

Yes, low unemployment does raise wages

By Dean Baker

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In the fall of 2013, Jared Bernstein and I wrote a book called *Getting Back to Full Employment: A Better Bargain for Working People*. The main point of the book was that low unemployment rates disproportionately benefited those who are most disadvantaged in the labor market. For this reason, we argued for using macroeconomic policy to get the unemployment rate as low as possible, until inflation became a clear problem.

At that time, the unemployment rate was still close to 7.0 percent. It was coming down from its Great Recession peak of 10.0 percent, but there were many economists, including some at the Federal Reserve Board, who argued that it should not be allowed to fall below a range between of 5.0–5.5 percent because lower rates of unemployment could trigger spiraling inflation. Our argument challenged that view.

We felt the evidence that unemployment rates this high should pose any sort of floor for macroeconomic policy were weak. Given the enormous gains from allowing the unemployment rate to fall further, we argued the Fed should take the small risk of accelerating inflation, and allow the unemployment to continue to decline.

Thankfully, Janet Yellen, who was then Fed chair, agreed with this position. (It helped that our friends with the Fed Up Coalition were also pushing hard in this direction.) Her replacement, Jerome Powell, seems to be following the same path, more or less.

Anyhow, we have now seen the unemployment rate fall below 4.0 percent, getting as low as 3.7 percent last fall, with impressive results.

First, it is easy to see who benefitted the most from the reduction in the unemployment rate. In 2013, when we wrote the book, the unemployment rate for Black people averaged

more than 13.0 percent. The average for the second half of 2018 was just over 6.0 percent. The Latino unemployment rate fell from more than 9.0 percent to 4.5 percent. For workers with less than a high school degree, the drop was from more than 11.0 percent to less than 6.0 percent.

While it would be foolish to celebrate unemployment rates that are still way too high, it would also be foolish not to acknowledge the enormous gains to the most disadvantaged segments of the labor market that have resulted from the low overall unemployment rate.

These gains are also showing up in higher wages. Over the last four years, average weekly earnings, adjusted for inflation, have risen by 10.1 percent for workers at the cutoff for the bottom tenth of the wage distribution. They rose 8.5 percent for workers at the cutoff for the bottom quarter, and 5.6 percent for workers in the middle. Increases in state and local minimum wages almost certainly contributed to the wage gains at the bottom, although low unemployment was undoubtedly the major factor higher up the wage ladder.

The median weekly wage for Black workers has risen 7.4 percent over this four-year period, while the median wage for Latino workers has risen 6.8 percent. The median weekly wage for workers with just a high school degree rose 5.3 percent, and 3.7 percent for those with some college. Ironically, workers with a college degree have fared poorly, seeing their inflation-adjusted median wage actually fall by 0.2 percent over the last four years.

This is the only period, apart from the low unemployment years of the late 1990s, when workers at the middle and bottom of the wage distribution have seen sustained real wage growth. The story is turning out pretty much as

Jared Bernstein and I had expected. Low unemployment rates give even relatively disadvantaged workers increased bargaining power, allowing them to share in the benefits of economic growth. There are reports of employers looking to hire stigmatized groups such as people with criminal records — people they would never look to hire in a labor market with high unemployment.

The fact that workers at the middle and bottom have been seeing healthy wage gains for the last four years does not mean the economy is great. There are still many people who cannot afford health care, rent, child care for their kids and other necessities of life. Four years of decent wage growth does not undo the effects of forty years of rising inequality.

However, it is important to recognize that at least things are moving in the right direction for now. If the current sub-4.0 percent rate of unemployment can be sustained, or ideally even pushed lower, it will mean that workers in the middle and bottom will continue to share in the gains from economic growth and make up some of the ground lost in prior decades.

As a practical matter, there are many policies that we might like to see the government pursue to help those at the middle and bottom. But having a full employment economy is, by comparison, relatively simple. We just have to keep the Federal Reserve Board from slamming the breaks on the economy with high interest rates. There are many good things we want the government to do, but in this case, we just need to keep it from doing something bad.