

Senate Democratic Policy Committee Hearing

“Are We Exporting American Jobs?”

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Senator Dorgan and members of the Senate Democratic Policy Committee, my name is Martin A. Regalia and I am Vice President of Economic and Tax Policy and Chief Economist of the United States Chamber of Commerce, the world's largest business federation representing more than three million members and organizations of every size, sector, and region. We appreciate the opportunity to appear before you today to discuss the U.S. economy, the jobless recovery, and state of our manufacturing sector.

The Current Economic Environment and the Jobless Recovery

Although, the U.S. economy emerged from the last recession in November 2001, real economic growth remained lackluster advancing at less than a 3 percent pace for four quarters. Beginning in the second quarter of this year, however, the economy began to accelerate. Real GDP growth was 3.3 percent in the second quarter and a remarkable 7.2 percent in the third quarter of this year. At the same time, economic growth has become more balanced with business fixed investment growing more than 11 percent at an annual rate in the third quarter, and investment in equipment and software advancing at a 15.4 percent annual pace over the same period.

With the inventory-to-sales ratio at a record low level, a likelihood that the dollar will depreciate further, an expectation of somewhat lower oil prices, and the emergence of stronger than expected growth abroad, the prospects for economic growth in the near term look very good.

One area of the economy that has not performed well, however, has been the labor market. According to the establishment data, the economy has lost 3.0 million private sector jobs since the end of 2000 with 919 thousand of those occurring since the end of the recession. These statistics have led economists to compare this period to that following the last recession in 1991 and label both as “jobless recoveries”.

Fortunately, the labor market picture appears to be brightening. In the month of October, the economy created 116 thousand net new private sector jobs, and revisions to the prior two months indicate that over the last three months the economy has created 256 thousand net new private jobs. While we all hope the improvement continues, the job performance to date remains weak when compared to all but the last recession.

According to data on household employment provided by the Current Population Survey, the current situation is significantly better. Over the entire period from the end of 2000 to the

present, employment is up 394 thousand to 138 million, a new record. But, even using the household figures, the employment growth during this recovery has been anemic when compared to previous recoveries except that which occurred in 1990-1991.

Another factor in the weak labor markets in the last two recoveries has been the duration of unemployment. Individuals losing jobs have remained unemployed for longer periods and taken longer to be reabsorbed.

The marked difference in employment behavior during and following the last two recessions compared to the average post-war cycle has prompted a number of studies. Two that I found particularly informative are “A Closer Look at Jobless Recoveries” by Stacey L. Schreft and Aarti Singh published by the Federal Reserve Bank of Kansas City and “Has Structural Change Contributed to a Jobless Recovery?” by Erica L. Grosben and Simon Potter published by the Federal Reserve Bank of New York.

Schreft and Aarti point out that the reasons for the so-called jobless recoveries following the last two recessions result from both cyclical and structural factors. The cyclical reasons stem from the fact that real GDP growth following the last two recessions was well below that of the average post-war recession and, more importantly, below the economy’s potential rate of growth. These author’s estimate that the weak economic growth could explain about 20 percent of the weak job growth in 1991 and as much as two-thirds of the job weakness in the most recent cycle. The remainder of the problem these authors attribute to structural changes in employment practices which they term “just-in-time employment.” With “just-in-time employment” practices firms substitute temporary and part-time workers for permanent hires and use the existing workers more intensely through increased overtime.

Grosben and Potter also conclude that much of the difference in job loss between the last two economic cycles and others in the post-war period has to do with structural changes but they focus on specific industries rather than hiring practices. They noticed that the job losses were in certain industries while other industries fared much better. According to their theory, jobs migrated from the declining industries to the ascending industries. This job migration is a more time consuming process than the more traditional furlough and rehiring process of the typical post war recession. The authors pointed out that such structural shifts were more likely following periods of over-expansion, would be more noticeable when monetary and fiscal policy were effective at mitigating the economic cycle, and would be exacerbated if firms hiring practices were shifting toward the “just –in-time employment” model – all of which characterize the last two economic cycles.

What should be emphasized about both these studies is that the weak job market is temporary. The effects of these structural shifts cause the weak job period to be more drawn out and the post-recession boom to be delayed but the boom inevitably arrives. The restructuring in the early 1990s set the stage for the tremendous boom in the last half of the decade, the current restructuring could do the same.

Finally, we should keep a few things in perspective. While the current cycle has mirrored the 1990-1991 cycle's weak job growth, the economy is, in general, in much better shape. Productivity gains that have exacerbated the weak job market have contributed to strong real income growth and the tax cuts have bolstered real disposable personal income. The unemployment rate peaked at a historically low 6.4 percent and is currently 6.0 percent – a rate that not too long ago would have been considered full employment.

Manufacturing: A Good News/Bad News Story

The accompanying chart shows that real manufacturing output displays two undeniable facts – manufacturing output continues to grow, nearly doubling in the past two decades; manufacturing output remains highly cyclical. The recent economic downturn, which was centered on the investment side of the economy rather than the more normal consumption sector was particularly hard on manufacturing.

At the same time that manufacturing output was experiencing a cyclical downturn, labor productivity growth was particularly strong with the result that manufacturing employment plummeted. While manufacturing output is once again on the rise, labor productivity continues to grow at a pace that thus far has allowed manufacturers to meet the increases in demand without re-employing displaced workers. While we expect productivity growth to slow somewhat and thus improve the manufacturing employment picture, it is unlikely that manufacturing employment would reach the peak levels of the late 1970s or early 1980s.

Although we expect the manufacturing sector to weather the current cyclical problems, we see larger structural issues ahead. Despite the growth in manufacturing over the past two decades, growth in the service side of the economy has been even greater with the result that manufacturing's share of GDP has fallen noticeably. Moreover, with productivity rising, manufacturing's employment share has dropped even further. Should this trend be a concern? The answer to this question clearly depends upon the causes behind manufacturing's relatively slower growth.

Some analysts have focused on globalization, trade expansion and unfair trade practices as the reasons for manufacturing's problem, but we think that the answer lies closer to home with anti-growth policies.

It is estimated that regulatory policies, many of which do not have a sound scientific basis, cost business \$850 billion a year. Tort costs are estimated to cost business \$233 billion per year. We have an archaic, Byzantine tax code that places multiple layers of tax on saving, our economic seed-corn, prevents complete cost-recovery on investment, and places multiple layers of taxation on U.S. companies that do business abroad. Energy is the lifeblood of manufacturing and yet we do not have a national energy policy. Healthcare costs continue to skyrocket, while healthcare reform is bounced around like a political football. It may be easier to blame China, and clearly we should strongly encourage all our trading partners to adhere to all the provisions in trade agreement, but the declining share of manufacturing began well before our trade with China, and it will require more fundamental changes to fix it.

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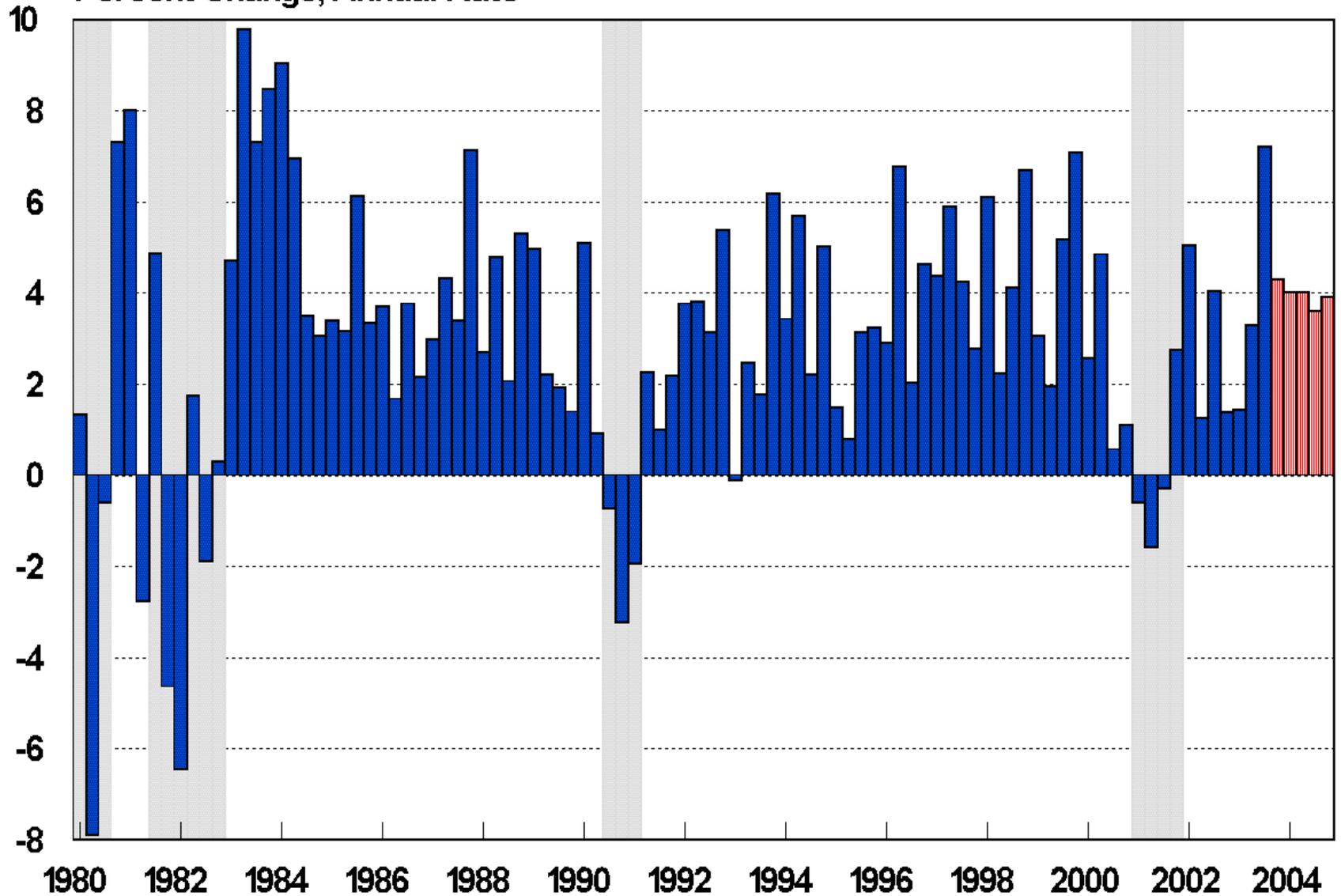
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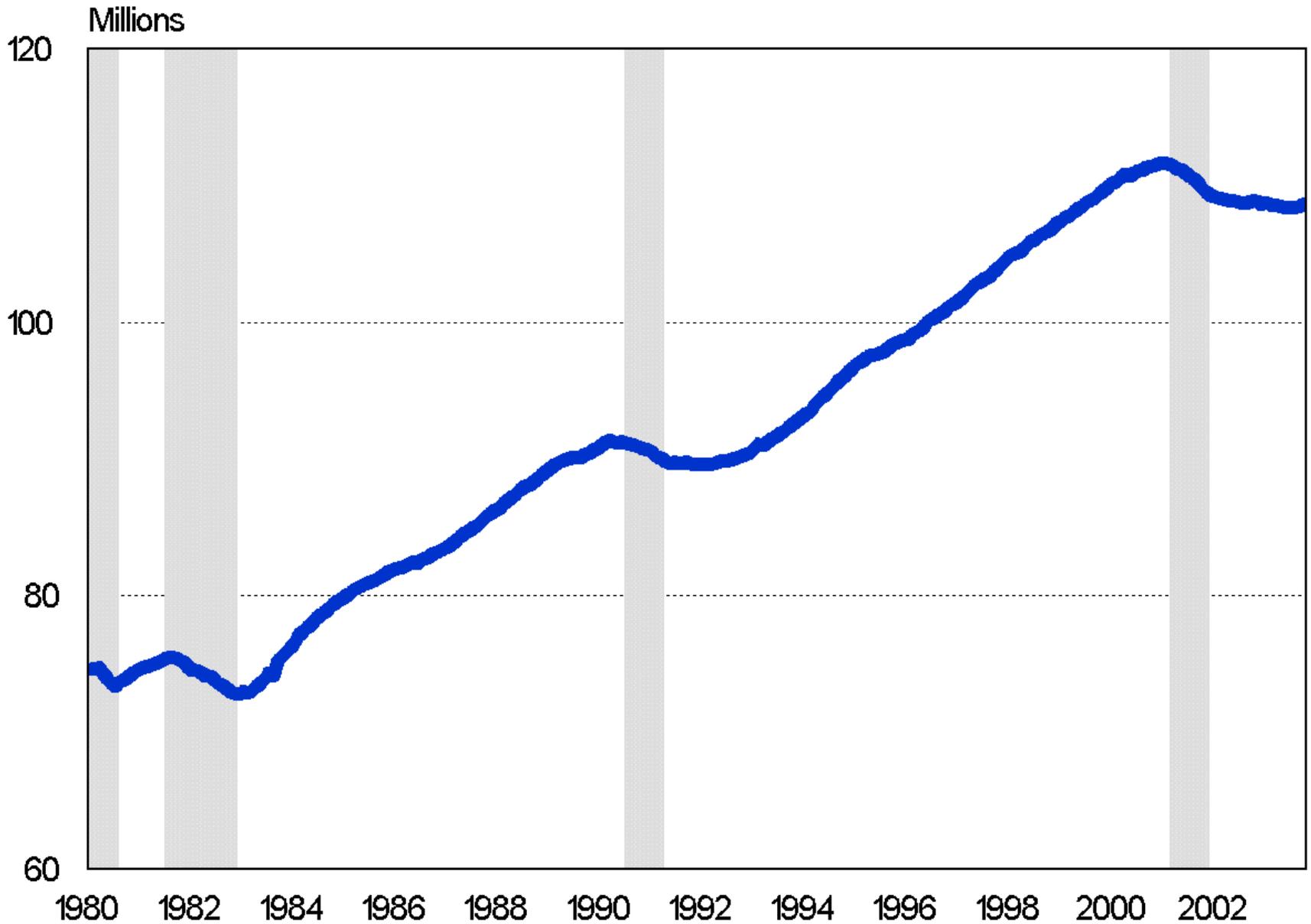
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Real GDP Outlook

Percent Change, Annual Rate

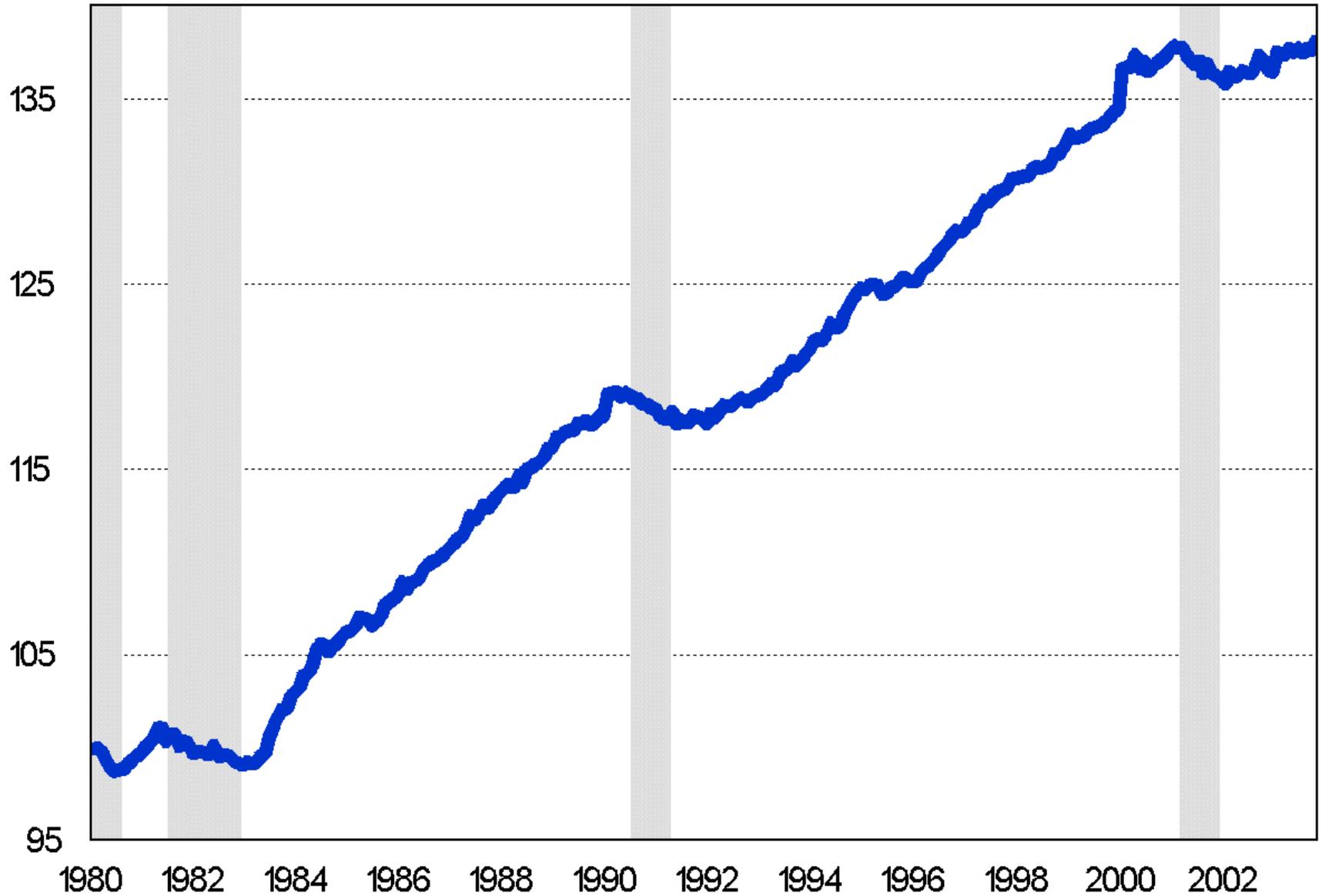


Total Private Jobs

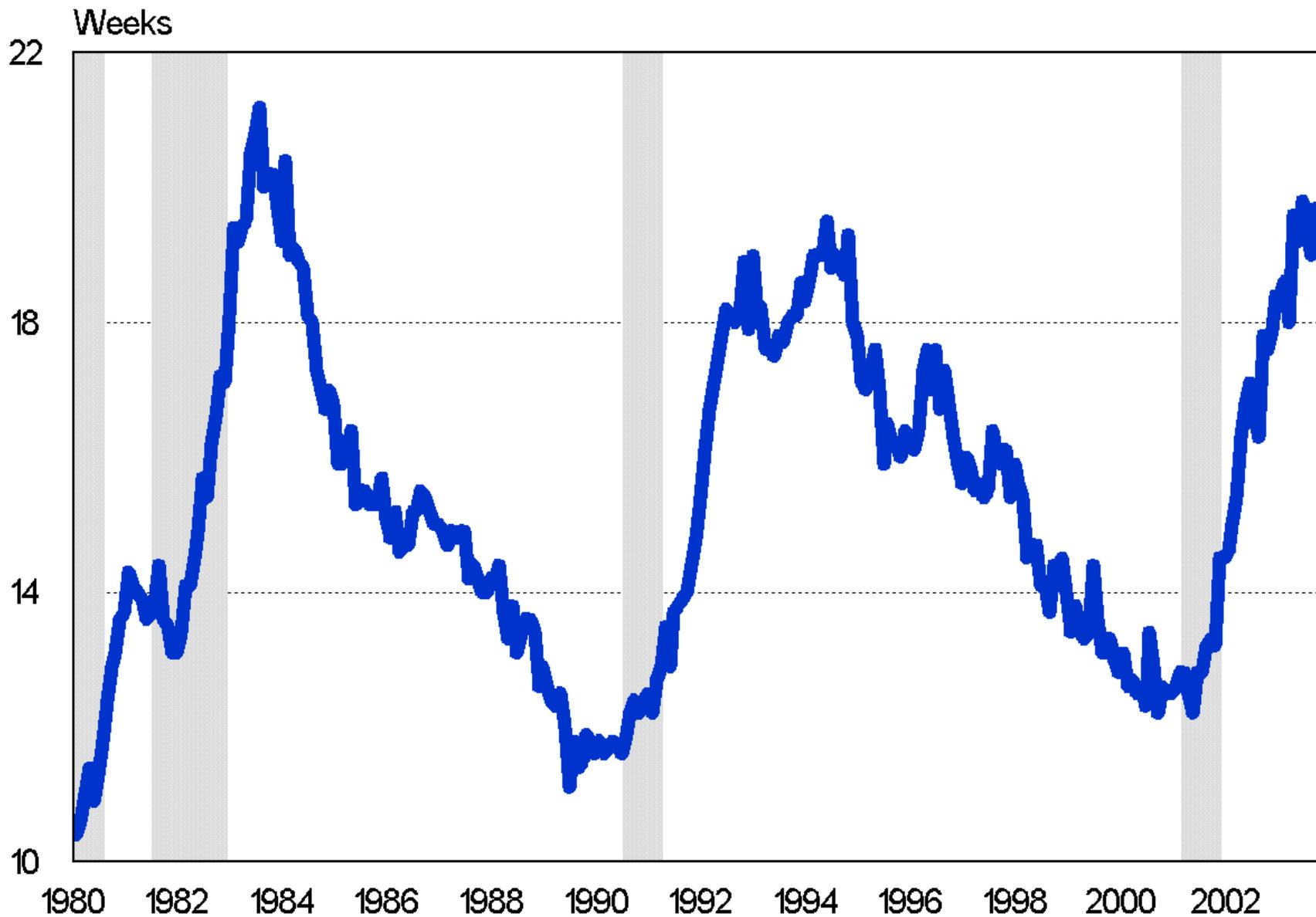


Household Employment

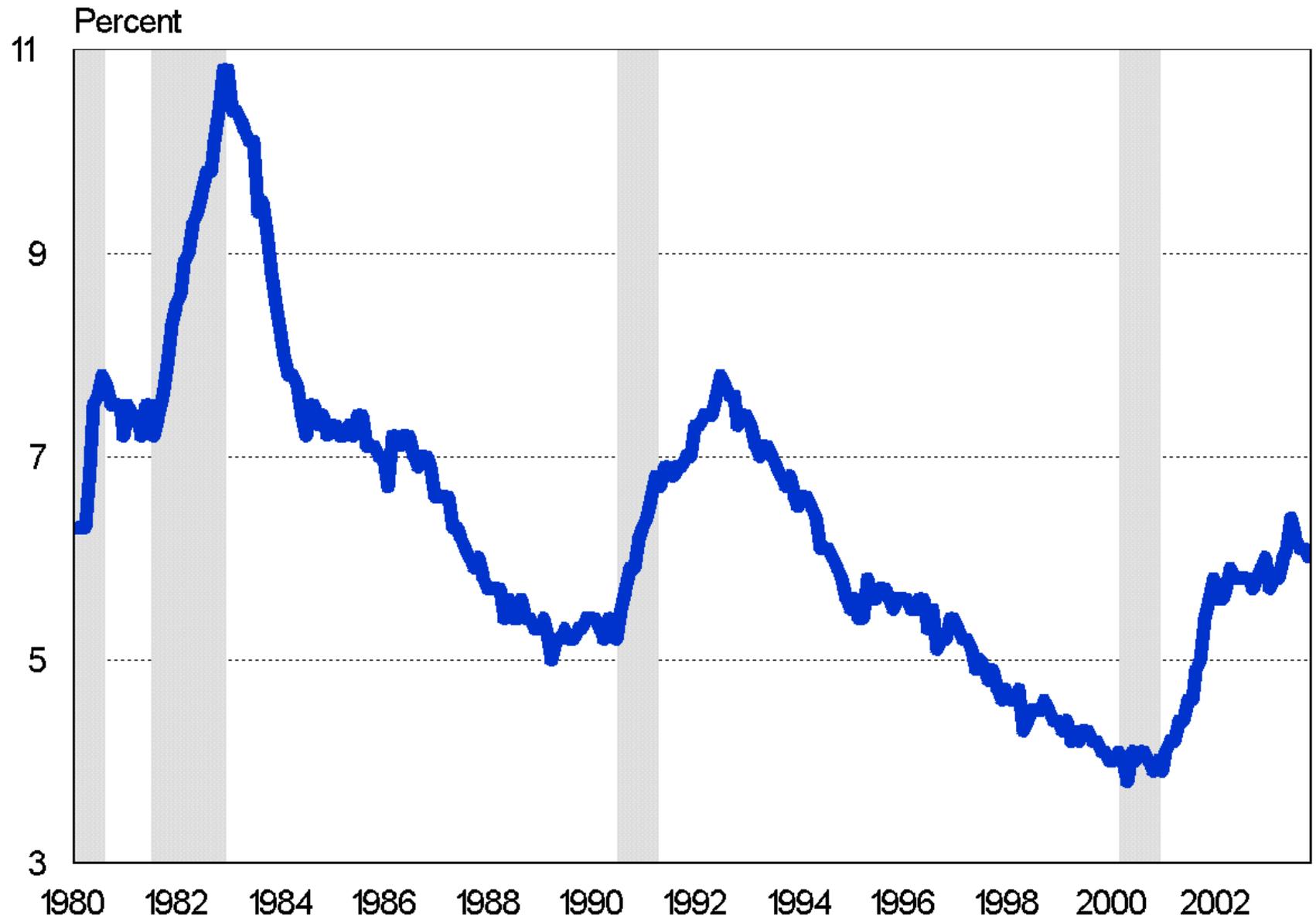
Millions



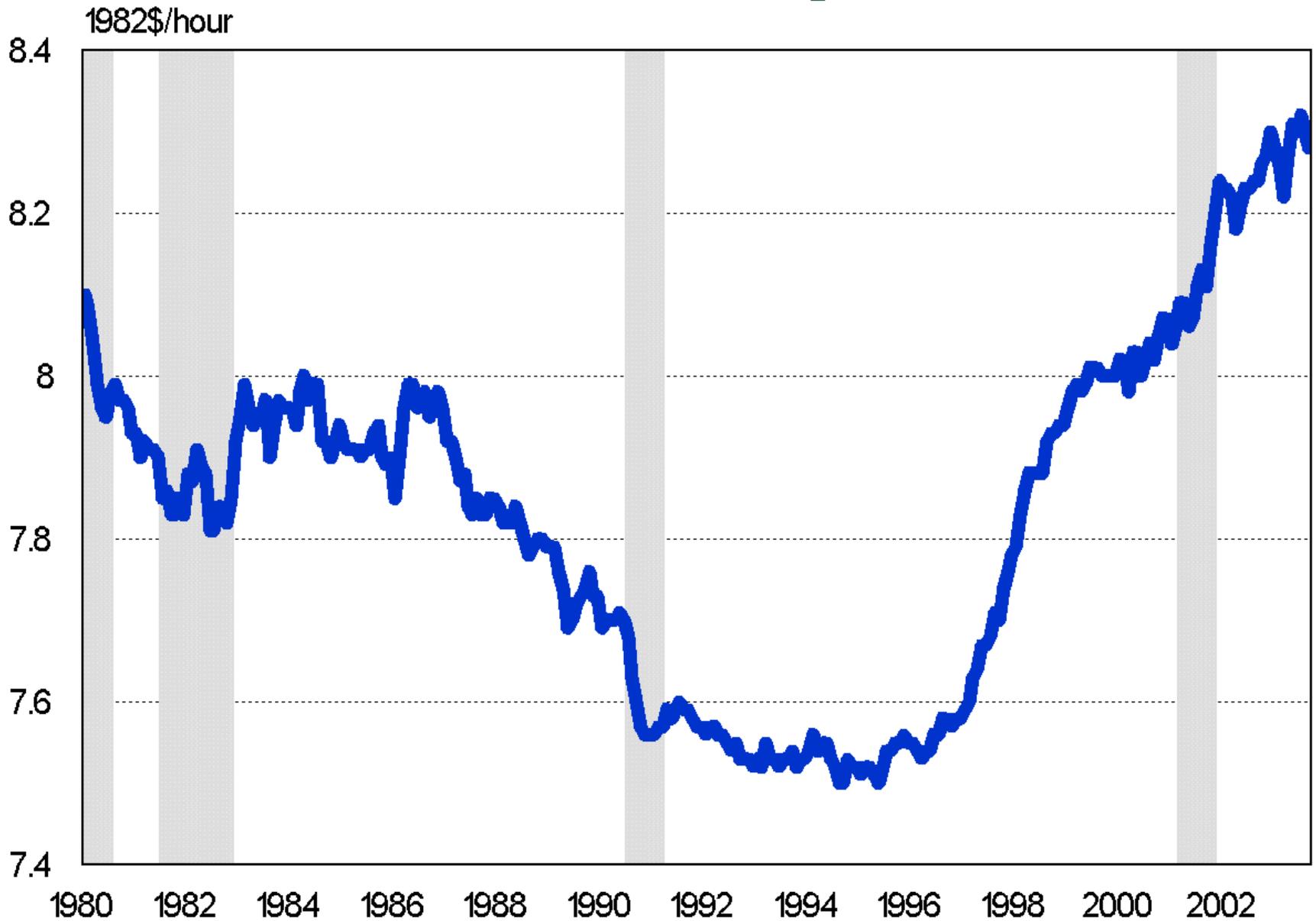
Average Duration of Unemployment



Unemployment Rate

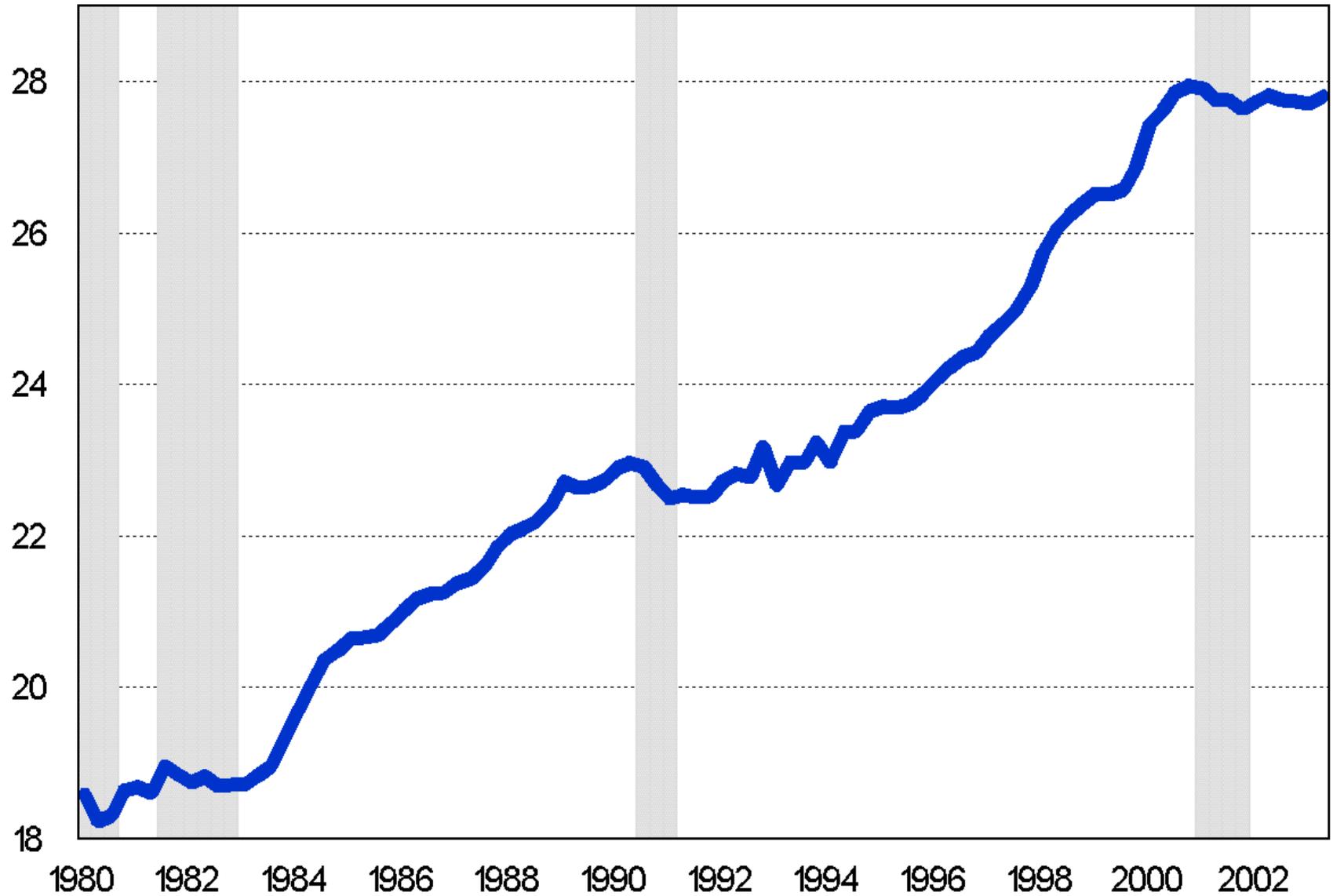


Real Earnings

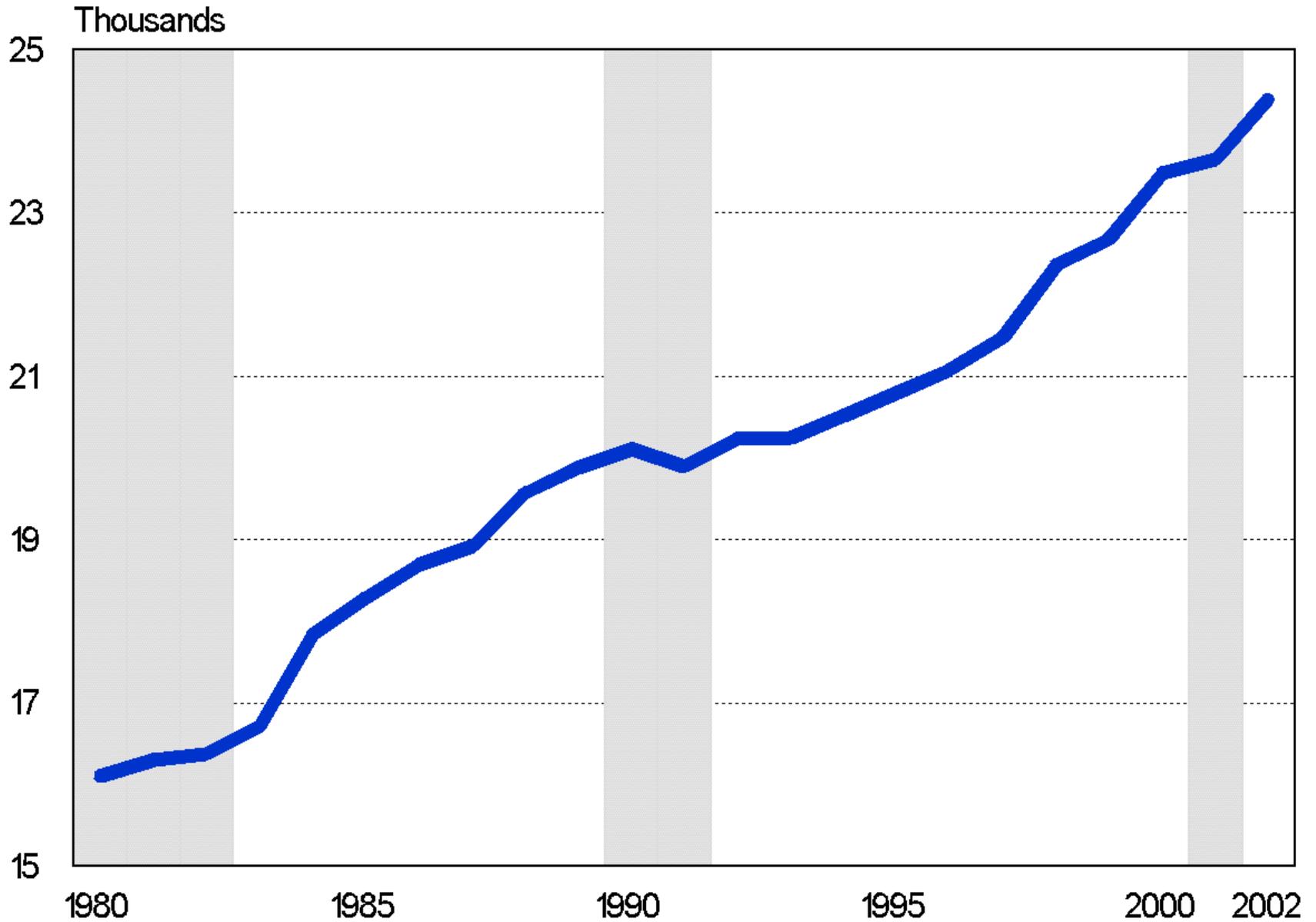


Real Per Capita Income

Thousands

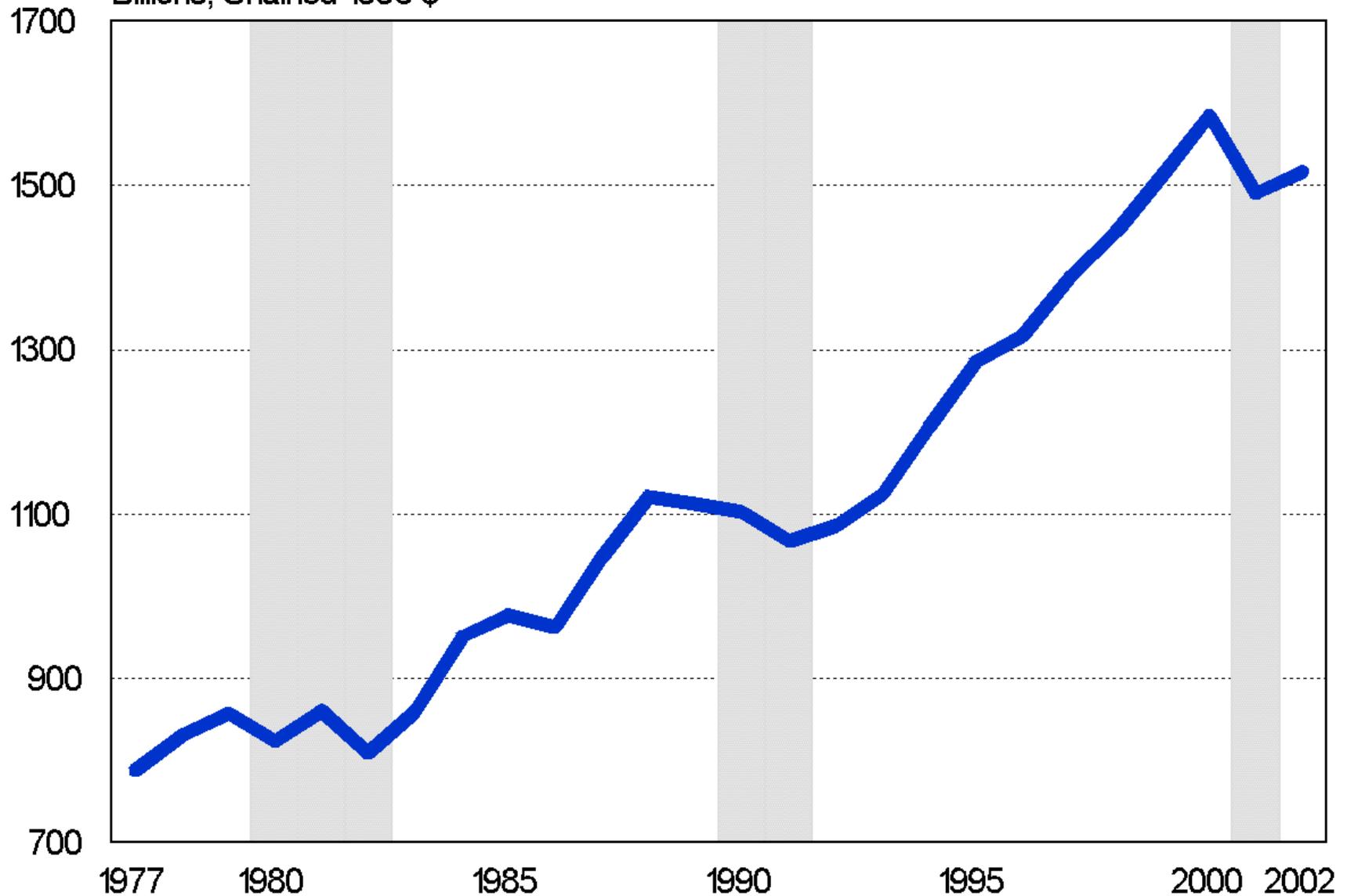


Real DPI Per Capita



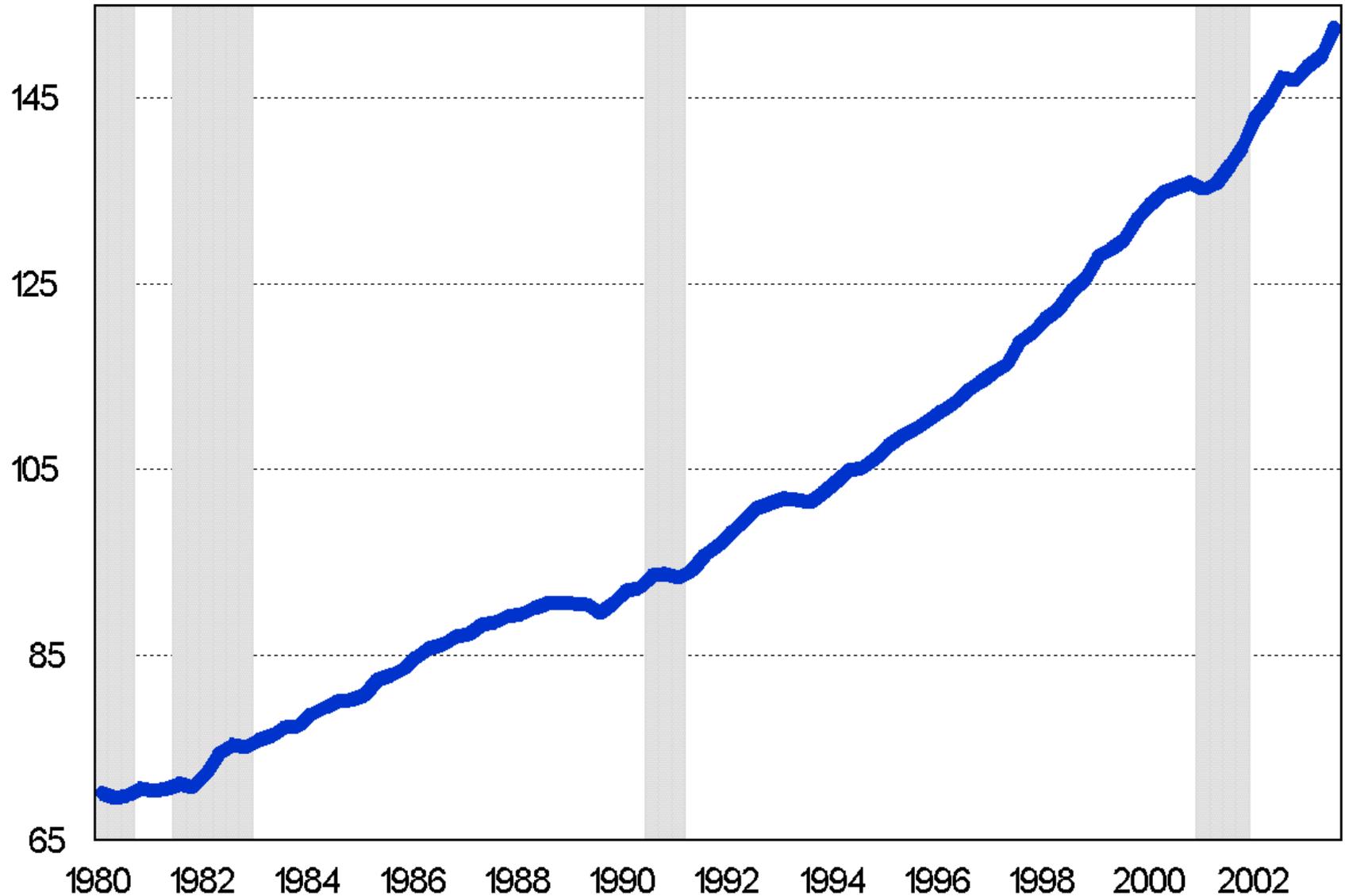
Manufacturing Output

Billions, Chained 1996 \$



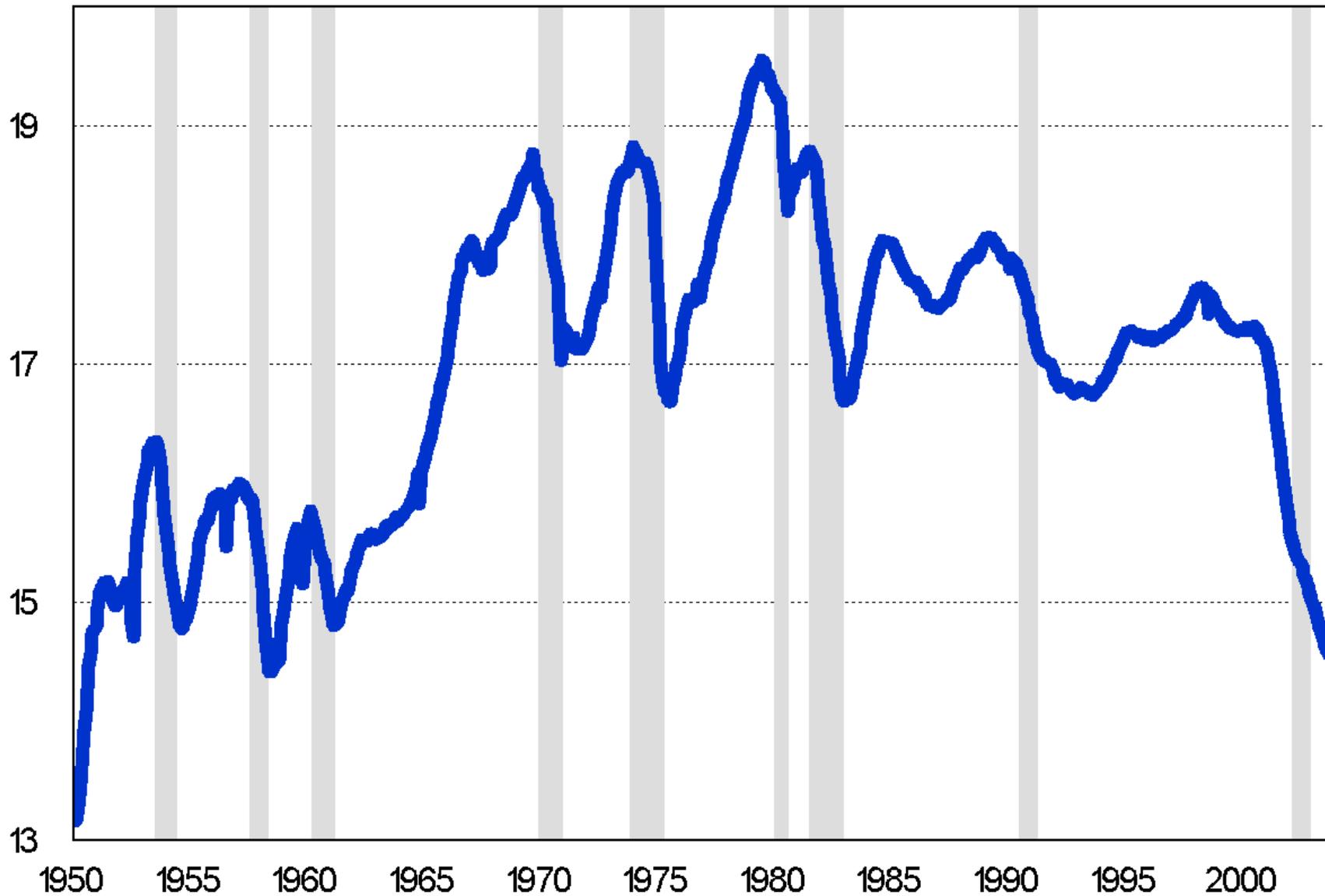
Manufacturing Productivity

SA, 1992=100

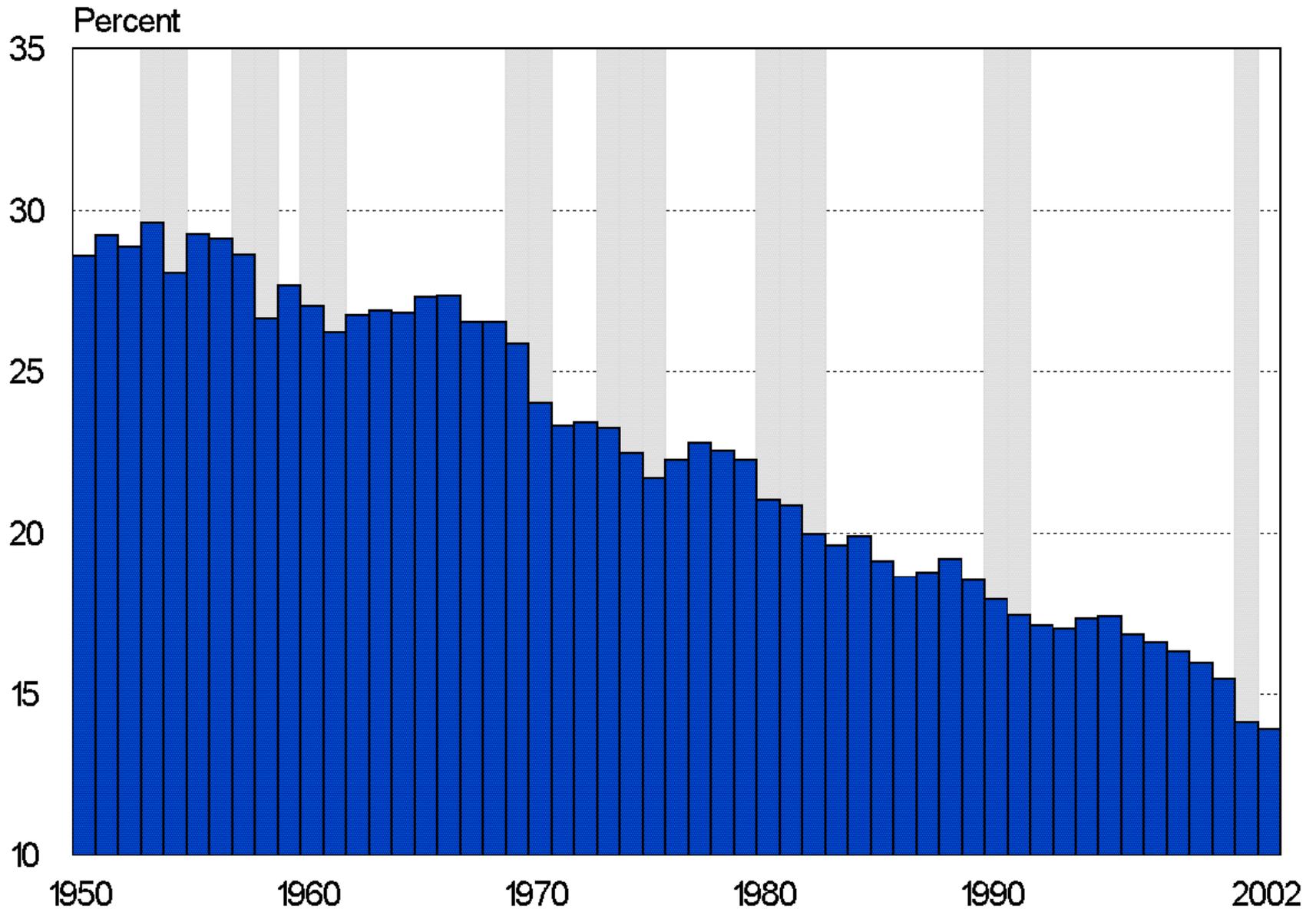


Manufacturing Jobs

Millions



Manufacturing GDP Share



Manufacturing Job Share

Percent of Total Private Jobs

