Strong Growth and a High Employment Level in the USA

The past four years have once again shown that the American economy is able to create a large number of new jobs in a short space of time following a recession. Since the start of 1992 US employment has increased by 8.2 million persons; this is more than 7% compared with the nadir of the recession in 1991. The volume of employment is at a new record. The unemployment rate fell by 2 percentage points to 5.5% during the same period. It is thus currently at a similarly low level to that prior to the last recession. Although the scale of American employment creation is impressive, as in the 1980s the question needs to be addressed whether the newly created jobs offer only relatively low incomes. An analysis of sectoral employment trends shows, however, that this is not generally the case.

Dynamic employment growth

In order to determine the true extent of the increase in employment, it is necessary to analyse the volume of total working hours, the product of the number in employment and average working hours.[1] The figures show that the volume of working hours in the USA has increased virtually constantly since 1980 (cf. figure 1). The upward trend was interrupted only in the two recessionary phases at the start of the 1980s and 1990s: both these "dips" were quickly overcome. Although the 1991 recession led to a perceptible decline in the volume of working hours, the pre-recession level was more than regained as early as 1993. This is in stark contrast to labour market developments in Germany, where the volume of working hours has remained virtually constant since 1980. Only by virtue of the boom that followed German unification did the volume of working hours rise significantly, and this proved only temporary.

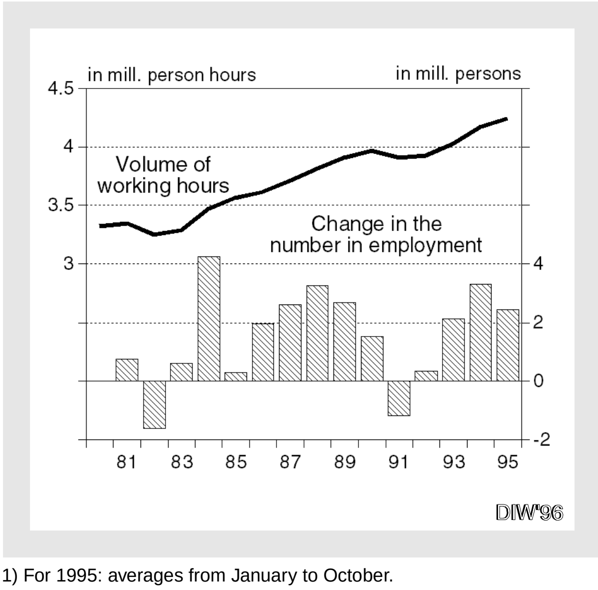
A look at cyclical economic developments in the USA reveals a close correlation between changes in total output and in employment (cf. figure 2). Both during the 1980s and in the most recent business cycle, employment trends followed the business cycle with only a short time lag. The employment trend was slightly more positive in 1981/82 than in 1992/93 (cf. figure 3). The cyclical decline and the subsequent recovery until the pre-recession level of output was reached lasted approximately the same length of time in the two recessions. Yet in the early 1980s employment had returned to its level at the start of the recession within about one quarter of the start of the recovery, approximately 12 months earlier than in the recent crisis.

Over the same period the US economy generated very little productivity growth. Thus while the employment problem steadily retreated into the background, real earned incomes rose only slightly.

Once output began, at the end of 1991, to grow once more, not only the volume of working hours, but also the level of employment began to rise as early as the first quarter of 1992, although initially very modestly. It took until around the start of 1993, i.e. around four quarters, until the same number of people were in employment as prior to the recession. Since then employment growth has accelerated.

Even in the USA, the initially hesitant expansion of employment in 1992 at the start of the last upturn led to fears that an era of "jobless growth" had begun. Yet this view has not only been contradicted by subsequent developments, it also suffers from weaknesses at a more fundamental level. There is no reason, for example, to

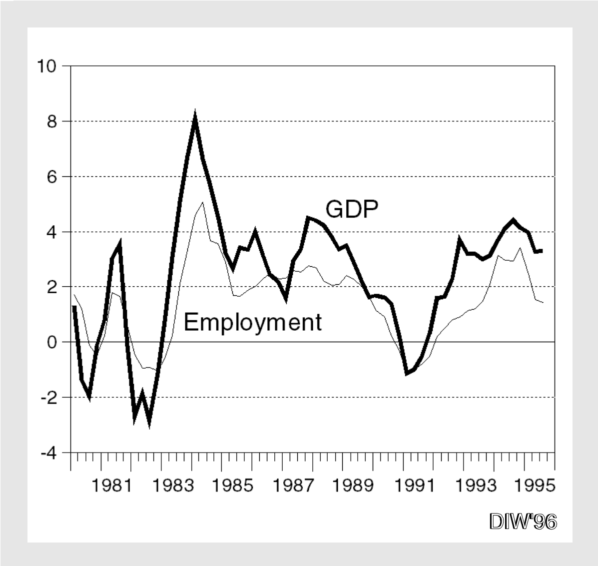
Figure 1
Employment and Volume of Working Hours in the USA 1980 to 1995



1) For 1995: averages from January to October.
Sources: US Department of Labor, Employment and Earnings.

[1] The volume of working hours was calculated here as the product of non-farm civilian employment and average weekly working hours. Thus this variable indicates the average total volume of hours worked per week in a particular year.

Figure 2
GDP and Employment Change in the USA
% change on the same quarter the previous year



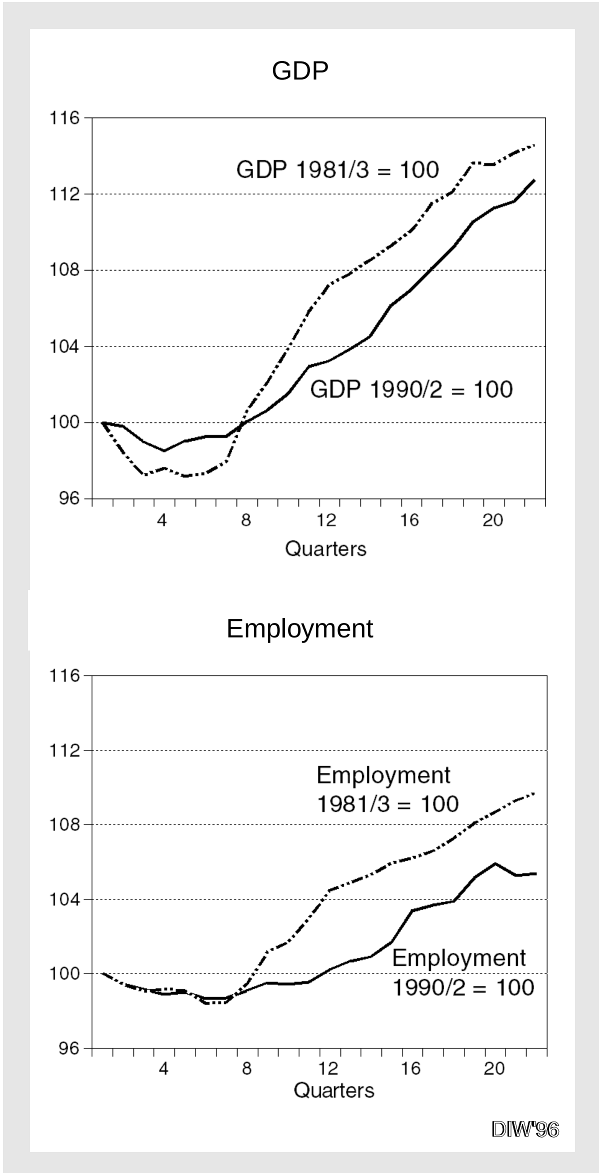
Source: OECD, Main Economic Indicators.

expect the relationship between economic activity and employment to be particularly close at the start of a recovery. After all, as developments in the last two recessions in the USA show, in the recession employment initially falls to a less than proportionate extent due to adjustment time lags. Firms, though, are continuously attempting to improve their competitive position through rationalisation. When output begins to pick up firms, keen to reap the harvest of their rationalisation efforts, will not recruit additional labour until output has returned to its pre-recession level. Indeed, output must generally be significantly higher, as was the case in the USA in 1993. This means that the relationship between economic growth and employment is only slightly positive, or actually negative at the start of an upturn, whereas productivity growth is already high. It is this observation that frequently leads to the diagnosis of jobless growth. Yet this phenomenon is merely a necessary phase in the course of a business cycle, during which corporate profitability improves significantly as firms benefit from their higher productivity. Only if this phase is successfully mastered do firms expand their investment and so create the basis for a dynamic upturn to be maintained.

Lasting and significant growth is required – as is again shown by US developments – for employment to increase perceptibly. Once growth rates have peaked, when the rate of productivity growth begins to decline, employment growth can actually be more than proportional, because of firms' delayed reaction to the cyclical weakening. Although the economy has already begun to cool down, job creation continues. It is not until this phase that it becomes apparent whether an economy will be able to keep its employment problems under control: it will not be able to do so if the upturn breaks off too early. The USA managed to avoid this danger in both the early 1980s and 1990s. This is the central reason behind the impressive employment growth in the USA in comparison to Europe.

The above considerations point to the prime importance for employment of an economic policy that makes

Figure 3
Cyclical Change of GDP and Employment in the USA

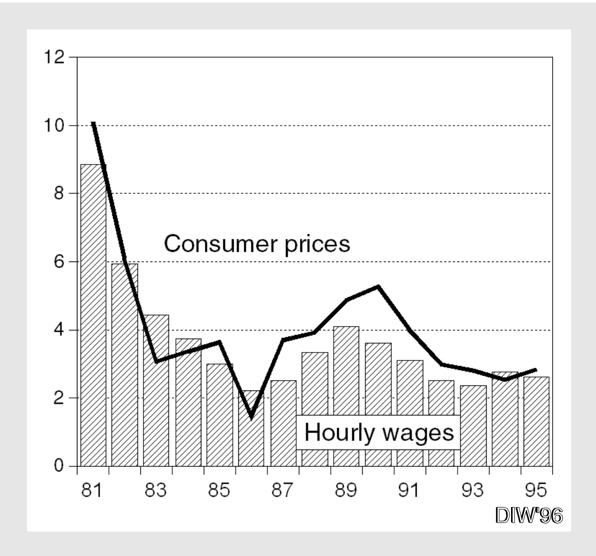


1) For 1995: averages from January to October.
Source: US Department of Labor, Employment and Earnings.

full use of the scope for expansion. In recent years the US economic policy stance has been virtually continuously expansionary. During the 1980s it was fiscal policy that played the leading role, providing a sharp expansionary impetus, in particular due to the sharp rise in defence spending and cuts in taxation. This was, however, not only the motive force behind the strong upturn, but also the root cause of the uncontrolled increase in the budget deficit, which subsequently seriously curtailed the scope for fiscal policy action. Consequently, the recent upturn is primarily the result of an expansionary monetary policy which, between 1990 and the start of 1994, stimulated – with the usual time lags – the economy with low interest rates over an extended period, and thus made a major contribution to employment growth.

Yet this would not have been possible had not wage trends been largely conducive to the attempts by economic policy makers to ensure low inflation. Following the deflationary phase at the start of the 1980s, wage rates increased only moderately until 1988 (cf. figure 4). Thus the expansionary impulses provided by fiscal policy were able to take effect against the background of declining inflation. Not until 1988 and 1989 did wage growth and, consequently, price inflation accelerate. This induced the central bank to adopt a restrictive stance to avert the threat to price stability. Given that in its attempt to consolidate the budgetary position, US fiscal policy also moved over to a restrictive course, the stabilisation recession of 1990/91 was inevitable. Since then wage growth has remained moderate despite the favourable employment situation. There are no signs at present of a renewed threat to price stability. There is much to support the view that the current upturn, and with it the expansion of employment, will continue, albeit at a moderate pace.

Figure 4
Hourly Wages and Consumer Prices in the USA
% change on the previous year



Sources: US Department of Labor, Employment and Earnings; DIW calculations.

Figure 5
Unemployment Rate in the USA
monthly, seasonally adjusted

Source: OECD, Main Economic Indicators.

Low unemployment

These positive trends are also reflected in a decline in unemployment (cf. figure 5).[2] The labour market situation is currently just as favourable as at the height of the previous cycle.[3] This means that in the course of the dynamic upturn enough jobs have been created not only for the unemployed, but also to absorb much of the substantial influx of labour – amounting to around 1% of the labour supply p.a. – on to the US labour market.

[2] The figures for the unemployment rate given here are not directly comparable with the official unemployment rate in Germany. A comparison of the rates in the two countries has to be based on the standardised rate calculated by the OECD which, in the case of Germany, is around 1.5 percentage points lower than the official national rate.

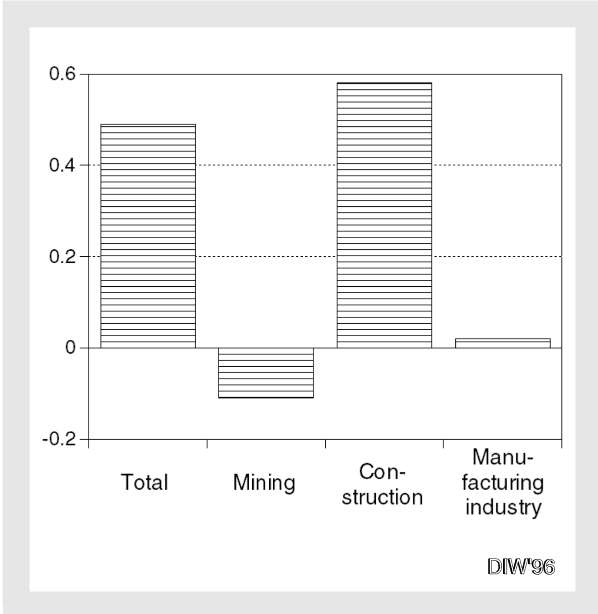
[3] In interpreting figure 5 it should be mentioned that at the start of 1994 the method by which the unemployment rate is calculated was changed, resulting in a slight – statistical – increase in the unemployment rate.

Although, unlike in Europe, the level of unemployment has not increased from one cycle to the next, there have been changes in the structure of unemployment. Compared with 1989 there has been a marked increase in the proportion of the unemployed out of work for more than six months: in 1989 less than 10% of the unemployed had been jobless for more than 27 weeks; the figure is now in excess of 20%.[4] Thus in spite of the generally very favourable employment situation, there is a trend towards persistent long-term unemployment. Clearly, the risk of remaining unemployed after an extended period of unemployment has increased.

Service sector growth

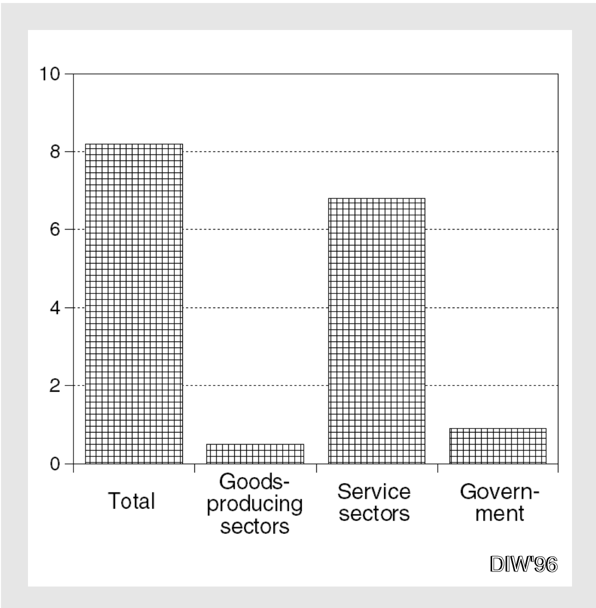
As early as the 1980s the criticism was raised that the expansion of employment consisted primarily of an increasing number of unattractive, so-called "bad jobs", work that is poorly paid because it is in low-wage sectors in which productivity is correspondingly low and, moreover, is often only part time. This "degradation" of the supply of jobs should manifest itself empirically, in the fact that employment growth is concentrated in those sectors in which wages are significantly below the average for the economy as a whole. Furthermore working hours although already below average should decline further in the course of the upturn.

Figure 7
Change in Employment in the goods-producing sector
in million persons



Source: US Department of Labor, Employment and Earnings.

Figure 6
Change in Employment, 1992 to 1995 by sector
in million persons



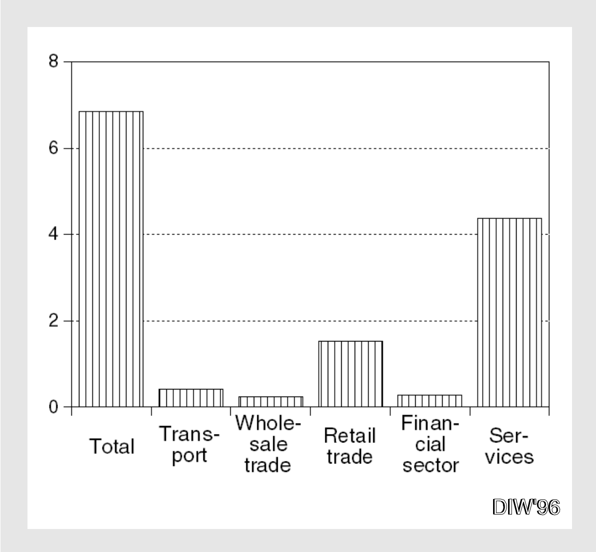
Source: US Department of Labor, Employment and Earnings.

At first sight the employment trends between the start of the upturn in 1992 and 1995 seem to confirm this view (cf. figure 6). Whereas the jobs lost during the recession were largely in the goods-producing sector, employment growth during the upturn was heavily concentrated in the service producing sector. In the goods-producing sector, by contrast, employment growth was negligible, and in any case results almost exclusively from the expansion in the extremely cyclically sensitive construction sector (cf. figure 7).

Only around 20 000 jobs were created in manufacturing industry. This figure does conceal a considerable dynamic, however. In 1992 more than 300 000 industrial jobs were lost. As the upturn strengthened, this loss has actually been more than made good. An additional factor is that average working time in this sector has increased substantially, even compared to the upturn during the 1980s. In other words, the rise in output induced firms less to recruit additional labour, than to work more overtime. Such behaviour led to a substantial increase in earnings by manufacturing employees dur-

[4] Here, too, the change in the method of calculation at the start of 1994 means that this figure is not directly comparable with the previous year's figures.

Figure 8
Change in Employment, 1992 to 1995 Service Sectors
in million persons



Source: US Department of Labor, Employment and Earnings.

ing the upturn. In this sector at least, there are no grounds for the claim that the quality of employment has deteriorated.

Given the debate on fiscal consolidation, it is surprising that public sector employment has expanded. It is important to note, however, that federal government, the tier of government that has to cope with the budget deficit, has in fact shed labour. The expansion is due almost exclusively to recruitment by local authorities.

More than four out of every five jobs created since 1992 have arisen in the service sector. Given the heterogeneity of this economic sector, it is not possible to state in general terms whether these are "bad jobs". The sector encompasses, for example the retail trade, in which wages are far below average, and the financial sector in which they are above average.

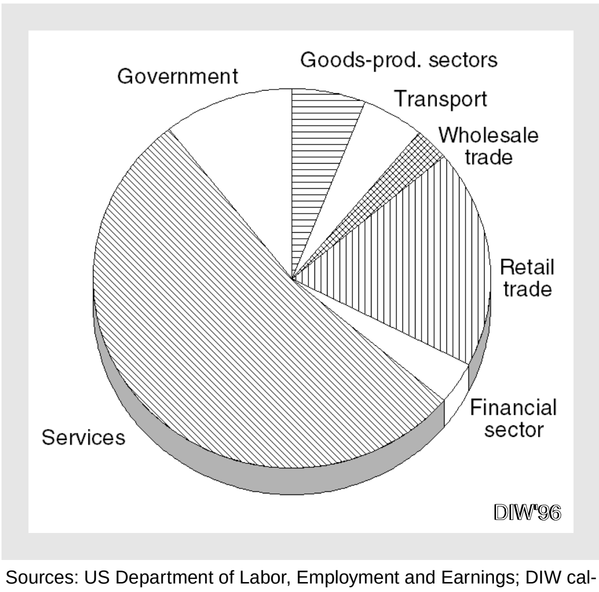
Analysis at a higher level of disaggregation shows that employment growth has been particularly substantial in the service sector (cf. figure 8). In this area pay levels are approximately equal to the average for the economy as a whole. Moreover, average working hours have remained constant since 1990, which suggests that there has not been a marked increase in part-time work; at 32.5 hours, average weekly working time is only sightly below the US average. Thus the expansion of employment in this sector does not per se mean that pay conditions have deteriorated.

The situation is rather different in the retail trade. This is the low-wage sector *par excellence,* and part-time work accounts for a large proportion of the total. Here, too, firms expanded employment markedly; the sector accounted for around one in five of the new jobs created between 1992 and 1995. While there has been scarcely any change in average working time, i.e. the already large incidence of part-time work has not risen further, the employment created in this sector has been associated with income levels that are below the average for the economy as a whole. Thus it is for this segment of the labour market that the hypothesis that recent trends have led to an expansion of "bad jobs" is most applicable.

The comparison with the upturn during the 1980s reveals similarities at the fundamental level, but significant differences in detail (cf. figures 9 and 10). Common to both phases of expanding employment was that employment growth occurred largely in the service sector, with goods production accounting for a very small share. Compared to the most recent upturn, however, the expansion of retail trade employment during the 1980s was much more pronounced in both absolute and relative terms. This trend was also accompanied by a marked fall in average working time due to a perceptible rise in the proportion of retail jobs on a part-time basis. Consequently, the view that the upturn has led to an expansion of "bad jobs" appears far more justified with respect to the 1980s than to the 1990s.

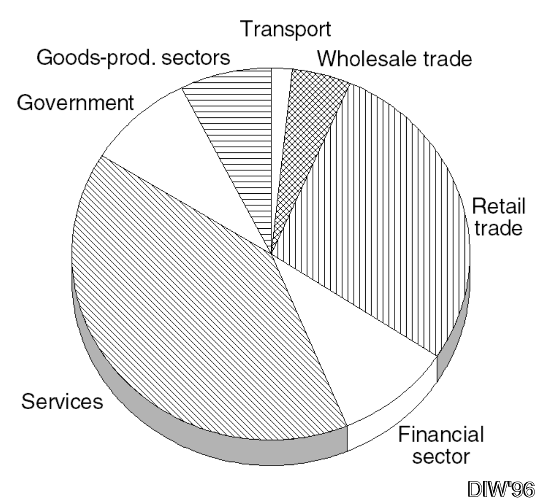
Yet even then, the situation was far from clear-cut. For instance, in the 1980s 10% of the new jobs, signifi-

Figure 9
Change in Employment by Sector 1992 to 1995
Percentage share of total change



Sources: US Department of Labor, Employment and Earnings; DIW calculations.

Figure 10
Change in Employment by Sector
1983 to 1986
Percentage share of total change



Sources: US Department of Labor, Employment and Earnings; DIW calculations.

cantly more than in the most recent upturn, were in the financial sector. This trend was accompanied by substantial increases in earned income. Thus even during the 1980s there was no general deterioration in conditions on the US labour market.

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