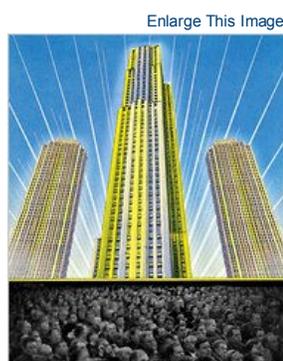


Profits Are Booming. Why Aren't Jobs?

By MICHAEL POWELL
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To gaze upon the world of American corporations is to see a sunny place of terrific profits and princely bonuses. American businesses reported that [third-quarter profits in 2010 rose](#) at an annual rate of \$1.659 trillion, the steepest annual surge since officials began tracking such matters 60 years ago. It was the seventh consecutive quarter in which corporate profits climbed.



Enlarge This Image

David Plunkert

Staring at such balance sheets, you might almost forget that much of the nation lives under slate-gray fiscal skies, a place of 9.4 percent unemployment and record levels of foreclosures and indebtedness.

And therein lies the enduring mystery of this Great Recession and Not So Great Recovery: Why have corporate profits (and that market thermometer, the Dow) spiked even as 15 million Americans remain mired in unemployment, a number without precedent since the Great Depression? Employment tends to lag a touch behind profit growth, but history offers few parallels to what is happening today.

“Usually the business cycle is a rising-and-falling, all-boats-together phenomenon,” noted J. Bradford DeLong, an economics professor at the University of California, Berkeley, and a deputy assistant secretary for economic policy in the Clinton Treasury Department. “It’s quite a puzzle when you have this disjunction between

profits on the one hand and unemployment.”

A search for answers leads in several directions. The bulls’ explanation, heard with more frequency these days, has the virtue of being straightforward: corporate profits are the economy’s pressure cooker, building and building toward an explosive burst that will lead to much hiring next year.

The December jobs numbers suggest that that moment has yet to arrive, as [the nation added just 103,000 jobs](#), or less than the number needed to keep pace with population growth. The leisure industry and hospitals accounted for 83,000 jobs; large corporations added a tiny fraction.

Consumers appear to have put a toe or two back into the water, as holiday spending rose (although it fell short of analysts’ forecasts) and families began to replace the ailing refrigerator or the aging minivan. Car sales are rising.

But relatively few economists, even those who see signs of an improving economy,

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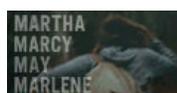
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sound particularly buoyant, a concern shared by liberals and conservatives alike. Jobless recoveries followed on the heels of the last two recessions, but neither prefigured the depth of the trouble this time. After the 1990-91 recession, it took 23 months to add back the jobs lost. After the 2001 recession, it took 38 months. (And it's worth keeping in mind that one of the great housing and credit bubbles in American history fed that hiring; no economist expects that to repeat itself).

At the current rate, the economy will need 72 to 90 months to recapture the jobs lost during the Great Recession. And that does not account for the five million jobs needed to keep pace with a growing population.

None of this has slowed the unprecedented rise in corporate profits. The reasons are many.

More so than in the past, many American-based corporations earn a great portion of their profits overseas. And thanks to porous tax laws, these companies return fewer of those profits to American shores than in the past.

"The big American companies are really global," said Robert Reich, former labor secretary for President Clinton. "They can show big profits from foreign sales. G.M. is making more Buicks overseas than in the United States. There's no special pop for the United States worker."

Key corporate sectors, too, have undergone a Darwinian pruning during the last three years. In the financial arena, a few hyperprofitable firms now stand where many more once stood.

"If you're Goldman and Morgan Chase, and you once had to compete against Bear Stearns and Merrill Lynch, well, of course it's easier now to show a profit," said Daniel Alpert, managing partner of Westwood Capital L.L.C., an investment banking firm. "If you have a modest reduction in expenses, and an industry consolidation at the same time, that translates into a massive increase in earnings."

Surviving corporate leaders drew sobering lessons from their near-death experience of 2008 and 2009, when brand-name corporations nearly ran short of the cash needed to meet payrolls.

"They found the financial system was nowhere near as safe as they thought — they no longer think they can borrow as quickly," said Simon H. Johnson, an economics professor at [M.I.T.](#) and former chief economist for the International Monetary Fund. "So the amount of cash that they think they should have for precautionary purposes is way up."

Interest rates are so low that traders can pile up profits by exploiting the spread between a near-zero funds rate and rates on Treasury bonds. This allows some corporations to mark profits without selling much or hiring anyone.

Desmond Lachman, a former managing director at Salomon Smith Barney who now serves as a scholar at the American Enterprise Institute, a conservative policy center, sees corporate leaders reshaping their worlds.

"Corporations are taking huge advantage of the slack in the labor market — they are in a very strong position and workers are in a very weak position," he said. "They are using that bargaining power to cut benefits and wages, and to shorten hours." That strategy, Mr. Lachman said, serves corporate and shareholder imperatives, but "very much jeopardizes our chances of experiencing a real recovery."

These profits, however, may not be as large as they seem. Justin Fox, editorial director of the Harvard Business Review Group, dices the question of productive corporate profits still more finely in a [recent column](#). He figures that pre-tax domestic corporate profits exclusive of the financial sector are the best measure of the "underlying health of business in America."

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He's not terribly impressed. Profits for these companies "repeatedly topped 12 percent in the 1950s and 1960s," he writes. But in the third quarter of 2010, this sector's share of national income stood at 7.03 percent.

Some economists, conservative and liberal, divine forbidding portents in all of this. If profits and employment no longer rise and fall together, they worry, then an already strained social compact will grow yet more frayed.

Market bulls applauded in November when the Conference Board revealed that consumer confidence was on the rise. But David Rosenberg, an economist at the investment firm Gluskin Sheff, noted that this increase owed entirely to the optimism of higher-income Americans, who are feeling better and better.

The housing market, by contrast, created millions of middle-class jobs and accounted for much of the wealth creation of the past decade. But that sector remains nearly comatose.

"I don't see a pop in corporate hiring, because why should they hurry?" said Professor Johnson, the former International Monetary Fund economist. "They are paying themselves well and with demand so low, they don't feel they are missing out on anything."

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