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Unemployment, labour slack and labour market accounting. Theory, measurement and policy
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SUMMARY

This study investigates how our understanding of unemployment and the utilisation of labour resources can be refined by the application of a system of labour market accounts and a new measure of labour slack.

Labour market accounts and the labour slack estimate are innovations stressed in this book. The former intend to organize labour market data into a coherent and consistent system of accounts. In these accounts the total available labour resources expressed both in persons and in hours are broken down in various types of activities. The labour slack estimate is an indicator of the degree of non-utilisation of labour resources that mitigates the shortcomings of the traditional unemployment rate. It takes into account non-utilised labour time due to unemployment, due to changes of the number of hours actually worked and due to changes in labour force participation. The labour market accounting framework is discussed in chapter III; the construction of the labour slack estimate is explained in the second part of chapter V. The state of the art in unemployment theory is summarized in the first chapter, while the second chapter and appendix C review the shortcomings of the traditional concepts (unemployment, employment, labour force) and of adjusted measures critically. Chapters four to six and appendices E to H illustrate how the information provided by the labour market accounts and the labour slack estimate may enrich labour market analysis.

The first chapter is devoted to the discussion of recent developments in the theory of unemployment. Recently acknowledged theoretical insights stemming from developments within the Pigouvian and the Keynesian tradition are discussed.

Following Pigou's track, the search theory basically describes the larger part of unemployment as the by-product of adjustment processes within the economy. Since, however, unemployment rose sharply and its average duration became longer, explanations for these phenomena are advanced, emphasizing the structural character of current unemployment without abandoning the appealing framework of the search theory.

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Unemployment theory within to the Pigouvian tradition tries to explain increases in the "natural rate of unemployment" (or the non-accelerating-inflation-rate of unemployment - NAIRU) and develop of what now may be called "Equilibrium Unemployment Theory" (Pissarides 1988). This bundle of theories is intended to explain wage rigidity by introducing institutional, social and behavioural changes in the labour market (taking into account minimum wages, social security benefits, labour unions, implicit contracts, social custom, efficiency wages) adverse selection and job matching deficiencies).

Unemployment theory within the Keynesian tradition on the other hand, analyses the sufficient and/or necessary conditions for a non-cleared labour market within a macroeconomic framework. The "non-Walrasian equilibrium model" (or disequilibrium theory of unemployment) shows that the economy tends to a stable and persistent situation that is unlikely to be characterised by Walrasian conditions; that is a situation where all markets are cleared simultaneously through price flexibility. The crucial element in the "non-Walrasian equilibrium analysis" is the assumption that prices and wages are rigid on the short term, while quantities can be adjusted more easily and frequently. The analysis results in three main conclusions. First, there is a second type of macroeconomic unemployment beyond the commonly accepted Keynesian unemployment, called classical unemployment. Second, Keynesian unemployment is likely to occur more often. Third, the nature of unemployment is not easy to determine and therefore therapies to combat unemployment are surrounded by many uncertainties.

The second main section of the first chapter elaborates the attempts to determine the nature of unemployment and to subdivide aggregate unemployment according to type and origin in order to diagnose the causes of unemployment as a basis for remedial action. It is argued that it is extremely difficult to distinguish unemployment due to one cause from unemployment due to other causes without a general model. The precise demarcation between the types of unemployment and the relative importance of the types is highly dependent on the theoretical assumptions and the operational decisions made within or on behalf of the models. The first section of chapter I indicated that the analyses of both theoretical schools have many unresolved prob-

lems. Mainly for this reason an undisputed analysis of the nature of unemployment is therefore not within our means, if ever. However, some theoretical convergence may be seen. Both the equilibrium unemployment theory and the non-Walrasian equilibrium theory (disequilibrium theory) stem from Walrasian general equilibrium analysis. Therefore they have some features in common (the assumption on price rigidity being the most important). It is, however, not clear at this moment how these approaches may be fully integrated. Especially the combination of macroeconomic demand effects with the assumptions of perfectly coherent individual behaviour seems to be most difficult. As to the rest of this book, however, the measurement of the volume of unemployment (labour slack) is emphasized. Our concern is mainly confined to the task of ameliorating measurement.

Chapter two discusses the advantages and disadvantages of the unemployment rate and related measures of labour capacity utilisation. The analysis leads to the following conclusions:

- registration data, used to calculate official unemployment rates in some countries do not guarantee a reliable estimate of the number of unemployed;
- the traditional unemployment rate shows a cyclical bias due to the discouraged (added) worker effect and to labour hoarding and dis-hoarding;
- differences in the impact of legislation and government policy upon the labour force introduce problems of intertemporal and international comparability;
- due to significant changes in the number or hours actually worked, the unemployment rate, expressed in persons, underestimates real labour slack.

In the remaining chapters a system of labour market accounts is developed and applied to the post-World-War-II developments in eight countries. The third chapter formulates four requirements that a system of labour market accounts should meet:

- the employment recruitment base should be better defined than in the traditional labour force account;
- the data should be counted in both persons and hours;

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- the figures should be given with enough detail to discern compositional shifts;
- the data should be organized in a way that allows monitoring the impact of social and economic policy.

These requirements are further refined and compared to the properties of similar accounts in the literature. The basic outline for the construction of the labour market accounts is spelled out and the practical difficulties of filling the accounts for the eight countries. The third chapter concludes with a first global application of the accounts.

The next chapter (IV) describes and discusses intertemporal and international differences in the utilisation of labour resources using information provided by the empirically filled labour market accounts for the eight countries under study. The detailed survey starts by close inspection of population growth and labour market participation. It illustrates the type of information that is provided by the labour market accounts. Moreover, it stresses the importance of international and intertemporal differences in participation rates and in the annual average hours actually worked when the utilisation and non-utilisation of labour resources are discussed. These observations are particularly meaningful discussing the construction of a labour slack estimate in the fifth chapter.

Chapter V starts with a more traditional analysis of the non-utilised labour resources in terms of unemployment, non-participation (according to reason) and absences from the job. The second part of the chapter is devoted to the construction of a new labour slack estimate. The labour slack estimate is intended to provide an accurate cyclical indicator of non-utilised labour time, taking unemployment, non-participation and the average annual working time into account and mitigating the shortcomings of the traditional unemployment rate (see chapter II). The labour slack estimate is applied to post-1973 data for four countries (Canada, the Netherlands, Sweden and the U.S.A.). It is argued that our labour slack ratio (LST/AALT) is a meaningful measure that may prove to be useful in international comparative and intertemporal studies.

The final chapter makes an attempt to use the information provided by the labour market accounts in order to estimate the impact of policy measures. Since, however, policy practices differ widely between countries and a complete survey of them (and their impact) would certainly require more than one chapter, the discussion is confined to the impact of working time reduction policies. Since a reduction of working time definitely alters the utilisation and non-utilisation of labour resources, while leaving the traditional indicators (unemployment, employment) unchanged, it can be used as an illustration of the significance of the information provided by the labour market accounts. Preceding this discussion on a taxonomic framework classifying labour market policy instruments is given. It focusses on the effects of the policy measures and distinguishes between policy actions that:

- adjust the price of labour;
- adjust the volume of labour supply;
- adjust the volume of demand for labour;
- adjust labour mobility by influencing the match of demand and supply.

As to the effects of policies to reduce working time, the labour market accounts developed in chapter III broadens the scope of the analysis. They direct our attention to policies, not intended to reduce working time but having a similar effect (institutional arrangements for being absent from the job or regarding early retirement and postponed entrance to the market) on the one hand, and to more general effects like changes in the time actually worked and the working time throughout the life cycle.

The modest employment effects realised recently through such measures in many European countries give weight to the conclusion that working time reduction is not a panacea for the unemployment problem.

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