

### 3. UNEMPLOYMENT

Unemployment occurs when there are people who wish to work at the going wage but are unable to find a job.

Unemployment is an indicator of economic activity, which compares **the number of people in the labour force to the number of looking for work.**

**Unemployment in an economy with a given labour force will fall if the number of workers gaining jobs is greater than the number of people losing jobs.**

#### 1.1 MEASURING UNEMPLOYMENT

Data on work and unemployment are among the most carefully designed and comprehensive economic data the nation collects. The data are gathered monthly in a procedure known as “**Random Sampling**” of the population. Each month about 60 000 households are interviewed about their recent work history.

Measuring the number of unemployed in an economy is more difficult than economic theory might suggest. There are 2 ways in which unemployment can be calculated.

1. Government can undertake a survey of the population to identify the employed and the unemployed. As practiced in USA, Japan & Sweden.

The UK government does a quarterly survey of the work force called the “**Labour force survey**”, but this does not provide the main unemployment statistic for the UK economy.

The government can count all those who register as unemployed. In some countries a register of the unemployed is kept by the trade unions because unemployment benefit is linked with union membership.

The survey divides the population 16 years and older into 4 groups:

**EMPLOYED** – these are people who perform any paid work, as well as those who have jobs but are absent from work because of illness, strikes or vacations

**UNEMPLOYED** – this group includes people who are not employed, but are actively looking for work or waiting to return to work

**NOT IN THE LABOUR FORCE** – this includes the 34 % of the adult population that is going to school, keeping house, retired, too ill to work or simply not looking for work

**LABOUR FORCE** – this includes all those who are either employed or unemployed

$$\text{TheUnemploymentRate} = \frac{\text{NumberOfUnemployed}}{\text{TotalLabourForce}}$$

## 1.2 TYPES OF UNEMPLOYMENT

Unemployment can be grouped into two main categories:

**VOLUNTARY UNEMPLOYMENT** – occurs when workers choose not to take jobs offered at existing wage rates e.g. frictional, seasonal, structural and classical unemployment

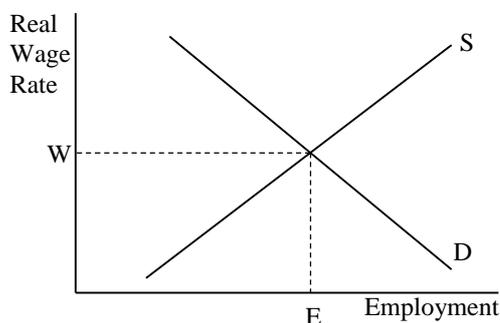
**INVOLUNTARY UNEMPLOYMENT** – occurs when workers are willing to work for existing wage rates but jobs are not offered to them e.g. cyclical unemployment.

### LABOUR MARKET EQUILIBRIUM

Equilibrium in the labour market is achieved when the demand for labour is equal to the supply for labour.

The demand for labour in an economy is determined by the **Marginal Revenue Product** of labour. As more and more workers are combined within **hed** stock of land & capital, the MRP of labour (addition to input **of the** extra worker) declines (and example of law of diminishing returns). Hence, the demand curve is downward sloping. The supply curve for labour in an economy is likely to be upward sloping. As real wage rates increases, more adults particularly women are attracted into the work force. In the very short term employees can also persuade existing workers to work overtime, if they offer higher rates of pay.

**Labour market equilibrium (FIG 1)**



Employment is OE

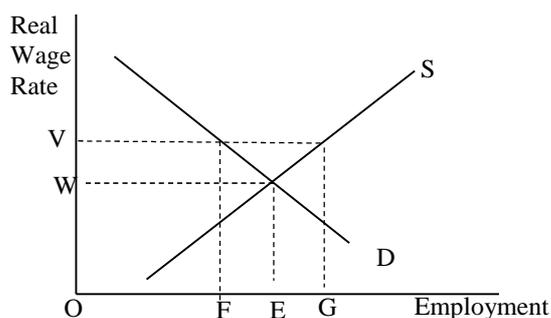
Equilibrium wage rate is OW

Unemployment then occurs for 2 reasons in the economy:

- (1) Labour market moves away from its equilibrium position E actual wage being above OW
- (2) There is some measured unemployment even when the labour market is in equilibrium

### UNEMPLOYMENT WHEN LABOUR MARKET IS IN DISEQUILIBRIUM

Supply > Demand (FIG 2)



The actual wage rate OV is above the market clearing wage rate OW

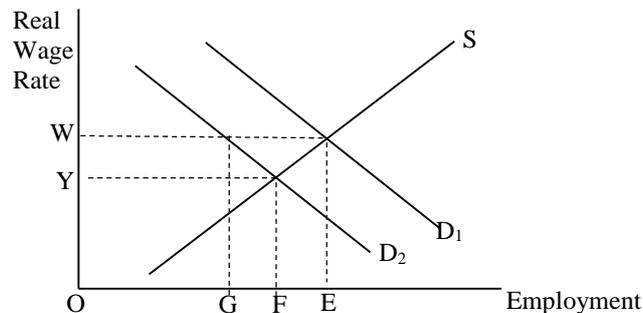
FE fewer workers are demanded by employers because the wage rate is too high

EG more workers want job because of high wages

Result is that there is **FG** Unemployment in the economy

If wage rates were to fall to OW unemployment would fall, as firms demand more workers and some workers will not be willing to work at the lower wage rate.

**INVOLUNTARY  
CYCLICAL (DEMAND DEFICIENT) UNEMPLOYMENT  
(FIG 3)**



When an economy goes into recession, unemployment rises because there is insufficient demand in the economy. It is not only labour that become unemployed. All other factors of production become unemployed too. The result is that the demand for labour falls, shown by a shift to the left in the demand curve.

Employment used to be at OE. Now it is at OG with the old wage rate of OW. This is because OE workers want a job, firms demand only OG workers.

The Unemployment of GE is called **cyclical unemployment**.

**VOLUNTARY**

**CLASSICAL UNEMPLOYMENT** – (Real wage unemployment) exists when real wage is above that needed to clear the labour market even when the economy is booming.

Jobs exists, but workers choose not to take them because they are not prepared to take the wages being offered, or they are unable to take them because of trade union power or government legislation (minimum wage).

In figure 2, the actual wage rate of OV is too high to clear the market. Thus wages are “**sticky downwards**”. Meaning that there are factors preventing wages from falling to clear the market.

1. One reason why unemployed people refuse to take jobs is because the unemployment benefit levels are too close to the level of pay being offered. If benefit levels are above OW in figure 2, there is no point for workers to accept a job at a wage rate of OW. The ratio between the benefit actually received and the wage a worker could receive is called the “**REPLACEMENT RATIO**”  
When unemployment benefit is cut, workers are given incentives to take a job.

2. Another reason why the labour market may fail to clear is because of minimum wage legislation. If the minimum wage is OV in figure 2, then there will inevitably be unemployment. People would not want to take jobs because the argument in favor of a national minimum wages.
3. Another reason is thr horizontal equity (situation whereby every worker should receive the same rate of pay for working an hour. This is not possible in the market economy. The market produces wage differentials in order to create an

efficient economy where wages reacts as signals, creating incentives for workers with high skills to take on jobs with high marginal revenue products.

### ***UNEMPLOYMENT WHEN LABOUR MARKET IS IN EQUILIBRIUM***

Even when labour market is in equilibrium, there might still be unemployment for number of reasons:

#### **FRictional UNEMPLOYMENT**

Temporary, unavoidable unemployment is described as frictional unemployment. There are always some people who are out of work from completely unavoidable reasons. For example, it takes time for workers to move from one job to another. Until they actually start working again, they will be counted in government data as “unemployed”. People entering the labour force for the first time are considered to be unemployed until they find their first job.

There will always be frictional unemployment in a free market economy. The amount of time-spent unemployed varies. The higher the unemployment benefits, the longer workers will be able to afford to search for a good job without being forced into total poverty. Equally, the better the job information available to unemployed workers through newspapers and job centers are, the shorter the time workers should need to spend searching for jobs.

#### **SEASONAL UNEMPLOYMENT**

Some workers such as construction workers or workers in the tourist industry, tend to work on seasonal basis. Seasonal unemployment tends to rise in winter when some of these workers will be laid off. Whilst unemployment falls in the summer when they are taken on again.

There is little that can be done to prevent this pattern occurring in a market economy where the demand for labour varies through the year.

#### **STRUCTURAL UNEMPLOYMENT**

It is the most serious type of unemployment. This occurs when the demand for labour is less than its supply in an individual labour market in the economy. It can be divided as follows:

- **REGIONAL UNEMPLOYMENT** – this can occur as a result of lack of mobility of factors of production between the regions e.g. throughout the **cost** war period, the south of England has tended to be at full employment while regions such as Northern Ireland have consistently suffered unemployment.
- **SECTORAL UNEMPLOYMENT** – the steel & shipbuilding industries in the U.K declined sharply between late 1970s and early 1980s, leaving a considerable number of skilled workers unemployed. Unfortunately their skills were no longer needed in the economy and without retraining & possible relocation, they were unable to adapt to the changing demand
- **TECHNOLOGICAL UNEMPLOYMENT** – groups of workers across industries may be put out of work by new technology. Again without retraining and geographical mobility, these workers may remain unemployed. E.g. there was a time when building elevator were run by elevator operators. Today elevator cars are self-service. Elevator operators who lost their jobs when self-service cars were installed became part of the structurally unemployed until they found other jobs.

Long-term changes in consumer preferences can also cause structural unemployment.

**The natural rate of unemployment** is the percentage of workers who are voluntarily unemployed when the labour market is in equilibrium.

**FULL EMPLOYMENT** – the economy is said to be at full employment when there is no involuntary unemployment in the economy.

### **1.3 COSTS OF UNEMPLOYMENT**

- The economy is losing the output that unemployed people might have been producing.
- The unemployed are losing the difference between their income in work and the benefits they receive.
- The government is losing the tax revenue that the unemployed would have, and had they been in work, plus the costs of whatever benefits that are paid
- Associated costs resulting from the poor health that can be associated with unemployment

Individuals tend to become demoralized, anxious, insecure and oversensitive.

#### **Tasks:**

1. Find out what the unemployment rate in Slovakia is and used to be in the past 5 years and compare it to other countries.
2. What form of unemployment mainly occurs in Slovakia? (cyclical, frictional, regional, ...) Explain.
3. Explain the reasons for unemployment in Slovakia. (historical background, structure of industry, population structure, education, political background...)
4. Give at least 5 examples of government policies to reduce unemployment