California Has Highest State Unemployment Rate (5.3%), Inland Empire: 5.4%. Are We the Biggest Losers?

by

Manfred Keil and Ethan Sattley[1]

Our great state has seen some negative headlines lately: we will lose a Congressional seat for the first time in our history, big name firms have moved headquarters out of state, some high tech firms are laying off workers in the Bay area, and so on. California currently has the highest state unemployment rate (5.3%), beating Nevada by 0.2 percentage points. South Dakota is in first place with 2.0%. While we do not see you packing your bags for a move to the Badlands or even a stay in a luxury hotel in Pierre, and, all jokes aside, these are significant unemployment rate differences between states even at times of full employment (the national unemployment rate is 3.9%). But there are, potentially, other, more attractive, alternatives, such as Texas (4% unemployment rate) and Florida (3.3% unemployment rate). These states have seen higher employment growth combined with higher in-migration (Texas will gain two Congressional seats, Florida one).

Here in the Inland Empire, the published (non-seasonally adjusted) unemployment rate stands at 4.8%. However, the Employment Development Department (EDD) does not remove regularly occurring seasonal fluctuations, as is done for state and national data. This is not a good gauge of economic performance, just like you would not look at morning temperatures to make statements about the average temperature of the day. Using standard statistical techniques, the (seasonally adjusted) unemployment rate for the Riverside-San Bernardino-Ontario Metropolitan Statistical Area (MSA) becomes 5.4%, topping the state rate. Within Southern California and using raw data, we are the "leaders" here in Southern California with Orange County at 3.9%, San Diego County at 4.3%, and Ventura County at 4.6% outperforming us; Los Angeles County is tied at 4.8%. We fully understand that Riverside and San Bernardino County saw better times during the earlier phases of the Coronavirus recovery when the Logistics industry was booming, but here we are in June 2024.

We want to stress upfront that unemployment, at this point, is not necessarily something to worry about, especially when the main concern of many employers is to find qualified workers. Instead we want to point to two facts regarding the current situation: (i) even though the Inland Empire unemployment rate is basically the same as the state unemployment rate, there are many more

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[1] Keil: Chief Economist, Inland Empire Economic Partnership, Associate Director, Lowe Institute of Political Economy, Robert Day School of Economics and Finance, Claremont McKenna College; Sattley: Research Analyst, Lowe Institute.

positive aspects to the regional labor market than the state; and (ii) given the current levels of the unemployment rate at full employment, we are pessimistic about the state's future economic performance. This is not the case for the regional economy. We look at the current relative standings as a predictor of how the state and regional economy will develop beyond the peak.

The state-to-state and regional comparisons need more context to determine "how bad is bad." For example, at the state level, the bad news may be tempered by the fact that California unemployment rates are typically higher than the national numbers. Looking back as far as 1990, the state's unemployment exceeds the national rate by an average of 1.3 percentage points, meaning the current difference does not seem that unusual. However, that gap narrows during good times. During each of the last four business cycles, the California unemployment rate is only 0.6 percentage points higher compared to the national rate in the late stages of the economy's expansion, almost half the current difference.

Moreover, although the Inland Empire's unemployment rate is higher than it was a year ago, the current rate is considerably lower than the region's average of 7.8% since 2010. And over the same period, the region's unemployment rate has exceeded the state's by an average of one-half percentage point, making the current 0.1 percentage points gap seem less concerning.

Unemployment rate differences between regions/states are typically explained by differences in socio-economic factors. For example, a region such as the Inland Empire, where only about 25% of residents have a bachelor degree or more years of education, will have higher unemployment rates when controlling for other factors, such as differences in industrial composition. Here we will focus on *changes* in the unemployment rate from a *previous level* - meaning we are controlling for level differences already, a "difference in difference" story.

There are significant differences in recent trends between the state and the region. Comparing the current situation to the last few months of the historically record breaking economic expansion, which ended with the pandemic shutdown in early 2020, the labor force in California is almost a quarter of a million people *smaller* for April 2024 when compared to February 2020. It gets worse for employment: according to the household (residency) survey: there are 413,000 fewer workers than there were prior to the pandemic. Since the change in the unemployment rate is approximately equal to the growth in the labor force minus the growth in employment, the unemployment rate has increased from 4.4% to 5.3%, or by almost a percentage point. This is a bad case scenario: the major reason why the state unemployment rate is "only" at 5.3% currently is because we experienced the Great Resignation - people dropping out of the labor force either because they could not find a job ("discouraged workers"), took early retirement, or left the state. Without the labor force shrinking, the current state unemployment rate would be 6.6%. In a healthy labor market, employment growth coincides or exceeds labor force growth. That is not what we currently observe for California, where the labor force is growing but not yet catching up to pre-pandemic levels, and employment changes are mixed.

Contrast this with the Inland Empire. The situation here is almost the opposite. The labor force grew by almost 70,000 people or 3.3% from February 2020 to now. Employment also increased but not by quite as much, namely by roughly 41,500 people or 2.1%. Hence the only reason why the Inland Empire unemployment rate went up by 1.2 percentage points was the inability for our area to find jobs for all of those who moved here and entered the labor force over this time span. Had the labor force not grown, then the unemployment rate in the Inland Empire today would stand at a remarkable 2.9%! This is in stunning contrast to the situation for California as a whole.

Some may counter that we have given California too bad a rap here. While the residency survey shows a *decline* in employment by over 410,000, there is an alternative survey, based on establishments, that shows California employment actually *growing* by 314,000 over the same period. There are a variety of reasons why the household survey can differ from the establishment survey. Most relevant for the Inland Empire, the household survey includes commuters while the establishment survey only looks at employment within the two counties. But it is unusual to observe such a large difference at the state level. You would find more workers in the establishment survey if there was a significant number of jobs held by individuals who have moved out of the state while working remotely, or if they had immigrated recently and found jobs (e.g. in Leisure and Hospitality, or Construction, or home Health services) but the U.S. Census had not documented their addresses (yet). At any rate, it is a puzzle. Even so, employment in California, based on these more positive establishment survey numbers, grew by only 1.8% from February 2020 to now. If you look at the same numbers for the second and third most populous states, then you find that Texas employment grew by 9.2%, and 9.5% for Florida. Characterizing California's labor market performance as abysmal hardly changes.

Bottom line, looks can be deceiving for both the Inland Empire and California if you just focus on the headline unemployment rate numbers. While both areas show almost identical unemployment rates currently, our region is actually doing relatively well, with an elevated unemployment rate due to (i) adjustments from the Logistics industry initial hiring boom following the Coronavirus recession and initial recovery, and (ii) the labor force and employment growing relative to the economic peak in 2020, with labor force growth outpacing employment growth. California outlook is mixed, given that nonfarm jobs exceed pre-pandemic levels, yet its labor force and household employment numbers remain persistently below their pre-pandemic benchmarks. With the state facing government expenditure cuts due to a large projected budget deficit and capital labor substitution (automation) likely accelerating as a result of increased minimum wages in fast food restaurants and in the health industry, the economic outlook for the state is cause for concern. Expect further bad news with additional losses of Congressional seats, and more workers and firms exiting the state unless significant policy changes are made.