

# HOW UNEMPLOYMENT IN THE UNITED STATES IS MEASURED

By  
BASSILIOS HOMBAS University of Athens

## 1. INTRODUCTION

The Census Bureau determines who is employed and who is not by interviewing a large sample of people every month. The sample involves about 100,000 people in every state and in the District of Columbia<sup>1</sup>.

Individuals are counted as unemployed if (1) they were not working during the interview week (called the «survey week» ), (2) they had tried to find a job during the previous four weeks, (3) they were available for work during the survey week (under due to temporary illness), or (4) if they had been laid off (even though they may have been told to report for work within 30 days).

An individual is counted as employed if (1) he or she is over 16 years of age and did a minimum of one hour' s work for pay or profit during the survey week, (2) he/she worked 15 hours or more as an unpaid worker in a family enterprise, or (3) he or she is temporarily absent from a job for noneconomic reasons ;—i.e. illness, bad weather, vacation, or a labor - management dispute<sup>2</sup>.

The unemployment rate is a percentage derived by dividing the number of people unemployed by the number of people in the civilian labor force. The civilian labor force is the sum of those employed and those unemployed. The unemployment rate for a whole year is based on yearly averages of the monthly surveys.

Of course, the unemployment rate may not give us a true picture of who is

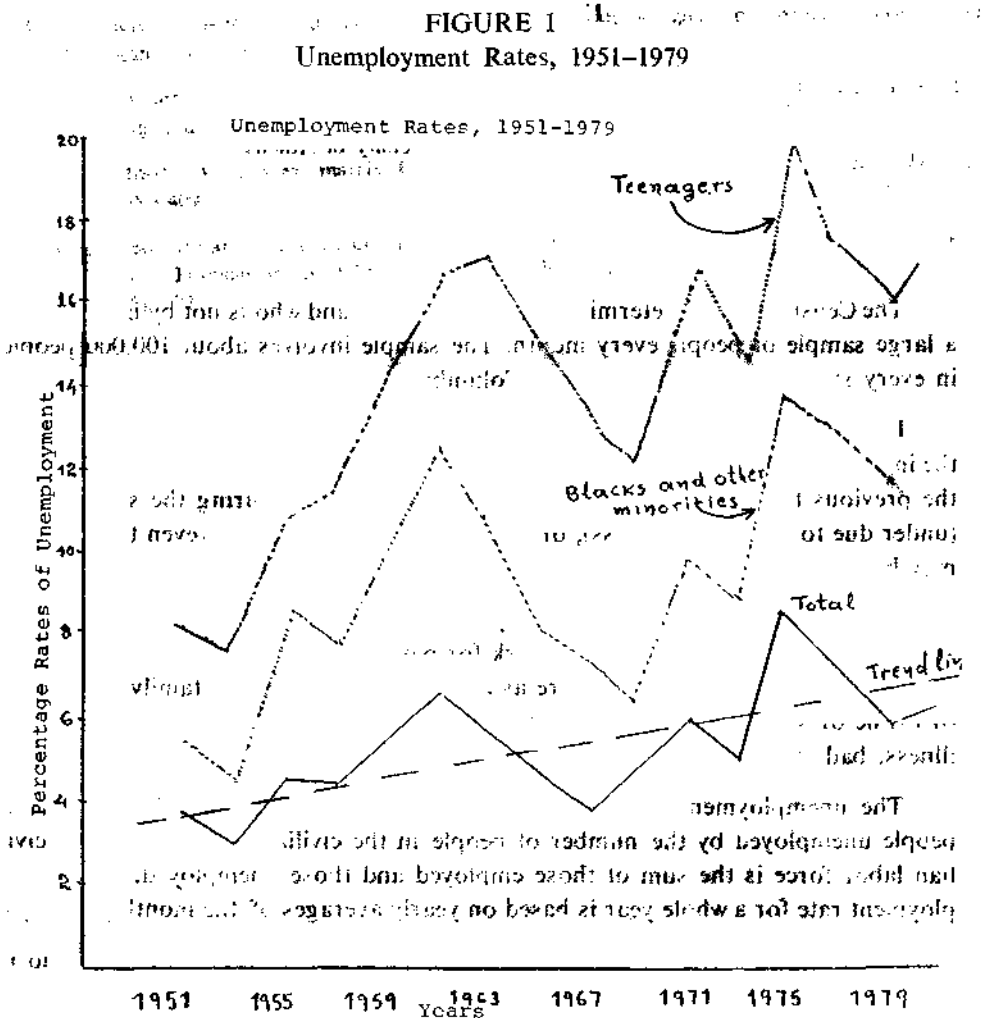
1 Statistical Abstract of the United States, 1975, p. 1.

2 Ibid., p. 340.

«really» unemployed. One person may have given up looking for work out of discouragement and will not be counted. Yet a college student only casually looking will be counted as unemployed if she or he has looked during the previous four weeks.

## 2. WHAT HAS BEEN THE RECORD ?

Figure 1 shows unemployment rates during the years 1951 through 1979.



At a first glance, the figure looks like three zig - zag lines. However, one can discern a pattern of two recessions—one in 1961 and the other in 1975. The figure also shows the drop in unemployment from 1951 to 1953 and from 1961 through 1969. In both cases the United States was involved in war ; first the Korean war and then the Vietnam war. War seems to reduce unemployment. (See Figure 1). Unemployment changes among blacks and teenagers are parallel to changes in total unemployment. This pattern suggests that, if the United States can bring down total unemployment, unemployment of blacks and teenagers will fall too. However, the experts disagree on this point, as the next section will show.

Finally, a trend line has been draun through the total unemployment data. Unfortunately, the trend seems to be up.

### 3. THEORIES OF UNEMPLOYMENT

Full employment is said to exist when the unemployment rate is less than 4 percent. Figure 1 shows that the rate has been higher than that since 1970.

There are many explanations for unemployment. Seasonal unemployment occurs when the demand for labor drops because of the season. Frictional unemployment occurs when workers change jobs. These tow types of unemployment are considered temporary and not serious.

Unemployment that is caused by generally poor business conditions is sometimes called cyclical unemployment because it is associated with the «through» of a business cycle. Monetary and fiscal policy may help by increasing aggregate demand.

More serious is structural unemployment. The term «structural» means that a particular industry is having difficulfy or that a particular group of people cannot find jobs. Structural unemployment can occur because some products are replaced by new ones (for example, the replacement of adding machines and slide rules by hand calculators, the closing of a pollution-creating factory). In other cases machines may replace labor (called technological unemployment). Hard—core unemployment is another form of structural unemployment. It refers to those who are unemployed because of the unwillingness of employers to hire minority workers, uneducated people, people without skills, or people with special handicaps.

Another form of unemployment is disguised unemployment or underemployment. Both terms mean the same thing. They mean that people are employed but are working at jobs beneath their capabilities, like mathematical statisticians

selling newspapers or Columbia University graduates washing dishes<sup>3</sup> These terms also refer to people who may be working, but in situations where they are not needed. An example is 100 people picking rice when 80 people could do the same job. The unneeded 20 people represent disguised unemployment. This kind of under-employment occurs in many less developed countries.

During the early 1960s, the great debate in President Kennedy's office was whether or not unemployment was primarily due to inadequate demand or the result of structural unemployment. The debate is important because it represented a tough question : why does the United States have high levels of unemployment in good times and bad ? Attempts to answer this question resulted in new explanations of the causes of unemployment, to be discussed below.

## New Theories of Unemployment

The new theories of unemployment are called (1) the job - search, labor - turnover theory ; (2) the human - capital theory ; (3) the dual labor - market theory ; and (4) the unemployment compensation theory. Each of these will be briefly discussed (4)

### The Job - Search, Labor - Turnover Theory

This theory is frictional unemployment by another name. Unemployment of this type occurs when a worker changes jobs. Neither the worker nor potential employers have sufficient information to bring them together. Information costs are to blame. However, research has also shown that such a worker may remain voluntarily unemployed during at least part of his or her job - changing time. It is generally not in the worker' s interest to take the first offer. The job search continues and is thought of as an investment by workers in obtaining more information about the job market. Some of this unemployment is therefore seen as voluntary. In theory, a society can reduce this kind of unemployment by lowering the costs born by job - hunters in obtaining and by subsidizing relocation.

### The Theory of Human Capital

The human - capital theorists respond to be job - search theorists by saying

<sup>3</sup> See Paul E. Steiger, «Skilled People in Unskilled Jobs - The 'Unemployed' : A Growing Class» Los Angeles Times, 20 February 1977, pt. I, p. 1.

<sup>4</sup> For a discussion of the first three theories see Stephen P. Zell, «Recent Developments of Kansas City», September/October 1975, pp. 3-10.

that the job - search theory does little to help the situation of unskilled workers who cannot get jobs even when vacancies exist and when they know the vacancies exist. The human - capital theory holds that the inability of these workers to find jobs is not the result of high information costs but of insufficient investment in their own education and training (human capital). The theory suggests, then, that the appropriate policy to reduce the unemployment of disadvantaged workers consists of extensive training and skill upgrading.

The job-search and human - capital theorists differ as to causes : the former emphasize information costs, the latter, the lack of investment in human capital, but both schools of thought propose the same cure -expanded training and programs for relocation.

### The Dual Labor - Market Theory

This theory holds that the first two theories are wrong - that we cannot assume employers will be willing to employ the unemployed as «trainees», nor can we assume that workers will be willing to accept training or relocation programs. The theory maintains that there are really two labor markets and two separate sets of problems.

The primary labor market is characterized by high wages, satisfactory working conditions, employment stability and prospects for promotion. The secondary labor market is characterized by bad jobs, low wages, poor working conditions, layoffs, little chance for advancement, and high turnover. (These jobs are often called dead - end jobs).

People unemployed in the primary market are usually in the job - search category. They are usually white males and have skills that will, sooner or later, be matched to a job.

The secondary market is another matter. Here we find minority workers, women, and teenagers. When these workers find themselves in the secondary market, they find that their employers offer little on - the -job training and that their wages differ little from those in many similar jobs. They find little incentive to stay on the job or perform well. They often quit without good reason after a short time.

A vicious circle begins. Employers have little incentive to train such workers, the workers have little incentive to learn, and employers find it easy to fire workers in whom they have invested, little.

The dual labor - market theorists conclude that, as one writer put it, the «potential effectiveness of skill training programs proposed by the human capital school (and the job search school is open to serious question».<sup>5</sup> If the labor market is secondary in nature, something else must be done. The «dualists» propose a two - pronged attack :

First, with the help of the federal government, the United States Economy should try to upgrade secondary - type jobs into jobs with primary characteristics. Examples of success in this area are long - shoring (now a skilled machine operation), unskilled construction labor (the apprenticeship system), and office cleaning (specialists handling machines).

Second, the federal government should pursue a long run, stable, full - employment monetary and fiscal policy. When employers see stop - go policies in Washington, they are reluctant to risk hiring too many people or to train them. Employers incur much less risk in hiring temporary people from the secondary market.

Unfortunately, the «dualists» also have a problem. They assume that workers in the secondary market have the desire and ability to invest the human capital needed to succeed in the primary labor market. If secondary - market workers do not have this ability or desire, government spending to help them will be wasted and will only add to inflation.

### The «New Unemployment»

Many experts now recognize that unemployment compensation is making unemployment an attractive alternative to work. Some writers call the unemployment that is induced or prolonged by unemployment compensation the new unemployment<sup>6</sup>.

The experience in Massachusetts helps to illustrate the point. With no change in the number of jobs people held in that state, the unemployment rate went from 7.5. percent in October 1974 to 11. 1 percent in October 1978 and then back down to 7. 1 percent in October 1978 and then back down to 7. 1 percent in 1976.<sup>7</sup>

How could the unemployment rate change so much when the number of peo-

5 Ibid., p. 9.

6 Martin Feldstein, «The Economics of the New Unemployment,» *Public Interest*, Fall 1973.

7 Milton Friedman, «Behind the Unemployment Numbers», *Newsweek*, 7 February 1977.

pie employed stayed the same ? The increase in 1975 is attributed entirely to any increase in unemployment benefits that became effective January 1975. The number of people claiming unemployment benefits increased thereafter by 100,000. Then, in 1976, the governor and the state legislature tightened the state's unemployment compensation, making it impossible for people who quit their jobs voluntarily to collect benefits. The result ? The Massachusetts labor force declined by 120,000 people. The number of people at work increased by 19,000 and the unemployment rate declined. National data indicate that recent U.S. unemployment policies add between 1 and 2 percent to the unemployment rate <sup>8</sup>. Another example is «the government owes me the money» attitude. A young mother of three works as a waitress six months a year in California and they collect unemployment compensation for the rest of the year. (In California, she can qualify for unemployment compensation as soon as she has earned \$750 in any three - month period.) The waitress does not feel guilty ; she feels she deserves the money her employer had paid in unemployment insurance taxes<sup>9</sup>.

The problem is that unemployment compensation is often so good that the unemployed worker has little incentive to work. Here is one example involving a working couple with two children. The husband earns \$6,000 a year, or \$500 per month. Out of that, he pays \$134 a month in income tax and social security tax, leaving a net income of \$366 per. month. But if he is unemployed for a month, he will receive \$302 in unemployment compensation that is tax free -just \$64 less than if he worked. The loss of \$64 is 12.8 percent of his gross pay of \$500. This means that if the man works, 87.2 percent (100 - 12.8) of the extra income he gets from working is lost through taxes. His extra (marginal) income is taxed at a 87.2 percent rate. So why work if one can only become 12.8 percent better off by working ? <sup>10</sup>.

#### NOTES

1. Statistical Abstract of the United States, 1975, p. 1. 2. Ibid., p. 340.
3. See Paul E. Steiger, «Skilled People in Unskilled Jobs—The 'Unemployed': A Growing Class» Los Angeles Times, 20 February 1977, pt. 1, p. 1.
4. For a discussion of the first three theories see Stephen P. Zell, «Recent Development of Kansas City, September/October 1975, pp. 3-10. 5. Ibid., p. 9.
6. Martin Feldstein, «The Economics of the New Unemployment», Public Interest, Fall 1973.
7. Milton Friedman, «Behind the Unemployment Numbers», Newsweek, 7 February 1977.
8. Ibid. 9. «A Savior or Windfall?» Los Angeles Times, 20 February 1977, **pt. VIII, p. 1.**
10. «Economic Report of the President» Transmitted to the Congress January 1980.

#### **8 Ibid.**

- 9 «**A Savior** or Windfall ?» Los Angeles Times, 20 February 1977, **pt. VIII, p. 1.**
- 10 «Economic Report of the President» Transmitted to the Congress January 1980.