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Years of High Unemployment Ahead at Recovery's Pace

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Despite the official end of the recession in June 2009, the labor market remains stagnant. Employment has fallen by nearly 7 million jobs since the recession began. Unemployment remains above 9 percent. This is the weakest recovery of the post–World War II era. Current policies have not stimulated business hiring. If job creation occurs at the same rate as in the 2003–2007 expansion, unemployment will not return to pre-recession levels until 2018. If job creation continues at the low rate of the past year, unemployment will remain permanently high. Congress needs to act to prevent this by removing federal barriers to business investment and success.

Deep Recession, Weak Recovery. The collapse of the housing bubble and the resulting financial crisis plunged the U.S. economy into a deep recession in 2008. Unemployment rose above 10 percent, and employers shed more than 8 million net jobs.

The recession officially ended in June 2009, but payroll employment remains 6.9 million jobs below its December 2007 peak. The average unemployed worker has been without work for 39.7 weeks (nine months)—the longest since the government began keeping track in 1948.[1]

This is the weakest recovery of the post–World War II era. In past recessions, employment fully recovered within two to three years. As of May 2011—three and a half years after the recession's onset—payroll employment remains 5 percent below pre-recession levels. Unemployment stands at 9.1 percent.

How Long Until Unemployment Falls? Some unemployment will always exist in the economy. Even in good economic conditions it takes time for workers to move between expanding and contracting businesses. Economists estimate that the "natural rate of unemployment" in the U.S. economy is 5.2 percent.[2]

The Heritage Foundation used data from the Bureau of Labor Statistics[3] to calculate how long, given certain levels of job creation, it would take unemployment to return to its natural rate.[4] These estimates are not a prediction of how quickly unemployment will fall; instead, they illustrate what different rates of monthly job creation imply about the speed of the labor market recovery.

Even with strong economic growth, it will take time for unemployment to return to normal levels. If employers add an average of 260,000 net jobs per month—the rate the payroll survey showed during the late 1990s tech bubble[5]—then unemployment will not return to its natural rate until August 2014.

If employers add 216,000 net new jobs per month—the rate the household survey showed in

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1997, the year of the greatest job growth in the tech bubble[6]—unemployment will return to its natural rate in October 2015.

Slow Recovery Likely. These are optimistic assumptions. The late 1990s was a period of unusually strong economic growth. During the 2003–2007 expansion, employers added an average of 176,000 jobs per month.[7] If the recovery takes that more recent pace, unemployment will not return to normal rates until January 2018. Matching the rate of job growth in the recovery from the last recession would mean Americans would wait seven years for unemployment to recover.[8]

The Congressional Budget Office (CBO) expects that the recovery will occur at roughly the same pace as the 2003–2007 expansion.[9] The CBO's latest economic forecasts show the economy returning to full employment in 2017. In other words, the CBO expects employers to soon begin hiring at a slightly faster rate than during the best years of the last decade. Even at that pace, unemployment would not return to normal levels until after the 2016 presidential election.

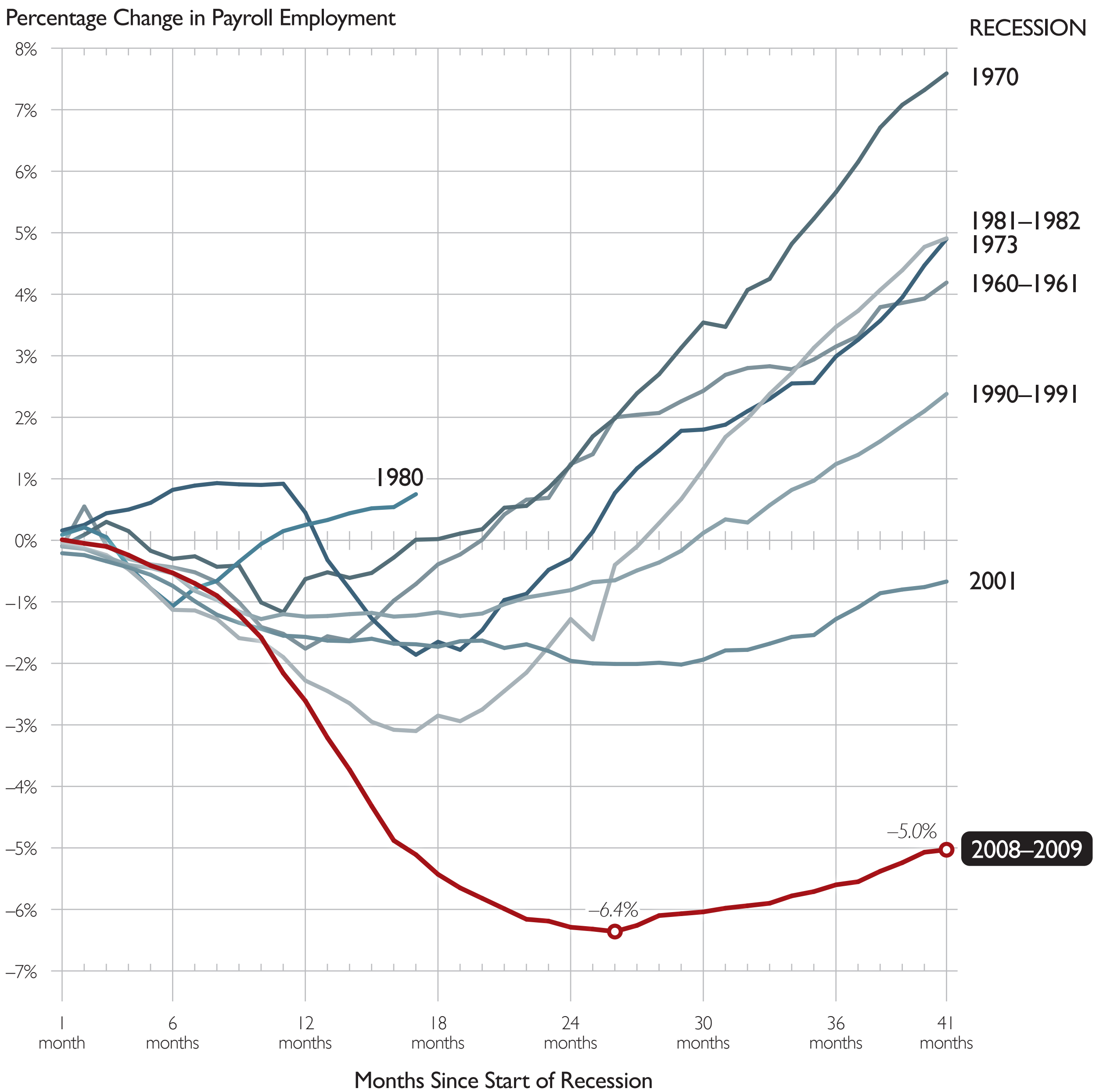
Unfortunately, the recovery has not proceeded even at this pace thus far. Following anemic job growth in 2010, the first quarter of 2011 showed

1. Department of Labor, Bureau of Labor Statistics, "The Employment Situation," December 2007 to May 2011, data collected by Haver Analytics.
2. Congressional Budget Office, "The Budget and Economic Outlook: Fiscal Years 2011 to 2021," p. XII, at *http://www.cbo.gov/ftpdocs/120xx/doc12039/01-26_FY2011Outlook.pdf* (June 28, 2011).
3. The Bureau of Labor Statistics conducts two monthly surveys of the labor market: the household survey and the establishment survey. The household survey is a monthly survey of individuals that includes questions about whether they are working or unemployed, and is the source for information on the unemployment and labor force participation rates. The establishment survey asks businesses how many employees they have on payroll and is the source for the monthly job creation figures reported in the press. The establishment survey has a considerably lower monthly margin of error in estimating total employment than the household survey, but it omits some categories of workers included in the household survey, such as agricultural employees and the self-employed. Over time, they typically report similar—but not identical—results. In the tech boom of the late 1990s, the payroll survey showed greater job creation than that of the household survey. In order to avoid combining the results of two distinct surveys, figures from the household survey were used to calculate future unemployment rates.
4. The employment, unemployment, labor force, and population sizes reported in the May 2011 household survey were taken as the starting point for the economy. The (16 and over) population was inflated at a 1.0 percent annual rate to account for population growth, as projected by the Census Bureau. Total employment in June 2011 and subsequent months was estimated by adding to the previous month's employment the assumed level of monthly job growth. The size of the labor force was estimated by multiplying the labor force participation (LFP) rate by the population projections. Unemployment was calculated as the difference between the size of the labor force and total employment. The unemployment rate was the ratio of the estimated unemployment level to the estimated labor force. LFP rates were derived from the CBO's March 2011 LFP projections. Current LFP rates are below the CBO projections of the LFP rate for 2011. Consequently, the simulations held LFP at 64.2 percent between June 2011 and May 2012 and then decreased by 0.1 points per year until it reached the CBO's estimated rate of 63.9 percent in 2015. Thereafter, the CBO's projected LFP rates were used.
5. This is the average monthly job creation for the payroll survey between 1997 and 1999. These figures are for illustration only. The household survey and payroll survey measure jobs differently. While they show similar trends over time, they measure different universes of employees and are not strictly comparable. All other monthly job creation estimates used the household survey results.
6. The household survey showed average monthly payroll growth of 216,450 jobs in 1997. This figure omits estimated December to January employment changes, which are skewed by updates made to the population estimates.
7. Department of Labor, Bureau of Labor Statistics, Household Survey/Haver Analytics, August 2003 to November 2007. Figures omit December to January employment changes because of the updates to the population controls.
8. This is close to the rate the establishment survey shows for the first quarter of 2011 (+165,000 jobs per month).
9. Congressional Budget Office, "CBO's 2011 Long-Term Budget Outlook," June 2011, p. 25, at *http://cbo.gov/ftpdocs/122xx/doc12212/06-21-Long-Term_Budget_Outlook.pdf* (June 28, 2011).

strong employment gains. This raised hopes that the economy had finally begun a strong recovery. The most recent data suggests these hopes were illusory—hiring stalled and unemployment rose in April and May. The labor market appears stuck in neutral.

Recovery from Current Recession Far Slower than Normal

Payroll employment today is 5 percent lower than it was before the recession began 41 months ago. That places the current economic recovery far below all other recessions dating back to the 1960s.

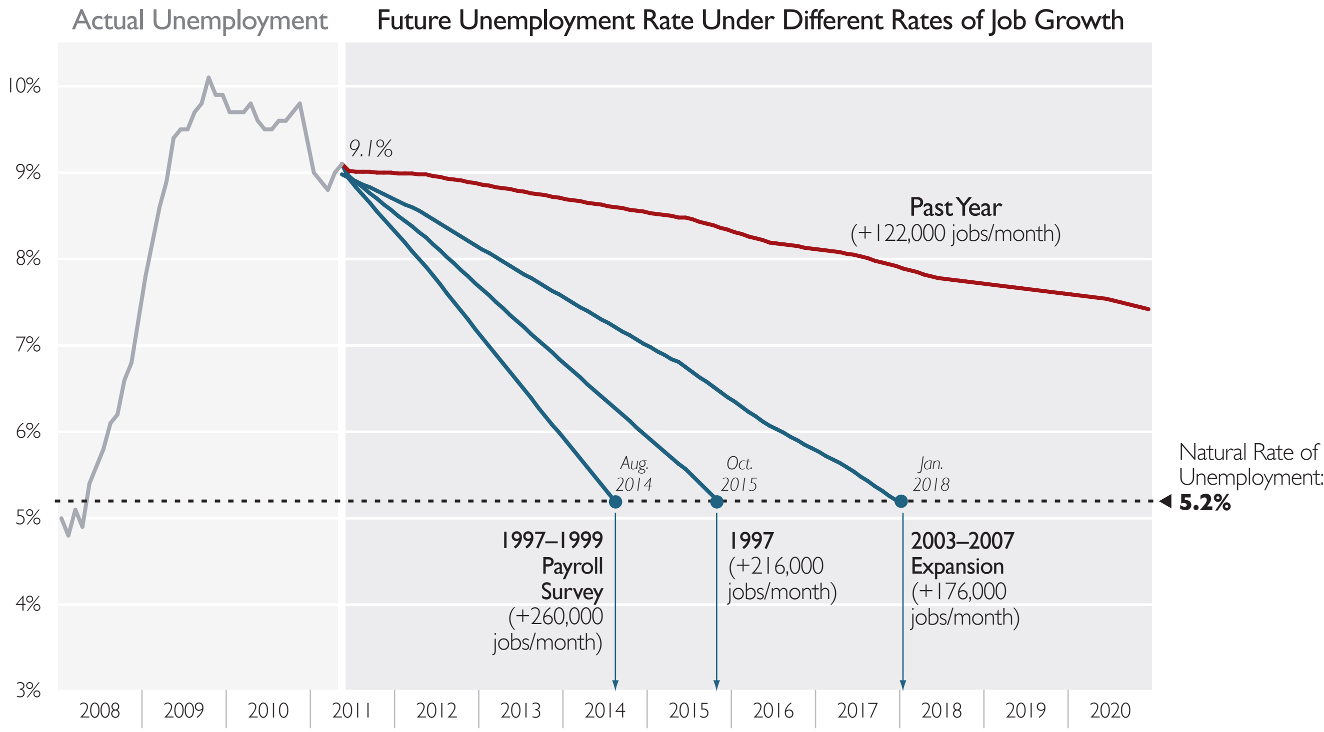


Source: U.S. Department of Labor, Bureau of Labor Statistics/Haver Analytics. Figures are for nonfarm payrolls and exclude temporary census workers.

Chart 1 • WM 3307 heritage.org

Current Job Growth Rate Foretells Lengthy Stagnation

Over the past 12 months, the economy has added an average of 122,000 jobs per month. At that rate, it could take decades to return to the Natural Rate of Unemployment, 5.2 percent. By comparison, if jobs grew at the same rate as they did in 1997–1999, unemployment would reach 5.2 percent sometime between 2014 and early 2016.



Source: Heritage Foundation calculations using data from the U.S. Department of Labor, Bureau of Labor Statistics/Haver Analytics.

Chart 2 • WM 3307 heritage.org

If that is the case, Americans will wait a long time for unemployment to fall. Modest job growth does not necessarily mean lower unemployment. The economy needs to add between 100,000 and 125,000 jobs per month to keep pace with population growth.[10] Unemployment will rise if employers consistently create fewer jobs than this.

Over the past year, employment has grown by an average of just 122,000 jobs per month.[11] If job growth continues at this rate, then the unemployment rate in January 2021 would stand at 7.4 percent. At the current rate of recovery, high unemployment will become the new normal.

Improve the Business Climate. Congress and the Administration should take immediate action to encourage job creation. Successfully doing so requires understanding why employers create jobs. Businesses and entrepreneurs hire workers to take advantage of opportunities to create goods and services consumers value—at a profit. Many govern-

10. The Census Bureau projects that the population 16 and over will grow by 1.0 percent per year over the next decade—roughly 190,000 people per month. A 64 percent labor force participation rate implies a monthly expansion of the labor force of 120,000 workers. To keep unemployment from rising above 9 percent, 110,000 of those workers need to find jobs.
11. Heritage Foundation calculations using data from the Bureau of Labor Statistics, Household Survey/Haver Analytics.

ment interventions in the economy reduce those opportunities. Small businesses currently identify taxes and government regulations as their most important problems.[12]

Congress and the Administration can encourage lasting job creation by creating a better business climate. Removing barriers to business success and reducing unnecessary costs encourages businesses to hire. Such measures include:

- Repealing Obamacare and its associated employer mandates and tax increases;
- Preventing the Environmental Protection Agency from regulating carbon dioxide;
- Passing tort reform to reduce the cost of meritless lawsuits;
- Expanding trade agreements;
- Permitting more domestic energy production; and
- Reducing spending to mitigate the specter of enormous tax increases.

Congress can significantly intervene in the economy and erect barriers to business success—or Congress can remove artificial barriers to entrepreneurship and encourage risk-taking and innovation. Americans do not have to settle for 9 percent unemployment. Lasting economic stagnation is a policy choice.

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12. 36 percent of small business owners identify taxes or government regulations as their single largest problem, while 25 percent identify poor sales. William Dunkelberg and Holly Wade, "NFIB Small Business Economic Trends Survey," National Federation of Independent Business, May 2011, p. 18, at *http://www.nfib.com/Portals/0/PDF/sbet/SBET201105.pdf* (June 28, 2011).