



USA: Where are the jobs?

March 25, 2010

Employment creation measures under Obama

- **The US economy is recovering, but the labour market is still weak.**
- **The fate of Obama's policy agenda may depend on a jobs recovery.**
- **Will additional employment measures provide enough bang for the buck?**

The highest unemployment rate in a quarter century and a “jobless” recovery have propelled jobs to the top of the list of Americans’ concerns. Criticized for devoting too much attention to bank rescues and health care reform over the past year, the Obama Administration and the Democratic majority in Congress are fervently defending their record on job creation and at the same time attempting to push through new measures aimed at stimulating employment. Unemployment would be considerably higher today were it not for the stimulus measures enacted over the past year – but it’s difficult to sell that point when nearly one in ten people of working age is out of work and at least one in six is “underemployed”.

The US economy has lost 8.4 m jobs since the onset of the deepest and longest recession since WW II. Months after GDP growth turned positive in Q3 of 2009, the US labour market has yet to stage a recovery. Net payrolls continued to fall by 36,000 in February, more than in January but less than expected, and in line with recent moderate declines compared to the net job losses in excess of 700,000 per month in early 2009. On a positive note, the unemployment rate, which is based on a different survey than the payroll results, has declined to 9.7%, down from 10.1% in October 2009. Moreover, for the first time in over a year, the number of long-term unemployed (workers out of a job for 27 weeks or more) decreased slightly in February. Yet the number of long-term unemployed (6.1 m) remains extremely high, and the average length of unemployment is still hovering around 30 weeks, compared to 16.5 weeks at the start of the recession. Also less encouraging, the rate of underemployment ticked up again in February, to 16.8%, as 26.3 million workers were either unemployed (14.9 m), discouraged (2.6 m) or involuntarily part-time (8.8 m).

It took six to twelve months after the official end of the two previous recessions for net job creation to even begin, and years to return to the level of employment at the start of the recession. This time around, the loss in output and jobs has been much more severe and the current headwinds to job creation greater than in recent recoveries. Indeed, the Obama Administration forecasts average monthly net job gains of 95,000 this year, which is still below the 100,000-125,000 net new jobs per months required just to absorb new labour market entrants and to keep the unemployment rate steady. Even with its relatively optimistic GDP growth assumptions (3.8% annual GDP growth in 2010 and over 4% in 2011-2013), the Administration predicts the unemployment rate will remain over 5% until 2016.

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dbresearch.com

Author

Amy Medearis
+49 30 3407-2950
amy.medearis@db.com

Editor

Barbara Böttcher

Technical Assistant

Angelika Greiner

Deutsche Bank Research
Frankfurt am Main
Germany

Internet: www.dbresearch.com

E-mail: marketing.dbr@db.com

Fax: +49 69 910-31877

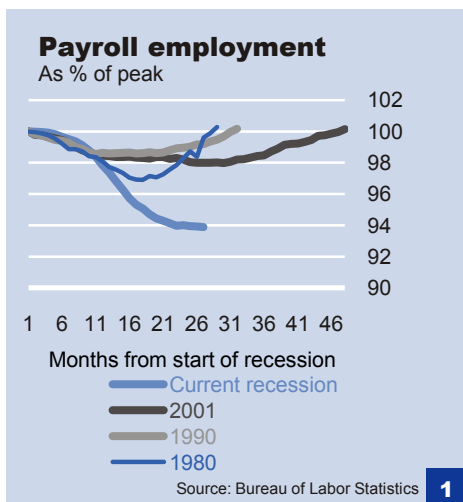
Managing Director

Thomas Mayer

There are some hopeful signs of a pending labour market recovery, incl. the fact that temporary work contracts have risen markedly, a harbinger of increasing demand for labour. Moreover, the recent productivity surge (labour productivity increased at a 6.9% annual rate in Q4 2009) eventually will run its course, as firms who have over the past few months increased output without adding or replacing workers will find it difficult to expand further without hiring.

Still, the labour market recovery is likely to continue to be sluggish, due to a number of headwinds, both cyclical and structural:

- As growth resumes, discouraged workers will return to the labour market and increase the pool of unemployed.
- Employers will remain hesitant to hire amid a still-tepid economic recovery marked by increased private savings and hesitant consumer demand.
- Workers formerly employed in the construction and auto sectors, where many of the jobs lost are not coming back, may require retraining in order to qualify for employment in other sectors.
- Long-term unemployment, currently at a historic high, erodes worker skills and in many cases reduces employability.
- Many workers whose home values have plummeted are finding it difficult to move to another region for work.

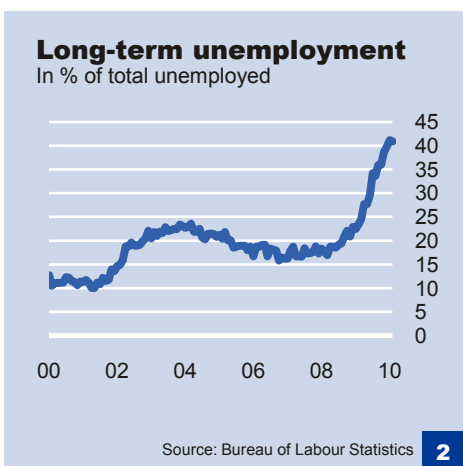


It would have been even worse without stimulus

The massive fiscal stimulus undertaken since the onset of the recession has undoubtedly lessened the impact of the crisis on the labour market. Yet it has not been easy, either economically or politically, for the Administration to argue this point effectively, due to the persistent labour market malaise and the lack of a counterfactual to prove precisely how many more jobs would have been lost in the absence of the stimulus. Thus, even though there is a substantial amount of stimulus still in the pipeline and limited fiscal room for manoeuvre, the Administration and Congress have come under increasing pressure to enact further measures designed to boost job creation and bring down the near-double-digit unemployment rate.

American Recovery and Reinvestment Act (ARRA)

Obama's signature stimulus legislation, the ARRA was enacted just over a year ago on February 17, 2009. Estimates of the USD 787 bn stimulus package's impact on economic growth and employment vary, but serious studies from both within the government and from private economists conclude that the recession would have been deeper and longer in the absence of the ARRA. The Council of Economic Advisers calculated that the USD 263 bn spent under the ARRA by the end of 2009¹ (approximately one-third of the USD 787 bn recovery package), added roughly 2.8 pp to GDP growth in Q2 2009, 3.9 pp in Q3 and 1.8 pp in Q4. Through this boost to GDP, the ARRA is estimated to have created or saved 1.5 m to 2 m jobs through the end of 2009. These results are consistent with the findings of the Congressional Budget Office (CBO) and a number of professional forecasters. The Administration



¹ Council of Economic Advisers 2010. The Economic Impact of the American Recovery and Reinvestment Act of 2009. January 13, 2010. Of the USD 263 bn, USD 99 bn went to tax cuts and USD 164 bn for infrastructure and other projects and for direct aid to states and individuals. A further USD 150 bn had been obligated but not yet outlaid. Most of the funds allocated for infrastructure projects have yet to be paid out due to the long lag times.



ARRA's impact

Jobs created or saved, thousands
Estimates as of Dec. 2009

CEA: Projection approach	2,068
CEA: Model approach	1,772
CBO: Low estimate	1,000
CBO: High estimate	2,100
IHS/Global Insight	1,248
Macroeconomic Advisers	1,057
Moody's Economy.com	1,586

Source: Council of Economic Advisers, updated by author to reflect Congressional Budget Office (2010)

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US Unemployment Insurance

The federal-state Unemployment Compensation (UC) program, created by the Social Security Act of 1935, is a counter-cyclical social insurance program intended as a temporary, partial wage replacement for the unemployed. Its eligibility requirements are determined by the states in accordance with broad federal guidelines, and it is funded through a tax on employers (a federal effective tax rate of 0.8% of workers' gross income plus a state average tax rate of 0.6%).

Benefit amounts and duration are determined by income earned while employed. The average weekly unemployment benefit check amounts to slightly under USD 325, which represents just over one-half of average weekly earnings. In most states, UC benefits last for up to 26 weeks. In periods of high unemployment, federal-state funded 'extended benefits' (EB) can kick in for an additional 13-20 weeks. The Emergency Unemployment Compensation program currently provides a federally-funded extension of unemployment benefits for up to 53 weeks.

Under 40% of the total unemployed receive unemployment benefits, which is why the US unemployment rate is calculated from survey data rather than from the weekly statistics on unemployment insurance claims. Still, the claims data provide a timely indicator of employment conditions. Even though new (initial) jobless claims peaked last spring, they have yet to fall below the 400,000 level generally considered a threshold for job growth.

predicts that a total of 3.5 m jobs will have been created or saved by the end of the spending period in 2011.

So far, the Recovery Act has had the greatest positive employment impact in the sectors that were hardest hit by the recession and where the ARRA provided targeted assistance, specifically in manufacturing (mainly durable goods), construction, and professional and business services (in particular due to growth in employment services). Regionally, states with a large share of industry have had larger employment effects relative to their populations, as have in general states hardest hit by the recession and with the highest unemployment rates at the time of the ARRA's passage². It is also evident from the CEA report that the USD 60 bn in state fiscal relief through December 2009 resulted in the preservation of many state and local government jobs.

Unfortunately for the Obama Administration, this rather positive report card for the ARRA is not reflected in public opinion. A recent CNN poll³ found that 56% of Americans oppose the stimulus package, against 42% in support of the plan. Moreover, nearly 75% of those surveyed believe that at least half the money spent so far has been wasted, and 63% think projects in the plan were included for purely political reasons. These negative perceptions have likely been driven by Americans' low opinion of Congress and by the fact that many of the funded infrastructure projects are still in the planning phase and thus not yet visibly bearing fruit.

Direct assistance for the unemployed

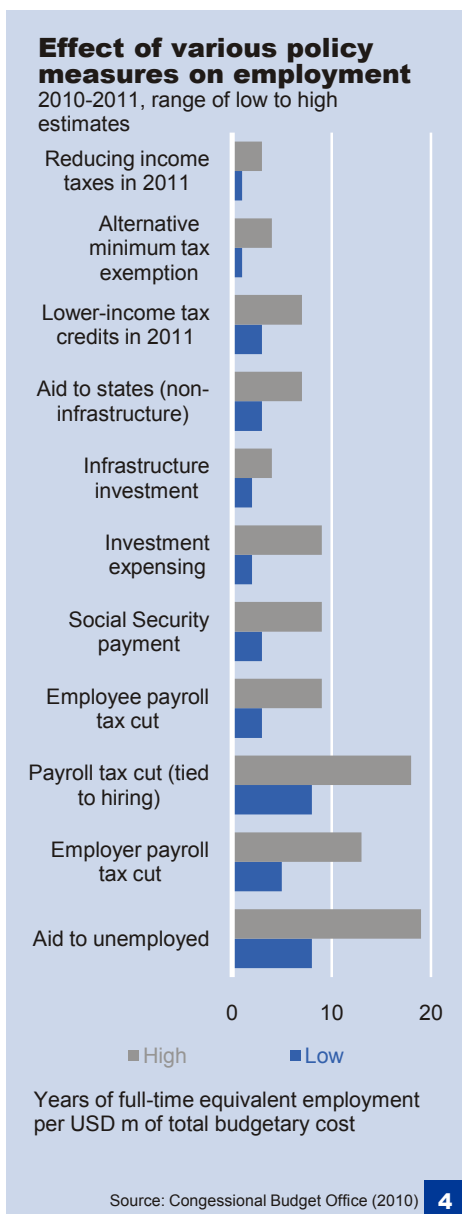
In July 2008, still under the Bush Administration, Congress passed the first Emergency Unemployment Compensation package that increased benefits by USD 25 per week and extended the period of eligibility. As the recession intensified, the duration of unemployment insurance was again extended in November 2008, in February 2009 under the ARRA, in November and December 2009, and most recently in March 2010. In addition, the ARRA introduced assistance to the unemployed to purchase health insurance (65% of the cost of the insurance premium to be paid by the government for up to nine months), and extended this in December 2009 (to up to 15 months). These measures aim to cushion the impact of unemployment on household finances, while also indirectly boosting consumer demand and, in turn, raising national output and generating jobs.

More jobs stimulus to come (well, a little more)

In early March, Congress passed the first pieces of legislation in what Congressional Democratic leaders are calling a 2010 "jobs agenda". The first measures included a USD 15 bn employer tax credit for hiring new workers and a USD 10 bn short-term extension of benefits for the unemployed. Under the Hiring Incentives to Restore Employment Act, firms who hire new workers are exempt from the 6.2% Social Security tax for the remainder of 2010.

² States with the highest unemployment rates in 2009 included Michigan, Nevada, South Carolina and California.

³ CNN poll conducted January 8-10, 2010.



Employers whose new hires remain on the payroll for at least a year will receive an additional USD 1,000 tax credit. Beyond this, the Senate is currently debating a larger (approx. USD 100 bn) bill that would renew an array of business tax breaks and extend unemployment benefits through the end of 2010. This would have to be reconciled with a broader USD 154 bn bill passed by the House in December 2009 and other measures endorsed earlier by the Senate Finance Committee and the White House that remain on the table.

Sufficient job “bang” for the deficit “buck”?

The most recent jobs legislation is likely to have a positive but relatively small effect on employment. Extending unemployment benefits and reducing employer payroll taxes for firms that hire new workers is a relatively quick and efficient job creation policy. Using the CBO’s estimates (see chart), the USD 13 bn payroll tax credit measure alone would create a total of 104,000 to 234,000 jobs over 2010 and 2011. That is certainly better than nothing, and at an average cost range of USD 56,000 to USD 125,000 per full-time job is on par or even somewhat more efficient than the approximate USD 100,000 cost per job created through the ARRA. But the employment impact of the payroll tax credit may be limited by the bill’s restrictions (e.g., workers must be unemployed for at least 60 days) and by weak domestic demand, which business surveys indicate is a much greater concern for companies than high taxes.

The employment impact of these and other measures being debated in Congress will vary. Further direct assistance to the unemployed should help increase demand (and thus support growth and jobs), and aid to state and local governments in various forms will save some jobs (in particular teachers and police). With the total budget gap of states expected to reach USD 142 bn for fiscal year 2011, further severe budget cuts at the state and local level are inevitable. But investment in infrastructure and tax breaks to businesses that are not tied to job creation will have a smaller effect on employment, either due to a delayed impact (infrastructure) or lower multiplier effect (tax cuts). With many Republicans as well as Democrats resisting additional deficit spending, the political scope for further stimulus is limited, particularly if it is not accompanied by offsetting cost savings (in keeping with so-called pay-go rules). Congress seems likely to approve at most USD 100-150 bn in additional employment-related measures this spring, which might create or save an additional half-million jobs over the next two years. While significant, this number pales in comparison to the 8.4 million jobs lost in the recession and the even greater number of jobs needed to close the employment gap. It also comes with a large price tag at a time when deficit spending is becoming politically unpopular and economically risky.

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