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IWS Issue Brief - Wanted: Jobs

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IWS Issue Briefs

Wanted: Jobs

The debate over job creation used to be simple. When government leaders decided it was time to stimulate economic growth and thus levels of employment, they chose from two distinct but interlocking tool sets: fiscal and monetary. Often blending elements of both – targeted tax cuts for consumers and increased public spending (fiscal) with lower interest rates and more dollars in circulation (monetary) – policy makers aimed for a result that balanced greater output of goods and services, low levels of unemployment, and stable prices.

That approach served our economy well through the growth and recession cycles in the decades following World War II. But today, the new world economic order (i.e., the explosion of trade, foreign competition, and international capital flows) and the surge of technological know-how have complicated the assumptions upon which the traditional policy prescriptions were based. Almost three years after economists officially declared the end of the last recession, job creation remains sluggish and inconsistent despite a steady up-tick in economic activity. If history were to be an accurately predictive guide, an economy growing at a 4% annual rate, as the U.S. is now doing, should be churning out roughly 225,000-250,000 additional payroll lines a month, or nearly 3 million new jobs annually; between September 2003 and June 2004, the monthly average has been 150,000, a statistic buoyed by particularly strong gains posted in the spring. It is worth noting that just keeping even with the natural increase in the working-age population requires the creation of about 140,000 new jobs each month, or 1.7 million a year.

Policy makers and political leaders have been frustrated at every turn. A series of individual and corporate tax cuts, massive spending on security and defense, and record low interest rates have failed to ignite the jobs-creation machine. Although the unemployment rate has fallen to 5.6% from the June 2003 peak of 6.3%, at least some of the improvement reflects increasing numbers of people dropping out of the work force because they despair of finding jobs. Indeed, the labor force participation rate, i.e., the number of people working or actively searching for work as a percent of the working-age population, has dipped to 66% compared to the recent high of 67.3% in early 2000. The number of people out of work longer than six months now stands at 1.8 million, down from the high of 2.1 million in September 2003, but still more than double the number of two years ago. And while the Bureau of Labor Statistics' (BLS) Current Population Survey indicates there are a record 139 million people at work, up from 137.7 million in June 2003, the economy has yet to replace all the 2.7 million jobs that have disappeared since early 2001 or fully absorbed the 3.6 million-person net increase in the labor force.

To be sure, dynamic and open economies like that of the United States are always producing jobs and destroying others. Innovation and entrepreneurship seed new industries even as existing industries mature and contract. Productivity growth and international trade further fuel the evolutionary process. Over the past five decades, for example, manufacturing lost pride of place in the U.S. economy. Data from the Bureau of Economic Analysis shows that factory output now accounts for a mere 12.7% of gross domestic product (GDP) compared to 29.5% in 1953. The number of manufacturing jobs shrunk by 20% between 1997 and 2003 and a recent BLS survey found that nearly one-third of the 5.3 million workers with at least three years' tenure who were laid off between January 2001 and December 2003 had held jobs in manufacturing. Meanwhile, the share of the economic pie produced by services, including retail, transportation, financial, information, and high-tech, has been steadily climbing; last year services generated 68.1% of GDP.

Despite the expansion of sectors such as bio-technology, telecommunications, and healthcare, something is clearly out of whack. Jobs are disappearing faster than new ones are popping up. It used to be that less skilled jobs were displaced by more skilled jobs as technology and efficiency gains worked their way through the system. At the same time, the total number of jobs increased as the overall economy grew, providing employment opportunities for the vast majority of displaced workers, many of whom gravitated to the burgeoning service and technology sectors and retrained for new careers. But now, two trends are converging: jobs at the top half of the skill ladder are vanishing without any strong signal about which "boom" industries will emerge to absorb the growing pool of skilled, professional unemployed workers while service sector jobs, following the path first trod by manufacturing, are disappearing into the fog of productivity gains and foreign outsourcing. Net new jobs are cropping up in retail, temporary help services, and leisure and hospitality, but these are often low-skill, part-time, low-wage jobs – not the type of work that can long sustain an affluent, consumer-oriented society or generate enough demand for goods and services to soak up the steadily rising supply of labor. The BLS recently reported that 57% of the "long-tenured" workers who lost their jobs during the past three years but found new ones were earning less than they had previously.

The current bout of new-jobs malaise is keenly felt among college-educated and middle-income wage earners. Anecdotal and media reports attribute much of their dilemma to offshoring, i.e., the practice of sending jobs overseas (where workers are paid substantially lower wages). This phenomenon has been particularly visible in the customer services field, where call centers and similar operations have moved to locales as distant as India. Back office and technology service work, including the reading of medical X-rays, is also being exported, as are demanding and high-skilled software design and engineering jobs. But how much blame for the economy's anemic job creation can be placed on offshoring is not clear. Existing statistics are neither refined nor conclusive but they do suggest that offshoring is not the prime cause. Forrester Research, a technology research company, estimates some 300,000 of the 2.7 million jobs lost during the past three years were shipped overseas and that another 3 million more may be exported by 2015. Economists from University of California-Berkeley take a more dire view, predicting that 14 million U.S. jobs, or 11% of the total, are at risk of moving beyond our national borders.

Economists are generally agreed that the dearth of hiring reflects several factors. One is the business community's aversion to risk that evolved in the wake of the dot-com bust of the late 1990s, the 9/11 terrorist attack, the recent spate of high-profile corporate scandals, the war in Iraq, the ballooning federal deficit, and the steadily rising cost of health care benefits. Another is the trend within the corporate community to retain earnings, now at near record levels, instead of investing in new hires or improving employee compensation. According to the BLS, average pay for production workers, after accounting for inflation, is not much changed from levels reported in October 2001. Average weekly earnings for nonsupervisory workers rose 1.7% this past year, a rate of increase that that barely kept pace with inflation.

Of course, employers are under no pressure right now to pay workers more because the job market is sufficiently slack and full up with available talent. And herein lies the root of the job creation shortage. Employers are doing just fine with less; that is, they are getting more work out of fewer workers. Some would argue they have little choice. International trade, with its unrelenting pressure from lower-cost foreign rivals, has forced American companies to seek savings and efficiencies at every stage of the production process. Technological advances that reduce the need for labor, generate savings, and speed up production all facilitate employers' efforts to meet financial, quality, and quantity targets. In the current business cycle, an unusually strong and sustained surge in productivity that began in 2001 has taken the urgency out of adding to payrolls even as the pace of economic activity picks up. Labor force productivity soared 4.2% in the 2001-2003 period compared to the average 1.4% yearly gains recorded from 1973-1995 and the 2.5% increases generated in the second half of the 1990s. Economists figure that each percentage point increment in productivity is paid for by the loss of 1.3 million jobs.

This being a presidential election year, the job creation quandary has taken on a partisan cast. The Bush administration has consistently issued over-optimistic jobs-growth forecasts that have subsequently been retracted. Still, the president hasn't veered from the supply-side approach to economic policy that he laid out early in his term: tax cuts for individual and corporate taxpayers (especially the wealthiest), incentives for small businesses to invest in capital equipment, and regulatory and tort reform. The underlying assumption in the Bush plan is that more capital in the hands of business and fewer constraints on doing business will inevitably lead to more jobs. Sen. John Kerry, the Democratic challenger, is pushing a demand-side approach that aims to generate jobs by giving more Americans more money to spend. The senator's plan would redirect tax cuts toward the middle and lower rungs of the income ladder, close tax loopholes (including those that effectively reward companies that rely on overseas labor), offer employers incentives to create new jobs, and lower the cost of health care premiums.

But given the confluence of world events and economic trends, the right antidote to weak job growth has yet to be found. Even academic economists are unsure how much of which cures to apply. The research literature offers scant evidence to support the efficacy of government spending as a prod to near-term job creation. Researchers are likewise unsure about the long-term impact of tax cuts. The stimulative monetary policy pursued by the Federal Reserve Board during the last couple of years substantially lowered the cost of capital but has been only minimally effective on the jobs front.

Unlike economic recoveries that typically generate gains all around, this one has sidelined a lot of people. Companies may be reaping the benefits of higher productivity and consumer confidence may be sustained by relatively steady prices, but many thousands of people cannot find steady employment at decent wages and thousands more cannot find high-skilled professional jobs that suit their talents and expertise. An array of factors and forces has rendered the usual policy tools obsolete. Short of a total re-imagining of the theories underlying job creation and the political will to implement remedial strategies, the jobs conundrum will be more than just an abstract economic problem.

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