A Healthy Labor Market Still Includes Many Puzzles

Atlanta Fed economists examine which recessionary changes are cyclical and which are more permanent. Good news: Labor force participation has surprisingly risen. Less good news: The abundance of involuntarily part-timers seems here to stay.

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Several years removed from the worst economic slump in nearly a century, economists continue to puzzle over the state of the U.S. labor market.

This much is certain: the Great Recession changed the jobs market profoundly. Of course, additional forces are at work, including technology, globalization, and demographics.

A key question that economists at the Atlanta Fed and elsewhere are untangling is which labor market changes are temporary and which are lasting. In economic parlance, what recent changes are cyclical, or subject to return to past patterns based on traditional economic cycles? And which conditions are structural and thus likely beyond the reach of Federal Reserve monetary policy?

Job market doing well, all in all

It's important to note that, broadly speaking, U.S. labor markets are performing well, explains the Atlanta Fed's top economist, executive vice president, and research director Dave Altig. The nation continues to add about double the number of jobs each month needed to keep the unemployment rate from rising. To be sure, the 12-month running average in monthly payroll employment growth has slowed a bit lately, to about 160,000 from 200,000-plus.

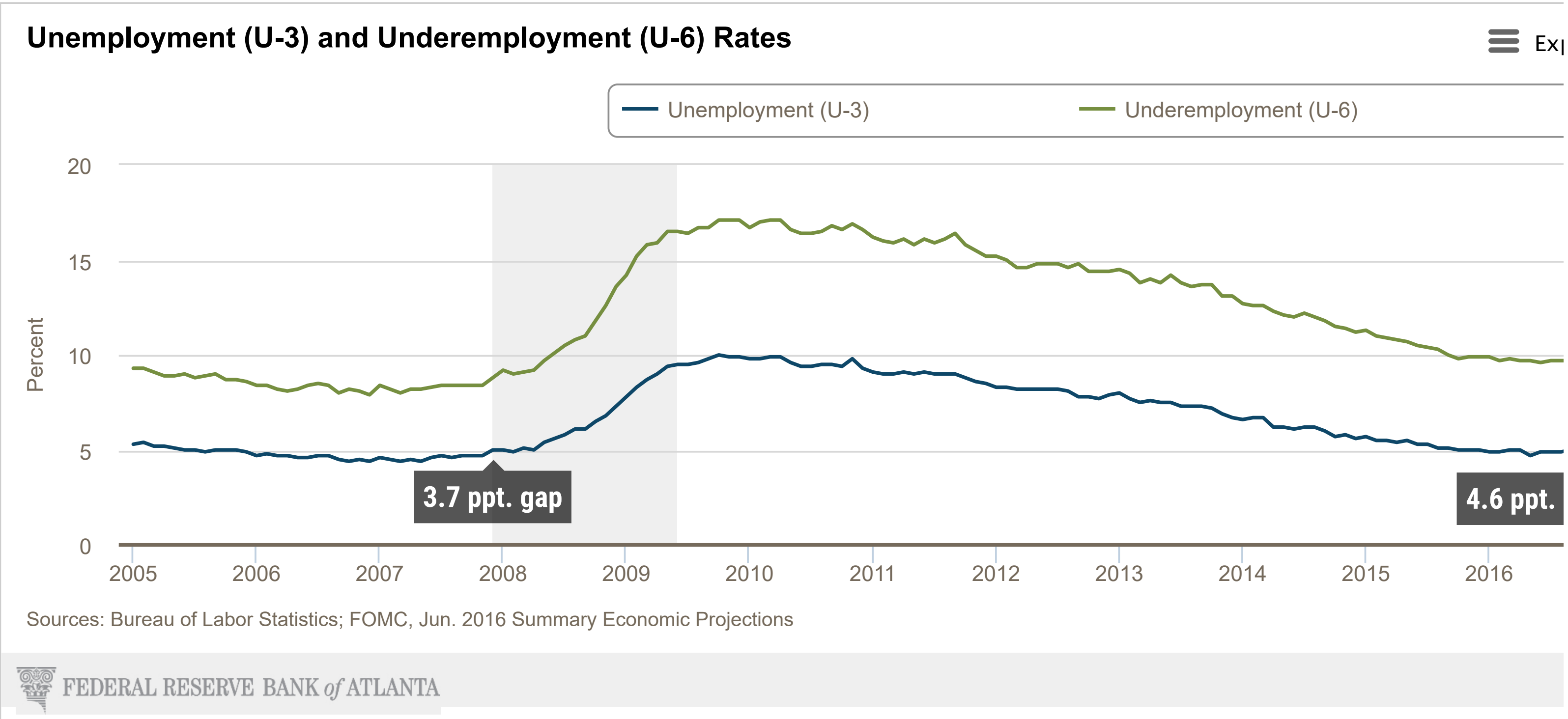

Dave Altig

But that slowing job growth, Altig says, is consistent with a tightening labor market—as employers fill jobs, they don't need quite as may new workers. Bottom line, Altig concludes: "Labor markets in the United States are performing quite well."

Yet nettlesome questions remain.

At the heart of those questions lies an ongoing gap between two different measures of unemployment. That might sound technical, but it's reasonably straightforward and explains a lot about the state of the labor market and thus the economy.

The Great Recession's labor market upheaval heightened attention paid to the U-6 unemployment rate, which includes not only people who are jobless but also those working part-time who'd prefer full-time work. In particular, the gap between the U-6 rate and the more familiar U-3 reading widened significantly during the recession. Before the downturn, the difference in the rates was 3.7 percentage points. That gap grew to more than 7 percentage points during the recession. The space has narrowed during the recovery but has remained wider than it was before the downturn, and now sits at 4.6 percentage points, Altig points out (see the chart).



Atlanta Fed economists have plumbed the data and concluded that a large number of people working part-time involuntarily explains most of t gap between the U-6 and U-3 unemployment rates. Further, research is tending toward an answer that the difference between U-6 and U-3 m not return to prerecession levels. In other words, it is looking like this is a structural, rather than cyclical issue, Altig says.

A key argument for the structural answer is that even as the jobs market has strengthened, it has become less likely that part-timers will move into full-time jobs, Altig says, citing data from the U.S. Bureau of Labor Statistics (BLS).

In fact, the probability of a worker moving from part-time to full-time work within 12 months fell to about 24 percent over the past 12 months, according to BLS data and calculations by Peter Diamond of the Massachusetts Institute of Technology. Right after the recession, in 2009, the likelihood of moving from part-time to full-time work within a year's time stood at about 29 percent.

The reasons why the part-time to full-time move has gotten tougher are not fully understood. But cyclical factors do not appear to be the main explanation.

One popular theory, Altig says, is that the Affordable Care Act (ACA) has discouraged employers from giving people full-time hours because t don't want to fund health insurance, as the law would require. The data, however, do not support that idea, says Altig. He and other economis studied the impact of the health care plan in Massachusetts, which is similar to the ACA. In that state, Altig notes, there was a modest effect o employment that took years to show up.

"This smells like a structural problem," Altig says. This suggests that no matter the cyclical strength of the economy, the number of part-time workers who want full-time work could remain higher than was once customary.

Labor force participation rate surprisingly picks up

A higher number of part-time workers desiring full-time work might sound like bad news. But as is often the case in labor economics, it's complicated. Other signals seem pointed in a different direction. For example, labor force participation (LFP), a key measure of labor market health that had been declining since roughly the turn of the 21st century, has surprisingly ticked upward in the past year. (People are consider part of the labor force if they are working or have looked for work in the past four weeks.)

As Altig describes, change in the LFP rate is the difference between those leaving the labor force and those joining it. During the recovery fro the Great Recession, the numbers of people leaving the labor force received considerable attention. But the outflow is slowing. In particular, t out of work 27 weeks or more are no longer leaving the labor force in big numbers, according to BLS data and Atlanta Fed research.

It's not clear exactly why they are staying. It is not to draw unemployment insurance benefits; the long-term unemployed have exhausted their payments. "Maybe it's optimism that is not manifesting itself in pulling people off the sidelines," Altig says, "but in keeping people from going to the sidelines."

LFP is an important vital sign for various reasons. As Altig indicates, it is a clue about the attitudes of workers and potential workers. It is also critical because a severe drop in participation can threaten the nation's long-term economic prospects.

Already, a couple of powerful forces are decreasing participation among specific demographic groups. An aging population naturally lowers LF as people retire. Between 2010 and 2030, the number of Americans over 65 will nearly double to 74 million, according to the U.S. Census Bureau. The aging of the population has broad implications for the nation's economy and labor market.

Yet aging is a natural phenomenon. What is less inevitable is the long-term decline in LFP among prime-age men, those between 25 and 54. gradual decline has lasted since the 1950s, so long that perhaps it could be considered natural after all.

Poor health appears to be a major reason why so many men are not working or even seeking work, Altig explains. About 43 percent of prime-men who are out of the labor force describe their health as poor or fair, compared to just 12 percent of employed men and 16 percent of those unemployed but in the labor force, according to research that Princeton University economist Alan Krueger presented in October at a Federal Reserve Bank of Boston conference. Indeed, Krueger concludes that about half of prime-age men who are not in the labor force may have a serious health condition.

On a brighter note, Atlanta Fed senior policy adviser John Robertson has noted that the incidence of self-reported nonparticipation among pri age men because of poor health or disability has declined recently. "We've yet to see how much longer this turnaround could continue, but it's encouraging development," Robertson wrote in a July 29 *macroblog* post.

These unhealthy men sitting out the labor market appear to be a gloomy lot. They report "notably low levels of emotional well-being throughou their days, and low satisfaction," Krueger writes.

By contrast, a lot of 20-something labor force dropouts seem content. That cohort is generally either in school or spending more time playing video and computer games, Krueger reports, citing BLS data. In BLS surveys, these men tend to report high levels of satisfaction.

"Those guys are ecstatic," Altig says.

Of course, a lifestyle of whiling away the days with a joystick as mom and dad pay the bills is fleeting. The larger point is that this slice of the population is yet another component of the generally healthy but varied and often vexing post–Great Recession labor market.

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