



LONG-TERM UNEMPLOYMENT

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Chairman Brady, Vice Chairwoman Klobuchar, and Members of the Committee: thank you for the chance to discuss the current employment situation and how long-term unemployment has affected and will continue to affect economic growth. I appreciate the opportunity to testify today.

We are now a full three years from the labor market trough of the Great Recession. Job creation has been relatively steady but modest since 2011. We averaged about 175,000 new jobs per month in 2011; 183,000 per month in 2012; and 168,000 jobs per month so far this year. While this job growth is welcome, it is far short of what we need to achieve a full labor market recovery. Two significant problems have become evident through this lengthy period of slow job growth. First, there has been an unprecedented disengagement from the labor force with current participation at its lowest level in almost 35 years. This means there are currently 102 million jobless people in the United States, but less than 12 million are still actively looking for work and therefore counted as unemployed. Second, the number of long-term unemployed is at a record high. They currently represent over 4.6 million people, and the long-term unemployment rate (the share of the labor force unemployed for over six months) remains well above historical levels at 3.0 percent.

Comparing the current situation with that of October 2009 helps put the effects of the disengagement from the labor market into perspective. In that October, the unemployment rate was at the recession high of 10.0 percent, and 41.5 percent of the working age population were without jobs. Today, the unemployment rate has fallen to 7.6 percent, but labor force participation has declined so much that the jobless rate remains the same 41.5 percent. By this latter measure, we've made little progress towards a full labor market recovery. I estimate that there are over 5 million people missing from the unemployment rate because of the disengagement from the labor force caused by the Great Recession and slow recovery.

The other significant problem is that we currently have 4.6 million long-term unemployed. Although the long-term unemployment rate of 3.0 percent is down from the record high of 4.3 percent from early 2010, it remains well above the previous record high. Furthermore, two-thirds of these people have been jobless for over a year and might be classified as very long-termed unemployed. Large as these numbers are, they dramatically underestimate

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the long-term jobless problem. The same disengagement from the labor force that has driven down the unemployment rate without reducing joblessness has led to a serious underestimation of the problem. To be counted as long-term unemployed (as opposed to long-term jobless), an individual needs to:

- Have no work whatsoever for at least six months
- Want to work and be nearly instantly available if offered work
- Be actively looking for work. By “actively” looking, I mean that every month this individual must send out a resume, contact an employer directly, engage an employment agency, or engage in some other sort of activity that, by itself, could result in employment. Checking for new job openings on the internet or in the newspaper alone does not qualify as active job search.

This sets a high bar for someone to remain “unemployed” for long enough to be considered as long-term unemployed. In 2007, the average unemployed person who eventually exited the labor force looked unsuccessfully for work for just under nine weeks. In 2011, this had risen to over 21 weeks. That means the average person that left the labor force did so before even being classified as long-term unemployed and almost certainly could eventually be called long-term jobless. Consequently, millions of people have dropped from the labor force over the past five years who perhaps should be counted as long-term unemployed but are not.

We can make a simple calculation to get some idea of the actual number of long-term jobless. Every two years the Bureau of Labor Statistics (BLS) projects the size of the US labor force. BLS first examines the future size and composition of the population as affected by the trends in births, deaths, and immigration. Then it analyzes the trends in labor force participation rates of different age, gender, race, and ethnic groups in a total of 136 separate categories and makes its projections.

In 2007, just prior to the Great Recession, BLS estimated that labor force participation would decline slowly (about 0.1 percent per year), due mainly to the aging of the US population. Using this as an estimate of *what would have happened in the US labor market if the recession had not occurred*, we can calculate the number of people that unexpectedly dropped out of the labor force, presumably due to the recession [see graph 1 below]. If these people had not stopped actively looking for work and dropped out of the labor force, they would be counted as unemployed. It is impossible to know how many have been jobless for over six months, but considering that the average time spent searching before becoming inactive is about 22 weeks, this number could be as high as 5 million. Since there were 5.1 million people counted as long-term unemployed in 2012, the long-term jobless rate could be as much as twice as high as its current 3.0 percent [see graph 2 below].

Over time, the incidence of long-term unemployment has likely been increased because of the aging population in the United States and because of the higher level of labor force participation by women. The former creates higher levels of long-term unemployment because older, longer-tenured workers who are less likely to move in and out of employment are declining as a share of the labor force. Also, during the current recession and its aftermath, the extension of unemployment insurance benefits has likely contributed to the number of long-term jobless. Designed to ameliorate the negative financial impact of unemployment, unemployment insurance makes workers more willing to reject job offers in the hope of receiving a better offer in the future. This delays the movement from unemployment back to employment and raises the number of long-term unemployed. Although the size of the estimated effect varies, virtually every study on the effects of unemployment insurance finds that it has a negative influence on reemployment.

Despite these other influences, the main reason for the current, unprecedented level of long-term joblessness is weak economic growth. Since the end of the recession over three years ago, we have not had sufficiently strong economic growth to strengthen the labor market and trigger the rehiring of the long-term unemployed.

There is a predictable business cycle pattern to long-term unemployment. The number of long-term unemployed rises well after a recession begins and continues to rise well after the official end of a recession. The latter is simply because the process of full labor market recovery requires that GDP grow faster than its long-term trend. After

the 2001 recession, this did not happen until mid-year 2003. The economic expansion between the 2001 and 2007 recessions was too mild and too short to result in a full rehiring of the long-term unemployed from the previous recession. As a result, when the Great Recession began, we already had a historically high long-term unemployment rate for a recession onset. But the primary reason is that the current economic recovery appears to be the weakest in 60 years. The recession officially ended in 2009; economic growth has been weak since then, though consistently positive, and the trend is not encouraging. The recovery began in 2010 with GDP growth of 2.4 percent, but rather than strengthening, it has steadily slowed—with growth falling to 2.0 percent in 2011 and to just 1.7 percent last year. This is too slow to support strong job growth. In fact, this level of slow growth has historically resulted in much slower job growth than we’ve actually seen. Economic growth alone would have predicted just 134,000 jobs per month in 2011 and 120,000 jobs per month in 2012 [see chart 3 below]. This effect can also be seen in the very weak labor productivity growth that we’ve experienced over the past two years.

The challenges for the long-term unemployed and jobless are daunting. Joblessness is costly, particularly for high-tenure workers who have invested time and resources in job-specific knowledge and skills. Studies consistently show that the longer someone is unemployed, the less likely they are to find new work. They may have lost job skills over time, have less connection with informal job networks, or face potential employers more reluctant to hire the long-term jobless. And because those with job skills in shortest supply will be reemployed first, the ranks of the long-term jobless may accumulate those that worked in permanently declining industries and those that have job skills that don’t translate well to new employers or industries.

Even after being reemployed, the permanent lost earnings for the jobless will likely be significant. Studies have shown that it can take as long as 20 years for reemployed workers to catch up on lost earnings, largely due to skill mismatches between the jobs lost and the new jobs created in the economy. These losses occur for workers with different lengths of previous job tenure, in all major industries, and for workers of any age. Recent estimates of the permanent earning losses range from 1.4 years of earnings in good times to 2.8 years during times of high unemployment (above 8 percent). After such an unprecedentedly deep recession and extended period of weak job growth, the job mismatch both now and in the future is likely to be the cause of even larger permanent earnings losses.

While the rate of economic growth affects the labor market, the high level of long-term unemployment also affects economic growth. For example, the Congressional Budget Office routinely estimates “potential” GDP as a measure of what level of national income could be generated if the economy were at full employment. The CBO’s most recent estimate suggests we are still losing about a trillion dollars a year from the effects of the Great Recession, five years after it ended. There is also concern that we will have a permanently higher level of unemployment going forward. Although it is, in my opinion, far too early to have a good idea if this will happen, a permanently higher level of joblessness will result in lower income growth.

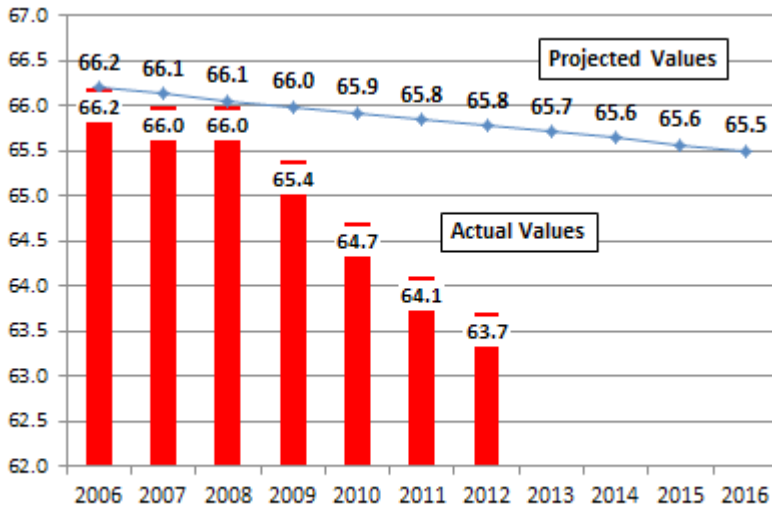
Finally, the number of long-term unemployed also has significant impact on the level of government spending. Estimates place the annual expenditure on means-tested government programs at a trillion dollars a year. More broadly, spending on the whole range of government programs designed to provide for assistance under circumstances of unemployment, poverty, sickness, and retirement has surged in recent years. This spending, called Government Social Benefits to Persons, is estimated every quarter by the Bureau of Economic Analysis. Their data shows that American households now have an unprecedented dependence on these government programs. A remarkable 17.2% of total household income now comes from government social benefits, and such spending tracks pretty closely to the jobless rate (the share of the working age population without employment) [see Graph 4 below].

In closing, the recovery from the effects of the Great Recession on the labor market has been very slow. One of the results of this slow progress has been the unprecedented growth in the number of long-term unemployed and, as bad as this official data appears, it underestimates the problem. There are almost certainly millions of people that are long-term jobless that are not considered unemployed. Although other factors may have contributed to this, the main cause is slow economic growth. The only real solution to this problem is a significant and sustained increase

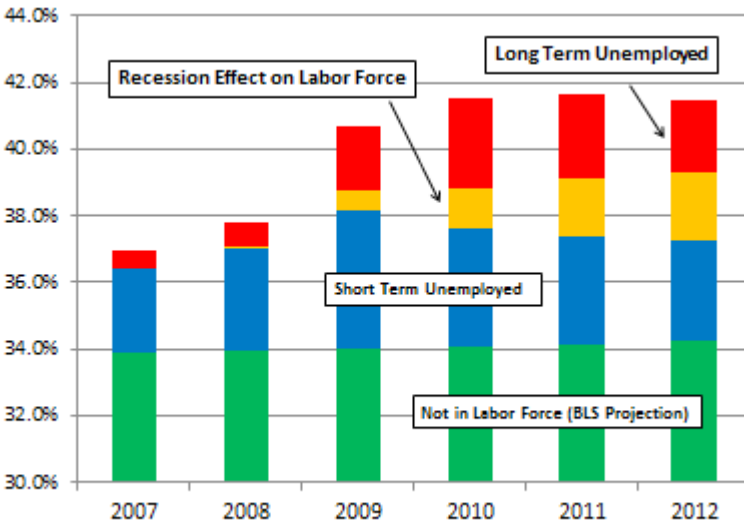
in economic growth. Unfortunately, just as slow economic growth has created long-term joblessness, long-term joblessness is helping to hold back economic growth and has had a significant impact on government spending.

I thank you again for inviting me here today and I would be happy to take any questions.

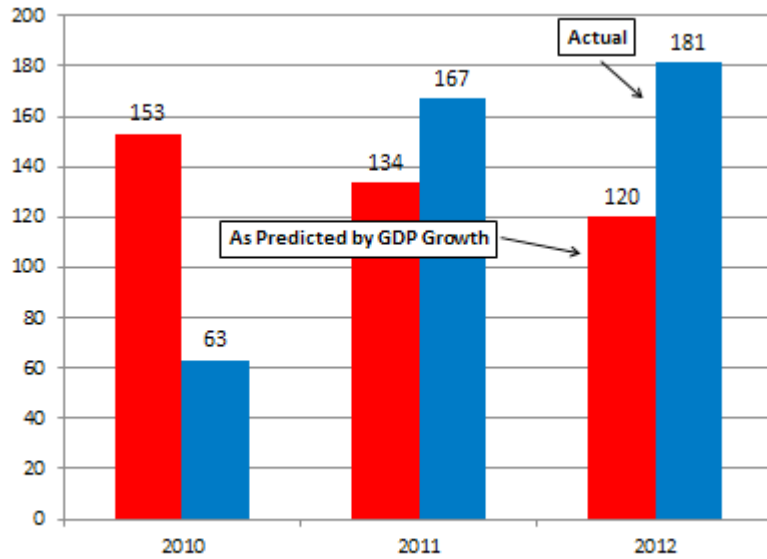
Graph 1: Labor Force Participation: BLS Projections In 2006 versus Actual Values (percent)



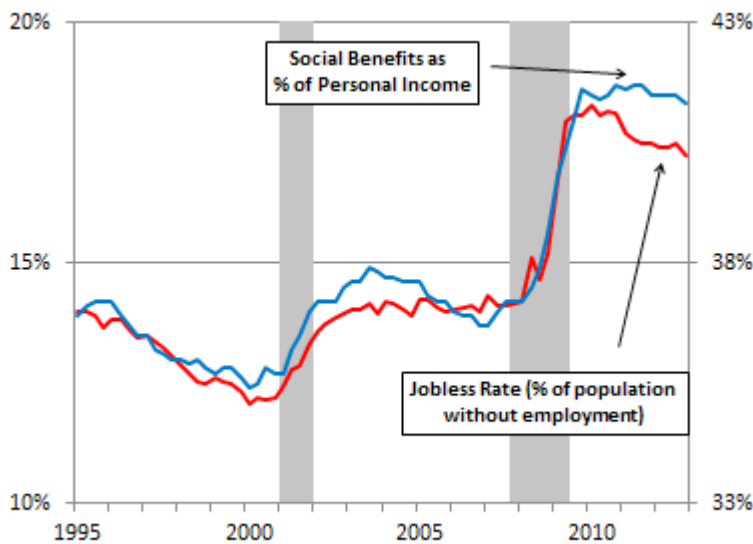
Graph 2: The Jobless Rate (share of population)



Graph 3: Monthly Job Growth. Actual versus Predicted



Graph 4: Spending on Social Benefits



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ABOUT THE AUTHOR

Keith Hall is a senior research fellow at the Mercatus Center at George Mason University. From 2008 until 2012 he served as the thirteenth Commissioner of the Bureau of Labor Statistics. In this role, he headed the principal fact-finding agency in the Federal Government in the broad field of labor economics and statistics. The BLS is an independent national statistical agency that collects, processes, analyzes, and disseminates essential statistical data to the American public, the U.S. Congress, other Federal agencies, State and local governments, business, and labor.