Research @ Citi Podcast Episode 75: The Ripple Effect of AI on the Global Job Market

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Rob Rowe (00:02)

Hi everyone. I'm Rob Rowe, U.S. Regional Director of Research here at Citi. Welcome to our Research @ Citi podcast. My guest today is our Global Chief Economist, Nathan Sheets.

And our discussion today is something that's on everyone's minds, given all the numerous headlines that we've been seeing about the labor force and AI. And obviously, there's a lot of Sturm und Drang in whether AI will be productive for labor or whether it's going to be destructive for labor.

I'd love to preface this by saying that I took a look all the way back, actually, and I'll quote the year: 1957. Because in 1957, a movie came out called *Desk Set* with Spencer Tracy and Katharine Hepburn, in which Spencer Tracy played a person who was introducing a computer into this research organization that Katharine Hepburn was overseeing. And there was this argument in that movie — in 1957 — about whether it was going to eliminate Katharine Hepburn's whole team, in terms of this computer being able to provide research internally to the rest of the firm.

Now, I don't bring that up because we're both in research, but anyway, it started very early on that people have had concerns about this. And in the internet revolution, I also took a look at headlines in the late-90s and saw very similar headlines where it just said it was going to cannibalize a ton of jobs.

There's probably another story to that, which is productivity and whether instead it's going to produce productivity advantages. And I don't want to speak for you, but you've always said to me, “Well, if it was cannibalizing all those jobs, why have we had such extraordinary job growth in the United States over the last, call it, 50 to 70 years now, in terms of the growth of the economy?”

So I want to see if we can put all this in context. I want to know, first of all, what are your views on labor right now? Because it's also been a concern — forget about AI for a second. And it's also been a concern about whether we're seeing a weakness in the labor force, whether that's going to lead to a downturn in certain economies. But globally and within the U.S., maybe we just start off with, What is the state of the labor force? What is the state of employment? And then you can then delve into how AI may influence that over time.

Nathan Sheets (02:40)

Yeah, thanks Rob. A very rich set of issues that you lay out there. And I've got to respond a little bit to your prelude just because it's so thoughtful and provocative.

When I think of big themes for global economic performance over even centuries, maybe the biggest of all is the emergence of new technologies and what that's meant for productivity. And that really has been a feature of the last few hundred years.

But right hand in hand with that ongoing march of productivity has been this reality that people have been worried about their jobs. And you can go back to, say, even the early 1800s when the Luddites were destroying the machines because they were worried that those machines were going to be taking away employment.

And so we've seen these massive waves of innovation and economic transformation over this period. Including mechanization, and automobiles, and the railroad, and the IT revolution, and now AI. In each instance, there's been this tension about, “Well, what does it mean for us, as human beings? What does it mean for employment?”

And the underlying reality is all of those technologies, in the end, have created more jobs than they've destroyed. At the moment, we have more people employed than we've ever had employed before. And 60% of the jobs that we do today didn't even exist in 1940. So I think that is the backdrop here and I think it's important for us to keep that in mind, as you were alluding to.

Now, briefly, labor markets globally remain pretty firm. Wage growth is pretty solid around the world. We're not seeing a lot of loose labor markets in various countries. In the United States, the story is a little more nuanced than that: Over the last, say, year or 18 months, we've seen a meaningful pullback in labor demand, firms a little more nervous to continue to expand their hiring. They had hired a lot of people over the previous few years and didn't need a lot more. I think there's some pressures associated with the tariffs, and pressures on margins from that.

And most recently now, we have this oil shock. And in this environment, labor demand has been soft. We've had this simultaneous labor-supply shock where the Trump administration has slowed immigration dramatically. And at the moment, we may be at a place where net immigration in the United States, the ins vs. the outs, is right at zero.

And so we're at a place where we're seeing very little new job growth. We're also seeing fewer people enter the labor force. And as a result of that, the unemployment rate has maybe moved up a little bit — a few tenths over the last year — but is still at a low level from a historical standpoint.

Rob Rowe (05:52)

And how about entries from universities, etc.? There's always been this discussion about the fact that we have a student population that's graduating. What impact does that have? What kind of pressure does that put on the labor market?

Nathan Sheets (06:05)

Let me make two comments there. First, everything we're hearing anecdotally is that new college grads are struggling to find employment and that it is a tough labor market out there. And I think that's the manifestation of the softness in labor demand. And it may be that that softness is particularly acute for new workers, for junior workers.

And if we step back, I don't think I'm seeing a lot of effects yet of AI on the labor market. But to the extent that we are, I think it's going to be in firms' appetite for junior workers. And the leading example of that is that a lot of work as coders and programmers that was previously being done by new graduates can now be done by AI.

So it is a soft market, and I think that reflects some macro realities. The labor demand is soft. But it may also be that some of our new grads are implicitly competing, maybe for the first time in history, against AI. Maybe this is the leading edge of that reality here that we're going to be seeing and playing through in the labor market during the coming years.

Rob Rowe (07:32)

Nathan, when you look at the impact that AI may be having on the labor force or even on industry, what are some of the metrics that you're looking at? And what's the converse argument that AI will be enhancing the productivity of individuals?

In other words, some people have said anecdotally, “Well, if you had some low-skilled individuals, like a low-skilled programmer, you've now enhanced this programmer and made them a high-skilled programmer, in a sense, because they're working with AI.” So how are you looking at this transformation? And what metrics are you looking at? What does it lead you to believe right now vs. what may happen in the future?

Nathan Sheets (08:16)

To the last part of your question, there is a fair amount of research out there that suggests that at a micro level, AI can operate by reducing returns to experience, and reducing returns to skills, for exactly the reason that you say. That if you have an experienced programmer who, say, has been programming for 20 years, that person has learned a lot of stuff about how to handle various kinds of problems. And then if you have somebody, in contrast, who is relatively inexperienced as a coder, but then you hand them AI, which of those two workers is going to benefit more from the AI? Well, the inexperienced worker is going to benefit more because AI is going to tell the experienced person what he or she already knows.

And so there is an argument that it can close wage gaps and experience gaps and, in that sense, reduce inequality in terms of wages and the labor force. Which is a very interesting thought, in that we're used to new technologies widening the skill gap. It may be that AI operates somewhat differently.

And then briefly, I love your question. What kind of metrics should we be looking at? Some that came to mind as you asked that question: I think the hallmark here, what I really, really want to see, is what's happening to productivity growth in the economy.

Productivity growth is as close a thing there is in economics to a free lunch. It basically means you're able to take the same outputs and make more or make what you were making before, more quickly. And that is the backbone of rising standards of living.

So I want to follow productivity. I want to follow what the implications are for wages. As productivity rises, that means that workers are producing more, and their wages should rise correspondingly. What's happening to the unemployment rate? What's happening to profitability of firms — which should also be rising as a result of this — and ultimately real GDP growth?

Those are some of the metrics that jumped to mind, but first amongst those is definitely the productivity. If we have higher productivity, that means the pie is getting bigger and it should give scope for all of us to eat more, so to speak.

Rob Rowe (10:55)

And on that note, I know that I have a favorite chart that you and the team produced in our Must C piece on AI and Productivity, which we did now, I would say a few months ago. But in that piece, you have a labor-productivity contribution to GDP, and you compare it to the internet revolution. And maybe you could comment on that.

I wish we could show the chart; that particular chart was rather interesting to me in terms of what it's showing. [*Transcriber's note: It's Figure 13 in the report linked above.*]

Nathan Sheets (11:23)

Well, during the Internet Revolution — and I'll define that as roughly 1995 to 2005 — we saw labor productivity in the United States accelerate by about a percentage point. So we had an extra percentage point of productivity, which roughly passes through into similar-size — maybe slightly smaller — increase in real GDP growth.

And when I think about how big AI could be and how AI could influence the macro economy, in many ways the experience with that internet revolution is what I'm using as my template. And I'm convinced that AI could be at least that large. And there are various other ways to come to this conclusion as well, that we could see higher U.S. real GDP growth and productivity growth of a percentage point for a decade.

And if that's the case, then that would mean at the end of the period, the level of GDP is 10% higher than it would be otherwise. That is enormous from a macro standpoint. And candidly, when I look at AI vs. the internet? Internet was important, it was transformative, it was significant. AI, if anything, feels even bigger to me than that.

So I would suggest the internet experience as a reasonable benchmark, but one that's more likely to be too small rather than too large.

Rob Rowe (12:56)

And where are we in that trajectory right now, would you say? Are we actually seeing some change right now?

Nathan Sheets (13:05)

That is the big, big question. To be candid here, the recent productivity data have been a little bit more lively, a little bit perkier than they had been before. I have not interpreted it yet based on the whole picture that I see as reflecting AI. I think it reflects maybe some other technologies and some normalization from the very weak productivity growth after the Global Financial Crisis and before the pandemic.

But we are starting to see better productivity performance. And I would expect that over the next, say, three years, plus or minus a year, we're likely to meaningfully see an imprint from AI and productivity. So, we're not there yet, but the adoption of this is just happening at a very, very rapid pace.

Now, a key to that is getting the necessary investment. And last year, we had $300 billion of AI investment in the United States, but that's got to continue. And Heath Terry, who you mentioned, our AI analyst, it's even got to accelerate to much higher levels. He estimates that over the next five years, the US will need $4.4 trillion of AI investment. So a $900 billion run rate vs. the $300 billion that we're at.

So to get there, it's going to require a lot more financing. That also is a whole interesting set of issues that is a concern and something we're quite focused on as well.

Rob Rowe (14:46)

And is it true that in general, wage growth has been rising or at least rising faster than the pace of inflation? Is that a generalization that I can make?

Nathan Sheets (14:56)

Yes. That in the United States, since the pandemic, wages have typically grown more rapidly than inflation, would suggest that real wages have been flat to rising through that period. And that is a feature of the U.S. experience that is somewhat different than many of the other developed-market economies, where they saw a meaningful adverse hit to real wages during the post-pandemic period. They're recovering now, but real wages have been quite weak.

Rob Rowe (15:34)

And lastly, because there are a lot of headlines saying there could be a lot of job losses: During the internet revolution, was there an experience that at least in some sectors, there was some cannibalization of jobs, or some jobs that went away, vs. jobs that were created?

Nathan Sheets (15:53)

Yes. And that's exactly the balance. We did lose jobs as a result of the IT revolution. How many bookkeepers do we have now, for example? There was a hollowing out of certain types of employment, but it created new kinds of employment as web designers and cybersecurity

And Uber is kind of pulling that bricks-and-mortar taxi into the virtual space. So absolutely, we've seen that. And the tension, in thinking about AI, is how many jobs are going to be destroyed — and we can see them — but it's much harder to imagine what are the new jobs that AI is going to create. And that's where people have always struggled.

Going back to your story about Spencer Tracy and Katharine Hepburn, that computer came, but so did a lot of other new kinds of employment inside the firm. And that's that dynamic economic process of productivity growth and transformation.

Rob Rowe (16:59)

Well, thank you very much, Nathan, for your comments today. Really appreciate the insight. And, well, we're going to be observing this in real time for a while now.

Nathan Sheets (17:09)

Keep us busy.

Rob Rowe (17:12)

Yeah, that's right. Thanks again, Nathan.

Nathan Sheets (17:13)

Pleasure.

Rob Rowe (17:15)

Today's recording was done on April 16. Please join us for our next podcast when we'll have a follow-up update on private-credit markets with Mike Anderson.

Disclaimer (17:24)