Road to Economic Recovery to be Paved by the Private Sector

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There's an old saying that "slow and steady wins the race," but when it comes to hastening the nation's economic recovery, positive change can't happen nearly quick enough.

Truth be told, the U.S. economy has lost such a massive amount of jobs in this recession that it is difficult to predict how long it will take before any meaningful restoration of these positions will begin. U.S. payroll employment is now almost 300,000 jobs below the worst month in the previous recession. To provide a bit of perspective, after a severe downward revision in the past year's payroll employment figures, the total U.S. employment for January 2010 was 129,527,000. The minimum payroll employment in the previous recession was 129,822,000 for August 2003.

Unemployment rose in 30 states in January, evidence that jobs remain in short supply in most regions of the country. The official unemployment rate in January was 9.7 percent, but that doesn't include discouraged workers (people who have stopped looking for work) and those who are forced to secure part-time employment in the absence of full-time positions. A more comprehensive calculation would imply a much higher unemployment rate.

So what does this all mean? Well for starters, in many ways, we are facing a "lost decade" in terms of job creation. With only 378,000 jobs added over the past 10 years while the labor force increased by over 12 million over the same period of time, the message is simple – labor supply continues to increase while labor demands tend to be slack.

Estimates for Recovery

In total, almost nine million jobs have been lost since the beginning of the Great Recession. But how fast does the economy have to grow before those positions are back in play? One good way to make that estimation is to look at the following table that shows the beginning and end dates of the last seven recessions since 1970, the number of months in recession (peak to trough), the number of months the economy expanded prior to the recession (trough to peak) and the declines in GDP, industrial production and employment associated with each recession. The table also shows the month when jobs recovered their pre-recession peak, the number of months for job recovery from the recession's end and the associated average annual GDP growth in that time period.

Tracking recessions and job recovery

		Duration in Months		Peak-to-Trough % Change					
Peak	Trough	Recession Peak to Trough	Expansion Preceeding Trough to Peak	Real GDP	Industrial Production	Nonfarm Employment	Month that jobs recover to previous peak	Job recovery Months from recession end	Job recovery Average Annual Real GDP Growth
Dec-07	**Aug-09**	**20**	**73**	**-3.90%**	**-19.20%**	**-6.20%**	**?**	**?**	**?**
Mar-01	Nov-01	8	120	-0.40%	-6.30%	-2.00%	Jan-05	38	2.9%
Jul-90	Mar-91	8	92	-1.30%	-4.30%	-1.50%	Feb-93	23	4.3%
Jul-81	Nov-82	16	12	-2.90%	-9.50%	-3.10%	Nov-83	12	7.8%
Jan-80	Jul-80	6	58	-2.20%	-6.20%	-1.30%	Dec-80	5	8.1%
Nov-73	Mar-75	16	36	-3.10%	-14.80%	-2.70%	Dec-75	9	5.1%
Dec-69	Nov-70	11	106	-1.00%	-5.80%	-1.40%	May-71	6	6.9%
Averages (not including most recent recession)				-1.82%	-7.82%	-2.00%			

Prior to the 1990's recession, companies that laid off workers would hire them back quickly once economic conditions improved. This was partly due to the fact that economic growth, as measured by GDP, was robust coming out of a recession.

In the 1970's and 1980's recessions it took about six months to a year for the job base to return to the pre-recession job level. The average economic growth in those recovery months was from 5% to 8% annually.

However, it's important to note that the time it takes to return to the pre-recession job level has been steadily lengthening. In the early 1990's recession (July 1990 to March 1991), it took almost two years (until February 1993) to regain the jobs lost. The economy grew by only 4% annually in those two years. The job recovery in the 2001 recession was even longer – 38 months (more than three years) from recession's end in November 2001 to January 2005, when the number of jobs finally equaled the prior peak employment in March 2001. Economic growth in the years 2002 through 2004 averaged 2.9% per year.

Two facts suggest that the getting all the jobs back from the losses in the Great Recession could take many years. First, the job base declined by more than 6% in the current recession, three times more than the 2% average decline in the previous six recessions. Second, expectations are that economic growth will be subpar in the next two years. The Congressional Budget Office's most recent forecast calls for 2.2% GDP growth in 2010, followed by 1.9% growth in 2011. The CBO expects growth in 2012 and 2013 to average about 4.7%, and growth to slow again to about 2.5% after 2016.

So there is a simple way to think about the problem. When the economy grows by 7% to 8% per year it takes six months to a year to recover a 2% job loss. When the economy grows by only 3% to 4% per year it takes two to three years to recover from a 2% job loss.

If it took three years in the last recession to recover from a 2% job loss, will it take nine years to recover from a 6% job loss, especially if GDP does not grow more than 2% in the first few years of the recovery? That would mean the year 2018 before we see jobs return to their 2007 level, a startling prediction with dire consequences.

If economic growth returned to the 6% to 8% range, one would expect the job recovery to be quicker. The problem is that the job decline in the Great Recession was 6%, not 2%. Even with double the CBO expected economic growth, it would be four years before the U.S. regains all of the lost jobs in the Great Recession.

Policy and Practicality

What are the policy implications of a slow return to historical job levels?

First, we must remember that the government doesn't actually 'create' jobs. The government simply takes money from one sector of the economy through taxes and fees, and then subsidizes other sectors of the economy. The jobs 'created' by the American Recovery and Reinvestment Act of 2009 are jobs that are being borrowed now against tax increases in the future. In other words, today's stimulus is tomorrow's new tax dilemma.

The first rule of public finance is "do no harm," meaning that taxes shouldn't be onerous enough to stifle entrepreneurship and that subsidies should be targeted to projects that have real value. So at best, we are creating public jobs now that will have to be paid for through higher taxes (or higher deficits) at some point in the future.

At worst we may actually be hampering employment growth by moving money from one sector of the economy to another. We appear to be at an important juncture in our nation's history in terms of health care reform, yet in many ways seem no further along the path of trying to fix what most now believe is a broken system. Any solution to the problem of the uninsured seems to only mean higher health care costs for everyone else.

In addition, economic forecasters hail the impending arrival of a "green economy," but the only way to achieve that goal is to make energy more expensive, which may make business more energy efficient but will also create a new tax on energy producing industries. Jobs gained in so-called "clean" industries will be offset by jobs lost in coal and oil production, automobiles, etc. In other words, we're plugging one hole by creating another.

The truth of the matter is that we didn't lose jobs in this recession because of higher health care costs or the lack of a "green economy." We lost jobs because of the collapse of the financial asset bubble, which was brought about by overinflated real estate values. A bursting housing bubble caused the recession, and it's very difficult to reverse the effects of a collapsed financial bubble; so economic growth will be slow in the recovery, which means that job growth will be equally slow.

Charting a Course for Growth

So how do we rebound and begin crafting a plan for national economic recovery? There is no one correct answer nor one approach to developing a solution. Indeed there are a number of elements that must be in place for significant growth to occur:

Education and Retraining: Bank of America statistics show that the unemployment rate for skilled/highly skilled workers is about 5%, demonstrating that those with higher educational and vocational attainment are still being hired. However, lower skilled and unskilled workers are being laid off in immense numbers and their jobs will in all likelihood not be replaced. Therefore, much more focus needs to be shifted to retraining workers for the jobs of today and tomorrow. Hitching our wagon to “green jobs” is political rhetoric, not reality as the “green industry” simply isn’t ready for an influx of hundreds of thousands of workers. Instead, we need to focus on high demand industries such as health care, science, technology, education, building trades and infrastructure construction.

Understanding of Basic Economics: Federal and state governments need a reality check. If you want less of something, tax it. High taxes and fees on employers and employees serve as a disincentive for growth. The free market system must be allowed to breathe.

Increased Emphasis on Trade: The United States is the largest exporter in the world and 95% of all markets exist outside of our nation’s borders. Trade arrangements which have stalled (Columbia, Panama and South Korea) need to be revisited post haste and new markets need to be identified and acted upon. Protectionism is a failed concept. When the free market isn’t allowed to operate, it only results in Americans paying more for goods and services.

Deficit Reduction: Deficits are weakening the dollar to an alarming degree. We need to get spending under control and spread the existing taxpayer base. There aren’t enough families in the $250,000 and up tax bracket that would allow for absorption of natural growth in spending, even after drastic spending cuts.

Elimination of Uncertainty: Uncertainty leads to economic decline. The expiration of the Bush tax cuts, proposed surtaxes on specific industries, taxes on repatriation of foreign income, cap and trade, health care, redistributive tax credit programs and other tax and spend programs being discussed in Washington are causing Americans and businesses to stow away their cash, preparing for the worst to come. In a period of uncertainty and political volatility, consumer and business demand for goods and services is delayed.

Social Security First Aid: Social Security can be fixed by lowering benefits, increasing the tax rate and tax base and dedicating taxes received from illegal immigrants to a pool for legal workers. This is the only way out. Americans will have to assume a much greater personal role in saving and planning their retirement security.

Conclusion

Economic recovery won't happen overnight – indeed, it took us quite a long time to arrive at this stage in our economic history. However, in times like this, it is always helpful to reflect on what we've learned from history and therein lies a few indisputable truths – that slow economic growth means slow job growth, that the government can move capital from one sector to another, but is unable to create jobs, and most importantly, that the private sector will pave the way for economic recovery, no matter how slowly or quickly that race will be run. There is much work to be done, but the U.S. business community is well equipped to handle the task, armed with history and the ingenuity that makes all good things possible.