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Economic Research
Global Data Watch
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Economic Research Note

Jumping off of the 'rising NAIRU' bandwagon

- **A popular argument claims high unemployment is currently the result of structural factors**
- **A closer inspection of the data does not lend much support to this argument**
- **The job market is functioning fairly well, what is missing is labor demand**

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Is high unemployment the result of weak demand or of structural changes in the economy? We first began noting evidence as early as December, 2008 that the data were hinting that structural unemployment could be moving up. Since then, this view has gained increasing popularity. Meanwhile, with the benefit of more data we have actually found the story somewhat *less* convincing. There may have been some move up in structural unemployment, but the overwhelming share of the current unemployment problem is cyclical.

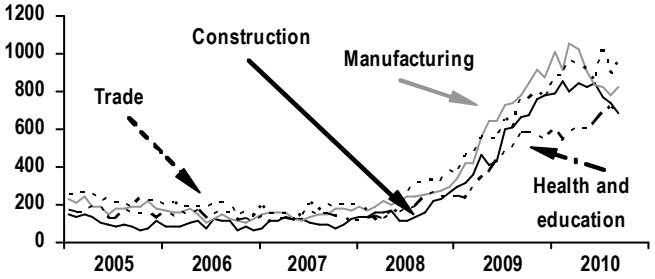
Mismatch misfires

There are three prominent arguments for a significant rise in structural unemployment: skill mismatch, geographical immobility, and increased unemployment compensation. The mismatch story says the problem is that the skills the unemployed possess are not the ones that are sought by the industries that are hiring. Special attention here is usually given to the construction industry, the thinking being that the economy may never need as many constuction workers as we did during the boom years, and so their skills will be structurally mismatched with the skills actually needed by business.

If this skill mismatch view were correct, then one would expect to see that while certain industries like construction are wallowing, there are other industries where workers are in short supply. The data do not bear this out. Among those unemployed 26 weeks or longer—that is, those most likely to be considered structurally unemployed—there has indeed been a large surge in unemployed construction workers. However, starting from about the same point, there has been an even larger increase in the number of chronically unemployed in manufacturing, the trade industries, and most surprising of all, in health and education.

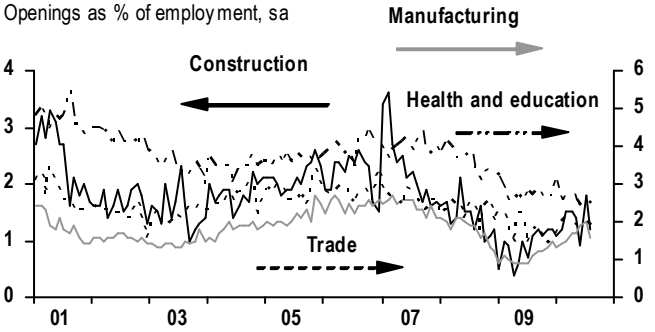
Long term unemployed

thousands, sa, unemployed 27 weeks or more



Job openings rate by industry

Openings as % of employment, sa



In the Job Opening and Labor Turnover Survey (JOLTS) there is also litle evidence that some industries are starving for workers: in every industry tracked in the survey, the job openings rate is lower than it was at the end of the last expansion. (More formally, in the first fourteen months of this expansion, the first principal component of job openings by industry explains 59% of the variance. Over the same period in the last expansion, the first principal component explained only 38% of the variance. The implication is that labor demand across industries in this expansion is more driven by the common, cyclical factor, rather than by sectoral, idiosyncratic factors—a conclusion at odds with the mismatch story.) In short, when looking at either job openings or unemployment, there is little evidence that some industries are doing well and others doing poorly, but considerable evidence that almost all industries still have quite weak labor demand.

Mobility and job matching

Another possible reason for a higher structural rate of unemployment is that negative equity in housing may be preventing households from moving in search of jobs. If this were a significant impediment to the normal matching of jobs and workers, then one would expect to see a drop-off in the number of people moving for work-related reasons. In the Census Bureau's detailed data on internal migration

there is indeed a decline in work-related moving. In 2009, a total of 6.7 million people, who were in families headed by someone who relocated for work-related reasons, moved, a decline of 1.4 million from the peak in such moves in 2007. This would seem to suggest a fairly considerable lift to unemployment from immobility.

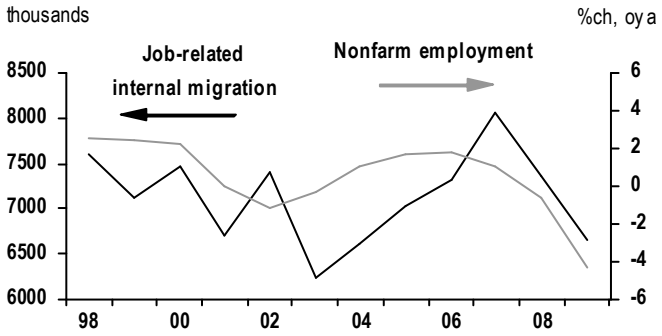
However, there are several reasons why this dramatically overstates the impact of negative housing equity on the unemployment rate. First, while 2007 was the peak of such moves, 2009 was not the trough. In the history of the data, which goes back to 1998, the amount of work-related moving in 2009 was far from the bottom and actually fairly close to average. Given the short history of the data, its hard to say anything too definitive, but work-related moving has been procyclical, increasing when the labor market is strong and slowing when its weak. Given this, its not surprising that such moves peaked in 2007 and bottomed in 2009.

A second and perhaps more important reason why the lift to unemployment from immobility is much less than 1.4 million is that this figure captures the total number of persons, many of whom are children, in families that moved for work-related reasons. The change in the number of heads of households who moved for work-related reasons declined by much less—about 200,000. Even if all of that decline were due to negative equity, that would have a relatively small effect on the unemployment rate. One reason that there is so little evidence of negative equity-related labor maket immobility may be "jingle mail:" households with underwater mortgages that have job opportunities elsewhere may simply be mailing the keys to the bank.

Unemployment compensation

A third reason often given for the rise in structural unemployment is the increased availability of unemployment benefits. Emergency unemployment compensation is almost always enacted by Congress during recessions, and this time has been no different in that regard. What has been different has been the length of those benefits, in some cases making unemployment benefits available for up to 99 weeks. Increased unemployment benefits may increase measured unemployment both by giving jobseekers an outside option and by encouraging people who would otherwise drop out of the labor force to report themselves as jobseekers. The mangitude of this effect on lifting the unemployment rate is disputed by analysts, with estimates ranging from 0.4%-pt (San Francisco Fed) to 1.8%-pt (Brookings Institute). If we take a central estimate as a 1%-point lift to the unemployment rate, that would not be an inconsequential effect. Whether that effect is "structural" is

Job-related moving



Beveridge curve 2000-2010

another matter. While emergency benefits have been made available in every lengthy recession, they have just as regularly expired sometime after the recession. That is likely to happen again—perhaps as soon as the end of this November—and so this "structural" lift to unemployment will likely prove temporary.

A Beveridge on ice

Our analysis has looked at particular arguments behind the view that strucural unemployment is higher and has found them not very convincing. Another argument for a higher structural unemployment rate comes from looking at the Beveridge curve—the relation between the unemployment rate and the job vacancy rate. An outward shift in that curve has usually been thought to represent a deterioration in job matching efficiency, i.e., an increase in strucutral unemployment. The Beveridge curve has indeed shifted outward, and recent research from the Federal Reserve concludes this has pointed to a loss in matching efficiency that has contributed 1-1/2%-pts to the unemployment rate. However, this same research has documented that matching efficiency normally declines after severe recessions. In short, it appears a more nuanced look at the Beveridge curve comports with our findings from looking at the differing explanantions for higher structural unemployment: the vast majority of the increase in unemployment is due to cyclical, not structural, factors.