

**TESTIMONY OF HARRY J. HOLZER**  
**BEFORE THE JOINT ECONOMIC COMMITTEE**  
**ON IMPROVING ASSISTANCE FOR THE UNEMPLOYED**

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As the U.S. economy continues to show modest growth, the nation's labor market remains soft. Employment and labor force activity remain well below the levels achieved in the late 1990's, and unemployment remains high. In addition, a number of groups suffer from serious long-term labor market difficulties that are unrelated to the current economic downturn.

How serious are the current problems that we experience in U.S. labor market – both those related to the business cycle and those reflecting longer-term structural factors facing specific groups of workers? What are the appropriate policy responses to these issues? Are the Bush Administration proposals for Personal Reemployment Accounts (PRA) and cuts in job training programs, along with their reluctance to extend federal Unemployment Insurance benefits, the most sensible approaches to these issues?<sup>1</sup> What other alternatives might be considered?

Below I argue that the U.S. labor market suffers from two sets of employment problems – one that might be labeled *cyclical* (or short-term) and the other *structural* (or long-term). On the first issue, the labor market continues to show very sluggish performance, and that the current unemployment rate is not the best indicator of that

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<sup>1</sup> I will not be addressing some other Bush Administration proposals here regarding reauthorization of the Workforce Investment Act (WIA) or on the devolution of greater authority over Unemployment Insurance to the states.

sluggishness. On the second issue, particular groups (such as less-educated minority men) suffer worsening labor market difficulties that are unrelated to the downturn.

While it has some positive features, the Administration's PRA proposal alone is not an adequate response to the short-term cyclical problem; and proposed cuts in funds for training programs could aggravate the longer-term structural problems. Instead, we need to extend federal Unemployment Insurance (UI) benefits while the downturn remains serious, preserve or increase funding for training programs, and consider some additional measures to improve the job market prospects of less-educated young workers.

## **Employment and Unemployment: What are the Problems?**

### **1) Cyclical Joblessness**

As of January 2003, the nation's unemployment rate stood at 5.7 percent. By recent historical standards, this is not a very high level of unemployment. Yet it would be a mistake to conclude that this recession is unusually mild, or that it is effectively over.

The unemployment rate remains nearly 2 percentage points above its lowest point (3.9 percent) during the boom years of the 1990's. Furthermore, the unemployment rate fails to capture individuals who drop out of the labor force. The labor force participation rate (LFPR) in January 2003 stood at 66.3 percent, well below its peak of 67.6 percent (in February 2000). The LFPR has dropped continuously over the past several months, even while the unemployment rate has remained fairly constant. The nation's employment-to-population ratio (E/P) has also been dropping. In January 2003 it stood at 62.5 percent, or 2.4 percentage points below its earlier peak of 64.9 percent (in April 2000). In all, an

additional 4-5 million Americans would be working if labor force activity returned to the levels reached in 1999-2000.<sup>2</sup>

*These employment and labor force losses are also similar to or higher than those experienced at comparable points during the recession of the early 1990's.* For instance, the percentage of the unemployed who have been without work for 6 months or longer has averaged just over 20% in recent months, just as it did during 1992. And the number of long-term unemployed workers exhausting their UI benefits is running well above the level at the same point in the early 1990's recession (Primus *et. al.*, 2003).

With most economists forecasting only 2-3% economic growth during 2003, employment rates are unlikely to grow very substantially this year. Slack labor markets and low employment rates will therefore persist into 2004 and perhaps beyond.

## **2) Structural Joblessness**

During the boom years of the late 1990's, some groups of disadvantaged workers experienced major progress in the labor market. But others continued to suffer long-term declines, especially in ways that are not captured by their unemployment rates.

For instance, employment rates improved markedly for less-educated young women during the 1990's – due to tight markets, welfare reform, and the growth of income supports for working poor families with children.<sup>3</sup> But employment activity continued to decline for some groups of less-educated men. The LFPR's of less-educated young black men aged 16-24 declined from 82 percent in 1979 to 77 percent in 1989 and then to 68 percent in the years 1999/2000. Comparable numbers for those aged 25-34 fell

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<sup>2</sup> The labor force participation rate is generally defined as the fraction of the population that is working or looking for work. The E/P is the percentage of the population employed. Unlike the unemployment rate, which omits those who are out of the labor force, the E/P captures the effects of labor force withdrawals.

from 91 percent in 1979 to 87 percent in 1989 and 84 percent in 1999/2000. The E/P's for these groups showed similar declines.<sup>4</sup>

Furthermore, these rates are based only on those counted in the civilian noninstitutional labor force, which excludes those who are incarcerated. If the latter were included, the declines in labor force activity observed for young black men would be far more dramatic. And labor force activity among young and less-educated white and Hispanic men, while stable during the 1990's, remains below the levels observed during the 1970's.

The low employment rates (and also low wages) of less-educated young men reflect a variety of problems: disappearing blue-collar jobs, poor education and cognitive skills, limited early work experience, discrimination, and limited access to areas of job growth. In addition, as very large numbers of young men (over 600,000) now are released from prison each year, many face significant barriers to becoming employed. Stiff enforcement of child support orders out of wages that are low to begin with further reduce the incentive of many young men to seek legitimate work.

The problems of long-term joblessness and labor force inactivity among less-educated young men prevent them from becoming stable and contributing members of their families and communities. The children in these families suffer when their fathers are permanently detached from the world of work. Families are unlikely to escape poverty or gain self-sufficiency from the earnings of mothers alone.

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<sup>3</sup> Even among current and former welfare recipients, those with strong skill deficiencies or other personal problems experienced low employment, while others worked more but with little wage advancement. See Blank and Haskins (2002).

<sup>4</sup> See Holzer and Offner (2002). These calculations are based on young men who are not enrolled in school and who are high school graduates or dropouts.

The nation's employers and overall economy will increasingly lose out as well if large segments of the young male population remain detached from the labor market. For as the "baby boomers" begin retiring in a few years, labor markets will grow increasingly tight, and employers will have more and more difficulty finding qualified workers to fill their jobs. This may ultimately constrain our rates of economic growth. And the nation will continue to spend hundreds of billions of dollars annually on incarceration as long as low-income men cannot or will not find gainful employment.

### **Are PRA's the Solution to Our Cyclical Problems?**

President Bush' proposal for PRA's would provide up to \$3.6B during the current and next fiscal years to provide job training and work supports to unemployed workers at risk of exhausting their Unemployment Insurance benefits. In addition, workers would have greater incentives to accept employment, as they would be eligible to keep some or all of the unused funds in their \$3000 accounts upon taking jobs.

This proposal has some appealing aspects. Significant additional funds for training and work supports are welcome, assuming that they are spent in cost-effective ways. Improving incentives for reemployment within the Unemployment Insurance system also makes some sense - at least when jobs are readily available and are being foregone by workers with weak incentives to become employed.

But a number of concerns can be raised about the proposed PRA's. The start-up times needed and administrative costs imposed on the states by this new program may be significant. Large numbers of the currently unemployed will not be eligible for these funds or services. In particular, workers who have already exhausted their unemployment

benefits more than 6 months before the beginning of this new program will derive no benefit from it.

There is strong reason to believe that money spent on reemployment bonuses in the current economy will have very little effect on overall employment outcomes. Reemployment bonus experiments within the Unemployment Insurance system were conducted in the 1980's and early 1990's in the states of Illinois, Pennsylvania and Washington. Outside of Illinois, the reductions in unemployment attributed to the bonuses were very modest – in fact, too modest to generate enough savings in Unemployment Insurance payments to offset the administrative costs of the programs. While “profiling” unemployed workers and targeting the bonuses on those at risk of long-term unemployment may improve their efficiency somewhat, their effects will likely remain quite small (O’Leary *et. al.*, 1998).

Under current proposals, PRA bonuses could be much larger and more expensive than those used in the earlier experiment. But, given the current weakness of the labor market, it is even less likely that bonuses will significantly reduce unemployment. For them to be effective, large numbers of jobs must be available and not quickly accepted by any workers. During an economic downturn, this is simply not the case. Even if bonuses induce some individual workers to accept jobs more quickly than they otherwise would, they would likely be displacing some other workers who would have accepted those same jobs - leading to no net gain in the nation’s level of employment.

Thus, a proposal that might generate some modest improvements if done in a stronger economy will have little effect if done, as proposed, only during a period of economic downturn. The proposal becomes more sensible if the bonuses are limited in

magnitude (to roughly \$1000 or so), and implemented on a permanent basis. The remainder of the funds could then be targeted towards training or work supports, and perhaps administered through the current WIA system rather than an alternative administrative structure.

### **PRA's: No Substitute for Extending Unemployment Insurance Benefits**

Perhaps the greatest concern over PRA's is that they seem to be viewed by Administration proponents as substitutes for temporary extensions of federal Unemployment Insurance.

During recessions, workers often exhaust the 26 weeks of benefits that they are entitled to in most states, even while remaining unemployed. In these circumstances, the federal government frequently provides emergency benefits for limited periods of time. In previous recessions – including that of 1990-92 – federal benefits were extended several times, to ensure that unemployed workers had access to funds while jobs remained in short supply.

But the current program (called Temporary Extended Unemployment Compensation, or TEUC), has been extended only through May 2003, and provides no benefits to the one million workers who have already exhausted their 13 weeks of additional benefits and who remain unemployed.<sup>5</sup> Given the likelihood that labor markets will remain weak in throughout 2003 and beyond, many more workers will continue to exhaust their benefits and remain unemployed over the coming months. The disappearance of benefits might improve the incentives of some workers to more quickly

gain employment than otherwise. But, as argued above, this will not generate faster declines in the nation's overall unemployment rate, as long as overall labor market weakness continues and new jobs remain relatively unavailable.

Thus, *any money spent on PRA should not be considered a substitute for temporary extensions of federal Unemployment Insurance benefits*. The costs of providing these extra benefits would not be trivial, but they are indeed miniscule compared to the cost of new tax cuts proposed by the Bush Administration.<sup>6</sup>

Furthermore, there are probably a relatively large number of jobless workers who have not been eligible for UI benefits at all. For instance, part-time workers and low earners often do not qualify for these benefits. Among the more than 2 million women who left the welfare rolls and entered the workforce in the 1990's, it is likely that 100-200,000 now have no jobs, no welfare benefits, and no UI benefits. Some temporary provision of Unemployment Insurance benefits to these workers, in lieu of more permanent reforms in the UI system, might be useful as well.<sup>7</sup>

### **Structural Unemployment: Should Federal Job Training Funding Be Cut?**

Despite the evidence of growing long-term joblessness among less-educated youth and young adult men, the Bush Administration has proposed significant cuts in federally-funded job training programs for disadvantaged adults and youth.

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<sup>5</sup> In addition, a joint federal-state program that provides extended benefits can be accessed only in a limited number of high-unemployment states. Some additional weeks of federal benefits are also available in a few high-unemployment states.

<sup>6</sup> The additional cost of providing extensions of UI today comparable to those provided in the previous recession would be about \$20-30B. This amount is miniscule compared to the total cost of proposed tax reductions by the Bush Administration, which recently have been estimated at \$1.5T.

<sup>7</sup> For instance, in the recession of 1974-75 the federal government established a temporary UI program for workers who were otherwise ineligible for benefits. See Vroman (1998) and Holzer (2000).

The most troubling of these cuts is the proposed phasing out of the Youth Opportunities program. This important and innovative effort targeted a number of high-unemployment neighborhoods around the country for intensive efforts to improve the skills and employability of young people living there, at a cost of \$225M per year for five years. The program was carefully planned and developed over a period of several years. But this investment is now at risk of being completely squandered. *The Bush Administration has decided to end this effort, even before the program could be fully implemented and without obtaining any meaningful evaluation results regarding its cost-effectiveness.*

The very modest increases in funding for the Job Corps do not offset the larger cuts made in Youth Opportunities and other programs funded by Title I of WIA. Indeed, proposed cuts in total funding for employment and training programs amount to nearly 10% of the total - even without adjusting for inflation or population growth (Primus and Goldberg, 2003). Even the training programs for disadvantaged adults, that have strong and proven track records of cost-effectiveness, are also being cut. And the amount of actual training provided in these programs under WIA has already been dramatically reduced from the earlier JTPA years, even before the new round of cuts becomes implemented.<sup>8</sup>

Thus, funding for training in these programs should at least be maintained, if not increased, while we continue to evaluate their effectiveness and seek ways to improve them over time. In addition, we need to develop some new strategies for addressing the

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<sup>8</sup> See Heckman *et. al.* (2000) for a review of the very strong evidence on effectiveness of training for disadvantaged adults, particularly under JTPA. The calculations of reductions in training provided to adults under WIA have been prepared by the Center on Law and Social Policy, using WIA data (Savner *et. al.*,

long-term problems of less-skilled workers whose labor force activity keeps declining. These strategies need to address not only the limited skills and work experience of this population, but also the specific barriers to employment faced by low-income men with criminal records as well as stiff child support orders and arrearages. Innovative approaches that help link at-risk high school students with employers and the labor market, in order to prevent their early detachment from school and work while helping employers build their future workforces, also need to be developed. A set of new competitive grant programs in these areas thus deserve strong consideration.

## **Conclusion**

The nation continues to suffer from two distinct problems of worker joblessness: one related to the short-term business cycle, and the other related to longer-term structural problems that face particular groups of disadvantaged workers.

Personal Reemployment Accounts are unlikely to help generate lower unemployment rates, though if restructured they might contribute somewhat to worker skill development. There remains a strong need for additional federal extensions of Unemployment Insurance to workers who exhaust their benefits. Training programs for the disadvantaged such as Youth Opportunities need to be preserved, and other alternatives developed.

These costs of extending UI and preserving or modestly expanding our training programs would be fairly small, relative to the massive tax cuts that the Bush Administration has proposed. In terms of enhancing economic growth, maintaining fiscal

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2003). Their analysis indicates that training for disadvantaged adults and dislocated workers has fallen by over 70% since 1998.

balance and insuring minimal levels of equity across social groups, the case for these expenditures is far stronger than for the tax cuts that are under discussion.

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