

**AGRON NICAJ**  
US Economist

Economic Research Office

T: +1 (646) 357 6180  
E: anicaj@us.mufg.jp

**MUFG Bank, Ltd.**  
A member of MUFG, a global financial group

## Uncertainty over future labor supply

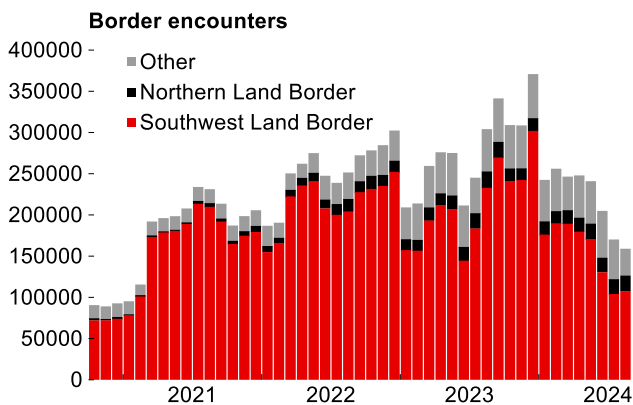
September 24, 2024

- Growth in unemployment, so far, has largely been a result of rising numbers of new and re-entrants to the labor force. High immigration levels have primarily driven growth in new entrants, but declining encounters along the southwest border may signal a slowdown in new workers entering the US. Additionally, strong political pressure to curb immigration may alter the trajectory of labor force growth over the next decade.
- Re-entrants to the labor force comprise a significant share of total unemployment, with growth over the past few years contributing to labor force participation rates exceeding expectations. Projections over the next decade, however, show participation rates falling across the broader labor market and even for prime-age workers.
- Continued growth in re-entrants to the labor force can keep participation rates above projections, but historically that means less than favorable economic conditions. There exists a historically negative relationship between perceptions of good buying conditions and growth in re-entrants to the labor force, but there has been a dramatic reversal since 2021. This “new” relationship appears unlikely to hold, with Fed rate cuts supporting improved household financial conditions and less of a need for workers to re-join the labor force.

### Immigration will likely slow

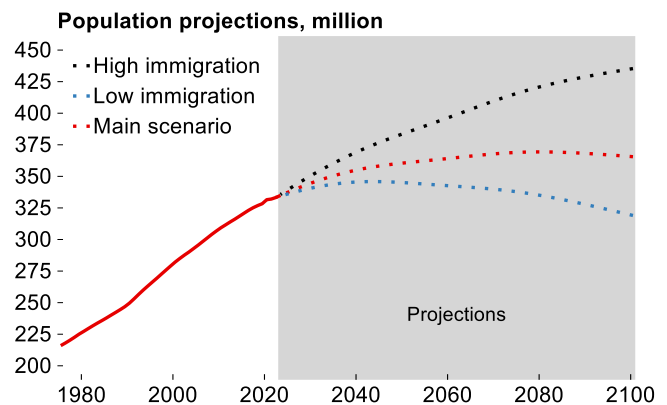
Strong immigration growth has notably altered labor market dynamics in the short-run. In 2023, the unemployment rate remained below 4% while nonfarm payrolls grew by an average of 250,000 per month. For this to occur, breakeven jobs growth (monthly job growth needed to avoid a change in the unemployment rate) would have to have risen.

**Chart 1:** Southwest border encounters have fallen sharply since the start of summer



Source: Department of Homeland Security, MUFG Bank Economic Research Office

**Chart 2:** Recent immigration trends and political pressures make the high immigration scenario less likely



Source: Census Bureau, MUFG Bank Economic Research Office

Long-run breakeven employment growth is estimated to be around 70,000 to 90,000, but surging immigration and improvements in labor force participation rates over the past couple of years have significantly increased the size of the labor force, pushing short-run breakeven growth to at or above 200,000. Over the past 5 months, average monthly jobs growth has fallen below that estimate to 135,000, while 40,000 new entrants and 212,000 re-entrants were added to the labor force. A slower absorption of more workers into employment has allowed the unemployment rate to rise above 4% without a significant rise in job losses.

Immigration has been the primary source of growth in new entrants (unemployed people looking for their first job), pushing the share of foreign-born workers to 19% in Q2 2024, up from about 17.5% in 2019. This level of growth is significant by historical standards, and it has helped the Fed manage inflation by shrinking the gap between labor supply and demand, easing labor shortages and slowing nominal wage growth. Going forward, however, immigration is expected to slow, which may have implications for broader economic growth and for monetary policy.

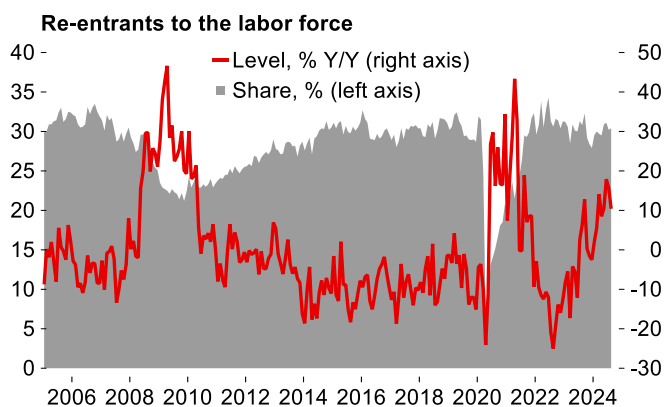
Shown in Chart 1, the number of nationwide border encounters (including apprehensions, inadmissibles, and expulsions) has gradually fallen over the past 3 months, with most of the slowdown concentrated at the southwest border with Mexico. Attempted migration to the US may be “normalizing” toward a more sustainable level after historically high peaks from 2021 to 2023.

To add to it, the current political environment makes the US ripe for immigration reform. Depending on the outcome of the elections in November, there could be substantial changes made to immigration policy that would affect the trajectory of population growth in the US. Under a Republican president and Republican controlled Congress, more significant reform can be expected as it remains a leading concern among the voter base. Even under a Democratic president, there is an expectation that immigration will slow under claimed proposals, especially considering the high likelihood of a Republican controlled Senate. Projections of a high immigration scenario now appear less likely than they did at the beginning of this year (Chart 2).

### Re-entrants drove participation rates higher

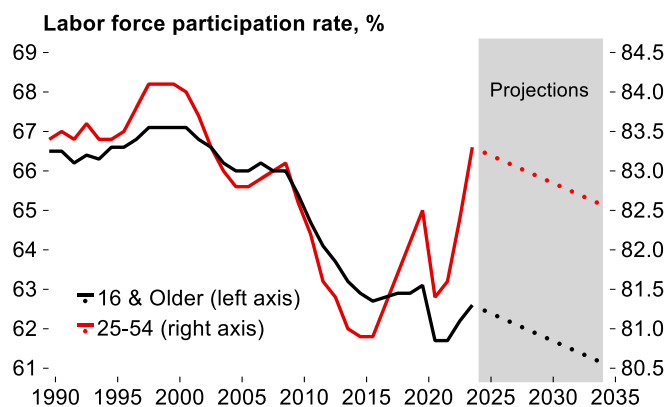
Labor supply growth was supported not only by immigration, but also by re-entrants to the labor force (unemployed people with past work experience that left the labor force for a period of time before returning) that pushed up participation rates. Re-entrants comprise a significant share of total unemployment, and if growth can be sustained at its current rate, it can help offset some of the negative effects of slower immigration.

**Chart 3: Re-entrants make up a substantial share of the total unemployment level**



Source: BLS, MUFG Bank Economic Research Office

**Chart 4: Continued growth in labor force re-entrants can keep participation rates higher than current long-run projections**



Source: BLS, MUFG Bank Economic Research Office

Shown in Chart 4, labor force participation rates have been trending downward for the broader labor force (16 & older) over the past 20 years. Projections from the BLS show a continued decline, with demographic forces being the major driver. The participation rate of older workers (55 & older) is considerably lower than other workers (less than 40% compared to over 80% for workers 25-54), and with America's largest generations by population aging out of the workforce, we can expect a continued decline.

Strong immigration growth can certainly alter this demographic trend, but with uncertainty clouding future policy, the focus should be on the prime-age workforce (25-54) where labor force participation rates have been exceeding expectations. Since January 2023, the prime-age participation rate has risen by 1.2 percentage points, a significant and largely unexpected increase given how pessimistic longer-run projections are. The latest BLS projections show the prime-age labor force participation rate falling by nearly 1 percentage point over the next 10 years (Chart 4), little change from annual projections made last year.

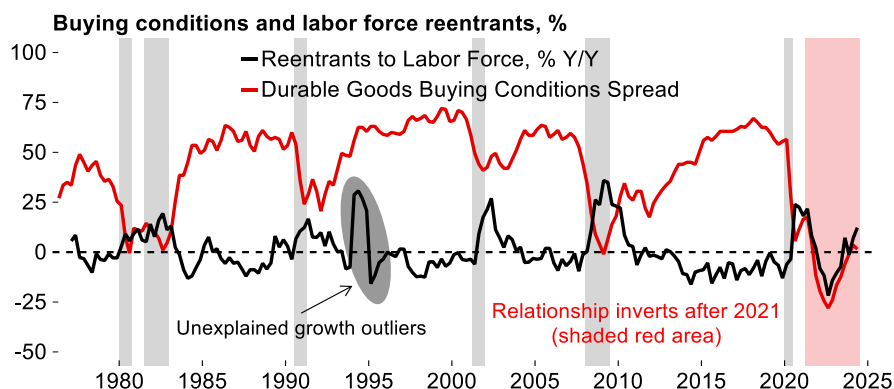
Most of this unexpected improvement can be attributed to growth in re-entrants to the labor force. The share of re-entrants has fully recovered to pre-pandemic levels and the growth in level continues to trend upward toward rates typically only experienced during recessions (Chart 3). Immigration certainly played some role in increasing participation rates overall, but the rate of native workers is almost 4 percentage points higher than foreign-born workers in the 25-54 age group. The question now becomes why are workers returning to the labor force at such a strong rate, and can growth continue amid an uncertain future of domestic and monetary policy?

### Perceived buying conditions and labor supply growth

Maintaining growth in the labor force has strong implications for monetary policy. Slower growth in the labor force can expand the gap between labor supply and demand, increasing the severity of labor shortages and applying upward wage pressures. If sustained for long enough without parallel productivity gains, the upward pressure on prices increases.

Though the Fed has no control over immigration, monetary policy does directly influence and react to economic conditions that impact workers' willingness to return to the labor force. Historically, poor economic conditions, and more specifically, negative consumer perceptions of buying conditions correlates with growth in re-entrants to the labor force. Shown in Chart 5, there exists a negative relationship between annual growth in re-entrants and the spread between perceived buying conditions of large household durable goods.

**Chart 5: There exists a negative relationship between perceptions of good buying conditions for large household durables and workers re-entering the labor force**

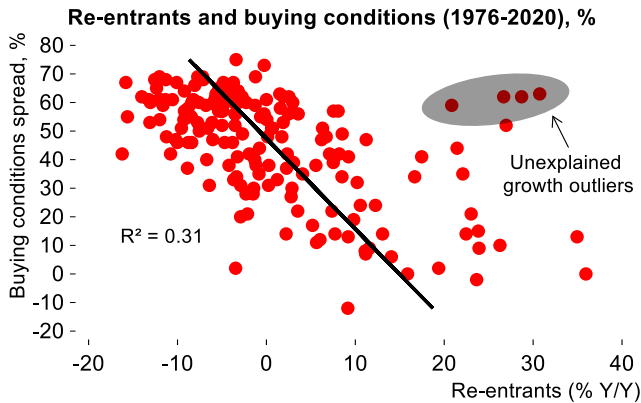


Note: 2-quarter moving average buying conditions spread  
Source: BLS, University of Michigan, MUFG Bank Economic Research Office

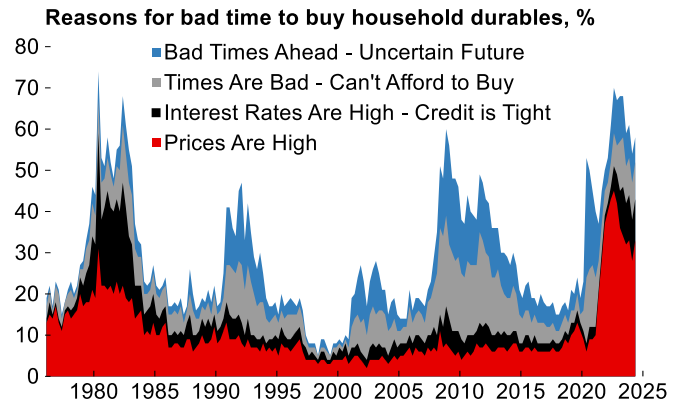
The University of Michigan Survey of Consumers measures perceived buying conditions for large household durables, where respondents assess whether it is a good time to buy, a bad time to buy, or an uncertain time. The percentage reporting good time to buy minus the percentage reporting bad time to buy equals the spread. From 1976 to 2020, this relationship between buying conditions and re-entrants was negative and statistically significant, where for every percentage point increase in the buying conditions spread, there was an expected average decrease of 0.32 percent points in growth rate of re-entrants (Chart 6).

**Chart 6: The relationship between perceived buying conditions and re-entrants is negative and statistically significant**

**Chart 7: Elevated prices is the leading reason why respondents report buying conditions to be bad**



Source: BLS, University of Michigan, MUFG Bank Economic Research Office



Source: University of Michigan, MUFG Bank Economic Research Office

From this perspective, you can broadly conclude that when consumers perceive the economy as being in bad shape, workers are more inclined to re-join the labor force. Intuitively, this relationship makes sense. Degrading household finances can contribute to bad perceptions of buying conditions and it can drive consumers to the labor market where they can increase their incomes. This interpretation has serious implications because it would mean that the economy needs to weaken for labor supply to grow outside of immigration.

The main caveat is that other factors were not controlled for, including any changes to domestic and foreign policy or industry specific factors. Additionally, the historical negative relationship completely reversed after 2021, where improving economic perceptions now coincides with growth in re-entrants (Chart 5). It's not entirely clear why this relationship reversed, but much of the economic pessimism looks to be due to elevated inflation, or more specifically, perceived price levels. Shown in Chart 7, high prices is the most prominent reason that respondents reported buying conditions of large household durables to be bad, despite the relative health of US economy.

As for how this will impact the labor market, it all depends on whether this current relationship holds. Optimism around buying conditions will likely further improve as inflation continues to cool, and credit will be less of a factor now that the Fed's rate cutting cycle has begun. But all of this appears unlikely to drive continued growth in re-entrants to the labor force. The historical relationship between perceived buying conditions and re-entrants will likely re-emerge.

Historically, the perception of "times are bad" contributed to a significant amount of buyer pessimism (Chart 7). Deteriorating household finances is likely a major factor even in today's environment, and elevated inflation may have distorted signals this survey might otherwise deliver. At the moment, re-entrants are joining the labor force at a rate that is historically consistent with a recession. If indeed the signals are distorted from inflation, then growth in re-entrants to the labor force will slow through 2025 as the Fed continues to cut rates and household finances improve. The outlook on labor supply growth overall looks relatively bleak.

## Analyst Certification

The views expressed in this report solely reflect the personal views of Agron Nicaž, the primary analyst responsible for this report, about the subject securities or issuers referred to herein, and such views may not necessarily reflect the thoughts and opinions of MUFG Bank, Ltd. and its affiliates or management team. No part of such analyst's compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed herein.

## Disclaimers

The information and views contained herein are not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject MUFG Bank, Ltd. (collectively with its various offices and affiliates, "MUFG Bank") to any registration requirement within such jurisdiction or country. The information and views contained herein are provided for general informational purposes only, are subject to change, and are not intended to be, nor should be used, or considered, as an offer, or the solicitation of an offer, to sell or to buy or to subscribe to or for securities or any other financial instruments, and do not constitute specific investment, legal, tax or other advice or recommendations. The information contained herein reflects the thoughts and opinions of the noted authors only, and such information does not necessarily reflect the thoughts and opinions of MUFG or its management team. Neither this nor any other communication prepared by MUFG Bank should be construed as investment advice, a recommendation to enter into a particular transaction or pursue a particular strategy, or any statement as to the likelihood that a particular transaction or strategy will be effective and it does not take into account the specific investment objectives, financial situation, or the particular needs of any specific person who may receive this information. Any information relating to performance contained herein is illustrative and no assurance is given that any indicative returns, performance or results, whether historical or hypothetical, will be achieved. Before entering into any particular transaction, you should consult an independent financial, legal, accounting, tax, or other advisor as may be appropriate under the circumstances. In any event, any decision to enter into a transaction will be yours alone, not based on information prepared or provided by MUFG Bank. MUFG Bank hereby disclaims any responsibility to you concerning the characterization or identification of terms, conditions, and legal or accounting, or other issues or risks that may arise in connection with any particular transaction or business strategy. While MUFG Bank believes that any relevant factual statements contained herein, and any assumptions on which such statements are based, are in each case accurate, neither the authors nor MUFG have independently verified its accuracy, and such information may be incomplete or condensed. The information is provided "AS IS". The authors and MUFG do not warrant the accuracy of the materials provided herein, either expressly or implied, for any particular purpose and expressly disclaims any warranties of merchantability or fitness for a particular purpose. The authors and MUFG cannot and do not guarantee the accuracy, validity, timeliness or completeness of any information or data made available to you for any particular purpose. MUFG Bank may have issued, and may in the future issue, other reports that are inconsistent with or that reach conclusions different from the information and views contained herein. Such other reports, if any, reflect the different assumptions, views and/or analytical methods of the analysts who prepared them, and MUFG Bank is under no obligation to ensure that such other reports are brought to your attention.

© 2024, MUFG Bank, Ltd. All Rights Reserved.

## About MUFG and MUFG Americas

Mitsubishi UFJ Financial Group, Inc. (MUFG) is one of the world's leading financial groups. Headquartered in Tokyo and with over 360 years of history, MUFG has a global network with approximately 2,000 locations in more than 40 countries. MUFG has nearly 120,000 employees and offers services including commercial banking, trust banking, securities, credit cards, consumer finance, asset management, and leasing. The Group aims to "be the world's most trusted financial group" through close collaboration among our operating companies and flexibly respond to all the financial needs of our customers, serving society, and fostering shared and sustainable growth for a better world. MUFG's shares trade on the Tokyo, Nagoya, and New York stock exchanges.

MUFG's Americas operations, including its offices in the U.S., Latin America, and Canada, are primarily organized under MUFG Bank, Ltd. and subsidiaries, and are focused on Global Corporate and Investment Banking, Japanese Corporate Banking, and Global Markets. MUFG is one of the largest foreign banking organizations in the Americas. For locations, banking capabilities and services, career opportunities, and more, visit [www.mufgamericas.com](http://www.mufgamericas.com).