

Types of Unemployment

And their impact on the Montana Economy

by Barbara Wagner, Chief Economist

Strong job growth in 2012 and 2013 has brought Montana’s unemployment rate down to lower levels, with the 2013 unemployment rate of 5.4% nearly at the level that economists consider ‘normal’ unemployment. Yet underneath the state’s unemployment rate, different industries and regions are experiencing very different situations. While Eastern Montana and Billings have had fairly low unemployment throughout the recession (and very low in some oil-rich counties), unemployment in Northwestern Montana is still above normal. While healthcare and leisure activities experienced strong growth exiting the recession and are searching for workers, the construction and wood products manufacturing industries are still facing high unemployment. Although our economy is growing and the overall unemployment rate is low, pockets of high unemployment persist.

Economists refer to different types of unemployment based on their cause. Frictional unemployment refers to a constant low level of unemployment due to natural frictions

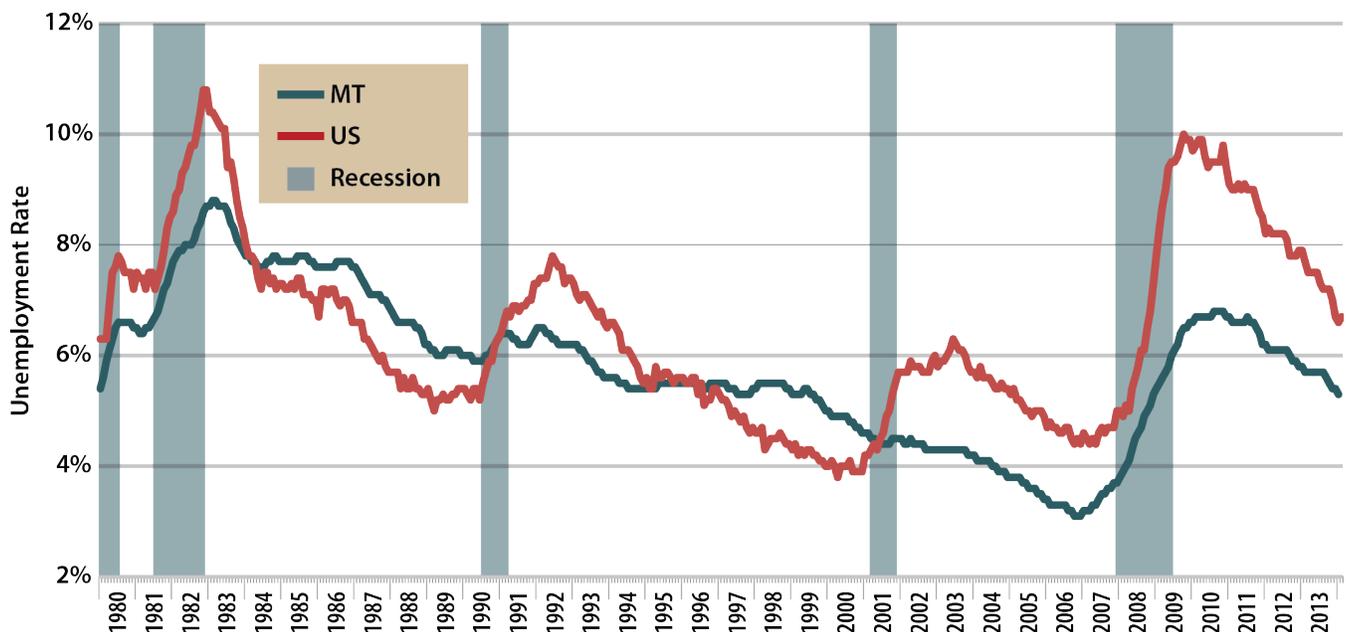


in the labor market. In other words, workers are constantly looking for new jobs, and businesses are constantly looking for the best workers. Frictional unemployment is seen as a natural and normal part of an efficient labor market, and it exists even during economic booms when overall unemployment is very low.

Cyclical unemployment is due to the business cycle, such as the spike in unemployment due to the most recent recession. Economies naturally and regularly go through periods of economic booms followed by recessions. During recessions, slower demand causes businesses to lay off workers, resulting in cyclical unemployment.

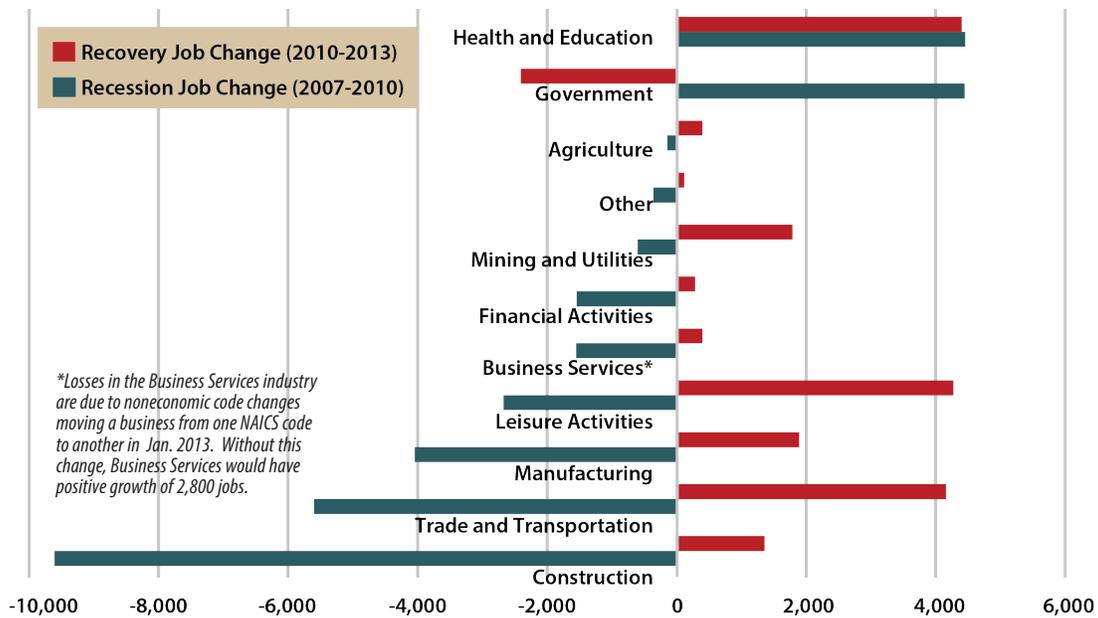
Figure 1 illustrates the U.S. and Montana unemployment rates since 1980 to demonstrate both cyclical and frictional unemployment, highlighting the recessions in gray. Unemployment spikes during recessions in a cyclical manner, generally returning to its pre-recession levels soon after the recession ends. Yet the unemployment rate never falls

Figure 1: Montana and U.S. Unemployment Rates since 1980



Source: Local Area Unemployment Statistics for Montana and Current Population Survey for U.S. Bureau of Labor Statistics and MT Department of Labor and Industry

Figure 2: Montana Employment Change in Recession and Recovery



Source: Quarterly Census of Employment and Wages, Annual Averages. Bureau of Labor Statistics and MT Dept. of Labor and Industry. 2013 data estimated using employment growth from first three quarters of 2013 over 2012.

to the level where every individual is employed, leaving some frictional unemployment of workers and businesses searching for the best fit. The lowest unemployment rate Montana has ever had was in 2006 at 3.2%. During this period of strong economic growth, wages were increasing rapidly due to the high demand for workers. Higher wages and more job openings can increase frictional unemployment by giving workers more incentive to seek out better career opportunities.

Both cyclical and frictional unemployment can cause a great deal of stress to workers and their families, but there is little policy response to these two types of unemployment at the state level. Frictional unemployment is a normal part of a healthy labor market. National monetary and fiscal policy attempts to moderate recessions and recoveries to reduce cyclical unemployment, but state level budgets are generally not large enough to influence the macro economy. Instead, the policy response at the state level focuses on alleviating social difficulties related to recession periods.

The last type of unemployment is called structural unemployment, and it has received a fair amount of attention during the recovery because it is the most challenging to

address and because it can slow economic recovery out of recessions. Structural unemployment occurs when the economy is not the same before and after the recession, thus resulting in a mismatch of worker skills and available job openings.

For example, Figure 2 illustrates the employment change in recession and recovery by industry, with the blue bars illustrating job losses during the recession, and the red bars illustrating the job growth in recovery since 2010. During the recession, construction lost nearly 30% of its pre-recession employment levels, putting over 9,000 workers out of a job. This industry has yet to make a strong recovery, meaning that unemployed construction workers have had little chance to become re-employed in jobs similar to their previous position. In contrast, other industries had growth throughout the recession or have made a strong recovery since 2010. These industries are searching for workers, but not workers with construction skills. This mis-match between the industrial structure before and after the recession can cause structural unemployment where the skills demanded by employers are not the skills held by workers.

Structural unemployment is also problematic because it can lengthen unemployment periods and cost workers significant time and effort to be retrained in a different occupation or industry. For example, it would take significant time for a carpenter to be retrained as a registered nurse, possibly even keeping the worker out of the workforce for several years to obtain education. Such a long unemployment period would be costly for the carpenter and his family, but also can slow the recovery of the economy out of recession. Instead of businesses producing goods to fill rising demand, businesses wait for workers to obtain the training needed to fill openings.

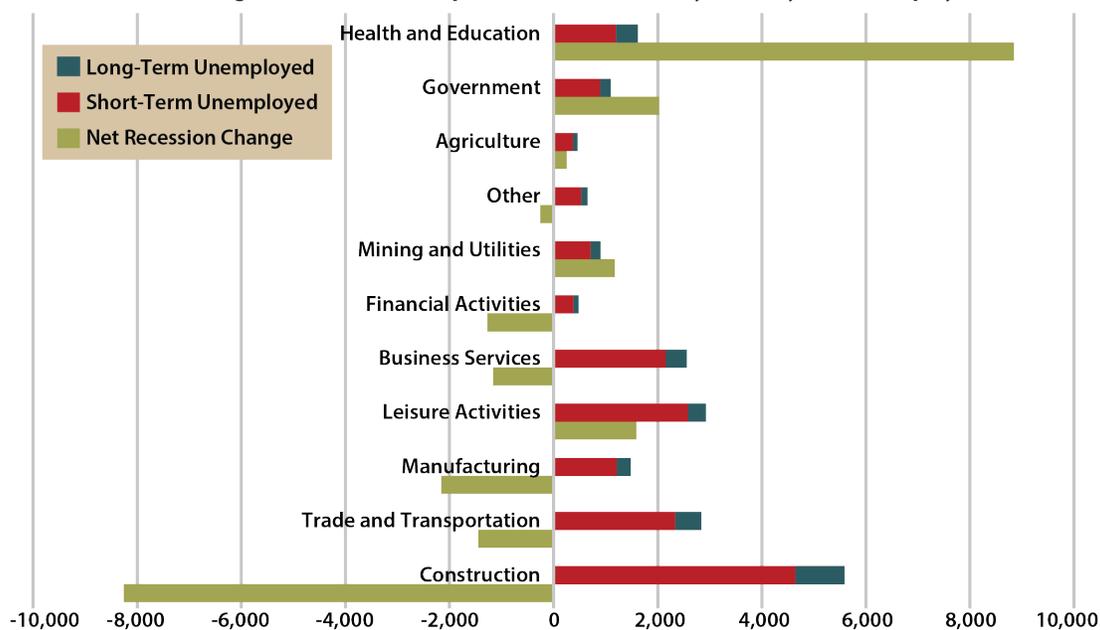
Differences in industrial structure pre- and post-recessions do not guarantee skills mismatches and structural unemployment. For example, a heavy equipment operator that previously worked in construction could likely require only a short amount of training to become a heavy equipment operator in the mining industry. Re-hiring a worker in a similar field is the fastest way back to re-employment. Further, structural unemployment can also result due to geography, such as having high unemployment in Northwest Montana while businesses are searching for workers in Billings and in Eastern Montana. Additional

education and training of workers won't help geographic differences in employment; such differences are typically resolved only with the migration of workers or businesses.

So, how much of Montana's pockets of high unemployment are due to structural issues, and how much is due to cyclical and frictional unemployment? It is difficult to pinpoint the differences exactly, and unsurprisingly, the evidence suggests a mixture of the three types of unemployment. Figure 3 illustrates the net recession job change (the sum of the bars in Figure 2), compared to the former industry of unemployed workers receiving unemployment insurance claims in January and February of 2014. UI claimants don't represent all of the unemployed. Only about 35-45% of the unemployed receive UI benefits. Other unemployed workers either do not qualify or choose not to apply for benefits. However, looking at this sub-group of the unemployed can provide information on how a worker's former industry is related to their length of unemployment.

The number of UI claimants is further broken down by the short-term unemployed versus the long-term unemployed. The long-term unemployed are those who have been

Figure 3: Net Recession Job Change 2007 to 2013 Compared to UI Claimants by Industry and Unemployment Duration



unemployed for 26 weeks or more. These workers are of particular concern because finding a job gets harder the longer a person is unemployed. Many of the long-term unemployed end up dropping out of the labor force completely, representing a permanent loss of human capital in our economy and fewer workers for employers. About 16% of Montana's UI claimants have been unemployed long-term, compared to about 34% for all unemployed individuals in the U.S. Further, long-term unemployment at this stage of an economic recovery is also a sign of structural unemployment issues. Looking for employment for over 26 weeks in a fairly strong economy suggests either low levels of job skills on behalf of the worker or their job skills are in low demand, with both situations requiring a solution of additional education and training.

Unsurprisingly, given the large number of job losses during the recession, the construction industry has both the largest number of unemployed workers and the largest number of long-term unemployed workers. The high number of long-term unemployed in this industry is likely due to some structural unemployment issues. These long-term unemployed construction workers may need to seek re-training in a different field. However, there is also a fairly high level of short-term unemployed in the construction industry. Leisure activities, trade and transportation, and business services (which includes temporary employment firms) also have high levels of short-term unemployed workers. These industries are fairly seasonal industries with short job duration, resulting in unemployment that would be more properly characterized as short-term cyclical unemployment than structural unemployment. Based on this data, unemployment among construction workers looks to be both cyclical and structural.

Despite net job gains over the past six years, mining and government still have some unemployed workers. For mining, this likely illustrates frictional unemployment as workers search for the best opportunities. However, government has undergone job cuts in recent years, eroding

the job gains from 2007 to 2010. Cyclical unemployment is likely the cause of unemployment in the government sector.

Of particular interest is the number of UI claimants that were previously employed in the health care industry. This industry has not experienced any employment losses in recent years – in fact, the health care industry has posted job gains throughout the recession and recovery and has been in need of workers. Some of the short-term unemployed may simply be an illustration of frictional unemployment as workers are looking for the right employer match. But the long-term unemployed have had over six months of job searching, and yet they are still unemployed. Perhaps these workers are geographically isolated from the employment opportunities, or perhaps they have low job skills, making them unattractive to employers. The question for employers and workforce planners is how to find those workers and get them into employment as quickly as possible, possibly boosting their job skills through short-term training if necessary?

In conclusion, structural unemployment is just a complex economist term for describing what many workers and workforce professionals already know – displaced workers often need new training to pursue new career opportunities. As more and more of our aging workforce retires in the upcoming years, causing more worker shortages for Montana businesses, it will become even more important to identify workers who need to be retrained for open jobs and get them retrained quickly. Organizations throughout the state already are looking at ways to address structural unemployment now and in the future, with business organizations in Billings, Great Falls, and in the health care industry working with the Montana Department of Labor and Industry to identify unemployed workers and develop programs to quickly train them for future jobs. Such efforts work to improve the efficiency of Montana's labor markets and can speed economic growth.