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More entrants or fewer leavers? A look at rising labor force participation

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Labor force participation declined significantly for prime-age workers (25 to 55 years old) during the Great Recession of 2007–09. However, in "Is the hot economy pulling new workers into the labor force?" (*Economic Letter*, Federal Reserve Bank of San Francisco, May 20, 2019), author Regis Barnichon argues that the current rising labor force participation rate for prime-age workers is a result of fewer people leaving the labor force rather than new people entering.

Barnichon uses counts of individuals in different labor force states at a point in time and counts of individuals moving between labor force states to describe potential scenarios for rising labor force participation. Although most people believe that the rise in labor force participation is the result of a large number of new entrants, the author argues that rising labor force participation is actually a result of fewer labor force leavers.

Using Current Population Survey data from the U.S. Bureau of Labor Statistics, Barnichon compares the inflows and outflows (the probability that workers enter or exit the labor force from one month to the next) from 1976 to 2018 and estimates their contribution to overall labor force participation rates. Based on comparisons, with inflows remaining steady, overall participation closely followed changes in outflows since the end of the Great Recession.

Inflows and outflow rates typically increase during recessions. Some researchers say that the countercyclical inflow rate is a result of the "added-worker effect" in which households that previously had one income might have another adult begin to look for work during economic slowdowns. Outflows vary over the business cycle, and the outflow rate captures the probability of an average labor force participant leaving, called the composition effect. Unemployed workers are more likely to leave the labor force as they become discouraged, whereas an employed worker has no obvious reason to leave. During recessions, job seekers stay unemployed for a longer period of time, causing the outflow probability of the average labor force participant to increase.

Using a more detailed framework to account for the contribution of the composition effect to changes in the outflow rate, Barnichon analyzed the structure of the labor force and other factors, such as the propensity of employed and unemployed people to leave the labor force. The results show that during the Great Recession, large numbers of people could not find work and left the labor force and that the composition effect in the outflow rate was entirely responsible for the overall labor force participation rate decline.

Barnichon closes by noting that as the labor market improves, particularly as unemployed workers find jobs faster, participants are less likely to become discouraged and leave the labor force, causing the overall labor force participation rate to rise.