

The Unemployment Explosion of the 1970s

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Unemployment has literally exploded in the United States during the 1970s. At the peak of unemployment in 1975, there were nearly three times as many unemployed Americans as there were in 1969. There were as many people unemployed as there were employed in all of manufacturing nondurables. Extremely high unemployment has persisted since 1975. ~~Is this just another bad experience with the same process that brought high unemployment in the previous recession years, 1949, 1954, 1958, 1961, and 1971?~~ This paper takes a look at some evidence about conditions in labor markets during the 1970s. It finds ~~a striking contradiction between high unemployment, which suggests some slack in all years except 1973 and extraordinary slack starting in 1975, and other indicators of conditions in labor markets. These are, first, the rate of wage inflation, which has responded only weakly to the deep recession and accelerated markedly during the eight years, second, lay-off rates in manufacturing, which suggest generally tight conditions~~

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except in 1975, and third and perhaps most surprisingly, very low rates of initial claims for unemployment insurance. The unemployment explosion has not been accompanied by any explosion at all in rates of job loss measured by either variable.

The paper lacks a persuasive explanation for this contradiction. It makes one conjecture that might explain part of the mystery. It concludes with a cautionary note against the belief that unemployment today is just the result of a cyclical shortfall in demand as in past recessions and that the right response is conventional expansion.

Alternative measures of conditions in labor markets.

Unemployment has been high throughout the decade. Table 1 gives unemployment rates for various groups in the labor force as measured in the official household survey. In the total labor force, unemployment was below 5 percent only in 1970 and 1973, when it was 4.9 percent, and has been above 5.5 percent in every other year. In 1975, unemployment hit 8.5 percent, almost two percentage points higher than had ever before been recorded by the survey since its inception in 1947. In 1976, unemployment was at the very high rate of 7.7 percent and the rate for 1977 will probably be about 7.0 percent. Nothing like this has been seen in the U.S. since the Great Depression.

High unemployment has spread throughout the labor force. The relationship among the unemployment rates of different groups is not too different from earlier years. The year 1974 resembles 1964 fairly closely--the unemployment rate for the largest group, adult men, was 3.8 percent in 1974 and 3.9 percent in 1964. Teenage unemployment was 16.0 percent in 1974 and 16.2 percent in 1964. Unemployment among women and blacks was somewhat higher in 1974--5.5 percent and 9.9 percent as against 5.2 percent and 9.6 percent in 1964. Further, the total unemployment rate was higher in 1974--5.6 percent compared to 5.2 percent in 1964. This reflects the shift in the composition of the labor force whose significance was first noted by George Perry [/]. Most of the compositional shift had

[/] "Changing Labor Markets and Inflation", BPEA 3:1970, pp. 411-441.

Table 1. Selected Unemployment Rates, 1955-1976

<u>Year</u>	<u>All workers</u>	<u>Teen- agers</u>	<u>Adult men</u>	<u>Adult women</u>	<u>Blacks</u>
1955	4.4	11.0	3.8	4.4	8.7
56	4.1	11.1	3.4	4.2	8.3
57	4.3	11.6	3.6	4.1	7.9
58	6.8	15.9	6.2	6.1	12.6
59	5.5	14.6	4.7	5.2	10.7
60	5.5	14.7	4.7	5.1	10.2
61	6.7	16.8	5.7	6.3	12.4
62	5.5	14.7	4.6	5.4	10.9
63	5.7	17.2	4.5	5.4	10.8
64	5.2	16.2	3.9	5.2	9.6
65	4.5	14.8	3.2	4.5	8.1
66	3.8	12.8	2.5	3.8	7.3
67	3.8	12.8	2.3	4.2	7.4
68	3.6	12.7	2.2	3.8	6.7
69	3.5	12.2	2.1	3.7	6.4
70	4.9	15.2	3.5	4.8	8.2
71	5.9	16.9	4.4	5.7	9.9
72	5.6	16.2	4.0	5.4	10.0
73	4.9	14.5	3.2	4.8	8.9
74	5.6	16.0	3.8	5.5	9.9
75	8.5	19.9	6.7	8.0	13.9
76	7.7	19.0	5.9	7.4	13.1
77	7.0	17.7	5.2	7.0	13.1
78	6.0	16.3	4.2	6.0	11.9

already occurred by 1969 and only 0.2 or 0.3 percentage points of the worsening of unemployment after 1969 relates to the growing proportion of teenagers and women.

The standard interpretation of these facts holds weak aggregate demand responsible for high unemployment. Two separate recessions, in 1971 and 1975, with no compensating booms, created conditions in the labor market that were distinctly unfavorable on the average. Though most economists grant that the changing composition of the labor force has raised the appropriate target for unemployment to 5 or even 5.5 percent, there is widespread agreement on the need for a cautious expansion to this target. According to the standard view, unemployment is 1.5 to 2 percentage points above the target, or real GNP is 4 to 6 percentage points below potential. The dividend from an expansion to close this gap would be increased output and income of \$80 to \$125 billion in 1978 prices. If the standard view is correct, judicious expansion ought to be the first order of business.

The standard view accepts the proposition that pushing unemployment below the target would stimulate accelerating wage and price inflation. It also accepts the converse: A period of extended unemployment ought to be accompanied by decelerating inflation. Phillips curves estimated by Robert J. Gordon ¹ and others suggest that for each full year that

¹ "Inflation in Recession and Recession and Recovery", BPEA 1:1971, 105-158, "Wage-Price Controls and the Shifting Phillips Curve", BPEA 2:1972, pp. 385-421 and "Can the Inflation of the 1970s be Explained?", BPEA 1:1977, pp. 253-277.

unemployment exceeds the natural or non-accelerating-inflation rate, wage inflation should decelerate by about 0.4 percentage points. This implication is checked against the record in Table 2. Here the natural rate is assumed to be 5.5 percent. The net effect of labor market conditions on wage inflation should have been roughly zero from 1970 to 1974, so the high inflation inherited from the booming 1960s should have propagated itself more or less unchanged through these years. From 1970 to 1973, the data do not refute this prediction. There was a bit less inflation in 1972 (the first full year of wage controls) and a bit extra in 1973. Then a wide gap begins to open. Wage inflation in 1974 was 9.4 percent when it should have been only 6.7 percent given the lack of impetus from conditions in the labor market. In 1975 the deep recession should have decelerated wage inflation to 5.5 percent but instead it rose to 9.7 percent. A further deceleration to 4.7 percent in 1976 and 4.1 percent in 1977 should have occurred and would have brought the economy close to the point of stable prices. Nothing like this has happened. Wage inflation promises to continue at above 8 percent. The net effect of the generally adverse labor market conditions of the 1970s should have been to decelerate wage inflation by 2.4 percentage points; instead it accelerated by over 2 percentage points. By all rights, the problem of inflation should be almost completely solved by now, but it is not. The recession has been an enormous disappointment to those who thought that its one good effect might be the restoration of price stability.

Table 2. Hypothetical and Actual Rates of Wage Inflation in the 1970s

Year	Unemployment rate	Departure from natural rate of 5.5%	Predicted acceleration(+) or deceleration(-)	Cumulative acceleration and deceleration	Actual	
1969				6.5	6.5	4.4
70	4.9	-0.6	.2	6.7	6.7	6.6
71	5.9	0.4	-.2	6.5 6.4?	6.6	6.7
72	5.6	0.1	0	6.5	5.8	6.5
73	4.9	-0.6	.2	6.8	7.8	7.8
74	5.6	0.1	0	6.7	9.4	9.1
75	8.5	3.0	-1.2	5.5	9.7	9.9
76	7.7	2.2	-0.9	4.7	9.0	8.4
77	7.0	1.5	-0.6	4.1	8.6	8.1
78	6.0	0.5	-0.2	3.9		9.4

Notes: For explanation see text. Actual wage inflation is annual percent change in compensation per hour, private nonfarm business.

This disappointment has hardly escaped the attention of students of the Phillips curve. It has reinforced the belief of many in the importance of the feedback from prices to wages. The year when wages accelerated without much stimulus from the labor market, 1974, was also the year when prices rose more than wages because of the increased price of oil. In normal years, wages rise by about 2.6 percentage points more than prices, so the excess wage inflation is attributed by most successful Phillips curves to the efforts of workers to maintain the relation of wages to prices. For the part of the labor force paid under cost of living escalators, this response is automatic. For the rest (the great majority), considerations of equity somehow overrule the market forces that ought to limit the response of wages to an increase in other costs of production.¹

¹ James Tobin put the contrary argument well, writing in early 1974: "In the fight against inflation, the urgent matter in 1974 is to keep the fuel-food bulge in prices from escalating the rate of wage inflation. From the record so far, one can be moderately hopeful, and there are reasons why one would not expect rising commodity prices to pull wages all the way up after them. These price increases do not improve the bargaining power of most employees. They do not inflate the profits of employers or the value to them; in many instances the opposite is true. They do not distort the pattern of relative prices and provoke another round of wage-wage spiral. Still, with George Meany talking 12 percent, no one would underrate the problem." ("Monetary Policy in 1974 and Beyond", BPEA, 1:1974, ~~00~~^{PP.} 219-232.). I would guess that most economists judge Tobin the loser in this

prediction. But some of the evidence of this paper suggests that Tobin may not have been as wrong as many think.

Suppose, for the moment, that one accepts the special influences of oil price increases in 1974 and goes further to say that 9.4 percent wage inflation became the new base from which acceleration or deceleration occurred (a very strenuous assumption since nobody thought that similar increases would occur every year after 1974). Even then, 2.6 percentage points of deceleration should have occurred by 1977, when actually only 0.7 points occurred. There is more to the mystery of high wage inflation during the recession than can be explained by special considerations in 1974. Wage inflation seems much less responsive to unemployment than it used to be, or the natural unemployment rate is higher.

There is a quite separate body of evidence that raises similar questions about the weakness of labor markets in the 1970s. Layoff rates in manufacturing have historically been closely related to overall unemployment even though manufacturing itself accounts for only about 20 percent of employment. About 25 percent of the unemployed have worked most recently in manufacturing in a typical year and this rises to over 30 percent in recessions. In a remarkably prescient Brookings Paper published in 1971, Charles Schultze observed a departure from the long-run relationship between unemployment and layoffs starting in the mid-1960s.^L

^L "Has the Phillips Curve Shifted? Some Additional Evidence", BPEA 2:1971, pp. 452-467.

The departure has become many times more significant since he wrote. Table 3 presents data on the layoff rate. Look first at 1973. The pattern of unemployment in 1973 was similar to the pattern in 1964. But the layoff rate in 1973 was 0.9 percent, far below the rate of 1.7 in 1964 and in fact well below anything experienced during the boom years of the 1960s. An equal surprise is the low level of layoffs in 1975--2.1 percent--which is well below the rate of 2.6 percent in 1958 and even below the rate of 2.2 percent recorded in 1961. In 1976, according to the layoff rate of 1.3 percent, conditions were about the same as in 1965-66, when the unemployment rate was 4.1 percent, as against the 7.7 percent rate reported for 1976. From the evidence of layoff rates, the 1970s were years of tight and very tight labor markets, interrupted by a single year of mild recession, 1975. ~~The failure of wage inflation to decelerate is no mystery if layoffs are taken as a measure of labor markets pressure in place of unemployment.~~

Manufacturing is not the whole economy. A second measure of the involuntary flow of workers out of jobs is available from the records of unemployment insurance programs. The percentage of covered workers making new claims each month, also shown in Table 3, is an economy-wide measure of the flow into unemployment out of jobs, primarily but not exclusively via layoffs. Its evidence is completely consistent with the evidence from manufacturing layoff rates. Unemployment insurance claims have been made at a much lower rate in the 1970s than would be predicted by the high unemployment rates. In 1973, fewer UI claims were made per worker than in any previous postwar year except 1969. Far fewer claims

Table 3. Layoffs and New Claims for Unemployment Insurance, 1955-1976

Year	Layoff rate (percent per month)	New UI claims per worker (percent per month)	
1955	1.5	2.7	
56	1.7	2.6	
57	2.1	2.9	
58	2.6	4.0	
59	2.0	3.1	
60	2.4	3.6	
61	2.2	3.7	
62	2.0	3.2	
63	1.8	3.1	
64	1.7	2.7	
65	1.4	2.3	
66	1.2	1.9	
67	1.4	2.0	
68	1.2	1.7	
69	1.2	1.6	
70	1.8	2.4	
71	1.6	2.4	
72	1.1	2.1	
73	.9	1.8	
74	1.5	2.4	
75	2.1	3.1	3.1
76	1.3	2.6	2.5
77	1.2	2.4	2.4
<u>78</u>	<u>.9</u>	<u>2.1</u>	<u>2.1</u>

Notes:

Layoff rate is the percentage of all workers in manufacturing who are laid off each month (annual average of monthly data).

New claims per worker is the percentage of all workers covered under state unemployment compensation who file new claims each month (annual average of weekly data multiplied by 4.3).

were made in 1975 than in 1958. Again, conditions appear much tighter when measured by the flow of new claims in place of the unemployment rate. This is especially surprising in view of the prevailing opinion that UI has become more generous and attractive in the 1970s. The unemployment explosion has not been accompanied by an explosion in new recipients of unemployment compensation.

The changing character of unemployment

The most important change in the character of unemployment in the United States is the growing importance of joblessness among the unemployed. Only since Martin Feldstein's recent work [/] have economists

[/] "The Importance of Temporary Layoffs: An Empirical Analysis", BPEA 3:1975, pp. 725-744.

become aware that some of the unemployed are not jobless. In the 1960s, many of the unemployed were on temporary layoff from jobs and had good reason to expect to return to them. But all the evidence suggests that temporary layoffs have almost nothing to do with the recent explosion in unemployment. Though we know very little else about the unemployed, it is apparent that very few of them have jobs.

Within manufacturing, the role of temporary layoffs has been investigated with great care recently by David Lilien.[/] He has inferred

[/] The Cyclical Pattern of Temporary Layoffs in United States Manufacturing, Ph.D. dissertation, Department of Economics, MIT, August 1977.

the pattern of temporary layoffs from data on layoff and recall rates, with the following results:

Year	Fraction of the labor force on temporary layoff	Fraction of the labor force unemployed
1965	1.7	4.9
66	1.3	3.2
67	1.4	3.6
68	1.3	3.3
69	1.1	3.3
70	1.6	5.6
71	1.8	6.8
72	1.5	5.6
73	1.1	4.3
74	1.6	5.7
75	3.3	10.9

The years 1965 and 1975 are roughly comparable in terms of conditions in the manufacturing labor market. In 1965, 2.3 percent of those workers who were working in manufacturing or had most recently worked there were unemployed and jobless. In 1974, the fraction rose to 4.1. In the recession in 1975, the great bulk of the increase in manufacturing unemployment represented genuine joblessness.

Lilien's findings are consistent with data recently made available for the economy as a whole. In 1976, of the 6.3 million unemployed

workers, 3.2 million had lost jobs but only 853,000 of them were on layoff.¹ Eighty-six percent of the unemployed were jobless.

¹This statistic is to be distinguished carefully from the number of non-job-seekers reported in the survey and the subject of recent controversy.

Feldstein's and Lilien's evidence for manufacturing shows that the great majority of layoffs are temporary--70 percent in normal years and 80 percent in recessions. The unimportance of temporary layoffs in total unemployment reflects a combination of the following considerations:

1. Outside of manufacturing, especially in trade and services, a lower fraction of layoffs are temporary.
2. The duration of unemployment among those who have truly lost their jobs is longer.
3. Layoffs account for less than half of the unemployed in times other than deep recession. More than half the unemployed have previously been out of the labor force or have quit their previous jobs.

Layoffs in manufacturing account for a tiny and shrinking fraction of the total flow of workers into unemployment. In 1964, 510,000 people became unemployed each week. Total layoffs in manufacturing were 68,000 per week, or 13 percent of the flow into unemployment (and not every laid off worker becomes unemployed--some take other jobs immediately). In 1974, a comparable year, the flow into unemployment had risen to 771,000

per week, while layoffs in manufacturing ^were essentially the same as in 1974, 70,000 per week or 9 percent of the flow into unemployment. Workers employed in manufacturing are less likely to become unemployed than those employed elsewhere, and manufacturing is a small and declining fraction of the total economy. The rather special institution of the temporary layoff in manufacturing is not very important relative to the magnitude of the unemployment explosion.

Today, the typical unemployed workers is a young man or woman, previously employed in the trade or service sector but now genuinely jobless. The unemployment explosion is mainly a tremendous increase in the number of such people. Between 1969 and 1973, for example, the number of unemployed workers who had previously been employed in trade and services rose from 954,000 to 1,515,000, or 59 percent, while the comparable increase for manufacturing was from 708,000 to 925,000, or 31 percent. The central problem of unemployment continue to be the high frequency of short spells of unemployment, concentrated disproportionately among the young and disadvantaged.[/] The data shown in

[/]The conclusion of my "Why is the Unemployment Rate So High at Full Employment?", BPEA 3:1970, pp. 369-402, seems to hold even more strongly today than when it was written.

Table 4 suggest little departure from the historical relation between the unemployment rate, the frequency of unemployment, and the duration of unemployment in the 1970s. When unemployment is around 5 percent, as

Table 4. Unemployment Rate, Average Duration of Unemployment, and
Frequency of Unemployment, 1955-1976

Year	Unemployment rate, percent	Average duration, (weeks)	Frequency, percent per month
1955	4.4	7.1	2.7
56	4.1	6.5	2.7
57	4.3	6.8	2.7
58	6.8	8.7	3.4
59	5.5	7.9	3.0
60	5.5	7.5	3.2
61	6.7	8.7	3.3
62	5.5	7.8	3.1
63	5.7	7.7	3.2
64	5.2	7.4	3.0
65	4.5	6.9	2.8
66	3.8	6.1	2.7
67	3.8	6.1	2.7
68	3.6	5.9	2.6
69	3.5	5.8	2.6
70	4.9	6.4	3.3
71	5.9	7.4	3.5
72	5.6	7.3	3.3
73	4.9	6.5	3.3
74	5.6	6.6	3.7
75	8.5	9.0	4.1
76	7.7	8.7	3.8
77	7.0	7.9	3.8
78	6.0	7.2	3.6

Notes: Frequency is measured as the number of people unemployed fewer than five weeks divided by the labor force and adjusted (i) by dividing by 3.3 to obtain the weekly frequency and (ii) multiplying by 4.3 to convert to monthly. The conversion factor of 3.3 was derived from unpublished data on the duration of unemployment by single weeks. Average duration is the unemployment rate divided by the frequency and converted to weeks by multiplying by 4.3.

in 1964 or 1973, each month about 3 workers become unemployed for each 100 in the labor force. This can fall as low as 2.6 in very tight markets or rise to over 4 in deep recessions. The duration of unemployment moves in the same way--the typical spell of unemployment lasts 7 weeks in normal times, falls below 6 weeks in booms, and rises to 9 weeks in recessions. Even in recessions, unemployment is a very transitory experience for the typical unemployed worker. Whatever trend is visible in Table 4 is toward even briefer and more frequent spells at any given unemployment rate. This probably reflects the shift in the composition of the labor force and nothing more.

It is hard to find any hint in the survey data on the unemployed, broken down by virtually any personal characteristic, that indicates important change in the nature of unemployment that would point in the direction of large increase in the natural, equilibrium, or "full employment" unemployment rates. Though we still lack a good understanding of why people lose or leave their jobs so frequently, and wind up looking for new work, the pattern of this activity has not changed in the 1970s--there are just many more people doing it now. Nothing seems to refute the view that inadequate demand is causing jobs to terminate more rapidly now than ten years ago and is making it harder to find new work. But the puzzles of continuing high rates of wage inflation and low layoffs and UI claims remain unexplained. Only a total optimist would remain untroubled with the inadequate demand explanation of the unemployment explosion and confident that the full-employment target should be 5 or 5.5 percent unemployment.

A possible influence of changes in unemployment insurance

Though new claims for UI have remained at remarkably low levels throughout the 1970s, there has been an explosion in the fraction of the labor force drawing benefits from UI. Table 5 presents data on unemployment as viewed from the UI system. UI benefits are paid under state programs for up to 26 weeks of unemployment, and under federal-state programs for extended benefits beyond 26 weeks in some years of recession. The typical duration of unemployment as measured by the UI system can be derived by dividing the number of people recorded as unemployed by the flow of new claims. This is done in Table 5 first for the state programs, where only those unemployed 26 or fewer weeks are counted, and second for the state programs together with those receiving extended benefits. The typical spell with the state UI system lasted six weeks in 1964, almost 7 weeks in the recession of 1958, and as little as 5.2 weeks in the boom of the late 1960s. This relation seemed quite stable through 1970. Then in the recession of 1971, it rose to 7.3 weeks, well above its previous high of 5.8 weeks in 1958. In 1972 and 1973, duration remained above its historical relation to unemployment. In 1974, duration fell to 6.2 weeks, only slightly above would be predicted by the unemployment rate but far above its usual relation to the claim rate.¹ Then in

¹The claim rate was only 2.4 percent per month in 1974. Comparable years are 1965 with claims at 2.3 percent and duration at 5.7 weeks, and 1956 with claims at 2.6 percent and duration at 5.4 weeks.

Table 5. Unemployment Rates and Durations for Unemployment Insurance Programs, 1955-1976

Year	Unemployment rate, state programs (percent)	Average duration, state programs (weeks)	Unemployment rate, all programs (percent)	Average duration, all programs (weeks)
1955	3.5	5.6	3.5	6.2
56	3.2	5.4	3.1	5.8
57	3.6	5.4	3.6	5.8
58	6.4	6.8	7.4	8.9
59	4.4	6.1	4.6	7.6
60	4.8	5.8	4.5	6.3
61	5.6	6.5	6.5	8.6
62	4.4	5.9	4.1	6.4
63	4.3	6.1	4.1	6.6
64	3.8	6.0	3.5	6.5
65	3.0	5.7	2.8	6.3
66	2.3	5.2	2.1	5.6
67	2.5	5.3	2.3	5.6
68	2.2	5.5	2.0	5.9
69	2.1	5.5	2.0	5.9
70	3.4	6.1	3.5	7.0
71	4.1	7.3	4.4	8.8
72	3.5	7.1	3.3	8.4
73	2.7	6.6	2.6	7.3
74	3.5	6.2	3.5	7.0
75	6.0	8.3	7.0	10.3
76	4.6	7.7	NA 5.2	9.9
77	3.9	7.0	4.1	
78	3.3	6.8		

Notes: Average duration, state programs is unemployment rate for state programs divided by claim rate, Table 3, multiplied by 4.3. Average duration, all programs is unemployment rate, all programs divided by state claim rate (new claims are not required for extended benefits). This procedure omits a small flow of new claims for federal programs other than extended benefits.

1975 duration jumped to 8.3 weeks, 22 percent above its level of 6.8 weeks in 1958. Duration has remained far above normal since then.

The calculations for regular and extended benefits tell a very similar story, with more cyclical variation both before and during the 1970s.

How can it be that the duration of unemployment as recorded by the UI system has grown so rapidly at the same time that duration as recorded by the household survey has been stable or falling? Unemployment as measured by the UI system is about half of the unemployment reported in the survey:

Year	UI Unemployment (thousands)	Survey unemployment (thousands)	Survey unemployment because of job loss (thousands)
1958	3269	4602	NA
64	1753	3786	NA
67	1270	2975	1049
70	2070	4088	1658
71	2608	4993	2133
72	2192	4840	2021
73	1793	4304	1472
74	2558	5076	1726
75	4943 4937	7830	4391
76	3822 3846	7288	3201
77	3111	6855	
78	2640	6047	

On the other hand, UI unemployment exceeds the number of people recorded in the survey as unemployed because of job loss (as opposed to quits or entering the labor force). This gap was fairly small until 1974 when it jumped to 832,000 or 48 percent of job-losers. Those eligible for UI benefits but not classified in the survey as job-losers would include

workers who have quit and completed the waiting period to qualify for benefits and those who lost jobs, left the labor force, re-entered, and claimed benefits. In 1974, the survey recorded only 566,000 as unemployed because of quitting, so even if all quitters now draw benefits, a substantial part of the gap must come from the 1.8 million unemployed re-entrants.

During the 1970s, the UI system became available to a growing fraction of the labor force:

Year	Employment covered by UI (thousands)	Total civilian wage and salary workers (thousands)	Ratio (percent)
1960	46,334	59,692	78%
65	51,580	65,176	79
70	59,526	74,382	80
71	59,375	74,609	80
72	66,458	77,186	86
73	69,897	80,348	87
74	72,451	81,905	88
75	71,037	80,275	88
76	73,459		
77	76,419		

Average benefits paid remained stable at a low fraction of average earnings:

Year	Average UI weekly benefit	Average gross weekly earnings	Ratio
1960	\$33	\$81	41%
65	37	95	39
70	50	119	42
71	53	127	42
72	57	136	42
73	59	145	41
74	64	154	42
75	70	164	43
76	75	175	
77	78	187	

The explosion in UI recipients is certainly not the result of a large increase in its relative financial attraction. But UI might have a role in explaining the contradictory evidence about conditions in the labor market in the 1970s along the following lines: The market really was fairly tight in every year except 1975, and is tight today. Thus wage inflation has remained at high rates and layoffs and initial claims for UI have been low. However, several million low-wage workers have discovered the virtues of unemployment compensation as an alternative to the limited selection of disagreeable jobs available to them. The UI system has faced a sudden increase in the number of its clients just as every other income maintenance program has, especially public assistance and food stamps. The number of people filing claims on this account has been lost in the avalanche of legitimate claims for temporary

unemployment, but this group remains on UI benefits far longer than the typical legitimate claimant. Thus the duration of benefits rose while the frequency of claims remained about the same. Since conditions in the labor market were truly strong, the household survey should have shown a low duration of unemployment. But duration has been pushed upward by this group, and appears to be consistent with the reported high unemployment rates.

To explain the puzzle of the unemployment explosion, this hypothetical group of predators on the UI system must account for at least a million unemployed workers in recent years. They must be spread among the population more or less in proportion to the incidence of unemployment, since there has been little change in relative unemployment rates during the 1970s. Of course, this means that a disproportionate share are young and earn low wages, because unemployment falls most heavily on these groups already.

It is difficult to prove or disprove this conjecture. The UI system provides only very limited information about the characteristics of those receiving benefits, and absolutely nothing about the flow of new claimants beyond their number. Until last year, the household survey did not inquire about UI benefits. A further investigation of information from individual states about legal and administrative changes in UI may be of some help.

One additional scrap of evidence seems consistent with the conjecture. The "uninsured unemployment rate", the ratio of the number of unemployed not receiving UI benefits to the total labor force, has not exploded in the 1970s:

Year	Uninsured unemployment rate
1958	2.0
59	2.4
64	2.8
67	1.5
70	1.6
71	2.1
72	2.5
73	2.3
74	1.7
75	2.9
76	2.6

This rate measures primarily the role of new entrants to the labor force and re-entrants who have been out of the labor force long enough to disqualify them from UI benefits.[/] The flood of former

[/]The data from the household survey on unemployed re-entrants apparently contain a fairly large number of people who do qualify for benefits because they have been out of the labor force very briefly.

housewives who entered the labor force during the 1970s does not seem to be a contributor to the unemployment explosion.

Conclusions

In 1974, James Tobin wrote, apropos of a paper of mine:

It has been a dismal experience over the years to come to the Brookings panel meetings and see the empirical long-run Phillips curve shift steadily upward and become steeper and steeper. Now Hall has outdone his predecessor, including himself, and tells us that the natural rate of unemployment...is about 5.5 percent. I find one consolation in this estimate. No one can identify 5.5 percent natural rate with optimal unemployment or voluntary search unemployment or frictional unemployment matched by vacancies.¹

¹ BPEA 2:1974, p. 399.

There is some evidence that the dismal experience is continuing. Certainly 5.5 percent seems the lowest defensible estimate of the non-accelerating or natural unemployment rate. The suspicion is justifiable that it is somewhat higher. Certainly I must agree with Tobin that 5.5 or 6.5 percent cannot be the optimal rate of unemployment. Something is making unemployment much higher than it should be. Until we find out what it is, we need to be careful in pushing unemployment too far down, because the problem may not be weakness of demand.