

# Poverty and worklessness

**Stephen Nickell provides a profile of poverty in Britain today and argues that it is high by European standards because of our exceptionally long tail of very low skilled adults.**

**B**ritain is exceptional in having much more poverty than most of the other countries of Northern Europe. Furthermore, poverty in Britain has increased dramatically since 1979.

Britain also has a particularly large number of working age "workless households": quite surprising in view of its relatively high employment rate. This is reflected in the fact that, if you were not employed in 1996, the probability of your living in a household where no one else worked exceeded 50%, higher than in any other OECD country except Finland. The connection between poverty and worklessness is a strong one. Over 53% of poor children live in workless households, whereas only around 20% of children overall do so.

In Britain today, a little over 20% of people are poor, generally when no one in their household works or when one person works and is not paid very much. If two or more people in a household work and at least one works fulltime, poverty is unlikely to be found (i.e. in less than 5% of cases). The proportion of children in poverty (around 30%) is higher than the overall poverty rate because children are more likely than adults to live in poor households. In particular, they are more likely to live in single parent households and are less likely to live in households where two adults are working.

While poverty is measured in terms of money, it is not just about money. Almost anything bad you can think of, poor people have more of it: more illness, more accidents, more crime, fewer opportunities for their children and the most fantastically expensive credit. So it is important to shed some light on where all this poverty comes from and on what might be done about it.

**Table 1. Individual Poverty in Different Family Types, 2000/1 (1997 in brackets)**

	% of individuals in each type	% of each type in poverty	contribution to overall poverty
Couple with children	42.4 (44.0)	20.9 (23.0)	40.0 (41.3)
Couple without children	25.5 (26.2)	12.2 (11.3)	14.1 (12.2)
Single with children	10.1 (9.9)	53.8 (62.0)	24.5 (26.0)
Single without children	22.0 (19.9)	21.7 (24.3)	21.4 (20.5)
Total	100	22.2 (23.6)	100

Source: Piachaud and Sutherland (2002), Tables 1, 3.

Table 1 shows how poverty is distributed across households of different types. In the second column we see how single parent households are far more likely to be poor than any other household type, but there are few enough of them to contribute only one quarter of total poverty. Poverty is high in single parent households in

**Table 2. Individual Poverty in Households with Different Employment Circumstances 2000/1 (1997 in brackets)**

	% individuals in each type	% of each type in poverty	% contribution to overall poverty
Workless	17.0 (19.5)	64.4 (68.4)	51.4 (56.7)
One or more PT	10.0 (9.0)	29.4 (31.9)	13.8 (12.2)
Head self-employed	10.9 (12.2)	24.6 (21.9)	11.6 (11.4)
Couple, one FT	14.5 (14.8)	19.7 (20.5)	13.4 (12.9)
Couple one FT, one PT	17.5 (17.1)	5.1 (4.4)	4.2 (3.2)
Single/Couple, all in FT work	30.1 (27.4)	4.0 (3.1)	5.6 (3.6)
<b>Total</b>	<b>100</b>	<b>21.3 (23.5)</b>	<b>100</b>

Source: Piachaud and Sutherland (2002), Table 4.

part because more than half of the single parents do not work and many rely on state benefits. By and large, any household that has to rely solely on state benefits will be poor on standard definitions. It is worth noting that couples without children are much less likely to be poor than singles without children and that households with children make up just over half of all households, but nearly two thirds of those in poverty.

Table 2 cuts things a different way, focussing on employment status. As we have already noted, worklessness is a key factor. Although only 17% of individuals live in

workless households, because nearly two thirds of them are poor, they contribute more than half of all poverty. It would be a mistake to conclude that these facts point to a "simple" solution to poverty, namely get every adult to work. Workless adults tend, on average, to have significantly lower earning power than those in work. So getting them to work would have much less of an impact on poverty than might be imagined, unless they receive other benefits.

Table 3 focuses on child poverty. Here worklessness is even more important. Over three quarters of children

**Table 3. Child Poverty in Households with Different Employment Circumstances, 2000/1 (1997 in brackets)**

	% children in each type	% children in poverty	% contribution to overall child poverty
Workless	20.7 (24.6)	77.4 (80.1)	52.8 (58.3)
One or more PT	9.7 (7.8)	42.2 (48.7)	13.5 (11.2)
Head self-employed	11.6 (13.0)	30.8 (28.1)	11.8 (10.8)
Couple, one FT	17.6 (18.3)	25.2 (27.1)	14.6 (14.7)
Couple one FT, one PT	23.5 (22.0)	6.2 (5.5)	4.8 (3.6)
Single/couple, all in FT work	16.8 (14.3)	4.5 (3.3)	2.5 (1.4)
<b>Total</b>	<b>100</b>	<b>30.3</b>	<b>100</b>

Source: Piachaud and Sutherland (2002), Table 5.

**Table 4. Workless Households in 1999**

	% workless	% of individuals in workless households
Couple with children	7.3	18.1
Couple without children	8.5	12.7
Single with children	56	32.9
Single without children	29	36.3

Source: Dickens and Ellwood (2001).

**53% of poor children live in workless households**

## Poverty is not just about money

Table 5. % Workless

	1979	1999
Couple with children	4.5	7.3
Couple without children	3.4	8.5
Single with children	35	56
Single without children	18	29

Source: Dickens and Ellwood (2001).

living in workless households are poor. It is clear from all this that worklessness and low pay generate poverty. Table 4 shows the distribution of worklessness across household types. Not surprisingly, we see that around 70% of individuals in workless households live in single adult households.

Turning to low pay, we find that 72% of workers in poor households are low paid. Of course, the relationship between low pay and poverty is not strong in the sense that only around 14% of low paid individuals live in poor households. This is because many low paid individuals (e.g. students) live in households where others earn enough to lift the household out of poverty. Nevertheless, there is a strong connection between low pay and worklessness. For example, the probability of working for low pay is nearly 60%, if the individual did not work in the previous year, but only 22% if they did. Alternatively, if someone is low paid in one year, the probability of not working 12 months later is nearly three times greater than if they were not low paid.

As we can see from Table 5, worklessness among working age households has risen within all categories, a fact which was first noted in the seminal work of Gregg and Wadsworth (1996, 2001). This happened despite the fact that the UK employment rate rose between 1979 and 1999 from 70.8% to 71.7% (OECD, 1995, Table A and OECD, 2002, Table B). Since the rate of individual worklessness actually *fell* over this period, what explains this apparent contradiction?

Some relevant facts are the following. Overall, neither unemployment nor inactivity changed greatly from 1979 to 1999. Unemployment among low skill men (with no qualifications) rose from 7.0% in 1979 to around 12% in 1999. There was no significant change for low skill women. Inactivity among working-age men rose substantially (4.7% to 15.9%). To compensate, inactivity among working age women fell from 34.6% to 26.9%.



What seems to have happened is that the increase in female participation in work is among married women whose partners are typically working. At the same time, participation of single women with children has fallen. This is, in part, a composition effect arising from the increase in the proportion of single parent households where the head is a never-married woman who is living apart from her own parents and, therefore, with less access to childcare.

The rise in inactivity among men has been concentrated on married men whose partners are not (or cease) working and among single men. Among couples, we have seen a substantial rise in households where both partners are working (from 55 to 64% of all two adult working age households from 1979 to 1999). We have also seen a substantial rise in households where neither partner is working (from around 4% in 1979 to around 8% in 1999).

Perhaps the most interesting feature of these changes is the significant rise in inactivity among men of working age.

In Figures 1 and 2, we can see the overall picture. The key feature here is the rise in the median relative to the 10th percentile, where many in poverty are located. These changes mean that the UK has a much more dispersed pay distribution than nearly all northern European countries (France being the notable exception). Even in 1979, the UK pay distribution was dispersed; since then, the gap has widened further (see OECD, 1996, Table 3.1).

For much of the period from 1979, state benefits for workless individuals were indexed to prices. Thus, over a period where median real wages were rising, it should be no surprise that benefit increases did not greatly moderate the rise in relative poverty. During the 1990s, however, average real benefits did rise quite significantly, because of the operation of the housing benefit system. By and large, housing benefits can be thought of as indexed to rents. In-work benefits also became more generous in the

later 1990s and the trend continues, particularly for households with children.

Wage dispersion in the UK, already in 1979 higher than in much of northern Europe, has since increased substantially, both absolutely and relative to most OECD countries (the US being a notable exception). Analysis of this increase suggests that the increase in demand for skilled workers relative to unskilled, in the 1980s in particular, outstripped the increase in the supply of skilled workers, relative to unskilled.

While the relative demand for skilled workers has been rising in the UK, so has their relative supply. The outcome in the labour market in any period will depend on which side is winning the race. In the UK (and the US), the evidence suggests that the demand side was winning during the 1980s and the early 1990s (see Nickell and Layard, 1999, Table 24). In most of northern Europe, this was not the case. The consequence of the demand side winning was that, *relative to supply*, the demand for skilled workers was rising and the demand for unskilled workers was falling. The

Figure 1. Real Wages in Britain for Males Working at Least Half Time

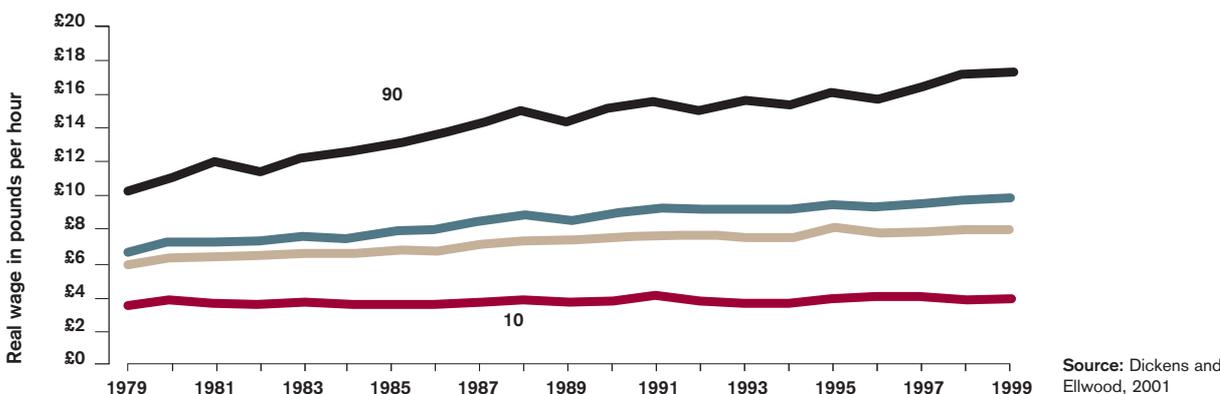
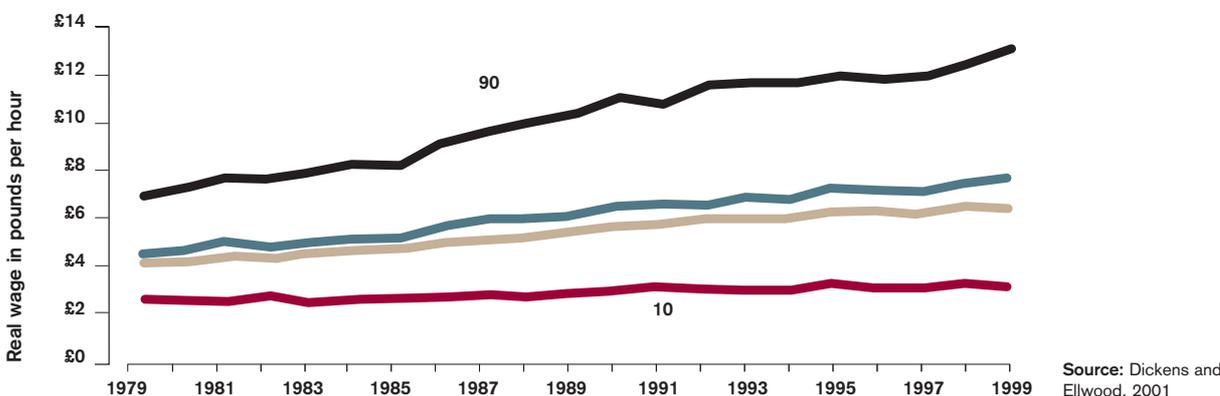


Figure 2. Real Wages in Britain for Females Working at Least Half Time



consequence was a weakening labour market for the unskilled with relative wages falling and jobs becoming harder to find.

This is a very simple story and additional factors may be important, notably the falling minimum wage (relative to the mean) in the United States in the 1980s and the decline in private sector unions in the UK over the same period. Some argue that the contrast between northern Europe and the UK/US is explained by the (in)famous European labour market institutions, which compress wages and raise unemployment among the low skilled. In fact, when unemployment rose in most European countries in the 1980s, it rose proportionately as much or more among the skilled as among the unskilled.

A particular feature in the UK exacerbated the decline in the unskilled labour market. The UK has a particularly large number of very low skill individuals. This is apparent for the whole adult population and there is no sign of any improvement in younger age groups (see Table 6). The comparison with the other north European countries is very telling and

suggests that, relative to the UK, their education systems have managed to raise a higher proportion of young people above a decent minimum threshold.

The disadvantage of the long tail in the UK skills distribution is that, when labour demand shifts towards those with higher skills, the problems this generates are going to be seriously exacerbated for the over 20% of the population of working age with very low skills.

Table 7 shows that the rise in male worklessness is not just concentrated among older men but has occurred among the prime aged as well. The patterns of increase are, however, different. For older men, the rise in inactivity was concentrated in the 1970s and 1980s, particularly following the recession of the early 1980s, but stopped in the 1990s. By contrast, for the prime aged, inactivity has continued to rise up to the present, despite the relatively buoyant labour market in the last eight years.

The weakening of the low skill labour market suggests that we might expect relatively larger increases in inactivity

**Table 6. Is Literacy Getting Better in the Adult Population?**

Age	Prose Literacy % in Level 1			Quantitative Literacy % in Level 1		
	16-25	26-35	36-45	16-25	26-35	36-45
US	23	20	19	26	20	18
Germany	9	12	14	4	5	6
UK	17	18	17	22	20	19
Netherlands	8	6	9	8	7	10
Sweden	4	5	7	5	4	7

Source: OECD (1997).  
Note: Level 1 is the lowest of five and close to functional illiteracy. The levels are based on tests as part of the Adult Literacy Survey in many OECD countries in the mid-1990s.

**Table 7. Inactivity Rates of Men (%), 1972-2002**

Ages	25-54			55-64		
	GHS	LFS	LFS (ILO)	GHS	LFS	LFS (ILO)
1972-76	1.6	1.1		11.9	9.1	
1977-78	2.1	2.0		14.2	14.2	
1979-81	2.6	2.5		18.7	18.2	
1982-86	3.4	4.7		28.3	31.1	
1987-91	4.0	5.7		32.4	33.1	
1992-96	5.9	5.7	6.9	37.7	35.3	36.0
1997-99	7.9	7.2	8.3	39.9	36.0	36.6
2000-01	8.1	7.4	8.5	38.9	35.2	35.7
2002		7.5	8.6		34.5	35.0

**Notes:**

- (i) GHS is the General Household Survey, LFS is the Labour Force Survey.
- (ii) Data are available as follows: GHS, 72-96, 98, 2000. LHS, 75, 77, 79, 81, 83-2002. LFS (ILO), 92-2002.
- (iii) The inactive are those who are not working and not unemployed. LF unemployed are those without a job who are (a) looking for work in the reference week or (b) prevented from seeking work by temporary sickness or holiday or (c) waiting to start a job or (d) waiting for the results of a job application. ILO unemployed are those without a job who are available to start work in two weeks and (a) have looked for work in the previous four weeks or (b) are waiting to start a job.
- (iv) The GHS uses the LF definition up to 1996, the ILO definition in 98, 2000. The LFS series uses the LF definition. The LFS (ILO) series used the ILO definition.

**There is a strong connection between low pay and worklessness**

**Table 8. Inactivity Rates for Men in and Outside the Bottom Skill Quartile (%), 1972-2002**

Ages	25-54				55-64			
	GHS		LFS		GHS		LFS	
	BSQ	NBSQ	BSQ	NBSQ	BSQ	NBSQ	BSQ	NBSQ
1972-76	2.2	1.4			12.7	11.6		
1977-78	2.9	1.8			14.9	14.0		
1979-81	3.5	2.3	4.3	1.9	20.7	18.0		
1982-86	5.8	2.6	7.4	3.8	30.9	27.4	33.0	30.5
1987-91	8.1	2.6	9.6	4.4	36.6	31.0	37.8	31.5
1992-96	11.7	4.0	13.4	3.1	42.4	36.1	43.4	32.6
1997-99	15.4	5.4	17.7	3.7	50.6	36.3	47.4	32.1
2000-01	15.8	5.5	18.1	3.8	45.4	36.7	48.0	30.9
2002			18.8	3.7			47.6	30.1

**Notes:**

- (i) As in Table 7.
- (ii) BSQ (the bottom skill quartile) is based on educational qualifications. Until the early 1990s, those in the bottom skill quartile are a subset of those without qualifications. Later, those without qualifications are less than 25% of prime age men. So the bottom quartile also includes some proportion of the next education group, i.e. those with some GCSEs. NBSQ represents those outside the bottom skill quartile.

**Table 9. % of Men Affected by Chronic Illness**

Ages	25-54		25-54		55-64	
	LLSI	LHPD	LLSI	LHPD	LLSI	LHPD
1972-76	15.0		11.2		28.1	
1979-81	18.7		14.7		32.8	
1982-86	18.2	12.7	14.0	8.7	33.2	27.1
1987-91	19.0	14.8	14.8	10.4	35.0	31.8
1992-96	20.0	16.5	16.2	12.2	35.5	34.3
1997-99	20.0	17.0	16.6	13.3	33.6	36.6
2000-01	18.9	18.5	15.0	14.6	32.9	37.3
2002		18.1		14.1		36.3

**Notes:**

- (i) As in Table 7.
- (ii) LLSI refers to a limiting long-standing illness. This is reported in the GHS, where people are asked if they suffer from a long-standing illness that limits things that they would normally do. LHPD refers to a limiting health problem or disability. This is reported in the LFS and refers to a health problem or disability that affects the kind of work the person does.
- (iii) The GHS failed to ask a consistent question of this type in 1977-78. The LFS question was changed in 1997 and we have made some slight adjustment to the data post-1997 to correct for this.

**There has been a significant rise in inactivity among men of working age**



among unskilled men. Table 8 shows that this is indeed the case, particularly for prime age men. Among the older age group, the higher skill groups have access to good early retirement packages. The consequence of these changes is that some 50 to 60% of inactive prime age men are now in the bottom skill quartile. Furthermore, the relative situation of the low skilled has worsened substantially since the 1970s. Indeed, since the early 1980s there has been no increase in prime age inactivity among those outside the bottom skill quartile, whereas the inactivity rates of the low skilled have risen over 2½ times.

Inactive men over the age of 25 report themselves as being in one of four major categories: full-time student; looking after family; early retired; and sick or disabled. In the prime age group, around 70% of the inactive report themselves as sick or disabled. In the older age group, the equivalent figure is over 50%, with another 35% being early retired. So “disability” is a key factor in understanding the rise in male inactivity.

To pursue this, we must first find out how many people report themselves as chronically ill. In Table 9, we see that just under 20% of men aged between 25 and 64 report themselves as having a limiting long-standing illness (LLSI), with around 18% reporting a limiting health problem or disability (LHPD). This difference appears to be systematic among the prime aged, perhaps because, in the case of LLSI, the illness limits “things people normally do”, whereas with LHPD the illness limits “the kind of work the person does”.

Table 9 shows that the proportion reporting LLSI has not risen systematically since the late 1970s. By contrast, the numbers reporting LHPD have risen steadily. The different patterns of incidence observed for LLSI and LHPD may, perhaps, arise because LLSI is less responsive to a decline in labour demand than LHPD, which directly refers to work. Either way, what is absolutely clear is that the rise in self-reported illness or disability in the 1980s and 1990s is relatively small compared with the rises in inactivity.

In the light of this, is the typical person with an LLSI or an LHPD inactive? The short answer is no. As we can see from Table 10, the majority of prime age men with a limiting illness or disability are economically active. However, whereas in the 1970s a mere 10% of this group were inactive, by the late 1990s this number had risen to around 35% (LLSI) or 43% (LHPD). Inactivity among prime age men without an LLSI has also risen, but among those without an LHPD there has been no significant change since the early 1980s.

If we use these data, plus changes in the incidence of long-standing illness in the working age population (Table 9), we can work out what proportion of the dramatic rise in inactivity among prime age men is “explained” by the rise in inactivity among those with a limiting illness or disability. The answer is that around 70% of the rise in prime age male inactivity since the 1970s can be accounted for by rising inactivity among those with an LLSI and that more or less *all* the rise since the 1980s can be accounted for by rising inactivity among those with an LHPD.

Among older workers, the situation is different, with around half the rise in inactivity since the 1970s “explained” by rising inactivity among those without any reported limiting illness. This expanding group would tend to report themselves as inactive because of early retirement rather than because of sickness or disability. They would consist mainly of occupational pensioners taking early retirement (i.e. prior to age 65), an option widely available, particularly in public sector occupations (e.g. teachers, doctors, police, civil servants).

The question, however, arises as to why all this rise in non-employment has been so heavily focussed on inactivity as opposed to unemployment? For example, the unemployment rate among those without qualifications fell from 19% in the early 1980s to around 12% in the late 1990s, whereas the inactivity rate among the same group rose by a multiple of around three.

**Table 10. Inactivity Rates Among Men (%)**

Ages	25-54				55-64			
	With		Without		With		Without	
	LLSI	LHPD	LLSI	LHPD	LLSI	LHPD	LLSI	LHPD
1972-76	10.0		0.4		32.0		4.0	
1979-81	11.9		0.7		39.7		8.4	
1982-86	15.9	28.8	1.2	1.9	53.4	66.6	16.4	18.4
1987-91	19.2	28.5	1.3	1.5	59.1	65.0	18.6	16.6
1992-96	26.3	36.3	1.8	1.5	66.0	68.6	23.2	17.7
1997-99	33.8	43.1	2.8	1.9	64.6	72.8	29.6	18.5
2000-01	34.5	41.8	3.2	2.0	70.9	70.2	25.1	18.7
2002		43.6		2.1		70.2		18.3

**Notes:** See the notes to Tables 7 and 9. LLSI is a limiting long-standing illness. LHPD is a limiting health problem or disability.

To answer this question, let us first consider another. Given the weakening labour market for the low skilled, which group would one expect to be particularly badly hit? A plausible answer is that it would be the group that has an additional disadvantage, namely those who suffer, or potentially suffer, from a long-term illness or disability, which limits the sort of work they can do.

The story would then proceed as follows. Back in the early 1970s, even the men in this group with low skills did not tend to withdraw from the labour force. Around 87% of men in this category were economically active at that time. However, they did find it harder to get work. Back in the 1970s, those with a long-term illness or disability were three times as likely to be unemployed as the remainder of the work force. So, once the low skill labour market started to weaken, those unskilled men with an actual or potential chronic illness or disability were particularly badly hit. Because the low skill group found it much harder to get work, those operating the social security system found it much easier to shift them onto incapacity or invalidity benefit. Further, doctors, whose certification was required for benefit entitlement, were influenced by their assessment of the probability of patients finding a job.

These might be termed "push" factors, forcing men into inactivity. "Pull" factors include the fact that invalidity benefits were considerably higher than those available to the unemployed. This gap increased from the mid-1980s to the mid-1990s, before falling back in the later 1990s. This occurred because of the operation of the Additional Pension system, an earnings related supplement to invalidity benefit.

Another factor on the "pull" side is the fact that, once in the invalidity or incapacity benefit system, the pressure to take up work is minimal. For example, Beatty and Fothergill (1999) report that, in their survey of working age men who had not worked for six months, only 5% of those reporting themselves as long-term sick were looking for a job. The upshot of all this was that the number of male invalidity benefit claimants doubled from the early 1980s to the mid-1990s.

It is clear from our discussion that public policy can be used

to reduce significantly and, indeed, eliminate poverty. To achieve this, people in poverty must earn more, work more or receive higher transfers.

"Earning more" centres on the longer term issue of education and the shorter term question of low pay. With education, the key problem is how to eliminate the long tail in the skill distribution. From Table 11, we see that public expenditure on education in the UK has fallen substantially since the mid-1970s, reaching a minimum in the late 1990s. We know also that the relative pay of schoolteachers fell significantly over the same period and there is some evidence of a decline in quality among new entrants to the profession.

Against this rather gloomy background, increased expenditure on schools is necessary. This is happening, but recent research indicates that it is far from sufficient. First, in order to attack the long tail problem, employing the best teachers and heads in the poorest schools would seem sensible. This would, of course, require significant financial incentives.

Second, curriculum and teaching policy must follow the evidence. For example, literacy and numeracy hours appear to have had some success in reducing dispersion in skill levels at the primary school stage (see Table 12). However, the Improving Primary Mathematics project, initiated in Barking and Dagenham by researchers at the National Institute for Economic and Social Research, indicates that things could easily be a lot better. The methods used, based on those current in Switzerland, can generate substantial improvements in primary school mathematics attainment even in the poorest schools. Third, a lot of evidence suggests that heads are crucial to success and failure in schools. The conclusions to be drawn from this are obvious.

While education is the key policy area for attacking poverty in the long run, what are we to do in the mean time? The obvious short-run method of raising pre-tax earnings is to pass laws to prevent low pay. These may be in the form of minimum wage or fair wage legislation. The obvious potential danger here is that this will cut the employment of the

## The number of male invalidity benefit claims has doubled

**Table 11. Public Expenditure on Education in the UK (% of GDP)**

	Public	Total
1975-9	6.02	6.42
1980-4	5.40	5.90
1985-9	4.88	5.36
1990-4	5.02	5.72
1995-9	4.90	5.94
2000-3	5.03	

**Source:** Glennerster (2002), Table 1. 1998-2000 were the years with the lowest public expenditure in the last quarter of the 20th Century (4.5% of GDP).

**Table 12. Scores of Schools 1995-2000,  
Maintained Schools Key Stage 2:11 years, Level 4+**

	% Reaching Expected Levels			
	1995	1997	1999	2000
<b>Maths</b>				
75th percentile	63	78	83	85
median	47	65	72	74
25th percentile	31	50	59	60
<b>English</b>				
75th percentile	65	78	84	88
median	50	67	73	78
25th percentile	35	52	61	64

Source: Glennerster (2002), Table 5.

low skilled, thereby raising worklessness and poverty from another direction. While simple economics suggests that raising wages above the equilibrium level will reduce employment, this is not necessarily the case. For example, low pay establishments, such as fast food outlets, often operate with very high turnover and a permanent level of vacancies. Under these circumstances, a forced increase in pay could even raise employment.

The introduction of the National Minimum Wage in the UK in 1999 appears to have generated little overall job loss. Machin et al. (2002), in a "before" and "after" analysis of UK care homes, discover some evidence of employment and hours reductions as a result of the minimum wage. In this sector, minimum wages had a substantial impact on the wage structure because around a third of workers were paid below the minimum level prior to its introduction. Relative to this, the employment effects were small.

Overall, however, the impact on employment seems to have been minimal. This suggests that the best policy should be of the "suck it and see" type. The statutory wage floor should be raised slowly, relative to the general level of wages, until employment effects become noticeable. To some extent, this is indeed the existing policy where, from 1999 to 2004, the rise in the National Minimum Wage from £3.60 to £4.80 per hour represents a rise of around 5.7% per annum, slightly higher than the rate of increase of average earnings. However, a somewhat faster rate of relative increase would probably be safe on the employment front and have more of an impact on low pay.

What about "working more"? Dickens and Ellwood (2001) calculate that, if work patterns returned to the 1979 level and if work were made to pay enough so that no child living in a household with at least one full-time worker was poor, then child poverty would fall by 60%. So the combination of increased work and take-home pay is potentially very effective in reducing poverty. Both "push" and "pull" policies are relevant here.

The standard push policy used in the UK is the New Deal, combined with Job Centre Plus. The idea here is to provide a strategy for each individual in the target group that leads on to some form of training, job search assistance, subsidised employment and so on. This job finding process is integrated with the benefit system so that each individual has a single personal adviser who will deal with all work, benefit and related issues. The process also includes the possibility of benefit sanctions for individuals who fail to participate in the programme or turn down suitable employment.

The workless groups in the UK for whom New Deals are available include young people (18-24) who have been out of work for 6 months, adults (25-59) who have been out of work for 18 months, over 50s who have been on any benefit for 6 months, the disabled and single parents. The schemes are compulsory for the first two groups. The New Deal for young people started in January 1998 and evaluations published so far indicate that it has generated 20,000 extra jobs each year and has significantly reduced unemployment rates among young persons. Furthermore, there is no evidence as yet of a significant adverse impact on the labour market prospects of groups outside the programme.

The standard policy of the pull type is the tax credit. This is essentially an in-work benefit or pay top up that depends on family circumstances. Such a policy raises both employment and take-home pay for the target group. For any given policy, the bigger the employment effect, the smaller the take-home pay effect and the size of the former will depend on the extent to which pre-tax pay falls in response to the increase in labour supply. By and large, if tax credits are focussed on individuals whose pay is at or near the wage floor (minimum wage or minimum union rate), the employment effect will be small and the take-home pay effect correspondingly large.

In the UK, the Working Families Tax Credit (WFTC) was fully phased in from April 2000, replacing Family Credit

(FC), a benefit paid to low earners with dependent children. The WFTC was substantially more generous than FC, increasing both credits for younger children and the threshold as well as reducing the withdrawal rate. Furthermore, it included a new childcare credit. While the overall employment effects appear to have been small, when combined with the tight labour market, it has helped raise the employment rate among lone parents, which is now over 50% (up from 38% in 1993). However, the major gain from WFTC and its successor tax credits has been their contribution to reducing child poverty without negative labour supply effects. From 1996/7 to 2000/1, child poverty fell by around 3.5 percentage points, with the WFTC making a significant contribution to this reduction.

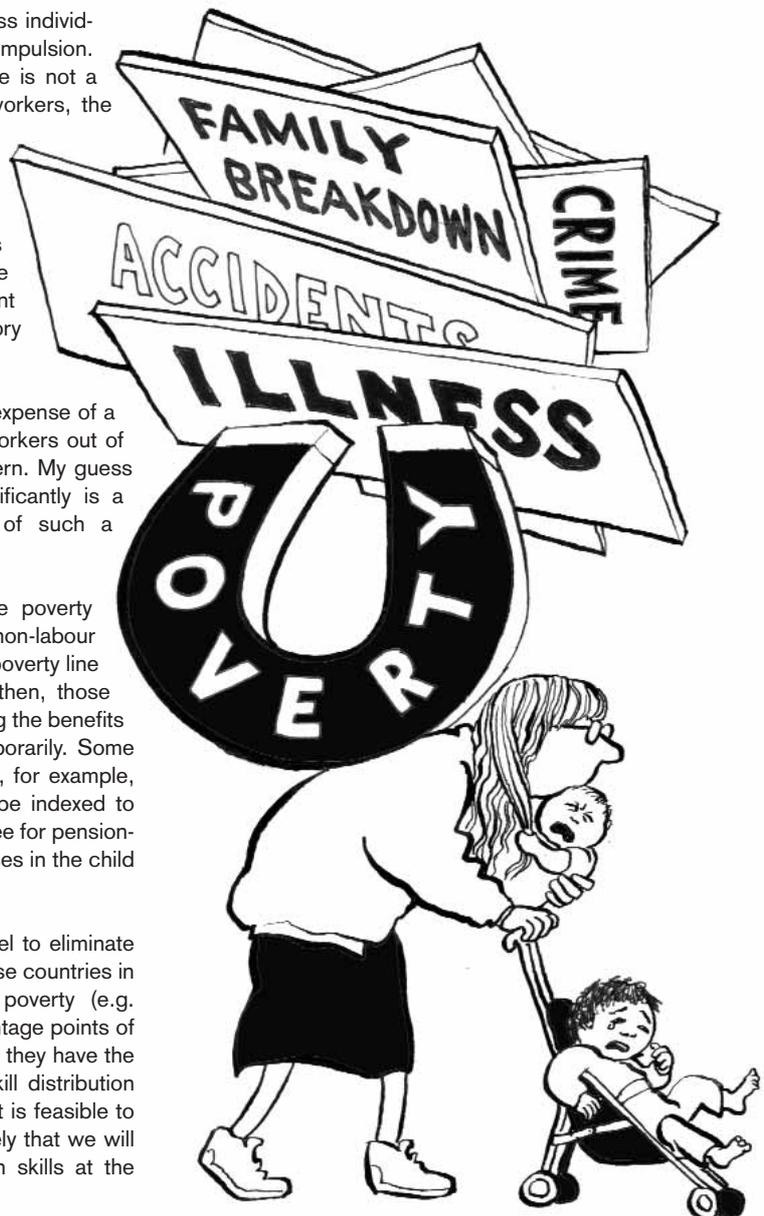
## The National Minimum Wage appears to have generated little overall job loss

The basic issue with policies to push workless individuals into employment is the extent of compulsion. Currently, entry into a New Deal programme is not a condition for receipt of benefits for older workers, the disabled and lone parents. This is related to the fundamental question of who in society is expected to work and who is allowed to receive benefits without looking for a job. Not surprisingly, this topic arouses great passions and a great deal more could be done to smooth the path of older, lone parent and disabled benefit recipients into satisfactory employment.

The basic issue with in-work benefits is the expense of a fully comprehensive system that will lift all workers out of poverty, given the UK's skill distribution pattern. My guess is that cutting the long low skills tail significantly is a necessary condition for the introduction of such a generous system in the UK.

It remains a fact, though, that to eliminate poverty among those without alternative sources of non-labour income benefits will have to be raised to the poverty line and then indexed to median wages. Even then, those who, for one reason or another, are not getting the benefits will typically remain in poverty, at least temporarily. Some elements of this policy are being introduced, for example, part of the new Child Tax Credit is set to be indexed to earnings, as is the Minimum Income Guarantee for pensioners. Also, there have been substantial increases in the child elements of the benefit system.

Overall, however, to have benefits at the level to eliminate poverty would be enormously expensive. Those countries in northern Europe with very low levels of poverty (e.g. Denmark, Sweden) collect at least 10 percentage points of GDP more in taxes than we do in the UK and they have the advantages of much shorter tails to their skill distribution and higher overall employment rates. While it is feasible to move further in that direction, it seems unlikely that we will get far without a significant improvement in skills at the bottom end.



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This article is an edited version of his paper "Poverty and Worklessness in Britain", (CEP Discussion Paper No. 579), which was his Presidential Address to the Royal Economic Society.

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