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Unemployment Insurance and Job Search in the Great Recession

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The last several years have seen the worst labor market in the United States in several generations. As of April 2011, the unemployment rate has not fallen much below 9 percent – and has more often been closer to 10 percent – for well over two years, and 43% of the unemployed have been out of work for six months or longer. Affected workers are experiencing substantially reduced consumption and spending what assets they have; it seems likely as well that long spells of unemployment will be permanently scarring, leading to reduced earning capacity in the future.

An important part of the policy response to the so-called "Great Recession" has been a series of dramatic expansions of Unemployment Insurance (UI) benefits. Preexisting law provided for up to 26 weeks of benefits, with a provision that allowed for up to 20 additional weeks of "Extended Benefits" (EB) in states experiencing high unemployment rates. On top of this, the Emergency Unemployment Compensation (EUC) program was introduced in June 2008, providing an additional 13 weeks of benefits. Subsequent legislation, most notably the American Recovery and Reinvestment Act enacted in February 2009, has repeatedly extended EUC benefits to as many as 53 weeks and delayed the expiration of the EUC program[1]. Combining the regular UI, EB, and EUC programs, unemployed workers have been able to draw as many as 99 weeks of unemployment benefits.

In this project, I will investigate the effect of these UI extensions on job search and reemployment. Exit rates from unemployment have fallen to unusually low levels during the Great Recession, and many commentators have attributed this decline in part to the disincentive to work created by UI benefits. An obvious alternative hypothesis is that the decline in unemployment exit rates reflects a shortage of labor demand. To distinguish these hypotheses, I will use the longitudinal structure of the Current Population Survey to construct hazard rates for unemployment exit that vary across states, over time, and between individuals with differing unemployment durations. I will use these hazard rates to explore a variety of comparisons intended to identify any effects of UI extensions on the probability of reemployment and on other measures of job search behavior.

Preliminary analysis points to two main conclusions. First, while reemployment rates of the unemployed fell dramatically as the labor market weakened with the onset of the recession, much of this fall was unrelated to unemployment insurance and likely reflected weak labor demand. Second, unemployment insurance extensions had small negative

[1] The ARRA also encouraged states to offer EB by eliminating the required state contribution and made weekly benefits more generous.

effects on both the probability that eligible unemployed workers would find a job and the probability that these workers would abandon their searches.

Combining these two results, the analysis indicates that the extension of UI benefits increased the measured unemployment rate over what it would otherwise have been, but only by 0.5 percentage points or less.

Future work on the project will take several directions. First, the above analyses will be refined and their sensitivity investigated to a variety of alternative empirical specifications. Second, I will use simulations to decompose the roles of reduced job-finding rates and reduced labor force exit rates in raising measured unemployment and delaying reemployment. Third, I will probe deeper into the details of job search efforts, investigating whether unemployment insurance extensions led to changes in the intensivity of job search.

The project has clear policy implications. Congress has repeatedly extended unemployment durations in recent recessions, consistent with a view that the efficiency cost of unemployment insurance is lower, and the optimal generosity therefore higher, in times of high unemployment. But there is little evidence about the effects of these extensions, and thus little guidance about the optimal cyclical behavior of UI benefit generosity. This paper will shed light on this question.

The project also has a clear relationship to the mission of the Center for Equitable Growth. Unemployment spells, particularly in times of weak labor demand and low job finding probabilities, can be a source of immense inequality, as individuals must cannibalize what assets they have to survive during prolonged periods of joblessness. In this view, unemployment insurance provides an extremely important social insurance function.