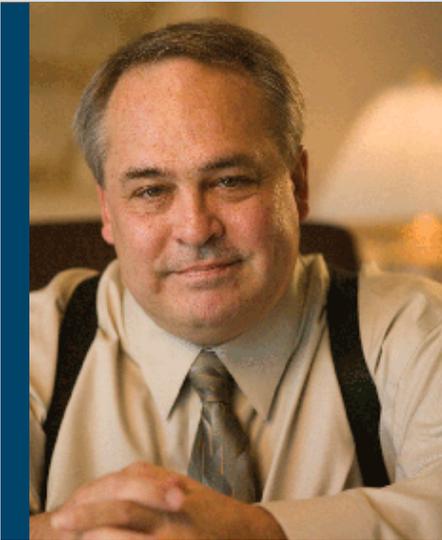


Weaving a Web for Watching Indicators



DAVE ALTIG is executive vice president and research director of the Atlanta Fed.

The interest in the Fed's reaction to labor market reports has always been intense, given the employment half of the Fed's dual mandate (price stability and full employment) from Congress. But this attention has been heightened since the Federal Open Market Committee (FOMC) announced, first in September 2012, that it will continue its asset-purchase programs (often called quantitative easing) as long as "the labor market does not improve substantially."

The Atlanta Fed's view on what will determine "substantial" improvement in the labor market is multifaceted. As outlined by President Dennis Lockhart in a November 2012 speech:

For policy purposes, I think it's appropriate to be cautious about relying on a single indicator of labor market trends—for example, the unemployment rate—to determine whether the condition of substantial improvement has been met.

President Lockhart added:

The starting point certainly should be the headline unemployment rate and the payroll jobs number. The interpretation of movements in these two statistics would be enriched and reinforced by a review of additional data elements.

Here are examples of what President Lockhart is looking for:

First, I would look for lower unemployment rates that are driven by increased flows of job seekers into employment. I would not interpret discouraged workers

dropping out of the labor force as a sign of improvement, even if the unemployment rate falls as a consequence.

Conversely, I'd like to see growing public confidence in the labor market as measured by increased movement of people from out-of-the-labor-force status into the labor force—that is, growing labor force participation. I would interpret a reduction in the number of marginally attached workers as a sign of improvement, even if the unemployment rate goes temporarily higher.

Third, I'd look for employment gains that are associated with reductions in underemployment. I would interpret a pickup in job growth less positively if it is associated with increases in part-time jobs for people who seek full-time work.

Finally, I'd like to see signs that improvements in all these indicators are gaining momentum and are sustainable. A framework for assessing labor market conditions needs to include forward indicators of labor market health, such as falling claims for unemployment insurance.

The Atlanta Fed has developed a visual tool to help us track labor market trends. I wrote about this in a January 10, 2013, Atlanta Fed *macroblog* post titled "Visualizing Improvement."

We've organized a collection of variables we find interesting, grouped in

four broad categories. In the category of *employer behavior*, we include payroll employment (from the U.S. Bureau of Labor Statistics' [BLS] Establishment Payroll Survey, also known as the Current Employment Statistics survey), job vacancies or job openings, and hires (from the BLS's Job Openings and Labor Turnover Survey, or JOLTS). Variables in the *confidence* category include hiring plans (from the Na-

we capture *leading indicators* with initial claims for unemployment insurance (from the U.S. Department of Labor), difficulty in filling jobs (from the NFIB small business jobs report), and temporary help services employment (from the CES).

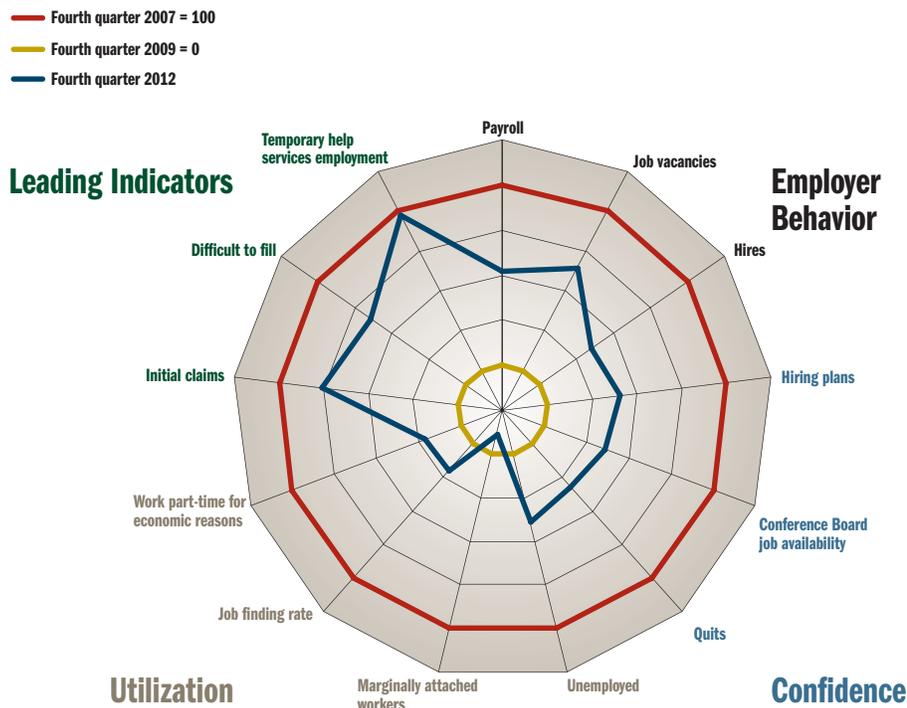
A prototype of how all of this information might be visualized simultaneously appears on the following "spider chart."

The chart tells a familiar, but not too happy, story. Only one of the variables in the collection of employer behavior, employee and employer confidence, and labor resource utilization categories has recovered even half the gap from its prerecession benchmark. The labor resource utilization variables look particularly bad, with one variable—marginally attached workers—actually getting worse over the recovery as a whole. On the brighter side, the leading-indicator variables are looking relatively strong, perhaps foreshadowing improvement.

The interpretation of this type of chart comes with several caveats. First, a variable such as the level of payroll employment will eventually exceed its prerecession level and grow consistently over time as the population grows. A variable like "hiring plans"—which is the net percentage of firms in the NFIB survey expecting to hire employees in the next three months—cannot grow without bound. Thus, the spider charts by construction are about visualizing the transition to some fixed benchmark, not a device for monitoring labor markets over the long run.

Second, it is not obvious that levels from the fourth quarter of 2007 are necessarily the best benchmarks for all (or even any) of the variables we are monitoring. For example, the demographics associated with the aging of the baby-boom populations have arguably slowed the long-term trend in employment growth, meaning that a return to prerecession payroll jobs will be slow even in the circumstance that we would characterize as a "substantially" improving labor market.

Finally, signs of labor market improvement sufficient to alter the pace of FOMC asset purchases may be more about momentum or steady progress than about the return to a specific target or threshold. Nonetheless, we see this approach as providing broader insight into labor market developments. ■



Note: The value for the fourth quarter 2012 represents the September–November average.
Source: U.S. Bureau of Labor Statistics, U.S. Department of Labor, National Federation of Independent Business, Rob Shimer's calculations, and Atlanta Fed calculations

tional Federation of Independent Business's [NFIB] jobs report), job availability (from the Conference Board's Consumer Confidence Survey), and quits (from JOLTS). The *utilization* group contains unemployment (from the BLS's Current Population Survey, or CPS), marginally attached workers (from the CPS), the job-finding rate (defined as the ratio of short-term to long-term unemployed as described in work by University of Chicago professor Rob Shimer), and workers who are part-time for economic reasons (from the CPS). Finally,

The red circle at the perimeter of this chart represents labor market conditions that existed before the recession got under way. The yellow circle at the chart's center represents the time when payroll employment reached its trough in late 2009. The irregularly shaped blue figure depicts the latest three-month average for each of the indicators relative to the benchmarks. This type of point-in-time snapshot provides us with a picture of how labor market conditions have evolved over the past four years.