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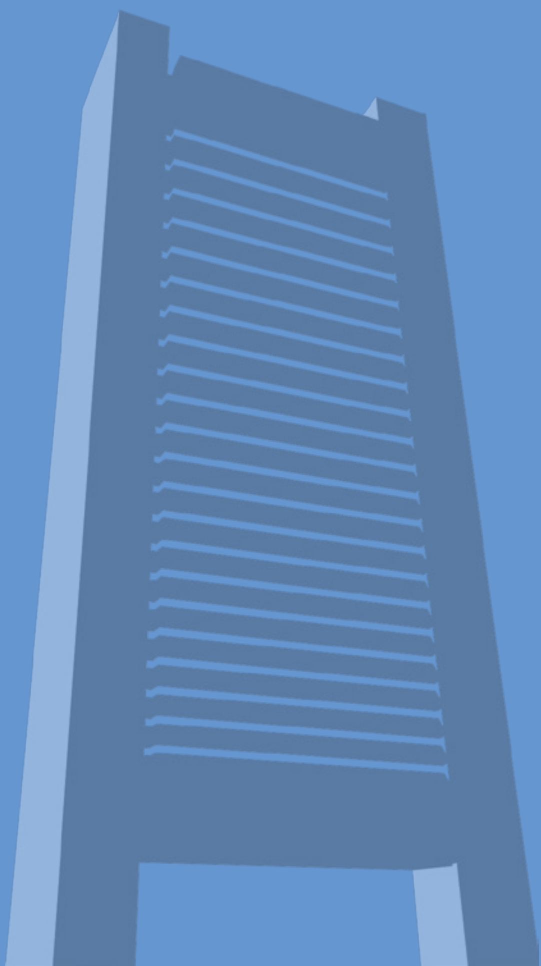

Labor Market Slack and Monetary Policy

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February 26, 2014

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Recent Economic Data

- Recent data have been disappointing
  - Payroll employment grew by 113,000 jobs in January and 75,000 in December
  - Two-month average of 94,000 is well below the previous two-month average of October and November
- Is the weakness a trend (slower economy) or an anomaly (severe weather)?
- This uncertainty provides an additional strong rationale for taking a patient approach to removing monetary policy accommodation

Does the Traditional Unemployment Measure Understate Labor Market Slack?

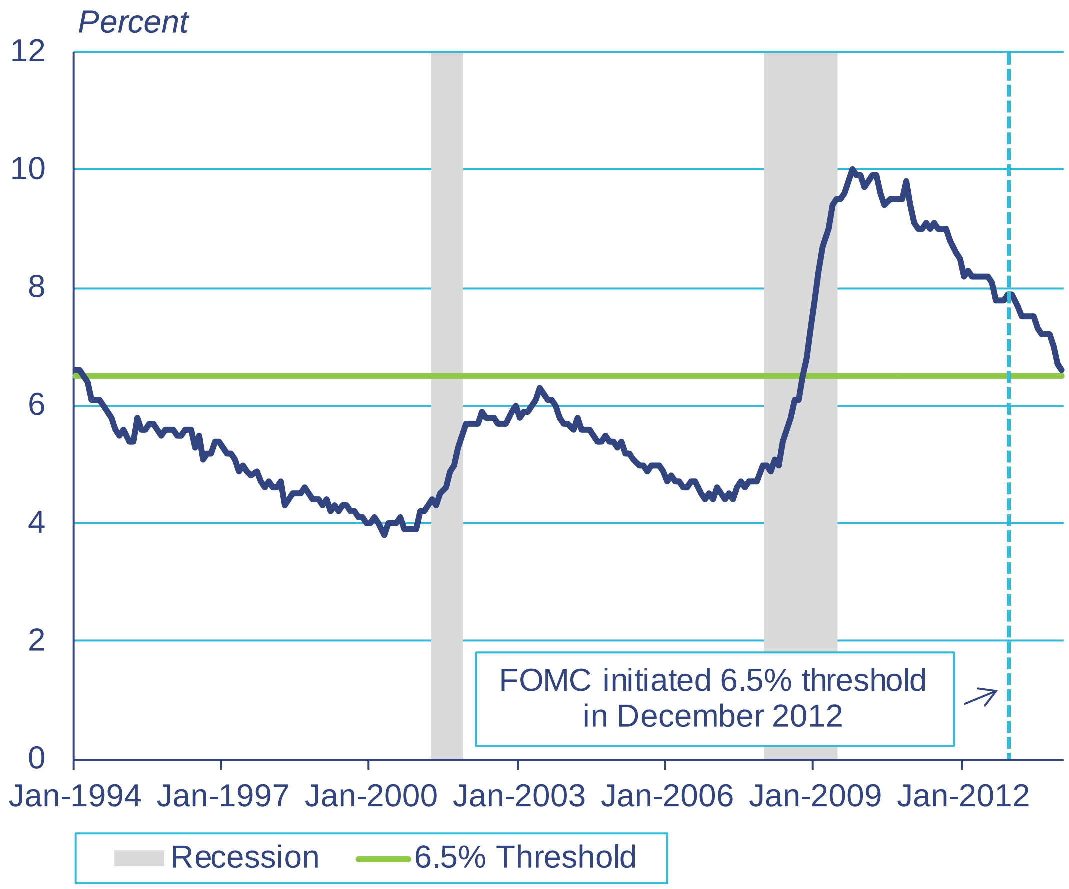
- Unemployment rate has fallen to 6.6 percent
  - Unemployment rate is near the 6.5 percent threshold noted in the Fed's guidance
  - Of late the unemployment rate has fallen more quickly than most forecasters expected
- Labor force participation remains low – are workers able and willing to work?

Other Indicators of Slack in Labor Markets

- 7.3 million Americans want full-time work but are currently working part time
  - A number that is dramatically higher than the 4.6 million workers in that situation in December of 2007
  - These workers are qualified and willing to work
- Very low inflation rate and very slow growth in labor compensation are consistent with significant labor market slack

Figure 1: Civilian Unemployment Rate (U-3): Total Unemployed, as a Percent of the Civilian Labor Force

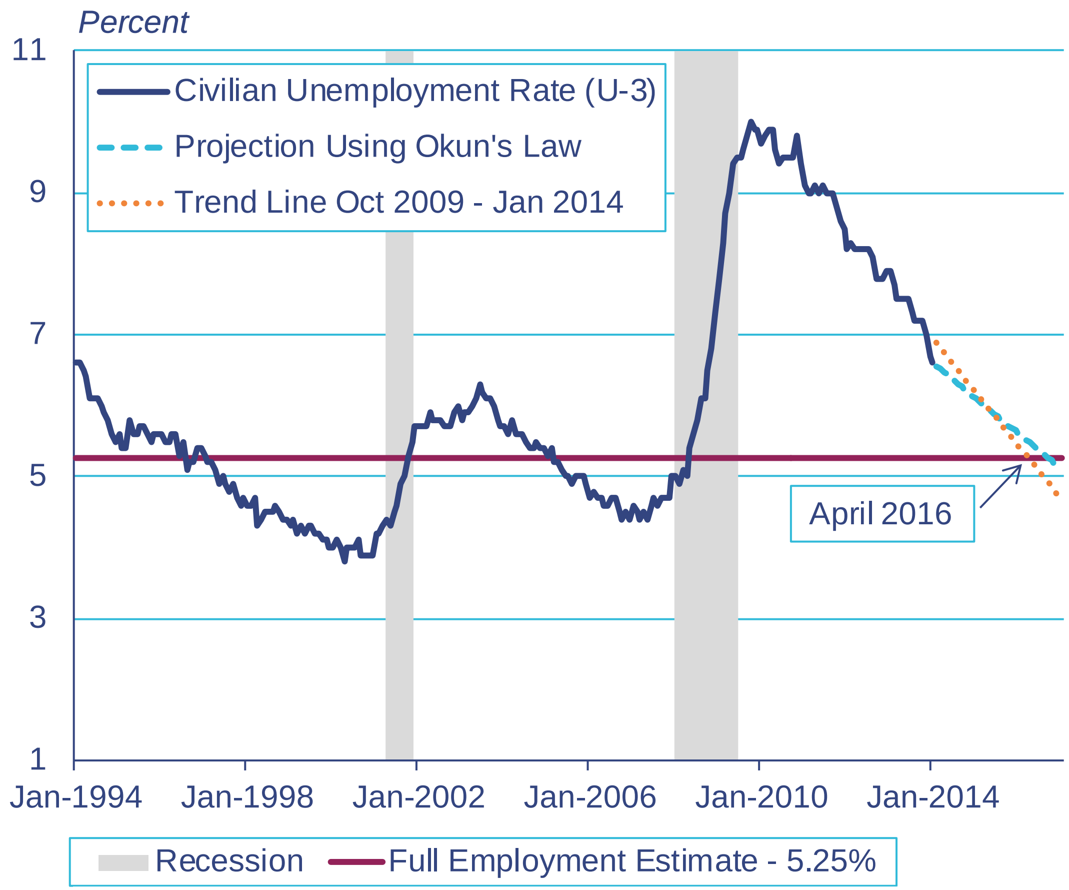
January 1994 - January 2014



Source: BLS, NBER, Haver Analytics

Figure 2: Civilian Unemployment Rate (U-3) Path based on Okun's Law and Recent Trends

Jan 1994 - Jan 2014 Actual, Feb 2014 - Jan 2017 Projections

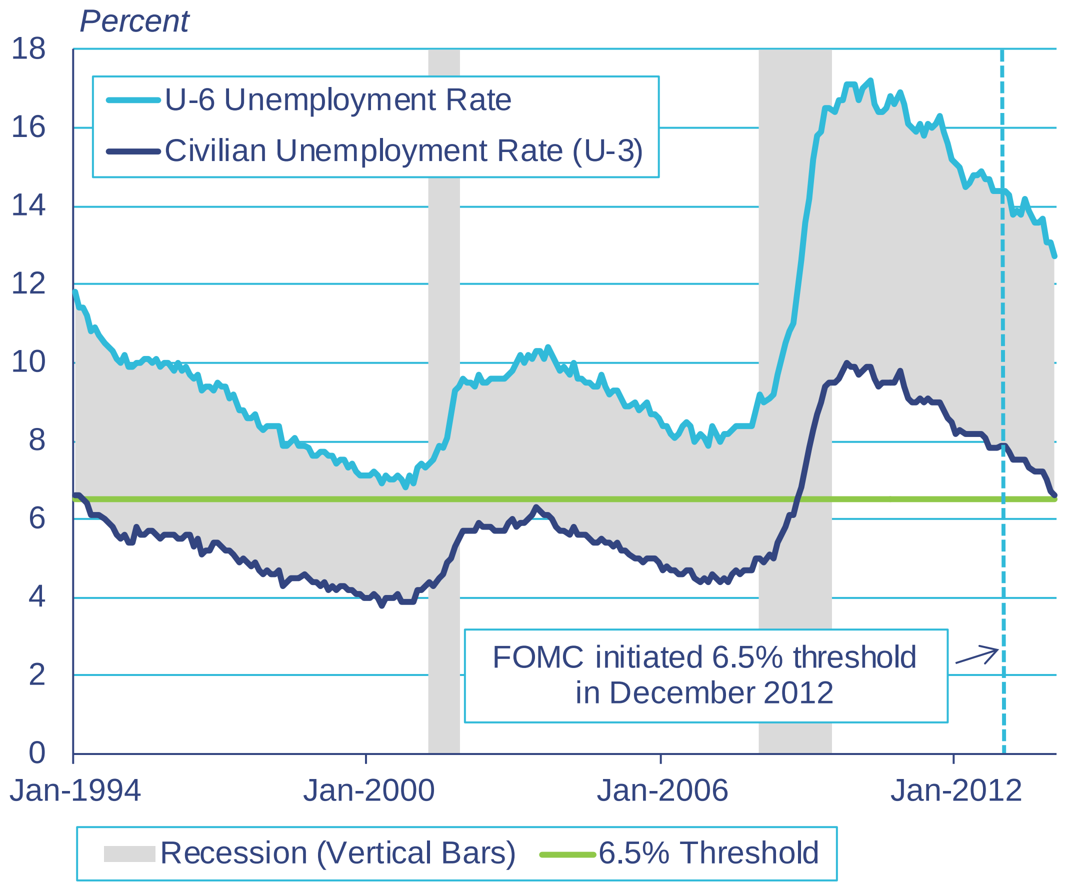


Note: Okun's Law projections assume growth of 1% above potential GDP growth of 2%.

Source: BLS, NBER, Haver Analytics and author's calculations

Figure 3: Measures of Labor Underutilization

January 1994 - January 2014

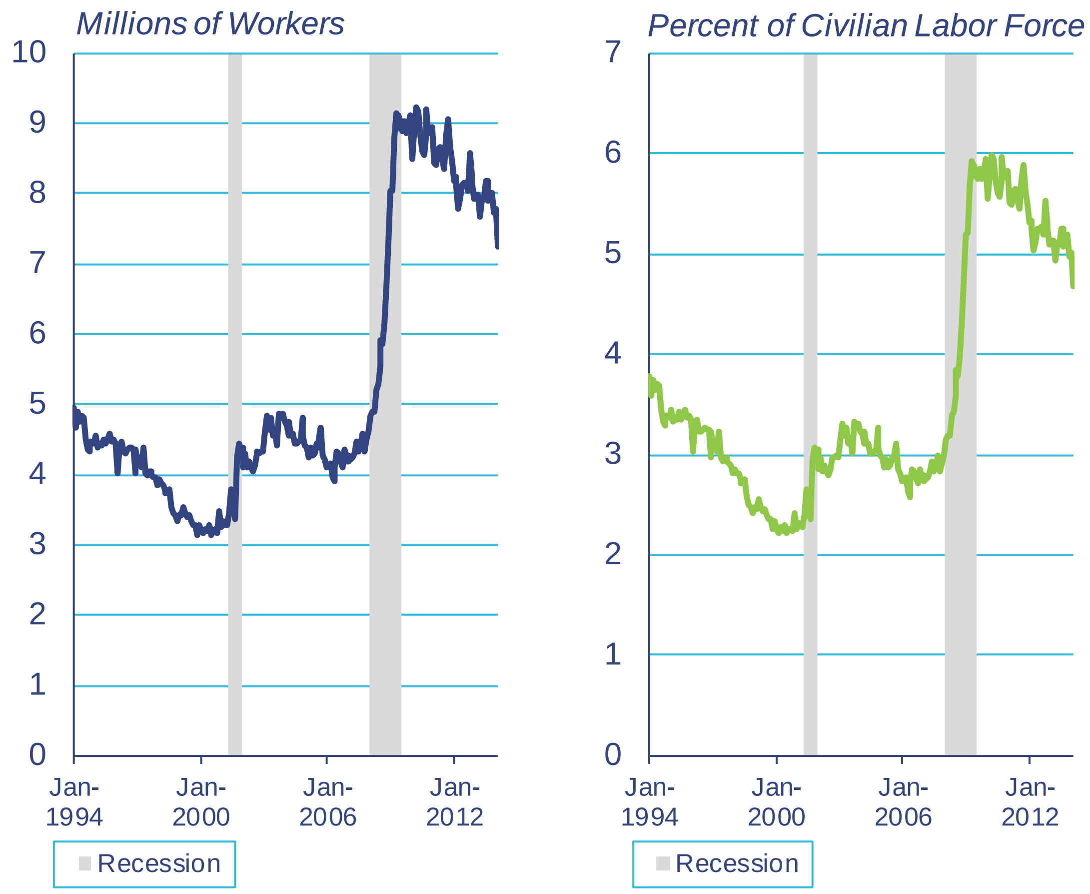


Note: U-6 measure is total unemployed, plus all persons marginally attached to the labor force, plus total employed part time for economic reasons, as a percent of the civilian labor force plus all persons marginally attached to the labor force.

Source: BLS, NBER, Haver Analytics

Figure 4: Persons Employed Part Time for Economic Reasons

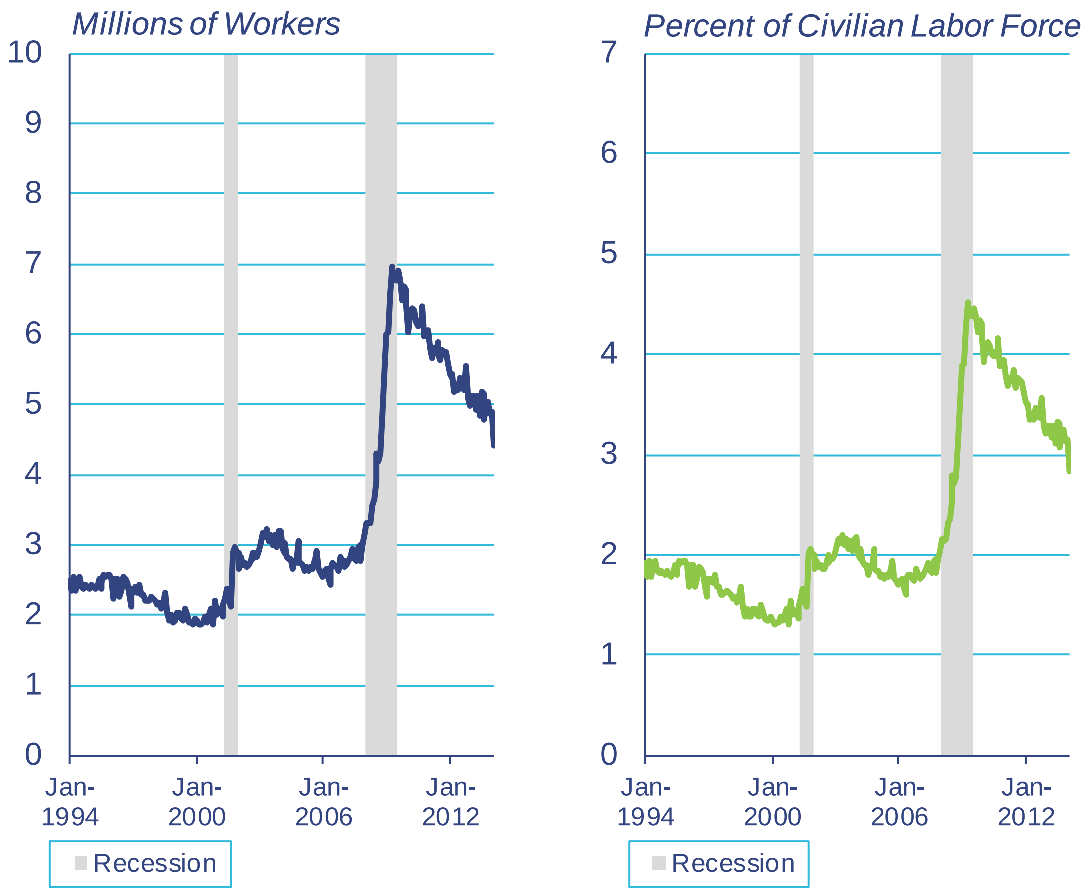
January 1994 - January 2014



Source: BLS, NBER, Haver Analytics

Figure 5: Persons Employed Part Time for Economic Reasons – Because of Slack Work or Business Conditions

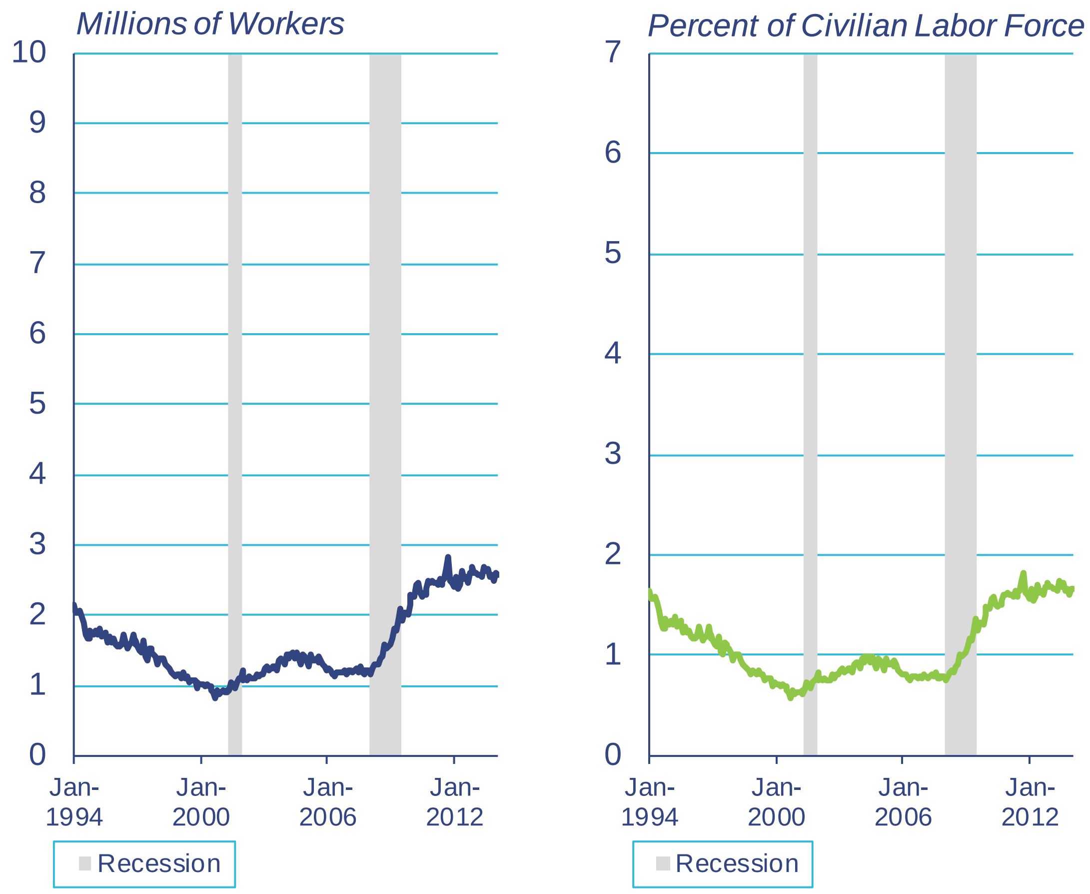
January 1994 - January 2014



Source: BLS, NBER, Haver Analytics

Figure 6: Persons Employed Part Time for Economic Reasons – Because They Could Only Find Part-Time Work

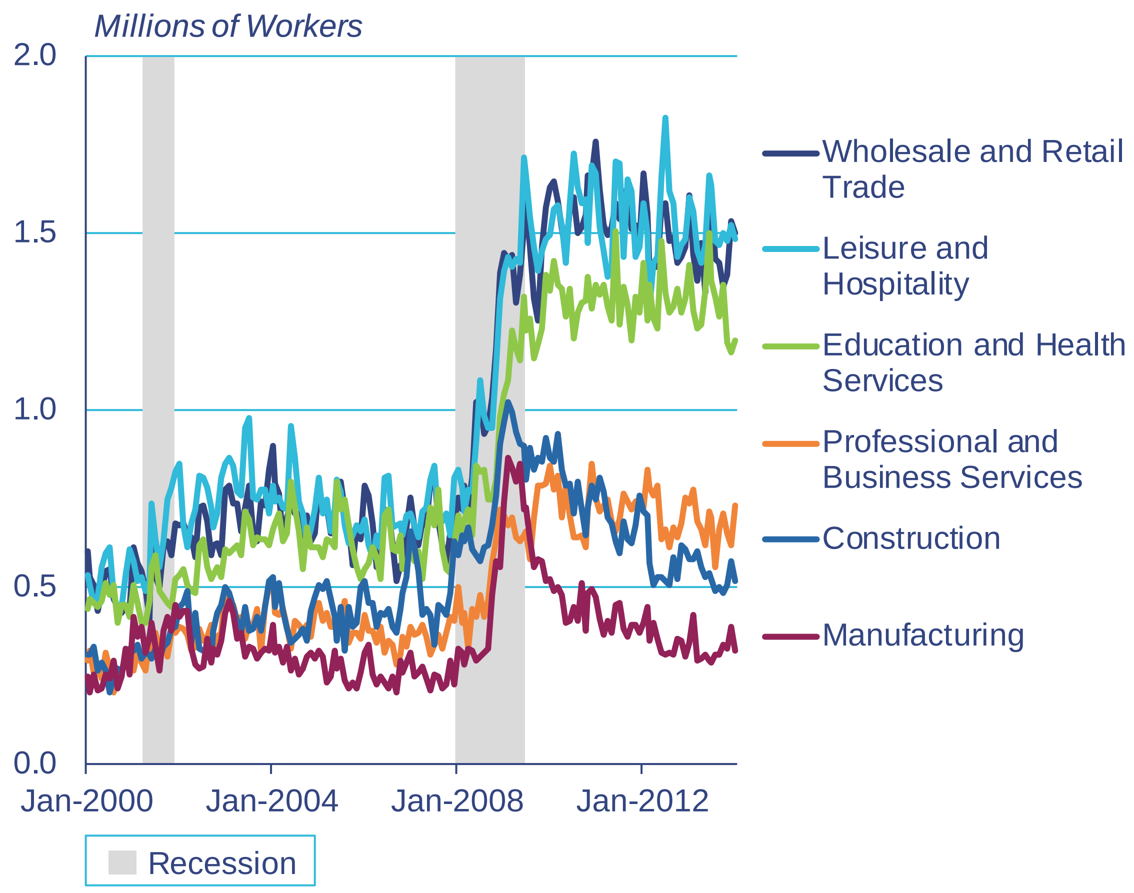
January 1994 - January 2014



Source: BLS, NBER, Haver Analytics

Figure 7: Persons Employed Part Time for Economic Reasons for Selected Industries

January 2000 - January 2014

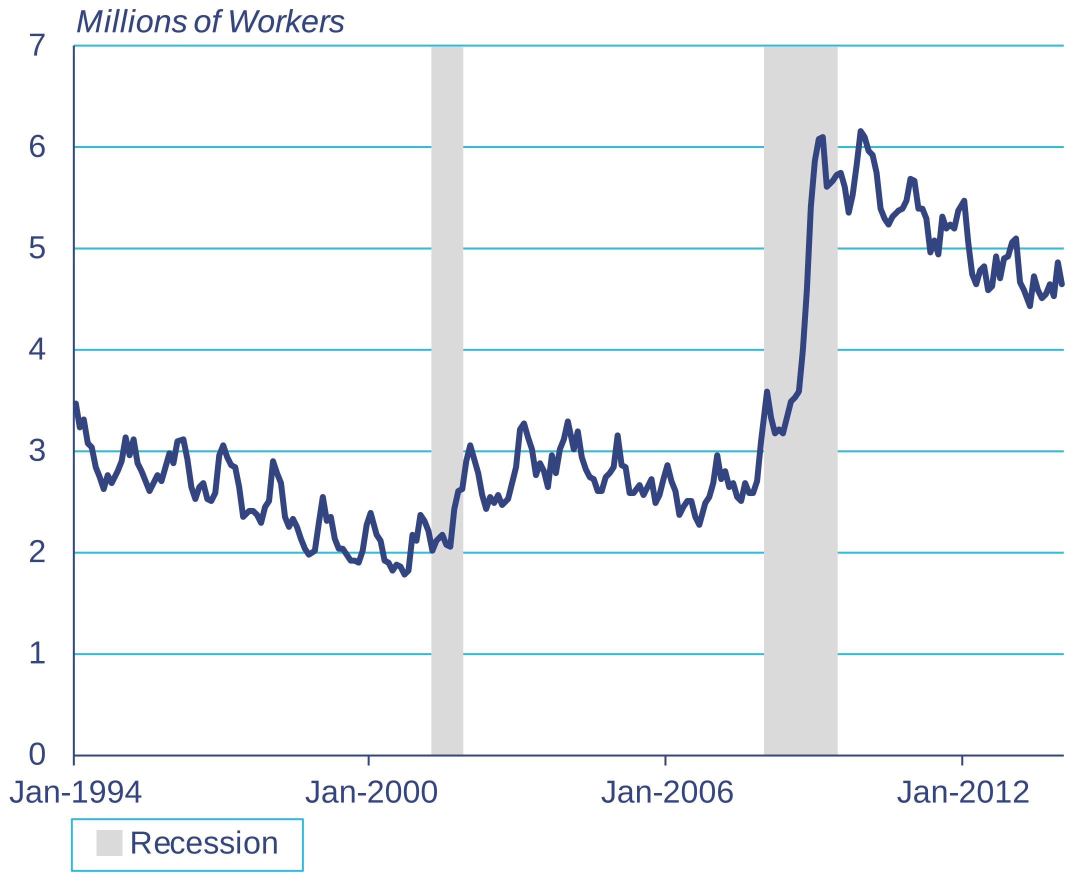


Note: Series are not seasonally adjusted. Selected industries are the industries with the largest numbers of workers part time for economic reasons in January 2014.

Source: BLS, NBER, Haver Analytics

Figure 8: Persons Employed Part Time for Economic Reasons: Age 25 - 54

January 1994 - January 2014

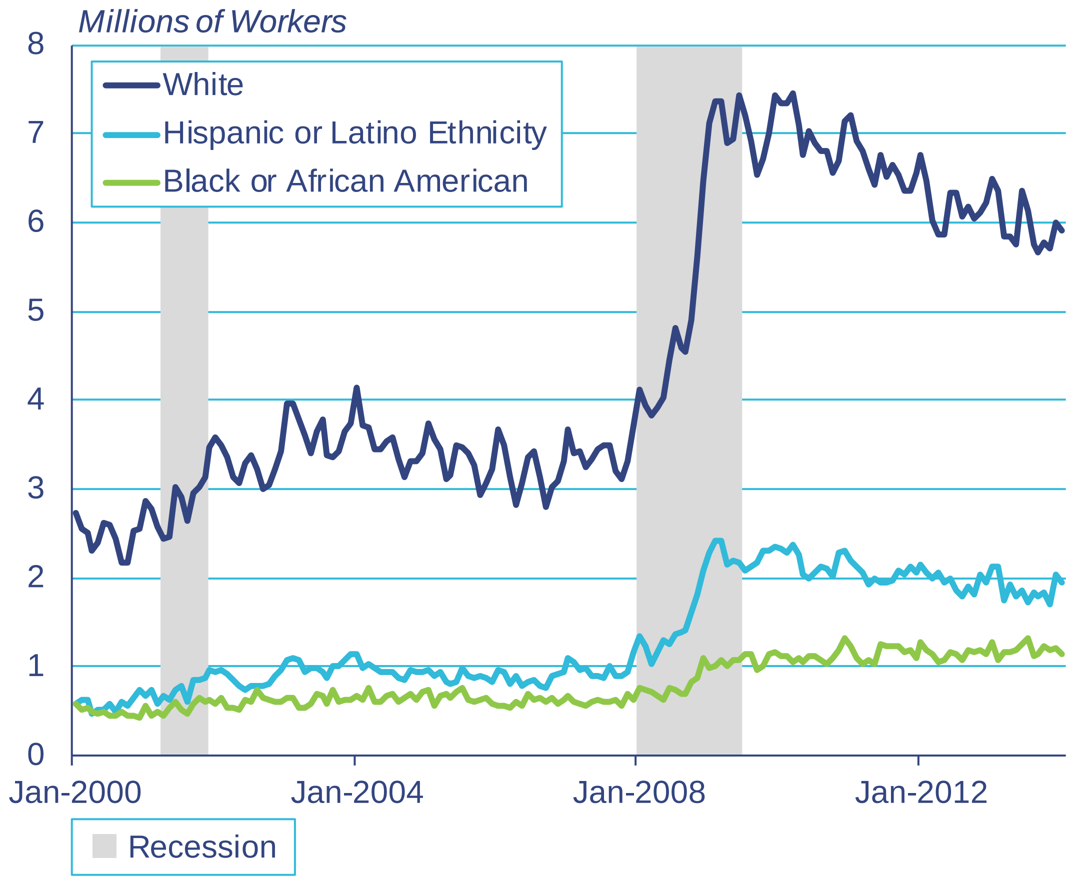


Note: Series is not seasonally adjusted.

Source: BLS, NBER, Haver Analytics

Figure 9: Persons Employed Part Time for Economic Reasons in Nonagricultural Industries by Race and Hispanic or Latino Ethnicity

January 2000 - January 2014



Note: Series are not seasonally adjusted. The numbers add to more than the total as workers may be counted in more than one category.

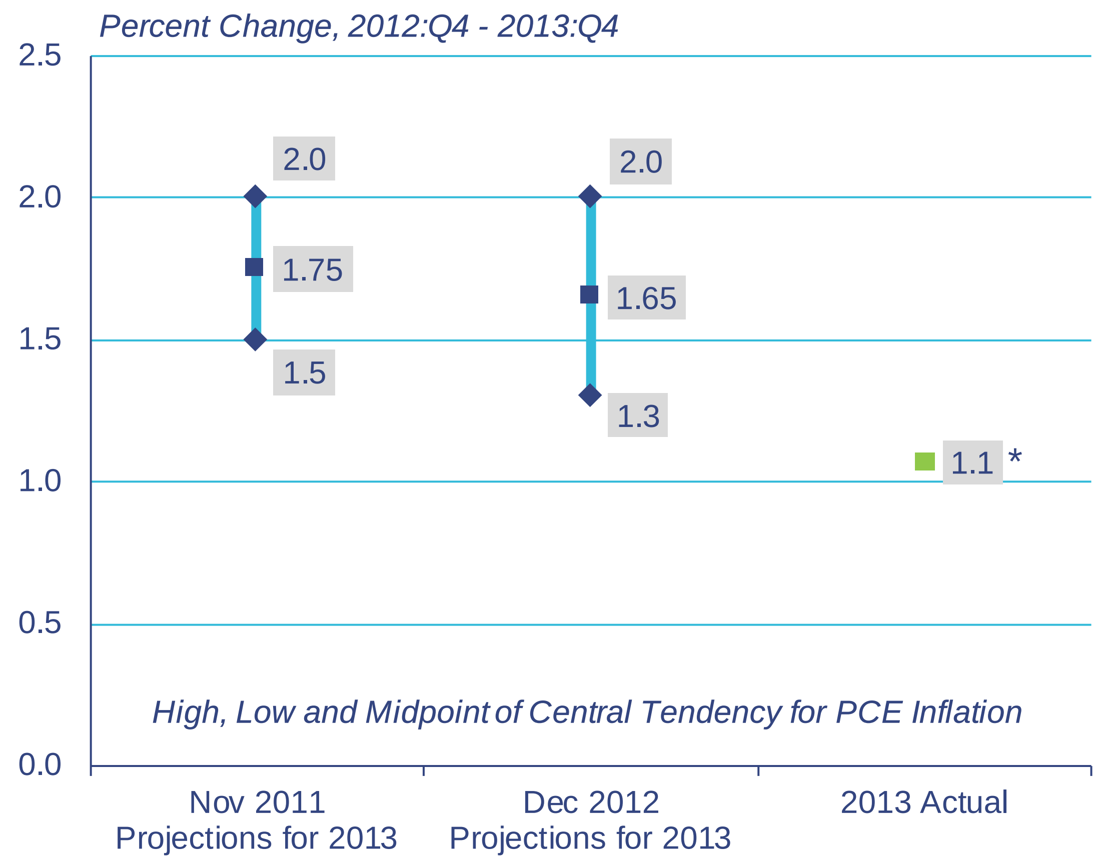
Source: BLS, NBER, Haver Analytics

Part Time for Economic Reasons and Economic Slack

- Debate over whether workers marginally attached to the labor force will return to the workforce
- Slack from workers part time for economic reasons is different
  - Employers have hired them (they have the necessary skills)
  - They are clearly willing to work
  - But economic conditions have been insufficient to convert part-time to full-time work
- Slack in labor markets may be better measured by U-6 than U-3 unemployment rate

Figure 10: Inflation Projections of Federal Reserve Governors and Bank Presidents for 2013

November 2, 2011 and December 12, 2012 Projections, December 2013 Actual

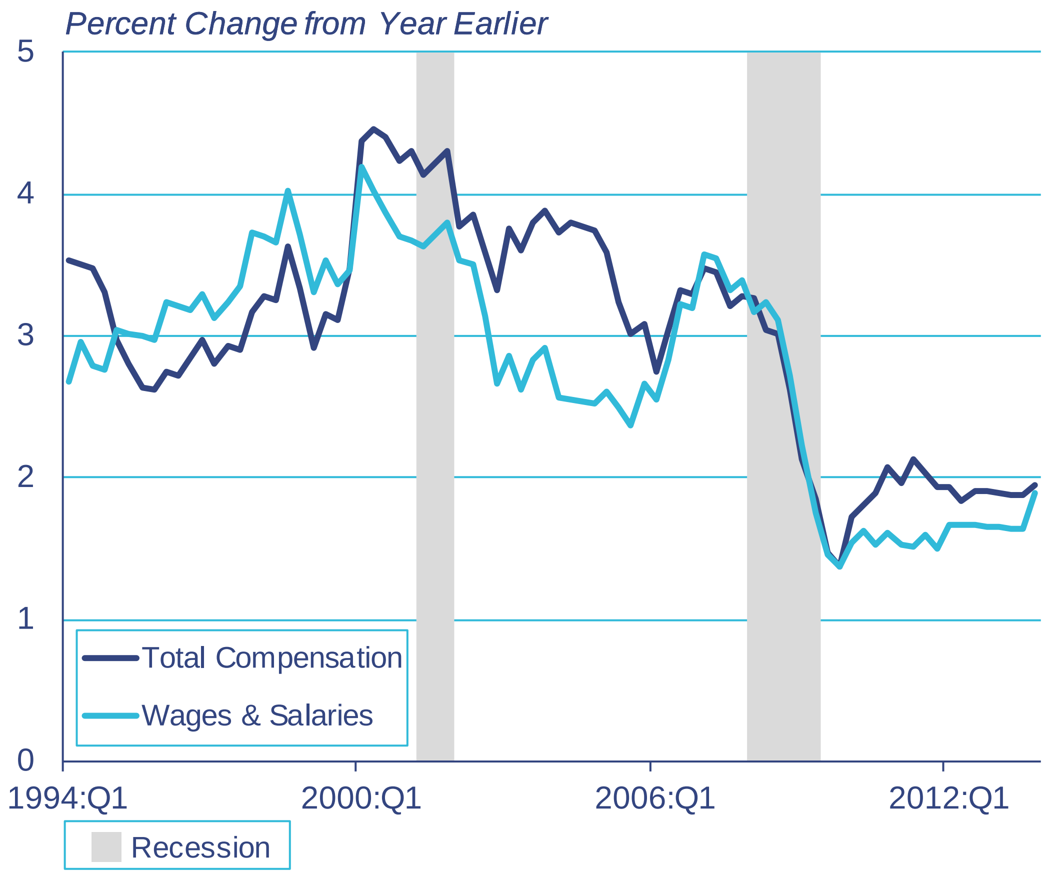


*Note: Central tendency excludes the three highest and three lowest projections for each variable in each year. *The 1.1% figure for 2013 is the percent change from December 2012 - December 2013.*

Source: FOMC, Summary of Economic Projections

Figure 11: Employment Cost Indices for Civilian Workers

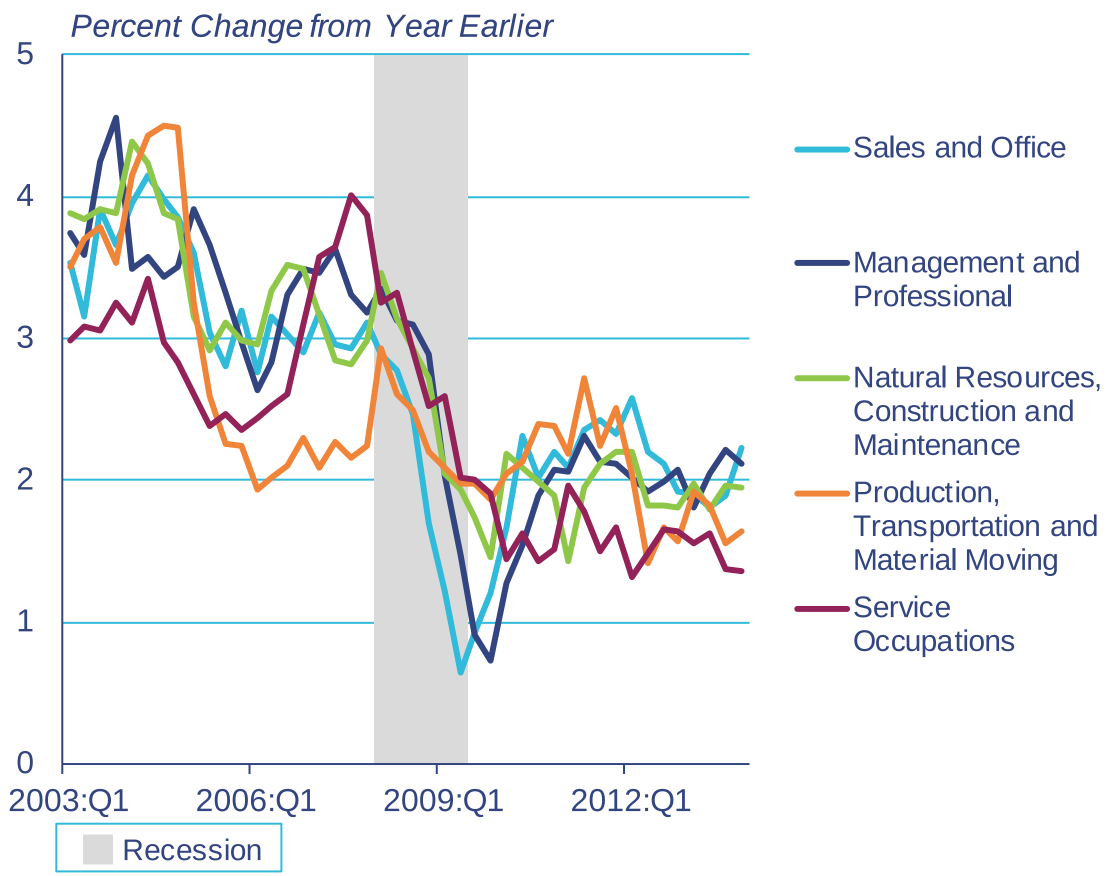
1994:Q1 - 2013:Q4



Source: BLS, NBER, Haver Analytics

Figure 12: Employment Cost Index for Total Compensation for Private Industry Workers by Occupational Group

2003:Q1 - 2013:Q4



Source: BLS, NBER, Haver Analytics

Concluding Observations

- Evaluating current labor market slack is important for setting monetary policy
- Evidence of significant slack even as we approach the 6.5 percent threshold
  - Elevated number of workers who are part time for economic reasons
  - Unemployment rate is still high
  - Inflation is very low – well below target
- This calls for a patient approach to removing monetary policy accommodation