

Joblessness among the UK's younger generation is currently at very high levels, but the rise in youth unemployment began in 2004, well before the onset of recession. **Barbara Petrongolo** and **John Van Reenen** consider potential explanations.

Youth unemployment

The UK economy has experienced the worst recession since the war in terms of loss of output, yet the overall unemployment rate is 8%, lower than the peak of the 1980s and 1990s recessions. Youth unemployment, however, has risen dramatically, and because of the 'scarring' effects of joblessness on an individual's later life, has become a key policy concern. But to tackle the problem, it is important to understand how youth unemployment typically responds to a cyclical downturn and why, this time, it started to rise well before the recession began.

Figure 1 shows the unemployment rates for the working age population (people aged 16 to 64) and for three subgroups – prime age (25-49), young (18-24) and teenagers (16-17). The prime age group follows the general pattern of the aggregate labour market, but it is clear that the young are much more sensitive to the state of the business cycle. The unemployment rate is higher for the younger groups and the magnitude of this disadvantage widens during a recession.

This is unsurprising as employers will be reluctant to lose more experienced workers who have firm-specific skills and greater redundancy costs. So the burden of adjustment typically falls on low-wage workers such as young people. Minorities

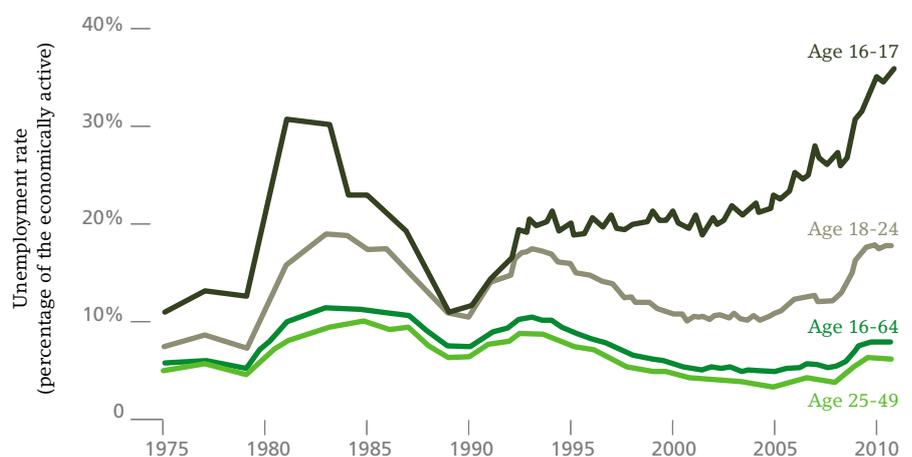
and the less educated also tend to fare worse during downturns.

The fact that teenagers do not appear to have experienced the same fall in unemployment after the 1990s recession as older groups can be explained by important concealed 'selection effects' as increasing numbers of teenagers without jobs stay in education. Indeed, if instead of focusing on unemployment figures we use information on the proportion of young people who are 'not in employment, education or training' (NEETs), the trend for 18-24 year olds is very similar to the trend in unemployment, while there has been a decline in the 16-17 year olds NEET rate.

Has the latest recession hit young people much worse than in the past? Figure 1 shows that the unemployment rate for the young has increased by more (in absolute terms) than the unemployment rate for older groups since the onset of the recession. Moreover, there has been a significant fall in hours worked by young people compared with older groups, while wages have flattened or fallen for younger workers. Both of these facts indicate that young people are faring worse during the downturn than other groups.

But it could be said that this has been the general pattern in all recessions. The

Figure 1:
Unemployment rates by age group, 1975-2010



Source: Labour Force Survey (annual data 1975-91, quarterly data 1992-2010)



unemployment rate for young people is about the same as at its 1990s peak and better than the 1980s peak, despite the fall in GDP being deeper. (The higher absolute number of young unemployed is due to the larger labour force and so is not really a relevant comparison.) The growth in youth unemployment relative to prime age unemployment in this recession looks no worse than in previous recessions. In fact, if anything, it looks slightly better.

So the data do not suggest that there is a special problem of youth unemployment in this recession compared with past experience. The fact that young people suffer more during downturns is quite consistent with what has happened in previous recessions in the UK and elsewhere. A bigger problem is what was happening before the recession.

Figure 1 shows that prime age unemployment has been falling dramatically since the early 1990s, and then rose again in 2008. Youth unemployment had also been falling since the early 1990s, and by 2004 it had dropped to about 9%, below its 1989 level. But then it started rising in 2004, several years in advance of the recession.

So there seems to be a component of the differential between adult and youth unemployment that is not explained purely by the stronger impact of cyclical downturns on young people. Despite several forces that may be related to the poor performance of the youth labour market in recent years, the bulk of the rise in youth unemployment in the period 2004-08 remains largely unexplained. What might be behind this increase? We look at six possible culprits.

Rising migration

As the rise in youth unemployment dates back to 2004, the year of the European Union's enlargement to take in eight Central and Eastern European countries

(plus Cyprus and Malta), it would be natural to think that the increase in youth unemployment is related to stronger competition from immigrant labour.

The UK has experienced a record increase in immigration in the past few years. The proportion of foreign-born population was below 6% in the early 1990s, but is currently about 10%. In London, this proportion rose from 28% to the current level of around 40%. Those immigrants who are less skilled than natives will be closer substitutes for inexperienced young people and may hurt young people more than adults.

Some simple evidence on this can be provided by looking at the correlation between youth unemployment and the migration rate across UK regions over time, controlling for the business cycle. Evidence shows that a one percentage point increase in the proportion of foreign-born in the working age population is associated with an increase in youth unemployment of 0.43 percentage points, holding the state of the business cycle constant.

So it might be concluded that foreign migration harms the job prospects of young people. But this result is largely driven by differences between London and the rest of the country, as the capital experienced particularly high rates of immigration and a relatively higher increase in unemployment. Excluding London from the sample, the correlation between youth unemployment and the migration rate is basically zero.

It could be argued that the simple correlation underestimates the impact of

migration, as immigrants will go to areas where the labour market is strong. But we suspect that other factors may explain this correlation. Consistent with research showing that immigrants do not seem to have large harmful effects on the labour market outcomes of natives overall (for example, Card, 2005), there is no compelling evidence of a strong causal impact of higher migration on youth unemployment.

Changing structure of welfare-to-work benefits

The poor showing of the youth labour market since 2004 is particularly disappointing given the considerable policy reform to the Employment Service (especially for young people) in the last two decades. Jobseeker's Allowance (JSA) was introduced in 1996 as the main form of unemployment benefit and greatly increased the job search requirements for receiving benefits. Although it appeared to reduce the claimant count, few of those leaving seemed to find sustainable jobs: not only did JSA not seem to improve the overall employment rate significantly (Manning, 2009), it may even have reduced it for the young (Petrongolo, 2009).

While the claimant count and unemployment as measured by the Labour Force Survey (LFS) were very close until October 1996 for people over 18, LFS unemployment (which includes people who report that they are looking for a job but not finding one) remained well above the claimant count in the post-JSA period. Thus there is evidence of increasing

Compared with the 1980s and 1990s recessions, young people have not done particularly badly in the latest recession

The unemployment rate is higher for younger age groups and this disadvantage typically widens during a recession

numbers of workers who left the unemployment register but did not find jobs. About half of the 18-24 LFS unemployed do not claim JSA (compared with a third of 25-49 year olds). When dropping out of the welfare system, individuals may become more detached from the labour market and spend less effort on job search.

The second policy, the New Deal for Young People, was introduced in 1998 with the aim of improving the incentives for young workers to find jobs. All 18-24 year olds on JSA for six months received help with job search from a dedicated personal adviser. So there was some 'carrot' of job search assistance as well as a tougher 'stick' of stricter monitoring. This seemed to be successful, rigorous evaluations showing that job finding rates increased by about 20% as a result of the policy (Blundell et al, 2004; De Giorgi, 2005).

But this success was possibly undermined when around 2004, the Employment Service was given incentives to focus less on young people on JSA and relatively more on other groups, such as lone parents and those on incapacity benefits. Although there is no rigorous evaluation of this change, the timing does suggest that this may have been a cause of the rise in youth unemployment before the recession.

A further problem is that the increasing numbers of LFS unemployed who are not claiming JSA separate them from any direct effect of the New Deal and the Employment Service in general. There is no way for the state to give direct help to young unemployed people who have little contact with the job finding agencies. An extreme example of this is 16-17 year olds who are not eligible for JSA so will not need to have any direct contact with the Employment Service.

The minimum wage

Is the National Minimum Wage another cause of increased youth unemployment? Although its extension in October 2004 to cover 16-17 year olds who are not apprentices did coincide with a strong increase in their unemployment rate, research has generally found few effects of the wage floor on jobs (Machin et al, 2003; Stewart, 2004a, 2004b). For example, the 2003 increase in the minimum wage had insignificant employment effects for all demographic groups including young people (Dickens and Draca, 2005).

Furthermore, if minimum wages were to blame, we would expect a positive jobs effect on teenage apprentices, who were exempt from the 2004 legislation. In fact the job rates of 16-17 year olds fell from 15% in early 2003 to 13% in early 2007, casting doubt on the minimum wage explanation.

Cohort size

Increases in the size of the youth cohort can increase competition for jobs and, by placing downward pressure on wages, make employment less attractive. In fact, the share of 18-24 year olds in the working age population fell through to 2000, but then rose from 13% to 14.6% by 2009. This roughly coincides with the fall and rise of unemployment.

Our analysis shows that this 1.6 percentage point increase in cohort size could have increased male youth unemployment by about a quarter of a percentage point. So this is unlikely to be the major cause of the increase.

Falling demand for low-skilled workers

There has been a large increase in UK wage inequality over the last three decades. The wage premium for being educated has risen despite a huge increase in the supply of college-educated workers,



which implies that there has been an increase in the demand for skills.

This is probably due to new 'skill-biased' technologies, but trade with less developed countries like China and India may also play some role in reducing demand for unskilled workers. There are similar rises in the relative demand for skills in the United States and other countries (Machin and Van Reenen, 2008).

A rise in demand for human capital may disproportionately hurt the young because they have less experience. But this explanation is not so persuasive for explaining the post-2004 changes, as youth unemployment was falling in the period 1992-2004 (and for parts of the 1980s) even in the face of this rising demand for skill. Thus, although skill-biased technical change has a lot to do with longer-run trends in wage inequality, it is not a good explanation for the rise in youth unemployment after 2004.

Education and school-to-work transitions

Another possible explanation is that the quality of education for the type of young people likely to be unemployed may have declined. Although standards as a whole appear to be rising, it is possible that targets have led schools to neglect some of the 'hard to reach', who may end up unemployed. For example, an evaluation of the Excellence in Cities programme in disadvantaged areas finds that the policy had a relatively high impact on high ability pupils in poor schools, but it did not help low ability pupils, who may have higher unemployment risk in the future (Machin et al, 2010).

Similarly, the publication of league tables gives schools incentives to focus on pupils at the margin of achieving the headline indicator (the percentage with five or more A*-Cs at GCSE) but few incentives to focus on those near the bottom of the distribution (Wilson et al,



2006). It is thus important that education policies do not neglect the bottom of the ability distribution, which is often hard to reach. More generally, improving the careers guidance service for school leavers could be a way of improving the position of young people.

Conclusions

The UK labour market has held up relatively well so far, given the depth of the latest recession. Young people, however, have fared much worse than other groups with larger increases in unemployment and bigger falls in hours and wages. Unfortunately, this is to be expected as young people always suffer worst during downturns.

More puzzling, however, is the fact that youth unemployment and NEET rates were already bad going into the recession, having been rising since 2004. The evidence gathered to date does not provide a firm answer to why, after over a decade of steady improvement, youth unemployment started rising in the mid-2000s.

With youth unemployment currently around 18%, policy actions will be key to reducing the threat of large numbers of young people facing long-term unemployment and the lifetime scars that leaves. In particular, it is important to maintain strong welfare-to-work policies that keep young people attached to the labour market, and to ease the transition from school to work with apprenticeship programmes targeted at low-achieving groups that are typically 'harder to reach'. But there is no evidence that caps on immigrant flows or a reduction in the minimum wage would have a strong bite on the youth labour market.

Further reading

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Mark Stewart (2004a) 'The Impact of the Introduction of the UK Minimum Wage on the Employment Probabilities of Low-wage Workers', *Journal of the European Economic Association* 2: 67-97

Mark Stewart (2004b) 'The Employment Effects of the National Minimum Wage', *Economic Journal* 114: C110-16

Deborah Wilson, Bronwyn Croxson and Adele Atkinson (2006) 'What Gets Measured Gets Done', *Policy Studies* 27(2): 153-71

Immigration, the minimum wage and changing demand for skills do not seem to be to blame for the rise in youth unemployment