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Market Insight

ING MARKET PERSPECTIVES

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Who Is to Blame for Sluggish Employment?

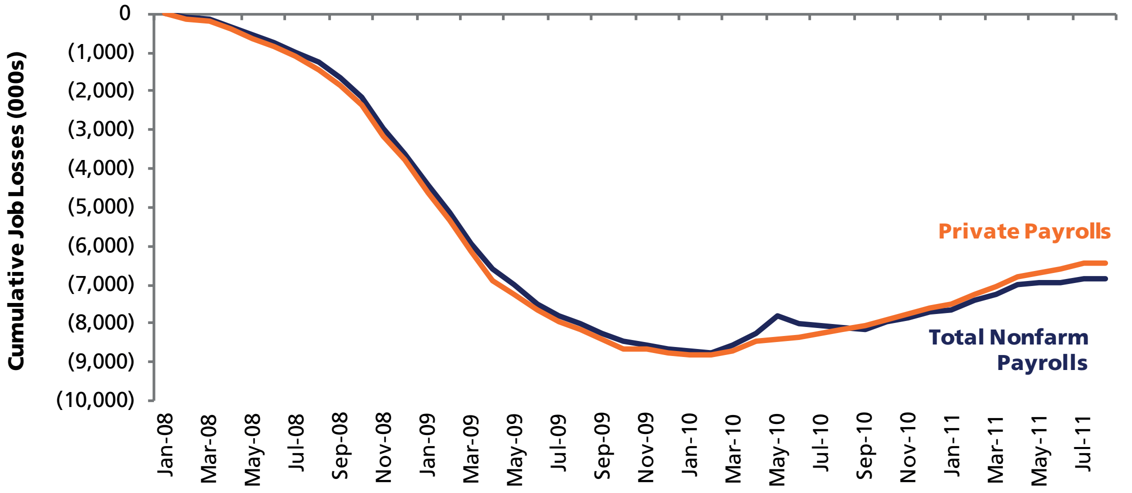
Although the Great Recession officially ended more than two years ago, the unemployment rate in the United States remains stubbornly high. As you can see in Figure 1, both total and private nonfarm payrolls remain about 6–7 million below their end-2007 peaks. Management teams at large corporations are often cited as contributors to the unemployment problem, accused of sitting on high cash balances and not investing in capital projects that would lead to additional hiring. To assess the fairness of these allegations, we analyzed the relationship between corporate employment levels and three key business metrics: revenue, operating income and capital spending. Our analysis suggests that, contrary to conventional wisdom, large corporations are not the primary cause of the weak recovery in the U.S. labor market.

Employment Has Rebounded at Large Firms, but Remains Depressed at Smaller Ones

Our analysis of the large corporate segment used data from our U.S. corporate investment grade issuer database. We constructed a sample set of over 400 companies for which we had revenue, operating income, capital spending and employee headcount data for each time period within our analysis horizon. This process allowed us to analyze the hiring activities of a constant set of corporations. The aggregate number of employees within our corporate sample set was more than 20 million at year-end 2010, equivalent in size to approximately 20% of total private nonfarm payrolls of about 108 million. The average number of employees at companies within this data set was over 49,000, and the median number was over 19,000.

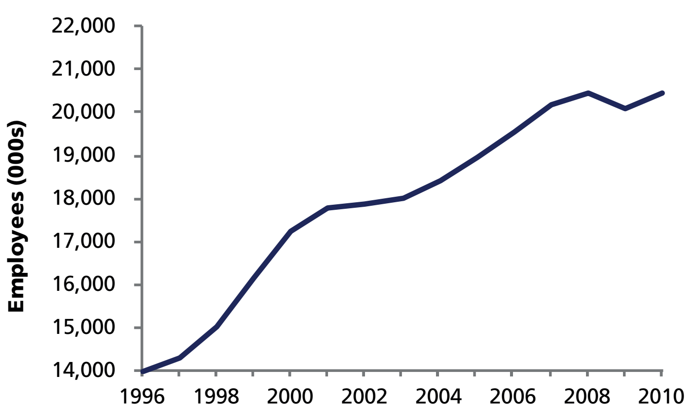
Figure 2 illustrates that the aggregate employment level for this sample set has returned to its late-2008 peak, suggesting that large corporations are not the source of the current unemployment problem. One caveat to this conclusion is that we do not have adequate information to determine the regional distribution of job losses and job recoveries; therefore, it is possible that some of the U.S. jobs lost were recovered in other countries in which these corporations operate. Our guess is that jobs were probably recovered in rough proportion to revenue, but foreign-based revenue may have recovered more quickly than U.S.-based revenue. Despite this possibility, we still think it is fair to say that large corporations are not the primary cause of the weak recovery in the U.S. labor market.

Figure 1. Employment Remains Far Below Its End-2007 Peak



Source: Bureau of Labor Statistics, ING Investment Management

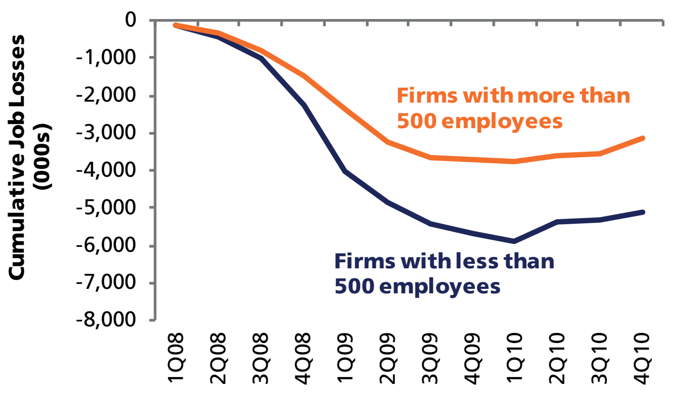
Figure 2. Investment Grade Corporate Employment Has Rebounded



Source: Bloomberg, Barclays Capital, ING Investment Management

This view is supported by data from the Bureau of Labor Statistics, as shown in Figure 3; since the end of 2007, firms with fewer than 500 employees have shed 5 million jobs while those with greater than 500 employees have lost 3 million. Given that large firms have had few, if any, net jobs losses, the missing jobs within the business sector lie within the small-business arena.

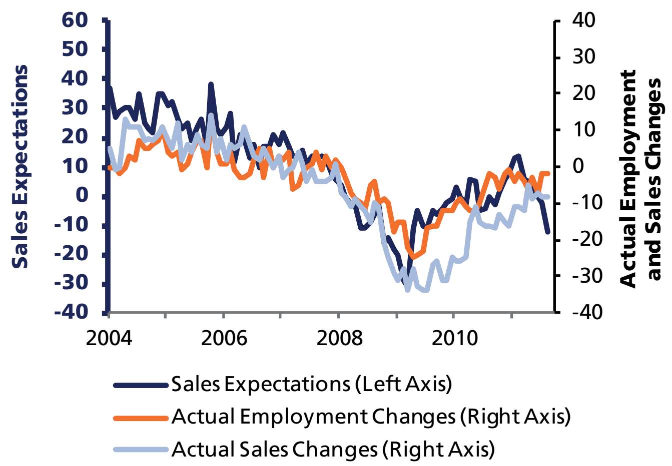
Figure 3. Small Firms Have Shed More Jobs



Source: Bureau of Labor Statistics, ING Investment Management

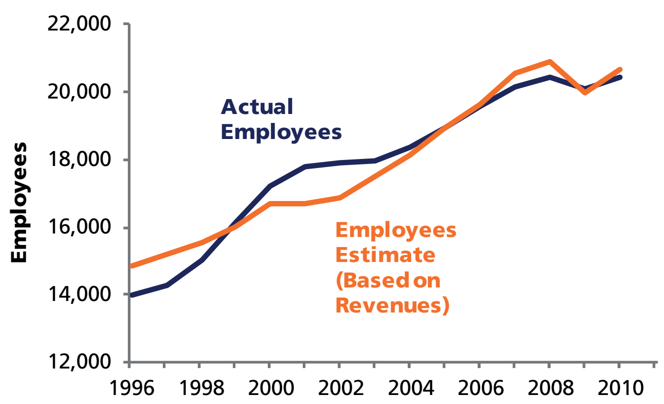
Last year, we wrote in detail on the topic of small business hiring (see "The Impact of Credit Availability and Sales Expectations on Small-Business Hiring," dated December 6, 2010), concluding that small-business hiring was closely tied to sales expectations (see Figure 4). We believe this same relationship exists for corporations of all sizes. We are not aware of an index that allows us to specifically measure sales expectations for large firms, so we utilized regression analysis to test whether revenue, operating income and capital spending levels could be used to explain employment levels. Our analysis revealed that revenue is a statistically significant variable and has a high degree of explanatory power with respect to employment levels. Operating income and capital spending levels were statistically significant variables for explaining employment levels when measured independently, but they were statistically insignificant when tested together with revenue as explanatory variables. In Figure 5, we plot actual employee levels versus the levels that would be suggested based on revenue.

Figure 4. Employment Closely Tracks Sales Expectations at Small Businesses…



Source: National Federation of Independent Businesses, ING Investment Management

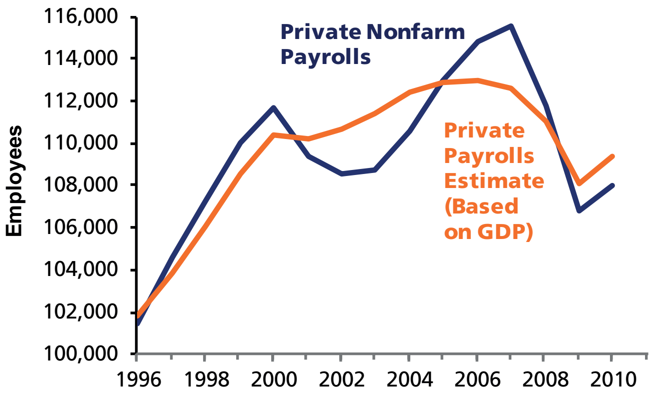
Figure 5. …and Revenue at Large Ones



Source: Bloomberg, Barclays Capital, ING Investment Management

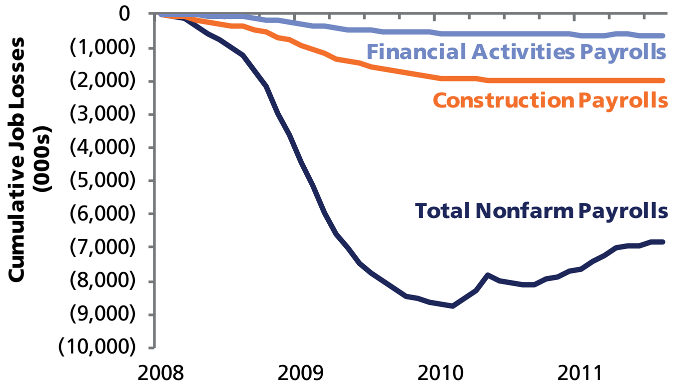
We performed a similar analysis using macroeconomic data, looking for the relationship between private nonfarm payrolls and nominal and real GDP. We found that both measures of GDP were statistically significant in explaining the level of nonfarm payrolls, not surprising given that nominal and real GDP can be thought of as proxies for the entire country's revenue and unit volume. Our findings are illustrated in Figure 6.

Figure 6. Employment Is Closely Connected to Changes in GDP



Source: Bloomberg, ING Investment Management

Figure 7. A Recovery in Construction and Finance Jobs Remains Elusive



Source: Bureau of Labor Statistics, ING Investment Management

Conclusion

In summary, we do not believe that large corporations are the primary source of the unemployment problem. As such, policy makers would be well advised to focus their attention on understanding the reasons for the weak recovery in hiring at small- and medium-sized firms. In our view, the implementation of pro-growth economic policies would improve hiring prospects at both small businesses and larger firms due to the potentially positive impact on revenue.

Many of the lost jobs were tied to the excesses in the construction and financial industries, which have lost about 3 million jobs combined and have shown no signs of recovery (see Figure 7). In our view, it will take years before employment in these industries bounces back; the best thing policy makers can do is encourage overall economic growth, which will foster job additions in more healthy industries.

While we all want a quick fix to the unemployment problem, many of the unemployed may not have the skills to readily transition to industries where employment demand is more robust, so re-training may be required. The labor adjustment process will take time; in our view, the best actions that the government can take are to allow the adjustments to occur while implementing policies that foster both economic growth and a healthy corporate sector. ■