Responding to Long-Term Unemployment

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Responding to Long-Term Unemployment

Even though the US economy has added more than 2.5 million jobs since the start of 2012, nearly 4.8 million people had been unemployed for more than six months as of February 2013. Those 4.8 million people represent about 3 percent of the labor force and 40 percent of all the unemployed. Another 900,000 workers had become discouraged and had stopped looking for work altogether. Long-term unemployment has become a chronic problem for the US economy and creates significant hardships for the workers themselves, their families, and their communities.

Reducing long-term unemployment and helping affected individuals, families, and communities deal with its fallout are important topics for policymakers at the federal, state, and local levels. A strong, growing, and vibrant economy would help address long-term unemployment, but as of yet, policies to stimulate sustained growth have proven elusive. Even in the absence of extremely fast economic growth, there are policies that can help the long-term unemployed find jobs, keep at-risk workers and recent job losers from becoming long-term unemployed, and assist families dealing with consequences of long-term unemployment. Those policies include improved job training and workforce development programs, changes to the unemployment insurance (UI) system to encourage employers to reduce workers’ hours through a program known as short-time compensation rather than lay off or discharge those workers, and changes to the eligibility rules for unemployment compensation to make it easier for low-income workers to qualify for benefits in the event of a job loss. This paper examines those policy options and others to identify promising approaches for addressing long-term unemployment.

Strengthening the Economy

Strong economic growth would be the most effective remedy for reducing today’s elevated levels of long-term unemployment. The severity of the economic contraction during the Great Recession and the relatively weak economic recovery are the primary factors accounting for persistently high levels of long-term unemployment. If the economy, as measured by gross domestic product, were to grow at an annual rate of 3 to 4 percent rather than 2 percent, the unemployment rate would quickly drop below 7 percent. That improvement in the labor market would likely keep some workers from

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1 For a critical review of research on this topic, see Acs (2013).
becoming long-term unemployed and allow some of those who have already been out of work for more than six months to find jobs. Note, however, that high demand for workers does not guarantee that the long-term unemployed will secure any of those new jobs, because employers may fill them with new entrants to the labor market and the more recently unemployed.

There is considerable debate about how to spur growth in the short term and the impact of short-term measures on long-term growth. Policies to spur growth fall into three broad categories: (1) direct government spending on goods and services, (2) increasing households’ disposable income, and (3) reducing the costs of doing business. Direct government spending on infrastructure projects or aid to states could generate modest employment gains in the short term. Estimates suggest that every billion dollars of federal spending on infrastructure or aid to states could create the equivalent of 4,000 to 6,000 full-time jobs. Policies that increase households’ disposable income have a wide range of potential effects on employment. Generally, policies that increase the incomes of households that are most likely to spend that money (e.g., those that recently suffered a loss in income like the unemployed as well as lower-income households, rather than high-income households) tend to be the most effective ways to encourage job growth. For example, an additional $1 billion spent on increasing aid to the unemployed would be expected to add the equivalent of 11,000 to 12,000 full-time jobs, whereas an additional $1 billion in refundable tax credits to low- and middle-income families could add about 8,000 full-time-equivalent jobs. Certain policies that support businesses could also effectively spur employment growth. For example, reducing firms’ payroll taxes, especially if those reductions are targeted at firms that increase their payroll, could generate an estimated 8,000 to 10,000 full-time-equivalent jobs for every billion dollars spent. Other “business-friendly” policies, such as reducing taxes on business income or reducing regulatory burden, tend not to create many additional jobs. It is difficult to estimate effects precisely; the actual effects could be half or twice as big as expected.

In the current federal fiscal environment, the funds for any of the programs and policies discussed above would have to come from increased borrowing. That borrowing would add to the deficit and the debt, which could crowd out private investment in the short term, raise interest rates in the longer term, and ultimately result in slower growth in the future. On the other hand, if high levels of long-term unemployment erode the skills of the US workforce and reduce the future

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2 The estimates discussed in this paragraph are from Congressional Budget Office (2012b).
productive capacity of the economy, then deficit spending to spur the economy and create jobs may actually offer some protection for the economy’s future growth prospects.

Although stronger economic growth would likely address much of the problem of long-term unemployment, factors well beyond the control of federal policymakers—natural disasters, the behavior of foreign governments, technological innovation, and individual entrepreneurship—will have profound effects on growth. Beyond focusing on growth, there are several actions policymakers can take to help the long-term unemployed find jobs, help other workers and the recently unemployed avoid long-term unemployment, and help the families and communities of the long-term unemployed deal with its consequences.³

**Helping Those Who Are Already Long-Term Unemployed**

Individuals who have been unemployed for more than six months face increasing obstacles in their search for jobs. Their workplace skills may have eroded as they remained jobless. Even if they do have suitable skills, employers may believe that a long spell of unemployment reflects badly on the workers’ potential productivity. Finally, the skills those workers do have may not be readily transferable across industries. Although a mismatch in the skills of the long-term unemployed and the needs of potential employers can account for only a modest portion of high long-term unemployment, skill deficiencies or skill mismatches may grow in importance the longer individuals remain unemployed.⁴

The most direct way to address the skills of the unemployed is through workforce development programs. Historically, training programs have varied in approach and effectiveness. Evaluations of training for adults under the Job Training Partnership Act of 1982 indicate that participants had higher earnings even four years after the training than otherwise similar individuals who did not participate in the programs (Government Accountability Office [GAO] 1996; Mueser, Troske, and Gorislavsky 2007). Generally, the least educated and experienced workers enjoyed the greatest benefits from training. About half the long-term unemployed have high school degrees or less education and about one in five are under the age of 26 (Mitchell 2013). Those subsets of the long-term unemployed are the most likely to benefit from training efforts.

³ Some of those policies and programs have the added benefit of spurring economic growth through higher consumption. In addition, some of the efforts to accelerate growth discussed in the preceding section would stimulate growth by increasing employment.

⁴ For a discussion of the role of skill mismatches in driving up long-term unemployment, see Acs (2013).
Another important consideration in training for the long-term unemployed is that the skills they are learning reflect the needs of employers in their regions. By its very nature, sectoral training approaches need to be grounded at the local level; a one-size-fits-all federal approach may not be effective. Generally, successful sectoral training efforts work with employers to identify the skills they are looking for and develop curricula to impart those skills to workers.\(^5\) Another important component of training is credentialing. That is, workers emerge from training programs with industry-recognized credentials that certify that the workers now have the skills to do particular jobs. Such degrees or certificates are particularly useful for displaced workers, who must change industries or occupations to find new jobs (Jacobson, LaLonde, and Sullivan 2005).

In addition to training programs, large-scale public works programs could help the long-term unemployed return to work. Indeed, during the Great Depression, the Work Projects Administration and the Civilian Conservation Corps hired millions of unemployed workers. Individuals hired into public works jobs could retain their skills and develop new ones, improving their private-sector employment prospects. And unlike formal training programs where one hopes there is a job at the end, public-service employment is a job. Under the American Recovery and Reinvestment Act of 2009, the federal government spent $1.3 billion to create 260,000 temporary jobs for welfare applicants (Pavetti, Schott, and Lower-Basch 2011).

Creating public-service jobs for the long-term unemployed poses several important challenges. First, there can be substantial up-front costs in identifying worthy projects and procuring supervisory staff. Second, workers in public-service jobs could end up crowding out private-sector workers. For example, if the public works project involved installing new playground equipment at local parks, that work could have been done by private contractors or municipal workers rather than as a job targeted at the long-term unemployed. Finally, if unemployed workers knew they could be hired into a public works program if they stayed unemployed long enough, it may reduce their incentive to search hard for jobs in the interim.

Policymakers could also consider creating incentives for employers to hire the long-term unemployed and for the long-term unemployed to accept jobs at lower wages than they previously had earned. For example, the government could offer a payroll tax credit to employers that hire individuals who have been out of work for six months or more. That approach, however, may not

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\(^5\) Maguire (2010) provides a review of successful sectoral training programs.
lead to any additional hiring overall, as employers may offer jobs to the long-term unemployed rather than other job seekers.

Wage subsidies to induce the long-term unemployed to take lower-wage jobs could encourage some of the long-term unemployed to take jobs, but such subsidies may not be particularly effective for several reasons. First, if those subsidies are offered only to the long-term unemployed, they would encourage individuals who would otherwise have taken a job quickly to wait longer and qualify for the subsidy. Second, past research on wage-subsidy programs suggests that some employers view subsidies as a signal that the potential worker is not very productive and, hence, do not extend an offer (Katz 1996).

One segment of the long-term unemployed, those with work-limiting disabilities, is at particularly high risk of never working again. Approximately 300,000 who have been unemployed for more than six months report work-limiting disabilities. Many of these people will end up applying for Social Security Disability Insurance (DI) or Supplemental Security Income (SSI). Applications to the DI program swelled during the recession (Manchester 2013). Under current program rules, which basically require an individual to be unable to work as condition for benefit receipt, DI recipients risk losing all their benefits if they earn even a small amount of money (Autor and Duggan 2010).

The long-term unemployed with work-limiting disabilities all had jobs, so with appropriate accommodations, many should be able to do some work. If they permanently leave the labor force, the economy loses their productive abilities. Further, the DI program itself has come under tremendous financial strain, and the DI trust fund is estimated to be exhausted in 2016. Modifying the DI program to keep as many individuals with work-limiting disabilities in the labor force could be an important step in helping a segment of the long-term unemployed.⁶

Many people with disabilities would like to work if possible (Ali, Schur, and Blanck 2011). For the long-term unemployed who also struggle with some kind of health impairment, a short-term disability program with a clear path back to work could be a better solution than the current DI and SSI programs. Currently only five states administer short-term disability programs (California, Hawaii, New Jersey, New York, and Rhode Island). Those programs provide cash benefits similar to UI benefits for qualified applicants, but for a longer time. A broader temporary disability insurance

⁶ For a discussion of options for reforming the DI program, see Autor and Duggan (2010) and CBO (2012a).
program could help some unemployed individuals with disabilities eventually transition back to work (Lindner and Nichols 2012). However, it is unclear what kind of services would be most useful for these people, and whether they receive some of them from other services, such as vocational rehabilitation (Stapleton and Martin 2012).

Keeping the Problem of Long-Term Unemployment from Growing

A key step in keeping the problem of long-term unemployment from growing is to help vulnerable workers stay in jobs and the recently unemployed find new ones quickly. Potential strategies include expanding the use of short-time compensation (STC), targeting job search assistance at the newly unemployed who may be at elevated risk of long-term unemployment, offering reemployment bonuses to recent job losers who find new work quickly, and providing wage insurance to workers who take new jobs paying considerably less than their previous jobs.

STC programs provide partial UI benefits to workers who have their hours reduced by their employers rather than being laid off. Workers whose hours have been reduced receive a prorated portion of the UI payment they would have received had they lost their jobs. In other words, they retain a portion of their earnings as they are still employed, and UI makes up for part of the earnings loss due to the reduction in hours. Because it forestalls unemployment, STC can reduce the flow of individuals into long-term unemployment. It also mitigates the potential consequences of job loss and long-term unemployment. Although STC is not widely used in the United States, other countries, such as Germany, have STC programs, and those programs helped keep unemployment from rising rapidly during economic downturns (Cahuc and Carcillo 2011; Vroman and Brusentsev 2009).

STC can benefit both workers and their employers, but there are drawbacks. For example, employers may not experience the same cost savings through hours reductions as they would through layoffs if they cannot also reduce nonwage benefits. Further, STC programs work best as an alternative to temporary or seasonal layoffs, but during the Great Recession, temporary layoffs have become less common, while permanent discharges have grown (Katz 2010).

Targeting job search assistance and other services at individuals when they initially file for UI benefits could help the newly unemployed find jobs relatively quickly, thus forestalling long-term unemployment. In recent years, states have increasingly turned to technology (e.g., automated phone
systems and the Internet) to make the process of filing initial and continuing claims for unemployment benefits easier and faster. But those systems reduce the chances that a claimant will receive any reemployment services (O'Leary 2006). Newly unemployed workers who receive job search assistance, individual counseling, and help accessing training tend to have shorter periods of unemployment (Black, Galdo, and Smith 2007; Decker et al. 2000; Meyer 1995). Some assistance programs identify the workers most likely to become long-term unemployed and make participation in job search assistance a mandatory condition for receiving UI benefits.

Reemployment bonuses and wage insurance programs can provide incentives for the newly unemployed to take new jobs quickly rather than risk becoming long-term unemployed. A reemployment bonus is a one-time payment to unemployed workers who find new jobs within a specified amount of time. Wage insurance programs make up part of the difference between a worker’s new wage rate and the wage rate on his or her previous job for a certain amount of time, say two years. The idea behind both those approaches is that there are jobs available for the recently unemployed but that those jobs do not pay enough for the worker to want them after a short period of unemployment. The worker believes that continued job search will result in a better offer. If there are very few available jobs, worker-focused incentives can have little effect. If better jobs are available through prolonged searching, then inducing unemployed workers to take steep pay cuts may harm the workers’ future earnings prospects and leave workers underemployed. When reemployment bonuses and wage insurance have been tried, the results have been mixed at best (Bloom et al. 2001; Meyer 1995).

**Addressing the Consequences of Long-Term Unemployment**

The consequences of long-term unemployment are closely linked to diminished current and future income as well as to the stress caused by losing a job. To the extent that a worker’s health status and children’s school-based outcomes suffer when that worker first becomes unemployed, policies that help workers stay employed, like STC, discussed previously, could be particularly helpful at preventing some of the adverse consequences associated with prolonged unemployment. Income losses, however, mount as the duration of unemployment increases. Not only do the unemployed have less income while they are out of work, their wage prospects diminish the longer they remain without a job (for a review, see Nichols, Lindner, and Mitchell 2013).
Providing a short-term income safety net to the unemployed and their families has many benefits. Specifically, UI and the extension of benefits during periods of extremely high unemployment allow families to carefully cut back on their expenses rather than suddenly reducing their standard of living. UI benefits can mean paying the rent or mortgage rather than having to move and dislocate a family. Some of the unemployed, however, do not qualify for benefits because they do not have an adequate work history. Those workers tend to be among the lowest-income workers, and the income loss associated with job loss may mean acute hardships. Expanding the eligibility criteria for UI benefits could help the most vulnerable of the unemployed cope with material hardships (Shaefer 2010). In addition, for unemployed individuals with very low incomes, other safety net programs like the Supplemental Nutritional Assistance Program (SNAP, formerly known as food stamps) help the unemployed put food on the table and come closer to making ends meet. Such assistance to families improves economic stability and improves the well-being of all family members.

Critics of that support argue that assistance that is too generous or lasts too long will undermine work effort and increase the duration unemployment (Mulligan 2012). The work disincentives in the UI program, however, are not particularly strong, and they may be weaker today than in the past, as is suggested by a comparison of newer estimates (Card, Chetty, and Weber 2007; Schmeider, von Wachter, and Bender 2012) to older estimates surveyed in Woodbury and Rubin (1997), Decker (1997), and Meyer (2002). One reason for a difference between recent and older estimates is a decline in temporary layoffs, which are more responsive to UI incentives (Katz 2010).

In addition to the concurrent loss of income associated with unemployment, the longer a worker remains jobless, the lower his or her reemployment wage is likely to be (Nichols et al. 2013). That wage erosion contributes to diminished family income decades into the future. The workforce development programs that aim to help the long-term unemployed find new jobs also offer the

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7 Gruber (1997) and Browning and Crossley (2001) provide evidence as to how UI reduces consumption declines at onset of unemployment.
8 For example, Gangl (2006) examines panel microdata for the United States and Western Europe and finds that the negative effects of unemployment on earnings are mitigated by more generous unemployment benefit systems, partly from behavioral responses preventing downward mobility as unemployment benefits increase liquidity for unemployed workers.
opportunity to improve those workers’ wages; the greater skills a worker has, the higher that worker’s wages are. The evidence on how much training raises wages is mixed, however.⁹

Finally, aid to states, cities, and neighborhoods with high concentrations of the long-term unemployed could help those communities address some of the challenges faced by the long-term unemployed and their families. For example, widespread, enduring unemployment may erode a community’s tax base and imperil such basic services as schools, sanitation, and public safety. Aid could help maintain those basic services, benefiting the long-term unemployed who live in those communities. Additional aid could also provide for enhanced services, such as mental health counseling and food pantries.

**Conclusion**

Long-term unemployment has touched millions of Americans since the Great Recession began. In early 2013, 4.8 million adults had been looking for work without success for at least six months, and another 900,000 had become so discouraged they had given up searching altogether. The longer these individuals remain out of work, the harder it will be for them to find new jobs, and their potential wages and incomes will continue to erode. Not only are those workers harmed by their prolonged unemployment, but the US economy misses out on their productive abilities.

Long-term unemployment will decline as US economic growth accelerates, but there is no guarantee that rapid growth will come any time soon. Further, our policy tools for stimulating the economy are blunt instruments at best. And in the present fiscal and political climate, it is not clear what, if any, steps the federal government will take to hasten job growth.

Outside of promoting economic growth, the most promising types of policies to reduce long-term unemployment provide new skills to the long-term unemployed while keeping at-risk workers in their jobs. Workforce development programs that are locally based and seek to match employer needs with training programs that certify that participants have attained the skills necessary to meet those needs would help the long-term unemployed obtain new jobs. Policies, such as short-time compensation, that help keep workers on the job, although at reduced hours, can staunch the flow of workers into long-term unemployment. Finally, policies that provide material assistance to the

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⁹ For example, von Wachter, Song, and Manchester (2009) conclude that most interventions have little effect on the future wages of the unemployed, whereas Jacobson and colleagues (2005) estimate that one year of training at a community college can reduce earnings losses by about a third.
families of the long-term unemployed, such as extended UI benefits and SNAP, can help reduce the income-related negative consequences of long-term unemployment. Further, training policies that help get the long-term unemployed back to work can also boost their reemployment wages, mitigating one of the more profound consequences of long-term unemployment. Policies like STC that forestall unemployment can protect the at-risk workers and their families from the adverse consequences associated with loss of a job regardless of the duration of unemployment.
References


