COMMENTARY ECONOMICS

Have You Seen the Missing Workforce?

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Today's Labor Department report revealed that the jobs engine that is driving the American economy sputtered in January—with more progress on unemployment needed to reach millions of uncounted jobless Americans who are ready to work.

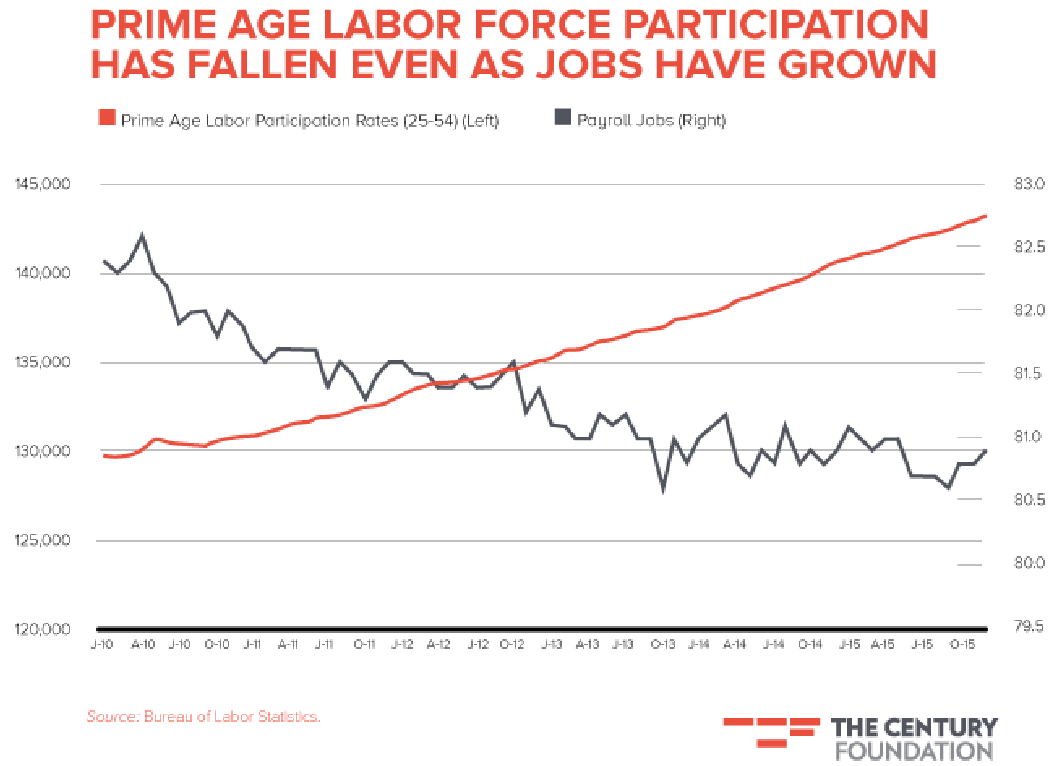
Job growth in January fell significantly short of the revised average of 279,000 in the fourth quarter of 2015 This level of job growth is consistent with an economy that is plodding ahead at a slower rate in 2016, than at the end of the last year. This was driven by a startling decline in service sector jobs, which had been the big success story in 2015. Confirming reports earlier this week of slowing service business growth, hiring in service jobs slid to 118,000 jobs after averaging 232,000 in the fourth quarter of 2015.

The slowdown in job growth is coming just at the time when Americans appear to be gaining some leverage in the job market, with positive signs throughout the report. Weekly earnings grew by $6.67 in January and are up by 2.54 percent over the last year, after gaining little in December. Below-trend inflation, driven by cheap gas, is making it possible for workers to feel the benefits of pay gains (that are still far short of what is needed to make up for years of slow growth). The Federal Reserve has not yet indicated it would change its plan to raise interest rates—the level of job and wage growth reported today by the Labor Department still gives little credence to worries that wages would drive up inflation in the economy. If anything, the question is when and if there would be enough labor market pressure to drive consistent and substantial real gains in earnings.

Why? Wages are still not climbing in the way that they should in an economy delivering a full-employment-sounding unemployment rate of 4.9 percent—a rate that should be celebrated and is the lowest reported since February 2008. The unemployment rate has been at or below 5.0 percent for the past four months, bu employers don't yet seem obliged to consistently jack up pay to keep or attract workers. And, those who are unemployed are still facing a tough journey back to work, with 28.9 percent out of work for twenty-seven weeks in January (a figure that is well short of the 16 percent rate reached during the last economic recovery in October 2006, and the highest report since May of last year).

The unemployment rate has rarely so badly masked the slack in the labor market. While the unemployment rate is now staying near its pre-recession levels, the labor force participation rate (either working or looking to work) is down 4 percentage points from the start of the recession, despite ticking up to 62.7 percent in January.

Many of those not counted in the official unemployment and labor force tallies in fact want to work—and this group represents the nation's phantom workforce. A recent analysis by the Center for Economic and Policy Research shows that increasing numbers of newly hired individuals were previously out of the workforce altogether. That's a good sign, meaning employers are now working hard to reach those who have been on the sidelines—including large numbers of individuals who were officially unemployed and simply gave up looking after being out of work for so long. This unique "out of the labor force" trend among prime-age workers demonstrates how badly the unemployment rate is now measuring labor market slack.



A close look at the prime-age workers (25–54) illustrates this point. The labor force participation rate of prime-age workers (25–54) has been at or below 81 percent since 2012, even as the nation's employers have consistently added jobs. (See the figure above.) Meanwhile, the working age population has surprisingly grown by nearly a million individuals over the past three years, despite conventional wisdom about demographic trends. If labor force participation was back at the 84 percent pre-recession level for prime-age workers, there would be 2.8 million more of them in the labor force—a figure that matches up to the job gap that the Hamilton project has found. We can imagine many public policies (like paid family leave and criminal record reforms) that would make it more possible for all prime-age Americans to work. But the bottom line is that those counted out of the labor force are in fact ready to work when jobs are available.