WebMemo

Published by The Heritage Foundation

No. 3336
August 5, 2011

Heritage Employment Report: July Jobs Grow Slightly

Rea S. Hederman, Jr., and James Sherk

The Bureau of Labor Statistics announced this morning that the U.S. economy added 117,000 jobs in July and that the unemployment rate fell from 9.2 to 9.1 percent, due in large part to people leaving the labor force. While the report indicates that the economy is still weak, it is a slight improvement from the previous month's report. Unfortunately, the improvement is mostly confined to the establishment survey, while the household survey remains weak.[1]

The context of this month's jobs report, of course, is the worldwide meltdown of financial markets and staggering economic activity. Not only is today's report a reminder of how weak the U.S. employment market remains—the nation would need twice today's gains to make a dent in the population of the unemployed—but it also challenges Congress to change course in its effort to stimulate the economy. Obviously, massive government spending has done nothing to improve the country's economic prospects. Congress should take today's report and the worldwide crisis to significantly lighten the tax and regulatory burden on businesses and reduce spending, thus allowing firms to expand their activities at much lower costs.

The July Report. The household survey continues to tell a depressing story in the labor market. While the unemployment rate fell from 9.2 to 9.1 percent, the fall is due to 193,000 people exiting the labor force. This lowered the labor force participation rate to 63.9 percent, the lowest level since 1984. This decline is almost entirely due to adult males no longer looking for work. Some of these people no longer in the labor force may be discouraged workers, who have recently increased in number in the past three months even as the official unemployment rate has remained stable.

The average duration of unemployment also hit a new record, surpassing 40 weeks for the first time ever. There was a sharp decrease in the number of newly unemployed, those reporting less being unemployed for less than five weeks. In June there had been a sharp spike in this category, but this number reversed itself in July, indicating that a sharp rise of layoffs is not underway in this report.

The establishment (or payroll) survey had good news besides the addition of 117,000 total jobs. Private-sector job growth was widespread and decent at 154,000 jobs. Many of the lost 23,000 state government jobs are an anomaly from the shutdown in Minnesota. Revisions to previous reports were positive by 56,000 jobs.

Job gains were spread throughout the private sector, with manufacturing (24,000), retail trade (25,900), professional services (34,000), and health care (36,700) experiencing growth. Construction

This paper, in its entirety, can be found at:
http://report.heritage.org/wm3336

Produced by the Center for Data Analysis

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
(202) 546-4400 heritage.org

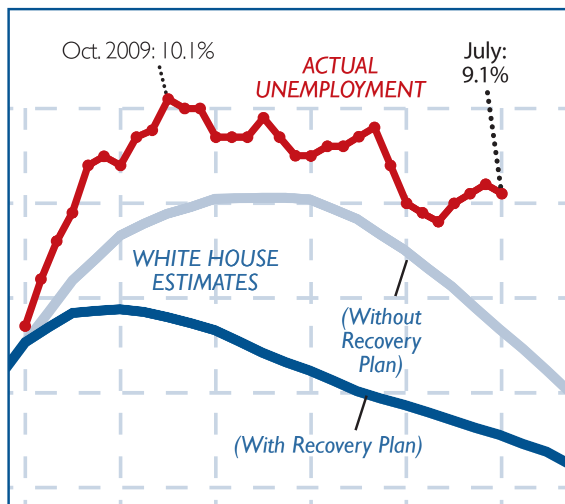
Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

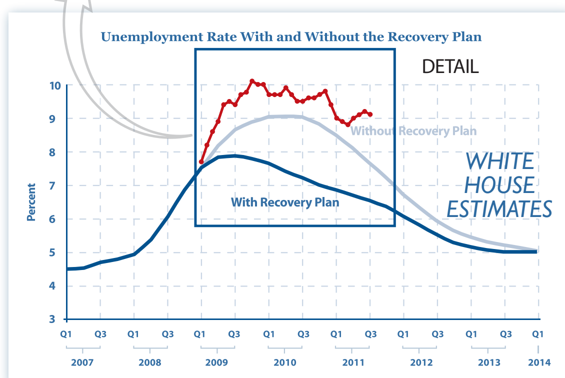
(8,000) and temporary help (300) showed slight growth as well.

There was also a solid recovery in earnings, as they grew by 10 cents, or 0.4 percent, last month.

Unemployment Rate: July 2011

President Obama promised that government spending would "stimulate" the economy and quell rising unemployment by "creating or saving" millions of jobs. In January 2009, Obama's advisers produced a chart (bottom) visualizing the positive results of his recovery plan. But actual unemployment (below, detail from box at bottom) has far exceeded the White House estimates.





Sources: Unemployment data from the Bureau of Labor Statistics; original chart from Christina Romer and Jared Bernstein, "The Job Impact of the American Recovery and Reinvestment Plan," January 10, 2009.

Chart 1 • WM 3336 heritage.org

While average hours remained flat, average weekly earnings were strongly up due to wage growth. This growth in earnings is a good sign given how flat earnings growth was in June.

Overall, the surveys are pointing in two different directions. The household survey is looking at a worsening job market, but the establishment survey is displaying a sluggish but still growing economy. Hopefully, the establishment survey is right and the more volatile household survey will have better data in the near future.

Liberal Fears About Spending Reductions. Many liberal commentators publicly worry that the spending cuts in the debt ceiling deal will hurt the economy. Unfortunately, these commentators are unfamiliar with the economic research in this area.

Many studies, using different methodologies, have looked into the economic effects of deficit cutting measures.[2] They all reach similar conclusions: Deficit-reduction measures that rely on tax increases hurt the economy and often fail, and deficit-reduction measures that focus on spending cuts typically succeed and are much better for the economy. In fact, spending-cut packages are frequently (though not always) associated with *stronger* economic growth.

The research shows that the most effective spending cuts are those in government employment and transfer (i.e., entitlement) programs. Even the study most skeptical that spending cuts can benefit the economy finds greater economic growth following reductions in transfer payments.[3]

One typical study of OECD countries found that after a one-percentage-point increase in taxes as a share of GDP, economic growth falls by 0.9 percent. After a one-percentage-point cut in government spending, economic growth increases by 0.6 percent.[4]

1. The jobs report has two different surveys. The household survey interviews individuals and reports data that is used to determine the unemployment rate. The establishment survey is the larger and usually more reliable survey. It surveys businesses about its payroll and employees. Its data is used to estimate the number of jobs created or lost in each industry as well as hours worked and wages.

The research does not prove that cutting spending improves the economy—economists have not definitely ruled out the possibility that other factors contributed to the higher growth. But it does show that, historically, tax increases are much worse for the economy than spending cuts and that spending less does not typically harm the economy. The evidence does not support the left's warnings.

No New Taxes. The economy is at risk of falling into a second recession, and the deficit remains on an unsustainable path. As it deals with these problems, Congress should learn from the experiences of other countries. Congress should not attempt to cut the deficit by raising taxes. This often fails while significantly harming the economy.

Anti-deficit measures should instead be comprised largely or exclusively of spending reductions—particularly entitlement spending. The Heritage Foundation's fiscal plan, "Saving the American Dream," lays out a framework for Congress to balance the budget by lowering spending and reforming entitlements in ways that assure their survival.[5] History shows that when governments follow such plans, economic growth does not weaken. The government should not do anything to hold the already weak economy back.

Persistent Weakness. The July jobs report underscores persistent weakness in the U.S. economy. The establishment survey is much more optimistic than the household survey, but even the establishment's optimism means that the labor market will not reach full recovery for many years at the current rate unless Congress immediately changes its economic policies.

Congress must not raise taxes, since that will cause a great deal of economic harm. Politicians should ignore the call that we can balance the budget only through tax increases. Instead, policymakers should look at making large entitlement programs more sustainable overall.

*—**Rea S. Hederman, Jr.**, is Assistant Director of and Research Fellow in the Center for Data Analysis, and **James Sherk** is Senior Policy Analyst in Labor Economics in the CDA, at The Heritage Foundation.*

2. Alberto Alesina and Silvia Ardagna, "Large Changes in Fiscal Policy: Taxes versus Spending," *Tax Policy and the Economy*, Vol. 24 (2010); Boris Cournède and Frédéric Gonand, "Restoring Fiscal Sustainability in the Euro Area: Raise Taxes or Curb Spending?," OECD Economics Department Working Papers No. 520 (2006); John McDermott and Robert F. Wescott, "An Empirical Analysis of Fiscal Adjustments," *Staff Papers - International Monetary Fund*, Vol. 43, No. 4 (December 1996), pp. 725–53; Alberto Alesina and Robert Perotti, "Fiscal Expansions and Adjustments in OECD Countries," *Economic Policy*, No. 21 (2005), pp. 207–47; Alberto Alesina, Silvia Ardagna, Roberto Perotti, and Fabio Schiantarelli, "Fiscal Policy, Profits, and Investment," *American Economic Review*, Vol. 92, No. 3 (June 2002), pp. 571–89; Francesco Giavazzi and Marco Pagano, "Can Severe Fiscal Contractions Be Expansionary? Tales of Two Small European Countries," *NBER Macroeconomics Annual*, Vol. 5 (1990), pp. 75–111; Alberto Alesina and Silvia Ardagna, "Tales of Fiscal Adjustment," *Economic Policy*, Vol. 13, No. 27 (October 1998), pp. 487–545; Jürgen von Hagen and Rolf R. Strauch, "Fiscal Consolidations: Quality, Economic Conditions, and Success," *Public Choice*, Vol. 109, No. 3/4 (2001), pp. 327–46; Andrew Biggs, Kevin Hassett, and Matthew Jensen, "A Guide for Deficit Reduction in the United States Based on Historical Consolidations That Worked," AEI Economic Policy Working Paper No. 2010-04 (2010).
3. David Leigh, Pete Devries, Charles Freedman, Jaime Laxton, Douglas Guajardo, and Andrea Pescatori, "Will It Hurt? Macroeconomic Effects of Fiscal Consolidation," *World Economic Outlook: Recovery, Risk, and Rebalancing* (Washington, D.C.: International Monetary Fund, 2010).
4. Ben Broadbent and Kevin Daly, "Limiting the Fall-Out from Fiscal Adjustment," Goldman Sachs, Global Economics Paper No. 195, April 2010.
5. Stuart M. Butler, Alison Acosta Fraser, and William W. Beach, "Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity," Heritage Foundation *Special Report* No. 91, May 10, 2011, at *http://www.heritage.org/research/reports/2011/05/saving-the-american-dream-the-heritage-plan-to-fix-the-debt-cut-spending-and-restore-prosperity*.