Bifurcated Economic Recovery from the Coronavirus Recession: And the Winner is…?

by

Manfred Keil and Arlo Jay[1]

The latest employment report released by the California Employment Development Department (EDD), contains labor market information on the 58 California Counties and 26 Metropolitan Statistical Areas (MSAs). The report does not contain much positive news for the Inland Empire MSA (San Bernardino County and Riverside County). The raw data, which does not take into account regularly occurring seasonal fluctuations, saw a slight 0.1 percentage point increase in the unemployment rate, but this was for December, a month during which seasonal employment should increase every year significantly because of the holidays. Once we remove the regularly occurring employment fluctuations, the Inland Empire unemployment rate increases to 5.7%, up from 5.4% in November, which is a large jump in terms of month-to-month changes. It means that while we missed a national recession in 2023, we are not out of the danger zone yet. Unfortunately there will be no report in mid February due to the annual revisions of the data, and we cannot tell before mid March what the underlying forces are. While there are many signs of a soft landing, don’t unbuckle your seatbelts yet until the plane comes to a full stand still.

Time to look at the big picture.

The economic expansion between the end of the Great Recession (June 2009) and the beginning of the Coronavirus downturn (March 2020) was the longest period of uninterrupted economic growth in U.S. post World War II history: it lasted 128 months. The initial recovery was not spectacular at all: it took five years (July 2014) for employment levels to return to pre-recession levels. Workers who had lost their jobs during the 2008-2009 recession were primarily working in manufacturing and construction (hence referred to as a ‘mancession’), and did not regain employment for quite some time.

The recoveries that followed the Great Recession and the Coronavirus downturn were uneven across industries and regions. Since our expertise is on the Inland Empire and the role it plays in

[1] Keil: Chief Economist, Inland Empire Economic Partnership, Associate Director, Lowe Institute of Political Economy, Robert Day School of Economics and Finance, Claremont McKenna College; Jay: Research Analyst, Lowe Institute of Political Economy.

Southern California, we want to focus here on San Bernardino County and Riverside County labor market behavior.

Let's start with the Great Recession of 2008 to mid 2009, and then compare that situation to the more recent Coronavirus episode. The Inland Empire had a "first in, last out" experience since we were one of the epicenters of the housing bust. With hindsight, we should have seen the oncoming train in the tunnel since housing prices started to decline long before the start of the recession in December 2007. Employment in construction and manufacturing peaked in June 2006, a year before the peak in total employment. Unemployment rates in the Inland Empire reached 14.2% in November of 2010. This was worse than the unemployment rate for California (12.6%), and much worse than the national rate (10.0%). Subsequently we saw a bifurcated recovery, where coastal regions performed significantly better than inland areas across the state of California.

What about the Coronavirus recession and its recovery? It is well known that the most affected industrial sector was Leisure and Hospitality. Hence geographical areas that had a higher share of employment in that sector suffered more than those that had a lower share: over 50 percent of the variation in the initial unemployment rate increase across the Metropolitan Statistical Areas can be explained by the difference in labor shares for Leisure and Hospitality. Hence while the Inland Empire peaked at 15.2% in May of 2020, Los Angeles County reached 19% and even California as a whole showed a 16.1% rate.

Subsequently, the Inland Empire experienced a much faster recovery back towards unemployment rate levels seen at the end of the previous expansion (February 2020). Logistics played a major role during the recovery. In the Inland Empire, it became the second largest employer, since we are the 'warehouse capital of the world' according to *The Economist* magazine. By December 2021 we saw extraordinarily low levels of unemployment rates in the Inland Empire, especially after seasonally adjusting the data: 3.2% (June 2022).

Since then, economic activity in the Inland Empire has slowed significantly. We do not attribute this to the early sign of a national recession ('first in…'), but instead to the adjustment by consumers from shifting expenditure patterns away from consumer goods and back towards services (eating out, hotels, entertainment, etc.). At face value, the impact of this transition struck the Inland Empire more than other regions in Southern California and indeed both the state and the nation. Since February 2020, the seasonally adjusted unemployment rate in the Inland Empire has increased by 1.5 percentage points, reaching 5.7%. It is thereby significantly above the U.S. figure (3.7%) and higher than the state's 4.9%. The Inland Empire unemployment rate is also significantly higher than that of Orange County (4.3%), Ventura County (5.0%), and Los Angeles County (5.6%).

This does not sound good at first. But the unemployment rate is made up of two underlying variables: the labor force and employment. The unemployment rate will *change* by the amount that the *labor force growth outpaces employment growth*. For example, if the labor force does not grow at all but employment increases by 0.3 percentage points, the unemployment rate falls by 0.3 percentage points. Now comes a less intuitive example: employment increases, say by 0.1% but the labor force attracts more people, not all of which find a job right away. Let's say this amounts to 0.3 percentage points. Here the unemployment rate will increase by 0.2 percentage points despite the fact that employment grew.

We are trying to torture you with a bit of algebra for a reason because it is relevant to understand the current situation in the Inland Empire labor market. Yes, we have the highest unemployment rate, but in all other Southern California areas, both the labor force and employment have shrunk since February 2020! *The Inland Empire is the only region in Southern California where employment and the labor force have actually grown* - this is a healthy situation. Unfortunately, the labor force grew faster than employment (it was up by 2.4% while employment increased by 0.9%), and hence our unemployment rate is 1.5 percentage points higher. If people had not joined the labor force in such large numbers, the unemployment rate for the Inland Empire would be roughly a percentage point below what it was in February 2020, namely at 3.3%. This suggests that we should worry less about our relatively high unemployment rate - we are doing comparatively well.

What about the other Southern California areas? Not so good. Los Angeles County did worse - its labor force shrank by 6.4% since February 2020 (roughly 1 out of 20 workers gone). Whether this is due to out net migration to another state or just a migration to the Inland Empire, which becomes more attractive with more work done from the home office and therefore less commuting, needs to be seen. The county also has an older worker population so this may partly be due to older workers leaving the labor force due to retirements. Employment in Los Angeles County also fell by 6.4% leading to a relatively small increase in its unemployment rate of 0.5 percentage points. Orange County is another loser: its labor force shrank by 1.8% and its employment by 3.1%. Similar numbers hold for Ventura County.

The bottom line is that the Inland Empire is doing relatively well economically and we are experiencing a bifurcated recovery. Compared to a year ago, we have the second highest employment growth among major MSAs in the state, including Silicon Valley and San Francisco. The Inland Empire used to be the loser in the recovery, it is now the winner. Behind the initially discouraging unemployment rate are a labor force and employment that continue to grow as the rest of Southern California experiences shrinkage in both.