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IS THE WORST OF THE RECESSION BEHIND US? HOW LONG WILL IT TAKE TO RESTORE FULL EMPLOYMENT?

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Is the worst of the recession behind us? How long will it take to restore full employment? Two questions uppermost in the minds of policy wonks in Washington, traders on Wall Street, and millions of Americans on Main Street.

No one can answer those questions with absolute certainty because the performance of the U.S. economy depends on decisions made by millions of economic agents whose behavior cannot be known in advance. The reason for that uncertainty gets down to this. In making decisions economic agents weigh what is gotten through market exchange versus what is given up-- they attempt to calculate the individual gain derived from the decisions before they make them. If they expect to gain more by waiting and there are many who decide to wait, their waiting becomes a drag on the economy. For that reason, we can answer our opening questions only with educated guesses.

Three sets of data on recent labor force developments supplied by the Bureau of Labor Statistics *suggest* that the worse may be over. First, the number of employed adult men, adult women, and teenagers each hit bottom in December. Second, the number of unemployed adult men and jobless teenagers both peaked in October. The number of adult women who were unemployed peaked in December. Third, the unemployment rate for adult men and for teens both peaked in October. For adult women, the jobless rate peaked in December.

What we don't know is whether the economy will tank in the months ahead or continue to recover. Mayo Research Institute comes down on the side of recovery.

Regarding the second question as to how long it will take to restore full employment, we argue with somewhat greater confidence based on BLS data over a much longer period of time. We would have preferred to use the Great Depression of the 1930s as our benchmark, but there are no comparable and reliable data on employment and unemployment prior to 1941. For that reason we take as our benchmark the recession of the early 1980s which was the first time in the history of the BLS data series launched in 1941 that the unemployment rate topped 10 percent.

The jobless rate hit 10.1 percent in October 1982, peaking at 10.8 percent two months later, and remained above 10 percent for seven more months. The rate finally dropped below double

digits in July 1983. Joblessness reached double digit levels because in order to bring inflation under control the Federal Reserve pushed the prime rate of interest in 1980-81 above 20 percent.

Economists generally agree that an unemployment rate of 3-4 percent is indicative of full employment. The historical record shows that the rate of unemployment fell and stayed below 5.0 percent in July 1997, which is *more than 14 years* after it peaked at 10.8 percent in December 1982. It took until September 2000 for the jobless rate to fall and remain below 4.0 percent. However, it dropped only to 3.9 percent rising above 4 percent in January 2001. Joblessness remained in the 4-5 percent range until August 2008 when it climbed to 6.1 percent.

This evidence indicates that it will take *many* years for joblessness to drop from the current 9.7 percent level to a much more acceptable 5 percent. To get that rate to the 4 percent level will take even longer. The last time joblessness dropped below 3.9 percent was in 1969.

The problem for economic policy makers is this. With interest rates at record lows, it simply is not possible to stimulate the economy through monetary policy. With the public debt at more than \$12 trillion and rising for years into the future, boosting aggregate demand in Keynesian fashion through more federal spending faces stiff resistance from fiscal conservatives. Stimulating aggregate supply through tax cuts as recommended by supply-siders runs amuck of progressives who oppose those cuts on grounds that they help only the rich. Moreover, over-stimulating the economy runs the risk of setting off a round of inflation.

While it is not clear what direction we should take to restore full employment, the current recession has taught us one important lesson. Even for an all-powerful federal government restoring full employment following double-digit joblessness does not come quickly. It's a particularly tough lesson for millions of jobless Americans who need work now and cannot afford to wait for the economy to turn around.

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