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TRENDMACRO LIVE!

On the February Jobs Report

Friday, March 9, 2012
Donald Luskin

What's improving in the jobs data is what didn't need to improve. The hard tasks remain.

This morning's February Employment Situation Report was about at expectations in most ways. On the surface it continued what has been good about the last several months' reports. By far the most encouraging number was the increase in the size of the civilian labor force by 476,000. For the unemployment rate to have remained unchanged means that all those new entrants are employed.

Improvement in the labor market continues to be cited most frequently by clients as the reason for the near-unanimous sense that "the economy is gaining momentum" or "things seem to be turning around." The jobs picture has certainly improved from the near-stall it experienced over the summer. It's about back to the growth-pace we saw a year ago. That's all to the good, but the fact remains that some of our most trusty macro indicators are flashing caution signs (see "When Bernanke Talks, People Sell" March 1, 2012).

Even focusing just on the improving labor market, we think that enthusiasm ought to be curbed. We are concerned that the most visible signs of improvement are in the one area of it that never needed much improvement to begin with -- and there's not much improvement at all where it is most needed.

Specifically, the best-looking labor market indicator is initial claims for unemployment benefits. The current level of about 350,000 each week is approaching the zone thought to be consistent with a healthy economy.

- But in the Great Recession, initial unemployment was never a great problem. As a percentage of the labor force, claims somewhat exceeded their levels in the prior two recessions, but unusually briefly -- and the peak was nowhere near the levels seen in recessions in the 1970s and the 1980s which were themselves less severe (please see the chart at the top of the following page).

A more comprehensive and sophisticated way of observing the same phenomenon is to look at what labor economists call the "inflow rate to unemployment" (please see the second chart on the following page, and Shimer: 2005). It can be understood as the percentage probability that an

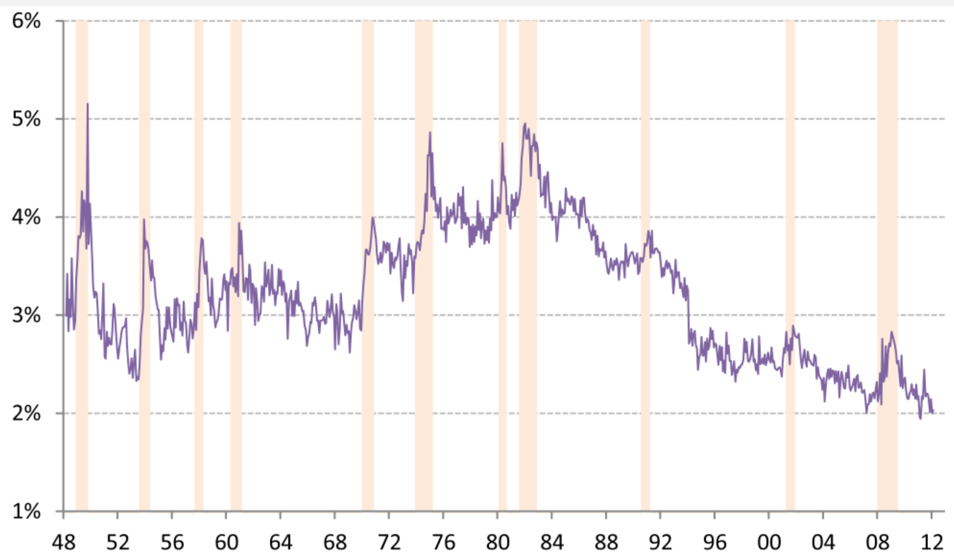
Update to strategic view

US MACRO: Another jobs report showing moderate improvement, with the most positive number being the large increase in the labor force without a corresponding increase in the unemployment rate. But we curb our enthusiasm. The US labor market is still without dynamism. Yes, that's good if it means it's unlikely you will lose your job. But the dark side is that if you do lose your job, you will not be able to get another quickly.

[Strategy Dashboard home]

Initial claims for unemployment benefits, 4-week moving average, as percentage of the civilian labor force

Inflow rate to unemployment: monthly separation probability



Source: BLS, TrendMacro calculations

employed person will become separated from his work for any reason -- fired, laid off, quit, disabled or retired.

- The cycle peak of the inflow rate has been getting smaller in each of the last three recessions, with the Great Recession the smallest of all. For all its extreme hardships, the Great Recession really wasn't about people losing their jobs. In fact, the inflow rate shows that job security was better at the very *worst* of the Great Recession than it was at very *best* of the long expansions of the 1960s and the 1980s.

So why did the unemployment rate go up so much in the Great Recession? It's not because so many people were losing their jobs: *it was*

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Recommended Reading

The Cyclical Behavior of Equilibrium Unemployment and Vacancies
Robert Shimer
The American Economic Review
Vol. 95, No. 1 (Mar., 2005), pp. 25-49

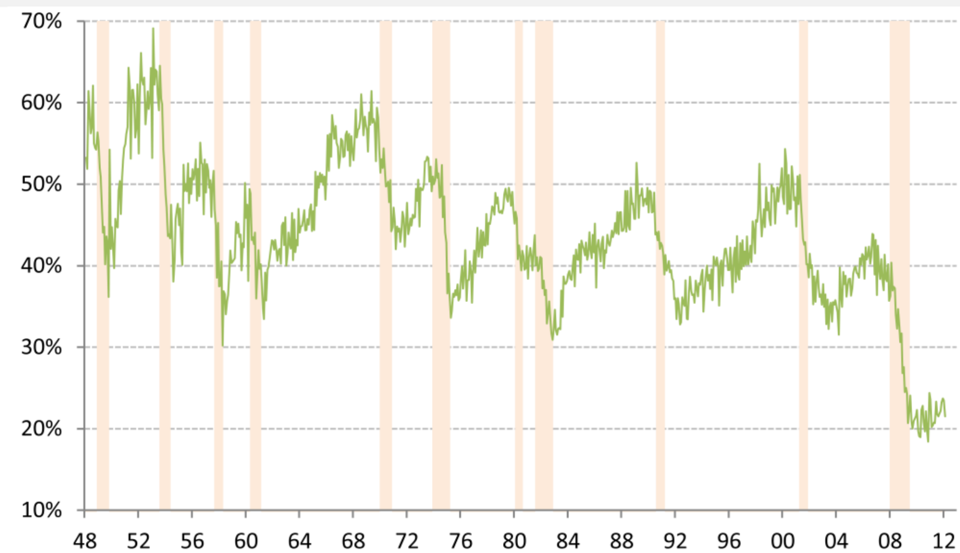
[Reading home]

because it was so hard for those who did to then get a new job, or for new entrants in the labor force to get a first job.

- An often-cited metric that captures this dynamic is the median duration of unemployment -- how long it takes for an unemployed person to get a job, or to give up trying. Here, the experience of the Great Recession is extraordinary, with median duration of unemployment touching 25 weeks at the worst, double the previous peak made after the double-dip recession of the early 1980s (please see the top chart below).

Median duration of unemployment in weeks

Outflow rate from unemployment: monthly job-finding probability



Source: BLS, TrendMacro calculations

This is where we need to see improvement in the labor market -- yet after the pullback from the one-month spike to 25 in June 2010, there's been no improvement here whatsoever.

- A more sophisticated way to capture the same dynamic is the "outflow rate from unemployment," the logical complement of the inflow rate (please see the bottom chart on the previous page, and again Shimer: 2005). This can be understood as the percentage probability of an unemployed person getting a job within a given month. The outflow rate fell precipitously to all-time lows in the Great Recession, and has made almost no improvement at all.
- The outflow rate has been cycling downward over the life of the data. This doesn't mean that it's been getting harder and harder to find work in America for more than half a century. It does mean that it has been getting harder and harder to find work *quickly*. And now more than ever.

Taken altogether, we see the portrait of a labor market in profound stagnation -- people don't leave old jobs, and the few that do don't get new jobs. One often hears that today's America is a place of almost excessive dynamism, where there is no such thing as the stable career that workers enjoyed in the supposedly halcyon days of the 1950s and the 1960s. But that sociological cliché doesn't show in the numbers -- quite the opposite.

- Whatever forces have caused this have apparently been in place for many years. And apparently they have been amplified by the rigors of the Great Recession.
- At the same time, America's labor market stagnation is itself a cause now -- a self-perpetuating one to some extent, perhaps an outright vicious cycle.
- First, when people know that they cannot quickly become employed, they will be content to stay stuck in their current job.
- Second, an economy with a stagnant labor market cannot grow, because human capital can't be deployed and redeployed as firms respond flexibly to new tastes and new technologies. And an economy that cannot grow cannot create new jobs.

These are the reasons why we aren't more encouraged by the supposed improvement in the labor market over the last six months. When we see the outflow rate -- the chance of getting a new job quickly -- show some truly visible improvement, then we'll stop curbing our enthusiasm.

Bottom line

Another jobs report showing moderate improvement, with the most positive number being the large increase in the labor force without a corresponding increase in the unemployment rate. But we curb our enthusiasm. The US labor market is still without dynamism. Yes, that's good if it means it's unlikely you will lose your job. But the dark side is that if you do lose your job, you will not be able to get another quickly.