Unemployment, its types, Recession, and Productivity

By

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Defining and Measuring Unemployment

- The most frequently discussed symptom of a recession is unemployment.
- An *employed* person is any person of 16 years old or above:
  1. who works for pay, either for someone else or in his or her own business for 1 or more hours per week,
  2. who works without pay for 15 or more hours per week in a family enterprise, or
  3. who has a job but has been temporarily absent, with or without pay.

Defining and Measuring Unemployment

- An *unemployed* person is a person 16 years old or above:
  1. is not working,
  2. is available for work, and
  3. has made specific efforts to find work during the previous 4 weeks.

Defining and Measuring Unemployment

$$\text{labor force} = \text{employed} + \text{unemployed}$$

$$\text{population} = \text{labor force} + \text{not in labor force}$$

$$\text{unemployment rate} = \frac{\text{unemployed}}{\text{employed} + \text{unemployed}}$$

$$\text{labor force participation rate} = \frac{\text{labor force}}{\text{population}}$$

Defining and Measuring Unemployment

- Computing the unemployment rate for the month of July 2003:
  - Labor force: 141.39 million
  - Employed: 133.47 million
  - Unemployed: 7.92 million

$$\text{unemployment rate}_{\text{July 2003}} = \frac{7.92}{133.47 + 7.92} = 5.6\%$$

Types of Unemployment

- **Frictional unemployment**

Frictional unemployment arises because of the time needed to match qualified job seekers with available job openings

  - New college grads looking for jobs
  - Parents returning to the work force
  - Quit job to look for a better one

- **Structural unemployment** is the portion of unemployment that is due to changes in the structure of the economy that result in a significant loss of jobs in certain industries.
- Technology (machines) displaces workers
- International Trade (workers lose jobs due to trade)

- **Cyclical unemployment** is the increase in unemployment that occurs during recessions and depressions.

- **Seasonal unemployment** is caused by seasonal shifts in labor supply and demand
  - Examples: construction, agriculture, Life Guards

- *Inflation* is an increase in the overall price level.
- *Deflation* is a decrease in the overall price level.
- A **recession** is roughly a period in which real GDP declines for at least two consecutive quarters. It is marked by falling output and rising unemployment
- A **depression** is a prolonged and deep recession..
- In recession unemployment increases

The Benefits of Recessions

- Recessions may help to reduce inflation.
- Some argue that recessions may increase efficiency by driving the least efficient firms out of business and by forcing surviving firms to trim waste and manage their resources better.
- Also, a recession leads to a decrease in the demand for imports, which improves a nation's balance of payments.

Okun's Law

- Defined by economist **Arthur Okun** in 1962.
- Describes the inverse relationship between **unemployment** and **GDP growth**.
- For every 1% increase in unemployment, a country's GDP falls by approximately **2%–3%** from its potential.
- It suggests that when the unemployment rate decreases, a nation's GDP grows at a faster rate, and vice versa.

Inflation

- *Inflation* is an increase in the overall price level.
- *Deflation* is a decrease in the overall price level.
- *Sustained inflation* is an increase in the overall price level that continues over a significant period.

- Inflation is a sustained increase in the average level of prices
- **Hyperinflation** is a very high rate of inflation
  - Brazil experienced inflation over 1000% during some recent years
  - Germany between WW1 and WW2

- **Disinflation** is a reduction in the positive inflation rate

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Inflation

Inflation is a continuous increase in average prices over time. A one-time increase of average prices is not inflation.

The formula to calculate an inflation rate is

$$\text{Inflation rate (\%)} = \frac{(\text{Current year price index} - \text{Previous year price index})}{\text{Previous year price index}} \times 100$$

How do we Measure Inflation?

1. Consumer Price Index
2. Producer Price Index
3. GDP Deflator

Recessions, Depressions, and Unemployment

- The *business cycle* describes the periodic ups and downs in the economy, or deviations of output and employment away from the long-run trend.

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Inflation: What Causes It?

- **Types of Inflation**

1. **Demand-Pull Inflation**
   a. Total spending in excess of production capacity
   b. Often described: "too many dollars chasing too few goods"
   c. Demand curve shifting to the right

Inflation

- Types of Inflation (continued)

2. **Cost-Push Inflation (Supply-Side Inflation)**
   - Cost-push Inflation summarized:
     - Prices rise due to rising production costs (factors of production) called “supply shocks” (oil, wages, other materials)
     - Supply curve “shifts to the left”