UNEMPLOYMENT & LABOR FORCE STATUS

LABOR FORCE STATUS

Out of the Labor Force

- No Job & Not Looking
- Includes Discouraged Workers

In the Labor Force

- Employed
  - Working for Pay in External Setting
- Unemployed
  - No attachment to job but want a job

MEASURES OF LABOR FORCE STATUS

- Unemployment Rate
  - \( U = \frac{\text{unemployed}}{\text{LF}} \)
- Labor Force
  - \( LF = \text{employed} + \text{unemployed} \)
- Labor Force Participation Rate
  - \( LFPR = \frac{\# \text{ LF}}{\# \text{ adult population}} \)
### EXAMPLES OF LABOR FORCE MEASUREMENTS

<table>
<thead>
<tr>
<th></th>
<th>Base</th>
<th>Good</th>
<th>Bad</th>
<th>Bad</th>
</tr>
</thead>
<tbody>
<tr>
<td># U</td>
<td>5</td>
<td>10</td>
<td>3</td>
<td>7</td>
</tr>
<tr>
<td>LF</td>
<td>100</td>
<td>110</td>
<td>98</td>
<td>100</td>
</tr>
<tr>
<td>LFPR</td>
<td>.67</td>
<td>.73</td>
<td>.65</td>
<td>.67</td>
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<tr>
<td>U Rate</td>
<td>.05</td>
<td>.09</td>
<td>.03</td>
<td>.07</td>
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### FOUR TYPES OF UNEMPLOYMENT

- Frictional
- Structural
- Deficient Aggregate Demand
- Seasonal

### TYPE 1: FRICTIONAL

- Unemployment associated with movement between jobs
- “Search” unemployment
- Dynamic nature of the labor market
- Part of “NAIRU” - Natural Rate of Unemployment
- Non accelerating inflation rate of unemployment
- Policy: Lower search costs
TYPE 2: STRUCTURAL UNEMPLOYMENT

- Arising from mismatch between characteristics of job vacancies and job seekers
  - Geographical
  - Skills mismatch
- Failure of labor market assumptions
- Policy: Training, relocation

TYPE 3: DEFICIENT AGGREGATE DEMAND

- Associated with business cycle: Insufficient product demand
  - Can be regional or economy-wide (recession)
  - Based on downward sticky wages
- Policy: Stimulate product demand

Unemployment - Inflation Trade-Off

- Phillips Curve:
  - When unemployment decreases, prices increase
- Mechanism:
  - Exogenous increase in spending $\Rightarrow$ increased aggregate demand $\Rightarrow$ increased employment/decreased unemployment $\Rightarrow$ price increase ($\Rightarrow$ increase in wages)
The Phillips Curve

Inflation Rate

Unemployment Level

COSTS TO HIGH UNEMPLOYMENT

1. Pure Economic Loss
   - Decline in product demand ⇒ investment
2. Human Capital Loss
   - Lower investment, depreciation, less mobility
3. Equity Loss
4. Psychological Costs

COSTS TO INFLATION

- Cost depends on whether inflation proceeds at steady, predictable rate or is volatile.
- All are buyers and sellers
- Costs under steady inflation: Problem only when price of products one buys rise faster than what one sells
- Costs under variable inflation: Creates windfall profits & deadweight losses
Stock v. Flows

- Stock
  - Masks movement, implying more static condition of labor market than exits
  - Labor force status measured at one point in time

- Flows
  - Movement between labor force statuses:
    - E→U
    - E→N
    - U→E
    - U→N
    - N→U
    - N→E
  - Better picture of labor market dynamics

Unemployment Rate 1994-2004

Employment to Population Ratio, 1994 - 2004