

ISSUE BRIEF

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Heritage Jobs Report: Unemployment Drop Is Coal in America's Stocking

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The Bureau of Labor Statistics reported that the unemployment rate fell to 6.7 percent in December from 7.0 percent in November, but the change was caused by people who gave up looking for work. Employers created only 74,000 jobs, a depressing drop from the previous three months. Labor force participation dropped to 62.8 percent, matching the lowest rate since 1978. The sharp slowdown in the labor market occurred despite a better-than-usual retail hiring for the Christmas shopping season.

Congress should focus on removing barriers to growth and entry into the labor market. An unprecedented increase in the legal minimum wage would dampen hiring at the level where most workers first enter the labor market, and the labor market is clearly still far below full employment.

The December Report. The household survey showed that unemployment dropped 0.3 percentage point to 6.7 percent—the lowest unemployment rate in five years. However, the drop occurred almost entirely because of a large drop in labor force participation.

This continues a long-term trend over the year of unemployment falling because of fewer Americans looking for work. The employment-to-population

ratio has not improved over the past year despite a 1.2 percentage point drop in the unemployment rate. Long-term unemployment also persists at historically high rates despite the large decline in the number of unemployed. Almost two-fifths of the unemployed—3.9 million workers—have been out of work for over six months. The proportion of jobless in long-term unemployment has barely improved over the course of the recovery. Most of December's drop in unemployment came from those out of work for less than six months.

A minority of the falling participation has occurred because of demographic changes, particularly the retirement of the baby boomers. However, the employment-to-population ratio of prime-age workers has also stagnated. Between December 2012 and December 2013, the employment rate of 25-to-54-year-olds increased just 0.2 percentage point—as their unemployment rate dropped almost a percentage point.¹ The weak labor market accounts for most of the stagnant employment rates.

The payroll survey report lost its momentum from the past three months. Employers added 74,000 net new jobs in December, far below the average for the past 12 months. Employment grew most in retail trade (+55,000) and professional and retail services (+19,000). Employment fell in construction (-16,000), local government education (-14,900), and motion picture and sound recording (-13,700).

Other measures in the payroll survey were mixed. The average workweek dropped and remains a touch below its December 2012 level, and the average hourly wage rose 3 cents. Wages have grown 2 percent over the past year, exceeding inflation. Another bright spot is that manufacturing overtime hours

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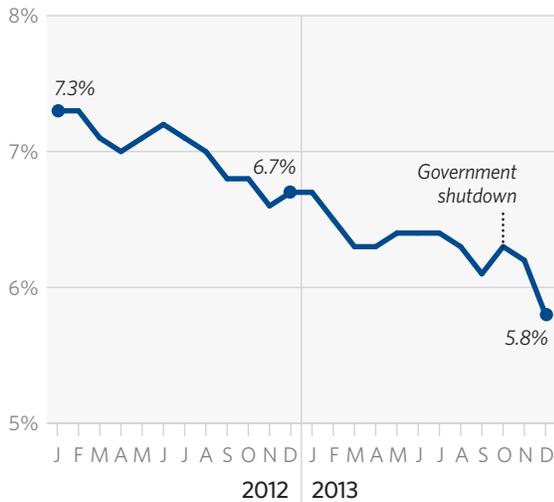
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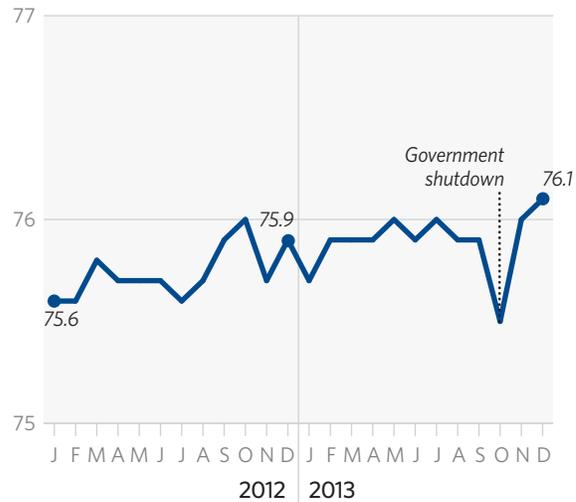
CHART 1

Employment for Prime-Age Workers

UNEMPLOYMENT RATE,
 25-TO-54-YEAR-OLDS



EMPLOYMENT-TO-POPULATION RATIO,
 25-TO-54-YEAR-OLDS



Source: U.S. Department of Labor, Bureau of Labor Statistics, "Labor Force Statistics from the Current Population Survey," at <http://www.bls.gov/cps/> (accessed January 10, 2013).

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have fully recovered, hitting a level last seen in 2006. Revisions added 40,000 jobs to November's survey, tempering the bad news.

Higher Minimum Wage a Barrier to Entry.

President Obama and some Members of Congress have argued that raising the minimum wage would help disadvantaged workers get ahead. But it would have the opposite effect on prospective labor market entrants. Most minimum-wage jobs are entry-level positions primarily filled by young and inexperienced workers.² Minimum-wage jobs teach these workers valuable "soft" employment skills, such as reliability, functioning within a hierarchy, and interacting positively with customers.

Employees need these skills in order to become more productive and qualify for higher paying jobs.

Few employers will pay \$15 per hour to workers who have not demonstrated their reliability. In fact, 55 percent of Americans began their careers making within a dollar of the minimum wage.³

However, once workers gain the skills and experience that make them more productive, they command higher pay. Two-thirds of minimum-wage workers make more than the minimum wage within a year.⁴ They either earn promotions at their existing jobs or accept higher paying jobs at other companies. The median minimum-wage worker whose pay increases sees his or her income rise 24 percent over the year.⁵ Employees who work longer hours and gain experience also see their pay rise more quickly.⁶ With more experience, workers become more productive and earn higher pay.

- Note that the employment-to-population ratio has as its denominator the adult population, while the unemployment rate has as its denominator the labor force, a subset of the adult population.
- See James Sherk, "Who Earns the Minimum Wage? Suburban Teenagers, Not Single Parents," Heritage Foundation *Issue Brief* No. 3866, February 28, 2013, <http://www.heritage.org/research/reports/2013/02/who-earns-the-minimum-wage-suburban-teenagers-not-single-parents>.
- William Carrington and Bruce Fallick, "Do Some Workers Have Minimum Wage Careers?," *Monthly Labor Review*, May 2001, <http://www.bls.gov/opub/mlr/2001/05/art2full.pdf> (accessed January 10, 2014).
- Jonathan Meer and Jeremy West, "Effects of the Minimum Wage on Employment Dynamics," National Bureau of Economic Research *Working Paper* No. 19262, August 2013 (revised December 2013), p. 8, http://econweb.tamu.edu/jmeer/Meer_West_Minimum_Wage.pdf (accessed January 10, 2014); and David Macpherson and William Even, "Wage Growth Among Minimum Wage Workers," Employment Policies Institute, June 2004, pp. 3 and 5, Table 1, http://www.epionline.org/studies/macpherson_06-2004.pdf (accessed January 10, 2014).
- Meer and West, "Effects of the Minimum Wage on Employment Dynamics," p. 8.
- Macpherson and Even, p. 8, Table 4.

Employers will not pay their workers more than the value they produce. Businesses respond to minimum-wage increases by reducing hiring—they will not bring on board inexperienced workers with productivity below the new minimum. In time, this reduced hiring substantially reduces total employment. Over a five-year period, a 10 percent increase in the minimum wage reduces total employment by 1.2 percent.⁷

Minimum-wage hikes make it harder for unskilled and inexperienced workers to get started in the job market. They cut off the bottom rung of these workers' career ladders. Despite proponents' good intentions, minimum-wage increases would further reduce the employment of unskilled workers.

A Bad Time for Bad Policy. The Bureau of Labor Statistics reported an unexpectedly weak labor market in December. The payroll survey reported net job growth falling 70 percent from November. Unem-

ployment dropped in the household survey—but only because a half million Americans stopped looking for work. Over the past year, the employment rate of adult Americans has not improved.

This is a particularly bad time for Congress to raise the minimum wage. Minimum-wage jobs are entry-level positions that teach inexperienced workers basic employment skills that qualify them for higher paying positions. The vast majority of minimum-wage workers either earn raises or switch to higher paying jobs within a year. Raising the minimum wage would cause employers to create fewer entry-level jobs, making it far harder for inexperienced workers to get started in the labor market.

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7. Studies looking for effects only in short-term employment levels contain serious statistical biases. See Meer and West, "Effects of the Minimum Wage on Employment Dynamics," pp. 19-20; and Isaac Sorkin, "Are There Long-Run Effects of the Minimum Wage?," unpublished working paper, October 7, 2013, <https://sites.google.com/site/isaacsorkin/papers/minwagesorkin.pdf> (accessed January 10, 2014).