

Economic Development and Transport Committee Paper Paper 3

**Date:** 22 October 2003  
**Venue:** Committee Room 1  
**Title:** Raising levels of economic activity

**Purpose**

Helping more people into jobs is one of the big issues highlighted in “Wales: A Better Country”. It links strongly with the need to tackle social deprivation and to improve health and complements the need to create better quality jobs in Wales. Officials are working to analyse the issues and identify what further action can be taken to make more progress in this direction. The purpose of this paper is to share with the Committee the work in progress.

**Summary**

Rates of economic activity in Wales have historically been lower than in England. However there have been recent rises in the numbers of people employed – and rates of both unemployment and inactivity have been falling faster than any other part of the UK.

**Background**

The most recent figures available, show that economic inactivity has been falling both in absolute terms, and relative to the UK levels. In the three months to July 2003, the inactivity rate in Wales, as measured by the Labour Force Survey, was 23.6 per cent of the working age population. This represents a **fall** of 3.3 percentage points since the same period in the previous year. This represented the biggest year-on-year reduction out of all the devolved countries and English regions and narrows the gap between Wales and the UK by half over the last year. Wales now has a higher working age employment rate than most EU countries.

**Consideration**

The attached analysis was recently prepared for Ministers and suggests that the main causes of growth of economic inactivity over recent decades prior to the recent sharp improvement has been:

- The weakening of the demand for unskilled labour across the developed world.
- People who are both low skilled **and** face the additional disadvantage of a work-limiting illness may have been particularly badly hit by this shift in demand.
- The consequences of the fall in demand for unskilled workers seem to have been particularly severe in the UK because of the existence of a long tail of very low-skill individuals compared to other advanced economies (even including the US).
- Inactivity has remained prevalent because those on benefits and inactive are not generally looking for work (although around one third would like to work) and the financial incentives may be weaker for those on higher rate benefits.

There are a number of very successful programmes that are making a significant impact in helping people through the transition from economic inactivity into jobs:

- ◆ The Department for Work and Pensions (DWP) run a number of voluntary New Deal programmes through Jobcentre Plus. Those in Wales have been particularly successful. DWP is about to launch the pilot programme Pathways to Work in Rhondda Cynon Taff and Bridgend aimed particularly at helping those who have a limiting long-term illness.
- ◆ This is complemented by a range of targeted measures aimed at improving both general and occupational health for specific groups.
- ◆ There are a number of successful childcare initiatives, funded through Cymorth, which pump-prime childcare places and are targeted at particularly deprived areas.
- ◆ School attainment figures are continuing to rise and the gap with England has almost closed.
- ◆ Our Communities First programmes are reaching out to the most deprived communities.
- ◆ There are a range of specific initiatives to overcome transport barriers run by Jobcentre Plus and local authorities.

Recent rises in economic activity levels indicate that real progress is being made but we are committed to doing more to help those people currently inactive who want to work. Officials are assessing the scope for additional action using EU structural funds where possible, and in particular are discussing with Jobcentre Plus whether action might be taken to complement the Pathways to Work project using EU structural funds.

### **Financial Implications**

There are no immediate financial implications.

### **Action for Subject Committee**

The Committee is asked to note the analysis and is invited to discuss the issues raised.

**Andrew Davies**

**Minister for Economic Development and Transport**

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## **Annex A**

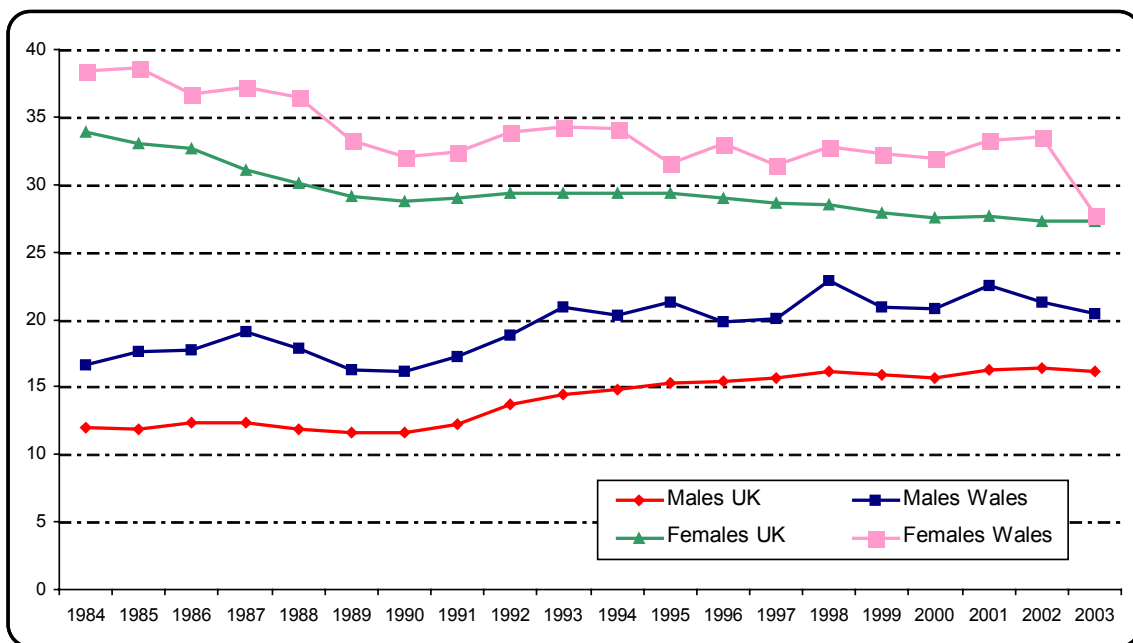
### **Raising Economic Activity Rates: Background Analysis**

1. Economic inactivity is a term used to describe people of working age who are neither in work nor unemployed. In other words, they are not working, not looking for work and/or not available for work.

#### ***Trends in economic activity in Wales***

2. Graph 1 shows the changes in inactivity rates for men and women over the past 20 years.

**Graph 1: Economic inactivity rates for people of working age by gender, Wales and UK 1984-2002**



3. The key points are as follows:

- Over the past 20 years, inactivity rates have risen amongst men, older men in particular, but have fallen amongst women. However, inactivity rates remain higher for women than for men both in Wales and across GB (except for Wales in the most recent period – but see below).
- GB figures show that the inactivity rate for people without qualifications has risen. We are investigating to see whether the same is true in Wales.

4. Over the last year, figures from the Labour Force Survey suggest a sharp rise in economic activity rates in Wales. The LFS reveals that most of this increase represents older women taking up work.

#### ***Economic inactivity in Wales***

5. Around one in four people of working age in Wales is officially economically inactive: this equated to 470,000 people of working age in 2001. It is important to recognise that many of

these people are very active in other ways, whether they are students, whether they are parenting, or caring for family members. In addition, some will be active economically in informal ways which are quite legitimate; for instance farmers' wives often play a very important role in the family business.

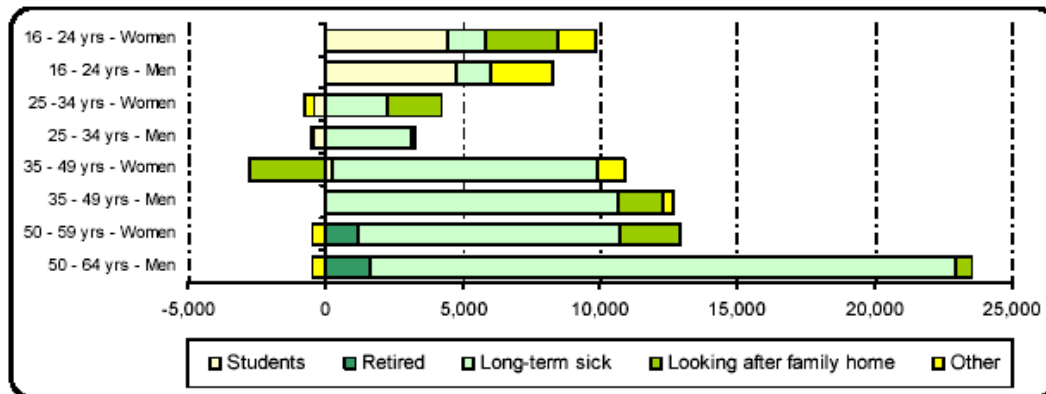
- The distribution of inactivity across gender and age groups is shown in table 1. As in other countries, in Wales more women than men are inactive. Inactivity follows a U-shaped pattern across age groups. Amongst younger people, inactivity is overwhelmingly caused by participation in higher education, while for older people self-reported long-term sickness is the most likely cause.

**Table 1: economic inactivity by age and gender, 2001**

	Thousands			Percentage of population		
	Men	Women	Total	Men	Women	Total
16-19	33	34	66	42.2	44.7	43.4
20-24	20	30	50	22.2	35.6	28.7
25-29	8	22	30	9.1	27.1	17.8
30-39	19	55	75	9.0	26.6	17.7
40-49	27	49	77	14.2	25.2	19.7
50+	95	78	172	35.7	40.0	37.5
<b>Working age</b>	<b>202</b>	<b>268</b>	<b>470</b>	<b>21.8</b>	<b>32.0</b>	<b>26.6</b>

- Graph 2 shows the 'excess' inactivity in Wales, relative to the UK. Amongst older age groups, the striking feature of graph 1 is the large excess of people who are long-term sick. In particular, older men account for a large proportion of the excess inactive in Wales. For the 16-24 age group the main reason for inactivity is being a student.

**Graph 2: Inactivity: The 'excess' over UK average, by gender and reason**



Source: Annual Local Labour Force Survey

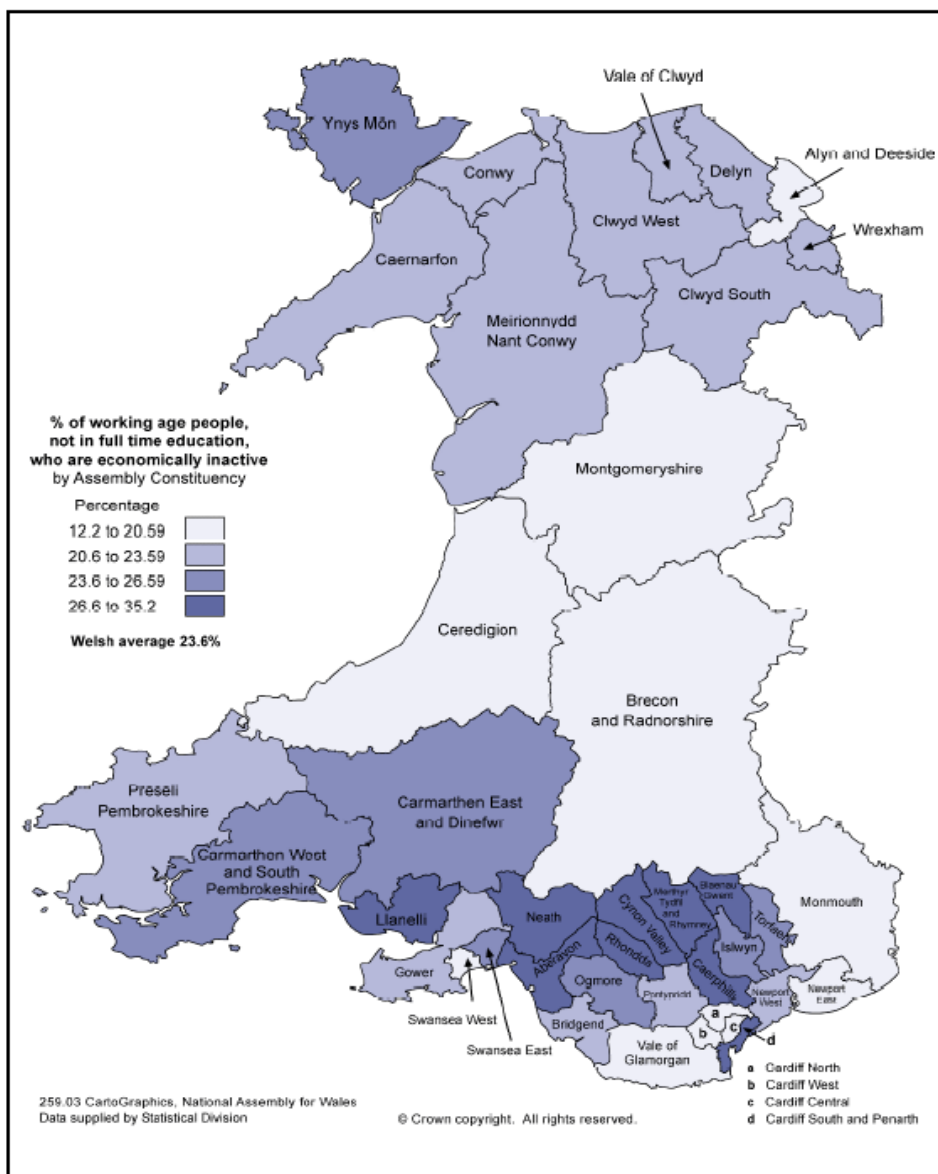
- Non-white ethnic minorities have lower rates of economic activity than whites, and the differences appear to be particularly acute for certain populations, although not large in absolute terms.
- Inactivity is more prevalent than unemployment: across Wales, the number of unemployed people of working age in 2001 was 72,000.

## Geographical distribution

10. In general, East Wales has lower inactivity rates than does West Wales and the Valleys. Powys has the lowest inactivity rate in Wales (17.4%). Excluding students, the highest inactivity rate in Wales is found in Merthyr Tydfil, where around one in three people of working age is economically inactive. As Map 1 shows, economic inactivity is concentrated in the more disadvantaged parts of Wales.

11. Overall, economic inactivity is concentrated on unskilled and older workers, and especially prevalent in the upper Valleys. The gap is greater for men than for women, and is disproportionately found amongst those who report a health problem.

**Map 1: Economic activity rates excluding those in FT education by Assembly constituency, 2001**



12. In most authorities, the main reasons given for economic inactivity are long-term sickness and looking after the family home. A higher incidence of long-term sickness is the main

difference between authorities with a high overall inactivity rate than those with the lower rates.

### **Why does this matter?**

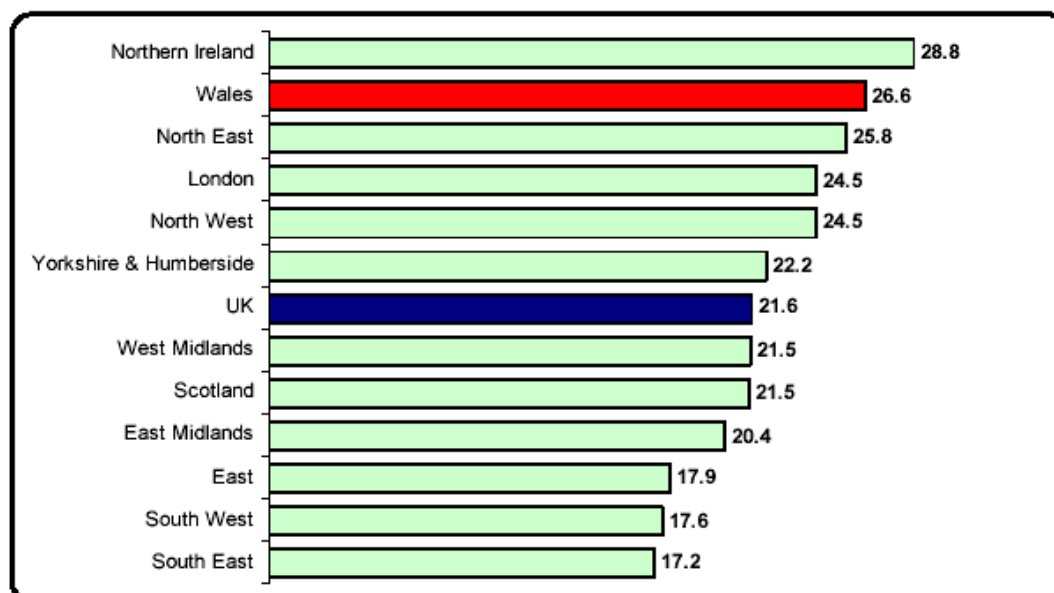
13. Lower employment rates, which are primarily related to lower rates of economic activity in Wales, are associated with relatively low GDP per head, concentrations of households where nobody works, and poverty. Raising activity rates is therefore central to poverty reduction and social inclusion, as well as to the economic development targets in 'A Winning Wales'.
14. International comparisons show that Wales has a high proportion of children growing up in workless households and the evidence suggests that this may have damaging long run consequences (including lower educational attainment, worse health and social problems).
15. The evidence suggests that getting a job is the best way out of poverty for individuals and their families. There is also substantial evidence that getting a job improves people's mental and physical health.

### **Comparison with rest of UK**

16. Within the UK, only Northern Ireland has a lower rate of economic activity than Wales (see graph 3).

**Graph 3. Economic activity rates for people of working age by region, 2001**

### **European comparisons**



Source: Annual Local Labour Force Survey

17. Aggregate inactivity rates in Wales are not high in comparison with the "big four" European economies of France, Germany, Italy and Spain, and are about the middle of pack for the EU-15 as a whole. But comparing with other EU members, Wales has higher inactivity rates for prime age men and younger women, and has higher rates of workless households. In other words, in France, Germany, Italy and Spain, economic inactivity is not associated in

the same way with poverty, and is for example more associated with middle-aged women working as housewives.

### ***Isn't the problem simply a legacy of heavy industry?***

18. The age profile does not suggest that the high male inactivity rate is simply the product of a cohort of people leaving heavy industry at the time of major closures in the 1980s. There is excess inactivity in all age groups and the bulk of the excess (in the 40-50 age group) would have been in their twenties at the time of the major shedding of labour in the early 80s. Women make up one third of the inactivity gap and did not work in these industries.
19. A survey of the inactive carried out in Wales in 1993/94 found that the distribution of industries in which the inactive were previously employed was very similar to that for the population as a whole. The majority reported having previously worked in service industries.

### ***So is the problem primarily one of ill health?***

20. Ill health is a problem in Wales, and particularly so in the Valleys, where inactivity rates are at their highest. This is confirmed by objective measures of illness such as life expectancy and morbidity rates. Many of the inactive in Wales report that they have health problems. Many are undoubtedly unable to work, and there is some evidence that there has been a fall in demand for workers who have health problems. However:

- Male inactivity rates have been rising at a time when objective measures of ill health have been improving.
- On many measures of ill health, Wales appears broadly similar to other regions of GB, yet has significantly higher rates of inactivity.
- It is accepted that the increase in incapacity benefit claimants during the late 1980s and early 1990s was driven partly by a desire to reduce headline unemployment figures (DWP). Across Britain, the number of people claiming IB has trebled since 1979 to 2.7 million, with the majority of this increase occurring before the mid 90s. Over the same period, there has been only a modest increase in the number of people who say they have a limiting longstanding illness from 15% to 19% of the working age population. This reflects the greater social acceptability of acknowledging a health problem, and is not enough to explain the large increase in numbers on benefit.
- Around a quarter of the inactive in Wales say that they would like a job, and some of these are actively looking for work. They are almost as likely to get work as people who are registered unemployed. For these people at least, their health problems do not seem to be a barrier to getting work.

21. The inactivity problem is therefore unlikely to be successfully addressed solely through measures aimed at improving health, even though such measures have a part to play.

### ***Simply not enough jobs?***

22. Across the UK, there does not seem to be a strong association between changes in unemployment, and changes in inactivity. If inactivity were mainly a form of 'hidden unemployment', then a fall (rise) in unemployment would be likely to occur alongside a fall (rise) in inactivity. Where there have been recent large falls in unemployment, these are not associated with similar falls in inactivity. If inactivity were mainly a form of 'hidden

unemployment', then a fall (or rise) in unemployment would be likely to occur alongside a fall (or rise) in inactivity.

23. This suggests that the causes of high levels of economic inactivity are more complex than a simple shortage of jobs. This is borne out by the picture within Wales. There are areas in Wales where very high levels of inactivity co-exist alongside a relatively buoyant local labour market. Some communities are short of jobs, and action is needed to help bring more jobs to communities with low levels of economic activity. But action on the demand and supply sides needs to go hand in hand; availability of jobs does not automatically make concentrations of inactivity disappear; and improving skill levels makes it easier to attract employment to an area.

### **Conclusions**

24. There is good economic evidence that the fundamental economic change underlying the growth in inactivity has been the weakening of the demand for unskilled labour across the developed world. This has occurred both as a result of a combination of technological change and increased competition from countries with a plentiful supply of unskilled labour<sup>1</sup>.
25. It is likely that people who were both low skilled **and** faced the additional disadvantage of a work-limiting illness were particularly badly hit by this shift in demand.
26. There is a general consensus that the consequences of the fall in demand for unskilled workers have been particularly severe in the UK because of the existence of a long tail of very low-skill individuals compared to other advanced economies (even including the US).
27. The collapse in demand for unskilled labour initially resulted in a sharp rise in unemployment, particularly concentrated in areas where unskilled workers were concentrated. However, the operation of the benefit system in the late 1980s and early 1990s provided incentives both to the state (which was keen to reduce headline unemployment figures) and to benefit claimants (who would receive higher benefits and minimal pressure to take up work) to move from unemployment and onto health-related benefits.
28. Under this analysis, the driving force behind the increase in male inactivity has been the substantial shift in labour demand away from low-skill workers which has outrun the shift in labour supply in the same direction. This particularly disadvantaged those low-skilled workers who were suffering from an actual or potential limiting illness or disability. When combined with the operation of the invalidity benefit system, the outcome was a dramatic rise in inactivity for this group. Despite recent falls in unemployment, this group has not been able to re-engage with the labour market; being out of work a long time is likely to damage a person's mental and physical health.

### ***And why is the problem so severe in Wales?***

29. A major part of the explanation of the inactivity problem is the skill profile of the Welsh population<sup>2</sup>. The available evidence suggests that the skills position in Wales is worse than

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<sup>1</sup> Note that there is in fact evidence of a rather more complex pattern than this summary account may suggest. Increases in the number of highly skilled jobs have been combined with a growth in the number of low skilled jobs in the service sector. But the net effect has been a reduction in the overall demand for low-skill and no-skill workers.

<sup>2</sup> although skills' levels are rising rapidly, 39% of working age adults in Wales have lower than level 2 NVQ (equivalent to 5 GCSE A\*-C); the proportion for 19 year olds is 25%.

in the UK as a whole, and that the position in the Valleys is worse than in the rest of Wales. The distribution of low skills therefore closely fits the distribution of inactivity across Wales, which is consistent with there being a strong skills-related cause to inactivity.

30. While low skills are an important cause of the Welsh inactivity problem, differences in skill levels are unable to explain the whole 'inactivity gap' between Wales and the rest of Britain. In broad terms, economic models suggest that around half of the higher inactivity rate in Wales compared to the rest of GB can be explained by characteristics of the Welsh population such as age, skill levels, gender, self-reported ill health and so on. The corollary of this is that around half of the excess inactivity cannot be explained by these characteristics. A person in Wales with a particular set of characteristics is significantly more likely to be economically inactive than an identical person living elsewhere in GB. For instance, diabetes makes a man in Wales 23% more likely to be inactive, while in England excluding the South East it only makes a man 9% more likely to be inactive. A similar pattern is found for a wide range of illnesses and for both men and women.
31. Wales has a fairly small excess of inactive individuals who say they want work (1.2% excess compared to GB) but a large excess of inactive who do not want to work (5.6% above GB).

### ***Does it pay people to get a job?***

32. The evaluation of New Deal for Lone parents shows that 70% of clients will be better-off in work<sup>3</sup>. A small proportion of this 70% will be only marginally better-off and may still make the decision not to work – but the vast majority of lone parents are better off in work. However for sick and disabled clients on higher rate benefits such as Incapacity Benefit, the decision is more marginal and will vary according to precise individual circumstances. The evidence suggests that fewer of them will be better off and that even when they are better off the amount of extra income (above benefit levels) may be less than for lone parents. Although in the longer-term there are increasing returns to work, the decision is often made on the immediate short-term return. Notwithstanding the assumptions in the calculations, it would appear that for many people in this group there are genuine short-term financial disincentives to look for work.

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<sup>3</sup> The calculations assume wage rates at NMW, and assume that lone parents will work part-time.