Which labor market data should you believe?

By Binyamin Appelbaum
June 13, 2016 – *The New York Times*

When the unemployment rate falls below 5 percent, it usually means things are going pretty well. It was 4.7 percent in May, a level last seen in November 2007.

A different measure of the economy's health, however, is beeping and flashing red. It says that labor market conditions have deteriorated with each passing month this year. In May, it fell to its lowest level in seven years.

Called the Labor Market Conditions Index, it has been billed as a more complete measurement than that old war horse, the unemployment rate. There are two possible explanations for the index's decline: one somewhat comforting, and the other scary.

Let's do comfort first. It's possible we're not making progress because we've more or less arrived at our destination — what economists call full employment. This somewhat misleading term doesn't mean that everyone has a job. It means that the reservoir of people seeking work has receded to a historically normal level.

There is some evidence for this. Notably, the low unemployment rate.

But there are also some pretty strong reasons for skepticism. My personal favorite: In 2007, about 88 percent of men between the ages of 25 and 54 were working. Now, roughly 85 percent of such men are working.

That's a difference of about two million men, most of whom probably would like jobs.

The scary explanation? Job growth is slowing because the economy is losing steam.

Fed officials, and other economists, have been grappling with the divergence between relatively weak reported economic growth and relatively strong job growth. Those at the Fed have largely taken the view that labor market data is more accurate, which has been true over time.

But this time, some economists say, the broader economic data may be closer to the truth. "Of course, the bond market understands this perfectly clearly," Michael Darda, chief economist at MKM Partners, noted recently. Investors have continued to discount the Fed's hints that it plans to raise rates this summer, and again later this year. They are betting the Fed will once again be forced to wait longer than it wishes.

(It has not escaped the notice of these pessimists that the Fed's labor market index started showing weakness after the Fed increased rates in December.)

The truth may be somewhere in between.

The Federal Reserve introduced the new measure of labor market health a few months after Janet Yellen became the Fed's chairwoman in 2014. It created the index because the unemployment rate is too simple. Even the name is too simple. It doesn't actually measure unemployment; it counts only people who are actively looking for work. Moreover, a low unemployment rate doesn't tell you how many part-time workers would like full-time gigs. It doesn't tell you how many full-time workers would like a better job at higher pay.

In short, particularly in the aftermath of the Great Recession, the unemployment rate has improved much more quickly than the actual labor market.

The Fed's corrective, however, is also imperfect. The central bank mashed together 19 kinds of labor data, including high-profile stalwarts like the unemployment rate and less familiar esoterica like the Conference Board's

"help-wanted advertising index." And it tried to clean that data, scrubbing away the noise to reveal the underlying trends. But there is no perfect method for telling the difference, and a recent Goldman Sachs analysis suggests the Fed scrubbed too hard.

Daan Struyven and Zach Pandl, economists at Goldman, concluded that the Fed is scrubbing away some of the economy's actual progress. But they caution that is only a partial explanation: Economic growth still appears to be slowing.

"This is not to say that the labor market is still firing on all cylinders," they wrote. "The labor market is still making progress, but at a meaningfully slower pace."

So there you have it.

The economy isn't great. The economy isn't terrible. We're just chugging along, and apparently that's about as good as it gets.