Do initial claims overstate layoffs?

As one of the components of The Conference Board Leading Economic Index®, initial claims for unemployment insurance (UI) are widely accepted as an accurate reflection of the health of the labor market: initial claims are high because of business layoffs in a weak economy, and initial claims decline when the economy improves. In "Do Initial Claims Overstate Layoffs?" (*FRBSF Economic Letter,* Federal Reserve Bank of San Francisco, February 7, 2011, **http://www.frbsf.org/publications/economics/letter/2011/el2011-04.html**), researchers Bart Hobijn and Ayşegül Şahin assert that there are other reasons why initial claims increase.

The authors note that initial claims rise not only when layoffs are high, but also when the eligibility for unemployment insurance coverage expands. When eligibility is expanded during recessions, increasing numbers of workers apply for benefits both because they've become eligible and because they believe they cannot find a job in the short run.

To understand how each of these factors affects initial claims, the authors looked at data from both the Job Openings and Labor Turnover Survey (JOLTS) of the Bureau of Labor Statistics and initial UI claims. They determined initial claims data have an upward bias, particularly at the late stage of a recession, because the proportion of UI-eligible people who claim UI benefits—what the authors term the "take-up rate"—rises during periods of recession or weak growth. That is, initial claims tend to remain high as long as UI benefits are extended, even if layoffs return to pre-recession levels.

The authors contend, however, that the take-up rate also can serve as an indicator of labor market health. Therefore, even though their alternative count of initial claims corrected for the take-up rate was well below the official claims level for 2010, they found little evidence that the labor market was stronger than the initial claims indicated.

Moreover, when interpreting declining initial UI claims, one should not necessarily assume that layoffs have subsided; the cause could be a decline in the take-up rate. The rate is expected to decline as UI benefit extensions end and as jobseekers begin to find employment more quickly.

The tax man cometh—to the G-7 countries

In an attempt to put America's financial "house" in order following the fiscal difficulties of recent years, many in Congress are seeking to put the brakes on our increasing national debt and to balance the national budget. And just as when dealing with a household budget, the policymakers have two main choices: cut back on expenses or increase income. On the income side, the primary method that governments use to acquire revenue is the collection of taxes.

In a comparison of the largest industrialized nations, just how do U.S. tax rates measure up? In his article, "How the U.S. Tax System Stacks Up Against Other G-7 Economies" (*Economic Letter,* Federal Reserve Bank of Dallas, November 2011, **https://www.dallasfed.org/research/eclett/2011/el1112.html**), Anthony Landry evaluates the revenue and taxation of the seven G-7 countries—Canada, France, Germany, Japan, Italy, the United Kingdom, and the United States.

There are two main types of taxes: those on consumption sales (such as a state sales tax and the federal tax on gasoline) and those on income. Landry found that, of the G-7 economies, the United States received 11 percent of its revenue from consumption sales taxes during the 2000–2009 period, the smallest percentage among the G-7 countries. In contrast, Japan received 14 percent of its revenue from taxes on consumption sales, while the proportions for Germany (23 percent) and the United Kingdom (26 percent) were more than double that of the United States. (The U.S. average tax rate on consumption sales was 3.7 percent in 2009, compared with an average of 11.1 percent in G-7 economies.)

The other main government revenue consists of three types of income taxes: labor income taxes (including payroll taxes and Social Security contributions), capital income taxes (such as capital gains tax on stocks and bonds), and corporate income taxes (on company profits). In all seven countries, the greatest source of revenue comes from labor income tax, accounting for 55 to 72 percent of government receipts during the 2000–2009 period (70 percent in the United States). The U.S. tax rate on labor income was 22.3 percent in 2009, compared with a 35.7-percent average rate for G-7 economies.

The second source of revenue, a tax on capital income, ranged from 2 percent of the revenue of Germany to 11 percent of United Kingdom revenue. In the United States, capital income taxes accounted for 10 percent of all tax revenue. The 2009 tax on capital income averaged 37.6 percent in the G-7 economies, with three countries having rates higher than the United States' 38.0 percent and three countries having lower. Germany's rate was the lowest at 24.7 percent.

The third source of revenue—taxes on company profits—is corporate income tax. In 2009, the two countries with the highest tax rates were Japan (39.5 percent) and the United States (39.1 percent). Italy and the United Kingdom had corporate income tax rates below 30 percent.

The taxes that a country levies affect individual and firm decisions. On the domestic economic front, incentives created by the tax structure are taken advantage of—regardless of what is happening in other countries. However, with globalization, the tax structure of one country can influence individual and firm decisions in another, such as where in the world corporations seek to invest and operate. Another example is the significant mobility of skilled workers across borders.

Landry notes briefly the importance of *how* a government spends its revenue, and he maintains that a challenge to the United States lies in narrowing the national deficit while competing favorably in the global marketplace. □