



## Hidden unemployment and its relevance to labour market policy in the East Midlands

BEATTY, Christina <<http://orcid.org/0000-0003-0943-9979>> and  
FOTHERGILL, Stephen <<http://orcid.org/0000-0002-4201-0640>>

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# **HIDDEN UNEMPLOYMENT AND ITS RELEVANCE TO LABOUR MARKET POLICY IN THE EAST MIDLANDS**

**A position paper commissioned by EMDA to inform the development of a Regional Skills Strategy**

**Christina Beatty and Stephen Fothergill  
Centre for Regional Economic and Social Research  
Sheffield Hallam University**

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## **1. PURPOSE OF THE PAPER**

This paper reviews the evidence on hidden unemployment in the East Midlands in order to inform the Regional Skills Strategy being developed for the region. It draws mainly on the extensive research by the authors into unemployment in the East Midlands and elsewhere in Britain. The paper is organised as follows:

- *Section 2* explains how unemployment becomes 'hidden'
- *Section 3* reviews the previous evidence on the scale and location of hidden unemployment in the East Midlands
- *Section 4* presents new figures on the largest of the distortions to official unemployment data – the diversion onto Incapacity Benefit
- *Section 5* looks at survey evidence on male Incapacity Benefit claimants in two contrasting parts of the region
- *Section 6* explores the implications of this evidence for the development of labour market policy in the East Midlands.

## 2. HOW UNEMPLOYMENT BECOMES HIDDEN

There are two official measures of unemployment across Britain:

- *Claimant count.* This is the number of people claiming unemployment-related benefits, principally Jobseeker's Allowance (JSA).
- *ILO unemployment.* This is the number of people who meet the International Labour Organisation (ILO) criteria for unemployment – ie they are out of work, have looked for work in the last four weeks and are available to start work within two weeks. The number of ILO unemployed is estimated from the Labour Force Survey.

In recent years the claimant count (currently just under 0.9 million) has been about half a million less than the ILO unemployment level (currently around 1.4 million) though both are well down on peak levels in the early 1990s.

The claimant unemployment rate is the one most frequently quoted for local areas. This is partly because it is available monthly and figures are only a couple of weeks old when released. The Office for National Statistics has recently changed over from expressing claimant unemployment as a percentage of the economically active population to expressing it as a percentage of the entire working age population. This has had the effect of lowering the published rate and adding to the impression of much lower unemployment than in the past.

The ILO figure is in theory the government's preferred measure of unemployment. However, ILO figures are much more limited at the local scale owing to sample sizes.

Both the claimant count and the ILO measure are accurate in recording what they each set out to measure. The trouble is that neither records the totality of unemployment. The central problem is the way the benefits system works. In the UK there are powerful mechanisms that:

- Divert some people from unemployment-related benefits (mainly JSA) to other parts of the benefits system

- Divert others out of the benefits system altogether.

The diversions impact most directly on the claimant count, which is entirely dependent on benefit numbers. It is well established that as the rules governing the eligibility for unemployment benefits tightened from the 1980s onwards, the effect was to reduce the claimant count. More generally, in so far as the benefits system works to divert people from JSA onto other benefits or out of the benefits system altogether, it reduces recorded, claimant unemployment.

The diversions impact on ILO unemployment in so far as they influence labour market behaviour. There is a requirement for JSA claimants to demonstrate that they are actively looking for work. However, there is no similar requirement on claimants of Incapacity Benefit (IB) or Income Support (IS). Therefore if an IB or IS claimant thinks there is no suitable work available and decides not to look for work, he or she will fail one of the ILO unemployment 'tests' and will be excluded from ILO unemployment figures as well as from the claimant count.

The impact of diversions within the benefits is substantial. It is worth bearing in mind that whereas around 0.9 million people are claimant unemployed, there are 2.7 million people of working age who are out-of-work and claiming sickness-related benefits, principally Incapacity Benefit. Also, unlike IB, JSA becomes means-tested for all claimants after six months. For many people this creates a financial incentive to claim IB rather than JSA.

On the other hand, not everyone without paid employment can be described as 'unemployed'. Men and women who have opted out of employment to retire early, to look after family and home or to be full-time carers cannot really be labelled as 'unemployed'. Nor could those whose illness or disability completely prevents them from working in any circumstances.

In our extensive research<sup>1</sup> we have defined the 'real' level of unemployment as including *all those who might reasonably be expected to have been in work in a fully-employed economy*. This is a wider group than just the claimant unemployed or the ILO unemployed, in that it seeks to include the unemployed who have been diverted

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<sup>1</sup> See for example C. Beatty, S. Fothergill, T. Gore and A. Green (2002a) *The Real Level of Unemployment 2002*, CRESR, Sheffield Hallam University.

onto other benefits or out of the benefits system. 'Hidden' unemployment is the difference between this wider group and 'visible' claimant unemployment.

Defined in this way, the hidden unemployed comprise a number of groups:

- Those who meet the ILO unemployment criteria (available and looking for work etc) but are excluded from the claimant count. This group includes particularly large numbers of women who are disqualified from means-tested JSA because of their partner's income. It also includes lone parents on Income Support who are looking for work.
- Those who have been diverted onto sickness-related benefits (mainly Incapacity Benefit). These are the men and women with health problems who nevertheless could be expected to be in work in a fully-employed economy.
- Those who have been diverted onto government schemes. Whereas most men and women on government schemes could not be described as unemployed, there is a group without a contract of employment that even the government itself does not count as 'in employment'.
- Those who have been diverted into premature early retirement. These are the men and women below state pension age that would have carried on working if a suitable job had been available for them.

### 3. THE SCALE OF HIDDEN UNEMPLOYMENT IN THE EAST MIDLANDS

In 2002 the present authors undertook a study for the East Midlands Regional Observatory into the scale of hidden unemployment in the region<sup>2</sup>. This remains the most comprehensive source of information on the issue, though the figures for the diversion onto sickness-related benefits have subsequently been up-dated (see section 4 of the present paper).

The study generated estimates, by district, for January 2002. The estimates were based on data from a range of sources, including the Labour Force Survey, the Census of Population and DWP benefits records. The methods are set out in full in the original paper. What should be noted here are three points:

- The estimated diversion from unemployment to sickness benefits is based on a benchmark for each district that reflects sickness claimant rates prevailing in fully-employed parts of southern England and underlying local divergences in sickness rates from the levels in this part of the South. The estimates were cross-checked by alternative methods and shown to be robust.
- The estimated diversion into premature early retirement is based on a similar benchmark, reflecting levels in fully-employed parts of the South and underlying differences.
- Only the people on government schemes without a contract of employment are counted as hidden unemployed.

Table 1 shows the estimates of hidden unemployment in January 2002, taken from this earlier study.

The first line shows that in January 2002 the total number of people in the East Midlands out-of-work and claiming unemployment-related benefits - the claimant count - was 65,000. About three quarters were men.

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<sup>2</sup> C. Beatty, S. Fothergill, T. Gore and A. Green (2002b) *Hidden Unemployment in the East Midlands*, published on the East Midlands Regional Observatory website.

**Table 1: Hidden unemployment in the East Midlands, January 2002**

	<b>Male</b>	<b>Female</b>	<b>Total</b>
<b>CLAIMANT COUNT</b>	48,500	16,500	65,000
Extra ILO unemployed	6,500	25,500	32,000
Government schemes	2,900	2,100	5,000
Diversion to sickness benefits	41,200	32,500	73,700
Diversion to early retirement	7,000	4,100	11,200
<b>HIDDEN UNEMPLOYMENT</b>	57,700	64,300	122,000
<b>REAL UNEMPLOYMENT</b> (ie claimant plus hidden)	106,200	80,700	186,900

Source: Beatty, Fothergill, Gore and Green (2002b)

The next four lines show estimates of hidden unemployment. In total, these figures point to 122,000 hidden unemployed in the region – equivalent to nearly two hidden unemployed for every person on the claimant count.

The largest component of hidden unemployment was estimated to be the diversion to sickness-related benefits - more than 73,000, of which a little more than 40,000 were men. These are large numbers but they need to be placed in context: a total of 176,000 people of working age in the East Midlands were out-of-work and claiming sickness-related benefits. In other words, the estimates suggested that only around four out of ten sickness claimants in the region might be regarded as hidden unemployed

The second largest group are the extra ILO unemployed - 32,000 in total, of whom three-quarters are women. Many of these are individuals who are denied access to Jobseeker's Allowance, for example because other household income eliminates their entitlement. The large number of women in this particular group is a common feature of comparisons of claimant and ILO unemployment.

The remaining components of hidden unemployment - government schemes and the excess early retired – were estimated to account for more modest numbers, 5,000 and 11,000 respectively.

Adding the hidden unemployed to the claimant count gives 'real' unemployment. The figures here point to 187,000 unemployed, of which 106,000 are men.

Hidden unemployment affects both men and women. In the East Midlands as a whole the numbers of hidden unemployed men and women were estimated to be broadly similar. However, women's unemployment is more likely to be 'hidden' – four out of five of the women counted as real unemployed are 'hidden', compared to only about one in two men. Among men, sickness claimants dominate the hidden unemployed. Among women, sickness claimants and the extra ILO unemployed both contribute substantially to hidden unemployment.

Table 2 shows estimates of claimant and real unemployment by district in January 2002. In both cases the unemployment rates are expressed on the old basis – ie as a percentage of the economically active population. Districts in the region are ranked from highest to lowest on the basis of estimated real unemployment.

Whereas claimant unemployment in January 2002 varied only modestly across the region, from around 1 to 6 per cent, estimated rates of real unemployment ranged from around 3 to 15 per cent. This reflects the distribution of hidden unemployment in the region. In the districts where claimant unemployment is low, hidden unemployment typically adds 2-3 percentage points to the unemployment rate. In the districts where claimant unemployment is high, hidden unemployment typically adds 8-10 percentage points. This tendency for hidden unemployment to be greatest in areas where claimant unemployment is already known to be highest can be observed in other regions as well as the East Midlands.

It is worth noting here that there is nothing especially unusual in the estimated level of hidden unemployment in the East Midlands. The diversions from JSA to other benefits, or out of the benefits system altogether, are a UK-wide phenomenon. So is the distortion to ILO unemployment rates that arises from these diversions. In fact, the estimated scale of hidden unemployment in the East Midlands is somewhat less than in the North of England, Scotland and Wales, though rather greater than in the



South East, South West and Eastern regions<sup>3</sup>. This reflects the general tendency, mirrored within the East Midlands itself, for hidden unemployment to be concentrated in the areas where claimant unemployment is highest.

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<sup>3</sup> C. Beatty, S. Fothergill, T. Gore and A. Green (2002b) op. cit.

**Table 2: Unemployment by district, January 2002**

	<b>Claimant count</b>	<b>Real</b>
	<b>(%)</b>	<b>unemployment</b>
		<b>(%)</b>
Mansfield	4.5	15.5
Bolsover	4.3	15.0
Nottingham	6.1	15.0
Chesterfield	5.3	13.6
Leicester	6.2	13.6
Bassetlaw	4.8	13.5
East Lindsey	4.2	13.1
Ashfield	4.1	12.9
Lincoln	4.3	11.8
Corby	3.4	10.8
Newark and Sherwood	2.7	10.6
West Lindsey	3.5	10.2
North East Derbyshire	3.6	10.1
Derby	4.5	10.0
Boston	2.5	9.4
Gedling	2.4	8.3
Amber Valley	2.7	7.9
North West Leicestershire	2.0	7.6
Broxtowe	2.4	7.5
South Holland	1.9	6.8
Erewash	3.0	6.7
South Derbyshire	1.9	6.5
Kettering	1.8	6.2
Wellingborough	2.5	5.7
Northampton	3.0	5.5
South Kesteven	2.0	5.5
Oadby and Wigston	2.3	5.5
North Kesteven	1.7	5.4
High Peak	2.0	5.2
Daventry	1.6	4.9
Charnwood	2.4	4.9
Rushcliffe	1.5	4.9
Melton	1.4	4.7
Blaby	1.6	4.6
Hinckley and Bosworth	1.8	4.3
East Northamptonshire	1.8	4.2
Derbyshire Dales	1.6	4.2
Harborough	1.3	3.3
Rutland	0.6	3.1
South Northamptonshire	0.9	2.8

Source: Beatty, Fothergill, Gore and Green (2002b)

#### 4. NEW ESTIMATES OF THE DIVERSION ONTO SICKNESS BENEFITS

The largest component of hidden unemployment identified in the 2002 East Midlands study was the diversion onto sickness-related benefits, principally Incapacity Benefit. This part of the estimates was based on DWP benefits data for August 2001. The estimates have subsequently been revised for all GB districts using DWP data for August 2003<sup>4</sup>.

The methods used are identical to those in the earlier East Midlands study. For each district, a 'benchmark' has been calculated that reflects present-day sickness claimant rates in fully-employed parts of southern England and the underlying differences in sickness rates between each district and that part of the South. Excesses over this benchmark are judged to be a form of hidden unemployment.

As previously, the hidden unemployed among sickness claimants are those who might reasonably be expected to have been in work in a fully-employed economy. There is no suggestion that their claims are fraudulent, or that the health problems are anything less than real. The point is that in the parts of Britain where there is effectively full employment, most people with health problems or disabilities do work. What happens in labour markets that are operating below full employment is that men and women with health problems are amongst those who find it most difficult to secure and hold on to employment, and when they are out-of-work their health problems qualify them to claim Incapacity Benefit rather than Jobseeker's Allowance. They therefore drop out not only from employment but also from recorded, claimant unemployment.

Table 3 presents these new estimates of the diversion from unemployment to sickness benefits, for each district in the East Midlands in August 2003. The districts are ranked from highest to lowest on the basis of the estimated rate of hidden unemployment among sickness claimants. There are three parts to the table.

The first two columns show the actual number of sickness-related claimants of working age (16-59/64) in each district, from DWP benefit records. This figure refers to recipients of Incapacity Benefit, NI credits for incapacity (for those without

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<sup>4</sup> See C. Beatty and S. Fothergill (2004) *The Diversion from 'Unemployment' to 'Sickness' Across British Regions and Districts*, CRESR, Sheffield Hallam University.

**Table 3: Estimated diversion from unemployment to sickness benefits by district in the East Midlands, August 2003**

	Sickness claimants		Full employment benchmark		Diversion from unemployment	
	no	% w. age	no	% w. age	no	% w. age
Mansfield	6,900	11.6	2,800	4.8	4,100	6.8
Bolsover	5,100	11.6	2,100	4.8	3,000	6.8
Chesterfield	6,900	11.5	2,900	4.9	4,000	6.6
East Lindsey	7,700	10.2	3,800	5.1	3,900	5.1
Ashfield	7,100	10.0	3,200	4.5	3,900	5.5
Nottingham	17,400	9.9	9,000	5.1	8,400	4.8
Lincoln	4,900	9.1	2,500	4.7	2,400	4.4
Bassetlaw	6,000	9.0	2,500	3.8	3,500	5.3
Corby	2,800	8.5	1,200	3.7	1,600	4.8
Leicester	15,100	8.4	8,200	4.5	6,900	3.9
Newark and Sherwood	5,000	7.8	2,400	3.8	2,600	4.0
Amber Valley	5,600	7.8	3,000	4.2	2,600	3.6
Boston	2,600	7.8	1,400	4.1	1,200	3.7
Derby	10,600	7.8	5,700	4.2	4,900	3.6
North East Derbyshire	4,500	7.6	2,400	4.1	2,100	3.5
West Lindsey	3,600	7.5	2,000	4.1	1,600	3.4
Erewash	4,200	6.2	2,800	4.1	1,400	2.1
Gedling	4,200	6.1	2,500	3.6	1,700	2.5
South Derbyshire	3,100	5.9	1,700	3.3	1,400	2.6
Broxtowe	3,900	5.8	2,400	3.5	1,500	2.3
North West Leicestershire	3,100	5.8	1,900	3.5	1,200	2.3
High Peak	3,200	5.8	2,300	4.1	900	1.6
Wellingborough	2,600	5.7	1,700	3.8	900	1.9
Kettering	2,900	5.7	1,900	3.7	1,000	2.0
South Holland	2,500	5.5	2,000	4.4	500	1.1
North Kesteven	3,000	5.2	2,600	4.5	400	0.7
Northampton	6,300	5.1	5,200	4.2	1,100	0.9
Oadby and Wigston	1,600	4.6	1,000	3.0	600	1.6
Hinckley and Bosworth	2,800	4.5	2,200	3.5	600	0.9
Rushcliffe	2,900	4.4	2,700	4.0	300	0.4
South Kesteven	3,300	4.3	2,800	3.7	500	0.7
Daventry	1,900	4.1	1,400	3.0	500	1.2
Derbyshire Dales	1,700	4.1	1,500	3.7	200	0.4
Charnwood	4,000	4.1	3,200	3.3	800	0.8
Blaby	2,300	4.1	2,000	3.5	300	0.5
East Northamptonshire	1,900	3.9	1,600	3.4	300	0.5
Rutland	700	3.4	700	3.2	0	0.2
Harborough	1,500	3.1	1,700	3.5	0	0.0
Melton	900	3.0	1,000	3.5	0	0.0
South Northamptonshire	1,400	2.7	1,500	3.0	0	0.0
East Midlands	177,700	6.8	105,600	4.1	72,600	2.8

Sources: DWP and author's estimates

sufficient credits to qualify for IB itself) and Severe Disablement Allowance. None of these people are included in the unemployment claimant count. The first column shows the absolute number in each district, and the second expresses this as a percentage of the total population of working age in the district.

The third and fourth columns show the 'benchmark' for each district. This shows the sickness claimant number and rate that could be expected if there was full employment in that district.

The fifth and sixth columns show the estimated scale of the diversion from unemployment to sickness benefits in each district.

Across the East Midlands as a whole, 177,700 adults of working age were out of work and claiming sickness-related benefits in August 2003. This represented 6.8 per cent of the entire working age population of the region. This headline figure was up very slightly from the total of 176,000 in August 2001 used in the earlier East Midlands study, and was made up of 105,400 men and 72,300 women. These numbers need to be seen in context. In May 2004 for example, only 38,600 men and 14,400 women were claimant unemployed in the East Midlands.

The geographical distribution of sickness claimants within the region reveals strong and systematic patterns. The highest sickness benefit rates are in the former coalfield districts of North Nottinghamshire and North Derbyshire. Mansfield and Bolsover are the extreme cases: here around one in nine of all adults of working age are sickness claimants. East Lindsey, on the Lincolnshire coast, also has a high sickness claimant rate. The region's three largest cities (Nottingham, Derby, Leicester) have the largest numbers of sickness claimants, but this represents a smaller proportion of their working age population, though still considerably more than in surrounding suburban districts. In the south of the region there is an extensive swathe of districts where sickness claimant rates are much lower, generally in the 3 to 5 per cent range.

The 'benchmark' number of sickness claimants in the East Midlands region is 105,600, made up of 65,100 men and 40,500 women. This is an estimate of the sickness claimant level in the region that might be achieved in the context of full employment everywhere, and below which the figure would be unlikely to sink in the absence of improvements underlying levels of health or changes in the ways that the

benefits system, the employment services and employers operate. The figure is principally a reflection of present-day sickness claimant rates in fully-employed parts of the South, with an adjustment for underlying differences in health between the South and the East Midlands. The benchmark does not vary enormously across the region but is a little higher in former coalfield districts, for example, reflecting higher underlying levels of incapacitating ill health.

The difference between the number of sickness claimants of working age in the region and the benchmark represents the estimated scale of hidden unemployment among this group. For the region as a whole the figures point to over 72,000 hidden unemployed, or 2.8 per cent of the total working age population, made up of just over 40,000 men and nearly 32,000 women. What is particularly worth noting is that the estimated scale of hidden unemployment among this group exceeds the current figure for claimant unemployment in the region (53,000 in May 2004).

The estimated scale of hidden unemployment among sickness claimants varies considerably across the region. In three districts – South Northamptonshire, Melton and Harborough – it is estimated that there is no hidden unemployment at all in this category. Indeed, in these three districts the number of claimants is actually fractionally below the benchmark. What this is in effect saying is that three districts are already at or very close to full employment and that just about all those people with health problems who might work do so already.

There is a further group of 15 districts, mostly in the southern half of the region, where the estimated hidden unemployment among sickness claimants represents less than 2 per cent of the working age population. In these 15 districts as a whole, it is estimated that there are fewer than 7,000 hidden unemployed in this category.

In contrast there is a group of ten districts where hidden unemployment among sickness claimants is estimated to account for between 4 and 7 per cent of the working age population. In these ten districts as a whole, more than 37,000 men and women fall into this category. Mansfield and Bolsover are again the extreme cases, both with nearly 7 per cent of adults of working age estimated to be hidden unemployed in this way. Of the ten districts, six are former coalmining areas (Mansfield, Bolsover, Chesterfield, Ashfield, Bassetlaw and Newark and Sherwood).

The region's three largest cities all have relatively high hidden unemployment, with one (Nottingham) coming eighth on the list. However, in each case the district boundary is drawn tightly around the urban core, excluding substantial commuter areas where hidden unemployment is estimated to be much lower. Taken as a whole, the region's three largest urban areas have rates of hidden unemployment that are well below those in the former mining areas.

## 5. SURVEY EVIDENCE ON IB CLAIMANTS IN THE EAST MIDLANDS

During the late 1990s the present authors undertook substantial survey work covering men of working age who had become detached from the labour market<sup>5</sup>. A high proportion of these men were Incapacity Benefit claimants. Two of the survey areas were in the East Midlands – Chesterfield and Northampton. Subsequent surveys in other parts of the country<sup>6</sup> indicate that the main features of this group of non-employed men have not altered greatly in recent years. The East Midlands survey data therefore still provides important insights into this important group.

Chesterfield and Northampton illustrate the contrasting labour market circumstances within the East Midlands. In August 2003, according to DWP data, Chesterfield had 4,200 men of working age out-of-work and claiming sickness-related benefits (mainly Incapacity Benefit), representing a claimant rate of 13.5 per cent. In Northampton, a rather larger town, the equivalent figures were 3,900 men representing a rate of 6.2 per cent. Our estimates of hidden unemployment among these men<sup>7</sup> are 2,500 in Chesterfield and 800 in Northampton, representing rates of 8.0 per cent and 1.3 per cent respectively.

Table 4 presents descriptive data on the key characteristics of male IB claimants in these two East Midlands towns. This information is based on face-to-face interviews with 156 men in Chesterfield and 134 in Northampton, from a representative sample of enumeration districts in each town.

There are a number of similarities between male IB claimants in Chesterfield and Northampton:

- In both towns, around three-quarters are manual workers

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<sup>5</sup> See in particular P. Alcock, C. Beatty, S. Fothergill, R. Macmillan and S. Yeandle (2003) *Work to Welfare: how men become detached from the labour market*, CUP, Cambridge.

<sup>6</sup> For example C. Beatty, S. Fothergill and N. Barraclough (2003) *Unemployment and Economic Inactivity in Britain's Seaside Towns*, CRESR, Sheffield Hallam University.

<sup>7</sup> C. Beatty and S. Fothergill (2004) op. cit.



- Around 40 per cent have no formal qualifications (though this proportion will have fallen since the time of the survey as an older cohort who left school at 14 or 15 reaches state pension age)
- Around half have been out of work for at least five years
- Relatively few are active job seekers, though more looked for work when their last job ended
- Nearly all report health limitations on the work they can do

**Table 4: Key characteristics of male IB claimants aged 25-64**

	<b>Chesterfield (%)</b>	<b>Northampton (%)</b>
<b>Personal attributes</b>		
Age 50+	64	53
No formal qualifications	39	44
Manual occupation	74	75
<b>Labour market attachment</b>		
5 yrs or more since last F-T job	53	50
10 yrs or more in last F-T job	57	42
Would like a F-T job	45	62
Looked for job after last job ended	25	26
Looking now	7	9
<b>Health</b>		
Health = main reason for job loss	44	60
Some health limitation	95	99
Can't do any work	11	21

Source: Sheffield Hallam survey data

There are however also important differences between male IB claimants in the two towns:

- Male IB claimants in Chesterfield are a somewhat older group – nearly two-thirds are over 50, compared to just over half in Northampton

- Chesterfield claimants are more likely to have held their last job for ten years or more
- More of the Northampton claimants say they would still like a full-time job
- Northampton claimants are more likely to have lost their last job mainly because of ill health or injury
- Northampton claimants are more likely to say that they can't do any work in any circumstances

These differences are not arbitrary or a reflection of sampling error. They reflect general trends that can be observed among male IB claimants across a range of survey areas. In general, where IB claimants are more numerous (eg Chesterfield) they are more likely to display greater detachment from the labour market despite substantial previous employment histories. They bear the hallmarks of group that has been pushed out of employment by restructuring and has not found a way back. Where IB claimants are less numerous (eg in Northampton) ill health or injury is more likely to lie at the root of job loss and continuing non-employment, even though the desire to work can remain strong. The differences between Chesterfield and Northampton therefore probably offer insights into the differences between IB claimants in the north and south of the East Midlands region more generally.

Table 5 looks at the financial circumstances of these men. There are again important similarities – a sizeable minority have pension income, and between a third and a half also claim means-tested benefits (eg Income Support, Council Tax Benefit) as a top-up to Incapacity Benefit. The differences between the towns are however at least as illuminating. On four of the five indicators, male IB claimants in Chesterfield appear to be a better off group than male IB claimants in Northampton. In Chesterfield, they are more likely to have pension income (from private or occupational schemes), more likely to have a redundancy lump-sum, more likely to own their home outright, and less likely to claim means-tested benefits. The exception is having a partner in work, which is more prevalent in Northampton. Male IB claimants in Chesterfield are therefore not only more numerous but also on balance somewhat better off. This is once more a tendency that can be observed

across a range of survey areas, rather than an observation specific to these two East Midland towns<sup>8</sup>.

What this survey information does is reinforce the impression that where there are relatively small numbers of IB claimants, as in Northampton, they are a more marginalized, disadvantaged group. In Northampton, and surrounding parts of the southern half of the East Midlands, male IB claimants are predominantly a group that faces greater health problems, has always found it difficult to find and retain a place in the labour market, and is less well-off as a result. In contrast in Chesterfield, and other areas with high numbers of IB claimants, there is clear evidence of a cohort of claimants passing through the system who have substantial work histories but have been made redundant by their previous employers. They have not re-entered employment and their joblessness now shows up in IB data rather than unemployment figures.

**Table 5: Selected financial circumstances of male IB claimants**

	<b>Chesterfield (%)</b>	<b>Northampton (%)</b>
Pension income	40	26
Lump-sum redundancy pay	21	8
Means tested benefits	37	48
Own home outright	25	19
Partner in work	27	33

Source: Sheffield Hallam survey data

<sup>8</sup> P. Alcock, C. Beatty, S. Fothergill, R. Macmillan and S. Yeandle (2003) op.cit.

## 6. THE IMPLICATIONS FOR POLICY DEVELOPMENT

### Key empirical observations

The evidence in the previous sections highlights five key observations that it is essential to bear in mind in designing labour market policies for the East Midlands:

- There is substantial hidden unemployment in the region. Despite sustained economic growth since the mid 1990s, there are around 120,000 men and women in the region who could be described as unemployed who are not included in the unemployment claimant count. This hidden unemployment is more than double the claimant count itself.
- Men and women who have been diverted onto sickness benefits, principally Incapacity Benefit, are by far the largest group among the hidden unemployed. We estimate that some 72,000 people fall into this category, or about four out of ten currently claiming these benefits. These are people who could reasonably be expected to have been in work in a fully-employed economy. They do not represent fraudulent claims.
- There are also substantial numbers of hidden unemployed who are looking for work and available for work but are not claiming either Jobseeker's Allowance or Incapacity Benefit. Women are especially well represented among this group.
- Hidden unemployment is unevenly spread across the East Midlands. In general, the areas with the highest claimant unemployment have the highest hidden unemployment. There is little evidence of substantial hidden unemployment across large parts of the southern half of the region. The worst concentrations are in the former coalmining districts of Nottinghamshire and Derbyshire.
- There is also evidence that joblessness among IB claimants in southern parts of the region, such as Northampton, is qualitatively different to that in other parts of the region where it is more widespread. Where IB claimants are less

numerous they are also more disadvantaged and likely to face greater personal obstacles to re-employment.

## **Two competing perspectives**

It is important to be aware that there are two competing perspectives concerning the scale and location of hidden unemployment across the UK. What the perspectives share is the view that there are very large numbers of working age adults who are not conventionally unemployed but who could – indeed should – be re-engaged with the labour market. Many of these people are benefit claimants, so a shift into employment would cut public expenditure and raise national output as well as address levels of poverty and social exclusion. Where the perspectives differ is in their assessment of the causes and solutions.

### *The supply-side perspective*

This is the perspective presently adopted by the Treasury and the Department for Work and Pensions. It is most fully articulated in the December 2003 report *Full Employment in Every Region*<sup>9</sup>. The argument is that plenty of jobs are becoming available all the time everywhere, and that the geographical distribution of benefit claimants, such as IB claimants, bears little relationship to the local availability of employment. Continuing non-employment and benefit dependency is therefore best understood by reference to skill levels, motivation and financial disincentives to work.

In this supply-side perspective, the correct policy approach is therefore to provide training and practical support, address issues of motivation, and ensure that the tax and benefits system makes working a worthwhile proposition. The implicit assumption is that if supply-side obstacles are addressed, individuals will find work.

In particular, the Treasury/DWP view is that if someone does not actively look for work they cannot be described as 'unemployed'. Many of the people who are identified as 'hidden unemployed' in the present paper do not look for work, so in the

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<sup>9</sup> HM Treasury and DWP (2003) *Full Employment in Every Region*, Treasury and DWP, London.

Treasury/DWP view they should be described instead as 'inactive', even though many of them are legitimate targets for labour market policies.

### *The demand-side perspective*

The Treasury/DWP view is not shared by the majority of urban and regional analysts<sup>10</sup>. Their view is that while there are elements of the supply-side perspective that have validity - more so in some parts of the country than others, and especially in understanding differences in claimant rates at the neighbourhood scale – the primary explanation for the distribution of JSA and IB claimants at the district, county and regional scales lies with labour demand.

According to this view, where labour demand is weak there are more people out-of-work on unemployment-related benefits and more people parked on Incapacity Benefit as well. The large numbers on Incapacity Benefit in some areas are the last to be taken up in an economic upswing because they are the least active job seekers and often the men and women with the greatest personal obstacles to re-employment.

From the demand-side perspective, therefore, supply-side measures have a supporting role but the primary solution lies with increasing the supply of jobs. The stronger the demand for labour, the lower claimant unemployment and the lower the number of hidden unemployed on benefits like IB.

### **Three strategic questions**

It is important to be aware of this fundamental divergence of perspectives because it determines the answers to three questions that matter a great deal to the policy response in the East Midlands.

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<sup>10</sup> See for example J. Adams, P. Robinson and A. Vigor (2003) *A New Regional Policy for the UK*, Institute for Public Policy Research, London.

*Q: Will the very large numbers on Incapacity Benefit simply fade away as a generation reaches state pension age?*

There is little dispute that many of the IB claimants in places such as North Nottinghamshire and North Derbyshire are men (and to a lesser extent women) who were made redundant during the great waves of industrial restructuring in the 1980s and early 1990s. Many are in their fifties and early sixties and have now been on Incapacity benefit for many years. They sometimes left employment with a financial package (redundancy money, early access to a pension) that enables them to get by without working. Realistically, the chances of re-attaching many of these men and women to paid employment are nil, and many would not want to work again. However, over the next decade or so most of these claimants will finally reach state pension age and thereby drop off IB. The question is whether this will lead to smaller numbers of IB claimants, and more generally to fewer non-employed working age adults.

The supply-side perspective would say 'yes'. This is a cohort whose labour market detachment is now deeply entrenched, but there is no reason to believe that the cohorts following them should face labour market or personal circumstances that should so comprehensively disengage them from paid employment.

The demand-side perspective would say 'no'. The diversion onto benefits such as IB is the single most important way in which the imbalances in local labour markets have been resolved in the wake of large-scale job loss. Crucially, as an older generation on IB reaches state pension age, they will not free up jobs for the generations behind them or the young people reaching working age. Therefore if the numbers on Incapacity Benefit were to fall – and it is now not so easy to access IB as before 1995 when the rules were tightened – and if there were to be no corresponding increase in the local stock of jobs, the continuing imbalance in local labour markets will emerge in other ways. Out-migration, increased out-commuting, and higher claimant unemployment are among the possibilities. In other words, the passing of a generation into retirement does not solve the problem, it only transfers the problem elsewhere.

*Q: Will additional labour supply generate its own demand?*

This is an old question in economics. It is central to assessing whether efforts to re-attach the hidden unemployed to the labour market will lead to a net increase in employment or simply displace others who would have been in work.

The supply-side perspective on the contemporary UK labour market, articulated by the Treasury and DWP, is that there is no shortage of job opportunities. Therefore if the large numbers of economically inactive adults of working age can be trained and motivated to look for work they will find employment that does not displace other workers. This is a fairly extreme view of how labour markets work. A more moderate supply-side view would be that extra labour supply would tend to generate extra labour demand by pushing down the level of wages. The market would tend to 'clear' – ie supply and demand would come into balance – but only at the expense of lower wages in the bottom-end segments of the labour market where most additional supply would be concentrated.

The demand-side view is that labour markets in countries like the UK don't work that way. There may be limited occupations or locations where labour is in short supply, and where an increase in supply would allow bottled-up expansion. But more generally wage adjustments are slow at best and do not succeed in bringing labour supply and demand into balance. The effect of additional labour supply will therefore in many circumstances be additional unemployment.

*Q: Will current national labour market policies deliver lower levels of joblessness?*

It is important to distinguish here between on the one hand macroeconomic policies (interest rates, exchange rates, fiscal policy etc) that impact on the labour market and on the other hand interventions directly in the labour market itself (training, Jobcentre Plus, benefits etc). Unquestionably, the policies pursued by the present government have delivered higher employment and lower joblessness, however defined. Whether this improvement has much to do with labour market intervention, as opposed to macroeconomics, is more questionable.



This is not the place to list or assess all the labour market interventions in operation or under development<sup>11</sup>. The point is that the policies being pursued under the umbrella of the DWP and DfES nearly all fall into the supply-side category. This is perhaps inevitable – it is not their brief to do anything else. Moreover, even those labour market policies that are usually described as ‘demand-led’ are in fact about adjusting labour supply to respond better to employers’ needs. From the supply-side perspective this focus on supply-side measures is of course entirely correct.

The demand-side perspective on DWP and DfES policies is more guarded. It is important that there is a plentiful and skilled labour supply, and that shortages are eliminated so that economic activity is not frustrated. But as noted earlier, extra labour supply cannot be relied upon to deliver extra labour demand. Therefore it is important that labour supply interventions are complemented by measures that promote demand – appropriate macroeconomic policies, and the right package of regional economic development measures to boost labour demand in the least prosperous areas.

Fortunately, despite the posturing in documents such as *Full Employment in Every Region* the reality is that the present government does not pursue supply-side labour market policies to the exclusion of attempts to manipulate labour demand through national regional and local policies. The backdrop to labour market interventions in the East Midlands is therefore that in practice they are not the only tools available to help deliver full employment, and it should not be assumed that they are the most important tools either.

### **Policy recommendations for the East Midlands**

**RECOMMENDATION 1:** *The emphasis among labour market interventions needs to shift away from the claimant unemployed towards other jobless groups*

Economic growth since the mid 1990s has made substantial in-roads into the numbers of claimant unemployed – ie those who are out-of-work and claiming Jobseeker’s Allowance. Growth has much less impact on the numbers in other non-employed groups, especially those claiming sickness-related benefits such as

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<sup>11</sup> For a full exposition of current policies see DWP (2004) *Building on New Deal: local solutions meeting individual needs*, DWP, London.

Incapacity Benefit. The number of non-employed working-age adults claiming benefits other than JSA now far exceeds the number of conventional, claimant unemployed.

The evidence shows that there is extensive hidden unemployment in the East Midlands. Many of the hidden unemployed are IB claimants who could reasonably be expected to have been in work in a fully-employed economy. There are also large numbers of unemployed, especially women, who have been diverted out of the benefits system altogether.

These groups of 'hidden' unemployed are not as easy to target as JSA claimants, not least because they have little if any regular contact with the employment services. However, they represent by some margin the largest labour reserve available within the East Midlands. They also represent the bulk of the East Midlands' on-going 'unemployment problem'. Nevertheless, they are a challenging target group that mostly requires more intensive support than JSA clients.

The precise ways in which employment and training services within the region should be re-focussed is something that needs to be worked out by partner organisations in the region. It is worth noting however that central government thinking is already moving along these lines and it is important that regional organisations therefore take full advantage of the policy shifts and revised tools that emerge from Whitehall.

*RECOMMENDATION 2: Sensitivity to the circumstances of IB claimants is essential, and none should be 'hounded'*

Any shift in emphasis away from JSA claimants towards other non-employed groups will inevitably bring the huge numbers of Incapacity Benefit claimants into the scope of labour market interventions.

The important point here is to remember that IB claimants are a diverse group – from those who would work if suitable employment were available through to those who are unable to undertake any work in any circumstances. The estimates presented earlier indicated that only around four out of ten sickness claimants of working age in the region might be regarded as 'hidden unemployed' in the sense that they could be expected to be in work in a fully-employed economy. They account for large

numbers – more than 70,000 – but that still leaves some 100,000 sickness claimants in the region who should not perhaps be regarded as legitimate targets. Furthermore, at the level of the individual it is not easy to make an allocation between the two groups.

What this means in practice is that interventions directed at IB claimants need to proceed with sensitivity. They need to recognise that the health constraints are very real and that the benefit claims are legitimate, even if some individuals might be successfully re-engaged with employment.

*RECOMMENDATION 3: The north and south of the East Midlands region require rather different labour market policies*

The East Midlands is not a cohesive region in labour market terms. The division is broadly a north-south one, though the fine-grain geography is more complex. The south of the region is already at or close to full employment, with low claimant unemployment and little estimated hidden unemployment. IB claimant rates across much of the south are low. In contrast the north of the region, especially the former coalfield, shows clear evidence of continuing and substantial labour market imbalance, with higher claimant unemployment and even higher hidden unemployment.

This requires a differentiated response. In the south, policies to boost labour demand have little relevance at present. In the north, the scale of continuing joblessness suggests that boosting labour demand remains the central way forward. In the north, the emphasis needs to remain on traditional economic development measures such as the provision of sites and premises and business support aimed at expanding local firms and attracting inward investors. The expectations placed on purely labour market interventions in the north of the region need to be limited: they can support job creation and development but they can never be the central solution to continuing joblessness and benefits dependency.

*RECOMMENDATION 4: In the south of the region, the primary aim of labour market intervention should be to support the individual*

With little evidence of a shortfall in the demand for labour across much of the southern half of the East Midlands, the logical conclusion is that the modest continuing unemployment there is primarily a reflection of the difficulties that individuals themselves face in taking up jobs. In the south of the region, the Treasury/DWP supply-side view has unquestioned validity.

It is in the south of the region that the full range of policy tools on offer from DWP and DfES therefore offer the key to further reducing joblessness and benefit dependency. Motivate the individual, provide them with training and practical support, and ensure there are no perverse financial disincentives, and they should be able to find employment in this part of the region.

The difficulties are two-fold. First, there simply aren't that many men and women in the target groups in this southern half of the region. Most people in this half of the region who could work already do so. Second, the residual non-employed are a potentially difficult group, requiring more intensive and personalised support than their counterparts in the north of the region. Often they will be people with greater health problems, and perhaps a less substantial employment history as well.

*RECOMMENDATION 5: In the north of the region, the primary aim of labour market intervention should be to address employers' needs*

There is only limited value in training or motivating people for work if at the end of the day those people find their hopes of employment dashed, or indeed if their employment means that someone else who is equally well-qualified is pushed out of work instead. This was the classic argument against some government schemes in the 1980s and 90s. In the context of a tighter labour market the argument has relevance in fewer places and across fewer segments of the labour market, but it has not lost its validity entirely.

In areas that still fall well short of full employment, such as the northern half of the East Midlands, training needs to be focussed on occupations for which there is a demonstrable shortage of supply. By targeting unmet demand, bottled-up business

expansion will be facilitated and consumer services will become more readily available and at lower cost. Training for occupations that are already in over-supply, or simply to allow employers to set unnecessarily high entry standards, is altogether more questionable.

Identifying the precise occupations to be targeted is again a job for local partners. Plumbers and lorry drivers are two examples of manual occupations for which there is an acknowledged shortage of skilled workers in most parts of the country, and there are no doubt others including shortages of many white-collar and professional skills. What this means in practice in the northern half of the East Midlands is that the proper starting point for training policies needs to be an accurate assessment of employers' needs. Training for 'stock', without clear evidence of present or likely future demand, runs the risk of proving wasteful and frustrating.