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COMMENTS AND CRITIQUE

ON

State Auditor's Report: Minnesota Economy: Facing the Facts, July 1990









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by

August 6, 1990



Executive Summary

Comments and Critique on State Auditor's Report Minnesota's Economy: Facing the Facts

Data from the Department of Jobs and Training was misused and misinterpreted in a recent report by the State Auditor that claimed the state's economy is deteriorating. These findings should be viewed with extreme skepticism.

This department collects data in many ways and from many sources. Some of our data, for example, is from reports of state employers who pay unemployment taxes. Other data stem from surveys required by the Bureau of Labor Statistics, with stipulated collection methods. The Auditor's report confuses different data series which are not interchangeable.

Other data problems confuse the issues raised in the Auditor's report. For example, the report does not always use the latest available data. It does not cite sources of data, and when it does, cites vaguely, as in references to "Department of Jobs and Training" without date, publication title, page number or any other specifics. Finally, the report uses unpublished data which the Bureau of Labor Statistics itself considers unreliable. The report creates charts and cites this agency as a source, when they are charts we have never published.

We agree that our data collection is not perfect--for example, sample sizes should be larger--but within budget constraints and federal requirements, it serves its purpose quite well. We regularly explain the limitations and cite mitigating factors in our publications.

Although not all indicators are unequivocally positive, our data do show several trends that argue against the "deterioration" claimed by the report. For example, the number of non-farm jobs grew faster from 1979 to 1989 in Minnesota than in the four surrounding states. Minnesota also created 17,500 manufacturing jobs during that period, resulting in a faster growth rate than the nation's or surrounding states' (except South Dakota, which had a small base to start with).

We agree that the truly rural portions of Minnesota face particular hardships, and that sluggish growth or decline in population and employment in these areas has been going on since at least 1950. Since 1987, however, Greater Minnesota overall has done better than the Minneapolis-St. Paul metropolitan area in terms of job growth.

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While the State Auditor claims that statewide employment grew by 4.6 percent in 1988 and 1.1 percent in 1989, our data show otherwise. The highly reliable Current Employment Statistics (CES) series, measuring jobs, shows 3.3 percent average growth in 1988 and 3.1 percent in 1989. The more inconsistent Labor Force series, measuring employed persons, shows 4.4 percent growth in 1988 and 0.4 in 1989.

The report speaks of the rising number of unemployment insurance claimants, which we at DJT have consistently reported. The number of claimants can rise while unemployment goes down for several reasons, including a growing pool of workers and fewer new entrants to the labor force looking for work.

The report lacks the broad perspective it advocates. If, as the report says, the Auditor needs a more comprehensive measure, he might consider personal income data from the U.S. Department of Commerce. Those data say Minnesota personal income rose by 8.4 percent from a year earlier, compared with 5.2 percent inflation. These growth rates exceed the nation's.

When all the data on jobs, wages and incomes are properly represented, it is evident that Minnesota's economic growth continues at or above the pace found in the nation, largely following U.S. and international trends.

Introduction

The comments and critique on the State Auditor's report, *Minnesota's Economy: Facing the Facts*, refer to only those statistics and statements directly related to the Department of Jobs and Training. We find two major shortcomings with the Report. First, it lacks an understanding of the various data series we produce, to the point where they are represented incorrectly, used interchangeably, and interpreted wrongly. Second, the report lacks the broad perspective it calls for, ignoring income and other economic data, failing to make comparisons with the nation or other states, and not incorporating in its analysis trends beyond the last year or so. Also, it is important to recognize that Minnesota's economy follows mostly the U.S. economic trends and is largely influenced by the economic and political decisions made at the national and international levels.

We are responding to those elements of the report related to us by grouping them in the following categories and treating them in this order. The page numbers refer to the location of that issue in the original report.

- 1. Statewide Employment (Page 2)
- 2. Labor Force Estimates for Substate Areas (Page 8)
- 3. Manufacturing Jobs and Earnings (Page 2)
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- 8. Covered Employment vs Nonfarm Wage and Salary Employment (Page 10)
- 9. Payroll Wages Adjusted to Inflation (Page 12)

Issues pertaining to Public Assistance (p. 6), Worker's Compensation Reform (p. 7), Telecommunications & Transportation System (p. 7), Home Care (p. 7), and Education (p. 7) are outside the scope of this Department.

Minnesota's economy is more stable relative to its surrounding states (Iowa, N. Dakota, S. Dakota, Wisconsin). Between 1979 and 1989, Minnesota's total nonfarm jobs grew faster than those totals in any of the four surrounding states. During that period, Minnesota created 17,500 manufacturing jobs, which was faster rate of growth than the nation or any neighboring state. The exception was South Dakota where the addition of 4,200 manufacturing jobs resulted in a large proportional change since that state had a relatively small number of manufacturing jobs. Between the first quarter of 1989 and 1990, Minnesota's quarterly personal income grew (8.4 percent) faster than the nation's (6.9 percent) and any of the surrounding states by a substantial margin, according to the data released by the U.S. Department of Commerce in July 1990. The author's claim in the Introduction to his Report that "statistics which illustrate the deterioration of the State's economy have received scant attention while the public eye has been fixed on a reassuringly low unemployment rate" is not based on complete facts.

The author also notes in his Introduction that "The problem of hardship is most acute in rural Minnesota". This is not a recent phenomenon, nor is it unique to Minnesota. We agree that the truly rural portions of Minnesota face particular hardships, and that sluggish growth or decline in population and employment in these areas has been going on since at least 1950. Greater Minnesota is not monolithic and cannot be referred to as such. Regions of the state have different economic bases, and in general, larger centers have seen remarkable growth while smaller towns have not. Department of Commerce information showing total employment losses since 1977 in 22 of the state's 87 counties is confirmed by our data on wage and salary jobs. Thirty-one counties had fewer of these jobs in 1988 than they did in 1978.

Since 1987, however, in a significant departure from long-term trends, Greater Minnesota has done relatively better than the Minneapolis-St. Paul Metropolitan Area in terms of job growth. Between 1987 and 1989, both total nonagricultural and total manufacturing jobs grew faster in Greater Minnesota (8 percent and 11 percent) than in the Minneapolis-St. Paul Metropolitan Area (6 percent and 4 percent).

While the issues raised in the report are legitimate, the author has not followed the generally accepted standards and practices in preparing the document.

1. The author does not always use the latest available data. For instance, the nonagricultural wage and salary employment figures appear to have been taken from our Minnesota Labor Market Review (monthly & quarterly publication). Preliminary data is published in the Review, with periodic revisions made to this data. The use of outdated or preliminary data would not only distort the magnitude and direction of change, but also the specific conclusions.

2. The author has not followed the common practice of citing sources of data when he makes a point. For example, when he illustrates wages and earnings (p. 12, p. 13) in real terms, the author does not mention which deflator was used in calculating the real earnings, and he should have included an explanation of how certain figures were derived in the appendix or in footnote.

3. Again, it is common practice to include in the source such items as the name of office or agency, name of the report or document, page number, and date of publication. For example, mere mention of Jobs and Training as a source will not suffice when data such as wages and earnings and employment statistics are estimated and published from more than one data series which use different methodologies and measures different things.

4. Very often, the author used two series of employment and earnings estimates, Covered Employment and Wages and nonfarm wage and salary employment¹ interchangeably without making any reference to either in the footnote or in the body of the report. These series are not comparable. It simply confuses the readers and renders erroneous conclusions if the series is not properly recognized and explained.

5. While the author has attempted to bring out some of the important economic indicators to support his notion of the "deterioration of the State's

¹ Non-agricultural wages and salary employment and non-farm wage and salary employment are used interchangeably in practice and they are derived from the Current Employment Statistics (CES) program.

economy", the conclusions are carelessly overstated and the presentation of data and analysis is clumsy at best.

One major recommendation of the report (Page 7) was that the "policy should flow from scientific measurements derived from as many sources as possible." We couldn't agree more wholeheartedly. The author is not aware that this is already being done. The data cited in the report — at least those that are the responsibility of our agency — are all derived from programs or surveys that are conducted in every state under the direction of the U.S. Bureau of Labor Statistics. We are subject to strict standards regarding collection and processing of this information.

With advice from the Economic Resource Group (ERG) and private sector economists, we are presently engaged in a project that will provide current data from many sources. The result of a two-year developmental effort, *Minnesota Economic Indicators* will briefly present trends for seven indicators of the state's economy that we have up-to-date information on: wage and salary employment, retail sales, manufacturing hours, manufacturing earnings, building permits, business incorporations and initial unemployment insurance claims. The first release of this publication will be later this year. The primary intention of this report is to take some heat off the unemployment rate, currently the most looked at indicator of state economic health.

In calling for use of more comprehensive measures, the state auditor also could have used personal income measures when he compared employment and wage trends from 1988 to 1989 using the U.S. Department of Commerce data. That would have been useful in explaining the full story of the current shape of Minnesota's economy. The latest information from this source (through the first quarter of 1990) shows that Minnesota personal income rose by 8.4 percent from a year earlier, well above inflation, which was 5.2 percent as measured by the March Consumer Price Index (CPI). Moreover, the component attributable to wages and salaries increased by an even greater 9.3 percent. These growth rates exceed the nation's.

While the data on economic and population characteristics are adequate and readily available for the U.S. through the Current Population Survey (CPS), federal-State data collection efforts, and special studies, adequacy and reliability of the data at the State and local levels leave much to be desired. A sound data base is critical to program planning, policy development and program evaluation. It requires a coordinated effort of all the State agencies with adequate resources made available for data collection, analysis and dissemination.

Statewide Employment (Page 2)

The author claims that statewide employment grew by 1.1 percent in 1989 and 4.6 percent in 1988. Because the state auditor failed to cite the data source for his calculations, we were unable to verify his stated growth rates. However, to set the record straight, we have included employment figures from two of our data series in the table.

	CES Employment	Percent change over the year	Labor Force total employment	Percent change over the year
Annual average 1987	1962.5		2139.0	
Annual average 1988	2028.0	3.3	2233.0	4.4
Annual average 1989	2091.2	3.1	2241.0	0.4
January-April 1989	2038.0		2190.7	
January-April 1990	2098.0	2.9	2232.0	1.9

It will be noted that the two series show somewhat different rates of growth, particularly between 1988 and 1989. Although we are unable to reconcile the differences in the two measures absolutely (3.1 percent and 0.4 percent for the CES and Labor Force employment, respectively from 1988 to 1989), it might be useful to mention the nature of these series as each is measuring somewhat different kinds of employment. The Current Employment Statistics (CES) program is generated through a monthly survey of some 6,000 Minnesota firms and benchmarked to employer unemployment insurance tax returns. It includes nonagricultural wage and salary jobs by place of work. It is a less comprehensive measure than is the total employment component of the labor force series (hence the larger numbers in the table). The labor force employment purports to include <u>all</u> people who work and is by place of residence (Wisconsin residents who commute to Minnesota for work would not be included); agricultural workers, and self-employed people as well as unpaid family members of a small business are included in total employment.

The monthly labor force estimates of total employment and unemployment are derived through a statistical technique called regression formulas. Regression is based upon historical relationships between known variables. These relationships are then applied to current variables to produce up-to-date estimates. At the end of a calendar year, the monthly regression based estimates are altered in a manner which will make the twelve month average of the regression estimates equal the annual average of estimates derived from a household survey conducted under the auspices of the Bureau of Labor Statistics (BLS). This survey is called the Current Population Survey (CPS) and is the instrument used to gauge the employment and unemployment status of the nation's labor force. A subsample of the national sample is used to yield Minnesota estimates.

Although this instrument produces very reliable monthly estimates for the U.S. and reasonably accurate annual average data for states, the monthly data for Minnesota are not considered reliable enough for direct use; hence, regression formulas. As stated above, the monthly regression estimates at the end of the year are changed and the annual average of the regression estimates will be the forced CPS annual average. Given the difference in what these two series are attempting to measure and the ways in which they are constructed, is it any wonder that they don't always agree?

While we may have arguments with the methodologies used in the construction of either series from time to time, but we are "stuck" with the system as both series are mandated and funded by BLS. In defense of BLS, we would like to say that the measurement of employment and unemployment, at a moderate cost, is not an easy matter. We think BLS does a good job of running honest, politically free programs.

Labor Force Estimates for Substate Areas (Page 8)

Let us now turn to a discussion of the labor force estimates for counties and Metropolitan Statistical Areas. These estimates, in the first stage, are developed through something called a "handbook procedure." The handbook categorically accounts for various types of employment and unemployment for a given area. It relies heavily on operations data (Unemployment Insurance claims and "covered" employment, byproducts of administering unemployment compensation), census data, and regional and national information from the CPS.

After handbook estimates are completed for all geographic areas within the state, the individual handbook estimates are summed and compared to the independently derived state estimates (the regression estimate). Next, the county estimates are proportionately changed so the sum of the parts (counties and MSAs) equals the whole (State regression estimates).

Are there weaknesses in the county estimates? Yes, unequivocally the state auditor was not the first person to discover the shortcomings. A Presidential commission headed by Sar Levitan (a professor at Georgetown University) studied this situation for over two years in the late seventies. Testimony was taken from academicians, government officials and laymen in 50 states. The report of Levitan's findings was some two inches thick. The report concluded that although county and MSA labor force estimates were weak, the system was working as well as could be expected, given the paucity of data and resources.

Manufacturing Employment and Earnings (Page 2)

It is true that manufacturing jobs in Minnesota have declined slightly over the last year or so. However, it is important to put this loss in perspective. Between April 1989 and April 1990, manufacturing jobs in Minnesota declined only 494 or 0.1 percent, despite the loss of over 3,700 jobs in the computer and office equipment sector. Over the same period, manufacturing jobs in the United States declined 260,000 or 1.3 percent.

It is also true that Minnesota production worker earnings in manufacturing have been sluggish over the last few years. The \$29.69 decline in earnings between 1986 and 1989 cited by the state auditor cannot be duplicated because of the use of unrevised data and the failure to cite which CPI series was used in the adjustment for inflation. Using the latest data and the CPI-W for the United States to adjust for inflation, we find that average weekly earnings in manufacturing declined \$23.52 or 5.3 percent between 1986 and 1989. During the same period earnings declined \$17.79 or 4.1 percent in the United States. However, in the period from April 1989 to April 1990, manufacturing earnings (not adjusted for inflation) increased \$4.80 per week in Minnesota and only \$0.64 in the United States.

Office and Computing Jobs and Earnings (Page 2)

It is true that over 5,000 computer and office equipment jobs have been lost in Minnesota over the last two years. The earning and payroll data used by the author, however, are not accurate and are based on both unrevised data and a lack of understanding of the data series.

The over \$600 figure used for average weekly earnings is based on unrevised data. According to revised data, the high point for this series was \$551 in May of 1989.

The figures given for total payroll are also not accurate. A total payroll figure <u>cannot</u> be computed using CES Statistics data. The earnings estimates are for production workers only; not for all employees. Production workers in this industry are estimated at about 25 percent of the total. Moreover, the estimates are based on the information for one reference week in the month. Evidently the figures given in the report assumed that the earnings figures covered all employees and computed a <u>weekly</u> payroll by multiplying the average weekly earnings by total employment. This is simply wrong and misleading.

Total Unemployment vs Insured Unemployment (Page 2)

The seven month average unemployment rate for the period October 1989 thru April 1990 was 4.4 percent, compared to 4.3 percent for the same months a year earlier. During the period in question, the labor force and total employment grew 1.8 percent and 1.7 percent, respectively. The increase in number of people unemployed (up 3.1 percent, not down 1.9 percent as stated by the State Auditor's report) outstripped employment in this time frame and boosted the jobless rate by one-tenth of a point. While it is true that unemployment claims were up an average of about 5,900 a month, or roughly 15 percent per month on average over the seven month period, that rise was not equaled by the increase in total average unemployment (103,900 minus 100,800 = 3,100). But, since claims, on an annual average basis, only account for about 1/3 of total unemployment, it doesn't necessarily follow that total unemployment must exactly track changes in claims data. The seasonal and cyclical patterns of various components may differ. For example, during the October through April 1990 period construction employment experienced layoffs of greater magnitude than it had the year before, as did manufacturing, causing the increased level of claims activity. Other major industries did not experience the same behavior. Employment in trade and services actually increased to more than offset declines in construction and manufacturing. These trends were noted in the various publications released by this agency.

Another characteristic of the unemployment insurance figures is that the number of claimants tends to rise on average from year to year. As the number of covered workers increase, the numbers subject to layoffs due to seasonal and other factors also increase.

Also, claims could be rising during a period of <u>slow</u> employment growth while new and re-entrants to the labor force could be declining. New and re-entrants may feel that job opportunities are scarce, consequently some may pursue activities outside the labor force, such as furthering their educations.

However, we do not ignore changes in claims data. We have from time to time pointed out in our monthly labor force news releases that the total unemployment rate and changes in claims data do not seem to be reflecting the same labor market dynamics that occur in the economy. We may not be able to offer a concrete explanation of "mixed signals", but we do mention it if we feel it is significant. Finally, this Department has <u>many</u> news releases. One of our releases is issued weekly and contains a host of unemployment insurance statistics complete with absolute and percentage changes from a year ago and comments to highlight changes of significance.

We agree that the number of persons receiving benefits has been above the comparable number for the same month a year ago for the last two years and this trend continues through July 1990. This is one of many indications of a slowing economy, and we have been watching it. It should be added, however, that 1988 was a very good year, and that the number of claimants receiving benefits in that year was so low that any increase, whether attributed to the seasonal or cyclical conditions, could create an increase as large as a 24 percent increase. Historically, whenever the number of claimants receiving benefits has risen, duration of claimants in claims status also has risen.

Changes in UI Claims (Page 15)

The author compares the seasonal declines in the number of Unemployment Insurance claimants from January to April of 1987 and 1988 with the declines in the number of claimants from January to April of 1989 and 1990. In 1987 and 1988, the drop in the number of claimants was greater from January to April than it was from January to April of 1989 and 1990. In 1989 and in 1990, some seasonal industries such as construction had slow starts, but by June, most of the laid-off workers had been re-called. While the number of claimants is higher in 1989 and 1990, seasonal factors caused the January to April comparison to present a distorted picture. The longer period of January through June provides a more realistic picture, rather than the shorter period, which is highly sensitive to seasonal variation.

Various Employment Series (Page 10)

The Minnesota Department of Jobs and Training produces three different series of employment statistics: (1) A <u>Labor Force</u> series, produced monthly, represents an estimate of total employment which includes both agricultural and nonagricultural employment; (2) A *Nonfarm Wage and Salary Employment* series, produced monthly, includes only nonagricultural wage and salary workers estimated from a sample survey of employers; (3) A *Covered Employment and Wages* series, produced quarterly, includes a complete count of workers covered by the unemployment compensation law. As evident from the information above, each series of employment and/or wages has different estimates and series are not comparable because they do not equally represent all segments of employment. There are also other differences, as well as specific purposes, for each series which we will not attempt to explain here, other than to say that an understanding of these difference and limitations is necessary so that they can be properly used. The author does not understand the difference between these series and uses them interchangeably without differentiation.

The author's reference to payroll employment refers to the Covered Employment and Wage series, with some error about who is excluded. Not all farm workers or domestic workers are excluded. The author states that payroll employment tends to increase whether times are good or bad. This is not correct. The record shows that covered employment did decrease in 1982 and 1983 from previous years. Also, it is not correct to say that economic conditions in covered employment between 1987 and 1989 were bad, or to suggest that a decline in employment should have occurred during a period of economic growth.

Covered Employment vs Nonfarm Employment (Page 10)

Based on the description of the statistics and numbers referred to as payroll employment, we are assuming that the author is referring to the covered employment series, but some of the data appear to be from the nonfarm employment series. Also, it is confusing when the author refers to payroll employment data on the graphs on page 11, which are from the nonfarm employment series and not comparable to the content on page 10. Also the nonfarm employment data shown on the graphs are data that have since been revised.

Payroll Wages Adjusted to Inflation (Page 12)

The author illustrates in a table on page 12 that the payroll wage increase adjusted for inflation rose only 0.98 percent in the first three quarters of 1989. Since we do not know what inflation factor was used, our analysis indicates a slightly different result. The figures we used to make inflation adjustments came from the U.S. consumer price index for wages (CPI-W) as released by the Department of Labor, Bureau of Labor Statistics each month and annually (1982-84=100).

INCREASE IN STATE PAYROLL WAGES COMPARED TO INFLATION (Millions)

0.S. CPI-w (1982-84=100)		PRIOR YEAR	INFLATION	ACTUAIL	REAL GAIN	
1987	112.5	\$36,023	\$37,317	\$38,867	\$1,550	(4.15%)
1988	117.0	38,867	40,422	42,177	1,755	(4.34%)
1989	122.6	42,177	44,196	45,113	917	(2.07%)

Our calculation using the U.S. CPI-W shows a real gain of 4.15 percent in 1987, 4.34 percent in 1988, and 2.07 percent in 1989. Data for all of 1989 was used in making this calculation. The author's use of the first three quarters for 1989 produces misleading results because annual salaries, bonuses, and other wage payments are usually made at the end of the year.

The table below shows the United States as a whole for the same years as in the Minnesota study in the previous table. The wages exclude those paid to federal employees in the U.S., and this would effect a small change on the results of less than 1 percent. The U.S. wage totals show a real gain of 3.85 percent in 1987, 4.17 percent in 1988, and 1.18 percent in 1989. The figures for 1989 include preliminary data.

Minnesota seems to be following a national trend as the real gain in payroll wages dropped to only 2 percent in 1989. However, the real gain in each of the last three years is slightly higher in Minnesota than it is nationwide. A further comparison of other data in this report with U.S. data would be helpful in determining if many of the statistical trends noted in this report are specific to Minnesota or are part of a larger nationwide pattern.

INCREASE IN UNITED STATES PAYROLL WAGES COMPARED TO INFLATION (Millions)

PRIOR YEAR		INFLATION	ACTUAL	REAL GAIN	
1987	1,890,437	1,958,326	2,033,648	\$75,322 (3.85%) \$88,093 (4.17%)	
1988	2,203,048	2,308,534	2,335,736	\$27,202 (1.18%)	

NOTE: DOES NOT INCLUDE FEDERAL GOVERNMENT *based on preliminary data Source: Bureau of Labor Statistics

The author's analysis correctly identifies a decline in real gain in wages. However, the author's report gives the impression that the decline is a Minnesota phenomenon without recognizing that it is also nationwide as indicated in the previous table.

Conclusion

When all the data on Minnesota's labor markets is properly represented and analyzed, it appears that the sweeping statements made by the State Auditor's Office are incorrect. The state's economy is not deteriorating -- growth in jobs, wages, and incomes continue at or above the pace found in the nation, and moves in lockstep with it. When compared to neighboring states, it looks even stronger. Moreover, recent growth is not limited to the Twin Cities a ea, rendering general cries of rural hardship overly simplistic.

Using a single indicator such as the unemployment rate to gauge the complexity of state economic conditions is not a stance we have taken. Bringing in other measures creates new problems, however, for data series will oftentimes conflict with one another. It is to be expected because they capture different populations and utilize different methods of collection and for different purposes. In our work we have always sought to understand and portray their distinctions while incorporating into analysis as much perspective as possible. If our past record is not enough to prove this point, then these comments in response to the State Auditor's questioning should suffice.