

## Economics Group

### Special Commentary

Sarah House, Senior Economist

[sarah.house@wellsfargo.com](mailto:sarah.house@wellsfargo.com) • (704) 410-3282

Sara Cotsakis, Economic Analyst

[sara.cotsakis@wellsfargo.com](mailto:sara.cotsakis@wellsfargo.com) • (704) 410-1437

# Tracking & Tracing Unemployment During COVID

## Executive Summary

The official unemployment rate, currently 7.9%, is generally a reliable benchmark of the labor market. However, this familiar measure of unemployment does not always fully reflect the state of the jobs market, particularly during periods of severe turmoil such as the COVID pandemic.

In this note, we highlight three ways to track labor market slack that are particularly suited for the COVID environment. The first accounts for the unprecedented decline in the labor force due to the pandemic. Adjusted for the millions of people who have exited the labor force, we estimate the unemployment rate would currently be around 10.5%. We also construct a broader measure of slack that encompasses the specific challenges to work. Our COVID-era measure of underutilization shows, since February, the employment situation has worsened for 5.4 million more workers than implied by the rise in unemployed workers. Last, we track the “permanent” unemployment rate, which strips out workers on temporary layoff and has continued to rise through September. The bleaker picture of the labor market cast by these measures suggests it will be years before the FOMC will be comfortable raising rates, absent inflation getting out of control before then.

*The unemployment rate is likely closer to around 10.5%.*

## Unemployment Adjusted for the Collapse in the Labor Force

The official unemployment rate, also called the U-3 rate, usually offers a good gauge of the labor market and how conditions fare relative to prior periods. However, in periods in which the economy has suffered a shock, such as today with the COVID pandemic, the familiar U-3 measure may not fully reflect the state of the jobs market.

In order for workers to be considered unemployed in the government’s official measure, they must be actively searching for work within the past four weeks. Officially, 7.9% of workers were unemployed in September. Yet that rate misses the millions of workers who have left the labor force since the start of the pandemic due to a dearth of jobs, health concerns and family care needs.

Figure 1

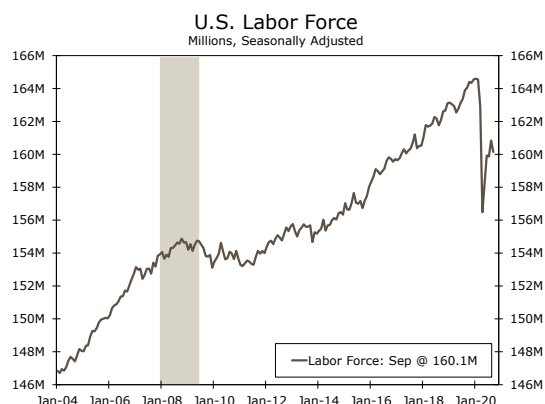
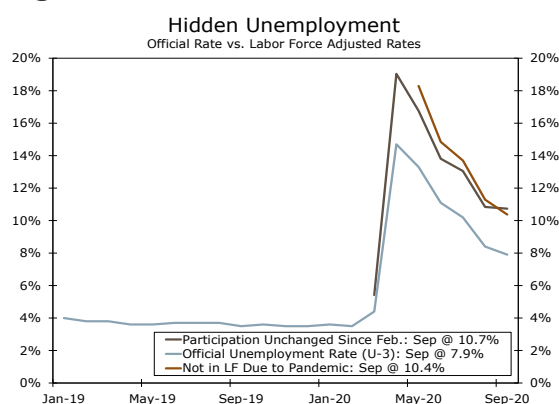


Figure 2



Source: U.S. Department of Labor and Wells Fargo Securities

**Under-employment and non-routine absences from work have also spiked.**

**The number of workers out of the labor force but want a job has swelled by 2.3 million since February.**

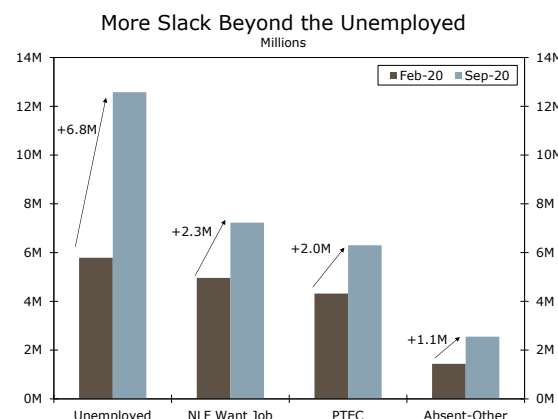
According to the Bureau of Labor Statistics (BLS), 4.5 million workers in September were not in the labor force specifically due to the COVID pandemic. If these workers were categorized as unemployed instead of out of the labor force, the unemployment rate would be 10.4% (Figure 2). Calculated slightly differently, the unemployment rate would be 10.7% if the labor force participation rate was unchanged since February.<sup>1</sup> In other words, there remains a substantial amount of “hidden” unemployment due to the pandemic, equal to about 4.5-5.0 million workers.

### A Broader Measure of Slack for the COVID-Era

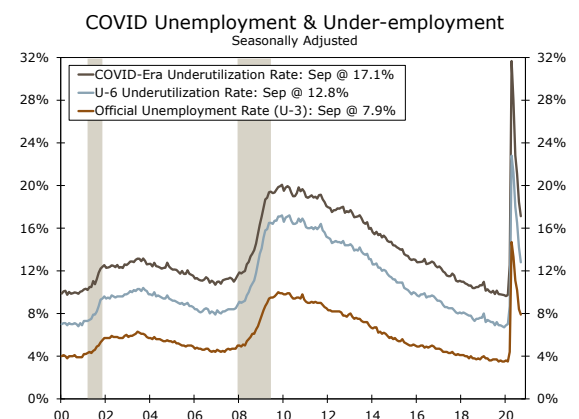
Another way to track slack in the COVID economy would be to account for not only those who have left the labor force due to the pandemic, but also those who are now underemployed or on leave from work for non-routine reasons. Therefore, we have constructed a COVID-era measure of labor market slack that is broader than the BLS’s most generous measure of underutilization (the U-6).

The BLS’s U-6 rate includes a relatively narrow group outside the labor force—marginally attached workers. In order to be considered “marginally attached,” workers must have searched for work (or been employed) within the past year, and both *want* and are *available* to start a job. Parents trying to guide children through remote learning or persons worried about their health may *want* to work, but are not *available* under present circumstances. Others may not have searched for a job in the past year, but want one now, such as recent graduates or members of a household where someone else recently lost employment. Therefore, the total number of workers not in the labor force but who want a job, regardless of recent search status and availability, likely better captures weakness in the labor market induced by the pandemic, in our view. The number of workers out of the labor force but want a job has swelled by 2.3 million since February (Figure 3).

**Figure 3**



**Figure 4**



**Source: U.S. Department of Labor and Wells Fargo Securities**

With many workers’ hours cut back due to weaker demand at their company or an inability to find full-time work, we, like the U-6 rate, also include workers part time for economic reasons in our COVID-era measure of labor market slack. Compared to February, almost 2.0 million more workers were part time for economic reasons in September.

Early in the pandemic, the BLS noted a large increase in the number of workers classified as “employed” but absent from work, presumably due to the pandemic. These workers should have been reported as “unemployed” and on temporary layoff. While the misclassification error has declined in recent months, there are over 1 million more workers absent from work for reasons besides illness, vacation, weather or a labor dispute relative to February. Therefore, we also include this group in our measure of labor underutilization.

<sup>1</sup> We calculated this “hidden” unemployment rate by holding labor force participation constant since February to create a counterfactual labor force level. The difference in the actual and counterfactual labor force level is assumed to be additional unemployed workers, which we calculate as a percentage of our larger, counterfactual labor force.

In total, our measure of labor slack for the COVID-era indicates 12.2 million workers' employment situation has deteriorated since February compared to the 6.8 million rise in official unemployment. While still staggeringly high, this measure has declined in recent months, signaling that jobs market conditions are at least starting to improve. And, like the official U-3 unemployment rate or U-6 rate, is now below the peak registered in the Great Recession.

## “Permanent” Unemployment Rate

In addition to the massive drop on labor force participation, another distinguishing feature of the COVID labor market has been the high proportion of temporary job losses (Figure 5). Temporary job losses should be considered more benign than permanent job losses, as workers stay linked to employers and jobless spells are likely to be shorter. But with no immediate end to the pandemic in sight, job losses have increasingly become permanent. In April, nearly 90% of job losers were on temporary layoff, but that share has shrunk to just about half as of September.

Stripping out workers temporarily laid off from the ranks of the unemployed better illustrates the intrinsic damage caused by the pandemic. The “permanent” unemployment rate suggests that the underlying jobless picture currently is not as severe as during the Great Recession.<sup>2</sup> However, the situation is deteriorating. The “permanent” unemployment rate has continued to rise since the spring, signaling that a full recovery in the labor market will not be quick as more lasting damage mounts.

*Permanent unemployment continues to rise.*

Figure 5

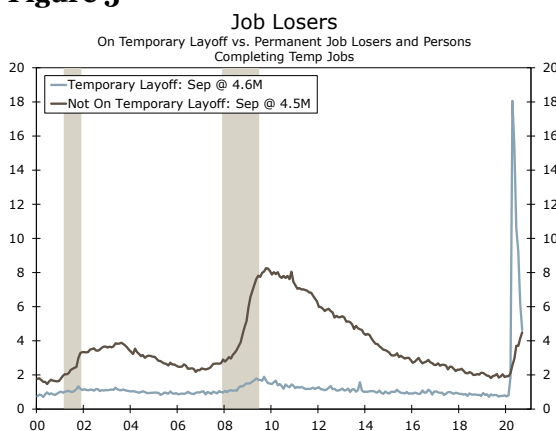
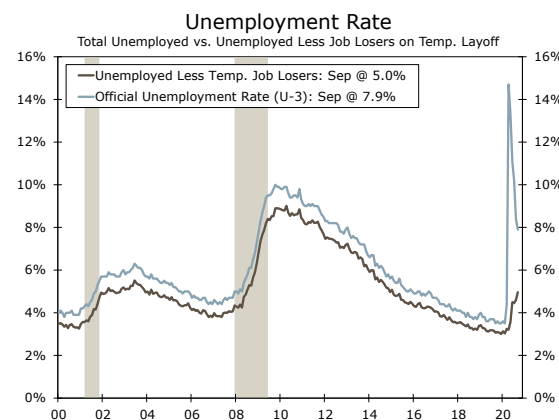


Figure 6



Source: U.S. Department of Labor and Wells Fargo Securities

## Conclusion: Improving in a Sense, but Underlying Damage Mounting

The sharp drop in labor force participation, reduction in hours and use of temporary layoffs all call for new ways of tracking the labor market's health in the current environment. The economic shock caused by the COVID pandemic has worsened the employment situation for millions more workers than implied by the official unemployment rate. While directionally the labor market is improving even accounting for changes in the labor force and other COVID-specific sources of slack, the labor market is still reeling. More positively, the widespread use of temporary layoffs offers some indication that unemployment is not as severe as the official figure would suggest, but the “permanent” unemployment rate is heading in the wrong direction. In other words, the real damage to the labor market from the COVID shock has not even begun to be repaired.

*The real damage to the labor market from COVID has not even begun to be repaired.*

The FOMC has emphasized shortfalls, rather than deviations, from its maximum employment mandate under its updated policy framework. With each of the measures highlighted in this report showing a more troubled state of the labor market than the official unemployment rate, it will likely

<sup>2</sup> Our measure of the “permanent” unemployment rate includes, in addition to permanent job losers, persons who completed temporary jobs, job leavers, reentrants to the labor force and new entrants in the labor force—in other words, all unemployed workers not tied to an employer through a temporary layoff.

be years until the FOMC feels comfortable to raise rates, assuming that inflation does not get out of control before then. In the coming months, we will continue to track these measures in an effort to better illustrate how the labor market is faring in this unique environment.

## Wells Fargo Securities Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	International Economist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Azhar Iqbal	Econometrician	(212) 214-2029	azhar.iqbal@wellsfargo.com
Sarah House	Senior Economist	(704) 410-3282	sarah.house@wellsfargo.com
Charlie Dougherty	Economist	(704) 410-6542	charles.dougherty@wellsfargo.com
Michael Pugliese	Economist	(212) 214-5058	michael.d.pugliese@wellsfargo.com
Brendan McKenna	International Economist	(212) 214-5637	brendan.mckenna@wellsfargo.com
Shannon Seery	Economist	(704) 410-1681	shannon.seery@wellsfargo.com
Jen Licis	Economic Analyst	(704) 410-1309	jennifer.licis@wellsfargo.com
Hop Mathews	Economic Analyst	(704) 383-5312	hop.mathews@wellsfargo.com
Nicole Cervi	Economic Analyst	(704) 410-3059	nicole.cervi@wellsfargo.com
Sara Cotsakis	Economic Analyst	(704) 410-1437	sara.cotsakis@wellsfargo.com
Coren Burton	Administrative Assistant	(704) 410-6010	coren.burton@wellsfargo.com

Wells Fargo Securities Economics Group publications are produced by Wells Fargo Securities, LLC, a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. Wells Fargo Securities, LLC, distributes these publications directly and through subsidiaries including, but not limited to, Wells Fargo & Company, Wells Fargo Bank N.A., Wells Fargo Clearing Services, LLC, Wells Fargo Securities International Limited, Wells Fargo Securities Canada, Ltd., Wells Fargo Securities Asia Limited and Wells Fargo Securities (Japan) Co. Limited. Wells Fargo Securities, LLC is registered with the Commodities Futures Trading Commission as a futures commission merchant and is a member in good standing of the National Futures Association. Wells Fargo Bank, N.A. is registered with the Commodities Futures Trading Commission as a swap dealer and is a member in good standing of the National Futures Association. Wells Fargo Securities, LLC and Wells Fargo Bank, N.A. are generally engaged in the trading of futures and derivative products, any of which may be discussed within this publication. Wells Fargo Securities, LLC does not compensate its research analysts based on specific investment banking transactions. Wells Fargo Securities, LLC's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm which includes, but is not limited to investment banking revenue. The information and opinions herein are for general information use only. Wells Fargo Securities, LLC does not guarantee their accuracy or completeness, nor does Wells Fargo Securities, LLC assume any liability for any loss that may result from the reliance by any person upon any such information or opinions. Such information and opinions are subject to change without notice, are for general information only and are not intended as an offer or solicitation with respect to the purchase or sales of any security or as personalized investment advice. Wells Fargo Securities, LLC is a separate legal entity and distinct from affiliated banks and is a wholly owned subsidiary of Wells Fargo & Company © 2020 Wells Fargo Securities, LLC.

### Important Information for Non-U.S. Recipients

For recipients in the EEA, this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). WFSIL is a U.K. incorporated investment firm authorized and regulated by the Financial Conduct Authority. For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 ("the Act"), the content of this report has been approved by WFSIL, an authorized person under the Act. WFSIL does not deal with retail clients as defined in the Directive 2014/65/EU ("MiFID2"). The FCA rules made under the Financial Services and Markets Act 2000 for the protection of retail clients will therefore not apply, nor will the Financial Services Compensation Scheme be available. This report is not intended for, and should not be relied upon by, retail clients.

SECURITIES: NOT FDIC-INSURED/NOT BANK-GUARANTEED/MAY LOSE VALUE