

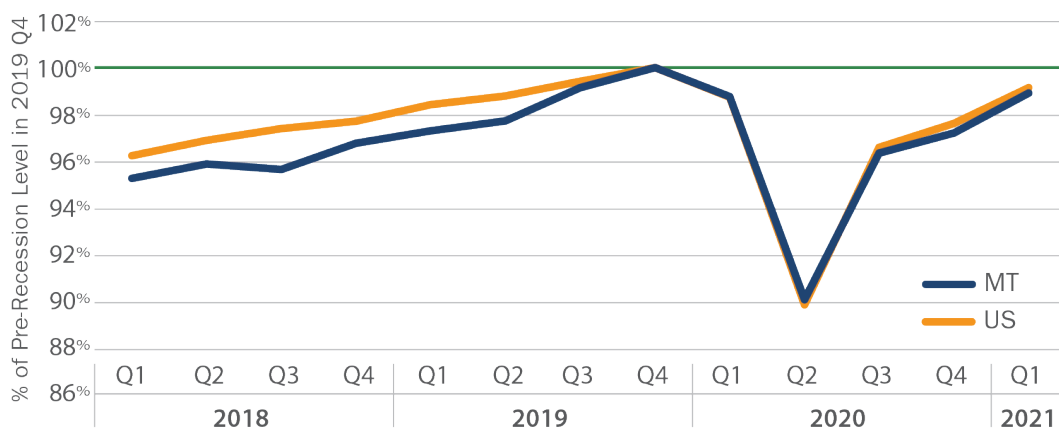
Labor Day Report 2021: A Summary

by Barbara Wagner, Chief Economist

Each year on Labor Day, the Montana Department of Labor & Industry issues a report on the Montana economy called the Labor Day Report. This article summarizes this year's report. The full report is available at lmi.mt.gov/publications.

On Labor Day 2021, the Montana economy is recovering from the COVID-19 pandemic, but uncertainty remains. After the COVID-19 pandemic battered Montana in 2020, bringing heavy job losses and record high unemployment, the state's economy demonstrated resiliency with a strong recovery. Montana posted the 3rd best payroll employment recovery among states since the start of the pandemic recession in February 2020. As vaccinations became available and business restrictions were lifted, Montanans returned to normal business activity, celebrating the ability to safely attend restaurants, concerts, and social activities. The release of this pent-up demand, relaxed COVID-19 protocols, economic stimulus, and higher wage and proprietor income all contributed to surging consumer demand this spring, with businesses scrambling to bring on enough workers to meet customer needs.

FIGURE 1
Real GDP Nearly Recovered from Pandemic Recession



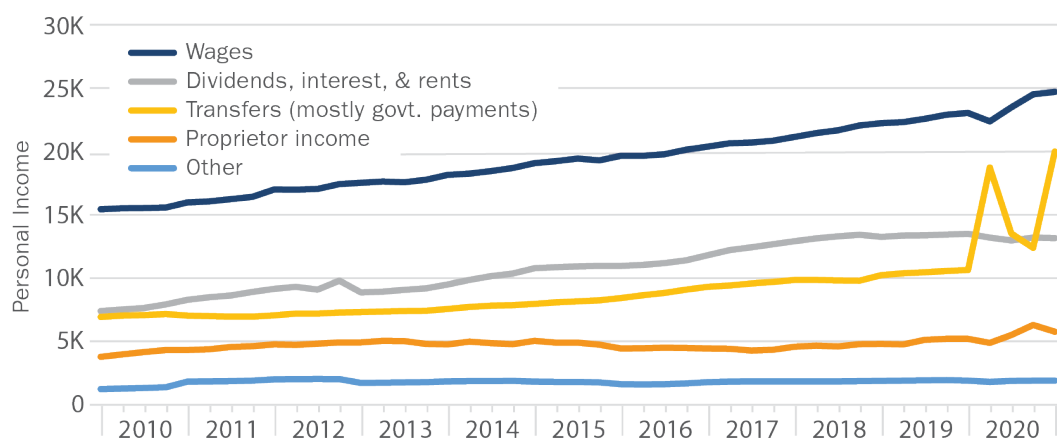
Source: Bureau of Economic Analysis (BEA).

Montana's Real Gross Domestic Product (GDP) levels during the pandemic recession are shown in **Figure 1** with the levels indexed to the pre-pandemic peak. GDP measures the value of goods and services produced by the Montana economy. The U.S. and Montana were very similar in the magnitude and timing of GDP changes during the pandemic. Heading into the pandemic recession, Montana's GDP had been growing steadily at a compounding annual rate of 2% from 2009 to 2019. Then, GDP fell by a total of \$4.8 billion (10%) in the first and second quarter of 2020 as the COVID-19 pandemic impacted Montana's economy. The largest real GDP losses occurred in the healthcare and leisure activities industries, but all industries except agriculture experienced losses. Production surged back in the third quarter, with continued growth in the 4th quarter. The recovery was led by the essential industries of agriculture and construction. Real GDP finished the 1st quarter of 2021 within 1% of the prerecession peak. Montana is expected to track with the U.S. into positive territory in the 2nd quarter of 2021 (state data not yet available). Montana's real GDP growth from 2019 to 2020 ranked 20th among states (with 1 being the strongest growth).

Both the private sector and increased government stimulus payments contributed to Montana's rapid recovery from the pandemic recession, as illustrated in **Figure 2**. **Figure 2** illustrates the sources of Montana personal income from 2010 to 2020. Personal income measures the amount of income received from economic activity, plus government transfers to business owners or households (such as social security, unemployment benefits, or stimulus payments). The increased unemployment benefits and stimulus checks are evident in the spikes in transfers during the second quarter of 2020 and the first quarter of 2021.

Wages paid to workers surged in 2020, despite the pandemic-related job losses, suggesting the wage gains for workers who retained jobs outweighed the wages lost from jobs that disappeared. In the 1st quarter of 2021, wages were \$1.7 billion higher than a year earlier, a 7.2% increase. One reason for the higher wage income is increased worker productivity from remote work. Nationally, nonfarm labor productivity soared during the pandemic, increasing by 3.9% for the year ending 2021Q1. Increased productivity translates into higher wages for workers and higher profits for Montana's businesses.

FIGURE 2
Montana Personal Income Sources



Source: BEA, Personal Income Components

Proprietor (business owner) income also increased in 2020 due to the Paycheck Protection Program and the Coronavirus Food Assistance Program. Overall, proprietor income increased by 10%, or \$506 million. However, without the \$724 million received by Montana business owners from these two economic stimulus programs, proprietor income would have been about \$218 million less than in 2019.

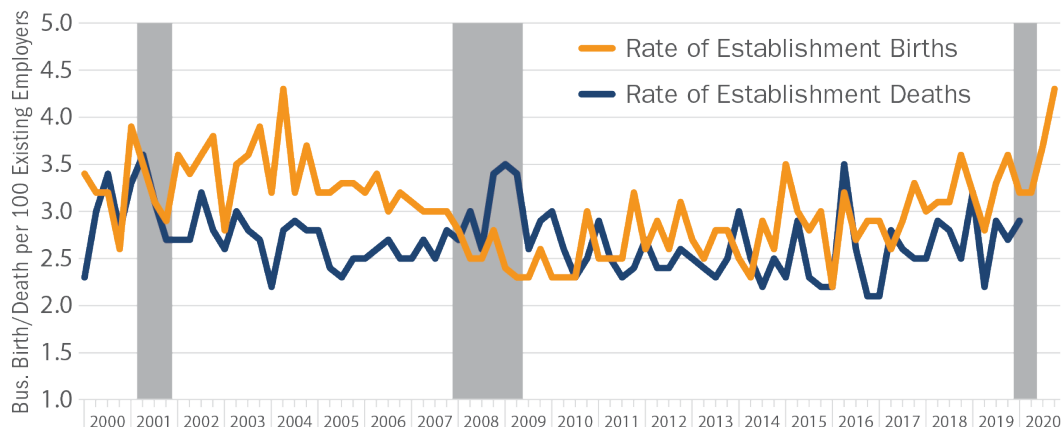
In addition to the increases in business owner income, other indicators also suggest that Montana's entrepreneurs thrived during the pandemic recovery. Entrepreneurship is a core element of Montana's economy. Montana has the 4th highest rate of business ownership in the nation, with 6.3% of Montana households reporting income from a business or farm. The number of self-employed individuals also increased over the last year, suggesting that workers who lost payroll jobs continued to work as self-employed, which often happens during recessions.

Business creation accelerated, with over 3,500 new businesses created in Montana in 2020. The rate of new businesses formed in the state skyrocketed to the fastest rate in ten years, as shown in **Figure 3**, hitting a rate of 4.3 businesses births per 100 existing employers. New establishments provide

a significant source of employment in the state. Over 10,000 Montanans work for businesses opened in the last year, and 45,000 work for businesses less than five years old. Just over half of Montana startups (53%) remain in business five years after their creation, making the state's entrepreneurs more successful than the national average. Existing businesses also demonstrated resiliency during the pandemic recession, with an improved bankruptcy rate in 2020 for both the U.S. and Montana.

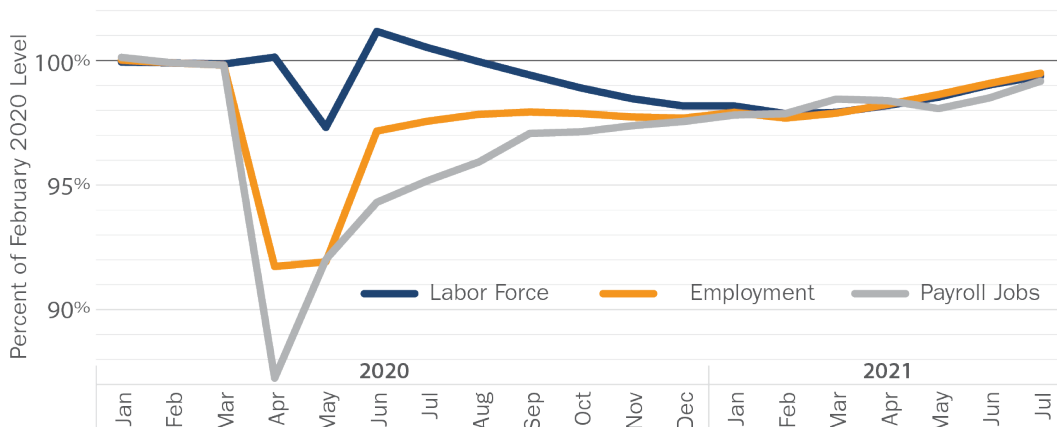
Employment and labor force levels are still lower than the pre-pandemic peak, although a full recovery is expected in the fall of 2021 (**Figure 4**). The COVID-19 pandemic had a tumultuous and dramatic impact on employment levels in Montana. After Montana's first COVID-19 cases were reported in March 2020, total employment levels dropped by 8% or nearly 43,000 jobs. Women, younger workers, those in lower-wage jobs, and workers in the more populated areas of the state were more impacted by the COVID-19 related business layoffs. Thankfully, many of these job losses were temporary, with employment recovering within 2-3% of the previous pre-recession level by September (but still down over 10,000 jobs). After stagnating during the fall and winter, employment levels once again made

FIGURE 3
Rate of Business Births and Deaths Among Private Establishments



Source: Bureau of Labor Statistics (BLS), Business Employment Dynamics.
Private Establishments Rate of Birth and Death as share of existing establishments, all size classes.

FIGURE 4
Indexed Employment and Labor Force



Source: MTDLI using CES & LAUS data published by MTDLI & BLS

gains in the spring of 2021 as vaccinations and additional stimulus led to strong business hiring. Both payroll and total employment levels are now within 1% of the pre-recession peak with a full recovery expected in the upcoming months. Throughout the pandemic and recovery, Montana has consistently remained in the top ten states for employment performance.

When businesses increased hiring in the spring of 2021, they were met by a shortage of available workers and higher average wages. The labor force steadily declined from June 2020 to early 2021 as Montanans struggled to balance work with the pandemic fallout (**Figure 4**). Thousands of workers left the labor force due to fears of contracting COVID-19 in the workplace, and 55,000 Montana parents decreased their work hours due to a lack of childcare and the need to monitor children learning at home. The labor force has started to improve since March as vaccinations reduced infection risk, with over 8,400 workers joining the labor force since February 2021.

Tight labor markets and strong productivity growth have brought higher wages for Montana workers. Total wages paid in all payroll jobs increased by over \$1 billion in 2020 over the prior year, despite a drop in annual employment levels of roughly 13,600 jobs. Average annual wages

in payroll jobs increased by 7.9% in 2020 (up to \$48,400), over double the wage growth rates posted in prior year. The dramatic increase in the average wage can be attributed to two factors. First, workers who retained their jobs had very strong wage gains due to increased productivity (some of which is due to remote work). Businesses were able to pass the savings from remote work on to their employees as wage gains. Second, lower wage jobs were more likely to be lost during the pandemic (leaving only higher wage jobs and driving up the average). Montanans are used to strong wage growth, with the state ranking 8th among states for the fastest average annual wage growth over the last 10 years.

However, COVID-19 remains a threat to our continued economic recovery. Global supply chain disruptions have increased prices and caused some Montana businesses to forego profitable ventures due to a lack of materials and inputs. The inflation and supply chain constraints are expected to be temporary and related to the COVID-19 pandemic. Steady increases in prices are normal – inflation averaged 2% each year since 2000, but prices increased over 5% during summer 2021 compared with summer 2020. Prices for gasoline and other energy have increased by over 20% over the last year. However, the price increases have not yet eroded all of the recent wage gains experienced

by workers, as shown in **Figure 5**. Only in the most recent months has inflation outpaced wage growth (with wage growth tempered by the addition of many lower-wage jobs in restaurants and leisure activities during the reopening this spring). Over the two years ending June 2021, hourly wages have increased by 8.7% while the price level has increased by 6.1%, leaving workers with a 2.6% increase in their real hourly wage.

Inflation has been notable in the rapidly rising home prices in the last two years, exacerbating concerns about affordable housing in Montana. Montana's typical home price was \$327,000 for the year ending June 2021, up 10.3% from one year prior, similar to national appreciation. Low mortgage rates are the primary driver of increased demand for home purchases over the last year, with housing supply shortages continuing to affect prices over the long-term. Montana has the 15th highest housing value of all fifty states.

Labor force participation rates are another area in which COVID-19 continues to challenge Montana's economic recovery. Aging demographics are the long-term cause for a constrained worker supply, but challenges balancing work with other life responsibilities were the force behind a decline in the labor force during the pandemic. Labor force participation rates dropped during 2020 for both the U.S. and

Montana, shown in **Figure 6**. If Montana's rate was the same in July 2021 as it was in February 2020, there would be 11,331 more workers participating in the labor force. Instead, the labor force remains 2,850 workers below the pre-recession peak.

The drop in workers is due to a lack of childcare, contracting COVID-19 or caring for someone with COVID-19, and the fear of contracting the virus. The childcare shortage was a drag on Montana's economy even before the pandemic, with licensed childcare capacity meeting only 44% of estimated demand and the majority of Montana businesses recognizing a shortage in their community. The school and daycare closures during the pandemic worsened this situation, causing 55,000 parents to reduce work hours. In addition, risk of contracting the virus or caring for others with the virus kept an average of 11,000 Montanans from working during the pandemic. Now that vaccines are widely available to the population over 12 years of age, the number of workers who are out of the labor force because of the virus directly has dropped significantly, falling below 5,900. However, COVID-19 outbreaks continue to threaten Montana's economic recovery. Additional workers falling sick from COVID-19 reduces the number of work hours available to the Montana economy and creates uncertainties in staffing for many Montana businesses.

FIGURE 5
Inflation and Montana's Hourly Wages

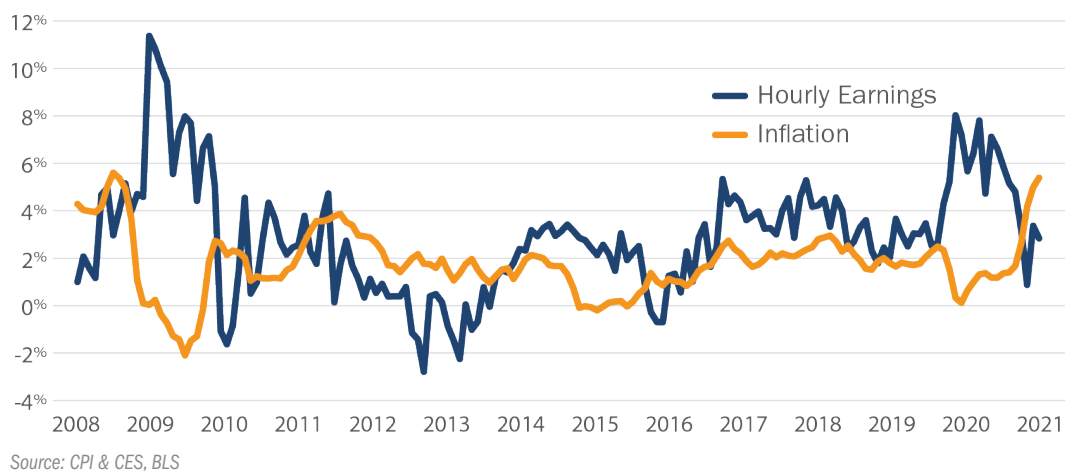
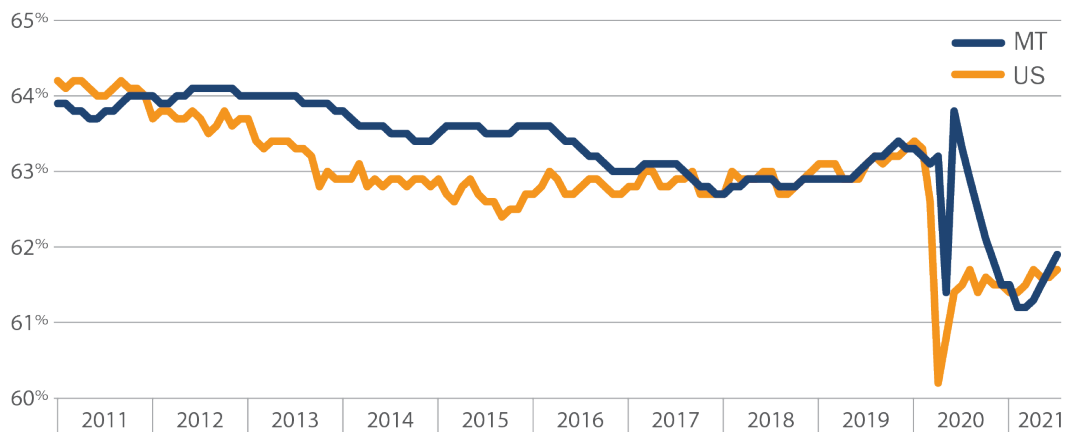


FIGURE 6
Montana & U.S. Labor Force Participation Rates



Source: CPS & LAUS, BLS

After a dramatic and challenging year, Montanans are ready to return to “normal” life. Workers and businesses have demonstrated resiliency with a surprisingly strong recovery. However, our economy is likely to be forever transformed by the pandemic. Remote work has changed the workplace for the better, with higher productivity and offering real potential to tap into underutilized, rural, and reservation worker groups. Greater understanding of how childcare availability impacts business health will likely result in more family-friendly work environments. The pandemic worsened the state’s preexisting worker shortage, but it also drove up wages, encouraging more Montanans to enter the workforce.

A limited worker supply is expected to be the most significant constraint to economic growth. Economic policy has shifted to focusing on engaging more people into the workforce, and ensuring existing workers have the training needed to compete in the global economy. Increases in automation, innovation, and human capital through training allows each Montana worker to achieve their fullest potential, thus reducing the economy’s dependency on labor supply while increasing profitability and output.

Engaging more Montanans in the labor market also will be critical for continued economic growth. Finally, employers can increase the hours of workers to meet demand. The average work week in Montana fell during the pandemic, moving from 33.4 hours per week in 2019 to 32.8 hours per week in 2020. If Montanans would have maintained a 33.4 hour work week in 2020, they would have worked nearly 230,000 more hours – equivalent to 5,700 full-time, year-round employees.

As Montana moves into the post-pandemic world, the new normal is still unknown. Certainly, workers will continue to be in high demand, ensuring greater focus on job quality and higher productivity through worker training and automation. Tapping into underutilized worker groups and more full-time work will also help create additional work hours. However, the resiliency of Montanans demonstrated over the past year can only provide reassurance that future challenges will be met with the same determination and perseverance. Montana’s economy is set to meet these challenges and take advantage of the opportunities available in the post-pandemic world.