

Unemployment and its effect on the economy and society



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Unemployment is an ongoing problem throughout the world. One may asked, what is unemployment? It is the number of persons who are willing and able to work but are unable to find jobs. Unemployment is harmful to a country because it imposes costs on a Society.

The cost of employment to a nation can be categorised under three heading, namely ·The Social Cost ·The Cost to the Exchequer ·The Economic Cost The Social Cost of Unemployment The social cost of involuntary unemployment is incalculable. For an individual, the demoralising effect that it can have clearly depends upon whether the period of unemployment is short term or long term. Short term unemployment may have no serious effect on an individual whilst long term unemployment can be devastating. According to the Labour Force Survey in 1998, over 26% of the people unemployed for more than a year were over 50 years of age.

Many of these people believe that they are failing to find jobs because they are too old and a large number of older people have become reconciled to the prospect of never working again. A major problem, of course, is that as job searchers become more and more pessimistic about their chances of finding jobs become even more remote. According to survey carried out by the Manpower Services Commission, many of the longer-term unemployed become bored, idle, lose their friends and suffer from depression. One respondent to the survey stated, " It is not just money. Work gives you something to do. I'm just wasting away.

" There is also evidence of increase family tensions leading in some cases to violence, divorce and family break ups. Unemployment can also lead to

homelessness, as in some circumstances building societies may foreclose on mortgage if repayments are not kept up. One can only speculate on the effect of long term unemployment on vandalism, football hooliganism and the crime rate in general. In countries without adequate welfare provisions for the poor, unemployment may be very much more severe in its effects. It may lead to a considerable degree of social deprivation and a miserable existence for the families involved. In extreme cases (eg.

Where unemployment means no income at all), it can lead to starvation. The cost of the Exchequer The cost of both voluntary and involuntary unemployment to the Exchequer is more readily quantifiable than the social cost. Voluntary unemployment is a situation in which workers refuse to accept a cut in real wages, so that the prevailing real wage is above the market clearing level whilst Involuntary unemployment is a situation in which a worker is unable to find a job at the going wage rate. It consists of the following components:

- Benefits which have to be paid to the unemployment.

These include unemployment benefits, supplementary benefit, housing benefit, government contributions to redundancy payments and payments to those men aged between 60_65 who no longer register as unemployed. The loss of tax revenue which would otherwise have been received. This consists mostly of the lost income tax, but also includes lost indirect taxes because of the reduction in spending.

- The loss of National insurance contributions which would otherwise have been received.

The economic cost The economic cost with respect to unemployment represents a waste of resources and means that the economy is producing a

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lower rate of output than it could do if there were full employment. Diagram showing a time-series of actual gross domestic product in the United Kingdom measured at 1975 prices since 1960. The trend line drawn through the peaks of the time-series can be regarded as providing a rough estimate of the economy's potential output during the period. Potential output is that rate of gross domestic product which would result if all resources were fully employed.

The shaded area between the actual time-series and the trend line is called the output gap and it is a reflection of the output of goods and services which have been lost as a result of the unemployment. It is clear, that the output gap has increased in size since the 1960s and early 1970s. This means that society has experienced a lower standard of living than would have been possible without rising level of unemployment. The loss of potential output resulting from involuntary unemployment is clearly a serious matter for an economy.

Resources which are willing and able to work in order to raise the rate of output and to boost living standards are failing to be employed. This is a true waste of resources. It is not so clear, however, whether the loss of potential output through voluntary unemployment is so serious. It may simply mean that more people are taking advantage of higher social security benefits to spend more time searching for suitable jobs. There are numerous causes to the problem of unemployment which may vary from country to country.

Amongst them are Natural unemployment The level of natural unemployment can be defined as the number of persons who are employed even when the labour market is in long-run equilibrium that is when the total demand for labour is equal to the supply of labour at the prevailing level of real wage rates. In this situation, people may be unemployed because:

- they are between jobs and are taking time to search for the most appropriate job with the highest wage(search unemployment)
- the industry in which they have traditionally worked have experienced a structural decline or has been influenced by technological advances (structural unemployment)
- there has been a seasonal decline in the demand for their labour services (seasonal employment)
- they are been regarded as “ unemployable” for one reason or another (residual unemployment).

Search Employment This is the unemployment, sometimes called fictional unemployment, which occurs because workers are searching for the jobs which suit them best. Some of these workers may have just entered the labour market from school, some may have been made redundant from their previous job, some may have been sacked for one reason or another and many will have quit their previous jobs in order to create time to search for more satisfactory ones.

All unemployed workers are of course searching for new jobs (apart that is, from those discouraged workers who regard themselves as having withdrawn from the labour market). This does not mean, however, that all unemployment is of the “ search” type. Search unemployment can be seen as part of the annual turnover of the job market meaning that firms re= id themselves of workers who have proved to be unproductive or unsatisfactory in some way, and workers quit jobs which have failed to meet their

expectations or which were intended only as stop gaps in the first place.

There are two main reasons why these why these unemployed workers do not find jobs immediately. First, there is imperfect knowledge and the collection of information is time consuming.

Secondly, most workers believe that more time they spend searching for a job, the more likely it is that they will obtain one which meets their requirements, particularly so far as the wage and working conditions are concerned. Thus the, the search for a job is not the period of inactivity that is, it involves finding out what jobs are available, sending off application forms, going to interviews and perhaps attending courses all of which make job searching a very busy time. The economic theory of job search has grown into an important aspect of labour economics in recent years. This theory sees the unemployed person as continuing the job search (that is remaining unemployed) so long as wage offers are less than a certain reservation wage. The reservation wage is the minimum wage the individual is prepared to accept. It will depend to what extent on the net costs of searching, that is, the lower the cost the higher the reservation wage is likely to be and, therefore the longer the spell of unemployment Diagram showing search unemployment, an unemployed person will remain unemployed as long as wage offers are less than the individual's reservation wage Structural Unemployment This is a more serious type of unemployment and is caused by changes in the structure of demand for goods and services in an economy and by technological changes, both of which affect the composition of the demand for labour.

To illustrate more clearly what is meant by structural unemployment, consider a region within a country which traditionally specialised in ship building. Suppose, as in a fact happened that the world demand for ships decreases and shifts to more efficient producers overseas. Although the demand for other goods and services may increase at the same time, this does not immediately help the obsolete shipbuilders. As they become unemployed, they find that there are a few jobs available in their local area and no job at all which require their specialised skills. They faced the prospect of having to accept unskilled jobs at a lower wage or retaining they may have to move to another part of the country. Structural unemployment persists mostly because of the geographical and occupational immobility of labour.

The major causes of geographical immobility include social ties and a reluctance to move away from family and friends although the problems and cost t of moving to a new location may be prohibitive for many people. The major cause of occupational immobility is the fact that many skills are not easily transferable from one occupation to another. The occupational mobility of labour can often be overcome by a period of retraining, but this takes time and may be costly for the unemployed worker. Also, workers may be reluctant to retrain until they are convinced that their present skills are not sufficient to enable them to find work.

Lack of information is another reason for the persistence of structural unemployment, being itself one of the causes of geographical and occupational immobility. Often the unemployed are not aware of the opportunities available in other parts of the country or in other occupations.

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In recent years, a great deal of emphasis has been placed on technological progress as a cause of structural unemployment. Advances in automation, the development of word processors and the many other applications of information technology have all been blamed for rising unemployment. It is true that these developments are likely to reduce the labour that is, capital ratios in a wide range of industries. This implies that the number of jobs associated with any given level of output in the economy will be smaller than it would have been without the technological advances.

However, the increased prices expand their levels of output, thereby increasing their demands for all factor inputs, including labour. The final effect on the overall level of unemployment is uncertain. For this reason, it would not be appropriate to discourage technological progress on the grounds that it is likely to increase structural unemployment. Indeed, discouraging technological progress within a particular country would make the country's goods less competitive in world markets and this might lead to an even greater increase in unemployment. An extensive retraining scheme for those who enter unemployment pool with the "wrong" skills would be a more efficient way of reducing this type of natural unemployment. Seasonal Unemployment At any given time of the year, there are always likely to be some workers who are temporarily laid off because of a seasonal fall in demand for their services.

In the winter months, for example, many building workers find themselves without work because of bad weather and many workers in the tourism industry are laid off. Similarly, in the summer months, workers associated with the winter sports industry and with the rush to produce and sell goods

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and services during the lead up to Christmas find that their services are no longer required. This type of employment can undoubtedly cause hardship to the workers involved; also it represents a waste of resources and a drain on the Exchequer. It is therefore be some cause for concern.

On the other hand, seasonal unemployment is thought by many to be earned without the ties of a more permanent job. Residual Unemployment This is the label given to that group of unemployed workers who suffer from mental and or physical disabilities which may limit the number of jobs opportunities available to them. The sum of frictional, structural, seasonal and residual unemployment equals the total amount of natural unemployment in an economy. Some economists claim that the natural rate of unemployment is roughly constant over time, possible about 5% of the labour force in the United Kingdom. Other believe that the natural rate can vary considerably over time and will depend on such factors as the size of ant structural changes taking place, and on the application of the supply side polices .

In addition some economist argues that the reductions of aggregate demand which occur during a recession may have a long term effect on the natural rate of unemployment. For example, recession which lasts several years may cause some workers to lose their job skills and/or become discourage from finding jobs in the future, so increasing frictional unemployment. This long term effect of changes in aggregate demand on unemployment is referred to as hysteresis which is a phenomenon that comes into effect when an economy in long-run equilibrium experiences a disturbance such as a recession. The result of the recession is such that when the disturbance has finally disappeared, the economy is unable to attain the initial long-run

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equilibrium level of output and employment. Demand- deficient

Unemployment This occurs when there is a general deficiency of the demand for labour in the economy such that it is impossible for all those who are seeking work to be employed.

The demand for labour is a derived demand that is; it is derived from the demand for goods and services. Thus, when one say that unemployment is caused by a general deficiency of the demand for goods and services. Thus, when we say that unemployment is caused by a general deficiency of the demand for labour, that is equivalent to saying that unemployment is caused by a general -demand-deficiency unemployment was emphasised by Keynes. It is because of this that demand-deficient unemployment is sometimes referred to as Keynesian unemployment. Diagram showing demand-deficient (Keynesian) unemployment. With extreme Keynesian inverted-L shaped AS curve, any changes in the economy which shifts the AD curve to the left will reduce the equilibrium level of real income and create demand-deficient unemployment.

Excessive real wage unemployment Monetarists deny the existence of demand-deficient unemployment and instead subscribe to the view that unemployment above the natural rate is caused by real wages being too high as a result of restrictive practices in the labour market. According to this approach, the solution to unemployment is a cut in the real wage, achievable either by cutting the money wage or by allowing the price level to rise more rapidly than money wages. Monetarist believe that this real wage adjustment will eventually occur in the long run, and will occur more quickly if the labour

market can be made more competitive. Diagram showing Excessive real wage unemployment. At the real wage $(W/P)_1$, there is an excess of labour .

this unemployment could be eliminated by a fall in the real wage to $(W/P)_0$

Fiscal and Monetary Policies Fiscal and monetary policies, sometimes called demand- management or demand-side policies, are intended to increase

aggregate demand and therefore, equilibrium national income. The principal policy instruments are government expenditure, taxation and the stock of

money in circulation. If unemployment is caused by a general deficiency of aggregate demand (eg. Increasing government expenditure, cutting

taxation or expanding the money supply) to shift the AD curve to the right

and so create additional income and employment. Supply side policies

Supply-side policies are intended to increase the economy's potential rate of output by increasing the supply of factor inputs, such as labour inputs and

capital inputs and by increasing productivity. Labour market policies

specifically designed to reduce natural unemployment might include the

following: ·Improvements in information dissemination: A lack of information is a likely cause of natural unemployment for two main reasons.

First, unemployed workers may take a long time to find suitable jobs if they are not made aware of all the available opportunities. ·Provision of retaining

scheme: We have seen the occupational immobility of labour is one of the major determinants of structural unemployment. One Way of tackling this

problem is for government to finance retraining schemes for those

unemployed workers who wish to acquire new skills. ·Assistance with family

relocation: We have also seen that geographical immobility is a determinant of structural unemployment. To tackle this problem, the provision of

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information concerning recreational facilities, schools and the quality of life in general in other parts of the country may be helpful, but more important would be the provision of financial help to cover moving costs and to assist with home purchase. ·Special employment assistance for teenagers: Many teenagers leave school without having studied work related subjects and with little or no work experience.

This makes it difficult for them to find jobs; those who do become employed may soon find that the work is not at all what they expected and so quit in order to search for more suitable posts. The strengthening of vocational counselling, the expansion of work-related studies (such as business practice, catering and information technology) and the payment of subsidies to those firms who take on young people for short periods of work experience may help to alleviate youth unemployment. Work related training schemes for school leavers may also be useful in this respect. ·Subsidies to firms which reduce working hours rather than the size of the work-force. : This proposal may help to reduce that structural unemployment caused by the displacement of workers by a new technology.

We have seen that this would be counter-productive to discourage firms from adopting new technology. The government could, however, encourage firms and trade unions to work towards a reduction in average weekly hours rather than a reduction in the size of the work force. This might be achieved by paying a subsidy to those firms which adopt new technological equipment and at the same time negotiate successfully with the relevant trade unions to reduce working hours rather than lay off workers.