

7.16: Frictional and Structural Unemployment

Learning Objectives

- Explain frictional unemployment
- Explain structural unemployment

Changes in Unemployment over the Long Run

Cyclical unemployment explains why unemployment rises during a recession and falls during an economic expansion. But what explains the remaining level of unemployment even in good economic times? Why is the unemployment rate never zero? Even when the U.S. economy is growing strongly, the unemployment rate only rarely dips as low as 4% (although it hovers around 4.2% in late 2017). Moreover, the discussion earlier in this module pointed out that unemployment rates in many European countries like Italy, France, and Germany have often been remarkably high at various times in the last few decades. Why does some level of unemployment persist even when economies are growing strongly? Why are unemployment rates continually higher in certain economies, through good economic years and bad? Economists have a term to describe the remaining level of unemployment that occurs even when the economy is healthy: it is called the **natural rate of unemployment**.

The Natural Rate of Unemployment

The natural rate of unemployment is not “natural” in the sense that water freezes at 32 degrees Fahrenheit or boils at 212 degrees Fahrenheit. It is not a physical and unchanging law of nature. Instead, it is only the “natural” rate because it is the unemployment rate that would result from the combination of economic, social, and political factors that exist at a time—assuming the economy was neither booming nor in recession. These forces include the usual pattern of companies expanding and contracting their workforces in a dynamic economy, social and economic forces that affect the labor market, or public policies that affect either the eagerness of people to work or the willingness of businesses to hire. Let’s discuss these factors in more detail.

Frictional Unemployment

In a market economy some companies are always going broke for a variety of reasons: old technology; poor management; good management that happened to make bad decisions; shifts in tastes of consumers so that less of the firm’s product is desired; a large customer who went broke; or tough domestic or foreign competitors. Conversely, other companies will be doing very well for just the opposite reasons and looking to hire more employees. In a perfect world, all of those who lost jobs would immediately find new ones. But in the real world, even if the number of job seekers is equal to the number of job vacancies, it takes time to find out about new jobs, to interview and figure out if the new job is a good match, or perhaps to sell a house and buy another in proximity to a new job. The unemployment that occurs in the meantime, as workers move between jobs, is called **frictional unemployment**. Frictional unemployment is not inherently a bad thing. It takes time on part of both the employer and the individual to match those looking for employment with the correct job openings. For individuals and companies to be successful and productive, you want people to find the job for which they are best suited, not just the first job offered.

In the mid-2000s, before the recession of 2008–2009, it was true that about 7% of U.S. workers saw their jobs disappear in any three-month period. But in periods of economic growth, these destroyed jobs are counterbalanced for the economy as a whole by a larger number of jobs created. In 2005, for example, there were typically about 7.5 million unemployed people at any given time in the U.S. economy. Even though about two-thirds of those unemployed people found a job in 14 weeks or fewer, the unemployment rate did not change much during the year, because those who found new jobs were largely offset by others who lost jobs. Thus, while *individuals* stay frictionally unemployed for relatively short periods of time, the size and dynamism of the labor market means that there is always a sizeable amount of frictional unemployment in the economy.

Of course, it would be preferable if people who were losing jobs could immediately and easily move into the new jobs being created, but in the real world, that is not possible. Someone who is laid off by a textile mill in South Carolina cannot turn around and immediately start working for a textile mill in California. Instead, the adjustment process happens in ripples. Some people find new jobs near their old ones, while others find that they must move to new locations. Some people can do a very similar job with a different company, while others must start new career paths. Some people may be near retirement and decide to look only for part-time work, while others want an employer that offers a long-term career path. The frictional unemployment that results from people moving between jobs in a dynamic economy may account for one to two percentage points of total unemployment.

The level of frictional unemployment will depend on how easy it is for workers to learn about alternative jobs, which may reflect the ease of communications about job prospects in the economy. The extent of frictional unemployment will also depend to some extent on how willing people are to move to new areas to find jobs—which in turn may depend on history and culture.

Frictional unemployment and the natural rate of unemployment also seem to depend on the age distribution of the population. As we saw earlier, unemployment rates are typically lower for people between 25–54 years of age than they are for those who are either younger or older. “Prime-age workers,” as those in the 25–54 age bracket are sometimes called, are typically at a place in their lives when they want to have a job and income arriving at all times. But some proportion of those who are under 30 may still be trying out jobs and life options and some proportion of those over 55 are eyeing retirement. In both cases, the relatively young or old tend to worry less about unemployment than those in-between, and their periods of frictional unemployment may be longer as a result. Thus, a society with a relatively high proportion of relatively young or old workers will tend to have a higher unemployment rate than a society with a higher proportion of its workers in middle age.

Watch It

Watch this video to analyze frictional unemployment, why it occurs, and how it fluctuates over time.

An interactive or media element has been excluded from this version of the text. You can view it online here: <http://pb.libretexts.org/mlum/?p=313>

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Structural Unemployment

Another factor that influences the natural rate of unemployment is the amount of **structural unemployment**. The structurally unemployed are individuals who have no jobs because they lack skills valued by the labor market, either because demand has shifted away from the skills they do have, or because they never learned any skills. An example of the former would be the unemployment among aerospace engineers after the U.S. space program downsized in the 1970s. An example of the latter would be high school dropouts. Structural unemployment is persistent, long term and difficult to reduce.

Some people worry that technology causes structural unemployment. In the past, new technologies have put lower skilled employees out of work, but at the same time they create demand for higher skilled workers to use the new technologies. Education seems to be the key in minimizing the amount of structural unemployment. Individuals who have degrees can be retrained if they become structurally unemployed. For people with no skills and little education, that option is more limited.

Watch It

Watch the selected clip from this video to learn about how structural unemployment is both persistent and long-lasting. When major shocks occur, such as changes in technology or a crisis that causes a shift in the skills needed in the labor market, structural employment is often the result. This clip will explain how labor regulations in Europe have created a situation where structural unemployment is more prevalent in Europe than in the United States.

An interactive or media element has been excluded from this version of the text. You can view it online here: <http://pb.libretexts.org/mlum/?p=313>

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Glossary

[glossary-term]frictional unemployment: [glossary-definition]unemployment that occurs as workers move between jobs

[glossary-term]natural rate of unemployment: [glossary-definition]the unemployment rate that would exist in a growing and healthy economy from the combination of economic, social, and political factors that exist at a given time; the sum of frictional plus structural unemployment

[glossary-term]structural unemployment: [glossary-definition]

definition]unemployment that occurs because individuals lack skills valued by employers[/glossary-definition]]/[glossary-page]

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