Closing the Gap
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Thank you very much for inviting me to talk with you today. Diversity is a major priority for us at the Richmond Fed and throughout the Federal Reserve System. And it's important for us to think about diversity not only in the context of our own workforce and supplier base, but also in the financial industry more broadly.

In many ways, the disparities we see at the management level — which I'm looking forward to hearing Daniel Garcia-Diaz discuss in our next session — have their roots very early, in the opportunities available to people even as young children. Today I'd like to talk about those disparities and put them in the context of the macroeconomy. I'll talk particularly about human capital, which plays a critical role in labor market outcomes. Before I say more, the views I express are my own and might not be shared by my colleagues in the Federal Reserve System or on the Federal Open Market Committee (FOMC).[1]

Growing the Labor Force

The FOMC met this week and reviewed a pretty healthy economy. Growth is strong. Inflation is moderate, and the unemployment rate is as low as it's been since the late 1960s. We've been adding an average of more than 200,000 jobs per month for over five years, which is a very large number when the "breakeven" to keep up with population growth is around 80,000-100,000 jobs per month. There are actually more job openings than there are people looking for jobs.

One question many people have is, how long can this kind of growth last? Economic growth depends on how many people are working and how productive they are. But currently, our labor force is growing quite slowly due to declining fertility rates, an aging population and declining immigration. None of these seem likely to change in the near term. At the same time, productivity growth has been relatively slow. Absent a major productivity surge, then, our growth depends on whether there are still a lot of people on the sidelines who can be drawn into the labor force.

There are definitely a lot of people on the sidelines. The labor force participation rate has dropped about 4.5 percentage points since 2000, from a little over 67 percent to less than 63 percent. That might not sound like a lot, but it is a really big number to the people who study this kind of thing. That means that while the unemployment rate has dropped about 6 percentage points since its Great Recession-era peak, the employment-population ratio has barely budged and is still below pre-recession levels.

But that doesn't tell us everything we need to know about how deep the labor market's bench is — we also need to consider how likely those people are to return to the labor force. Much of the drop is due to demographics, such as baby boomers retiring and more young people attending college. If we look at the labor force participation rate for so-called "prime-age" workers, between 25 and 54, the labor force participation rate is much higher, around 82 percent, and is only 2 percentage points lower than it was in 2000. This suggests that the people most likely to be in the labor force are already in the labor force.

So what can we do to bring people off the sidelines? We're unlikely to force retirees back into the workforce, and we want kids to go to school. But there are large disparities between groups of people of prime working age across a variety of dimensions, particularly education, which in turn is correlated with various measures of socioeconomic status, as well as with race and ethnicity. Education gives us an opportunity to boost labor force participation and improve employment outcomes for these groups. In my view, it's the biggest opportunity for the growth of our economy.

The Education Gap

Beginning around 1980, having a college degree emerged as one of the great dividing lines in our economy. College-educated workers earn about 80 percent more than workers with only a high school degree. They're also less likely to be unemployed and are less affected by swings in the business cycle. Following the Great Recession, for example, the unemployment rate for college-educated workers barely topped 5 percent; for workers with only a high school diploma, it peaked at 11 percent. Currently, the unemployment rate for workers with at least a four-year degree is 2.3 percent, while it's 4 percent for workers with only a high school diploma.

Granted, 4 percent is still a pretty low number. But it has to be weighed against the number of people with only a high school degree who have stopped looking for work: The labor force participation rate for this group is less than 58 percent, compared to 74 percent for college graduates. Putting together unemployment and participation, the employment/population ratio for workers who only completed high school is 55 percent. It's more than 72 percent for college graduates.

College enrollment has increased significantly since the 1980s. But roughly 40 percent of students who enroll don't graduate within six years — and they often leave with significant debt loads and without the benefits a degree offers. Both enrollment and completion are tied to socioeconomic status: Children from lower-income families and children who attend schools with a higher proportion of lower-income students are less likely to attend college and less likely to leave with a degree. For example, one study found a gap of nearly 30 percentage points in completion rates for students from low-income versus high-income families.[2] We also see variation by race and ethnicity, particularly when it comes to graduation rates. Black and Hispanic students are as much as 20 percentage points less likely to complete a degree than white and Asian students.

Let's dig in deeper — why is socioeconomic status tied to college achievement? It's not as simple as not being able to afford to go, although that is certainly an obstacle for some students. We also see wealth and income interact with how prepared students are for college. College is a risky investment, so, for example, a student from a low-wealth household who doesn't think he has a great chance of graduating might decide, quite rationally, to not enroll in the first place.[3] Similarly, a student from a lower-income family who learns after several semesters that she doesn't have the necessary skills might be more prone to drop out than a similarly skilled student with more family resources.[4]

We also know that socioeconomic status is tied to the opportunities students have to obtain those skills in the first place, beginning with access to high-quality early childhood education and continuing on through K-12. Finally, income is linked to how much "knowledge about college" students have, such as navigating the application process, taking entrance exams, and applying for financial aid. In part, this could be because students from lower-income backgrounds know fewer adults who have completed college. It also could be because they attend high schools with fewer resources for college guidance.

One avenue for policymakers is looking at how to reduce these differences in access and preparation during the elementary and high school years.[5] Schools can also look at how to help their attendees graduate; for example, mentorship programs such as the one offered at the online Western Governors University, which has an 80 percent graduation rate, can be very effective.

College Isn't the Only Option

I've spent the last few minutes emphasizing the benefits of a college education. But for some people, a four-year college just isn't the right fit. And at present, as I mentioned, there are actually more job openings than there are people looking for work — and many of those openings are for well-paying jobs that don't require a college degree. Health care workers, airline mechanics, truck drivers, and skilled tradespeople, for example, are all in high demand right now.

Thus, part of preparation at the K-12 level should be informing students about those opportunities and about how they can train for them, for example, at community colleges or via apprenticeship programs. This could help students improve their prospects relative to quitting their labor market preparation after high school, which they might do if they think a four-year school is their only postsecondary option, or by enrolling in and then dropping out of a four-year college.

Conclusion

The challenges are huge and the stakes are high, both for individuals and for our ability to develop the workforce we need. If we want to increase the diversity of our corner offices and boardrooms — and build a pipeline of diverse candidates for these offices — we need to address the disparities that exist well before the job interview. This is also one of our best opportunities to ensure our economy's continued growth.

The size of the opportunity is significant. If we could bring the employment/population ratio of those with only a high school degree up to the ratio of college graduates, for example, we would have roughly 11 million more people at work. That's a lot of people contributing to our country's economic growth.

The Richmond Fed is digging deeply into the issues and welcomes any thoughts you have on possible solutions. Now, please join me in learning from what Mr. Garcia-Diaz has to say.

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[1] Thank you to Jessie Romero for assistance preparing these remarks.
[2] National Center for Education Statistics. "Education Longitudinal Study of 2002."
[3] Kartik Athreya and Janice Eberly. "Risk, the College Premium, and Aggregate Human Capital Investment." Federal Reserve Bank of Richmond Working Paper no. 13-02R, revised November 2016.
[4] Ali K. Ozdagli and Nicholas Trachter. "On the Distribution of College Dropouts: Wealth and Uninsurable Idiosyncratic Risk." Federal Reserve Bank of Richmond Working Paper no. 15-15, November 2015.
[5] Urvi Neelakantan and Jessie Romero, "Falling Short: Why Isn't the U.S. Producing More College Graduates?" Federal Reserve Bank of Richmond 2017 *Annual Report*.