

Unemployment

**AS Economics Presentation
2005**

Key Issues

- The meaning of unemployment
- Different types of unemployment
- Consequences of unemployment
- Unemployment and economic growth
- Recent trends in UK unemployment
- Full employment

Measuring Unemployment (1)

- A Working Definition of Unemployment
 - People able, available and willing to find work and actively seeking work – but not employed
 - The unemployed are included in the labour force
- The Claimant Count Measure
 - The number of people claiming the Jobseekers' Allowance
 - Monthly count of unemployed
 - Currently under 950,000 – about 3.0% of the labour force

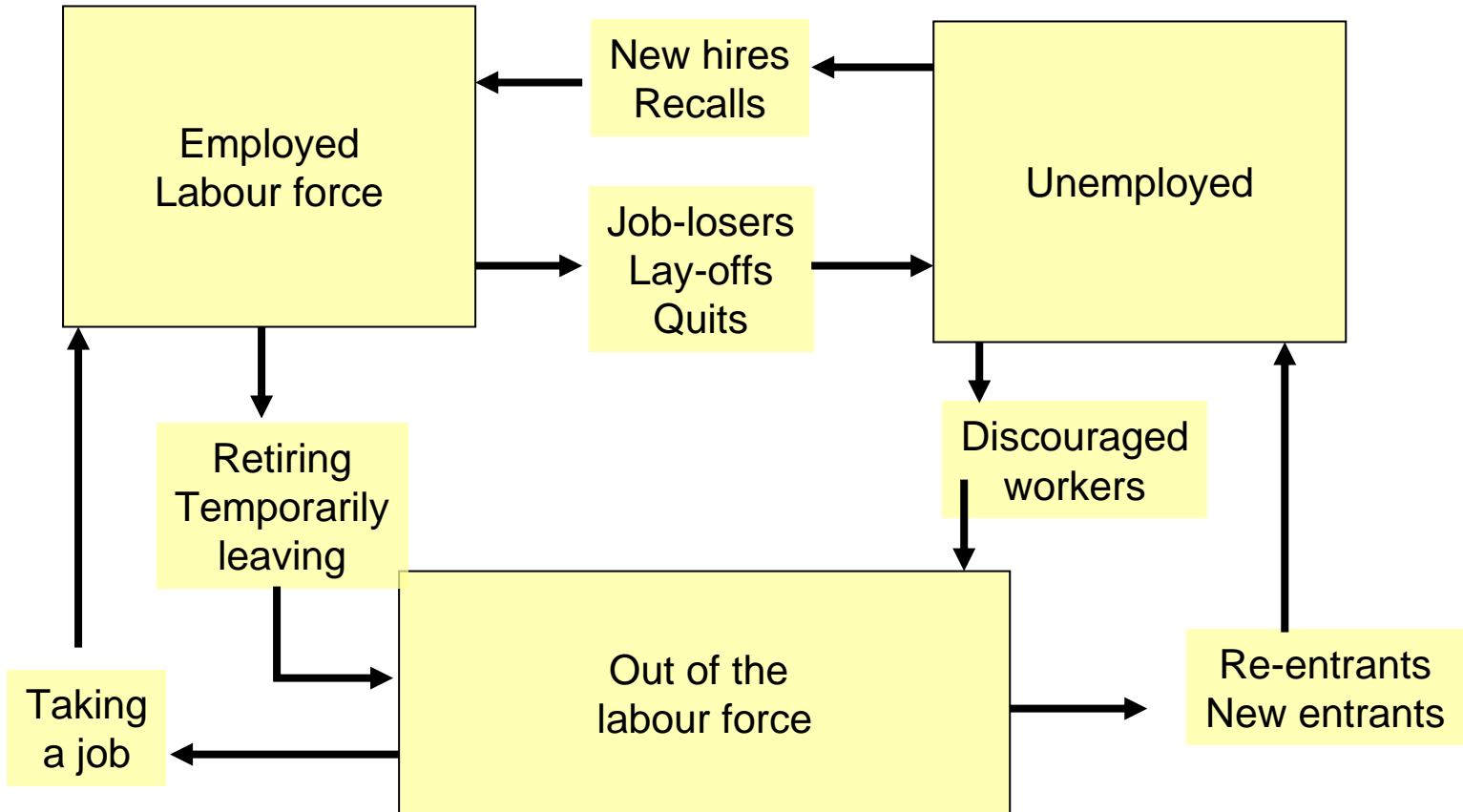
Measuring Unemployment (2)

- The Labour Force Survey (ILO measure)
 - An internationally agreed standard measure of unemployment
 - Must have actively sought work in the previous four weeks and be available to start work immediately
 - Higher figure than the claimant count – approximately half a million higher
 - Higher because there are limits on who can claim unemployment benefit – so the true level of unemployment is higher than the official figures suggest

Hidden Unemployment

- We may be under-counting the true level of unemployment
- Unemployment in Britain may be twice as high as official statistics show. Research on the UK labour market by economists at HSBC bank takes into account anybody who is 'economically inactive', but looking for a job, not just those who are eligible for unemployment benefits
- The report estimates that there are 3.4m Britons who are unemployed, as opposed to the current estimate of 1.4m people. Britain's official unemployment rate is 4.8% - one of the lowest rates of unemployment in the European Union
- Adapted from newspaper reports, July 2004

Flows in the Labour Market

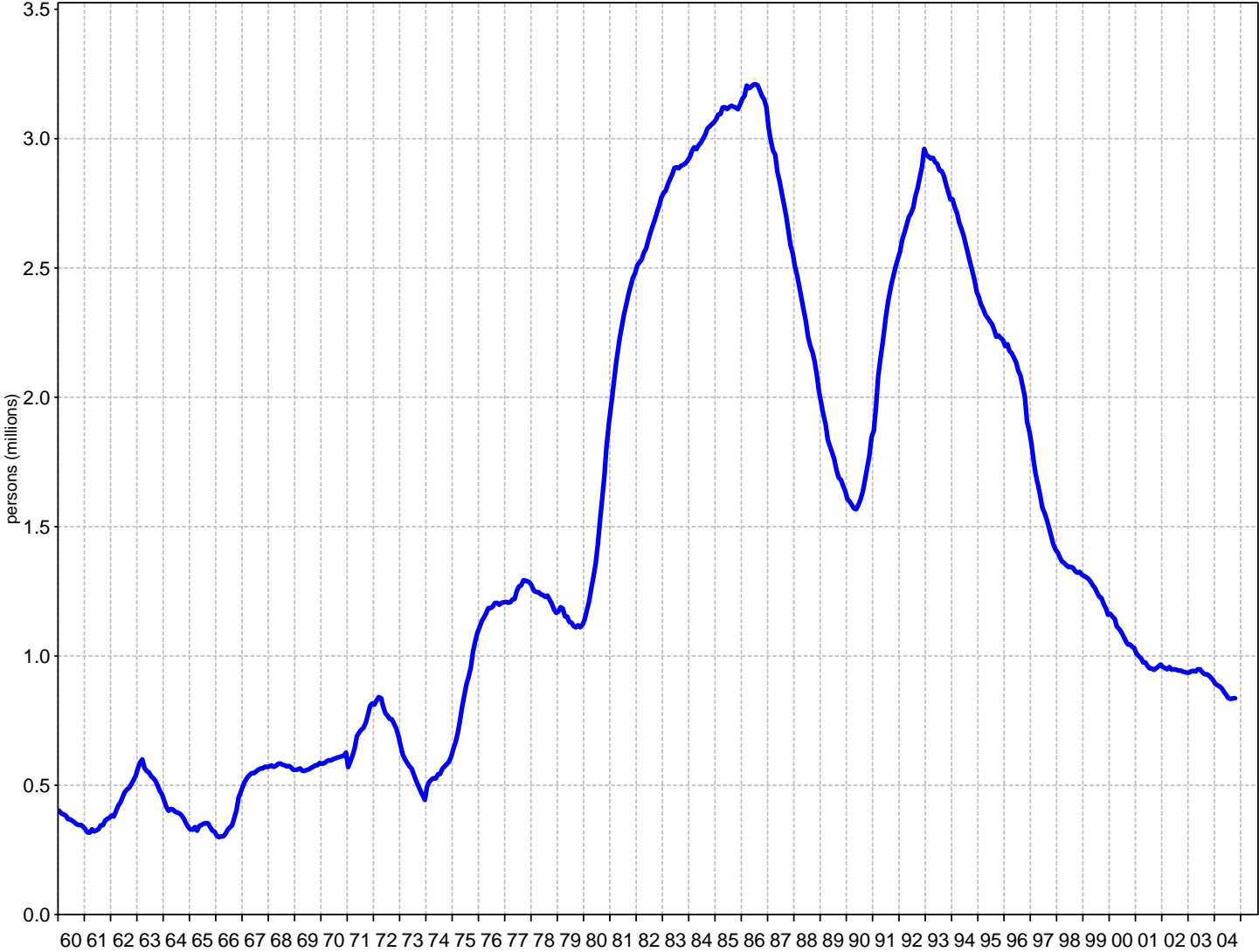


Regional Unemployment

<i>% unemployed (claimant count)</i>	1998	1999	2000	2001	2002	2003
South East	2.6	2.2	1.8	1.6	1.7	1.7
East	3.2	3.0	2.4	2.1	2.1	2.1
London	5.1	4.4	3.7	3.3	3.6	3.9
South West	3.5	3.1	2.5	2.1	2.0	2.0
West Midlands	4.6	4.4	4.1	3.7	3.5	3.5
East Midlands	3.9	3.8	3.4	3.1	2.9	2.9
Yorks & Humbs	5.5	5.1	4.4	4.0	3.7	3.7
North West	5.0	4.6	4.2	3.7	3.6	3.6
North East	7.4	7.0	6.4	5.6	5.3	5.2
Wales	5.4	5.0	4.4	4.0	3.7	3.7
Scotland	5.4	5.2	4.5	4.0	3.9	3.9
N Ireland	7.4	6.5	5.3	5.0	4.6	4.6
United Kingdom	4.5	4.1	3.6	3.2	3.1	3.1

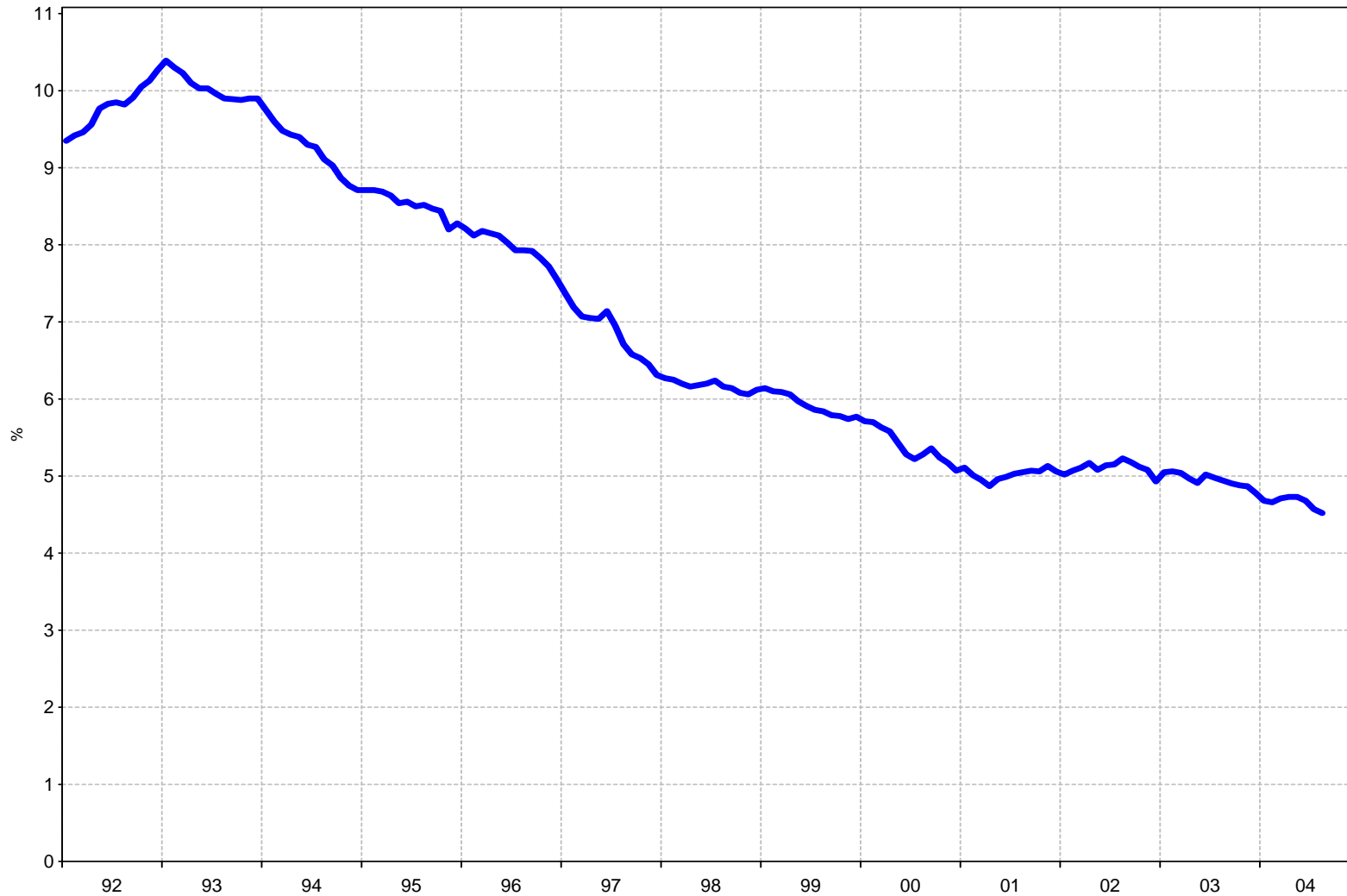
Unemployment trends

United Kingdom - Level of Unemployment
Claimant Count - seasonally adjusted, 000s



Labour Force Survey Measure

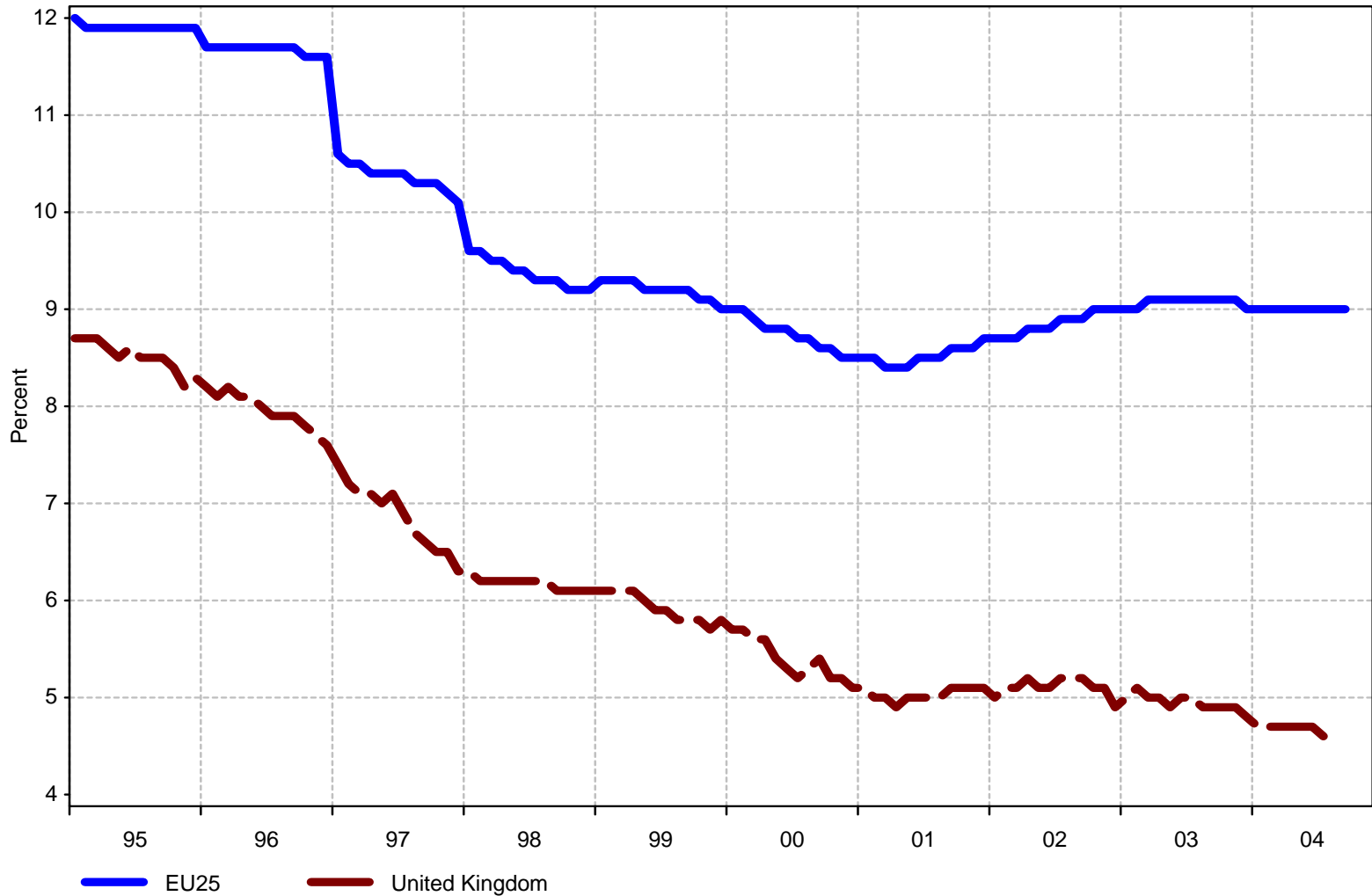
Labour Force Survey Unemployment Rate
Percentage of the labour force



Source: EcoWin

Comparing UK and European Unemployment

European Union (25) and United Kingdom Unemployment Rates
Seasonally adjusted, percentage of the labour force, source: Eurostat



Source: EcoWin

Types of Unemployment

- Seasonal
 - Regular seasonal changes in employment / labour demand
 - Affects certain industries more than others
 - Catering and leisure
 - Construction
 - Retailing
 - Tourism
 - Agriculture
 - Seasonal unemployment is not a major cause for concern

Types of Unemployment

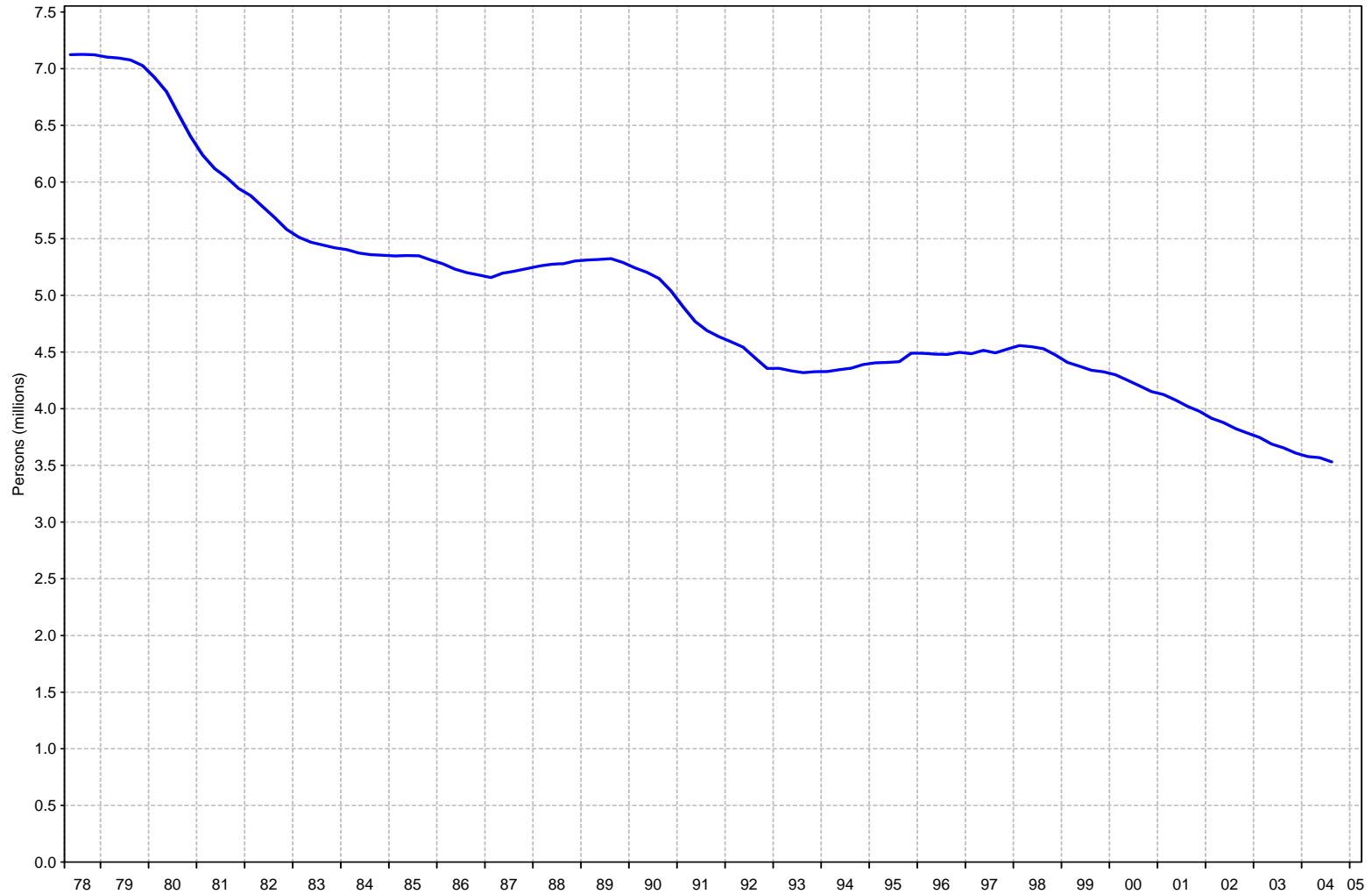
- Frictional
 - Transitional unemployment due to people moving between jobs: Includes people experiencing short spells of unemployment
 - Includes new and returning entrants into the labour market
 - Imperfect information about available job opportunities can lengthen the period of someone's job search

Structural Unemployment

- Structural
 - Arises from the mismatch of skills and job opportunities as the pattern of labour demand in the economy changes
 - Occupational immobility of labour
 - Often involves long-term unemployment
 - Prevalent in regions where industries go into long-term decline
 - Good examples include industries such as mining, engineering and textiles

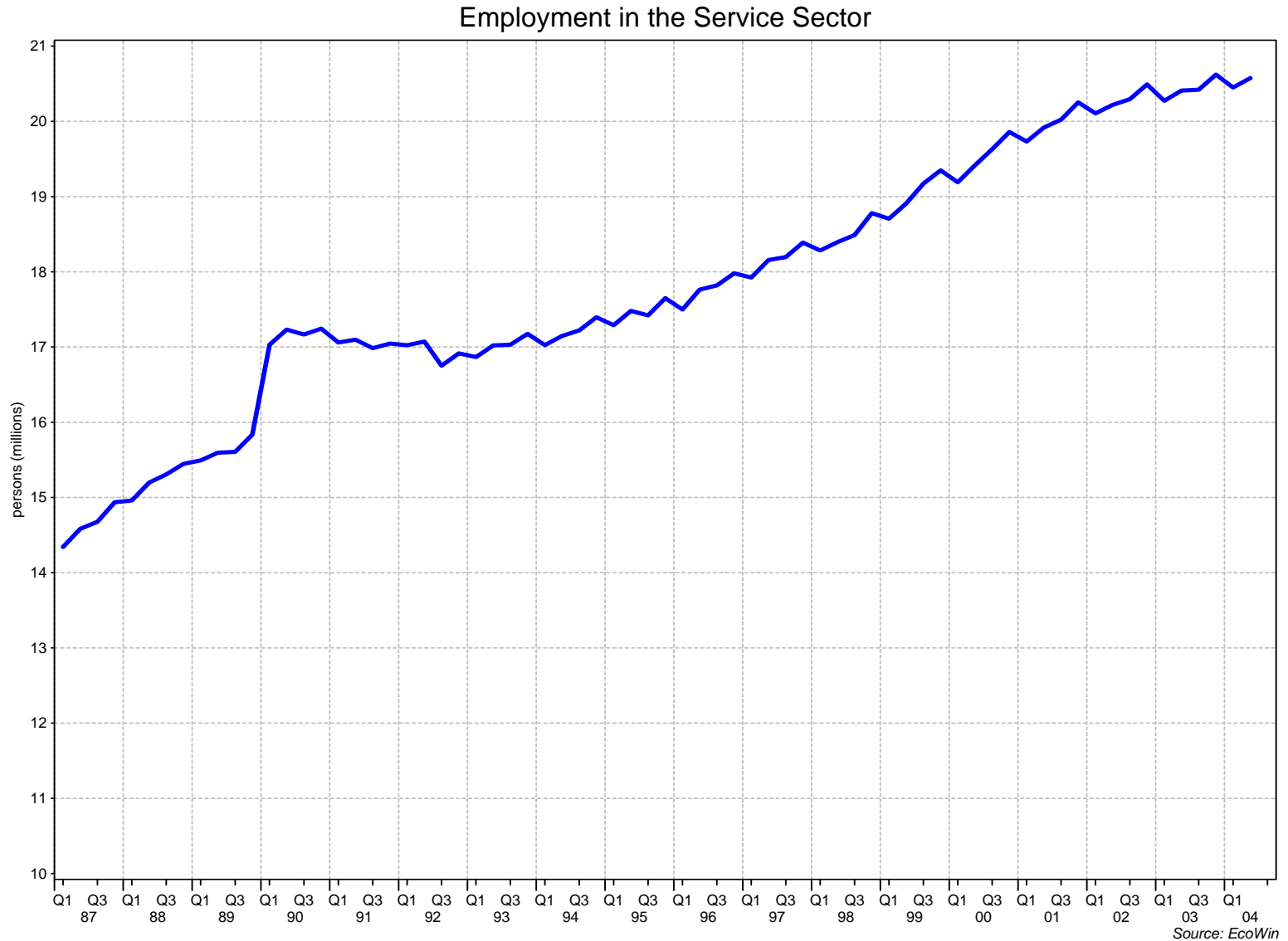
Manufacturing Employment

Employment in UK Manufacturing Industry
Millions, seasonally adjusted



Source: EcoWin

Service Sector Employment



Changing UK employment structure

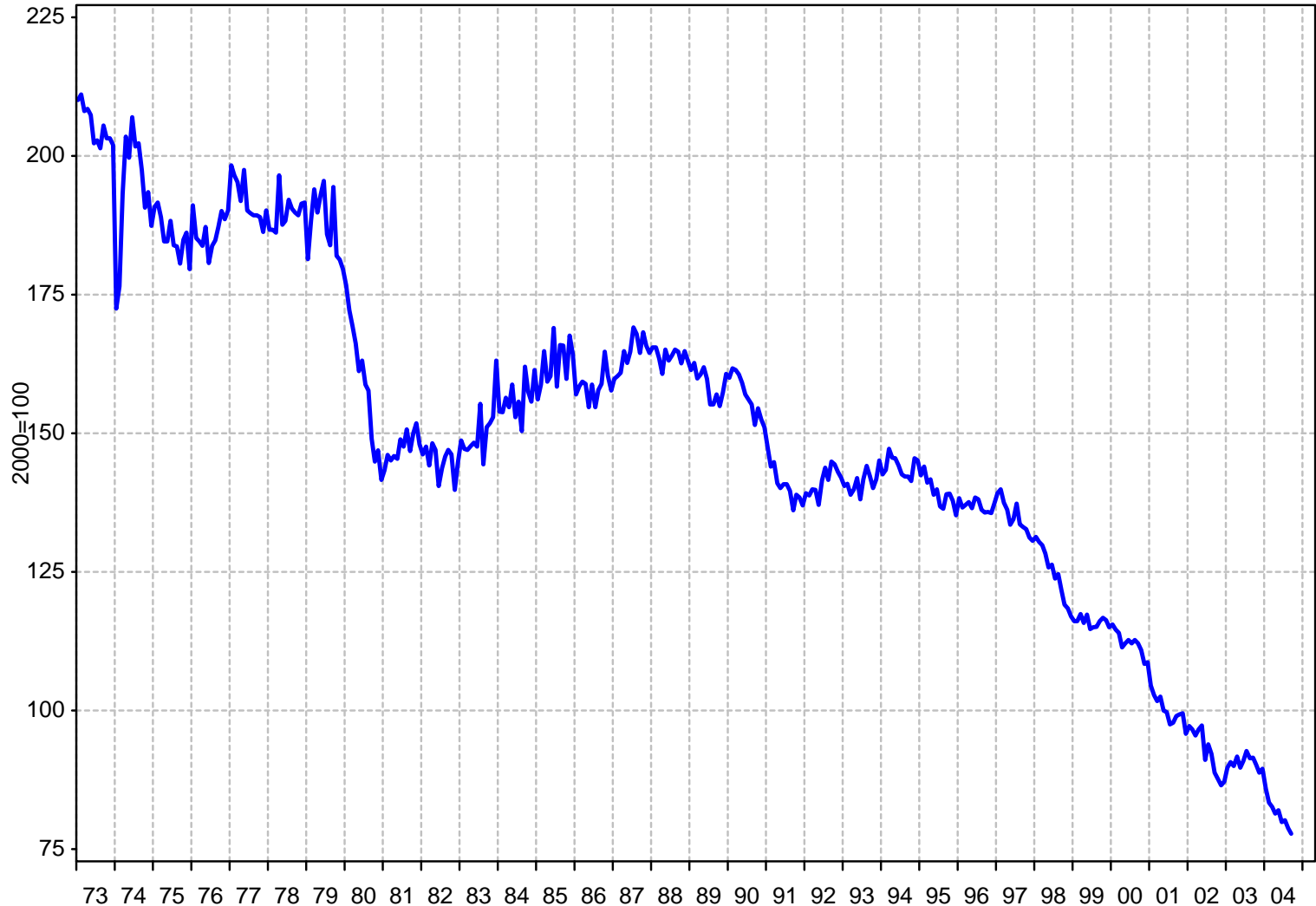
	Jobs (thousands)	Jobs (per cent)	Percentage change 1984–2004
Agriculture and fishing	420	1.4	–36.5
Energy and water	203	0.7	–64.3
Manufacturing	3,654	12.1	–32.4
Construction	2,111	7.0	15.5
Services	23,936	78.9	37.6
<i>of which:</i>			
Distribution, hotels & restaurants	7,040	23.2	25.3
Transport & communication	1,813	6.0	13.5
Finance & business services	5,828	19.2	80.0
Public administration, education & health	7,362	24.3	28.3
Other services	1,893	6.2	57.3
All jobs	30,325	100	17.3

1 Seasonally adjusted.

Source: Office for National Statistics

An industry in long term decline

Uk manufacture of textiles, leather and clothing
Seasonally adjusted level of output at constant 2000 prices



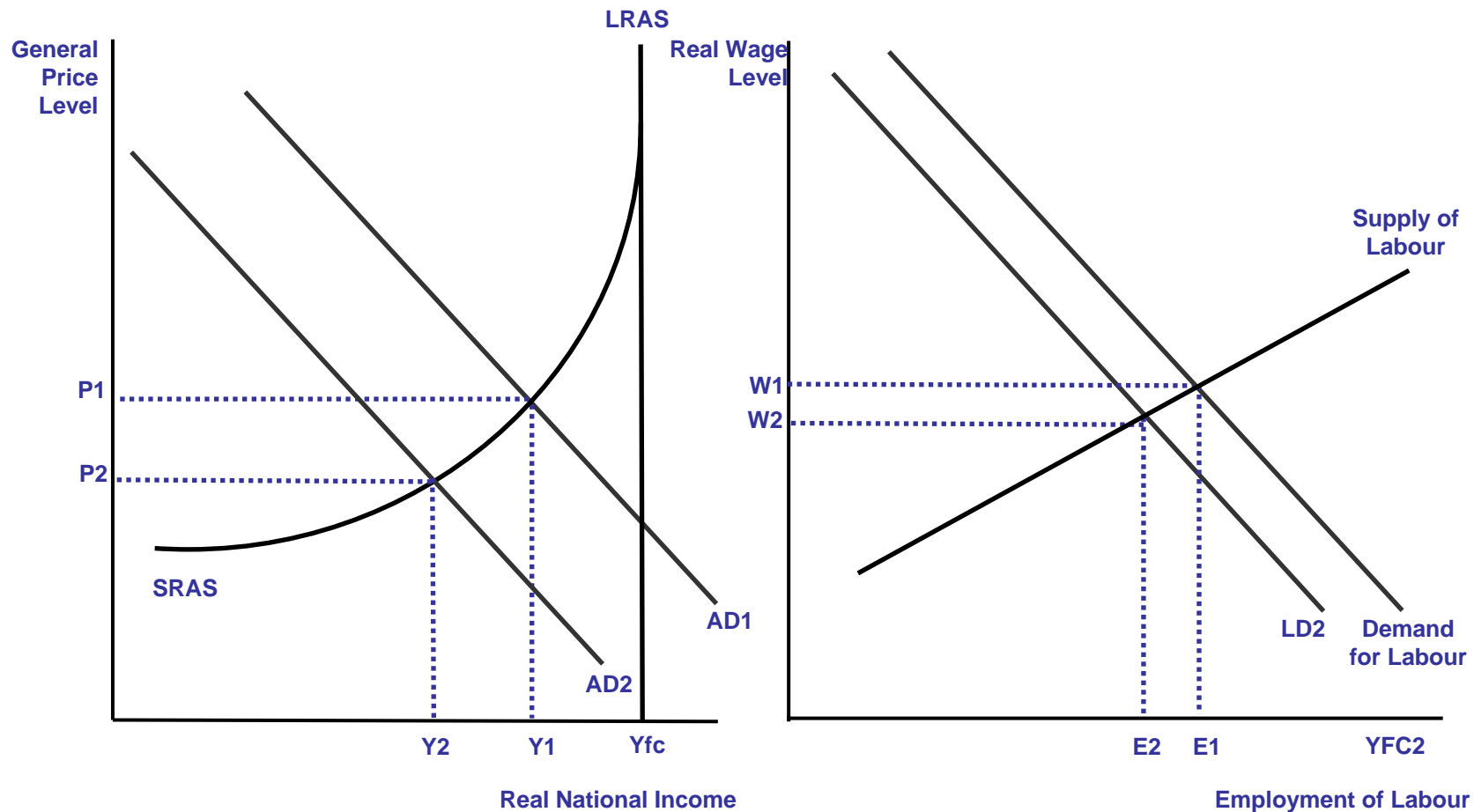
Source: EcoWin

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Cyclical unemployment

- Cyclical (Keynesian)
 - There is a cyclical relationship between demand, output, employment and unemployment
 - Caused by a fall in aggregate demand leading to a loss of real national output and employment
 - A slowdown can lead to businesses laying off workers because they lack confidence that demand will recover
 - Keynes argued that an economy can become stuck with a low rate of AD and an economy operating persistently below its potential

Cyclical unemployment using AD-AS

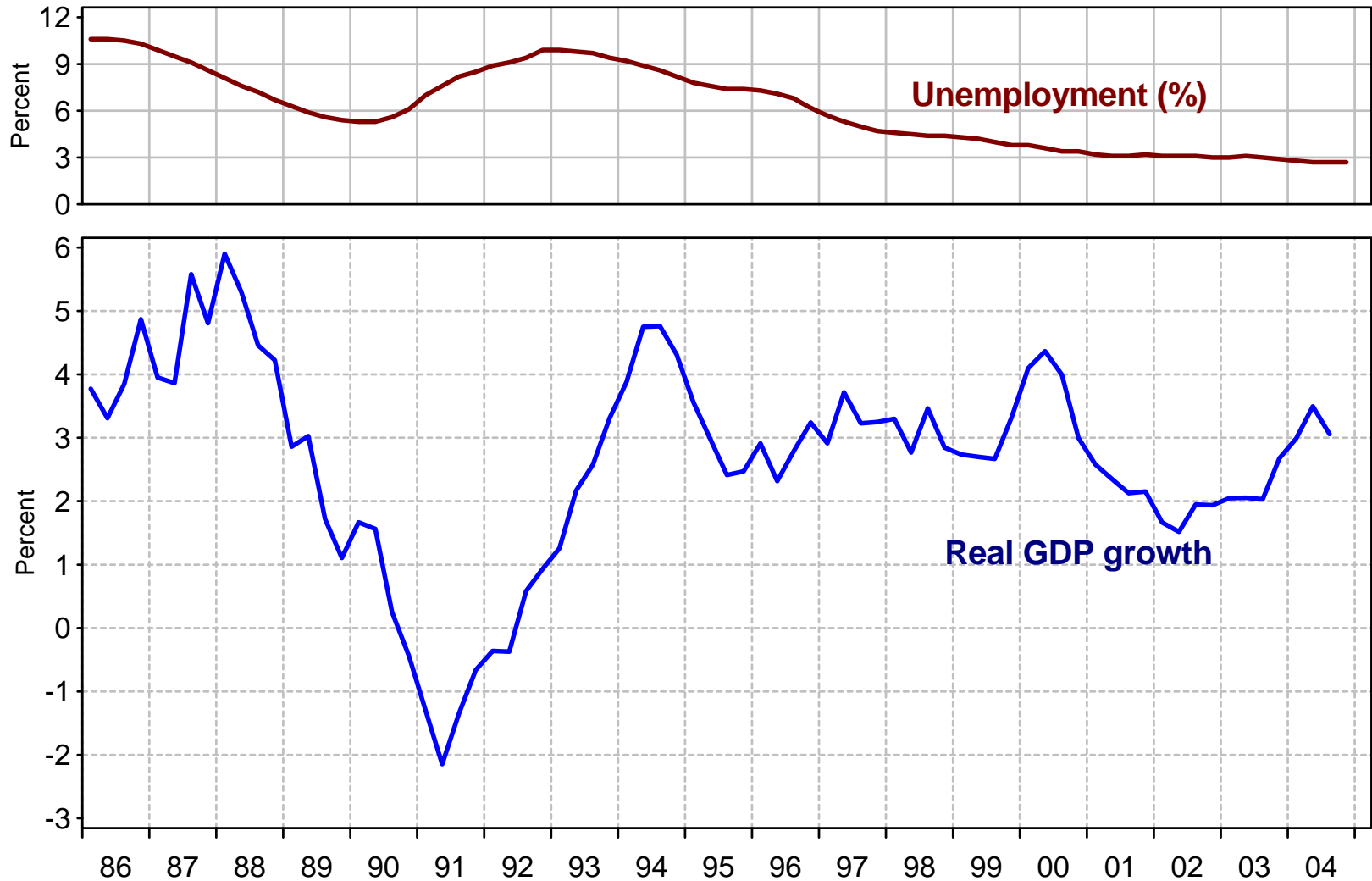


Real Wage Unemployment

- Real Wage Unemployment
 - Created when real wages are maintained above their market clearing level leading to an excess supply of labour at the prevailing wage rate
 - Some economists believe that unemployment can be created if the national minimum wage is set too high

Unemployment and Growth in the UK

Real GDP and Claimant Count Unemployment



— United Kingdom, Unemployment, Rate, Claimant count, SA — Real GDP growth [ar 4 quarters]

Recent examples of cyclical unemployment

- Recession in the UK in the early 1990s
 - Unemployment rose from 1.6 million in 1989 to 2.9 million in 1993
- The recent recession in UK manufacturing industry
- Slow growth and rising unemployment in Germany
- The end of full-employment for Japan during the last ten years

Economic and Social Costs of Unemployment

- The private costs for the unemployed
 - Loss of income – but many households have major spending commitments (mortgage, credit agreements etc.)
 - Fall in real living standards
 - Increased health risks
 - Stress
 - Reduction in quality of diet
 - Increased risk of marital break-up
 - Social exclusion because of loss of work and income
 - Loss of marketable skills (human capital) and motivation
 - The longer the duration of unemployment, the lower the chances of finding fresh employment - the unemployed become less attractive to potential employers

Consequences of Unemployment (2)

- Economic Consequences for Businesses
 - Negative consequences
 - Fall in demand for goods and services
 - Fall in demand for businesses further down the supply chain
 - Consider the negative multiplier effects from the closure of a major employer in a town or city
 - Some positive consequences
 - Bigger pool of surplus labour is available – but still a problem if there is plenty of structural unemployment
 - Less pressure to pay higher wages
 - Less risk of industrial / strike action – fear of job losses – leading to reduced trade union power

Consequences of Unemployment (3)

- Consequences for the Government (Fiscal Policy)
 - Increased spending on unemployment benefits and other income –related state welfare payments
 - Fall in revenue from income tax and taxes on consumer spending
 - Fall in profits – reduction in revenue from corporation tax
 - May lead to rise in government borrowing (i.e. a budget deficit)

Consequences of Unemployment (3)

- Consequences for the economy as a whole
 - Lost output (real GDP) from people being out of work – the economy will be operating well within its production frontier
 - Unemployment seen as an inefficient way of allocating resources – labour market failure?
 - Some of the long-term unemployed may leave the labour force permanently – fall in potential GDP
 - Increase in the inequality – rise in relative poverty

Demand side Policies to Reduce Unemployment

- These are mainly measures to boost total labour demand (reduce cyclical unemployment)
 - Lower interest rates (a monetary policy stimulus)
 - A lower exchange rate (helps exporters)
 - Lower direct taxes (fiscal stimulus to spending power)
 - Government spending on major capital projects (e.g. improving the transport infrastructure)
 - Employment subsidies (including the New Deal programme) – designed to reduce the cost to a business of employing additional workers
 - Incentives to encourage flows of foreign investment in the UK
 - particularly in areas of above average unemployment

Supply-side policies to reduce Unemployment

Supply-side policies

- These are measures to improve labour supply (reduce frictional and structural unemployment)
 - Increased spending on education & training including an emphasis on “lifetime-learning”)
 - Improved flows of information on job vacancies
 - Changes to income tax and benefits to improve incentives to find work
 - Measures designed to make the labour market more flexible so that workers have the skills and education that gives them improved employment options
 - Reforms to employment laws to make it less costly for firms to change the number of people they employ

The effects of the New Deal programme

People entering employment through the New Deal: by age and type of employment, 1998 to 2003

	Thousands		
	18-24	25 and over	All aged 18 and over
Sustained employment	367	130	497
Other employment ¹	96	35	130
All entering employment	463	165	628
Those entering sustained employment (percentage of all leavers from New Deal programme)	39	25	36

1: Employment lasting less than 13 weeks.

Source: Department for Work and Pensions

Consequences of falling unemployment

- The circular flow and the multiplier:
 - Incomes flowing into households will grow
 - Falling unemployment adds to demand and creates a positive multiplier effect on incomes, demand and output.
- The balance of payments:
 - When incomes and spending are growing, there is an increase in the demand for imports. Unless this is matched by a rise in export sales, the trade balance in goods and services will worsen

Consequences of falling unemployment

- Government finances:
 - With more people in work paying income tax, national insurance and value added tax, the government can expect a large rise in tax revenues and a reduction in social security benefits
- Inflationary effects
 - Falling unemployment can also create a rise in inflationary pressure – particularly when the economy moves close to operating at full capacity
 - However this is not really a risk when the economy is coming out of recession, since aggregate supply is likely to be highly elastic because of a high level of spare capacity

The Changing Pattern of Employment

The Changing Pattern of Employment Employee jobs: by sex and industry

Percentages

	Males			Females		
	1983	1993	2003	1983	1993	2003
Distribution, hotels, catering and repairs	17	20	22	26	26	26
Manufacturing	29	24	20	16	11	7
Financial and business services	12	17	20	14	17	19
Transport and communication	10	10	8	2	2	4
Construction	8	7	8	2	1	1
Agriculture	2	2	1	1	1	-
Energy and water supply	4	2	1	1	1	-
Other services	17	19	20	39	41	42
All employee jobs (=100%) (millions)	12.4	11.3	13.0	9.9	11.5	12.8

Source: Office of National Statistics

Falling unemployment in the UK

- Demand factors
 - Sustained economic growth since 1992
 - Growth creates jobs to replace jobs lost in industries suffering from long term decline
 - High levels of inward investment from overseas
 - Strong consumer demand and housing boom
- Supply factors
 - Extra investment in education and training may be working
 - Britain now has a more flexible labour market than in the past
 - workers have more adaptable skills
 - Employment laws have changed – easier for firms to take on extra workers
 - E.g. growth of temporary and part time employment

Falling unemployment

