What long term impacts did the Great Recession have on employment?

Summary of research by Danny Yagan

**Employment Rates Have Not Recovered From the Great Recession**

During the Great Recessions, the U.S. unemployment rate rose sharply from five percent to ten percent. By the end of 2015, it had returned to its pre-recession level below five percent. At first glance, this would seem to indicate that the U.S. labor market recovered from the recession. However, while the unemployment rate has bounced back, the labor force participation rate (the share of adults who are employed or seeking employment) did not return to pre-recession levels. In fact, it declined more than three percentage points between 2007 and 2015 and never recovered, as millions of adults exited the labor force. This drop in the labor force participation rate cannot be fully explained by demographic change. In this research brief, we present research from O-Lab affiliate Danny Yagan exploring the role of the Great Recession in producing this decline in employment.

**What Caused the Decline in Employment?**

It is possible that some of the decline in employment between 2007 and 2015 occurred independent of the Great Recession. Technical innovations and trade, for example, could have led to layoffs in certain industries that were not related to the recession. To separate out these factors and isolate the effect of the Great Recession, Yagan uses variation in the severity of the recession across parts of the country. He finds that the recession was responsible for most of the decline in employment.

Not all parts of the U.S. experienced the Great Recession equally. Phoenix, for example, experienced a large unemployment shock, while San Antonio was hit relatively mildly. To compare regional severity, Yagan categorizes all U.S. local areas based on the magnitude of the local unemployment shock between 2007 and 2009.

**Figure 1: Magnitude of Unemployment Shock**
Using anonymized individual data from over a million federal income tax records, Yagan finds that workers who were living in areas that suffered severe unemployment shocks in 2007 (like Phoenix) were less likely to be employed in 2015. These effects were largest for workers with lower initial earnings. Extrapolating from local areas to the aggregate United States, the results suggest that the Great Recession caused 76% of the decline in the overall U.S. employment rate.

**Figure 2: Effect of Great Recession Local Shock Over Time**

**Policy Implications**

In contrast to the conventional view that recession impacts are short-lived, Yagan’s research shows that the Great Recession’s employment impacts were persistent. Despite normal signals that the recession is over, it is possible that the U.S. is still not at a full employment level consistent with stable inflation. This paper opens opportunities for further research to model labor force exit during and after economic fluctuations, to test for the long-term employment impacts of previous recessions, and to examine any continued and future impacts of the Great Recession.

Beyond its implications for future research, the findings in this paper suggest that significant stimulus early in a recession may help avoid long-lasting labor market damage. Continued stimulus policies could even be warranted to spur reentry of those who are still non-employed years after the recession’s end. Alternatively, job training or skill development policies may be able to combat persistent non-employment—helping to replenish skills lost during joblessness and to prepare workers for jobs in the new economy.