

QUALITY OF THE LABOR FORCE

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It's a pleasure to be with you this evening to discuss issues surrounding the nation's labor force. Recently, our economy has grown at a robust pace, and, as a result, labor and capital resources are now at or near the point of full utilization. While inflation has risen because of increased energy prices, outside the energy sector, inflation has remained well contained. Over the same period, monetary policy has moved from a highly accommodative stance to one that today is more neutral. Remarkably, this economic performance has occurred despite a number of shocks to the economy, including hurricanes and considerable energy price volatility. The U.S. economy continues to demonstrate its resiliency and underlying macroeconomic strength.

As I talk with business people in the Tenth District, I am hearing more reports of shortages of qualified workers. This is one indication that resource utilization is increasing. In a recent survey of small businesses by the National Federation of Independent Businesses, 31 percent of firms reported unfilled job openings, almost twice as many as reported such openings in 2003. In addition, 13 percent of firms listed labor quality as their single most important problem—the third-most common response behind taxes and health insurance.

Mismatches between the supply of skills in the workforce and the demand for skills by employers create challenges for monetary policy, making it harder to achieve low overall unemployment with stable inflation. But shortages in skilled workers also raise longer-run issues for our economic performance. Inadequate growth in the supply of skilled workers can hold down our overall rate of economic growth. In addition, failure of the supply of skilled workers to keep up with the demand can worsen income inequality by widening the gap between skilled and unskilled wages.

Shortages of qualified workers have become more common partly because stronger job growth has reduced the overall rate of unemployment. But several other factors may be contributing to the increased reports of shortages. First, firms in some industries may be having more difficulty finding workers because the industries are being shunned by young people just entering the labor force. Before the 1980s, for example, manufacturing was seen as a source of stable, high-paying jobs with generous benefits. With frequent stories in the media about plant closures and cuts in wages and benefits, careers in manufacturing have lost some of their appeal to today's youth. In a similar manner, the boom-and-bust cycle in the energy sector over the last three decades discouraged many young people from pursuing careers as oil and gas engineers or rig workers.

Another factor that may be contributing to the increased reports of shortages is that firms are trying to fill new positions from outside instead of training their existing workers. According to this view, increased turnover in the labor market has reduced firms' incentive to invest in job training. Rather than bringing existing workers up to speed, firms may be seeking workers who already have the required skills and can hit the ground running. If the required skills are highly specific, such workers may be hard to find.

A final explanation for the reported shortages is that globalization and technological change are creating demands for new skills. In U.S. manufacturing, competition from foreign companies with access to low-wage, unskilled labor is causing a shift toward higher-end products that are technologically sophisticated or tailored to the specific needs of customers. These higher-end products have increased the demand for

highly skilled factory workers at the same time that the supply of young people interested in manufacturing careers has declined.

Reported shortages of skilled workers are less common today than during the economic boom of the late 1990s. However, there are reasons to believe such shortages may increase in the years ahead, even if the economy grows close to its potential. One reason is that in some industries, a high percentage of skilled employees are in their 50s and close to retirement. Two such industries that are important in our District are aircraft manufacturing and oil and gas extraction. In 2000, the share of employees aged 50 or older was 37 percent in aircraft manufacturing and 31 percent in oil and gas extraction, compared to 25 percent in all industries.

Another reason shortages of skilled workers may increase is that growth in educational attainment is projected to slow. The percentage of people aged 25 and older with college degrees has increased sharply since World War II—from only 6 percent right after the war to 28 percent in 2004. During the last three decades however, most of the increase in the share of college graduates has been due to the replacement of elderly people who grew up during times of low college enrollment by better educated young people. Over the same period, the share of adults aged 25 to 29 who graduated from college has increased only modestly. If college enrollment rates do not turn back upward, growth in the supply of college graduates will likely fall short of growth in the demand for such workers, which will continue to be boosted by technological change.

What can be done to alleviate such shortages of skilled workers? First is to raise college enrollment in the nation. During the last several years, there have been some signs of an increase in school attendance among people in their late teens. It is too soon

to know, however, whether this increased interest in school is a temporary response to the slowing of the economy in the early 2000s or a longer-term trend. At some point, further increases in college enrollment will come only by raising enrollment among the nation's disadvantaged minorities, who currently lag well behind in college attendance. For some states such as Wyoming, an additional challenge is to retain those young people who do go on to college. During the second half of the 1990s, for example, Wyoming suffered a net outflow of 3,800 college graduates aged 25 and older, more than 5 percent of the total.

Besides increasing the supply of college graduates in the U.S., it is important to upgrade the skills of blue collar and clerical workers in the middle of the job distribution. One way to do that is to devote more resources to primary and secondary education, including vocational programs. Another way is to take greater advantage of community colleges, which not only prepare local youth for technical careers but also retrain older adults whose skills have become outdated. Improving skills for middle-level workers is not only valuable in its own right but also can help states like Wyoming attract and retain highly educated workers. If Wyoming's blue collar and clerical workers are viewed as highly productive, more firms will choose to locate here. And if more firms locate here, more high-level jobs will be created for college graduates, slowing the brain drain.

While increasing the quantity of education in the United States is highly desirable, changes in the global economy make it equally important to increase the *quality* of education. The supply of highly educated workers in foreign countries has increased greatly over the last three decades. With advances in electronic communication, some services that used to be produced by well-educated workers in the United States now can

be provided by these highly educated workers abroad. In the face of these changes, we need to ensure that U.S. workers at all levels have the kinds of skills that allow them to do their jobs better than lower-paid workers overseas. That means putting more emphasis in our educational system on creativity, problem solving, and communication skills.

My main focus this evening has been on the need for skilled workers. But even with continued technological progress, there will still be many unskilled jobs that need to be performed in our economy. For the most part, these will be jobs that require little education but cannot be easily automated, such as janitorial jobs, restaurant jobs, and certain construction and agricultural jobs. In recent years, unskilled immigrants have played an important role in performing these jobs, and they can continue to do so in the future. However, because the potential supply of unskilled workers from poorer countries is so vast, it is important to bring the volume of immigration under better control, as Congress and the Administration are trying to do. Whatever level of immigration we do decide to allow in this country, we also must make sure to provide opportunities for poorly educated immigrants to upgrade their skills. That way unskilled immigrants can eventually move on to better jobs, leaving the many low-end jobs that still need to be performed in our economy to the next round of legal immigrants.

Let me conclude by saying that to ensure favorable economic performance in the U.S. economy over the longer run, it is important to increase the skills of our workforce. This will require us not only to raise college enrollment in the nation but also use our community colleges and other educational institutions to upgrade skills in the middle of the job distribution.