

Full employment: are we nearly there yet?

Last year's Welfare Reform and Work Act committed the Government to report annually on progress towards 'full employment'. There is no commonly-accepted definition of full employment, so in its first report, the Department for Work and Pensions will be setting out exactly what the full employment target means.

This briefing note provides background on what full employment means in the context of recent UK labour market experience, why full employment matters for poverty, and makes recommendations for what should be included in the Government's full employment target.

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What is ‘full employment’?

It was the previous chancellor that first made the full employment commitment. Speaking in March 2014, George Osborne didn’t give us a definition of what he meant by full employment, but he did give two ambitions: having the highest employment rate of the G7 group and adding two million more jobs by 2020.

Progress towards both targets is going well. According to the OECD, in the second quarter of 2017 – the most recent point for which comparable data exists – the UK employment rate was about a percentage point lower than that of Japan, which was the highest of the G7 countries.ⁱ The current UK employment rate is above 75% for the first time. In the three years following Osborne’s speech, the UK economy added more than an additional 1.5 million jobsⁱⁱ.

Figure 1: UK employment and unemployment rates



However, if we are approaching full employment, the economy isn’t acting like it. To economists, full employment means the economy is at its ‘natural’ rate of unemployment. There will always be some unemployment in the economy as firms shut down and workers lose jobs and search for new ones. Pushing unemployment below its natural rate would mean that firms have to offer higher wages to attract new workers, leading to rising wage inflation. Until recently, the received wisdom has been that full employment occurs when the unemployment rate is around 5%.

But the usual trade-off between lowering unemployment and stoking inflation seems to have broken down. The UK unemployment rate has now fallen to 4.3%. As the Bank of England’s Andy Haldane said in a recent speech this ‘would have led us to expect wage growth to pick up. That, plainly, has not happened.’ⁱⁱⁱ After a couple of years of slow growth in median real wages, wages have recently begun falling again. Average wages are still lower in real terms than they were 10 years ago.^{iv}

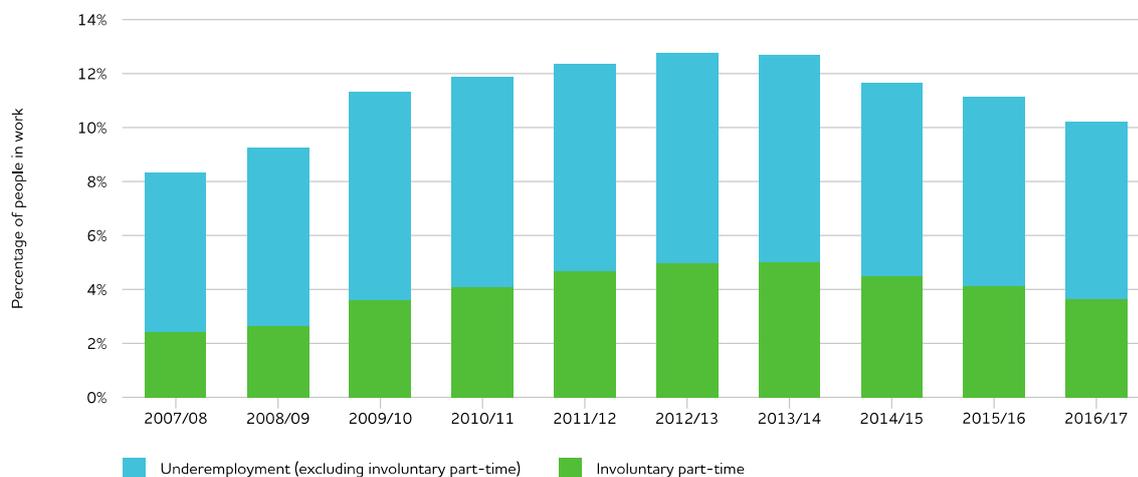
What could explain this puzzle? One possibility is that there remains a significant amount of slack in the labour market not captured by looking at headline employment

and unemployment rates. We need to look under the bonnet of the UK labour market to see where that slack is.

Underemployment of those in work

A first type of labour market slack comes from people being in work but not working as many hours as they would like. This ‘underemployment’ rose substantially after the financial crisis but has been slow to fall since. 3.1 million workers now say they are not working as many hours as they would like, equivalent to 10.2% of those in work, and up from 8.3% in 2007-08. This includes 1.1 million part-time workers who would like a full-time job (one seventh of all part-time workers).

Figure 2: Underemployment (4Q averages)



There may also be other forms of labour market slack contributing to underemployment. There is some evidence that a greater number of workers are in the ‘wrong job’ – a less productive job than they could be doing – than 10 years ago. For example, there has been a decline in job-to-job moves and a rise in the proportion of graduates in non-graduate jobs, suggesting skills are being underused. The rise of self-employment, temporary contracts and contracts without fixed hours may also to some extent represent underused potential in the labour market. However, measuring the contribution of these factors to falling short of full employment would be difficult.

Lagging employment rates for some groups

Behind the high national employment rate lies a great deal of variation in employment rates for specific groups and across the country. Figure 3 shows employment rates by disability status, region and ethnicity, and shows:

- Only half of working-age adults with a disability are in employment. The disability employment gap stands at more than 30 percentage points.
- The employment rate is above 75% only in the South and East of England (outside of London) and Scotland. Employment rates lag behind the national rate

in the rest of the UK. The employment rate in the North East is 3.0 percentage points lower the national average, and in Northern Ireland it is 6.7 percentage points lower.

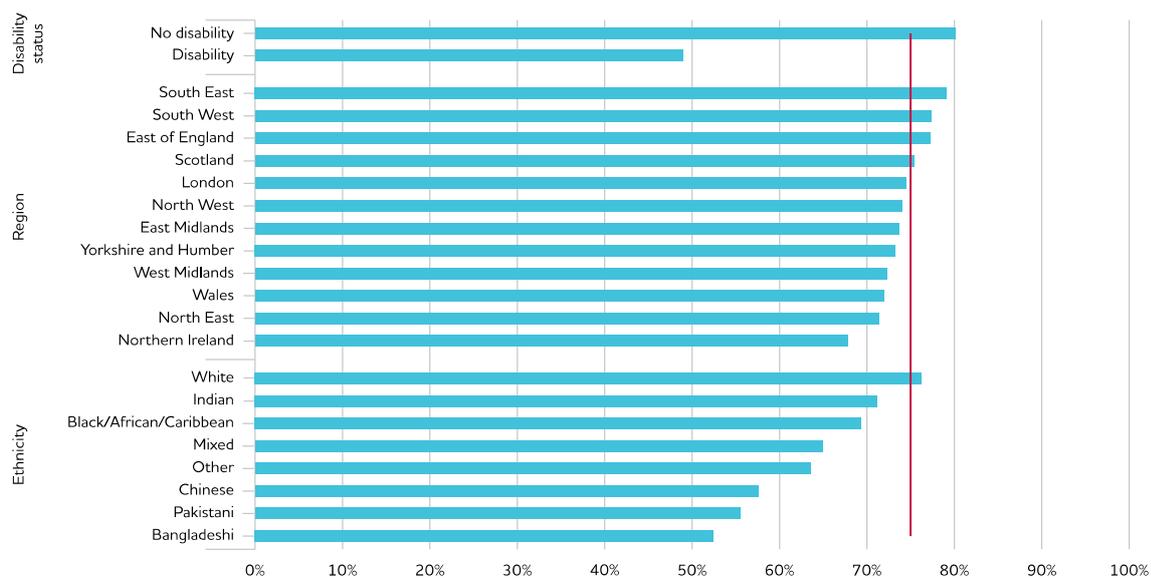
- Employment rates for all ethnic minorities lie below the national rate. Employment rates for Bangladeshi, Pakistani and Chinese ethnicities in particular lie far below the national rate at 52.8%, 55.9% and 57.9% respectively.

An important question is to what extent this represents slack in the labour market. Unemployment rates hint that there is quite a bit of slack for specific groups. The unemployment rate for disabled people is 9.0%, for people from Bangladeshi and Pakistani ethnicities it is over 10%, and unemployment rates are above 5% in the West Midlands and the North East.

There may also be wasted potential coming from those who are inactive – they are not actively seeking work – but nevertheless would like to work. This could be for a variety of reasons such as not being able to find suitable work due to disability or caring responsibilities. In all, two million adults are not working or looking for work despite saying that they want to work, equivalent to 5.3% of the working-age population and higher than the number of unemployed people. Two fifths of disabled people not in work say that this is despite them wanting a job.

There is also a case to be made that policy should aim to increase labour market participation for disabled people, and for regions and ethnicities with lower employment rates, regardless of whether this reduces labour market slack. The Government have notably committed to halving the disability employment gap.

Figure 3: Employment rates by disability status, region and ethnicity



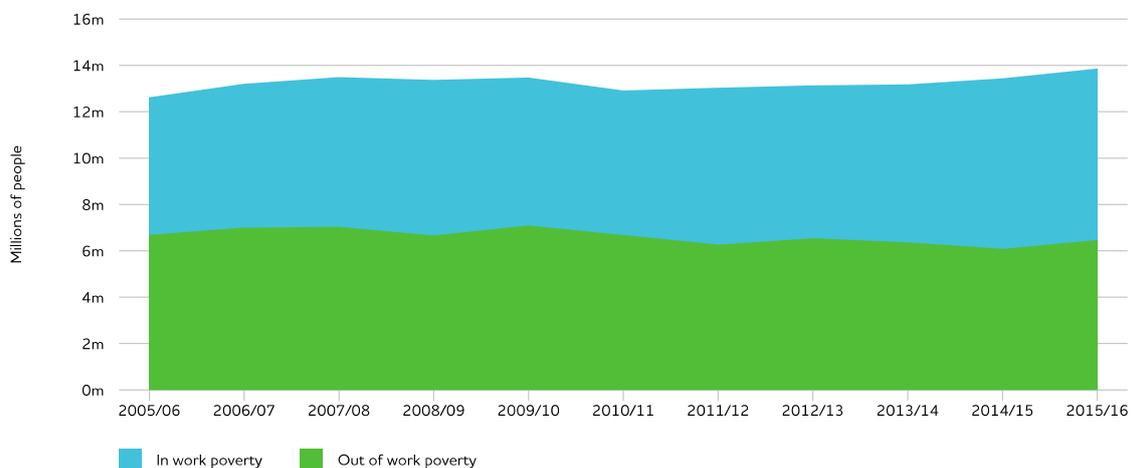
Full employment and poverty

To what extent would reaching full employment reduce poverty? Households with someone in work are much less likely to be in poverty than non-working households. 33% of those in workless households are in poverty, compared to 15% of households with at least one adult in work. The recent rise in employment rates should have been great news for tackling poverty.

The number of working age adults in non-working poverty did fall from 3.7 million to 3.4 million between 2010-11 to 2015-16, driven by a fall in the proportion of households with no-one in work from 19% to 15% over the same period. However, the UK relative poverty rate was slightly higher in 2015-16 (22%) than in 2010-11 (21%).

The fall in non-working poverty has been more than offset by the rise of in-work poverty in recent years. The relative poverty rate among households with at least one adult in work increased from 14% in 2005-06 to 16% in 2015-16. One cause of the increase in working poverty is the reduction in the real value of benefits since 2013, particularly affecting families with children. The proportion of lone parents in full-time work in poverty rose from 17% to 28% in a single year from 2014/15 to 2015/16, mainly driven by the freeze in most working-age benefits combined with high inflation. The likelihood of a working household being in poverty is also affected by pay and hours worked.

Figure 4: Number of people in poverty by work status



Targeting a broader definition of full employment could help tackle poverty. Reducing underemployment would help households relying on part-time incomes. Poverty rates are highest for disabled people, and ethnic minorities and regions with the lowest employment rates.

But reducing in-work poverty can't be done by targeting full employment alone. It would require tackling low pay, and seven in 10 households in in-work poverty include at least one person earning less than the higher, voluntary Living Wage (£8.45 an hour outside London). It would also require an effective benefits system that supports working households. Further reductions to family benefits and tax

credits introduced in 2017 and planned for the next few years are likely to lead to significant rises in poverty among working families. Low-earning families receiving Universal Credit could be helped by ending the benefits freeze and increasing the amount they can earn before support is withdrawn.

What should be in the full employment target?

As this analysis shows, full employment requires a high employment rate, but it also requires those in work to be working to their full potential, and for work to be shared by all groups across the country.

It is beyond the scope of this briefing note to suggest a full definition of the full employment target. However, it should include measures that represent the following ambitions:

- Maintain high employment and low unemployment rates;
- Reduce underemployment, including involuntary part-time work;
- Reduce the number of people not in work who would like to work;
- Bring the employment rate in lagging regions up to the national average;
- Bring ethnic minority employment rates up to the national average; and
- Close the disability employment gap.

Note: The figures in this briefing, unless otherwise stated, come from JRF's analysis of the Labour Force Survey and Family Resources Survey from JRF's forthcoming report, UK Poverty 2017

About the Joseph Rowntree Foundation

The Joseph Rowntree Foundation is an independent organisation working to inspire social change through research, policy and practice.

JRF is working with governments, businesses, communities, charities and individuals to solve UK poverty. The majority of the ideas outlined above were drawn from our recent [strategy to solve UK poverty](#) which contains analysis and recommendations aimed at the four UK governments.

All research published by JRF, including publications in the references, is available to download from www.jrf.org.uk

If you would like to arrange a meeting with one of our experts to discuss the points raised, please contact:

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ⁱ <https://data.oecd.org/emp/employment-rate.htm>

ⁱⁱ JRF calculations based on ONS Labour Market Statistics

ⁱⁱⁱ <http://www.bankofengland.co.uk/publications/Documents/speeches/2017/speech984.pdf>

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<https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/articles/supplementaryanalysisofaverageweeklyearnings/latest>