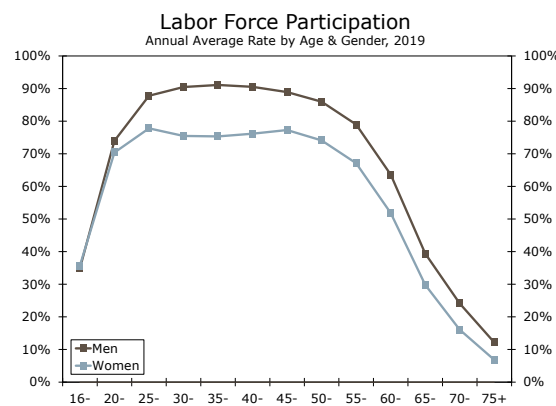
Where Has Participation Been?

On the eve of the pandemic, U.S. labor force participation had climbed to a seven-year high. Yet, the participation rate tumbled in the spring as most of the country imposed stay-at-home orders. Subsequently, the participation rate has partially recovered, but it remains nearly two points below its February rate (Figure 1). The drop equates to 4.1 million fewer individuals working or searching for a job. What's more, there has been no meaningful improvement in recent months, with the participation rate in November slipping back to its June level.

Figure 1



Figure 2



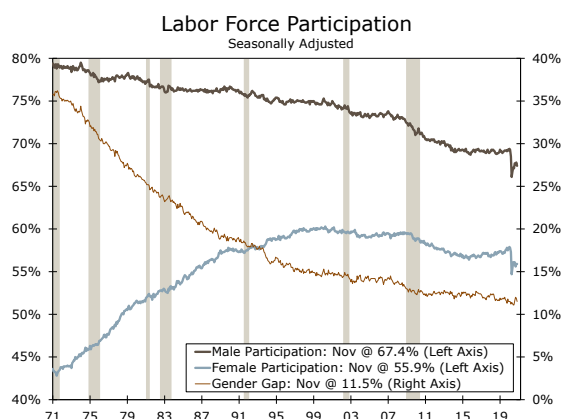
Source: U.S. Department of Labor and Wells Fargo Securities

The pandemic has exacerbated prior gaps in participation caused by social norms.

In August, we laid out some of the near-term challenges to labor force participation.¹ Health concerns about contracting COVID and the need to quarantine or take care of someone else who is sick has kept millions out of the workforce at any given time since the pandemic, particularly older workers.^{2,3} Parents juggling remote-learning and daycare closures have also found it difficult to continue working or searching for a job. Nearly one million parents with children under the age of 18 were not in the labor force in November specifically because of the pandemic.⁴ And of course, a lack of job opportunities—as there are nearly 10 million fewer jobs today than back in February—has also contributed to millions of workers remaining on the sidelines of the labor market. However, these hurdles are likely to be lowered over the coming year, as the risk of contracting COVID diminishes with the rollout of vaccines, in-person schooling returns and pent-up demand for services requiring face-to-face contact spurs related hiring.

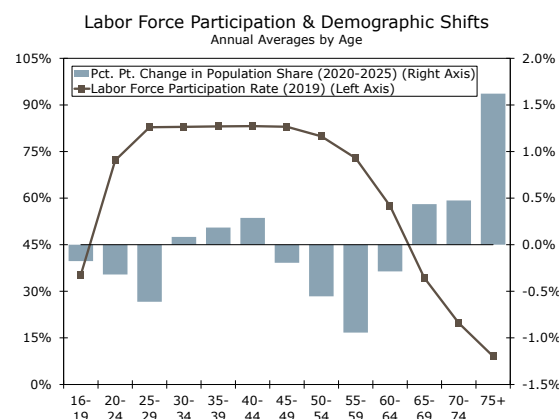
The extent of a recovery in participation will depend not only on reversing the unique challenges to working caused by the pandemic, but longer-term social and demographic factors as well. In terms of social considerations, the COVID recession has been particularly hard on women.⁵ Steeper job losses in service industries that employ a relatively high share of women have resulted in fewer job opportunities. But, the pandemic has also exacerbated prior gaps in participation caused by social norms, like household and caregiving responsibilities.⁶ Women also tend to work in lower-paid fields, making mothers more likely to leave the labor force than men when childcare responsibilities require a parent to stay home. As a result, a gap emerges between male and female participation rates when workers are in their early 20s, and lingers over the course of adulthood (Figure 2).

Figure 3



Source: U.S. Department of Labor and Wells Fargo Securities

Figure 4



But prior to COVID, the gap between men's and women's participation rates had narrowed to an all-time low of 11.3%, as women's gains in participation outpaced men's (Figure 3). There is reason to believe the narrowing could continue. First, employers' increased familiarity with working from home (WFH) could prevent more women from having to choose between paid and unpaid work after the pandemic. Second, women are obtaining college degrees at a higher rate than men, and education is positively associated with labor force engagement. Third, women account for the lion's share of employment in labor-intensive services industries, especially healthcare, where demand is expected to rise in coming years thanks to an aging population.

¹ See "[Prospects for a Recovery in Labor Force Participation](#)" (August 10, 2020).

² According to the U.S. Census Bureau Household Pulse Survey, 11.1 million adults were not working due to being sick with coronavirus symptoms, caring for someone with coronavirus symptoms, or concern about getting or spreading the coronavirus for the period covering November 25-December 7.

³ Labor force participation among workers ages 65+ since February has declined 3.6% compared to a 2.4% drop in the broader population.

⁴ See [Table 10](#) of Supplemental Data Measuring the Effects of the Pandemic on the Labor Market.

⁵ Employment among women has fallen by 5.3M since February compared to a 4.6M drop among men.

⁶ The labor force participation rate among women in their "prime" (ages 25-54 as defined by the BLS) has dropped by 2.5 points since February compared to a 1.9 point decline for prime age men.

That said, the rapidly aging U.S. population will weigh heavily on total labor force participation in the years ahead. The leading edge of the Baby Boomers turns 75 this year, and even the youngest Boomers are outside their “prime” working years, defined as ages 25-54. As illustrated in Figure 4, labor force participation declines for workers in their late 50s before falling more sharply once workers reach their 60s. Over the next five years, the share of the population ages 65+ is set to rise 2.5 points.

How Big of a Rebound Are We Talking About Then?

The labor supply is a critical ingredient for longer-term economic growth. A lower rate of participation portends slower growth in the economy, all else equal, as even the most capital-intensive businesses need workers to grow and expand. Therefore, the degree and timing to which participation recovers will bear on the outlook for economic growth beyond the immediate burst of activity we expect in mid- to late 2021 as vaccines become widely available. Given the importance of participation, we examine its possible path forward in four scenarios, using population and labor force data for the 13 age cohorts shown in Figure 4.

The degree and timing to which participation recovers will bear on the outlook for growth.

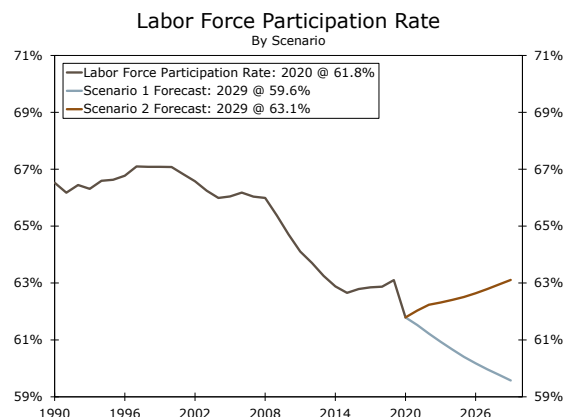
Scenario 1: Isolating the Demographic Effect on Labor Force Participation

Our first scenario demonstrates the toll that population aging will have on the labor force participation rate (Figure 5). We hold the participation rate for all age cohorts steady at their 2020 average, and then account for the shift in population shares across age groups.⁷ Holding participation rates constant, the total participation rate would slide to 59.6 by 2029.⁸ In other words, population aging alone is expected to shave about a quarter of a percentage point off of the labor force participation rate per year between now and the end of the decade.

Figure 5



Figure 6



Source: U.S. Department of Labor and Wells Fargo Securities

Scenario 2: Participation Rises Across Age Groups Similar to Their 2015-2019 Pace

Simply projecting demographic effects, however, is too pessimistic in our view, as we expect some recovery in participation within each age group. Widespread deployment of vaccines in 2021 should lead to stronger economic growth, which in turn should spur hiring. More ample job prospects should pull workers into the labor force who were previously discouraged or only passively interested in a job, raising participation rates across the board.⁹ At the same time, many individuals

⁷ We use the Department of Labor's [estimates](#) of the rate of growth in the civilian noninstitutional population beginning in 2021 through 2029 for each age cohort.

⁸ We break participation up by the five-year age cohorts and multiply the 2020 participation rate (held constant through 2029) by the projected population level before aggregating the cohorts into a total labor force participation rate.

⁹ Structural trends have dominated the path of labor force participation in the post-WWII era, but there is a positive relationship between job growth and participation.

with health concerns could very well re-enter the labor force once the risks of contracting COVID subside.

We thus attempt to quantify the scope for participation to increase within age groups, while also accounting for the downward impact of population aging. Figure 6 illustrates our second scenario, or the path of participation if all age groups were to recover back to 2019 participation rates by 2022. Subsequent increases in participation might be slower going after the initial transition to a world where COVID is under control. Increases in participation across cohorts after 2022 are likely to be more gradual, and we assume they follow a path similar to the latter half of the past expansion. From 2023 onward, this scenario has participation rising at its average annual pace from 2015-2019 across all age cohorts.

Scenario 3: A Stronger Recovery than the Great Recession for All Age Groups

There is a case to be made, however, that participation could be even stronger in a post-virus world. The pandemic has ushered in a certain comfort level of work-from-home, which may allow more individuals to join or stay in the workforce as they balance unpaid work than before COVID. In addition, it may be quicker for workers to return to the labor force this cycle once the crisis passes. A large share of job losses are still considered temporary, meaning workers remain connected to employers and labor market scarring may be more limited than in the wake of the Great Recession.

It is thus not only possible that female participation resumes its upward trend, but also male participation climbs faster in the coming years. In our third scenario, we assume participation rates across individual cohorts return to their pre-pandemic rates in 2022 as we assumed in Scenario 2, but beginning in 2023, participation rises more quickly. Instead of participation rates growing at their pre-virus average, we apply the stronger pre-virus trend of each cohort to both men and women. For example, for the 20-24 age cohort, female participation rose an average of 0.5 points per annum from 2015-19 compared to 0.2 points per annum for men, so we apply the 0.5 point average annual increase to both the female and the male 20-24 age cohorts. This results in a slightly stronger, but still reasonable, pace of participation (Figure 7).

Figure 7

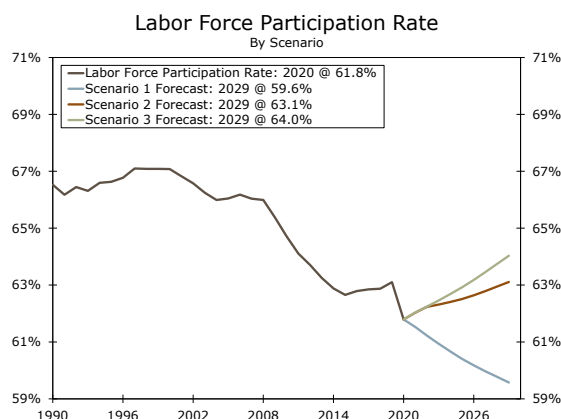
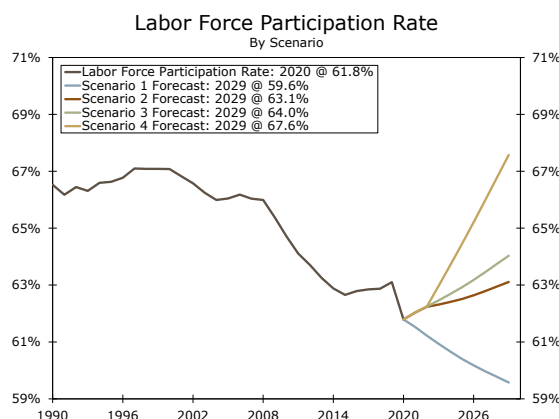


Figure 8



Source: U.S. Department of Labor Wells Fargo Securities

Scenario 4: The Heroic Assumptions Needed for a Fast and Full Recovery

What would it take to get a more meaningful recovery in the labor force participation rate in the next few years? In what is an extremely optimistic Scenario 4, participation skyrockets back above 67% by 2029 (Figure 8). Admittedly, this makes some rather heroic assumptions and is not a realistic scenario in our view, but it is important to show for comparative purposes. After getting participation by gender across age cohorts back to their 2019 rates by 2022, we grow male participation by its pre-virus 2015-2019 average annual rate and then incrementally grow the participation rate among women to the male rate by the end of 2029.

Increased comfort of work-from-home may allow more individuals to join the workforce.

This scenario is overly optimistic in our view, as the gap between male and female participation rates remains substantial and has narrowed only slightly in the two decades prior to COVID (refer back to Figure 3). Although we expect female participation to pick up, it is unlikely we see a complete closing in the gap between male and female participation rates in eight short years, as structural hurdles still loom large over labor force participation among women.¹⁰

Labor Supply to Weigh on Potential GDP, Higher Participation and All

Looking at our more realistic scenarios, the road to a full recovery in labor force participation remains long. It would take nearly a decade of uninterrupted growth and positive secular forces to get participation rates back to pre-COVID levels in light of the demographics ahead. The lengthy recovery underscores the economy's potential rate of growth post-pandemic is still likely to be constrained by the labor supply, even if there is less labor market scarring than in the wake of the Great Recession and workers return to the labor market more quickly.

The road to a full recovery in the labor force participation remains long.

Under Scenario 2, where the participation rates of all cohorts return to 2019 levels in 2022, and then continue to rise at the same clip as 2015-2019, the labor force would increase an average of 0.9% per year. Taking into account our reasons to be slightly more optimistic (presented in Scenario 3), the labor force would grow 1.1% per year over that horizon. While the rates of labor force growth in both scenarios would be faster than the decade following the Great Recession (0.6%), they still mark a notable slowdown from the second half of the 20th century, when the labor force grew at an annualized rate of 2.5%. As a result, the onus of a meaningful increase in potential GDP growth following the pandemic will rest heavily on raising productivity growth, prospects for which are uncertain at this time.

¹⁰ See "[The Girl with the Draggin' W-2](#)" (February 27, 2017).

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