Helping People and Communities Affected by Regional Economic Transitions

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Introduction

I thank the Kentucky Philanthropy Initiative (KPI) for inviting me to be with you today, and for the great partnership KPI has forged with the Cleveland Fed as we work together to understand and find solutions to the economic challenges facing this region. I appreciate this opportunity not only to enjoy the beautiful bluegrass scenery but also to gather firsthand information about economic conditions in this part of the country. Yesterday I observed an electrical/fiber optic lineman training program at Hazard Community and Technical College and met with representatives of the Eastern Kentucky Concentrated Employment Program, the Foundation for Appalachian Kentucky, the Housing Development Alliance, and the Mountain Association for Community Economic Development. These were very productive discussions.

Eastern Kentucky is part of the Fourth Federal Reserve District, which also includes the state of Ohio, western Pennsylvania, and the northern panhandle of West Virginia. That's a pretty diverse region, encompassing larger cities, small towns, and rural areas, with a mix of different industries and occupations. The Federal Reserve System, established by Congress more than 100 years ago, was designed in a way to ensure that the Fed's decisions about monetary policy take into account this very diversity. We recognize that our policy decisions affect Main Streets and communities all across the country. As the president of a Federal Reserve Bank, I make it a point to bring the economic information we have garnered from business, consumer, and labor contacts throughout the District to meetings of the Federal Open Market Committee. That's the body within the Fed that sets monetary policy. The insightful regional perspectives that our contacts provide, along with economic and financial data and analysis, all play an important part in the Fed's setting of national monetary policy in pursuit of our statutory goals of maximum employment and price stability.

While most people associate the Federal Reserve with monetary policy, the Fed has had an interest in community development issues for quite a long time. In 1981, the Fed created its Community Affairs function to provide technical training and support to depository institutions to bolster their compliance with the Community Reinvestment Act, a law that promotes equitable access to credit for all individuals and neighborhoods.

From this targeted beginning, the Federal Reserve's work in the area of community development has evolved and expanded, much as the nature of community development in general has changed over time. As people in this room know, access to credit is but one factor – albeit an important one – in determining the economic vitality of households and neighborhoods. Today, the Fed's community development function is active in research and outreach concerning housing markets, workforce development, education, health, and small business lending, among other issues.

While the focus may have changed over time, one thing that hasn't changed is the Federal Reserve's commitment to helping to identify effective policies and best practices for promoting economic progress in low- and moderate-income communities. The Cleveland Fed very much values the relationships we have built with key philanthropic, government, and other organizations working on programs aimed at improving the economic outcomes of people in eastern Kentucky. Those relationships were instrumental in informing our analysis of some of the community development efforts I'll discuss today. I want you to know that the Cleveland Fed's work is just part of the initiatives taking place at the 12 Federal Reserve Banks across the country. For example, the Minneapolis Fed has established a Center for Indian Country Development to forge partnerships between the Fed and other organizations to study business, housing, and educational issues affecting Native American communities. The Dallas Fed's Colonia project is examining infrastructure, housing, and economic opportunity efforts in the neighborhoods along the U.S.-Mexico border. And the St. Louis Fed's Delta Communities Initiative is working with distressed communities across the Arkansas and Mississippi Delta regions.

There are many other examples, but today I will focus on approaches and programs that are helping to make a difference in regions like eastern Kentucky, regions that are undergoing significant economic transitions. Before I continue, let me note that the views I'll present are my own and not necessarily those of the Federal Reserve System or my colleagues on the Federal Open Market Committee.

Eastern Kentucky in Transition

Eastern Kentucky, comprising 31 counties, has been facing economic challenges for some time. In 1964, President Lyndon Johnson knelt on the front porch of a Martin County family's cabin as part of his administration's "War on Poverty" tour. A photograph of that meeting became an icon in the country's effort to eradicate poverty.[1] As discussed in two recent Cleveland Fed articles, while some progress has been made, the challenges remain substantial.[2] In the 1960s, about 60 percent of families in eastern Kentucky lived below the poverty line. Today that percentage has fallen to around 25 percent, but that is still about twice as high as the national average and 9 percentage points higher than the rest of Kentucky. In fiscal year 2016, the Appalachian Regional Commission has designated 26 of the 31 counties in eastern Kentucky as distressed.[3]

The sources of eastern Kentucky's difficulties are familiar to all of you. Over the past decade or so, eastern Kentucky has lost more than 13,000 jobs; about half of those were jobs in coal mining. The decline in employment has affected the regional economy in a number of ways. Coal miners earn nearly double the average annual income in eastern Kentucky: about $73,000 per year compared to $36,000 per year. So the loss of those jobs has meant a sizable drop in local spending power. In addition, tax revenues derived from the coal industry have fallen sharply as the level of coal production has fallen. For

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[1] The photograph was reproduced in the Cleveland Fed's 2006 Annual Report essay (see Mark Schweitzer and Peter Rupert, "Understanding the Persistence of Poverty") and in a joint report profiling 16 high-poverty communities, including Martin County, Kentucky, issued by the Federal Reserve and the Brookings Institution (see "The Enduring Challenge of Concentrated Poverty in America," A Joint Project of the Community Affairs Offices of the Federal Reserve System and the Metropolitan Policy Program at the Brookings Institution, October 2008).

[2] Matt Klesta documents economic trends in eastern Kentucky in "Eastern Kentucky: A Region in Flux," *Forefront,* Federal Reserve Bank of Cleveland, March 2, 2016, and "Comings and Goings in Eastern Kentucky," *Forefront*, Federal Reserve Bank of Cleveland, August 1, 2016.

[3] See ARC-Designated Distressed Counties, Fiscal Year 2016.

example, the coal severance tax in Kentucky has dropped 40 percent in just the past three years. The weakened economy has exacerbated some social issues in the region. Eastern Kentucky has experienced the pain of the country's opioid epidemic. According to data from the Centers for Disease Control and Prevention, over the period 2000 to 2014, the age-adjusted death rate from drug overdoses more than doubled, with opioids being the main driver of these deaths.[4] According to this sad metric, in 2014, Kentucky's death rate from this cause was the fourth highest among the 50 states.

The economic challenges in eastern Kentucky are also reflected in population trends. While the rest of Kentucky has gained population since 1980, population in eastern Kentucky has been fairly flat and has even begun to decline over the past five years as the coal industry has contracted. Deaths are now outpacing births, and net migration in eastern Kentucky has shifted from an inflow of around 1,300 people a year on average from 1995 to 2011 to an outflow of about 1,100 people a year on average since then.[5]

Factors Supporting Regional Transformation

Eastern Kentucky is not alone in facing economic challenges, many of which arise from the transformation being driven by technological change and globalization. In the Fourth Federal Reserve District, regions that have been dependent on one particular industry like heavy manufacturing or oil have fared less well over time than those that have been able to diversify their industrial bases and adapt to the changing economy. Research and analysis by Federal Reserve staff and others have identified a number of specific factors that support regional economic transitions. The three I will discuss today are: leadership and collaboration, a skilled workforce, and infrastructure.

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[4] See Rose A. Rudd, Noah Aleshire, Jon E. Zibbell, and R. Matthew Gladden, "Increases in Drug and Opioid Overdose Deaths – United States, 2000-2014," *Morbidity and Mortality Weekly Report* 64, pp. 1378-1382 (January 1, 2016).

[5] These are Internal Revenue Service Migration data. See the August 1, 2016 article by Klesta referenced earlier.

Leadership and Collaboration

Effective leadership can make a big difference in how regional economies navigate transitions. The Boston Fed examined small and mid-sized cities that lost manufacturing employment and found that "resurgent cities," meaning those that successfully reinvigorated their economies, exhibited a high degree of leadership and collaboration among key institutions and individuals, including nonprofits, private citizens, corporations, and government.[6] But the researchers also found that to have an effect on economic outcomes, leadership and collaboration must be part of long-lasting campaigns. There are no shortcuts or easy fixes.

Fortunately, we are seeing some encouraging signs of leadership and collaboration in eastern Kentucky. This summit is a great example of a broad cross-section of funders coming together to support economic transitions. The Kentucky Philanthropy Initiative is aligned with the Appalachia Funders Network and the Appalachian Regional Commission, both of which are active partners of the Cleveland Fed, as well as the Richmond and Atlanta Feds, whose Districts encompass parts of central Appalachia. In fact, Federal Reserve staff members participate in four workgroups operated by the Appalachia Funders Network related to health, food systems, strengthening community capacity, and energy and natural resources. Our staff members are actively engaged with our regional partners to aid in data analysis when possible and to foster leadership connections and information sharing.

Leadership and collaboration also affect the success of employers in recruiting newly trained workers into their industries. Cleveland Fed analysts undertook case studies of five sector-based initiatives across the

[6] "Reinvigorating Springfield's Economy: Lessons from Resurgent Cities," Public Policy Discussion Paper No. 09-6, Federal Reserve Bank of Boston, October 1, 2009.

Fourth District.[7] These sectors were health care in western Pennsylvania, information technology (IT) in northeastern Ohio, advanced manufacturing in central Ohio, marine mechanics in northwestern Ohio, and coal mining in eastern Kentucky. Four of these five initiatives provide direct training to workers, while the IT initiative is focused on increasing and enhancing the pipeline of IT talent through deep employer engagement with educational institutions at all levels. The analysts found that successful programs involve employers who are actively and substantively engaged: they provide advice on curricula, directly interact with students, and tend to come from the highest ranks of their organizations so that they are free to speak on behalf of the employers. The case studies also showed that relationships and trust among employers and partners are important drivers of success. Trust is necessary because, in many cases, the employers are competitors; sustained relationships among the many partners are important because they give the initiatives time to evolve and grow.

Many of you are probably familiar with an initiative called Shaping Our Appalachian Region, or SOAR. This effort bears many of the leadership and collaboration qualities that are critical to supporting economic transitions.[8] Since its inception in 2013, SOAR has embarked on building a set of working committees that allow individuals and institutions to join together to steer the course of economic revitalization in the region. The leadership and collaboration displayed by SOAR are straight out of the resurgent cities' playbook: the leaders involved in SOAR recognize that it is in their own best interest to support economic rebirth and that collaboration is essential because the process of economic transition is necessarily complex. By providing an easy-to-access venue for eastern Kentucky's organizations, businesses, civic leaders, and private citizens to come together and plan for a stronger economic future, SOAR also provides the essential foundation to effect change. One concrete example of success is the new associate's degree program in broadband technology at Big Sandy Community and Technical

[7] "Addressing Employment Needs through Sector Partnerships: Case Studies from across the Federal Reserve's Fourth District," Federal Reserve Bank of Cleveland, August 15, 2016.

[8] See http://www.soar-ky.org/ for more information.

College. This is the first such program in Kentucky and only the third in the country. According to the college's president, the program came about in large part because of the coordinated work of SOAR, Kentucky public officials, and One East Kentucky, a nine-county regional organization comprising private businesses and local chambers of commerce.[9]

A Skilled Workforce

One of the areas SOAR is targeting is workforce development, and wisely so. Just as investments in physical capital, such as plants, equipment, and software, can make businesses more productive, so can investments in human capital – educational and training programs – that allow people to become and remain productive members of the modern labor force.

When it comes to the economic well-being of entire regions, many studies have documented the importance of investments in human capital. For example, Cleveland Fed researchers found that over a 75-year period, education levels were consistently one of the most reliable indicators for each state's per capita income growth[10] and that counties with higher levels of high school graduates tend to have lower poverty rates and higher levels of labor force participation.[11] A study by a Philadelphia Fed researcher found that resilient regions, that is, regions that have been able to avoid persistent declines in population over the long run, tend to have a more educated population and a more diverse industry mix.[12]

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[9] See "Board of Regents Approves Broadband Technology Degree Program at BSCTC," Big Sandy News and Events, March 11, 2016. The Kentucky Community and Technical College Board of Regents approved this new program in March 2016. The program will be divided into three tracks: broadband technician, broadband telecommunications equipment installer, and broadband design and applications.

[10] "Altered States: A Perspective on 75 Years of State Income Growth," Federal Reserve Bank of Cleveland 2005 Annual Report.

[11] Mark Schweitzer and Peter Rupert, "Understanding the Persistence of Poverty," Federal Reserve Bank of Cleveland 2006 Annual Report.

[12] Jeffrey Lin, "Regional Resilience," Federal Reserve Bank of Philadelphia Working Paper No. 13-1, December 17, 2012.

The benefits of investing in human capital are also evident at the individual level. For individuals, better education is correlated with lower levels of unemployment and higher wages. For example, at the national level, the current unemployment rate for those with a college degree is 2.5 percent, compared to 5.0 percent for those with a high school diploma, and 6.3 percent for those who didn't graduate from high school. The difference in wages between those with a college degree and those without, the so-called skill premium, has widened substantially over time, more than doubling since the 1970s. And over a lifetime, in present value terms, a college graduate can expect to earn nearly twice as much as a high school graduate.[13]

Most studies have tended to focus on the benefits of a college education because that's where the data are more readily available. But other approaches to workforce development are also needed. Technological change and globalization have been changing the nature of the jobs available in the U.S. Those workers who have been displaced from their current occupations, for example, coal miners and assembly line workers, often need to retrain for the modern economy. Apprenticeships, certificate programs, and on-the-job training can all potentially play an important role in getting people back into productive jobs.

The Registered Apprenticeship program is administered by the Employment and Training Administration's Office of Apprenticeship within the U.S. Department of Labor, in conjunction with State Apprenticeship Agencies. The apprenticeship programs offer structured on-the-job training combined with related technical instruction tailored to industry needs in a variety of occupations, including electricians, plumbers, truck drivers, and child care workers. One study of the program covering 10 states, including Kentucky, found that the program has been highly effective in generating

[13] Kartik Athreya and Janice Eberly, "The College Premium, College Noncompletion, and Human Capital Investment," Federal Reserve Bank of Richmond Working Paper 13-02R, February 2015.

higher incomes for participants in a cost-effective way.[14] In the ninth year after enrollment, the average person who had participated in the program was earning almost $6,000 more in annual salary than similar nonparticipants, and the difference in lifetime earnings amounted to about $98,000. These differences were even greater for those who completed the apprenticeship programs. For Kentucky, data limitations precluded looking at earnings in the ninth year after enrollment, but in the sixth year after enrollment, the average participant in Kentucky was earning over $5,700 more per year than the average nonparticipant. The study also concluded that the estimated social benefits of the program exceeded the social costs.[15] In sum, the study's evidence suggested that effective apprenticeships not only lead to higher earnings, but also help people stay employed longer.

While it is important to help people already in the labor force transition to other occupations in high demand, it is also important to start training people still in school so that they can develop the skills for the jobs of the future and to make sure that those providing that education and training understand what the jobs in demand will be. The Allegheny Conference on Community Development commissioned an in-depth analysis of the supply and demand for labor in the Pittsburgh region over the next decade.[16] The resulting report made a number of recommendations to help prepare employers, current and future workers, educators, and civic leaders for the coming changes. One initiative would create a digital career awareness hub for students and teachers in kindergarten through high school to better match curriculum to

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[14] Mathematica Policy Research, "An Effectiveness Assessment and Cost-Benefit Analysis of Registered Apprenticeship (RA) in 10 States," Final Report July 25, 2012. The 10 states included in the study were Florida, Georgia, Iowa, Kentucky, Maryland, Missouri, New Jersey, Ohio, Pennsylvania, and Texas.

[15] The potential benefits considered included the increased productivity of a worker trained through the program and their reduced use of government support programs, including unemployment insurance, welfare, and food stamps. The costs included the costs of administering the program at the federal and state levels, as well as the costs of community colleges providing supportive technical training. Under a baseline scenario, the study estimated that over the career of an apprentice, the estimated social benefits would exceed the costs by about $124,000. Under more conservative assumptions, the study estimated these net social benefits at about $49,000. See Mathematica Policy Research, 2012.

[16] "Inflection Point: Supply, Demand and the Future of Work in the Pittsburgh Region," report prepared by Burning Glass Technologies and the Council for Adult and Experiential Learning with Allegheny Conference on Community Development, May 2016.

the skill sets in demand in the future. Another would create a digital jobs database to make it easier to match those with particular skills to employers currently needing those skills. A further recommendation is to focus resources on high-growth "opportunity occupations," positions that pay higher than the median wage but don't require a bachelor's degree. This diverse group of occupations includes certain jobs in health care, transportation, and bookkeeping. Research by the Federal Reserve suggests that even in opportunity occupations, employers are demanding higher levels of skills than they did in the past, so aligning skill development with these types of jobs will need to be a priority.[17] And it's important to note that not all the necessary skills are technical ones.

The Cleveland Fed's case studies of sector-based training programs that I mentioned earlier found that even if a jobseeker meets the technical skill requirements for a position, lacking the necessary "soft skills" can be a significant barrier to employment. By their very nature, soft skills, such as the ability to work in teams and effective communication, are difficult to measure, but studies are now examining the role of characteristics like persistence and other personality traits as they relate to labor market outcomes.[18] The ACT WorkKeys test attempts to measure foundational and "soft skills," and Kentucky is using it as a metric to help evaluate whether a community has the infrastructure and workforce sought by employers.

Among Kentucky's most successful retraining efforts is the Hiring Our Miners Everyday, or H.O.M.E., program. Housed within the Eastern Kentucky Concentrated Employment Program , H.O.M.E. is funded by an emergency grant from the U.S. Department of Labor and, as its name implies, helps miners and their families affected by the decline in the coal industry. H.O.M.E. appreciates that displaced miners are far from unskilled; rather they need the opportunity to hone their skills for different industries. For

[17] "Identifying Opportunity Occupations in the Nation's Largest Metropolitan Economies," Federal Reserve Banks of Philadelphia, Cleveland, and Atlanta, September 2015.

[18] Paul Tough discusses some of the research in *How Children Succeed: Grit, Curiosity, and the Hidden Power of Character*, Houghton Mifflin Harcourt: New York, 2012.

example, the H.O.M.E. program puts out-of-work miners through a course to prepare them for work as electrical utility linemen, a job that not only pays well, but also provides much-needed fiber optic lines to rural areas. As a result of this program, eastern Kentucky may be able to keep a share of its skilled workforce in the region, thereby helping the local economy to grow. H.O.M.E. is also an example of community leadership and collaboration in action, as it brings together a wide range of entities and interlocking relationships, from the Kentucky Chamber of Commerce to Hazard Community and Technical College. An important next step will be for the partners to undertake a focused evaluation of the program so that we can all learn which specific strategies work and why they work, and which strategies are less effective and therefore less deserving of continued investment.

Infrastructure

The final factor I'll discuss today that's been found to help in revitalizing distressed communities is investment in infrastructure. In fact, infrastructure is a critical component of economies of all sizes. The Appalachian Development Highway System, started in 1965, is a key piece of eastern Kentucky's infrastructure. This system includes 3,000-plus miles of highways across 13 states and was designed for the express purpose of linking otherwise isolated and distressed areas of Appalachia to the Interstate Highway System. Several studies have documented that economic activity is higher in places connected by the highway.[19]

Of course, in 2016, the regional infrastructure needs of vibrant businesses and households have expanded to include not only the physical highway but also the digital highway. Broadband internet access has become a necessity in our connected world. A recent report issued by Cornell University found that nonmetropolitan counties that have had a high rate of broadband adoption have also experienced higher

[19] Some of these studies are summarized in "Appalachian Development Highway System Economic Analysis Study: Synthesis of Findings to Date," a study prepared for the Appalachian Regional Commission by the Economic Development Research Group, Inc., May 2016.

growth in median household income and lower rates of job loss than similarly situated counties that have had low broadband adoption.[20] A 2013 federal government report on broadband access and adoption found that adoption rates vary by household income levels: fewer than half of households with incomes below $25,000 a year use broadband at home, compared with over 90 percent of households with annual incomes exceeding $100,000.[21] There is also wide disparity in broadband access, especially access to high-speed broadband, between rural and urban areas, putting the growth prospects of rural areas at a disadvantage. Eastern Kentucky stands to benefit from KentuckyWired, a statewide effort to bring broadband access to underserved areas in the state.

I note that the Community Reinvestment Act (CRA) provides a significant opportunity to boost programs like this aimed at closing the digital divide. Recent revisions to the CRA rules recognize that a reliable communications infrastructure, such as broadband internet service, can help to revitalize or stabilize underserved nonmetropolitan, middle-income areas. So depository institutions will now receive credit for investing in this infrastructure for the purposes of meeting the CRA requirement of serving the needs of low- and moderate-income communities.[22]

Conclusion

Let me conclude by noting that the economy has made significant strides in coming back from the Great Recession. The unemployment rates in both the nation and in eastern Kentucky are down about 5 percentage points since their respective peaks during the recession. Accommodative monetary policy has provided important support to the economy on this cyclical journey, helping to promote improving labor

[20] Brian Whitacre, Roberto Gallardo, and Sharon Strover, "Broadband's Contribution to Economic Health in Rural Areas," Issue Number 64, Research and Policy Brief Series, Community and Regional Development Institute, Department of Development Sociology, Cornell University, February 2015.

[21] See "Four Years of Broadband Growth," Office of Science and Technology Policy and the National Economic Council, The White House, Washington, D.C., June 2013.

[22] See page 485111, "Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment; Guidance," *Federal Register*, vol. 81, no. 142, Monday, July 25, 2016, Rules and Regulations.

markets. But we need to recognize that the labor market outcomes for people in eastern Kentucky are below the national average and there continue to be longer-run challenges in regions like eastern Kentucky that are undergoing economic transformation. Technological advances and globalization are changing the nature of available jobs and the skill sets needed to perform those jobs. To raise our shared standard of living and to make us more competitive in the global economy, the U.S. needs to ensure that people can enter and remain productive members of the transforming economy.

You may have heard that, last week, I and several other Federal Reserve System leaders met with representatives from the Center for Popular Democracy's Fed Up Campaign in a public forum held before the Fed's annual symposium in Jackson Hole, Wyoming. It was a productive exchange of views about how to solve some of the labor market challenges still afflicting certain communities and demographic groups. Like the Fed Up Campaign, I believe these are important challenges that the country needs to address, but unlike the Fed Up Campaign, I do not believe that at this point in the business cycle, the current very low level of interest rates is an effective solution to these longer-run issues. But the good news is that the programs I discussed today and many of the other efforts underway can make a real difference to the people and communities in transition. To be sure, these programs are but a small part of the overall strategy needed to support economic transitions. Laying the foundation for sustained economic growth is neither a quick nor an easy task. It involves many different players working together with perseverance. I commend this audience for undertaking this effort. As members of the Kentucky Philanthropy Initiative and related charities, you provide leadership and foster collaboration, key ingredients to the revitalization and resiliency of our regions.

Like the KPI, the Federal Reserve takes seriously its role as a convener. Bringing together people to share their different perspectives and experiences can ultimately lead to more effective economic policies. I have spoken many times about how the diversity of views expressed around the FOMC table helps the Fed make better monetary policy. I believe the same is true for public policies aimed at addressing the challenges faced in community development. KPI performs an invaluable service by pulling together people and groups to support grant making and to promote public-private partnerships targeting the region’s persistent challenges. The Federal Reserve Bank of Cleveland looks forward to our continued collaboration with you in those efforts.