A Jobless Recovery?

Michael Mussa says the latest improved employment figures are consistent with his forecast of 5 percent growth next year, but it is still too early to say the recovery will accelerate to that pace.

Recorded December 7, 2009.

Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics with Michael Mussa, senior fellow at the Institute, to discuss the latest information about jobs and the economic recovery. Thanks Mike.

Michael Mussa: My pleasure.

Steve Weisman: In early December, a lot of people expressed surprise that the unemployment rate dropped from 10.2 percent to 10 percent. Were you surprised?

Michael Mussa: I wasn't particularly surprised. We had a large four-tenths of 1 percent increase month-over-month the preceding month. And these are numbers that—since they are based on a survey—have a kind of statistical sampling error. So, the thought that it might come down one- or two-tenths is not, I think, surprising and also not particularly reassuring just in and of itself.

Steve Weisman: Why?

Michael Mussa: You would say, well, it's only this one particular survey that's providing us with this signal. And that could be just a random statistical sampling effect. However, the establishment survey, which is a separate data source—

Steve Weisman: What is the establishment data survey?

Michael Mussa: In the household survey, they ask about 50,000 households various questions, about where they're employed or not employed. And so from establishment surveys, they get information from firms about the number of people that they are employing. And they refer to that number as the number of jobs. And they get comprehensive reports from larger firms, and then they sample a smaller firm. So, it's a different statistical base for collecting this information. And that figure also showed a surprising improvement. We had been losing around 200,000 jobs per month, and then the figure reported for November came in at only minus 11,000. And the job losses for both September and October were revised to much smaller losses than had been the case earlier. So, that series also improved both for the month and for the preceding months. And then we have an entirely separate series on claims for unemployment insurance, which is reported weekly. And the last two weeks have, for the first time in over a year, reported initial claims of less than 500,000. And it got up as high as 700,000 at the worst of the recession. So, all three government surveys that deal with employment and unemployment in jobs showed improvement beyond what people would normally expect.

Steve Weisman: You projected earlier this year that the recovery would be as sharp or as steep as perhaps as the down turn was. Do these numbers suggest that indeed, the recovery will be fairly brisk?

Michael Mussa: That's for the future. I think they removed a mystery—or at least removed much of the mystery—of why job growth remained so weak: why we were continuing to lose so many jobs in the face of an economy where other figures suggest the economy was growing 2.5 percent or thereabouts. Which normally should be enough to roughly stabilize the level of employment and slow down the rate of rising unemployment. And we weren't seeing that.

Now, with the new numbers and the revised numbers, there is much greater consistency between what the employment and unemployment data are showing us and what we've been estimating about the growth rate of the economy, which is still not in the buoyant recovery phase. In the summer, the latest estimate was we were growing 2.7 percent at an annual rate. And my forecast was about that, but I'm expecting it to strengthen to about 5 percent growth in 2010. The employment numbers certainly are not suggesting we're seeing that yet. But we'll see that, if it happens, in the employment numbers next year.

Steve Weisman: Why are the unemployment numbers so stubbornly high, even when there is a recovery? There are a lot of structural reasons, for what people call jobless recoveries in the last few recessions. What is your assessment?

Michael Mussa: Following the 2001 recession, the unemployment rate continued to rise for nearly two years after the recession was over. But the recession itself was basically an economic slow down. There were only two quarters—non- consecutive—where GDP fell, and it fell only at an annual rate of 1.5 percent. So there was virtually no downturn in output. And then I think, not surprisingly, the recovery wasn't much of a recovery either. That is to say, growth strengthened 1.25 percent for a year and a half. And that's not enough growth to get employment growing as fast as the labor force. And so, the unemployment rate continues to creep up after the recession was over.

The 1990-91 recession, which was relatively brief and mild, also didn't have that much of a downturn—though more so than in 2001—and the recovery was at a relatively tepid rate. So the job growth was weak and the unemployment rate did drift up after the recession was over, peaking about a year and a half after the formal end of the recession. If we go back to earlier recessions—which were, typically speaking, steeper and often longer—there would often be an initial quarter or two of recovery where the unemployment rate would continue to rise. And I'll get back to why that was the case.

And then as the recovery picked up speed, the unemployment rate would fall more substantially and employment growth would strengthen more. So in the Reagan recovery—which was particularly strong, beginning [in] late 1982 and extending through 1988-89—the unemployment rate peaked in November of 1982 along with the trough of the recession. And then we had a strong recovery. The first year of that recovery, GDP grew more than 6 percent and the unemployment rate fell from 10.8–10.7 percent down to 8.4–8.3 percent. So, we got a big drop on unemployment right in that first year associated with a very strong economic recovery. In contrast to the 2001 episode, we didn't have much of recession, we did not have much of recovery and the unemployment rate sort of creeped up through that process, until growth finally strengthened, beginning in the spring of 2003.

I think what we're seeing this time is: We've seen the bottom of economic activity. We've seen the start of a recovery and if—as I forecast—the recovery gathers strength up to a 5-percent growth rate in the coming year, then I think we'll see the unemployment rate come down next year from 10 or a little above 10—10.2 has been the peak so far—down to 9 percent or a little less, by the end of next year. But, as other forecasters believe, the economy remains very sluggish and we only get 2.5-percent growth, then we will probably see very little job growth. I think it'll be probably barely positive in terms of the job growth. But the unemployment rate may well continue to drift upward for a while, if we have only a very sluggish recovery.

Steve Weisman: What are the reasons for these high unemployment rates? As you just explained, partly it's because the recoveries were tepid. But aren't there other structural factors that are keeping unemployment high?

Michael Mussa: Actually the unemployment rate in the recent years has been running fairly low. We were running 4.5 percent before the recession started. The peak of unemployment in the 2001 recession was 6.3 percent, and that's very low as a peak of unemployment for relatively earlier in the postwar period. So the surge upward in unemployment is really a phenomenon of this very deep and sudden recession where we've seen the unemployment rate go up 4 percentage points over the past year.

Now, it's going to take a long time to come back down. I don't know if it will get back down to 4.5 percent again in the next decade or so, say back down to 6 percent. That's probably going to take three years or four years of recovery, even if we have a relatively vigorous recovery—as I anticipate—because it just takes a long time for the economy to adjust. There are a lot of people who have lost jobs—where those jobs are not going to come back—and they're going to need to find alternative employment, retool their skills, and so forth. They may need to move to different parts of the country. Working the unemployment rate down from very high levels takes time; there is no doubt about it.

Steve Weisman: Clearly [there are jobs] that are not coming back in obvious places— like the auto industry and some other manufacturing sectors. Has that factor accelerated? Do businesses look at recessions as opportunities to completely rethink their whole business structure?

Michael Mussa: Necessity is the mother of invention, I think, in a lot of this. Certainly as far as the auto industry is concerned. I mean, we saw auto sales decline from an annual rate of about 16.5 million vehicles on average—which has been sustained for six or seven years—down to earlier this year, about 9 million vehicles at an annual rate. So you got [a] 40-percent decline in purchases.

Steve Weisman: Is that ever going back up?

Michael Mussa: It already has gone up a little bit. I anticipate that by the end of next year we'll back up to 12.5 million or something like that. I think it will be a while before we get back up to 16 million, however.

In residential investment, we had new housing starts at the peak that were running about 2.2 million units per year. At the bottom this spring, we were barely [running] 500,000 new units started at an annual rate. We've come up 50,000–60,000, and I think by the end of next year we'll be up to about a million new units started at an annual rate. Maybe a little more than that, but still half of what we were at the peak of the housing boom. So, a lot of the constriction jobs and residential construction that have gone away are not coming back anytime soon. And in the auto industry, employment has declined substantially. Some jobs are coming back, but that industry is in secular decline as far as employment is concerned.

Steve Weisman: It's too soon to break out the champagne on this recovery. But it's also too soon to say that your rosier scenario can be ruled out. You still think that the recovery will be more robust next year than some of the other major forecasters?

Michael Mussa: Yes, I would say that the employment data we've gotten recently has now made the employment picture entirely consistent with the forecast—my forecast—that envisioned that we would bottom out around the middle of the year, then we would have modestly positive growth in the summer, and then things will begin to accelerate this quarter and particularly in 2010. We're on that path, but whether we will accelerate—there the evidence is not clear and is not going to be clear until we move forward over the next few months and see whether the growth rate does pick up. In which case I think we'll see the rate of job creation pick up, the rate of unemployment decline. It will take a while, however, to see much of an improvement in the unemployment picture. And how much we see how fast, it's going to be tied to how strong the recovery is. If we're growing at 2 percent per year we are not going to see the unemployment rate come down much, if at all. If we're growing 5 percent per year, then we're going to see a meaningful drop between the end of this year and the end of next year.

Steve Weisman: Well obviously, on that note we will have you back again to take stock. Thanks Mike.