



# Comments on “Some Benefits and Risks of a Hot Economy”

Remarks by  
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Views are my own and do not represent any position  
of the Board of Governors or other Federal Reserve  
policymakers.

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- The authors discuss three impacts from running a “hot” economy: labor market inclusiveness, potential financial market instability and a greater risk of excessive inflation.
  - Since time is short, I will focus most of my comments on the benefits of labor market inclusiveness.

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- The Federal Reserve’s new framework states that “full employment is a broad-based and inclusive goal.”
  - A challenge for policymakers is to try and determine when that goal has been achieved.
  - One interpretation is that it is when all groups have similar labor market outcomes according to various metrics.

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- For example, those metrics could include unemployment rates, employment-to-population ratios and labor force participation rates.
  - If these metrics do not show similar labor market outcomes, the question then becomes, “what can monetary policy do to improve these metrics?”

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- The evidence from the authors' research is that economic expansions show a strong narrowing of differentials for unemployment rates across groups.
  - And, only weak evidence for narrowing of labor force participation rates.
  - This is for prime age workers (25-54)—not very inclusive to people my age! The good news is I find it true for prime age and all workers.



- What should unemployment rates look like in a racially blind, gender-neutral labor market?
- In the basic Diamond-Mortensen-Pissarides labor search model, there are only “economic agents.” Race and gender are not specified.
- Given a certain matching efficiency, job finding and job separation rate, an equilibrium unemployment rate is generated.

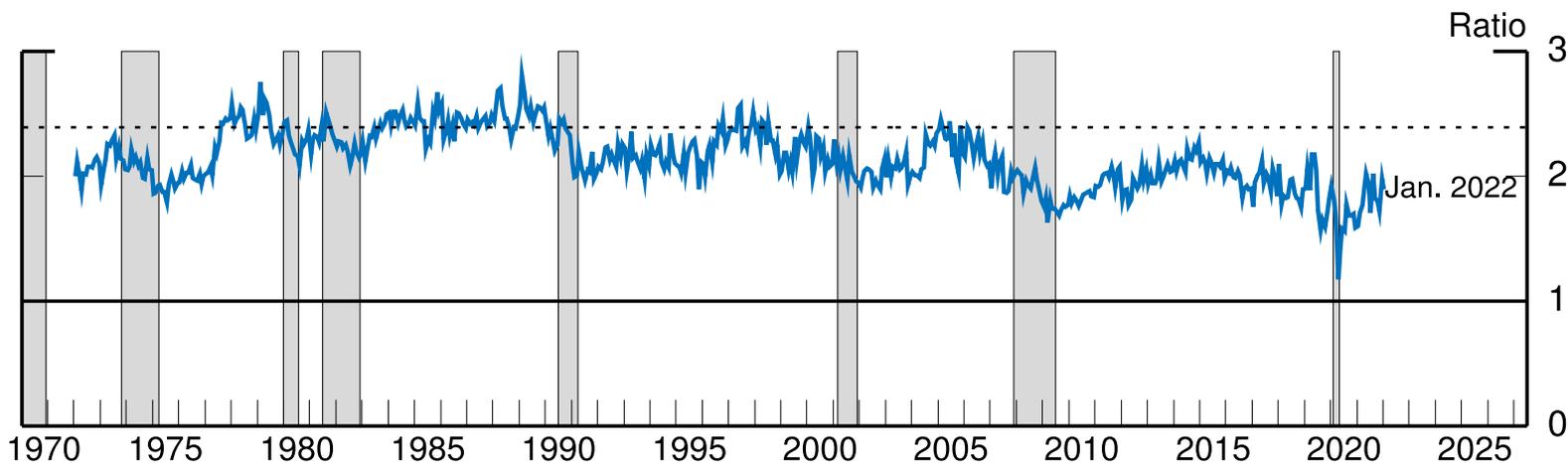
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- Let's arbitrarily assign workers a color: blue, green and red.
  - If these colors are meaningless attributes, then all groups will have the same unemployment rate and the ratios will be 1.
  - This implies that race and gender ratios should be 1.
  - Education ratios, because of differences in productivity, will not be 1.

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- By looking at the ratio, we get a measure of *relative* differences as opposed to absolute differences.
  - Looking at relative differences gives a better view of improving (or worsening) situations than absolute differences.
  - It measures gains and losses in percentage terms.

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- Consider income; someone makes \$100,000 and someone else makes \$50,000.
  - Now double both incomes; the first person will still make twice as much. So there is no relative change in the income distribution.
  - But in absolute terms, the first person has an extra \$100,000 in income and the other has an extra \$50,000. This looks like a worsening income distribution.

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- Looking at ratios raises three key questions.
  - First, how far are the ratios in the data from 1?
  - Second, is there a trend in these ratios toward 1 (improvement) or away from 1 (worsening)?
  - Third, do these ratios display *cyclical variations* that could be affected by monetary policy?

## Ratio of Unemployment Rates: Black to White



Note 1. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).

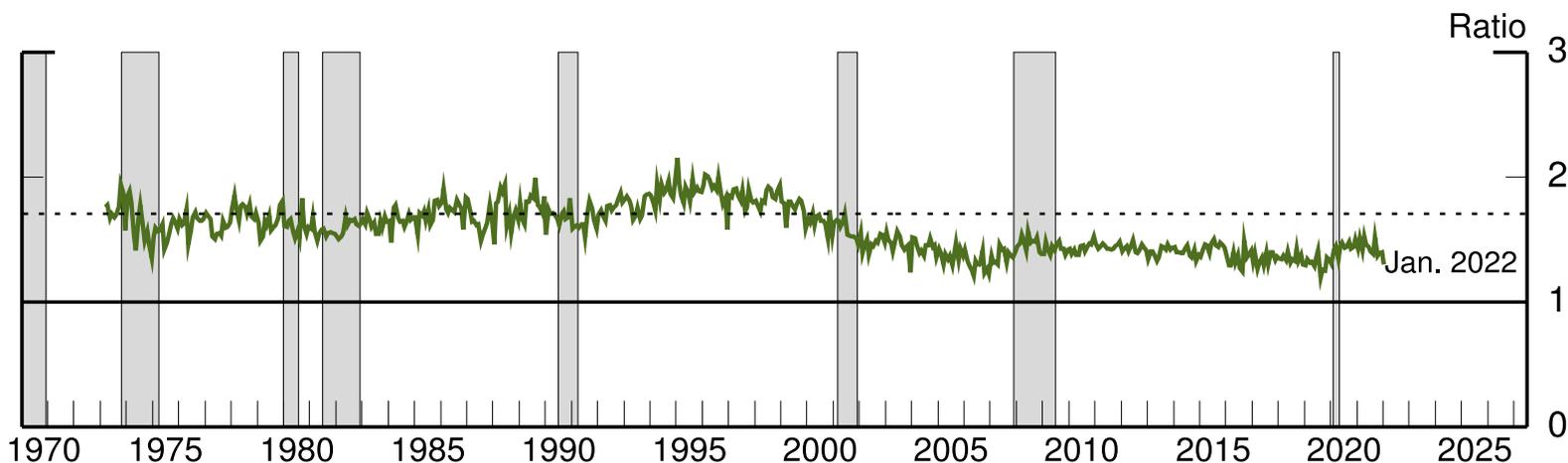
Note 2. The dotted horizontal line is the average ratio between 1977m1 and 1990m7.

Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio greater than 1. Race matters.
- 2) Clear downward trend.
- 3) Appears to exhibit cyclical pattern after the last three recessions— rises after a recession then falls later in the recovery.

## Ratio of Unemployment Rates: Hispanic to White



Note 1. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).

Note 2. The dotted horizontal line is the average ratio between 1973m3 and 2001m7.

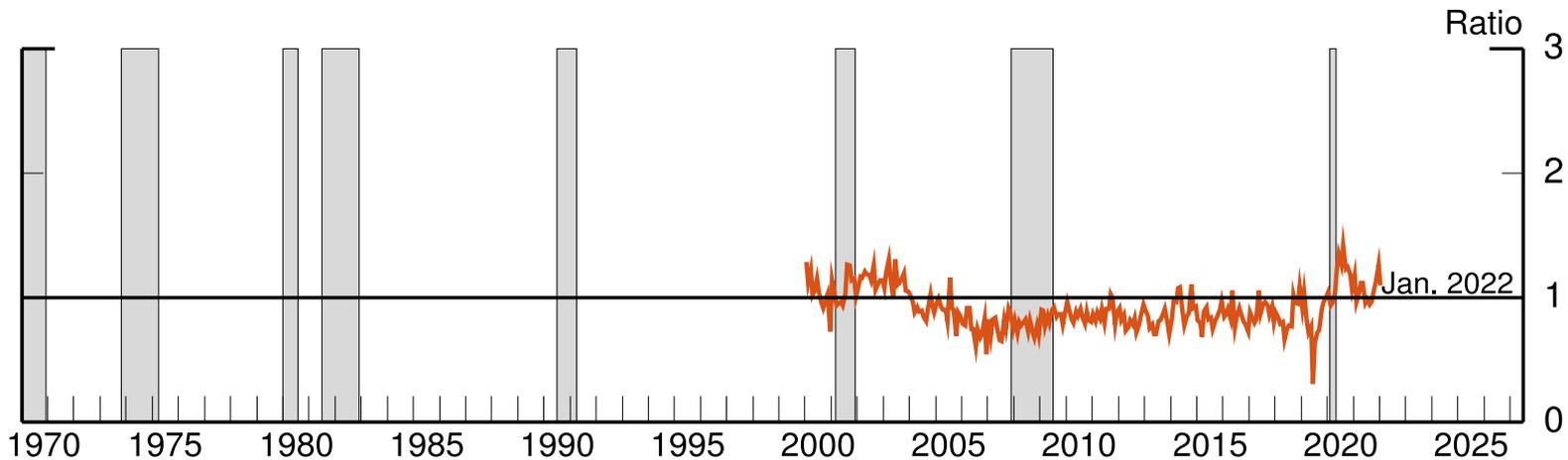
Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio greater than 1. Race matters.
- 2) Clear downward trend.
- 3) No apparent cyclical variation.



## Ratio of Unemployment Rates: Asian to White

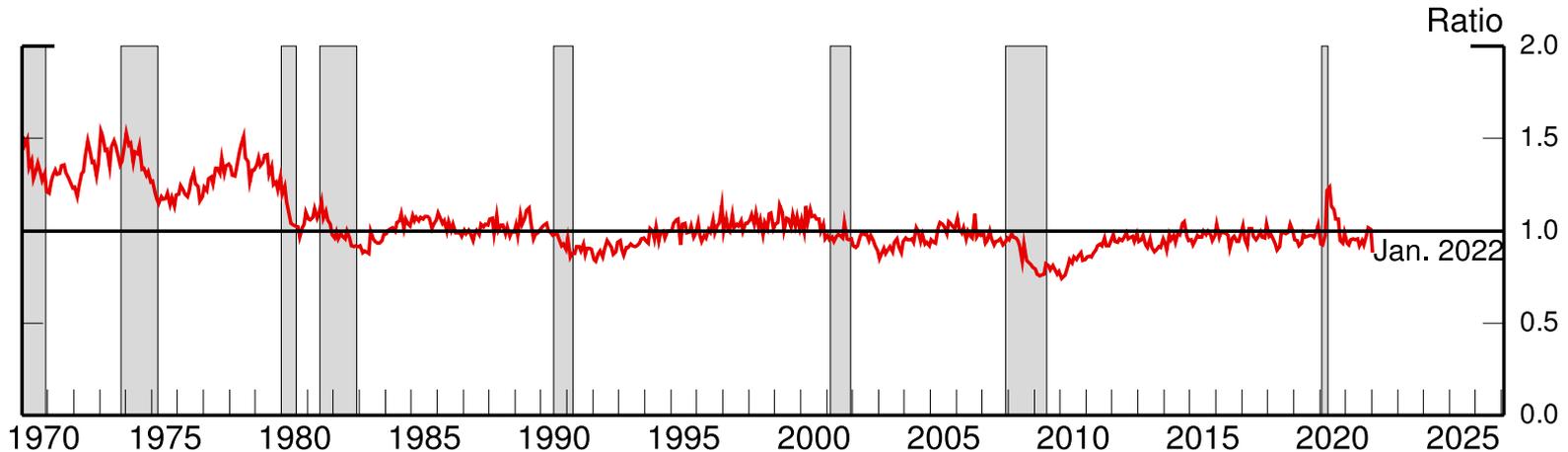


Note. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).  
Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio slightly less than 1 until recently.
- 2) No apparent trend.
- 3) No apparent cyclical variation.

## Ratio of Unemployment Rates: Women to Men



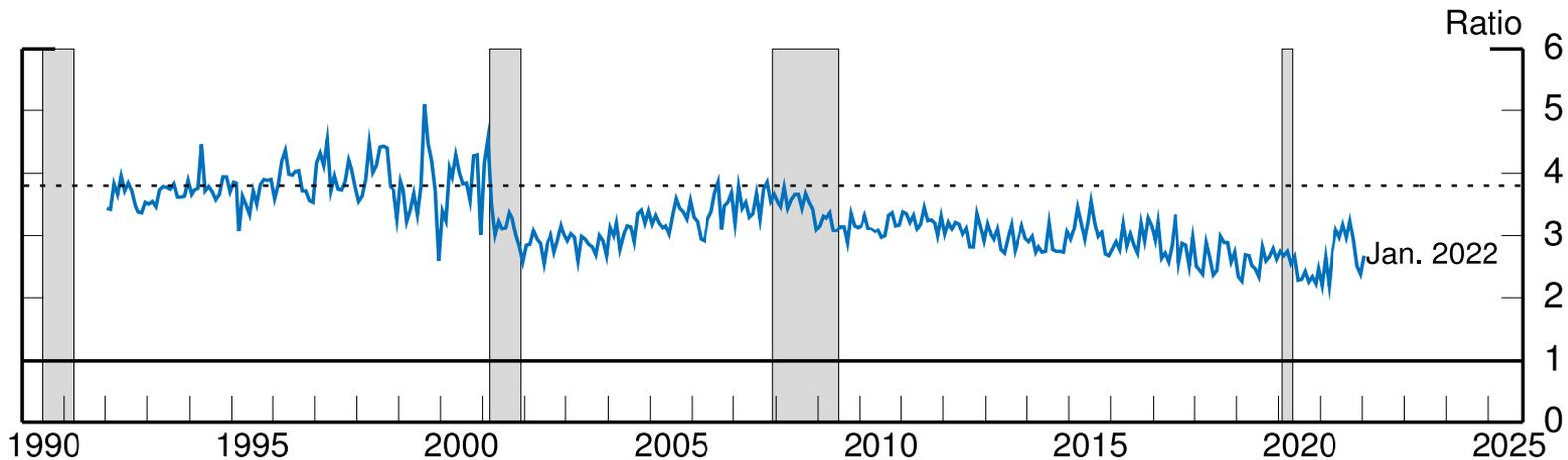
Note. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).  
Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio close to 1.
- 2) No apparent trend after the 1970's.
- 3) Some cyclical variation. Women experienced large unemployment at the start of the COVID shock. Men experienced larger unemployment in previous recessions.



## Ratio of Unemployment Rates: Less than High School to College Degree



Note 1. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).

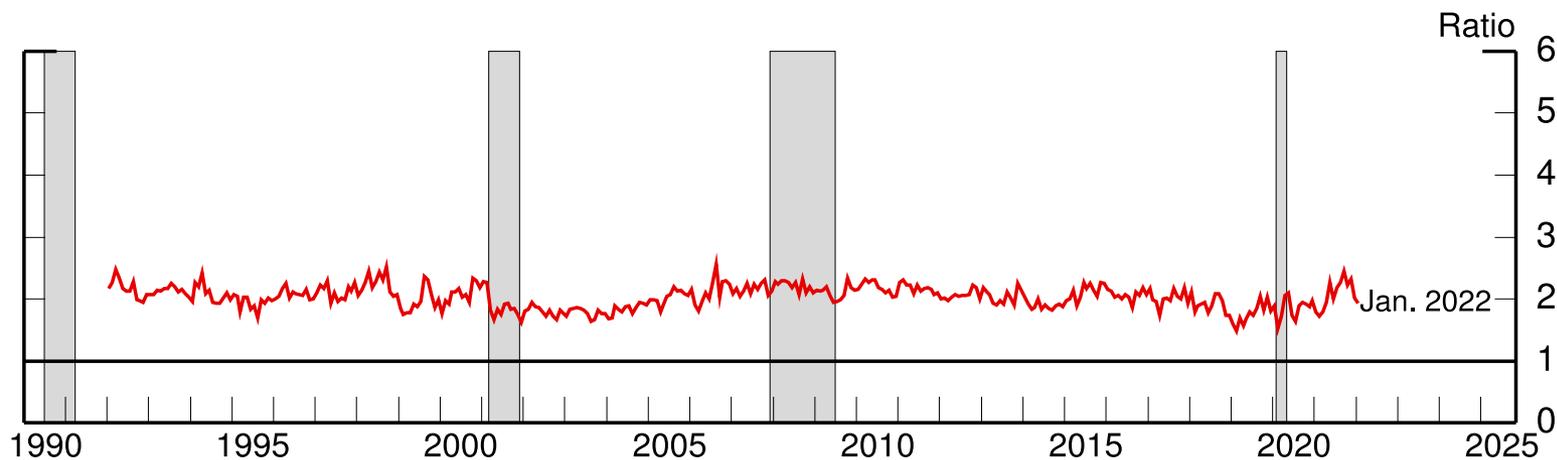
Note 2. The dotted horizontal line is the average ratio between 1992m1 and 2001m3.

Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio greater than 1 but not surprising.
- 2) Clear downward trend.
- 3) No apparent cyclical variation.

## Ratio of Unemployment Rates: High School to College Degree



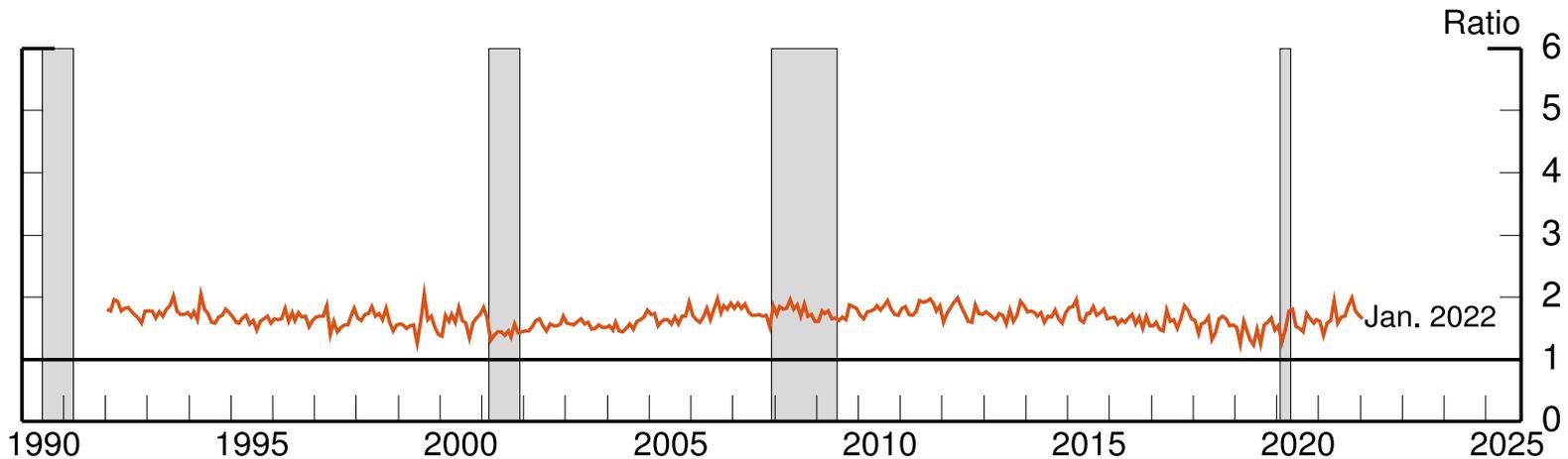
Note. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).  
Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio greater than 1 but not surprising.
- 2) No apparent trend.
- 3) No apparent cyclical variation.



## Ratio of Unemployment Rates: Some College to College Degree



Note. The shaded bars indicate periods of business recession as defined by the National Bureau of Economic Research (NBER).  
Source: Bureau of Labor Statistics data, seasonally adjusted by Federal Reserve Board staff.

### Takeaways:

- 1) Ratio greater than 1 but not surprising.
- 2) No apparent trend.
- 3) No apparent cyclical variation.



- So what conclusions do I draw from this data?
- First, for Black workers and Hispanics, the ratios are bigger than one – work is needed to try and lower this to 1.
- Second, there have been clear improvements for less advantaged groups in terms of longer-term labor market trends.
- It is unlikely that this type of improvement is directly driven by monetary policy.



- Third, running the economy “hot” does improve the relative performance for some groups, but not all, when comparing unemployment rates.
- In particular, longer expansions improve job finding rates for Black workers.
- Doing a similar exercise using relative employment to population ratios also shows improvement for Black and Hispanic workers.



# Empirical Studies

- Aaronson, Stephanie R., Mary C. Daly, William Wascher, David W. Wilcox. 2019. “Okun Revisited: Who Benefits Most From a Strong Economy?” *Brookings Papers on Economic Activity*, Spring, 333-404.
- Hotchkiss, Julie L. and Robert E. Moore. “Some Like it Hot: Assessing Long-term Labor Market Benefits from a High-pressure Economy.” *International Journal of Central Banking* (forthcoming)