“The Modest Economic Recovery Has Played an Important Part in Slowing Household Formation”

An Interview with Tim Dunne of the Atlanta Fed

The economic struggle of the millennial generation (those born since 1980) has been widely discussed in the media, and its behavior is also of great interest to economists. Tim Dunne, an economist in the research department at the Atlanta Fed who specializes in applied industrial economics and labor economics, has written extensively on household formation in the United States. Dunne recently spoke with EconSouth to discuss this demographic cohort.

EconSouth: What kind of rebound in household formation has there been over the last several years?

Tim Dunne: Unfortunately, the data that are typically used to measure household formation are presenting mixed signals at the moment. Not to be too wonkish here, but the U.S. Census Bureau has several different survey instruments that it uses to estimate the number of households in the United States. The more recent data from the housing and vacancy survey have shown only muted gains, whereas data from the annual supplement of the Census Bureau’s Current Population Survey [CPS] indicate a substantial rise. The observed difference in magnitudes—1.3 million versus 2.5 million from 2011 to 2013—is certainly large enough to influence one’s assessment of the overall strength of household formation over the period in question.

That caveat in order, I’ll focus here on the data from the CPS’s annual supplement. The recent data have been pretty solid. Household formation over the last two years has averaged about 1.25 million, close to the numbers seen prior to the Great Recession. The headship rate—the percent of the adult population identifying themselves as the head of a household—has risen but remains below prerecession levels. The headship rate fell relatively sharply over the Great Recession, accounting for the bulk of the decline in household formation rates. This decline was especially sharp for younger adults, those ages 18 to 34.

ES: Have millennials participated in the recovery in household formation?

Dunne: It’s a mixed picture. There has been some rise in headship rates for individuals 18 to 34 years old, but the headship rate for this age group remains well below the rate seen prior to the Great Recession. We know that much
of the falloff in household formation was the result of a decline in headship rates for the young adult cohort, many of whom ended up living with their parents. Greg Kaplan at the University of Pennsylvania recently published a paper showing that the option to move back in with parents serves as insurance against labor market risks. Indeed, that is still true in the most recent data, as well. The proportion of young adults living with their parents is almost as high as it was at the end of the recession.

It is clear that the modest economic recovery has played an important part in slowing household formation. Andrew Paciorek of the Federal Reserve Board has a very nice research paper on the cyclical nature of household formation that highlights the strong links between labor markets and household formation. Paciorek uses a relatively simple econometric model of the headship rate and then projects it forward using the Congressional Budget Office’s forecast of the unemployment rate through the end of the decade. The key point of the paper is that improvements in labor markets should lead to increases in headship rates and an increase in household formation—and this linkage should hold true for millennials as well.

However, as Paciorek says in his paper, “although data through 2012 suggest that new housing starts and permits have begun to recover, they remain far below their long-run trends.”

**ES:** How have headship and household formation rates evolved in southeastern states over the course of the recession and recovery?

**Dunne:** Admittedly, the statistics generated using the CPS data at a regional level are noisy, but the cyclical patterns in headship rates that we see at the national level are present in the South-East. Headship rates fell sharply during the recession but have made a partial recovery since 2010, supporting a rise in household-formation rates. In short, the region’s recovery in household formation is following the broad contours of the national recovery.

This interview was conducted by Mark Carter, a senior economic analyst in the Atlanta Fed’s research department.