

Unemployment and Inflation

Prepared by:

Fernando & Yvonn Quijano

Alcatel-Lucent Contributes to Unemployment



When total employment in the United States declined during 2001, Lucent contributed to the decline.

Learning Objectives

- 8.1 Define **unemployment rate** and **labor force participation rate** and understand how they are computed.
- 8.2 Identify the three **types** of **unemployment**.
- 8.3 Explain what **factors determine** the **unemployment rate**.
- 8.4 Define **price level** and **inflation rate** and understand how they are computed.
- 8.5 Use **price indexes** to adjust for the effects of inflation.
- 8.6 Distinguish between the **nominal interest rate** and the **real interest rate**.
- 8.7 Discuss the **problems** that **inflation** causes.

Recap:

In previous lecture:

1. Unemployment rate= # of Unemployed/Labor Force
2. Labor Force= Employed+Unemployed
3. Not in labor force
4. Household Survey, Payroll Survey, by US dep. Of Labor
5. Trend of employment

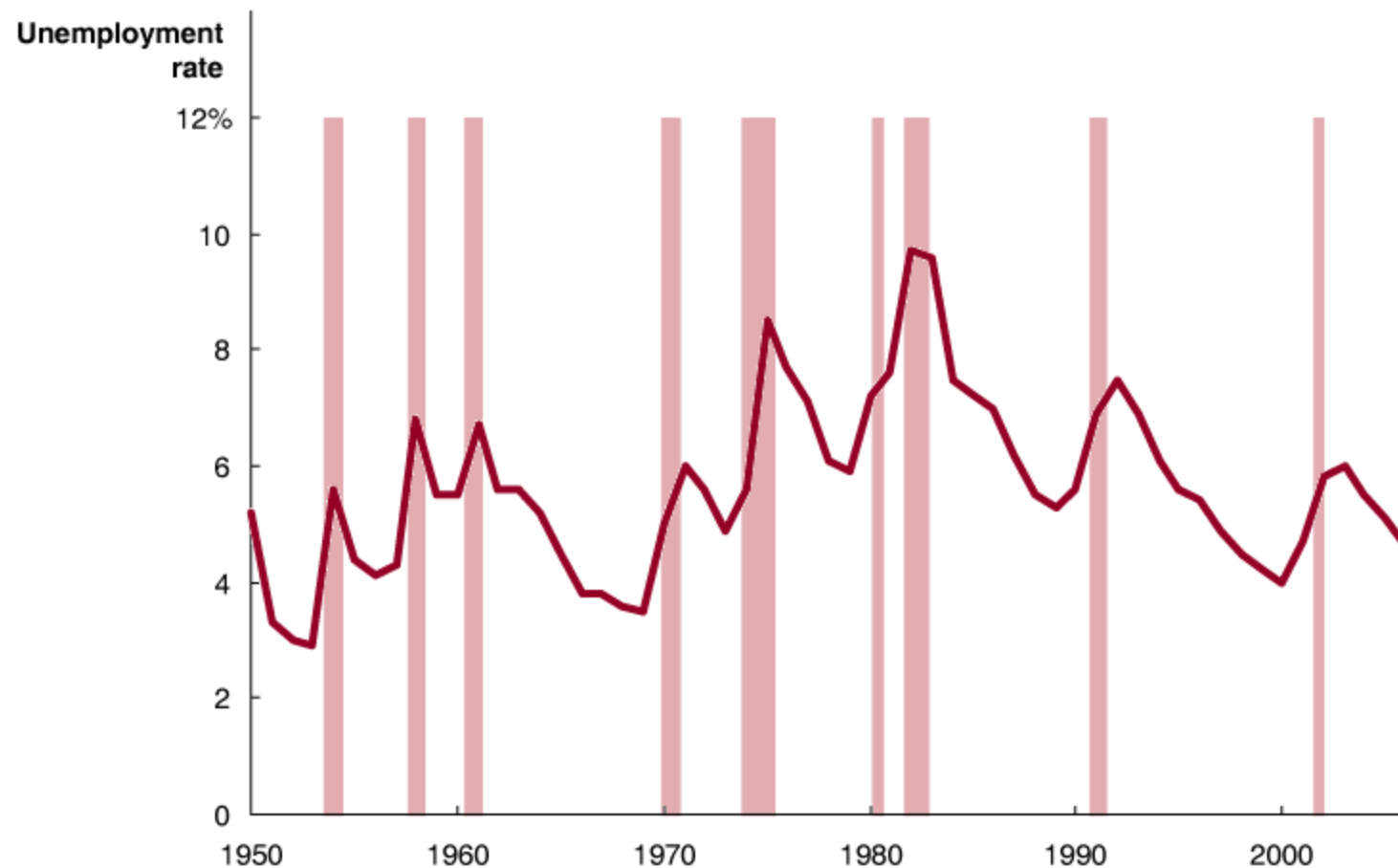
Today:

1. Types of Unemployment
2. Factors determine unemployment rate

Types of Unemployment

FIGURE 8-4

The Annual Unemployment Rate in the United States, 1950–2006



Types of Unemployment

Frictional Unemployment and Job Search

Frictional unemployment Short-term unemployment that arises from the process of matching workers with jobs.

Structural Unemployment

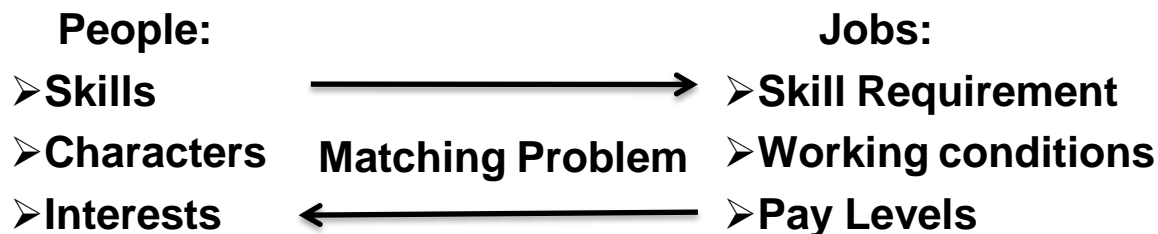
Structural unemployment Unemployment arising from a persistent mismatch between the skills and characteristics of workers and the requirements of jobs.

Cyclical Unemployment

Cyclical unemployment Unemployment caused by a business cycle recession.

Frictional unemployment

- Short-term unemployment
- Job Search: those new workers and who has lost spend some time engaging in job search



Unavoidable: always have some workers who are unemployed.

Frictional unemployment(Cont')

Seasonal unemployment: Due to weather or fluctuations of demand during different time of the year.

Examples:

1. In summer, stores located in beach resorts rise their hiring while reduce it in the winter
2. In opposite way, ski resorts rise hiring in the winter and reduce in the summer.
3. Department store increases hiring in Nov. and Dec. and reduce after New Year.

News Updates: Article 1: [Sainsbury's Charismas Hiring](#)

Seasonally adjusted Unemployment rate is more accurate!

Frictional unemployment(Cont')

Would eliminating all frictional unemployment be good for the economy?

NO!

It increases the economic efficiency, because it gives firms and workers time to ensure the good matches between attributes of workers and requirement of jobs.

Quantitative Analysis(NOT COVERED IN EXAMS,HWS):

Workers decision: accept this offer or not?

Bellman equation:

Reservation wage: $W \geq W_r$, accept this offer

Structural Unemployment

Definition:

Unemployment arising from a **persistent mismatch** between the skills and characteristics of workers and the requirements of jobs.

- Last longer than frictional unemployment because it takes time for workers to learn new skills.
- Examples:
 1. 3D animation force a lot of hand-drawn skilled workers in firms such as Walt Disney Picture and DreamWorks lost their jobs.
 2. American steel firms drop more than half employment from 1980s to 2000s because of competition of foreign firms and technological change

Cyclical Unemployment

Definition: Unemployment caused by a business cycle recession

➤ When economy is in recession----> Sales fall---> Cut back Production--->Laying off workers---> Economy recovered-
→Rehire workers

➤ Example: Article 2

[News from CNN Money about 2008/2009 recession](#)

Types of Unemployment

Full Employment:

When the only remaining unemployment is structural and frictional unemployment, the economy is said to be Full Employment.

Cyclical unemployment will drop to zero as economy moves through the expansion phase of the business cycle.

Natural rate of unemployment

The normal rate of unemployment, consisting of frictional unemployment plus structural unemployment.

Explaining Unemployment

Government Policies and the Unemployment Rate

Unemployment Insurance and Other Payments to the Unemployed

In the United States and most other industrial countries, the unemployed are eligible for unemployment insurance payments from the government.

In the United States, these payments are equal to about half the average wage. The length is six month.

Unemployment insurance helps the unemployed maintain their income and spending, which lessens the personal hardship of being unemployed and also helps reduce the severity of recessions.

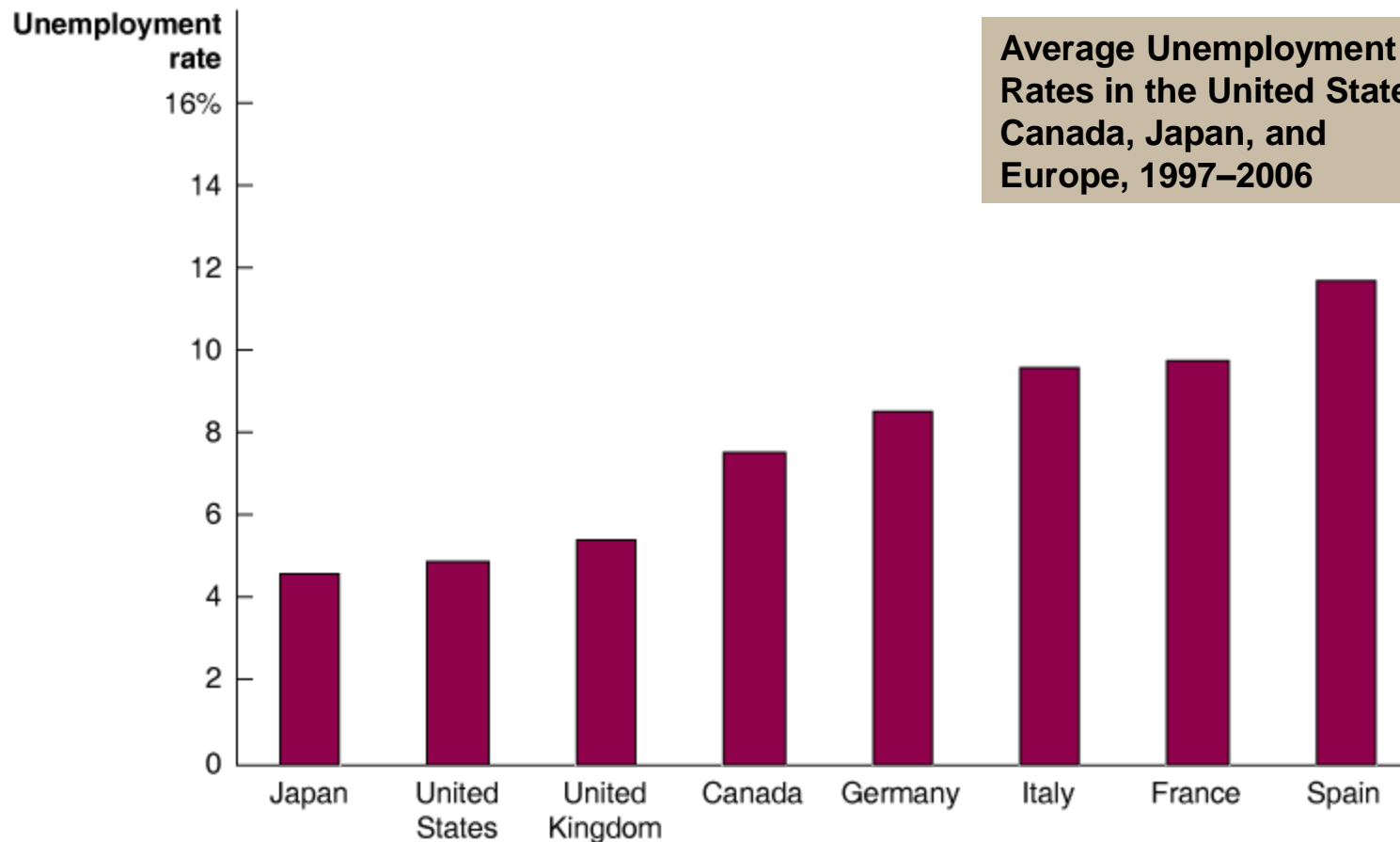
Explaining Unemployment

Government Policies and the Unemployment Rate

International Comparisons

FIGURE 8-5

Average Unemployment Rates in the United States, Canada, Japan, and Europe, 1997–2006



Explaining Unemployment

Government Policies and the Unemployment Rate

Minimum Wage Laws

In 1938, the federal government enacted a national minimum wage law. In 1938, \$0.25; In 2009, \$7.25

California: \$8; San Francisco: \$9.36;

If the minimum wage is set above the market wage determined by the demand and supply of labor, the quantity of labor supplied will be greater than the quantity of labor demanded.

Economists agree that the current minimum wage is above the market wage for some workers, but they disagree on the amount of unemployment that has resulted.

Explaining Unemployment

Labor Unions

Labor unions are organizations of workers that bargain with employers for higher wages and better working conditions for their members. Wages are higher than market wage in these industries which results in employers hire fewer workers.

Only 9% of workers outside government sector are unionized. It remain in a few industries such as airlines, steel, automobiles, telecommunications.

Efficiency Wages

Efficiency wage A higher-than-market wage that a firm pays to increase worker productivity.

Making the Connection

Why Does Costco Pay Its Workers So Much More Than Wal-Mart Does?



Costco's relatively high wages and health benefits reduce employee turnover and raise morale and productivity.

Wal-mart:

- 1.3 million workers
- Average wage: \$10.50/hr
- Benefit: 50% covered by medical insurance

Costco:

- Minimum wage: \$11
- Average wage: \$17
- Benefit: 90% covered by medical insurance

CEO of Costco: Paying good wages and keeping your people working for you is a very good business