Intelligence MEMOS

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To: Canada's employment ministers

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Re: **Understanding Canada's "Record" Unemployment Rate**

Statistics Canada's latest monthly Labour Force Survey showed a net gain of 27,700 new jobs in May, with that increase made up entirely of full-time jobs. With this gain, the unemployment rate fell to an all-time low of 5.4 percent. Unfortunately, the current headline masks disquieting issues with underemployment and wage growth.

We have previously written on the dangers of studying **the unemployment rate on its own** and the need for **a better way** of assessing the health of the labour market. The unemployment rate comprises both a numerator and a denominator. The numerator tells us how many people without a job are looking for work while the denominator tells us the sum total of employed and unemployed people belonging to the labour force. Missing from this are discouraged workers without a job that have given up looking for work, and those with part-time positions who want full-time work. While the share of these involuntary part-time employees is lower than before the recession, there remains more than 700,000 part-timers who would prefer full-time employment. And, if we factor in these folks, as well as discouraged workers, the unemployment rate would not look as rosy as the headline suggests.

To improve our assessment of the state of the labour market, the Bank of Canada produces a comprehensive measure called **the labour market indicator** (LMI), which incorporates unemployment-rate data with other crucial information, including wage growth, average hours worked, labour-force participation rates, flows into and out of unemployment, long-term unemployment, and underutilization of labour. It uses a statistical technique to turn all this data into a single index number that we can compare to the unemployment rate, at a quarterly frequency.

While the general direction of both the unemployment rate and LMI are often the same, the extremes during economic booms and recessions are greater in the case of the unemployment rate.

For example, in 2008Q3, the quarter prior to the beginning of the recession, these two measures were almost identical: 6 percent for the LMI, and 6.1 percent for the unemployment rate. The recession itself produced different peaks: 8.1 percent for the LMI, and a worse 8.7 percent for the unemployment rate.

More recently, in 2015 Q3, the two measures were again almost identical: 7 for the LMI and 7.1 percent for the unemployment rate. Since then, the LMI fell to 6.1 percent in 2018 Q4, while the unemployment rate fell to 5.6 percent – a decline of 1.5 times the LMI – and a record 5.4 percent in May 2019. The story is good for the LMI; it is exceptional for the unemployment rate.

Contributing to the discrepancies between these two measures is **sluggish wage growth** – puzzling given low unemployment, and a rise in job vacancies. According to Statistics Canada, more than 500,000 vacant jobs were available in the first quarter of 2019 – up by 9.6 percent from a year earlier.

This matters for how governments think about labour market policy. Given the importance in the Bank of Canada's measure to things such as wage growth, hours worked and full-time work, it's not just the quantity of jobs that matter but the types of jobs. This suggests that, to improve labour market conditions, policymakers should look beyond boosting the number of jobs with a focus on maximizing the quality of jobs available to Canadians. Moreover, businesses and policymakers alike need to continue to improve skills training as globalization, technology, and population aging disrupt the types of available jobs.

As always seems to be the case in economics, the devil is in the details. This remains true of interpreting the labour market and generating appropriate policy responses.

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