Executive Memorandum

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Emergency Unemployment Benefits Not Needed as Economy Recovers

Paul Kersey

As the country recovers from a mild recession, Congress is considering a further extension of unemployment benefits. Such an extension is not needed, would be unnecessarily expensive, and could delay employment growth.

Unemployment insurance (UI) offers three tiers of benefits. Regular benefits, lasting 26 weeks, are paid out of state funds. "Extended benefits," which may be triggered by unemployment rates on a state-by-state basis, are paid out of a combination of state and federal money and may be offered to workers for an additional 13 weeks. "Emergency benefits" may be enacted by Congress, further extending the length of benefits available to workers.

- Increasing the length of time that unemployment benefits are available intensifies the incentives for workers to decline employment and for employers to lay off workers, slowing the economic recovery process.
- Benefit extensions may be justified during a recession but are likely to be counterproductive during a period of recovery.

The most recent emergency benefits program, the Temporary Extended Unemployment Compensation (TEUC) program of 2002, was passed partly as a response to the economic fallout from the September 11, 2001, attacks. As the economy recovered from the unusual combination of cyclical recession and the destruction brought about by terrorism, TEUC was allowed to expire in December 2003. The House of Representatives has passed legislation (H.R. 3030) with a new emergency benefit provision, but a review of the economic effects of unemployment insurance and current economic conditions indicates that such benefits are not needed.

Creating Disincentives for Hiring and Employment. Unemployment insurance was designed to provide short-term income stability that allows workers time to look for work while maintaining customary spending patterns, thereby stabilizing the overall economy. But it can also be a disincentive to finding work, an effect that is intensified when recipients are allowed to receive benefits for a longer period of time.

- Because workers continue to receive an income while unemployed, they are likely to demand a higher wage before accepting a new job as long as benefits are available.
- Employers may be more likely to resort to temporary layoffs rather than other cost-cutting measures because UI recipients are less likely to find other employment. Some employers may be using UI to help keep their workforce intact during temporary layoffs.
- Economists have found that the likelihood of a given recipient's finding work (or being recalled

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to his or her prior job) increases significantly in the week before UI benefits run out.

In general, increasing the length of time that UI benefits are available intensifies the incentives for workers to decline employment and for employers to lay off workers, slowing down the process of economic recovery. In spite of these effects, however, emergency benefits might be called for during a recession, when jobs are difficult to find. When jobs are scarce, incentives against taking a job become less relevant, and there would be a strong case for providing economic relief for those who remain unemployed for long periods. Such is currently not the case.

Keeping the Condition of the Economy in Perspective. Compared to prior economic downturns, the U.S. job market was relatively undamaged during the most recent recession. (See Table.)

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Recession	Peak Unemployment
1973–1975	9.0 percent
1980–1982	10.8
1990–1991	7.8
2001	6.3

Of the four recessions the U.S. economy has encountered in the past 35 years, the most recent has produced the least severe unemployment. Since 1973, the lowest monthly unemployment rate the nation has experienced was 3.8 percent in April 2001. Last June's peak unemployment level of 6.3 percent was closer to that astonishingly low level than to the peak unemployment encountered in the mid-1970s or early 1980s.

Given the relatively modest unemployment rate associated with the most recent recession, it should be neither surprising nor disappointing that job gains have been modest. Overall, while certain sectors, especially in manufacturing, have seen significant job losses, they did not eliminate many jobs initially.

Job Market Improving. Nonetheless, job creation has picked up, in large part because of the President's pro-growth economic plan. The Bureau of Labor Statistics payroll survey estimates that the economy created 112,000 jobs in January and 366,000 since August. The total number of U.S. workers is at an all-time high of 138.6 million, and since peaking at 6.3 percent in June, unemployment has steadily decreased to 5.6 percent.

Nor do discouraged workers explain the drop in unemployment. The Bureau of Labor Statistics estimates that only 432,000 Americans—less than 0.3 percent of the workforce—qualify as "discouraged." Moreover, even if discouraged workers were included in unemployment statistics, the unemployment rate would still only be 5.9 percent. With a current unemployment rate of 5.6 percent, the U.S. may in fact be fairly close to full employment.

Conclusion. TEUC cost the federal government roughly $900 million monthly while it was in effect, and a six-month renewal of the program would likely cost over $5 billion. Democratic supporters of the more generous benefit program recently passed by the House estimate that their program would cost $6.7 billion. Extending these benefits at a time when unemployment is steadily declining and jobs are being added to the economy does not bode well for Congress's ability to curtail the growth in federal spending.

Economic indicators suggest that an economic recovery is underway, and that recovery is beginning to affect the job market. In such an economy, with jobs becoming more and more available, emergency unemployment benefits are not needed and might actually slow down the pace at which workers return to their jobs or find new ones. The best course of action for Congress is to let that recovery take its course.

—Paul Kersey is Bradley Visiting Fellow in Labor Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.