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Underutilization in U.S. Labor Markets

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Recent Economic News

- ▶ Generally, data have been positive
 - ▶ Q4 real GDP growth was 3.2 percent and 2013 H2 was 3.7 percent – well above the 2.4 percent average over the recovery
 - ▶ Unemployment has been declining – 6.7 percent in December
 - ▶ Over *20 million* Americans are either unemployed, marginally attached to the labor force, or working part time when they would prefer full-time work
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Evaluating Labor Markets

- ▶ Unemployment rate may not fully capture current slack in labor markets
 - ▶ Relevant for monetary policy
 - ▶ Current exceptionally low target range for short-term interest rates likely will be appropriate well past the time that the unemployment rate declines below 6.5 percent
 - ▶ Quickly approaching 6.5 percent
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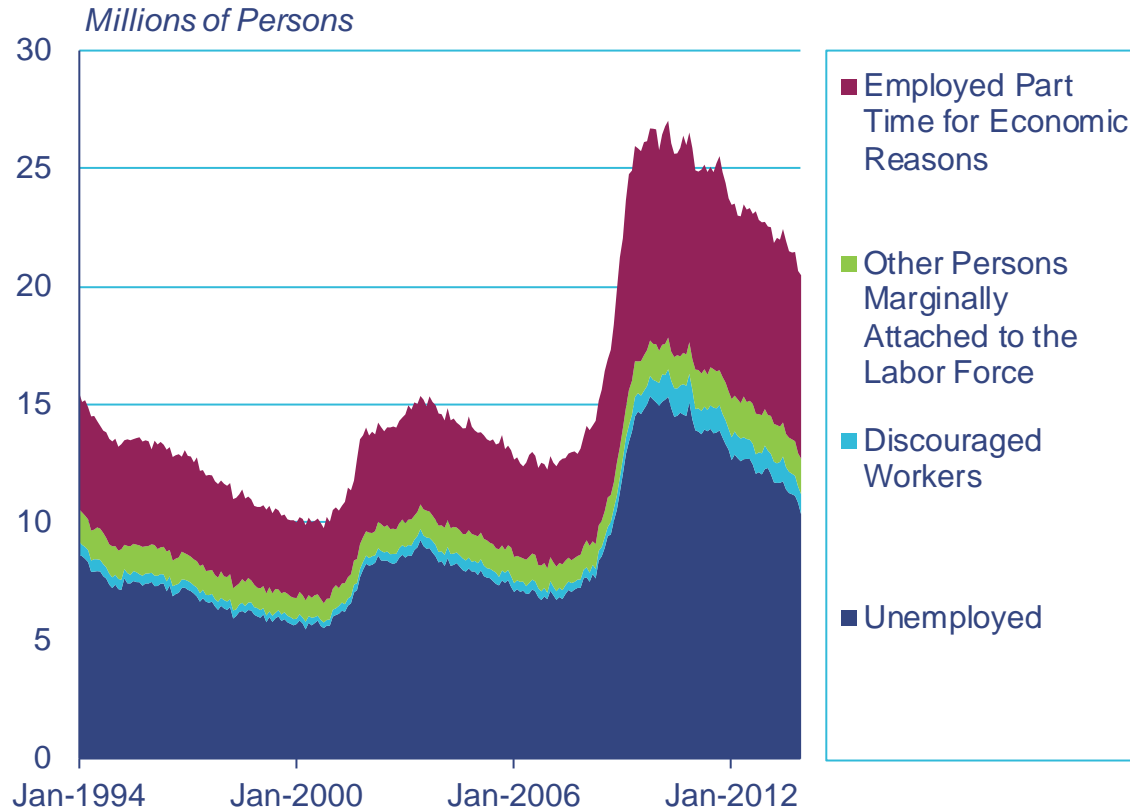


Implications for Monetary Policy

- ▶ Policy needs to place greater weight on broader measures of unemployment to capture labor market slack
 - ▶ Very subdued inflation reflective of labor market slack – 1.1 percent PCE inflation
 - ▶ Low inflation provides flexibility to accommodate a more rapid improvement in labor markets by keeping short-term rates low
 - ▶ Policy stance should be patient until we have a stronger recovery
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Figure 1: Alternative Measures of Labor Underutilization

January 1994 - December 2013



Note: All series in this chart are seasonally adjusted, including the series for discouraged workers and other persons marginally attached to the labor force, which are not seasonally adjusted by the Bureau of Labor Statistics.

Source: BLS, Haver Analytics



Alternative Unemployment Rates

- ▶ U-3 definition of unemployment includes people who do not have jobs but have actively searched for work in the last 4 weeks
 - ▶ U-4 includes discouraged workers – searched for work in the last year but not in the last 4 weeks
 - ▶ 917,000 of these discouraged workers in the U.S., compared to only 363,000 at the beginning of the recession in December of 2007
 - ▶ Discouraged – do not think jobs are currently available for them
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Broader Measures of Unemployment

- ▶ U-5 includes U-4 workers and all other marginally attached to the workforce
 - ▶ Available to work, searched for work in previous year, but not in last four weeks for reasons other than no available jobs
 - ▶ 1.5 million Americans in this category compared to 981,000 in December of 2007
 - ▶ U-6 includes U-5 and those employed part time for economic reasons
 - ▶ Had their hours reduced – or could only secure part-time work
 - ▶ 7.8 million workers who are part time for economic reasons, up sharply from the 4.6 million in December of 2007
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Measures of Unemployment Relative to First Tightening in the Previous Recovery

- ▶ June 30, 2004 was the first tightening
 - ▶ Unemployment at that time was 5.6 percent
 - ▶ PCE inflation was 2.8 percent
 - ▶ Current conditions quite different
 - ▶ Unemployment is much higher – 6.7 percent
 - ▶ PCE inflation is much lower – 1.1 percent
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Figure 2: U-3 – Civilian Unemployment Rate: Total Unemployed, as a Percent of the Civilian Labor Force

January 1994 - December 2013

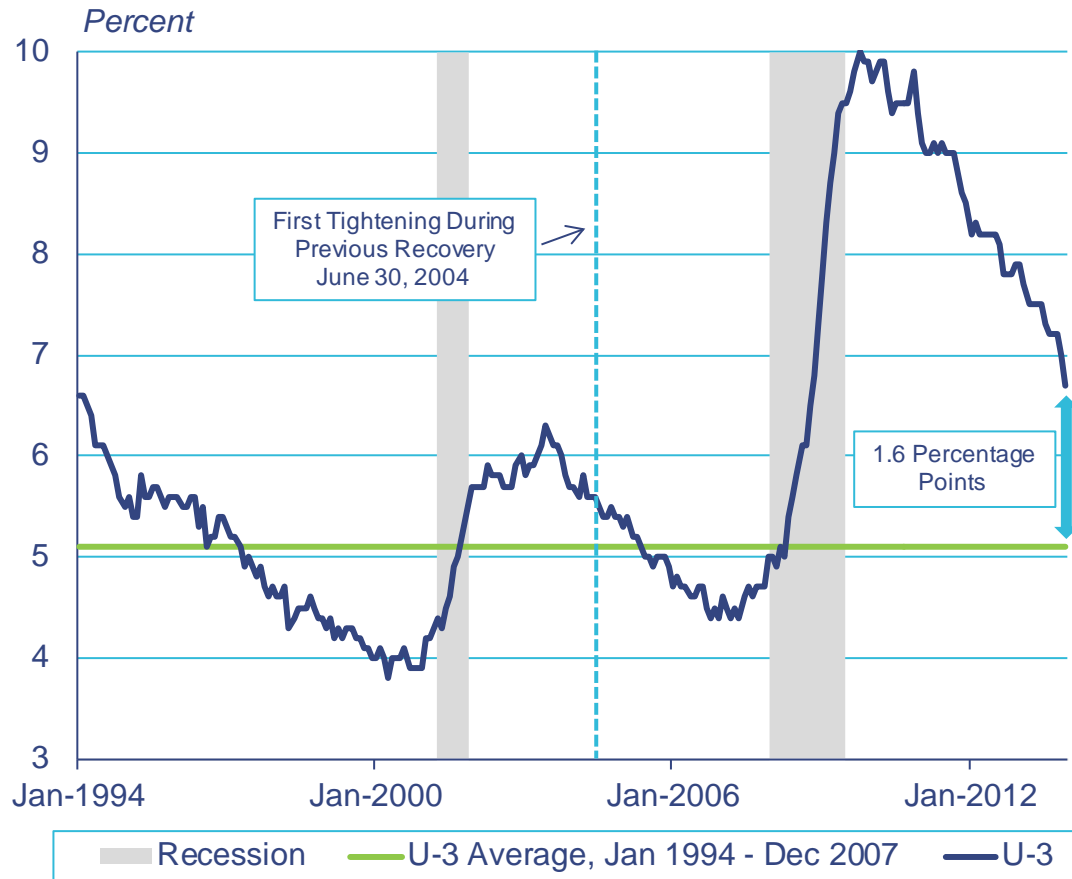




Figure 3: U-4 – Total Unemployed Plus Discouraged Workers, as a Percent of the Civilian Labor Force Plus Discouraged Workers
January 1994 - December 2013

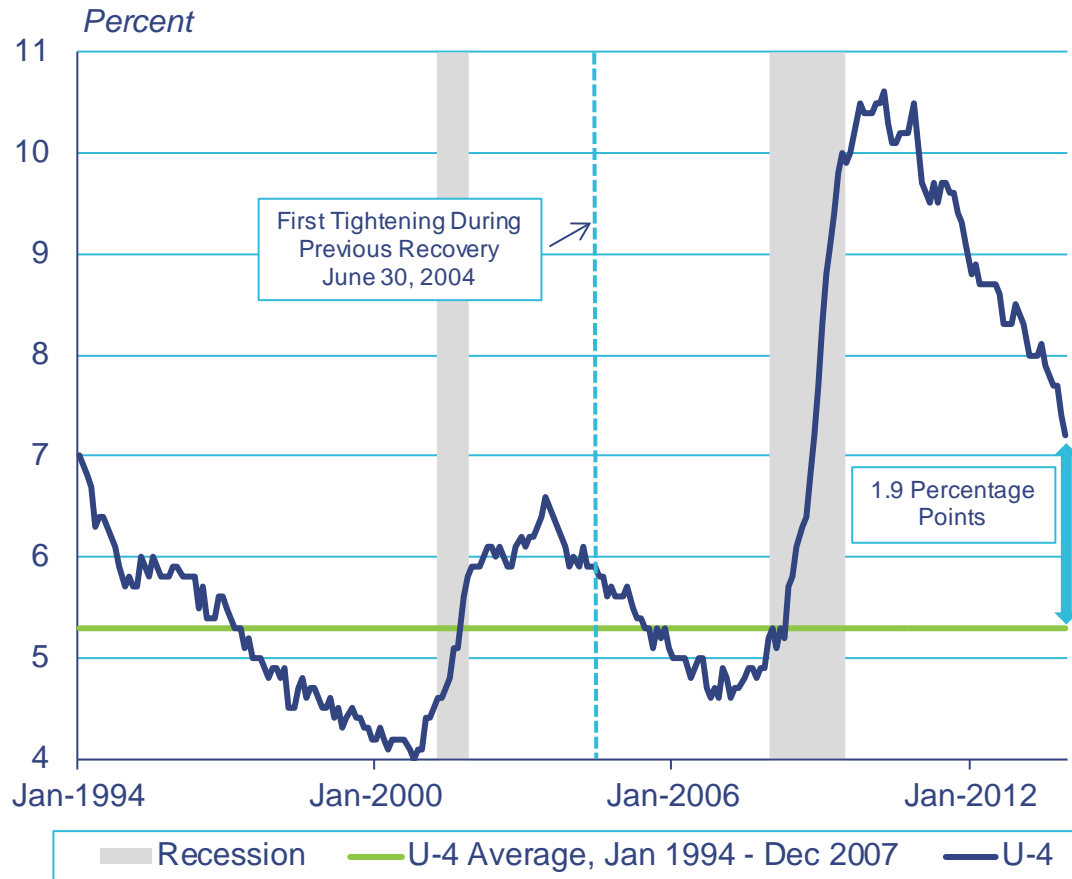


Figure 4: U-5 – Total Unemployed, Plus Discouraged Workers, Plus All Other Persons Marginally Attached to the Labor Force as a Percent of the Civilian Labor Force Plus All Persons Marginally Attached to the Labor Force
 January 1994 - December 2013

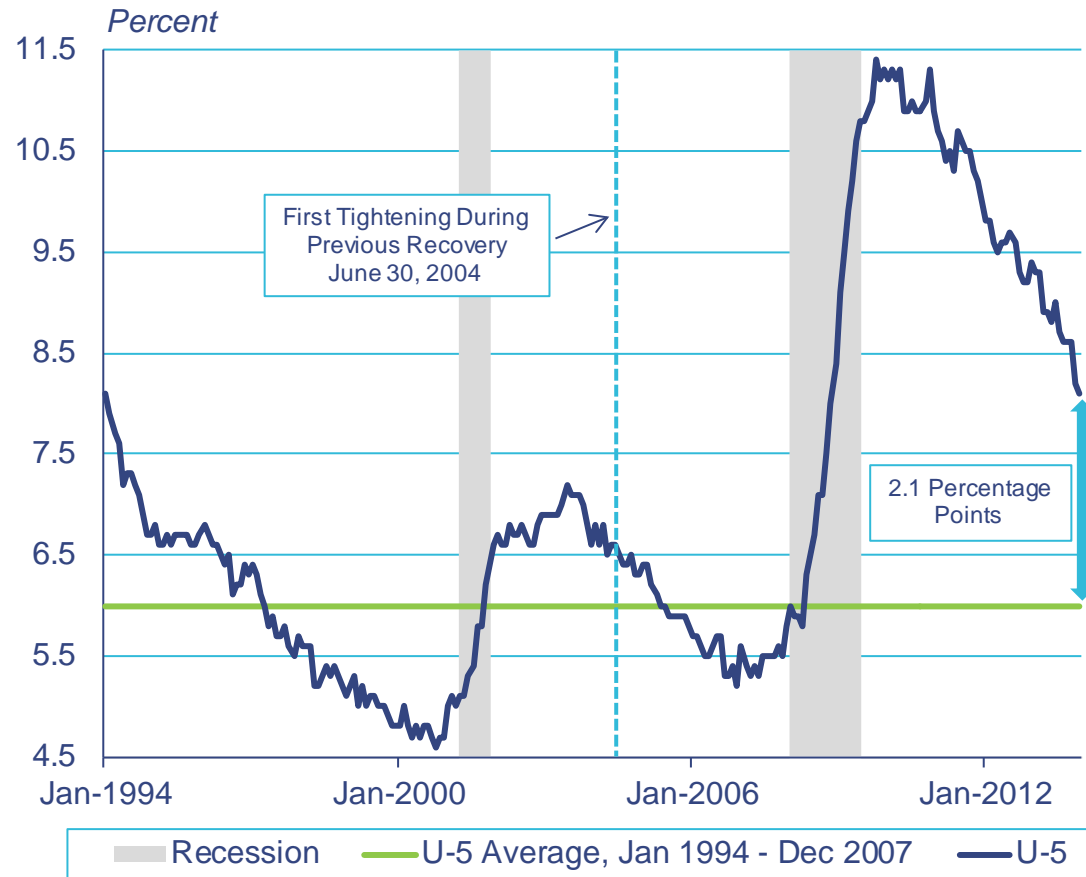


Figure 5: U-6 – Total Unemployed, Plus All Persons Marginally Attached to the Labor Force, Plus Total Employed Part Time for Economic Reasons, as a Percent of the Civilian Labor Force Plus All Persons Marginally Attached to the Labor Force

January 1994 - December 2013

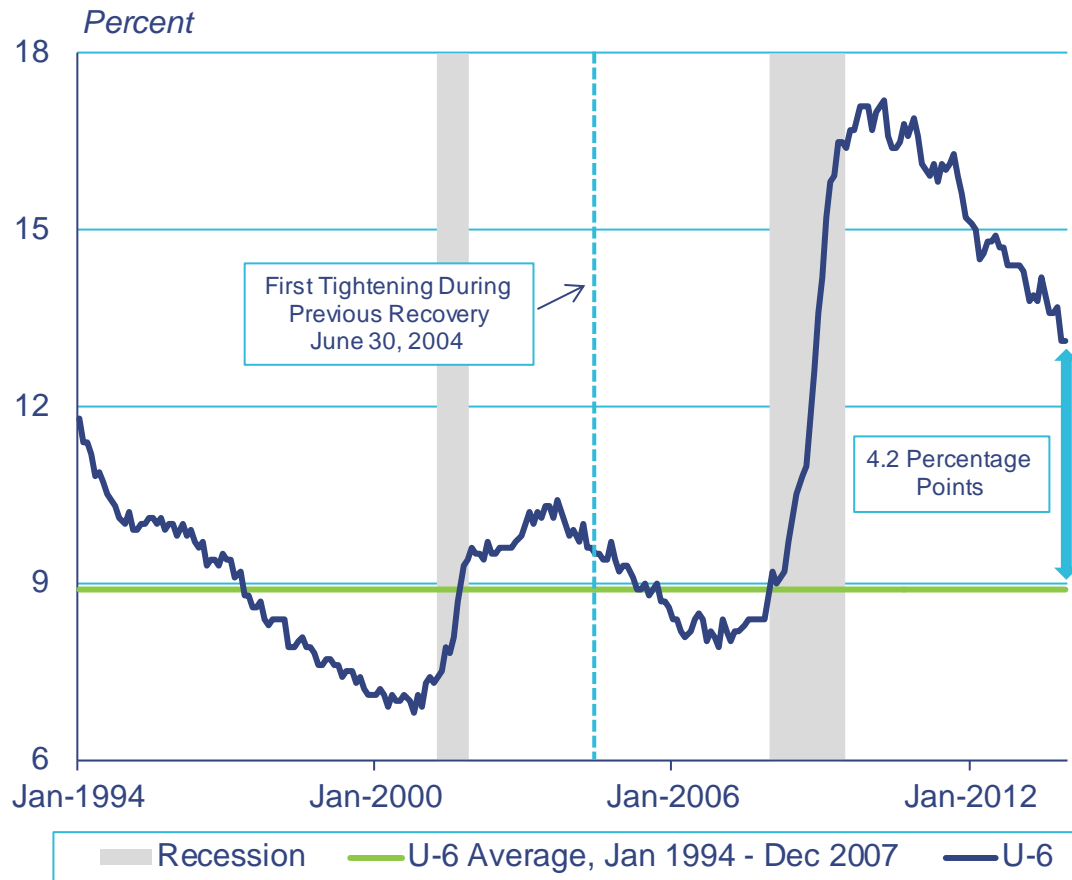


Figure 6: Alternative Measures of Labor Underutilization: Current and at Time of First Tightening During Previous Recovery

June 2004 and December 2013

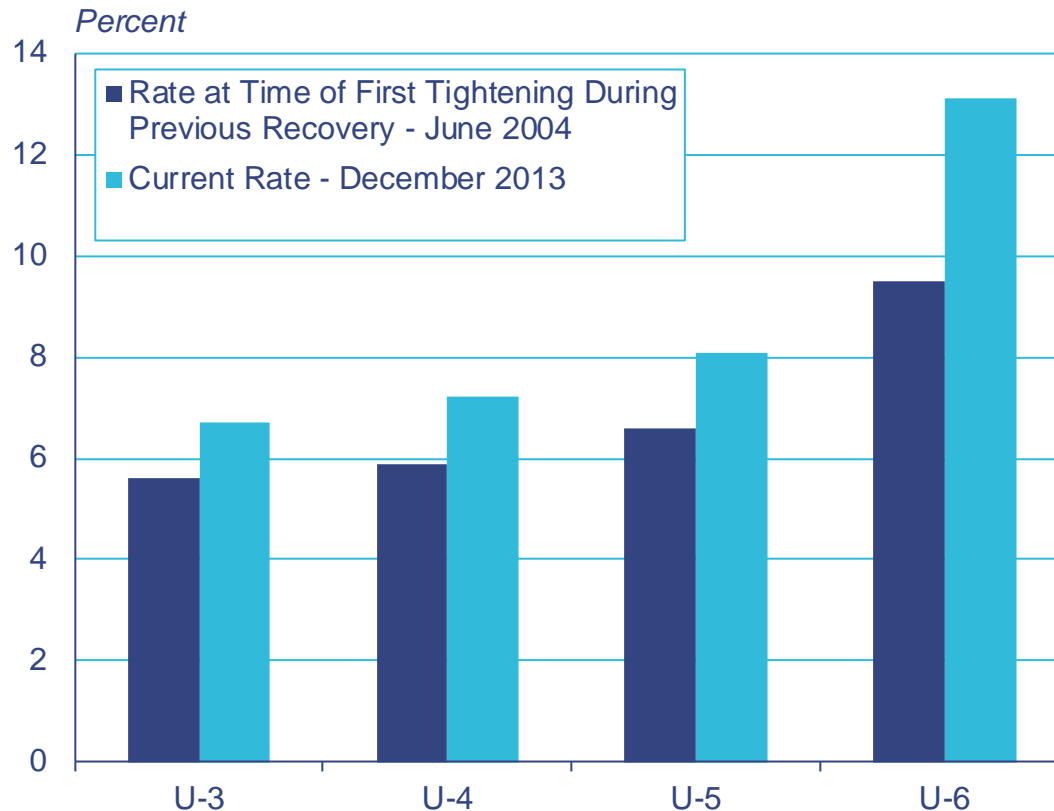
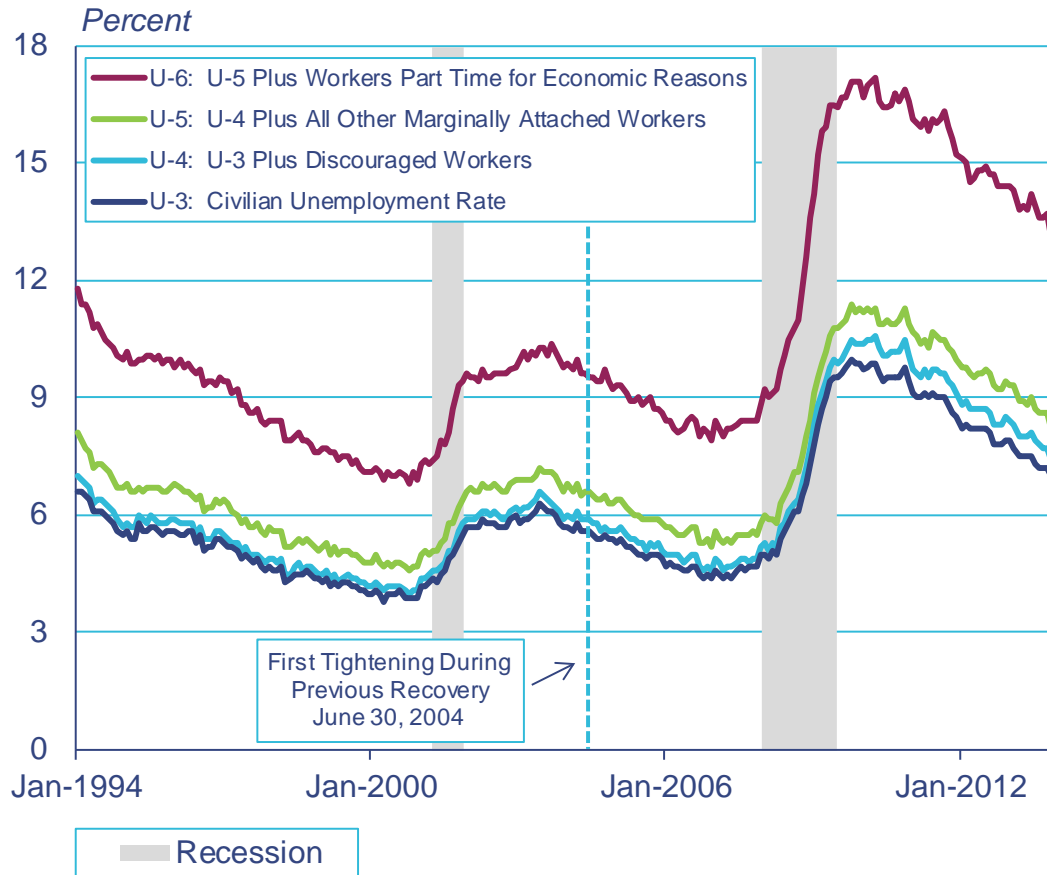


Figure 7: Alternative Measures of Labor Underutilization

January 1994 - December 2013





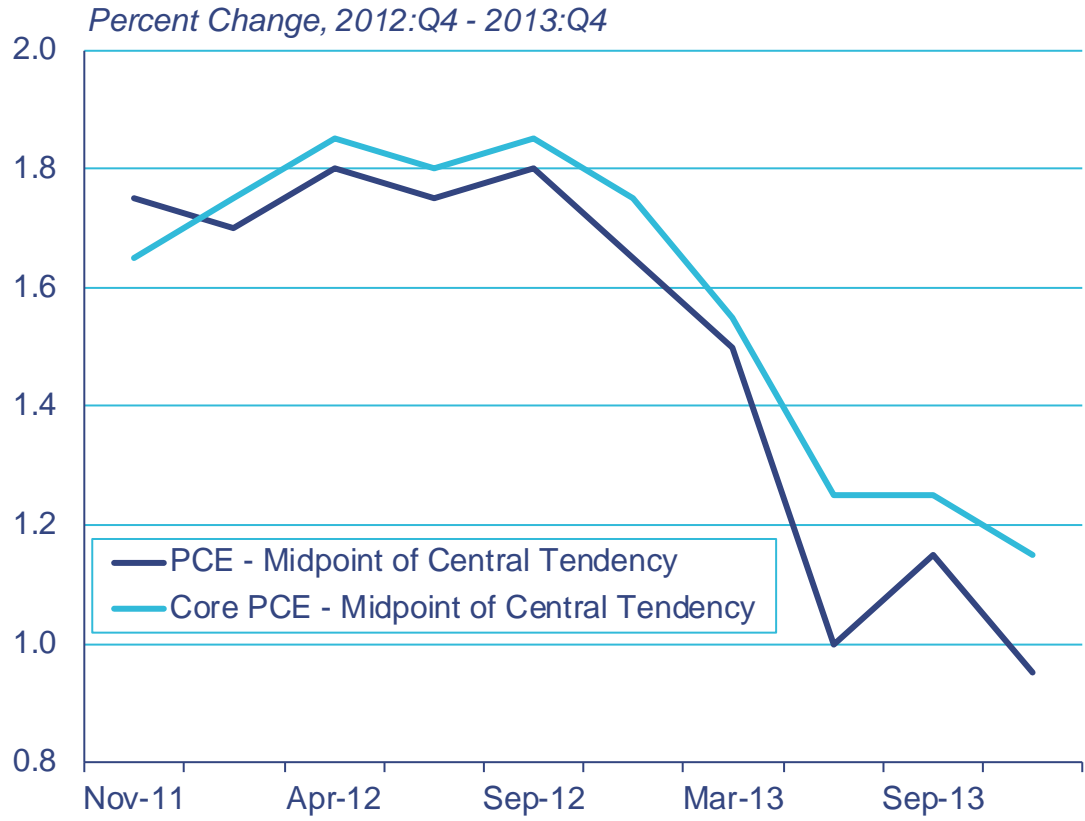
Important Questions

- ▶ Will the broader measures of labor utilization return to pre-recession levels?
 - ▶ How large an impact do these pools of underutilized workers have on wages and prices?
 - ▶ If normalization in labor markets requires returning to historical levels, then:
 - ▶ Need much more growth to absorb this large pool of underutilized workers
 - ▶ Inflation may return to target only slowly
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Figure 8: Inflation Projections of Federal Reserve Governors and Bank Presidents for 2013

November 2, 2011 - December 18, 2013

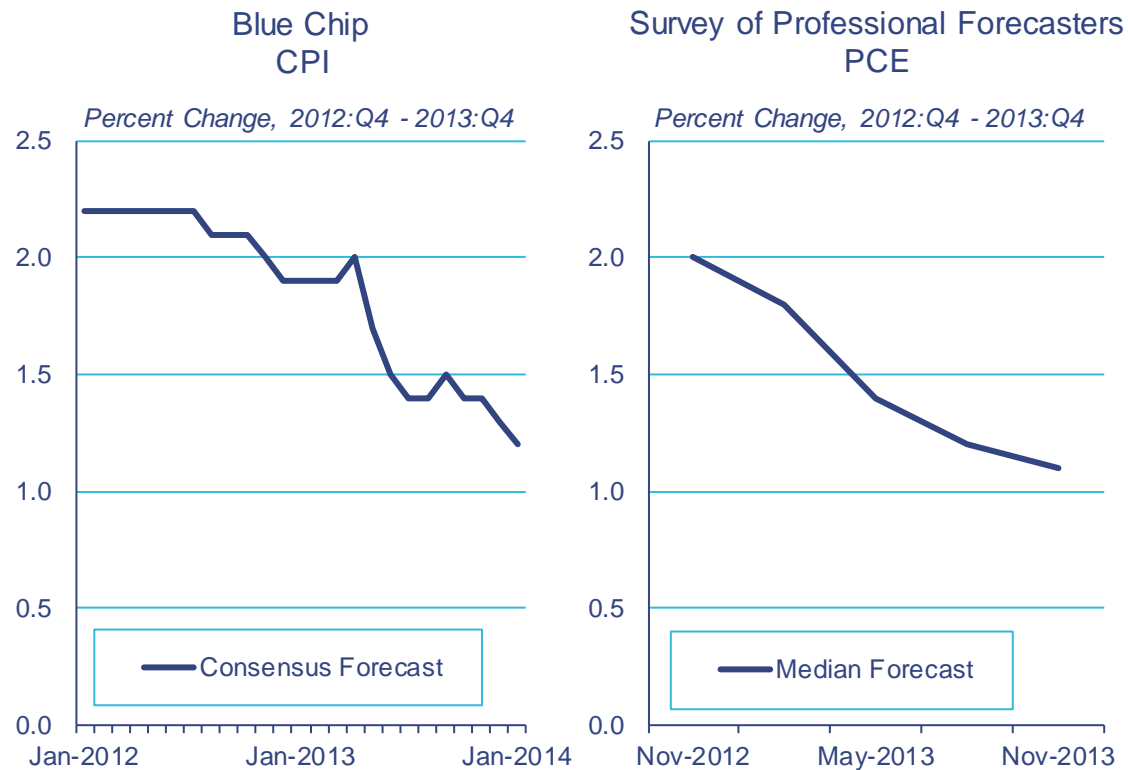


Note: Central tendency excludes the three highest and three lowest projections for each variable in each year.

Source: FOMC, Summary of Economic Projections



Figure 9: Private Sector Inflation Rate Forecasts for 2013





Implications for Structural Arguments

- ▶ Monetary policy will not effectively address structural problems in labor markets
 - ▶ Why are wages and prices so low?
 - ▶ Why has inflation returned to target more slowly than expected?
 - ▶ One potential explanation for persistently low price and wage growth may be that the broader measures of labor markets are signaling a weak labor market
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Concluding Observations

- ▶ Broader unemployment measures are much higher than they were at their peaks following the previous recession
 - ▶ Broader unemployment measures remain high relative to the traditional U-3 measure of unemployment
 - ▶ Monetary policy should focus more on these broader measures of unemployment
 - ▶ With too much labor market slack and very low inflation rates, monetary policy should continue to be highly accommodative
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