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The Enduring Local Harm from Recessions

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POLICY BRIEF

The Enduring Local Harm from Recessions

Brad J. Hershbein and Bryan A. Stuart

BRIEF HIGHLIGHTS

- We study the impacts of each recession over the past 50 years on the economic health of metro areas.
- Areas that suffer larger employment losses during a recession never fully recover their employment relative to less affected areas.
- Badly hit areas also have less population growth, and the share of the population that is employed, as well as per capita income, are lower for at least a decade.
- These areas also grow relatively older and often become less educated, with fewer management and professional jobs.
- Recessions play a role in some areas falling economically behind others, as employment opportunities shift across areas more quickly than people do.

For additional details, see the working paper at https://research.upjohn.org/up_workingpapers/325/.

Recessions receive enormous attention from researchers, policymakers, and the public. Most of this attention focuses on short-run, nationwide measures like the unemployment rate and gross domestic product. These outcomes are clearly important, but many of the broader and longer-lasting consequences of recessions remain uncertain. This is particularly true for how recessions affect local labor markets, such as metropolitan areas.

In particular, do badly affected areas eventually recover to be on par with their less-affected peers, or is the economic harm suffered during recessions persistent, possibly putting severely hit areas on a permanently lower trajectory for employment and earnings? To answer this question, we examine the long-term impacts of five national recessions—from the one in the mid-1970s through the Great Recession—on employment, population, earnings, and other outcomes for 363 metropolitan areas in the United States. Because the severity of each recession varied across these areas—some had heavy losses in employment while others actually gained jobs—we essentially compare worse-hit places to less-affected places, tracking outcomes for several years after each recession's end.

We find that, for every recession, harder-hit metropolitan areas suffer long-lasting economic harm relative to less-affected areas. Their paths diverge, and the former group falls behind in terms of employment, population, employment rates, and per capita earnings. Specifically, an area that loses 5 percent of its employment during a recession—the typical loss during the Great Recession—on average has 6.2 percent less employment than it otherwise would have almost a decade later. Population also falls, mostly because of fewer people moving in rather than more people moving out, but this loss is not as large as that for employment. Consequently, the share of the adult population that is employed falls by 2 percentage points, or 1 out of every 50 people. This decline in the employment rate also leads to a long-term 3.2 percent drop in per capita earnings.

Moreover, these persistent economic impacts are often accompanied by modest, but not trivial, changes in the demographic characteristics of affected places. The share of residents aged 65 and over increases, while the share aged 15 through 39 falls. Fewer workers are employed in managerial, professional, and technical occupations, and more are employed in manual and service jobs. The share of residents with a college degree falls. Even adjusting for these demographic changes, however, the majority of the employment and earnings impacts remain.

Our findings have important implications for the reallocation of economic activity across places, labor market dynamism, economic opportunities for workers and their children, and optimal policy responses. While our social safety net is mostly set up to respond to current (or very recent) economic conditions, our finding that recessions have enduring impacts on places long after the national economy has recovered suggests that targeting aid based on a longer economic history may be necessary to preserve economic opportunity for all.

How Recessions Can Have Long-Lasting Local Effects...

Recessions are periods of depressed economic activity, and they coincide with large cuts to employment as the demand for labor falls. These declines generally vary across

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places because of differences in industry specialization or in the types of workers affected, as well as the nature of the recession.

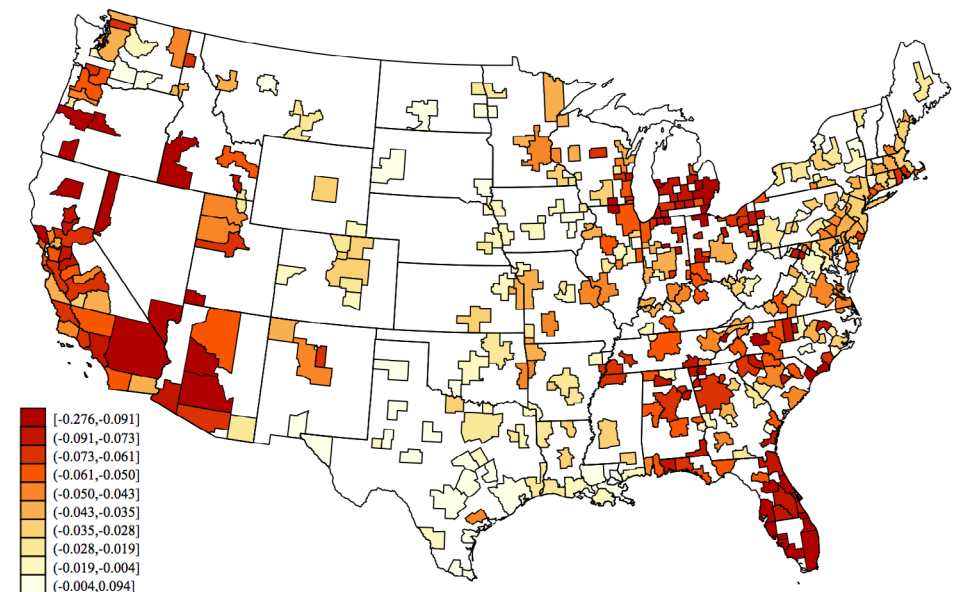
If during a recession most firms temporarily lay off workers or reduce their hours, then employment, wages, and the share of people employed are likely to quickly revert to previous trends once conditions improve. If, on the other hand, a recession causes employers to change their production processes or shut down, there could be long-term scarring in a local labor market. This could also happen if highly skilled (and higher-earning) workers are more likely to leave for other areas not as badly affected, or if the recession diverts would-be in-migrants—both people and businesses—to other areas. Recent research has found support for all these possibilities, but has not systematically examined the long-term outcomes of places badly hit by recessions.

...and Vary across Places

We thus look at places as defined by metropolitan areas. These 363 areas are groups of counties tied together by commuting patterns and having an urban center of at least 50,000 people. Although they exclude rural areas, they account for between 66 and 83 percent of the country's people and jobs between 1969 and 2016. These metropolitan areas proxy for local labor markets, the places in which people work and look for jobs. (Our results are similar when we examine commuting zones, which include rural areas.)

The severity of recessions varies considerably across metropolitan areas. Figure 1 shows this variation for the last recession we analyze, the Great Recession of 2007–2009. We measure the local severity of the recession by the change in employment between the national peak and the national trough—in this case between 2007 and 2009—in each metropolitan area. On the map, areas with darker red shading suffered greater proportional employment losses. Although some entire states were badly affected—Michigan, notably, as well as the Sun Belt states of Florida and Arizona—there are also several cases where neighboring areas fared quite differently, such as Providence and Boston, or Pittsburgh and Youngstown.

Figure 1 The Severity of the Great Recession Varied Considerably across Metropolitan Areas



NOTE: Figure shows the change in the natural log of employment (approximately equal to the percent change in employment) between 2007 and 2009 for 363 metropolitan areas (Core-Based Statistical Areas, as defined in 2003 by the Office of Management and Budget). Areas in darker colors experienced larger employment losses. SOURCE: Authors' analysis of Bureau of Economic Analysis Regional data.

Our analysis compares the long-term outcomes of places that were more severely affected to those were that less affected, for each of the past five recessions.

Our analysis essentially compares the long-term outcomes of places that were more severely affected to those were that less affected, and we do this separately for each of the past five recessions: the ones in 1973–1975, 1980–1982, 1990–1991, 2001, and 2007–2009. Of course, the metropolitan areas that suffered severe employment losses may have differed in several ways from those with smaller losses, and it is important to control for these differences. Therefore, we are also careful to account for differences in prerecession population growth (by age group), and we implicitly compare metropolitan areas within each of nine regions in the country. Moreover, our analytical approach, called an event study, allows us to confirm that more and less affected areas were trending similarly before the recession; this helps ensure that the less-affected areas serve as a good comparison to what would have happened in the more-affected areas had the recession there not been as severe.

Local Recessions Don't Just Fade Away

When we implement this approach, we find that employment doesn't just fall more immediately in harder-hit areas (this happens by construction), but it remains depressed for at least a decade, and often longer. Specifically, we estimate that for every additional 1 percent drop in employment during a recession, employment is between 0.8 and 1.7 percent lower than it otherwise would have been seven to nine years after the recession ended. For a Great Recession-sized shock, when a 5 percent employment loss was not unusual, this means a long-term reduction in employment of roughly 4–8 percent. To be clear, we don't mean that employment is necessarily lower than it was before the recession began, but that it is lower than it would have been in the absence of the recession. Put differently, growth is on a lower trajectory.

We also find this same pattern of persistently lower growth in an area's population. Every 1 percent greater employment loss during a recession translates to between 0.3 and 0.7 percent lower population nearly a decade later. One might think this is driven by people moving out of badly affected areas, but we find the opposite. Fewer people move away; rather, the population loss occurs because fewer people subsequently move into hard-hit areas, and this effect lasts a long time. Moreover, the composition of the population shifts, with the population of badly hit areas aging and oftentimes having fewer highly educated professional workers than less-affected areas.

Put together, the long-term impacts on employment are greater than those on population, and thus the employment rate—the share of people with jobs—also suffers long-term declines in areas that experienced more severe recessions. We illustrate this pattern in Figure 2, which shows these declines for each recession. For each panel, the two vertical lines indicate the beginning and end of the recession (in terms of employment). That the thick blue line is near 0 before the recession indicates that areas have similar trends in the employment rate, regardless of how large their employment losses will be. In each case, as expected, the employment rate falls sharply during the recession. This decline persists, however, once the recession is over: for the 1973–1975, 1990–1991, and 2001 recessions, there appears to be no recovery at all, while there is only incomplete recovery for the 1980–1982 and 2007–2009 recessions. Consequently, areas that lost 5 percent more of their employment during a recession have employment rates 1–2 percentage points lower, even up to a decade later. For a typical metropolitan area of 150,000 workers, that's 1,500 to 3,000 fewer people with jobs.

Policy Implications

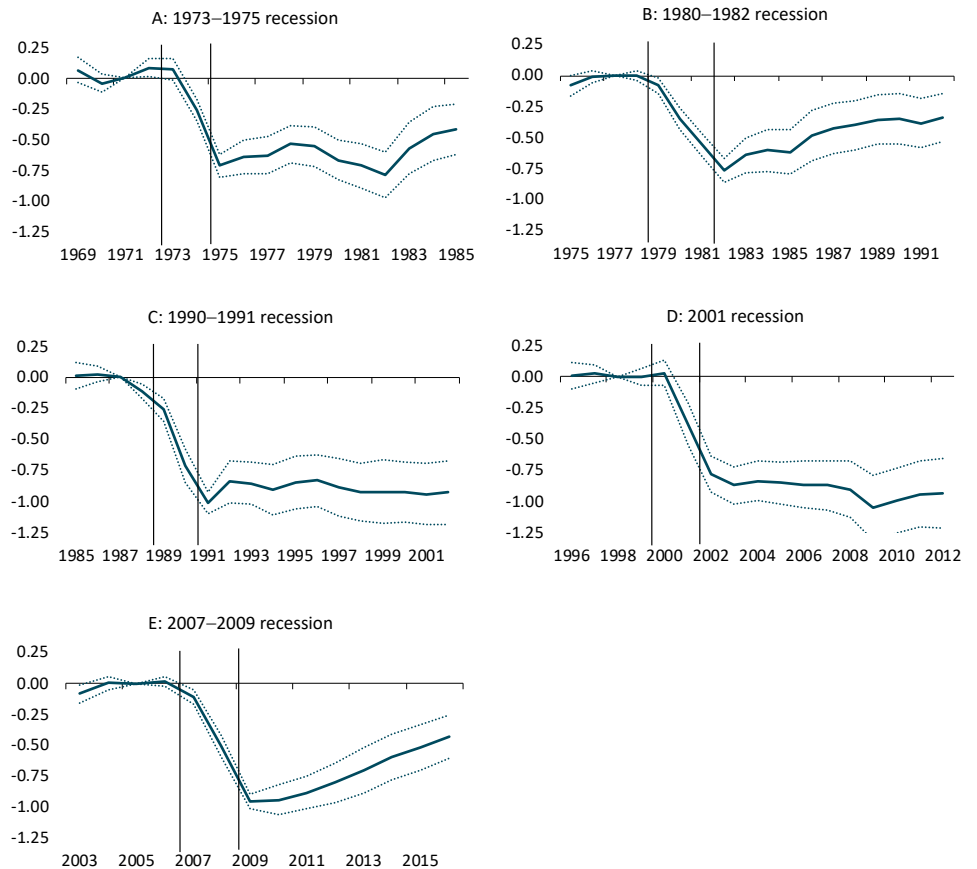
The long-term impacts of local recessions also affect income, and we estimate that in badly hit areas, long-term per capita earnings are between 1 and 5 percent lower than they would have been in the absence of the recession. These losses are disproportionately borne by residents in the bottom half of the earnings distribution.

What explains these long-term impacts? We are actively working on this question, but at a fundamental level, employment opportunities shift across areas more quickly than people do.

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Figure 2 In Every Recession, Harder-Hit Areas Suffer Persistent Declines in Employment Rates



NOTE: Figure shows, separately for each recession, the impact of a 1 percent greater employment loss during a recession (between the vertical lines) on the employment rate over time. Complete recovery is reached when the solid blue line returns to 0. Dashed lines indicate 95 percent confidence intervals.

SOURCE: Authors' calculations using Bureau of Economic Analysis Regional data (employment) and Surveillance, Epidemiology, and End Results data (population).

Altogether, our research indicates that recessions produce enduring economic disruptions to local economies, and this pattern has existed for at least the past five decades. Consequently, recessions likely play a role in the shift of economic activity across places over time; this, in turn, has implications for economic opportunity for people who grow up in areas badly hit—especially repeatedly—by recessions. The social safety net meant to deal with cyclical, temporary labor market disruption—unemployment insurance, SNAP (food stamps), and one-time cash grants—has not, in the past, led areas to recover. Instead, public policy may need to come up with more extensive and longer-term programs to help workers improve their skills, help businesses retool, and, more broadly, help communities reinvest in economic development.

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