

What Does the Unemployment Rate Actually Tell Us?

Working Together

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The percentage rate of unemployment, known as the “official unemployment rate,” is the ratio of those who are unemployed compared to those in the civilian labor force. Those in the labor force are defined as persons who were working or actively looking for work within the last four weeks. This percentage rate, called U-3, is published monthly by the U.S. Department of Labor, Bureau of Labor Statistics. The result just announced for June is 6.1% which, considering that the national unemployment rate had been over 8%, is being claimed as an indication of an improving economy. But since a ratio can be affected by either of its two components, what does the U-3 actually tell us about the state of employment in the country?

Consider a very simple economy: an island with only 20 people in the labor force; that is, ready, able and willing to work, and either employed or looking for a job. Of these, 10 have jobs and 10 do not, so the official unemployment rate of the island is 50%. This is a pretty dreadful unemployment rate. Then one of the workers is laid off, and he and the 10 people who were not employed all stop any active search for work. They move back into their parents’ huts, and spend their days on the beach. There are 9 people left in the labor force, all of whom are employed. The island’s official unemployment rate is now 0%, which seems like a dramatic improvement, but is the island’s economy any better off?

As Mark Twain observed, there are three types of lies: lies, damned lies, and statistics. The “official unemployment rate” is not a lie, but it is not the complete story. The BLS has other “U’s”: U-4 which adds “discouraged workers” (not currently looking for work for job-market rather than personal reasons), U-5 which adds the marginal labor force (defined as those who looked for work within the past 12 months, rather than just the past 4 weeks), and U-6, which adds those who would like to have a full-time job but could only find part-time work (the underemployed). Each of these rates is higher than the “official” unemployment rate; U-6 is over 12%.

In a booming economy, where jobs are available, the upper U’s are less significant, since those who drop out of the active labor force more likely choose to do so for a better option, such as continued education, rather than because they are discouraged or can’t find work. In a stagnant economy, the official unemployment rate is less informative, and more the type of statistic that Mark Twain would recognize.

Posted in Unemployment

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