14 Categories of Unemployment

15 The Costs of Inflation

16 Measuring Inflation
The Natural Rate of Unemployment

- Workers who spend time looking for employment are engaged in job search.

- Frictional unemployment is unemployment due to the time workers spend in job search.

- The natural rate of unemployment is often estimated around 5-6%.
The Nature of Unemployment

Labor Market Flows in an Average Month in 2007

- Employed: 4.118 million
- Unemployed: 1.781 million, 1.929 million
- Not in labor force: 1.601 million, 1.798 million, 3.920 million
The Nature of Unemployment

Distribution of the Unemployed by Duration of Unemployment, 2007

- Less than 5 weeks: 36%
- 5 to 14 weeks: 31%
- 15 to 26 weeks: 15%
- 27 weeks and over: 18%
The Nature of Unemployment

- **Structural unemployment** occurs when there are more people seeking jobs in a labor market than there are jobs available at the current wage.
**Structural Unemployment**

The Effect of a Minimum Wage on the Labor Market

- **Wage Rate**
  - $W_F$
  - $W_E$

- **Quantity of Labor**
  - $Q_D$
  - $Q_E$
  - $Q_S$

- **Labor demand**

**Minimum wage**

**Structural unemployment**
Causes of Structural Unemployment

- **Minimum wages**: a government-mandated floor on the price of labor. In the U.S., the national minimum wage is $7.25 an hour.

- **Unions**: by bargaining for all a firm’s workers collectively (collective bargaining), unions can often win higher wages from employers than the market would have otherwise provided when workers bargained individually.
Causes of Structural Unemployment (cont.)

- **Efficiency wages**: wages that employers set above the equilibrium wage rate as an incentive for better performance.

- **Side effects of government policies**: public policies designed to help workers who lose their jobs; these policies can lead to structural unemployment as an unintended side effect.

- **Mismatches between employees and employers**: caused by the time it takes for workers and firms to adjust to shifts in the economy; includes skills mismatch and geographic mismatch.
The Natural Rate of Unemployment

- The **natural rate of unemployment** is the normal unemployment rate around which the actual unemployment rate fluctuates.

- The natural rate of unemployment is the unemployment rate that arises from the effects of frictional plus structural unemployment.

- **Cyclical unemployment** is a deviation in the actual rate of unemployment from the natural rate.
Types of Unemployment

• Natural unemployment = Frictional unemployment + Structural unemployment

• Actual unemployment = Natural unemployment + Cyclical unemployment
Changes in the Natural Rate of Unemployment

- Estimates of the natural rate of unemployment show that the U.S. natural rate rises and falls over time.

- Factors that affect the natural rate of unemployment:
  - Changes in labor force characteristics
  - Changes in labor market institutions
  - Changes in government policy
Changes in the Natural Rate of Unemployment

The Changing Makeup of the U.S. Labor Force, 1948-2013

Percent of labor force

Women

Under 25

Year

1948
1960
1970
1980
1990
2000
2013
Economics in Action

Natural Unemployment Around the OECD

Average unemployment rate

<table>
<thead>
<tr>
<th>Country</th>
<th>Rate</th>
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<tbody>
<tr>
<td>Korea</td>
<td>3.59</td>
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<tr>
<td>Mexico</td>
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<tr>
<td>Slovak Republic</td>
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</table>

16%