FEDERAL RESERVE BANK *of* ATLANTA

WHERE ARE THE JOBS?

In the nearly five years since the recession ended, we have recovered a lot of ground in the labor market. But we still are far short of replacing the 8.7 million lost jobs.

To view the 2013 Annual Report, visit
frbatlanta.org/pubs/annualreport/13ar/

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PRESIDENT'S MESSAGE

The Federal Reserve has a dual mandate, with two objectives, and those objectives are full employment and low and stable prices. For most Americans, the critical element of our ongoing economy recovery is employment. Since the end of the worst recession in the post-World War II era, jobs in the nation and the Southeast have been growing more slowly than in earlier recoveries. Policymakers and researchers have been focusing on the forces that affect the labor market.

In this year's annual report, the Federal Reserve Bank of Atlanta is exploring the labor market in a lively and interactive format. We want to bring to life a timely and important topic: where are the jobs? I invite you to come along as the Federal Reserve Bank of Atlanta explores that question in our 2013 Annual Report.

"IN ITS MONETARY POLICY RESPONSIBILITIES, THE FED IS TASKED WITH PROMOTING STABLE PRICES AND MAXIMUM EMPLOYMENT."

Dennis Lockhart
President and CEO of the Federal Reserve Bank of Atlanta

WHERE DOES THE LABOR MARKET STAND?

EMPLOYMENT

Jobs in private service–providing industries came back relatively quickly, while other major sectors, notably manufacturing, construction, and government, lagged.

PAGE 8

UNEMPLOYMENT

How much of the improvement in the unemployment rate is due to declining labor force participation? A falling unemployment rate does not necessarily mean a healing labor market.

PAGE 10

The labor market has been recovering slowly. We look at vital signs, including recent employment growth and unemployment and some of the key ingredients of both. Labor force participation has been a particular concern for economists and policymakers.

LABOR FORCE PARTICIPATION

The unemployment rate has improved considerably since the recession ended, but other labor market indicators showed less progress.

PAGE 14

SOUTHEASTERN PERSPECTIVE

By the end of 2013, the United States had regained 87 percent of lost jobs; the Southeast had reclaimed only 62 percent.

PAGE 16

EMPLOYMENT RECOVERY HAS BEEN HISTORICALLY SLOW

The nation's labor market has recovered far more slowly after the Great Recession than it did following every other economic downturn since World War II. To be sure, employment growth was promising in 2013, and the unemployment rate declined.

Other measures of the labor market remained subdued, however. The compensation to workers—including benefits and adjusted for inflation—has barely risen above its prerecession level. At year's end, almost 38 percent of unemployed people had been jobless for at least 27 weeks, by far the highest percentage of long-term unemployment since World War II. Moreover, 12.6 million people left the labor force in the six years through December 2013.

By any measure, the labor market healing has been gradual. Consider that it took 10 months on average for the United States to regain all the jobs lost during seven recessions between 1950 and 1989. It's taken increasingly longer to recover lost jobs in each subsequent downturn.

This recovery has been the slowest yet. From the prerecession employment peak in 2007, total U.S. nonfarm employment declined by 8.7 million jobs. At the end of 2013, almost five years after the recession's end, the nation's labor market was still roughly a million jobs shy of that peak.

The muted pace of the jobs recovery has not been the result of just a few underperforming sectors. Employment in private service–providing industries, for example, now exceeds the level it had reached before the Great Recession. But the increase in service-sector jobs is still 20 percentage points below the average improvement enjoyed in recent recoveries.

The labor market recovery has been even more constrained by weakness in other major sectors. A long-term decline in manufacturing employment accelerated during the recession. Factory job numbers ticked back up a bit last year. Still, as 2013 ended, manufacturing employment remained below its cyclical peak in 2007 and at a level roughly equal to that of 1940, according to the U.S. Bureau of Labor Statistics.

Construction employment fared even worse. The number of construction jobs declined 30 percent during the Great Recession. At the end of 2013, construction employment was still nearly 25 percent below the prerecession high.

Unlike the manufacturing and construction sectors, public-sector employment traditionally withstands downturns relatively well. During this cycle, however, governments at all levels slashed staffing as revenues tumbled. Local government, the biggest public-sector employer, cut the most jobs. Like the manufacturing and construction sectors, government employment was still below its prerecession level at the end of 2013.

LABOR MARKET RECOVERY TAKING LONGER WITH EACH RECESSION

10 MONTHS

to replace all jobs lost during the average of seven recessions between 1950 and 1989

23 MONTHS

to replace all jobs lost during the recession of 1990-91

38 MONTHS

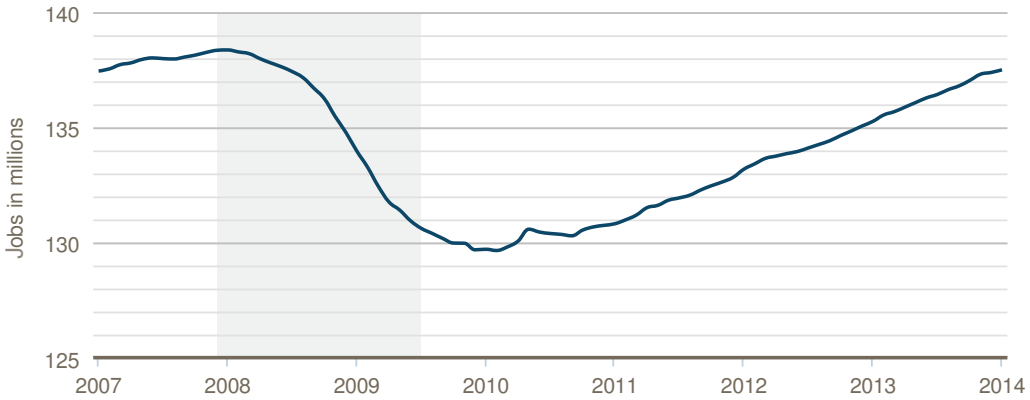
to replace all jobs lost during the recession of 2001

54 MONTHS

since the end of the Great Recession of 2007-09, and we still have not replaces all jobs

Sources: Atlanta Fed research, U.S. Bureau of Labor Statistics

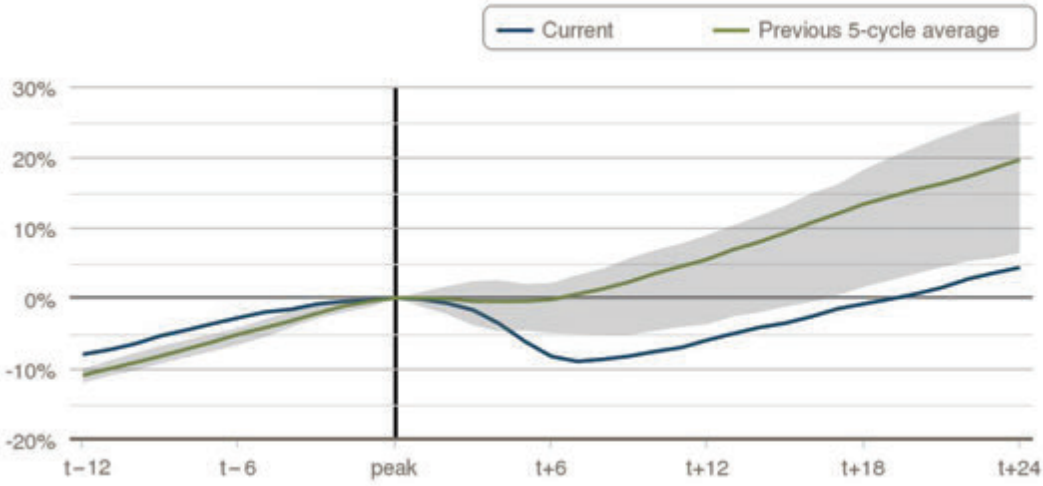
U.S. LABOR MARKET'S GRADUAL PROGRESS



Source: U.S. Bureau of Labor Statistics

U.S. PROFESSIONAL AND BUSINESS SERVICE EMPLOYMENT

Percent deviation from peak



Notes: The gray area indicates the range of the last five major recessions preceding the most recent one. Years of the previous recessions are 1970, 1974, 1981-82, 1990, and 2001. "Current cycle" measures the change in employment 12 quarters before the last recession's peak (Q42007) and the 24 quarters since the peak.

Source: U.S. Bureau of Labor Statistics

LOWER UNEMPLOYMENT DOESN'T TELL THE WHOLE STORY

Since peaking at 10 percent in October 2009, the U.S. unemployment rate has improved significantly. At the end of 2013, the jobless rate was 6.7 percent, its lowest point in five years. But that figure may overstate the actual level of utilization of the nation's labor resources for at least two reasons.

First, there is a thin line between being officially counted as unemployed and being counted as out of the labor force. This issue may be particularly severe among those who have been out of work for a long time. Consider, for example, that about 1 million more people are marginally attached to the labor force than before the recession, and much of that increase came from people who had previously been unemployed for more than half a year. If these additional marginally attached people were counted as unemployed, then the effective unemployment rate would be higher.

Second, since 2007, about 3 million more people say they are working fewer hours than they want to, either because of slack work conditions or the unavailability of full-time jobs. If this additional stock of involuntary part-time workers were counted as being at least partly unemployed, then the effective unemployment rate would be even higher. An upper bound on the possible distortion to the unemployment rate caused by these effects can be seen by comparing the official unemployment rate statistic known as U-3 with the alternative unemployment rate measure known as U-6.

Long-term unemployment

The Great Recession caused the largest surge in joblessness since the 1930s. About 3.4 million more people were unemployed at the end of 2013 than before the recession. In more normal times, jobs are created fast enough to absorb most people who are looking for work within just a few months. In the years before the Great Recession, only about 20 percent of unemployed people had been searching for a job for more than six months. But this figure rose sharply after the recession, reaching 45 percent in 2010 and 37 percent at the end of 2013. Moreover, those out of work for more than six months are getting a job at a much lower rate than before the recession.

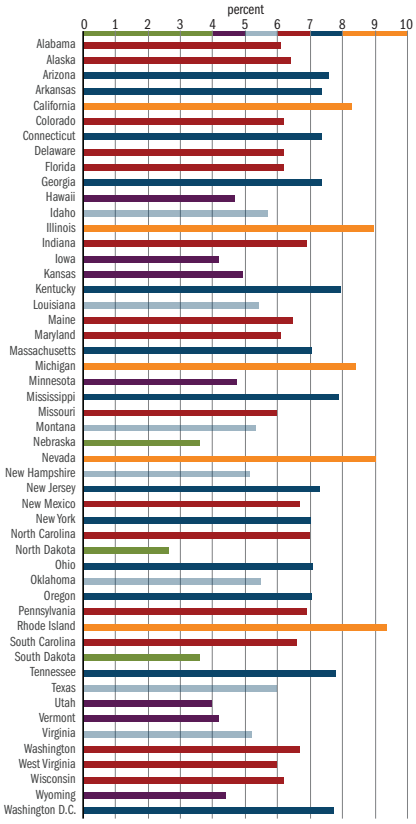
The economic and human costs of long-term unemployment are disturbing. A long spell of unemployment can create significant financial stress. People who endure long periods of unemployment tend to have a more difficult time reentering the workforce even after the economy improves. Long periods of unemployment can erode workers' skills, making it more difficult to find a comparable job. Once they do find a job, their wages are typically lower than before. A growing body of research, including a 2013 Urban Institute study, also points to potential negative effects on mental health and family stability.

THE STATE OF

UNEMPLOYMENT

STATE-LEVEL UNEMPLOYMENT RATES

December 2013



CITIES WITH BIGGEST CHANGES IN **UNEMPLOYMENT**

PERCENTAGE POINT CHANGE, DECEMBER 2012 TO DECEMBER 2013

THERE WERE

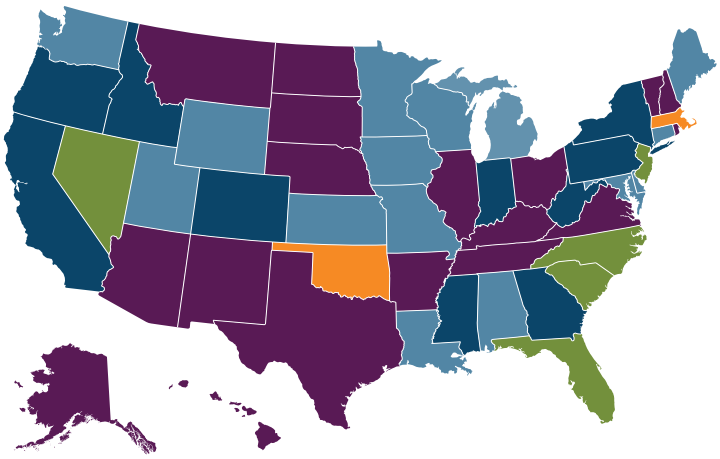
10.4

MILLION PEOPLE UNEMPLOYED

AS OF DECEMBER 2013

CHANGE IN UNEMPLOYMENT RATE

Percentage point change, December 2012 to December 2013



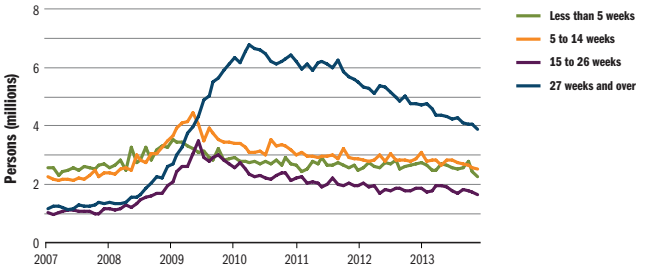
DATA FROM U.S. BUREAU OF LABOR STATISTICS

OTHER LABOR
MARKET INDICATORS

"It's important to remember, however, that the official unemployment rate and the monthly payroll jobs growth number don't represent a complete picture of labor market conditions."

—Dennis Lockhart, June 2013 speech

UNEMPLOYMENT BY DURATION



Sources: U.S. Bureau of Labor Statistics, Haver Analytics

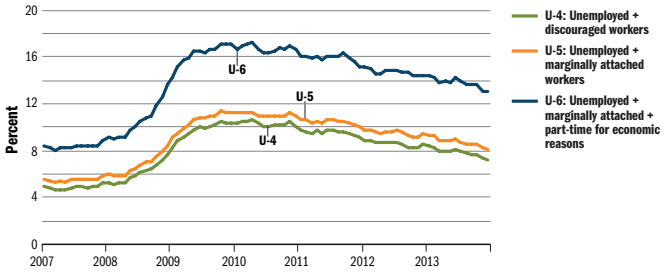
37.1 WEEKS AVERAGE DURATION OF UNEMPLOYMENT IN DECEMBER 2013

16.6 WEEKS AVERAGE DURATION OF UNEMPLOYMENT IN DECEMBER 2007

7.8 MILLION PEOPLE WORKING PART-TIME FOR ECONOMIC REASONS IN DECEMBER 2013

2.6 JOB SEEKERS FOR EVERY JOB OPENING
December 2013

ALTERNATE MEASURES OF UNEMPLOYMENT



Sources: U.S. Bureau of Labor Statistics, Haver Analytics

MILLIONS HAVE LEFT THE LABOR FORCE FOR VARIED AND COMPLEX REASONS

The unemployment rate not only reflects the number of people who say they looked for and couldn't find work, but also people's decision to look for work in the first place. Participation in the labor market has been declining in recent years for reasons that are not totally understood.

The labor force participation rate has been falling since the early 2000s, and that trend has accelerated since 2007. Between 2000 and 2007, the participation rate declined by about 1 percentage point. It dropped by another percentage point between 2007 and 2009, and by a further 2 percentage points since then. By the end of 2013, labor force participation reached the lowest level since the late 1970s.

The health of the labor market clearly affects individuals' decisions to enroll in school, apply for disability insurance, or stay home and take care of family. Discouragement over job prospects rose during the Great Recession, causing many unemployed people to drop out of the labor force. The rise in the number of marginally attached workers reflects this and can account for some of the decline in participation between 2007 and 2009.

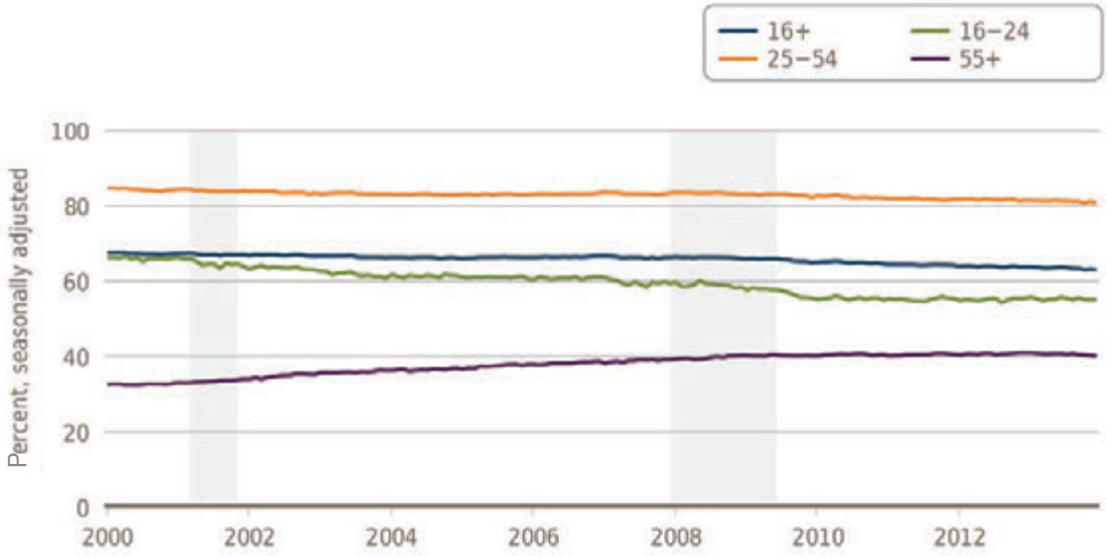
Discouragement may be a factor even when people say they don't currently want a job. The share of people aged 25–54 who said they didn't currently want a job remained relatively stable between 2002 and 2009, but has risen by almost 2 percentage points since then. It seems likely that some of the recent increase is associated with a rise in discouragement over job prospects.

However, the labor force participation rate can decline for other reasons. The most important of these is the aging population. For example, the share of the population aged 55 and older has risen by almost 4 percentage points since 2007. Because this age group also has a relatively low rate of labor force participation (because of higher levels of retirement and disability), the aging of the population is putting significant downward pressure on overall labor force participation.

Most research, including work done at the Atlanta Fed, suggests that about half of the decline in labor force participation since 2007 can be attributed to the ongoing compositional changes of the U.S. population. The rest is the result of declines in participation within demographic groups, especially by young people but also by men and women aged 25–54.

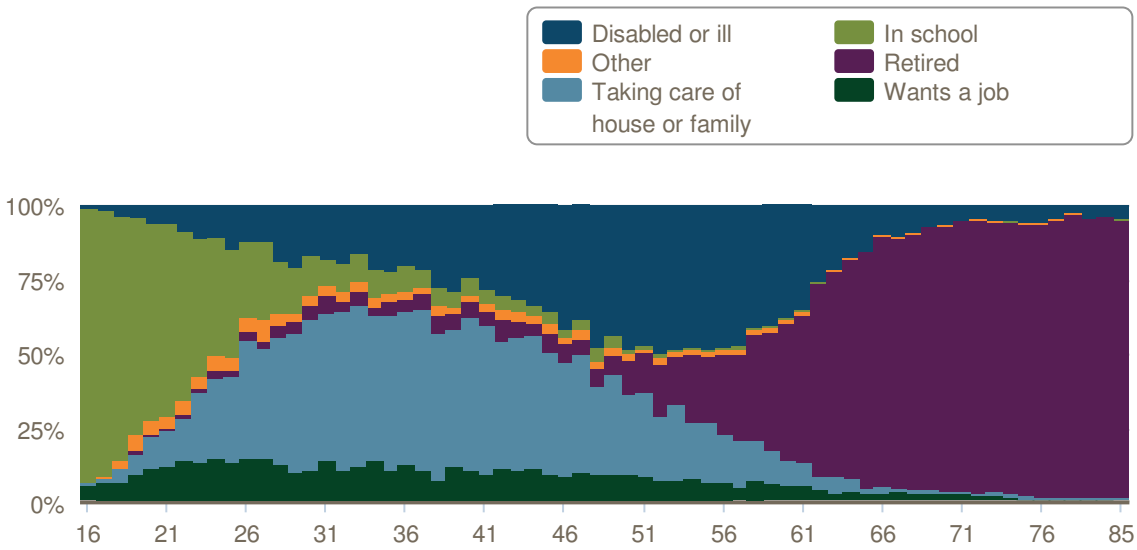
How much do these trends reflect changes over time, and how much can they be attributed to the recession and slow recovery? It's hard to say with certainty. For example, young people have been enrolling in school in larger numbers since the late 1980s, but enrollments accelerated somewhat after 2007. Some people will reenter the labor market as it strengthens. But for others, the prospect of not finding a satisfactory job will cause them to continue to stay out of the labor market. Overall, labor force participation is expected to edge down slightly more over the next few years. The effect of the ongoing aging of the population will dominate, only partially offset by upward pressure from improving employment prospects.

LABOR FORCE PARTICIPATION RATE, BY AGE



Source: U.S. Bureau of Labor Statistics

REASONS FOR BEING OUT OF THE LABOR FORCE, BY AGE



Sources: Current Population Survey, U.S. Census Bureau, and author's calculations

UNLIKE IN RECENT RECOVERIES, THE SOUTHEAST LAGS THE NATION

Employment in the Southeast declined more and recovered more slowly after the end of the Great Recession than in the nation as a whole. The second half of 2013 brought progress, as the region's two largest states—Florida and Georgia—led steady employment gains across the region.

Still, the Southeast ended the year with fewer jobs than it had before the recession. And the Southeast's labor market had more ground to make up than the national jobs market did. As 2014 began, the country had regained nearly 90 percent of lost jobs; the Southeast had reclaimed only 64 percent.

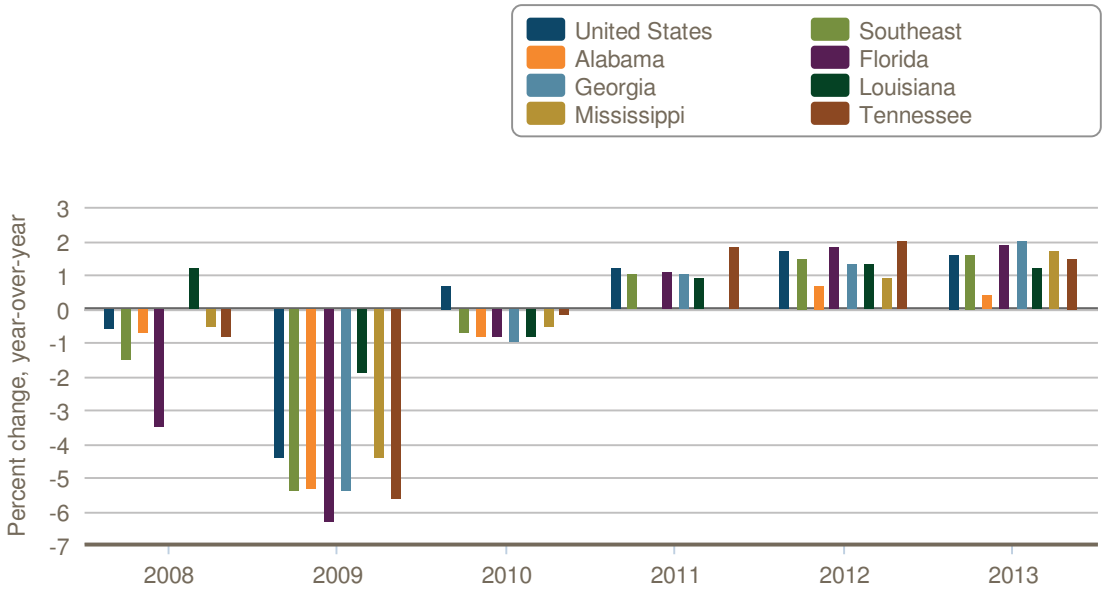
The region's labor market was weaker by other measures as well. At the end of 2013, the labor force participation rates in all six southeastern states were below the national rate of 63 percent. Broader measures of unemployment were also worse in most of the region. For example, only Alabama and Louisiana posted lower average U-6 unemployment rates than the country as a whole throughout 2013.

This recovery has been different. The Southeast weathered the downturns of the early 1990s and 2001 comparatively well, losing a smaller portion of jobs and recovering those jobs more quickly than the nation. Steady in-migration in the 1990s and early 2000s strengthened the southeastern economy and labor market. Population growth fueled housing construction, commercial real estate development, and related industries, generating large numbers of jobs.

But the Great Recession hit the Southeast's building sector especially hard. Florida alone lost more than half of its construction jobs, and a vast majority of those losses have not been recouped. Manufacturing was another sector in which the Southeast suffered severe employment declines. In fact, job losses in the construction and manufacturing sectors accounted for nearly the entire gap between the Southeast's nonfarm employment at the end of 2013 and the prerecession peak during 2007.

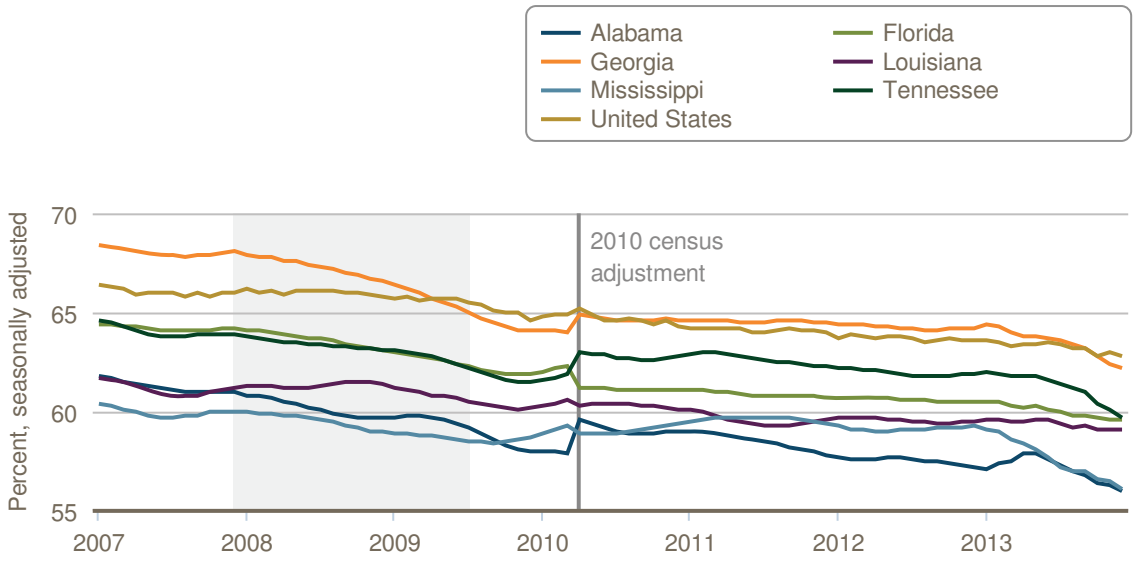
Those two sectors added jobs during 2013. Among the major economic sectors, only government did not add jobs last year. Meanwhile, the aggregate unemployment rate for the region ended the year at 6.7 percent, down from 7.8 percent a year earlier and well below the peak of 10.5 percent in January 2010.

EMPLOYMENT IN THE SOUTHEAST



Source: U.S. Bureau of Labor Statistics

SOUTHEASTERN LABOR FORCE PARTICIPATION



Source: U.S. Bureau of Labor Statistics

WHAT'S HOLDING BACK JOB GROWTH?

POLARIZATION-OFFSHORING

While it's clear that polarization in the labor market has occurred over the decades, it's not clear whether it accelerated during the Great Recession.

PAGE 20

SKILLS MISMATCH

Skills mismatch may be part of the story for the slow job growth that the economy has experienced, but it's not the full story.

PAGE 22

General economic weakness in the wake of a severe financial crisis is perhaps the biggest reason the labor market has not rebounded more quickly. Yet there is no single, simple answer to this question. We examine a few of the particular forces that continued to limit employment growth during 2013.

DYNAMISM & SMALL BUSINESS

The Atlanta Fed has investigated trends in a variety of firm types to better understand why labor market progress continued to be slow in 2013.

PAGE 23

UNCERTAINTY

The past several years have been marked by high levels of policy-related uncertainty. How has this affected the economy?

PAGE 26

ARE JOBS GOING OVERSEAS FASTER?

Since the 1990s, corporations have moved large numbers of jobs, especially in manufacturing, out of the United States to countries with lower labor costs. Yet that fact itself does not mean that offshoring results in no additional job creation here in the United States.

In fact, Atlanta Fed economists have looked at the net effect of offshoring and found evidence of some countervailing job creation that occurs as a result. For instance, when a manufacturer of hand-held electronic devices sends its manufacturing overseas, that might increase the overall competitiveness of the firm, pointed out Atlanta Fed research economist Federico Mandelman. Consequently, the firm could hire more higher-wage domestic workers such as marketers or product designers.

A paper prepared for a 2010 Atlanta Fed conference on immigration concluded that offshoring has little or no effect on domestic employment. "Increased offshoring reduces the share of native employment in an industry while...stimulating overall industry employment via the productivity effect such that offshoring has no aggregate impact on the level of native employment," wrote the economists Gianmarco Ottaviano, Giovanni Peri, and Greg Wright.

Labor market polarization has hollowed out middle of jobs spectrum

The U.S. labor market has become polarized over the past three decades: employment growth has been strong for both high- and low-skill occupations, while jobs for middle-skilled workers have disappeared. Real wages have followed a different pattern. Wages for high-skill occupations have increased; earnings of low- and middle-skilled workers generally have not.

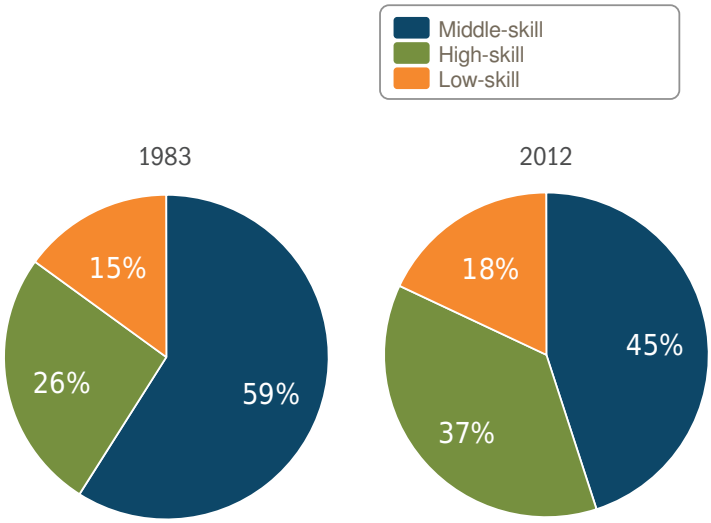
Along with technological change and immigration of low-skilled workers, offshoring appears to be a significant factor in labor market polarization, Mandelman has found. Jobs done by middle-skilled workers are the jobs that are typically offshored. In addition, research shows that the weakening of labor unions over time may have contributed to the decline of middle-skill jobs.

Labor market polarization has been associated with job losses in occupations that involve routine tasks, which are typically found in the middle of the skill distribution. Routine occupations include blue-collar manufacturing jobs and office and administrative support. These workers tend to follow well-defined procedures that can be coded in computer software, executed by machines, moved to lower-wage countries, or assumed by immigrants who will generally work for lower wages than native workers.

It's clear that labor market polarization has occurred over decades. But economists debate whether and how much polarization accelerated during the Great Recession and other downturns. Researchers at the Kansas City Fed concluded in a 2013 paper that while labor market polarization is a long-term phenomenon affecting all economic sectors, it intensifies during recessions. The rapid pace of polarization during recessions, according to the research, stems from the decline in the share of middle-skill occupations in manufacturing and, to a lesser extent, in construction.

MIDDLE-SKILL JOBS IN DECLINE

Percentage of nonfarm, civilian workers aged 16–64 who are not self-employed



Sources: Census data and calculations of Didem Tüzemen and Jonathan Willis, Kansas City Fed

SKILLS MISMATCH A FACTOR IN LABOR MARKET WOES

Skills mismatch, the situation in which workers lack the skills that employers need, appears to account for some of the rise in unemployment during the Great Recession.

Joblessness caused by skills mismatch can arise as the result of an economic downturn when job losses are concentrated in certain industries but job openings are in other industries. Between 2007 and 2013, about half of all jobs lost were in manufacturing and construction, while roughly 90 percent of new positions opened in other industries, according to the U.S. Bureau of Labor Statistics. That disparity suggests that "sectoral mismatch" may have increased. This sectoral imbalance of job losses and job openings held true in the Southeast as well as the nation.

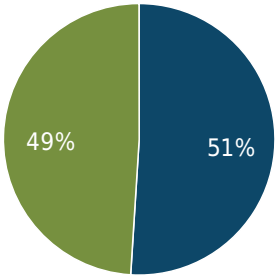
Skills mismatch is a real issue. However, the evidence is not conclusive on the degree to which higher joblessness during 2013 was caused primarily by persistent mismatch between available jobs and the skills of people seeking to fill them. Unemployment declined through the year roughly in proportion to the increase in job openings, which might suggest that more vacancies will absorb more job seekers. On the other hand, an Atlanta Fed poll of employers and providers of training and social services to low-wage earners in the Southeast revealed that lack of technical skills and lack of experience were the two biggest hurdles to low-wage individuals seeking jobs. On balance, though, it appears that skills mismatch may be part of the story for the less-than-desirable job growth the economy has experienced—but it's far from the full story.

The mismatch can also partly explain why there is an unusually large share of unemployed individuals who have been unemployed for a long time.

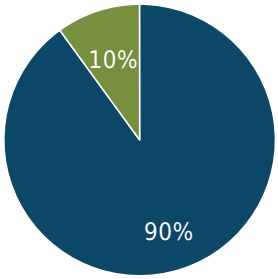
JOBS MISMATCH

Share of total jobs lost: 12/2007-02/2010

Share of total jobs lost: 12/2007-02/2010



Share of job openings: 03/2010-10/2013

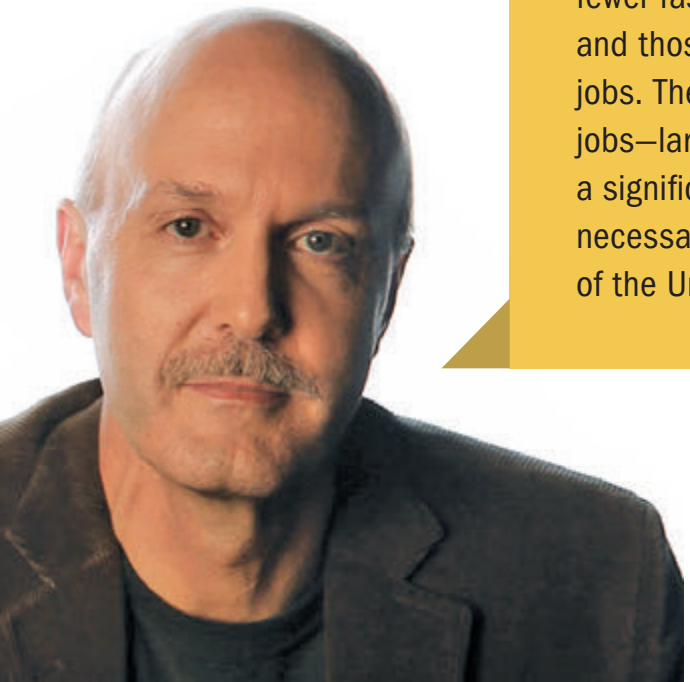


Note: February 2010 was the low point of U.S. nonfarm employment.
Source: U.S. Bureau of Labor Statistics Job Openings and Labor Turnover Survey

WHO OR WHAT CREATES THE JOBS?

Coming out of the Great Recession, one of the puzzles is, why has job creation not picked up? The Atlanta Fed recently completed a study that looked at the properties of fast-growing firms in Georgia. That study found that half of fast-growing firms could be categorized as gazelles—they were young fast-growing businesses. Turns out that older fast-growing firms actually contribute more to job creation than these young gazelle businesses.

There is evidence in the data to suggest that the dynamism of the U.S. economy has slowed over the last couple of decades. We still see fast-growing businesses, but we see fewer fast-growing businesses than we have in the past, and those fast-growing businesses are actually adding fewer jobs. The diversity of the types of businesses that create jobs—large firms, small firms, young firms, old firms—creates a significant economic policy challenge. No single policy is necessarily going to be effective in solving the jobs problem of the United States.



JOHN ROBERTSON
Vice President and Senior Economist

WHO OR WHAT CREATES THE JOBS?

A striking feature of the Great Recession was not so much the rise in the number of firms cutting their payrolls—that always happens in recessions. What was unprecedented was the dramatic collapse in the number of firms that expanded. Early in the recovery, firms continued to have the lowest rate of job creation on record, and fewer new firms were created in 2009 and 2010 than in any other time in the previous 30 years. Although the unemployment rate fell faster than expected in the latter part of 2013—roughly four-and-a-half years into the recovery—hiring rates at firms were still relatively subdued.

The Atlanta Fed has investigated trends in a variety of firm types to better understand why labor market progress continued to be slower than hoped for in 2013. Researchers started by looking at small firms, since their economic struggles are often singled out as a major reason why the U.S. jobs engine has faltered. These researchers found that all businesses were hit hard by the recession. They looked at firms across a variety of dimensions—age, size, industry, and location—to determine where the jobs are.

Small firms versus large firms

Most businesses are small. Almost 96 percent (or 4.7 million) of firms had payrolls with fewer than 50 people in 2011 (the latest census data available). These firms accounted for 28 percent of all payroll jobs. They also create many new jobs—about 40 percent of new jobs each year, on average. However, the rate of gross job gains fell sharply for small firms during the recession and recovery, in part because fewer new firms were created but also because small firms sharply curtailed hiring as heightened uncertainty and a weak economy made them more hesitant to expand.

Large firms are also an important source of new jobs. The largest 1 percent of firms account for about as many new jobs each year as do all the firms with fewer than 50 employees. But large firms have also been creating jobs at an unusually slow pace.

New firms versus young firms

Start-ups gained a lot of attention in the aftermath of the recession, in part because of the dramatic decline in new business formation. These new firms are also important because they create an outsized share of new jobs. In 2011, 8 percent of firms were new—most of them were very small—and they contributed about 16 percent (or 2.5 million) of new jobs that year. But having a continual flow of new firms each year is important because the jobs that start-ups create can be fleeting. Indeed, more than half of young firms typically fail within their first five years of operation.

Gazelles versus gorillas

Although many firms fail in their early years, a small fraction of young firms grow very rapidly. These so-called gazelle businesses are also a significant source of job creation. A recent Atlanta Fed study looked at the properties of fast-growing Georgia firms during the 2000s and found that about half of the firms that had a high rate of employment growth were young. However, more jobs were generated by older, generally larger, fast-growing firms, sometimes called gorillas. On a national level, high-growth firms have declined as a share of all firms, from 3 percent in the late 1990s to 1.5 percent in 2011. During the same time, these fast-growing firms added fewer jobs, falling from 45 percent of jobs created at expanding firms to 34 percent.

While data on these and other characteristics provide a window into the types of firms that typically create jobs, they also underscore the fact that when it comes to job creation, there is no simple solution.

WHERE DO

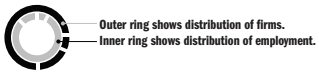
JOBS COME FROM?

Where are the jobs? Which types of companies create the most jobs? Researchers have studied firms across a variety of dimensions looking for the answers to these questions. What they've found is that when it comes to job creation, there's no simple solution.

FIRM SIZE

- 1–9
- 10–19
- 20–49
- 50–249
- 250+

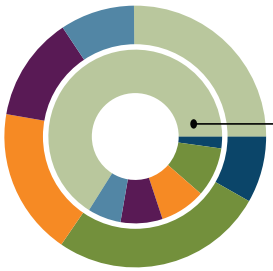
57 PERCENT
OF EMPLOYMENT IS AT FIRMS WITH MORE THAN 250 EMPLOYEES, EVEN THOUGH THOSE FIRMS ARE FEWER THAN 1 PERCENT OF ALL FIRMS!



MOST FIRMS ARE VERY SMALL, BUT MOST EMPLOYEES WORK FOR A HANDFUL OF VERY LARGE (AND OLD) FIRMS.

FIRM AGE

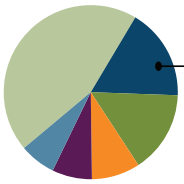
- New
- 1–5
- 6–10
- 11–15
- 16–20
- >20



66 PERCENT
OF EMPLOYMENT IS AT FIRMS OLDER THAN 20 YEARS.

JOB CREATION BY AGE

- New
- 1–5 YRS
- 6–10 YRS
- 11–15 YRS
- 16–20 YRS
- 20+ YRS

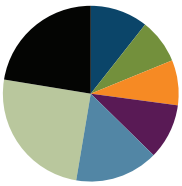


17 PERCENT
OF JOB CREATION EACH YEAR COMES FROM NEW FIRMS.

500,000
= NUMBER OF FIRMS BORN EACH YEAR.

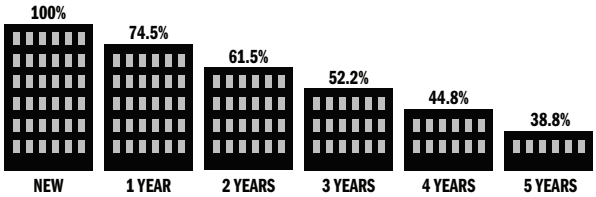
JOB CREATION BY SIZE

- 1–4
- 5–9
- 10–19
- 20–49
- 50–249
- 250–9,999
- 10,000+



FAST-GROWING YOUNG FIRMS—GAZELLES—ARE ONLY 1 PERCENT OF ALL FIRMS, BUT THEY ACCOUNT FOR ABOUT 10 PERCENT OF JOB CREATION.

AVERAGE SURVIVAL RATE OF FIRMS BY AGE OF FIRM (1983–2011)



SOURCES: U.S. CENSUS BUREAU BUSINESS DYNAMICS STATISTICS DATABASE AND DANE STANGLER, "HIGH-GROWTH FIRMS AND THE FUTURE OF THE AMERICAN ECONOMY," 2010

HAS UNCERTAINTY RESTRICTED HIRING?

Heightened uncertainty is one of several forces that weighed on the economy and hiring in 2013. Much of the uncertainty emanated from the government sector, especially regarding fiscal policy. Other factors clouded the outlook, too, including uncertainty about health care costs and the Affordable Care Act, and the economic outlook.

Although fiscal and monetary policy uncertainty seemed to ebb somewhat earlier in the year, it returned full force in the fall as the two-week federal government shutdown and the debt ceiling standoff dealt a blow to consumer and business confidence. Congress resolved the budget issue by the end of the year.

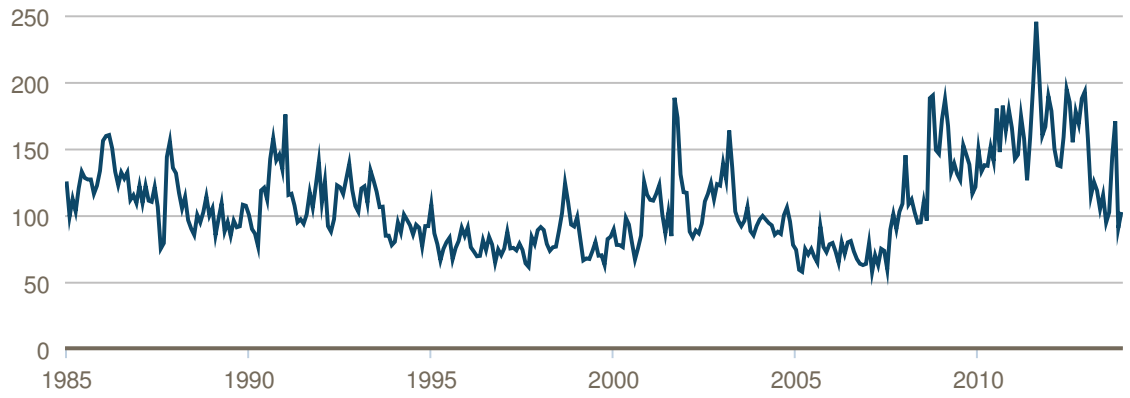
The question of how uncertainty affects the economy has been particularly relevant in the current recovery, although it has interested economists for some time. (Fed Chairman Ben Bernanke studied the topic earlier in his career.) According to a measure of economic policy uncertainty developed by economists Scott Baker, Nick Bloom, and Steven Davis, the past several years have been marked by historically high levels of policy-related uncertainty.

The crux of the problem is that firms—unsure of what lies ahead for taxes, regulations, and the economy—may delay investing and hiring. Anecdotal evidence gathered as part of the monetary policy process supports this theory. As the Federal Open Market Committee prepared to meet in October, the Beige Book noted that "employers continued to report hiring hesitancy related to changes in healthcare regulation and fiscal policy uncertainty."

The Atlanta Fed's Small Business Survey also honed in on the issue. Nearly half of respondents to the third-quarter 2013 survey reported a higher level of uncertainty relative to the first quarter. Moreover, many firms indicated that uncertainty was having a greater than usual impact on their decisions. Among them, about 20 percent expected their workforce to decrease and roughly half expected no change to their headcount.

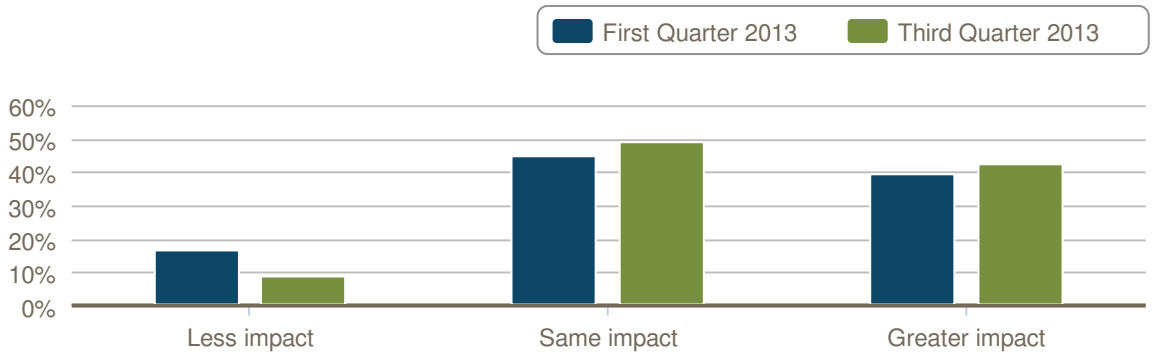
The evidence linking heightened uncertainty and sluggish economic growth is not just the anecdotal sort. An emerging body of research supports these linkages, too. Last year, a much-cited report by research firm Macroeconomic Advisers attempted to quantify the economic effect of fiscal policy uncertainty, estimating that since 2009 it has shaved 0.3 percentage point per year from U.S. GDP. In 2013 alone, fiscal policy uncertainty kept the unemployment rate higher by 0.6 percentage point—the equivalent of 900,000 jobs, the report said.

MONTHLY U.S. ECONOMIC POLICY UNCERTAINTY INDEX



Source: Scott Baker, Nicholas Bloom, and Steven J. Davis at www.PolicyUncertainty.com.

IMPACT OF UNCERTAINTY ON BUSINESS DECISIONS COMPARED TO PRIOR SIX MONTHS



Note: 268 firms participated in both surveys.

Source: Atlanta Fed Small Business Survey

HOW DO WE GET MORE JOBS?

MONETARY POLICY

With the appropriate monetary policy, the Federal Open Market Committee expected that the jobless rate would gradually decline toward levels the Committee judges consistent with its dual mandate.

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FISCAL POLICY

The good news was that the worst of the fiscal drag appeared to be over as 2013 ended. And the fiscal situations of states and municipalities generally improved.

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Stronger economic conditions, along with astute monetary and fiscal policy, can help accelerate job creation. Some of those conditions and policies are already in place. Some policies are widely accepted. Others are contentious and thus difficult to achieve.

GENERAL ECONOMIC CONDITIONS

Watching inflation and wage growth can help gauge whether the economy is gathering the underlying strength it needs to quicken the healing of the labor market.

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MONETARY POLICY IMPORTANT BUT NO PANACEA

With the federal funds rate as low as it could effectively go, the Federal Open Market Committee (FOMC) used two unconventional policy tools in 2013: forward guidance about the expected path of the federal funds rate and large-scale asset purchases (often called quantitative easing, or QE), at a pace of $85 billion per month. Both tools aimed to push down longer-term interest rates to spur households and businesses to borrow, spend, and invest—in turn, triggering a virtuous cycle that would include increased production, hiring, and more spending.

The FOMC conditioned the duration of the QE program on achieving substantial improvement in the outlook for labor markets. By the end of 2013, the unemployment situation had improved enough that the Committee voted to reduce its purchases by $10 billion per month, thus beginning the much-anticipated "tapering" process.

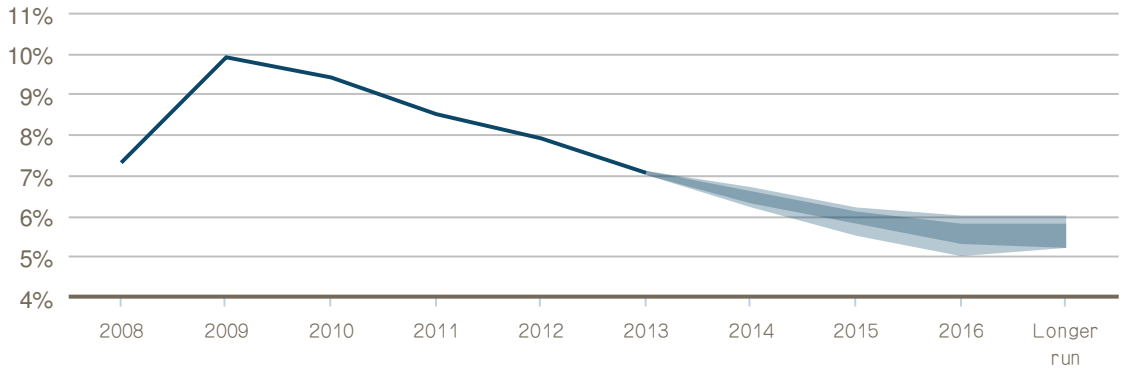
With that transition under way, the key monetary policy question for the Fed is how long to keep the fed funds rate at zero. Throughout 2013, FOMC members continued to anticipate that the fed funds rate would stay put at least until the unemployment rate falls below 6.5 percent. In the statement following its December meeting, the Committee also noted that the near-zero rate would likely be appropriate "well past" the 6.5 percent threshold, especially if annual inflation continues to look like it will fall short of the Committee's longer-run objective of 2 percent.

Is it working?

It's difficult to isolate precisely the effects of the Fed's monetary stimulus, in part because the linkages between policy and employment are indirect. However, recent research suggests that monetary policy has helped push down interest rates and boost asset prices. And as Atlanta Fed President Dennis Lockhart noted in a February 2013 speech, the Fed's monetary stimulus has "without question helped achieve the economic progress we've made since the end of the recession."

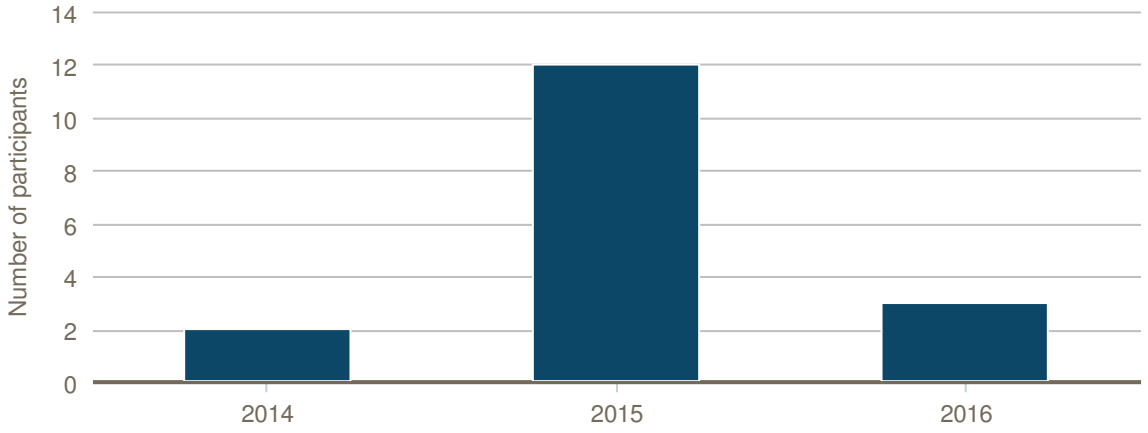
The economy has recovered considerably, but the job is not done. The jobless rate, at 6.7 percent in December, remained well above FOMC members' projections for the longer-run rate of unemployment, which ranged from 5.2 to 5.8 percent. Obviously, there's still work to do. But with the appropriate monetary policy, the FOMC in December expected that the jobless rate would gradually decline toward levels the Committee judges consistent with its dual mandate.

FOMC PROJECTIONS OF UNEMPLOYMENT RATE



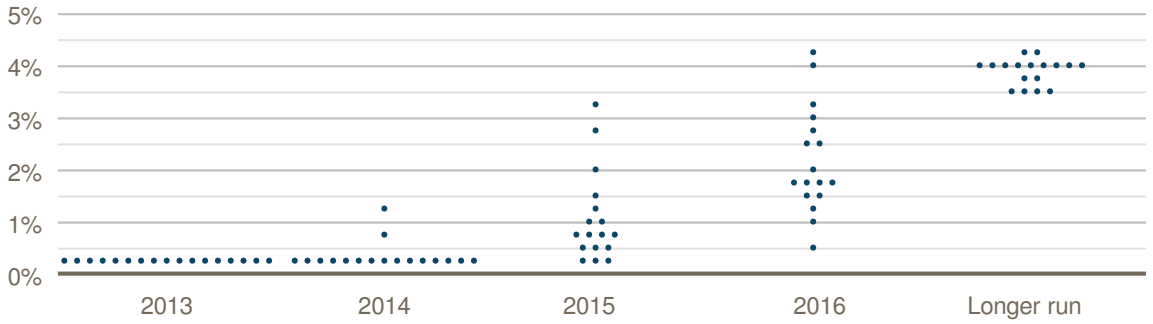
Note: Definitions of variables are in the general note to the projections table. The data for the actual values of the variables are annual.
Source: Summary of Economic Projections, Board of Governors

APPROPRIATE TIMING OF POLICY FIRMING



Note: The height of each bar denotes the number of FOMC participants who judge that, under appropriate monetary policy, the first increase in the target federal funds rate from its current range of 0 to 1/4 percent will occur in the specified calendar year.
Source: Federal Reserve Board of Governors

TARGET FEDERAL FUNDS RATE AT YEAR-END



Note: Each shaded circle indicates the value (rounded to the nearest 1/4 percentage point) of an individual participant's judgment of the appropriate level of the target federal funds rate at the end of the specified calendar year or over the longer run.
Source: Federal Reserve Board of Governors

"FISCAL DRAG" DISSIPATED LATE IN 2013

The executive and legislative branches of government control federal taxation and spending. But the Federal Reserve pays close attention to fiscal policy because it influences the economy and labor market.

Without advocating particular positions, it is possible to identify general fiscal conditions that would promote the ongoing recovery of the labor market. As Atlanta Fed President Dennis Lockhart explained in a September 2013 speech, public policy can foster economic dynamism "by removing obstacles to growth and entrepreneurship and contributing pro-growth actions that address investment in human capital and productive infrastructure."

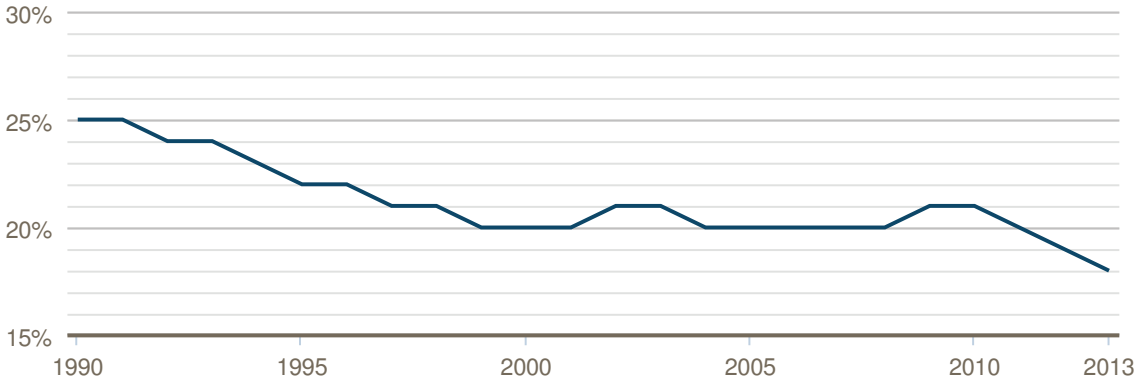
It is important for elected officials to set fiscal policy on a sustainable long-term path. Establishing a course on which the ratio of federal debt to gross domestic product (GDP) eventually stabilizes or declines is critical to ensure longer-run economic growth and stability, Lockhart pointed out. Yet even as policymakers address longer-range fiscal sustainability, they should avoid unnecessarily adding to forces that are slowing the economic recovery.

Those forces in 2013 included a "fiscal drag" consisting of the effects of tax increases early in the year, reduced spending, the partial federal government shutdown, and the impact of fiscal policy uncertainty on business investment and consumer spending.

The Congressional Budget Office (CBO) estimated that federal spending cuts lowered employment by between 300,000 and 1.6 million jobs. Meanwhile, the partial shutdown of the federal government in October reduced fourth-quarter GDP by an estimated 0.25 to 0.5 percentage point. In total, cuts in government spending and tax increases likely lowered economic growth in 2013 by as much as 1.5 percentage points, according to the CBO.

The good news: the worst of the fiscal drag appeared to be over as 2013 ended. In December, Congress reached a budget compromise and in January 2014 passed a comprehensive spending bill. Further, the fiscal situations of states and municipalities generally improved during 2013, likely reducing the need for further cuts in employment and investment.

GOVERNMENT SPENDING AS SHARE OF GDP



Note: Includes federal, state, and local governments.
Source: U.S. Bureau of Economic Analysis

A HEALTHY ECONOMY IS THE BEST MEDICINE FOR THE LABOR MARKET

In large part, the conditions that characterize a generally healthy economy are the same conditions that will encourage increased hiring.

The second half of 2013 brought promising signs on both fronts. Overall economic growth, as measured by the gross domestic product (GDP), improved significantly in the third and fourth quarters compared to the previous three quarters. In the first half of 2013, real GDP—adjusted for inflation—expanded at a rate of 1.8 percent annualized, slower than the average during the recovery from the Great Recession. Growth then accelerated to an estimated annual pace of 3.3 percent in the second half of the year.

Some of the strength in the second half resulted from the buildup of inventory, which can't go on indefinitely. But the economy also exhibited renewed strength in consumer spending, business spending on equipment, and exports—which suggests rising confidence about future prospects for the economy. Anecdotal evidence from business contacts in the Southeast also indicated solid confidence.

Brighter sentiment and stronger consumer spending bode well for the labor market. What's more, these two factors—business confidence and consumption—feed off each other. If people running firms believe demand for their products and services is sufficiently strong, then they are more likely to invest in people through hiring. Likewise, better job prospects, along with rising stock and home prices, should fuel more consumer spending.

As 2013 ended, it was premature to declare the start of such a virtuous cycle. Moreover, it is almost always difficult to discern the precise state of the economy, as incoming data are rarely unambiguously positive or negative. For example, because of declining labor force participation, the unemployment rate has been particularly difficult to read during the recovery. And month-to-month reports of employment growth can fluctuate dramatically. In such circumstances, measures of inflation can be especially helpful. In general, weak overall demand is associated with weak prices. Therefore, watching inflation and wage growth can help gauge whether the economy is gathering the underlying strength it needs to quicken the healing of the labor market.

Economic performance in the latter part of 2013 suggested glad tidings. If that pace of growth persists—thus signaling the long-awaited acceleration in the economic expansion—then better labor market conditions should follow.

Asking the question of what conditions need to be in place for employment growth is the same thing as asking the question about what conditions need to be in place for growth in general. That is, businesses have to have confidence in the fact that they're going to be able to make profits, which means they have to be confident that the demand will be there when they produce.

Monetary policy has an important role to play in supporting economic growth and employment growth. The Federal Open Market Committee [FOMC]—the decision-making branch of the Federal Reserve—has decided that it's going to keep in place the policy of accommodation—that is to say, really low interest rates—for some period of time to support exactly that growth in both jobs and in overall economic activity.

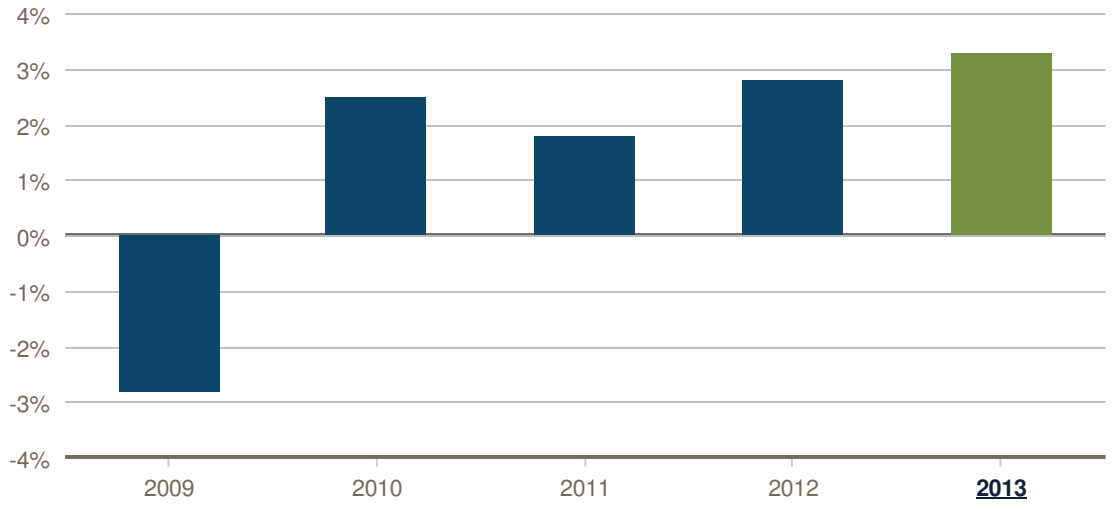
There's a lot of debate about how much of the employment picture is about structural developments—that is, things that monetary policy really can't fix—versus cyclical elements that have to do with not enough spending in the economy, for example. Monetary policy can do a lot about the spending side of the picture, and really, what we need to know is how much of the problem is associated with those demand-type problems.

How will we know when we've met our employment goal? Well, that's a tricky question, but interestingly, our second goal—our inflation goal—will help us know that. In an economy that's weaker than it should be, the rate of inflation is likely to be below the 2 percent target that the FOMC has set. So by keeping our eye on the inflation goal, we are also keeping our eye on the employment goal.

The conditions for a pickup in employment growth appear to be with us today. We ended the year with substantial momentum that ought to take us into 2014. So not only will 2014 be a year of better GDP [gross domestic product] growth, but hopefully of better employment growth as well.

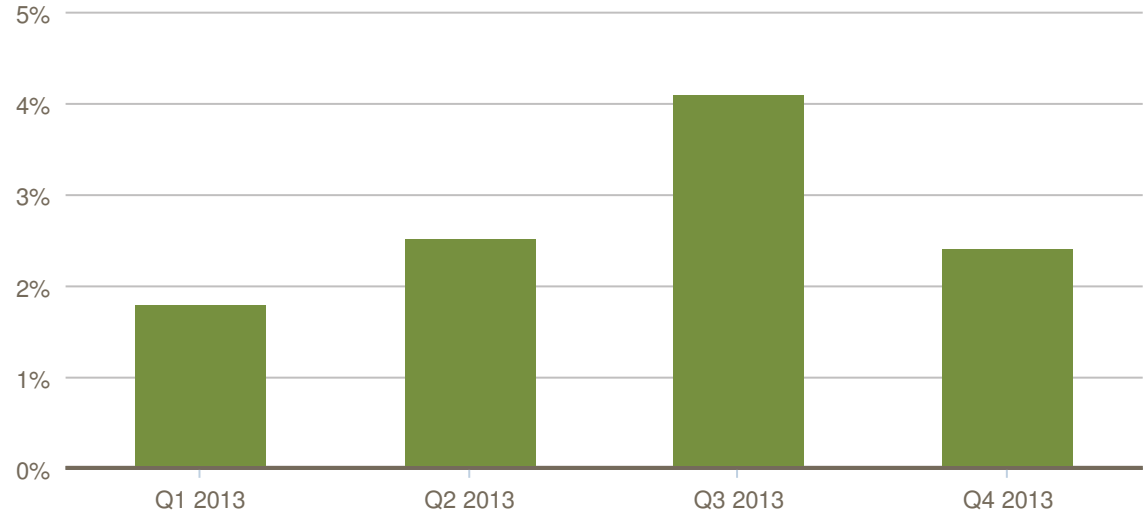
DAVE ALTIG
Executive Vice President
and Director of Research

GDP GROWTH



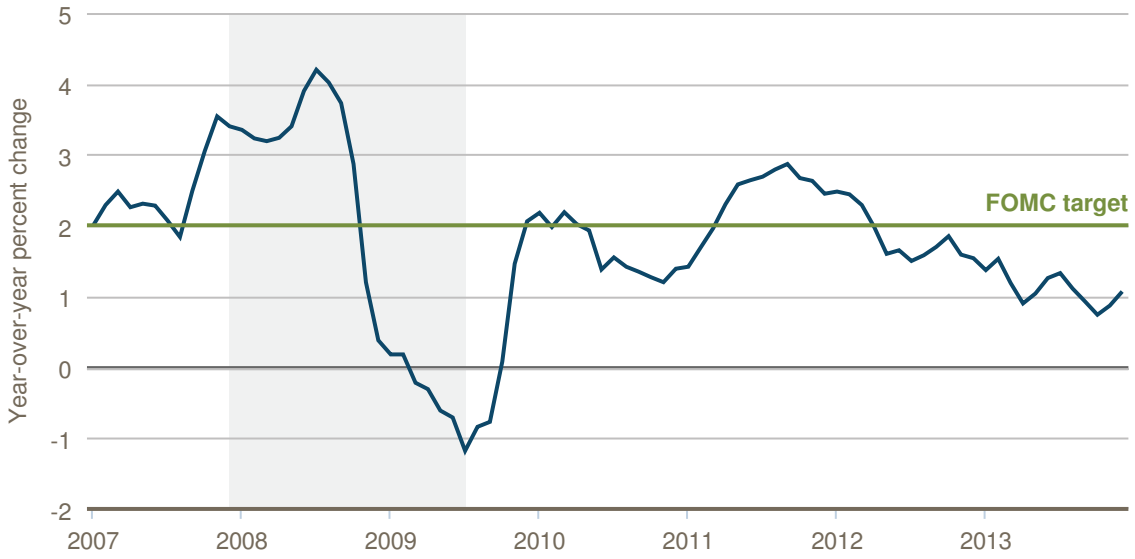
Source: U.S. Bureau of Economic Analysis

GDP GROWTH IN 2013



Source: U.S. Bureau of Economic Analysis

INFLATION: PERSONAL CONSUMPTION EXPENDITURES INDEX



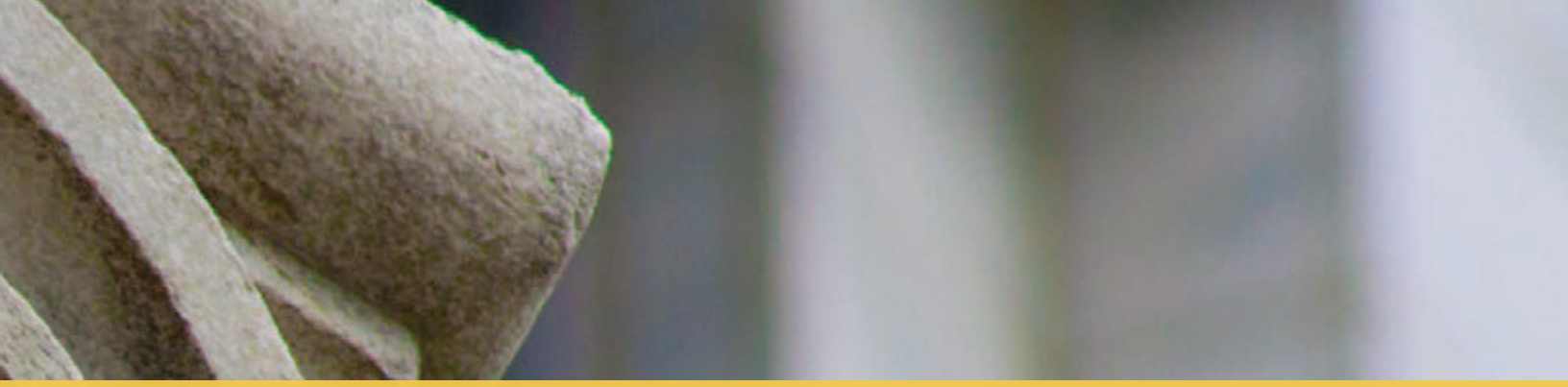
Source: U.S. Bureau of Economic Analysis

FEDERAL RESERVE BANK OF ATLANTA BOARDS OF DIRECTORS

Federal Reserve Banks each have a board of nine directors. Directors provide economic information, have broad oversight responsibility for their bank's operations, and, with the Board of Governors approval, appoint the bank's president and first vice president.

Six directors—three class A, representing the banking industry, and three class B—are elected by banks that are members of the Federal Reserve System. Three class C directors (including the chair and deputy chair) are appointed by the Board of Governors. Class B and C directors represent agriculture, commerce, industry, labor, and consumers in the district; they cannot be officers, directors, or employees of a bank; class C directors cannot be bank stockholders.

Fed branch office boards have five or seven directors; the majority are appointed by head-office directors and the rest by the Board of Governors.



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FEDERAL RESERVE BANK OF ATLANTA MILESTONES

RESEARCH / MONETARY POLICY

Atlanta Fed economists published research on myriad topics such as commodity prices, links between land prices and unemployment, household employment status and the likelihood of mortgage default, the economic consequences of cigarette smoking, and the benefits of social insurance programs.

The Atlanta Fed held a half dozen major research and policy conferences on topics including financial stability, monetary and financial history, labor market developments and policy responses, central bank business surveys, and the use of extremely detailed Census Bureau data in research.

The Bank launched a lecture series on real estate. Guest speakers included experts from the Federal Reserve Board of Governors and the Joint Center for Housing Studies at Harvard University.

Community and Economic Development discussion papers explored community resilience to disasters and whether locally owned businesses affect the health of local economies.

Atlanta Fed researchers tracked municipal and state budgetary issues, including high-profile municipal bankruptcies and their effects on financial stability.

The Community and Economic Development group convened presidents of historically black colleges and universities (HBCUs) and workforce development experts to discuss opportunities and issues HBCUs face in preparing students for the fast-changing labor market.

The Atlanta Fed's Regional Economic Information Network (REIN) gathered economic intelligence from southeastern business leaders and other sources in the region to inform monetary policymaking.

SUPERVISION AND REGULATION

The Atlanta Fed Supervision and Regulation division's annual Banking Outlook Conference in February assembled more than 200 bankers and regulators to address issues affecting financial institutions and the nation's financial system. They discussed topics that included concerns facing southeastern banks, regulatory matters, cyberthreats, and the impact of technology on banks and their customers.

The division led the Federal Reserve System's 2013 implementation of the Capital Plan Review for institutions with more than $50 billion in assets that were not among the nation's 19 largest banking companies.

Bank performance in the Southeast continued to improve during 2013. Only about 10 percent of the region's commercial banks were unprofitable, compared to more than 40 percent during the worst of the 2007–08 financial crisis.

The Supervision and Regulation division helped review and analyze the capital adequacy of the nation's largest financial institutions, including two institutions headquartered in the Southeast.

RETAIL PAYMENTS OFFICE / PAYMENTS

Cash Services operations met all cost recovery targets and continued to rank among the top tier of Reserve Banks' cash operations.

Officials from the Central Bank of Nigeria visited the Atlanta Fed to study the U.S. payments system as they seek to transform their country's payments infrastructure.

Under Atlanta Fed leadership, the Federal Reserve System's check and ACH services nationwide surpassed cost recovery targets in all retail payments processing operations.

The RPO improved efficiencies in check operations through the transition of all Treasury-item processing to a new technology platform. This centralized platform helped reduce Federal Reserve System costs to the U.S. Treasury by $1.7 million for Treasury check and postal money order processing.

The Retail Payments Risk Forum cohosted conferences on the nation's fast-changing payments system. Conferences explored payments risk management for financial institutions and the challenges and solutions involved in creating a more efficient, secure remote payment system.

EDUCATION AND PUBLIC OUTREACH

Atlanta Fed President and Chief Executive Dennis Lockhart delivered nearly two dozen speeches in 2013. Major themes included numerous aspects of employment and the challenges facing the recovering labor market, the dynamism of the U.S. economy, the impact of fiscal policy uncertainty, the economic outlook, and monetary policy response to economic and financial conditions.

Atlanta Fed forums featured renowned speakers on topics including the changing economics of higher education, global economic issues, and the ongoing loss of Louisiana's wetlands.

The Atlanta Fed launched ECONversations, a webcast series in which Fed experts discuss economic issues with bankers. The webcasts are held twice a year.

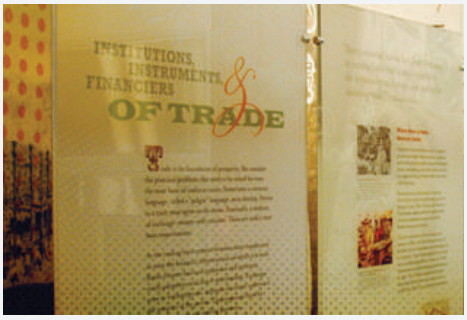
EDUCATION AND PUBLIC OUTREACH

The Atlanta Fed and the Federal Reserve System prepared to mark the central bank's centennial in 2014, with exhibits, speaking engagements, publications, and other events.

The Economic Education Team conducted 180 workshops, which reached 5,358 teachers, who in turn reached an estimated 401,850 students. The team made an additional 146 presentations at teacher workdays and conferences, reaching more than 6,000 teachers. Roughly 51 percent of the Atlanta Fed's financial literacy and financial education programming was consumed online during 2013.

The travel website TripAdvisor awarded its Certificate of Excellence to the Atlanta Fed Monetary Museum in Atlanta. The museum attracted nearly 13,000 visitors in 2013.

The Atlanta Fed opened the Museum of Trade, Finance, and the Fed at the New Orleans Branch. Exhibits highlight the city's evolution into a bustling trade and financial center.



The Atlanta Fed hosted two banker outreach forums. The sessions in Tampa and Birmingham assembled more than 100 senior bankers for candid conversation with Atlanta Fed officials about the evolving business of banking and the financial regulatory landscape.

CORPORATE CITIZENSHIP

The Atlanta Fed headquarters won a widely recognized certification for sustainability in building operations. The building earned LEED, or Leadership in Energy and Environmental Design, Existing Buildings Operations and Maintenance Gold level certification from the U.S. Green Building Council.

The Atlanta Fed was named one of America's Top Workplaces by Workplace Dynamics.

Forty-six percent of Atlanta Fed employees volunteered through workplace-based programs, contributing more than 5,100 hours to charities throughout the Southeast.

Forty-five employees served on the boards of directors of 98 nonprofit agencies, most of them focused on education, workforce development, and community building.

2014

FEDERAL RESERVE BANK OF ATLANTA 2013 AUDIT STATEMENT

The Board of Governors engaged Deloitte & Touche LLP (D&T) to audit the 2013 combined and individual financial statements of the Reserve Banks and those of the consolidated LLC entities.[1] In 2013, D&T also conducted audits of internal controls over financial reporting for each of the Reserve Banks. Fees for D&T's services totaled $7 million, of which $1 million was for the audits of the consolidated LLC entities. To ensure auditor independence, the Board requires that D&T be independent in all matters relating to the audits. Specifically, D&T may not perform services for the Reserve Banks or others that would place it in a position of auditing its own work, making management decisions on behalf of the Reserve Banks, or in any other way impairing its audit independence. In 2013, the Bank did not engage D&T for any non-audit services.

[1] In addition, D&T audited the Office of Employee Benefits of the Federal Reserve System (OEB), the Retirement Plan for Employees of the Federal Reserve System (System Plan), and the Thrift Plan for Employees of the Federal Reserve System (Thrift Plan). The System Plan and the Thrift Plan provide retirement benefits to employees of the Board, the Federal Reserve Banks, and the OEB.

FEDERAL RESERVE BANK *of* ATLANTA

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