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Unemployment a Secular Problem

Last Friday's employment report was a Rorschach test for economists. (You know, show an inkblot and find the obsession.) It's not a surprise that the response to the report was pessimistic. We heard all kinds of rhetoric, including a new one - "Zombie Economy."

A Zombie is an ["animated corpse brought back to life by mystical means."](#) We think the pundits who dreamed this one up are saying stimulus brought the economy back to life, barely. And they think this fits recent soft payroll data. Payroll gains have slowed to 75,000 per month in Q2 from 226,000 per month in Q1. The jobless rate seems stuck around 8.2%.

But there was some better data, too. Private payrolls did rise – for the 28th straight month – and the jobless rate is stable, not rising as it would in a recession. Moreover, the same slowing in jobs data happened at about the same time last year, which suggests some problems with seasonal adjustments. On a not-seasonally-adjusted basis, the US added 815,000 new jobs in June, which is a very active Zombie.

Civilian employment, an alternative measure of job creation that includes small business start-ups rose 128,000 in June. In addition, total hours worked in the private sector hit a new high for the recovery.

The Zombie label is a misnomer, this economy is not the walking dead...it never really died; it's the same economy, but it is carrying a heavier burden. Investors, analysts, and economists are comparing today's jobless rate to recent cycles. The boom of the 1980s brought the jobless rate down to 5.0%, in the dot.com era of the 1990s it fell to 3.9%, and during the housing bubble of the 2000s unemployment fell to 4.4%.

They should be comparing it to Europe's sustained high level of joblessness in recent decades or to the US in the 1970s. The unemployment rate is high today because of secular, or long-term, issues, not cyclical, short-term issues.

Government spending, regulation and taxation, including the anticipation of Obamacare, are weighing on economic

activity and pushing up the unemployment rate. It's like putting a 250 lb. jockey on a race horse or making a Plow Horse move through clay. Government was big in the 1970s which boosted unemployment. Government shrunk in the 1980s and 1990s and unemployment fell.

In recent years federal spending has climbed to about 25% of GDP – the highest on record absent a full-mobilization war, like World War I or II. As long as government remains this large – and it *will* if health care reform is not overturned by the voters this November – no one should reasonably expect the jobless rate to go down anywhere near prior lows.

In other words, we take the *secular* side of the recent debate. We believe high unemployment is here because government is too big. Not surprisingly, [many government officials, including IMF chief, Christine Lagarde](#), argue that high unemployment is a *cyclical* issue that can be fixed by stimulus. They urge more spending and more Fed ease.

But, this makes no sense. If government takes money from business to spend on highways or solar energy, jobs are created. However, the money can't be used twice, and the private sector is smaller and has fewer jobs. If government is more productive with its funds than the private sector then the economy wins. But history shows that when government is big, unemployment is higher than when government is small.

And when government is big, even monetary policy cannot boost growth for long. In 1979, the Fed drove unemployment down to 5.6%, but created double-digit inflation in the process. It wasn't until the 1980s, when government spending was reduced as a share of GDP, tax rates were cut, and the Fed tightened, that unemployment fell permanently.

If the IMF and global politicians want lower unemployment and faster growth, they need to stop stimulating and start cutting. Lower marginal tax rates, freer trade, and a smaller welfare state are the answer. Until then, be happy with a Plow Horse. It ain't a race horse, but it ain't a Zombie either.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
7-9 / 2:00 pm	Consumer Credit - May	\$8.0 Bil	\$11.0 Bil		\$6.5 Bil
7-11 / 7:30 am	Int'l Trade Balance - May	-\$48.5 Bil	-\$49.5 Bil		-\$50.1 Bil
7-12 / 7:30 am	Import Prices - June	-1.8%	-2.5%		-1.0%
7:30 am	Export Prices – June	-0.2%	-0.7%		-0.4%
7:30 am	Initial Claims – July 7	370K	374K		374K
7-13 / 7:30 am	PPI - June	-0.4%	-0.4%		-1.0%
7:30 am	"Core" PPI - June	+0.2%	+0.2%		+0.2%
8:55 am	U. Mich Consumer Sentiment	73.5	74.0		73.2