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Class C

Unemployment Differentials

Quoted References:

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- C.A. Pissarides and J. Wadsworth, "Unemployment Risks", in E. McLaughlin (ed.) *Understanding Unemployment*
- "New developments in the pattern of claimant unemployment in the United Kingdom", *Employment Gazette*, September 1995
- "Characteristics of ILO unemployed", *Employment Gazette*, July 1994

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Introduction

When given an aggregate level of unemployment, we are usually told nothing about how this level of unemployment is put together. That the rate of unemployment is not evenly spread across the entire population is almost a tautology, and it is a well-known fact that certain age-groups, skill-groups, genders, ethnic groups, regions and industries are more likely to be a victim of unemployment than others.

Furthermore, when we are given an aggregate rate of unemployment, we are told nothing about *how many* people are unemployed (*incidence of unemployment*) for *how long* (*duration of unemployment*). To segregate the two factors is important in order to take a closer look at the *burden of unemployment* a worker has to suffer, ie the combinations of incidence and duration that lessen the worker's well-being. (Filer 1996:303)

In this essay I want to take a closer look at which groups of people seem more vulnerable to the risk of unemployment, concentrating on age-groups, skill-groups and industries, starting with the discussion of a methodological problem. I shall discuss whether the unemployment hazard is due to incidence or duration and I will attempt to find a few main reasons for such differences. To conclude I shall briefly discuss in which way policy-making can and does deal with the problem of unemployment differentials.

Problem of Methodology

One of the main problems when analysing the way in which population groups and unemployment are correlated, is to find a direct causal link.

If, for instance, we find that people who wear pink shoes are more likely to be unemployed than others, we must ask ourselves, if their unemployment is directly due to the fact that they are wearing pink shoes, or if their unemployment has its causes in some other characteristics which are directly associated, but not causally linked, to the fact that they are wearing pink shoes, eg that all wearers of pink shoes tend to be rather clumsy.¹

In this case it is obvious that it is more interesting to pay attention to clumsy people as opposed to people wearing pink shoes. The pink shoes - unemployment correlation may in this case be quite interesting, but it is more informative to find the direct causation to the problem. Pink shoes may, however, still play a small direct part in the wearers' unemployment (imagine your interviewee wearing pink shoes), in which case it is necessary to find out to which degree one factor is the cause for unemployment and to which degree another factor. And this may not always be very easy.

The above is a very important methodological point. The article by Pissarides and Wadsworth tries to take into account the extent to which a factor is actually directly responsible for unemployment through a linear regression. The other articles merely state the overall correlation of belonging to one group of people and being unemployed without attempting to reduce the correlation to find a true probability.

¹ I am using a ridiculous example to avoid any political incorrectness that might involuntarily arise from using a real-world example.

The Groups at Risk

Age-groups

Almost any table will show that the unemployment rate declines as age-groups get older. However, Pissarides and Hamermesh note that "removing all but the pure age effect, shows that in 1979 age did not appear to exert an independent influence on male unemployment, but in 1986 there was some effect". Note that we are here talking about the incidence of unemployment: young people are more likely to experience one or more (short or long spells) of unemployment than older people. That Pissarides and Wadsworth point to a small age effect indicates that other factors such as education and human capital formation are much more important in determining employment.

What, in effect, would the pure age effect be? An employer may reason that young people are lazy, which leads him to employ older people. But then again one could argue that he discriminates against lazy people, and segregating the pure age effect once again becomes even more difficult.

Once we look at long-term unemployment, we notice that young people are least prone to suffer, which reverses the direction of the incidence of unemployment. Conversely, it is workers in the oldest age-group that are most prone to long-term unemployment.

In order to explain this, we must look at two opposing forces. Human capital formation and cost of training. A firm is most interested in employing a worker with as much human capital as possible. On the other hand a firm is also interested in employing and training a worker - thus paying for substantial

training costs - who will be of use to the firm as long as possible. These two notions contradict. If a company hires a young worker, it will have a worker with practically no human capital but with a long career ahead of her. The fact that the worker has not had any work experience dominates, however, and young people only find jobs of usually short duration. This would explain the high incidence but short duration of youth unemployment. After a while, however the accumulation of experience at such short jobs takes hold, and firms are now interested in steadily employing and training a worker. As people's ages progress, it gets less beneficial for a company to hire and - especially - train a worker. Older people now increasingly find that their accumulated human capital does not compensate for the cost to the firm of training them. In addition, it is also difficult for them to find the low-skill jobs young people can find, since they usually require some degree of physical fitness, which is more prevalent in young than in older people. Hence older people will stay out of work for a longer time, generally finding it difficult to find *any* job.

Another interesting fact is that there seems to be more long term unemployment among married men. Filer et al. explain, however, that "the *average* married man differs from the *average* single man in another important way: he is older". Hence causation can, once again, be too easily deduced.

Skill-groups

In discussing different skill-groups I want to look at both the way in which different levels of education and different types of on-the-job skills affect the risk of being unemployed.

Pissarides and Wadsworth report, rather unsurprisingly, that the higher the level of education, the less likely the incidence of unemployment. They note most importantly, however, that "the big rise at a time of high unemployment takes place when we move from the groups with some qualifications to those with none". This, they say, is due to the fact that people with no qualifications have other factors associated to them which makes it more difficult for them to find a job, rather than simply the fact that they don't have any education. Pissarides and Wadsworth don't mention what this may be, but a little bit of fantasy might give us some clues: there is usually a reason as to why people didn't, or couldn't attain a high level of education, which may colour off as well on to the working environment. If someone is incapable of learning academic skills, he may be equally incapable of learning on-the-job skills.

As for the duration of unemployment, Pissarides and Wadsworth note that there is no observable correlation between the level of education and the length of unemployment. They also note, however, that this outcome is due to statistical unreliability and that we can still assume that people with a degree are less likely to suffer from long-term unemployment.

However, high education does not imply job security. "For example, a secretary with a degree will have a higher risk of unemployment than a similar degree holder in a professional job."² In other words the occupation and the skills required to perform it are also an important factor. Pissarides and Wadsworth note that unskilled male manual workers have 20 percentage points more unemployed than professional men, 17 percent of which was attributable to mere occupational differences, and only 3 percent to education. They also note that manual workers are more prone to unemployment than others. These

²Pissarides and Wadsworth

observations may be due to many factors. The high incidence may be explained by the seasonal sensitivity of many manual-work jobs ³ or alternatively by other more psychological factors, such as job-satisfaction or motivation. These explanations are eclipsed, however, if we discuss the role of the type of industries the workers work in.

Industries

Some industries may be more sensitive to demand- or supply-shocks than others. The rise in oil prices in the 70s meant that many manufacturing companies couldn't afford to use as much labour as they had so far, so they had to make many workers redundant. These were mostly workers who had work directly relating to the raw material, ie manual workers. ⁴ Thus the nature of the work may be more sensitive to unemployment because the relating industries are more sensitive to economic circumstances.

An interesting factor that goes together with the phenomenon of different levels of unemployment due to different industries is the fact that some regions are more sensitive to unemployment than others. This can largely be explained by the fact that certain regions specialise in certain industries, whereas others specialise in a large number of industries or more secure ones. Hence, traditionally, Wales had been prone to high levels of unemployment for a long time, because their coal-mining industry was gradually declining due to the substitution of coal as an energy-resource with nuclear energy. The September 1995 issue of the *Employment Gazette* note, however, that the various regions

³if seasonal adjustment is not made

⁴Even if a firm cannot produce as many plastic bags as before, it still needs accountants, personnel-managers, financial analysts etc. White-collar workers are therefore less prone to redundancy in times of demand- or supply- shocks.

in Great Britain have been gradually converging towards the same overall levels of unemployment. Wales, for instance, has seen a high level of foreign investment on its territory, which has enabled the creation of new jobs. The *Gazette* notes, that there is far more a urban-rural divide prevalent than a regional one.

Policy-Making

Pissarides and Wadsworth conclude their paper by saying that "whilst the risk of unemployment is increasing, those at either end of the age spectrum and the unskilled will suffer disproportionately... Policy-makers should seek to target any training schemes at those vulnerable groups for whom the risks of unemployment are most severe". Layard, Nickell and Jackman explain that "the NAIRU depends on the *variance* of the relative unemployment rates. Hence equiproportional rises in unemployment rates do not increase the NAIRU."

From these two comments it is evident that unemployment differentials are a big problem and should be of great concern to policy makers. The *Employment Gazette* indicates that the Thatcher Government policies to reduce long-term unemployment had a considerable effect. The Blair Government is now concentrating on giving everybody equal opportunities through decent training and education. It will be interesting to see how far each of these will have enduring effect on the overall rate of unemployment.