



Economic Affairs Committee

Corrected oral evidence: UK labour supply

Thursday 13 October 2022

11.05 am

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Members present: Lord Bridges of Headley (The Chair); Viscount Chandos; Lord Griffiths of Fforestfach; Lord Layard; Lord Livingston of Parkhead; Lord Monks; Baroness Noakes; Lord Rooker; Lord Skidelsky.

Evidence Session No. 5

Heard in Public

Questions 50 - 57

Witnesses

[II](#): Hannah Slaughter, Senior Economist, Resolution Foundation; Ian Stewart, Partner and Chief Economist, Deloitte.

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Examination of witnesses

Hannah Slaughter and Ian Stewart.

Q50 **The Chair:** Welcome to this second session this morning of our inquiry into where all the workers have gone. Would you like to introduce yourselves, please?

Hannah Slaughter: I am a senior economist at the Resolution Foundation. We are an independent think tank. I focus on the labour market.

Ian Stewart: I am the chief economist at Deloitte, the business services firm.

Q51 **The Chair:** Thank you both for coming. It is very good to see you. I will start with the big question. In your minds, if you had to pick one cause for the labour shortages we currently see, what would that be?

Hannah Slaughter: Just a small question, then.

The Chair: Yes, it is just to put you on the spot.

Hannah Slaughter: The overall impact of the pandemic has been really stark. It changed the labour market as we knew it completely. With the big shutdowns of lots of different sectors, we did not see as many people as we were worried about losing their jobs. Instead, people took time out of work through the furlough scheme and then perhaps reconsidered their situations.

Some people did lose their jobs, although far fewer than we were expecting, thankfully. It was also an opportunity for some people, particularly older workers, to choose to leave the labour force and retire. On top of that, the health impacts of the pandemic have driven us further in that direction. I am not sure that was a single answer.

Ian Stewart: When the pandemic-related recession started, economists expected there to be a lot of scarring in the labour market. They were expecting the pandemic to have a big effect on unemployment for perhaps years to come. What we got wrong was that the scale of the support from government meant there was a very quick rebound in the labour market, but the scarring manifested in terms of not unemployment but inactivity.

It is a huge dislocation. It is worth remembering that this is the biggest dislocation in terms of GDP that we have seen in 300 years. We got it wrong because we were not sufficiently focused on the effects that this would have on inactivity.

The Chair: To what extent are the shortages due to search misallocation?

Ian Stewart: That is an element. We know there are some sectors such as hospitality where employment is significantly lower now than it was

two years ago. Both searching for work and finding workers are easier now than they have ever been because of technology. There is much greater transparency. I know your inquiry is not about demand, but I am left with the feeling that this is a reflection of excess demand in the economy.

Hannah Slaughter: I would agree with that. Job-to-job moves and people starting new jobs have been close to record highs for the last year or so. It is not a case of people not being able to find the right jobs. There is churn in the labour market.

There may be some element of it taking time for people to find new jobs, especially if people were not able to move jobs during Covid. They are almost making up for it now by making moves and moving through the labour market when they were not able to over the past couple of years. It seems like the fact that the labour force is smaller is still having a noticeable effect and creating pinch points in certain sectors, as Ian said.

Lord Griffiths of Fforestfach: I ask my question first to Ian Stewart. Your argument was that the pandemic and the lockdown created a structural dislocation between different parts. If, say, shipping was affected, people at the ports were out of work and so on. Why would this give a longer-term shortage of labour?

Ian Stewart: The mechanism is partly inactivity. I know that you have spent a lot of time on that and the role that earlier retirement and illness have played in inactivity. We will come on to this, but the more I have looked into it, the less certain I am about the cause of the rise in inactivity.

The scale of the shock probably caused a shift in preferences for quite a lot of people. You have anecdotal stories about people changing between sectors, for instance from long-distance lorry drivers to shorter-haul delivery drivers on better terms.

We also have a cohort of workers in the over-50s, many of whom are very asset rich with low levels of debt. They are relatively financially independent. This is one difference between the UK and a lot of continental countries, where state pension provision is more important. In the UK, our system of pension provision probably gives people more autonomy about the timing of decisions on when they exit the labour market. These dislocations have had effects on inactivity through retirement, illness and the allocations of people.

Baroness Noakes: Ms Slaughter mentioned churn. I have been pondering the relationship between churn and vacancy levels. Do we have any good data on those and the correlation between the two?

Hannah Slaughter: I do not have to hand any formal analysis of the correlation but, as we have seen vacancies rising post pandemic to close to record highs, we have also seen a rise in the number of people starting

new jobs and moving into new jobs. From that we can derive a proxy measure of the time to fill a vacancy.

When the economy first started to open up, that fell massively. Businesses were able to fill their vacancies quickly because there were lots of people moving and vacancies were only just starting to grow. As time has gone on, we have seen that measure get much higher. It is now taking businesses longer to fill vacancies because, even though we have people moving through the labour market quite a lot, making those job moves and starting with new employers, the level of vacancies has grown.

Baroness Noakes: What data could I look at?

Hannah Slaughter: I can follow up after the session. There is data from the ONS on quarterly flows of workers.

The Chair: That would be very useful.

Baroness Noakes: That would be very helpful.

Lord Livingston of Parkhead: I have a very quick question. Have you seen any data that looks at people who were on furlough against inactivity today? Is there a connection there? If you were on furlough, is there more chance of you being inactive, particularly in the older groups?

Hannah Slaughter: I have not seen anything particularly recently. I remember that we looked at that in a report we did last autumn, which particularly focused on the older cohort. With older workers, as Ian was saying, lots of the people among that group who have left the labour force have essentially been able to do so because they have wealth or other sources of income within the household. They basically tended to be richer, whereas the people who were furloughed and might have been more at risk of job loss tended to be in lower-paying sectors.

There will be a cohort of people on furlough who have chosen to leave the labour market because it is really difficult to find a new job when you are older. We know that from previous research.

Lord Livingston of Parkhead: Going to the scarring point—Ian referred to it—you had scarring in offer rather than in demand, which was the assumption. I think you are saying that you have not seen it, but is there any data to say that, if you were furloughed, you have less chance of being economically active today than if you were not? Has that changed? I take the points you are making. If the answer is that you have not seen any data, this may be something we can follow up.

Ian Stewart: I have not seen any data. If that were the case, one might have expected higher unemployment to manifest at the end of furlough too. You would see furloughed workers being displaced into inactivity and unemployment. There is not really any evidence of that happening.

Lord Griffiths of Fforestfach: You are not saying, therefore, that the labour shortage is due to economic incentives changing. Rather, people

suddenly have a shock because of the pandemic, which may be an illness, a bereavement or whatever it is. It makes them evaluate and ask, "What do I want to do with the rest of my life?" Is it that kind of one-off change in tastes, as economists would call it, rather than a change in price, wage or economic incentive?

Ian Stewart: It seems to be more to do with capacity and preferences than the kind of change you get in labour markets where changes to the welfare system increase the incentives to seek work. It seems to be less due to economic factors and more due to capacity and preferences. We know there is abundant work. Although real incomes are falling now, real income growth in the early part of last year was increasing. It is quite an attractive labour market. It is quite hard to see economic incentives as being a really powerful factor in this.

Q52 **Lord Skidelsky:** I want to ask about changes in the UK labour supply compared with those of other countries. We know there is a different pattern. We are an outlier; we have the data on that. We go up and they all go on going down. That is the inactivity rate. First, why is this and, secondly, does it matter? Are these changes so marginal, really, that there is not a problem? There may be a European problem, but there is not a specific British problem that one ought to be concerned with.

Ian Stewart: Yes. The data are pretty clear about the UK having seen an unusual shock in terms of inactivity compared with most economies. The US saw a rise in inactivity initially, but it has now seen a sharp decline. The UK stands out in terms of inactivity.

The second part of your question probably gets neglected. How much does it matter? If inactivity is a concern because of its effect on labour market tightness, it may be less of a worry. If we look at the labour markets of Germany, the United States, Italy or France, they are running very hot. They have not had the same inactivity shock as we appear to have had, but they have problems with labour supply, too. If you look at very simple measures of labour supply, such as total employment plus vacancies over potential workforce, these economies are all running at not dissimilar levels relative to historic averages.

The UK data on labour shortages seem to be quite rich but, to the extent we can see data in Europe, labour shortages are really quite acute. Construction skills shortages in the European Union are at all-time highs, as are manufacturing skills shortages in France. We know that central banks are very concerned about excess demand in the labour market in Europe and the United States. It is quite an important point.

Hannah Slaughter: My main focus is more on the UK than international comparisons but, on the question of whether it matters, one aspect is who are the workers who have left the workforce and what skills have they taken with them? To the extent that a lot of the rise in inactivity has been among older workers, who have lots of built-up skills and experience, that will have an impact at the macroeconomic level.

The UK has been quite interesting in terms of the gender differences in participation. In contrast to lots of other countries, we saw a rise in participation among younger women, which is unique among countries. We are not quite sure exactly why. It might just be because of the differential sectoral make-up of the UK labour market in terms of gender. It might be because the furlough scheme protected jobs, whereas in countries such as the US we know that lots of women had to leave work to care for children. It is worth bearing in mind that that is one area where we have seen an increase in labour supply, which may be a good thing.

Lord Skidelsky: One reason why it might matter that the UK has a higher inactivity rate is that it might tend to give us a higher rate of inflation. That could have an effect on the currency and lots of things. In macro terms, that is probably where the problem lies, is it not?

Ian Stewart: I think it is. It is clear that the Bank of England is very concerned about the tightness of the labour market and the perception that there is excess demand. That problem has clearly been exacerbated by the factors we have been discussing. Yes, it is a macroeconomic problem. Central banks are seeking to address it. They cannot affect supply, but they are trying to affect demand.

In the long term, the labour supply is very important. Although we are aware that the UK is a relatively lower-productivity economy within major industrialised economies, it has also been an economy with very high participation rates and where, over time, there has been very strong growth in labour force participation, which has been very helpful to growth rates.

If this presaged a permanent reversal in this long-term rise in activity—I do not think it will—that would clearly be negative for the capacity of the economy to grow.

The Chair: Can I just pick up on a point you made, Mr Stewart, about EU comparisons? In the previous session, we were hearing about the high level of inactivity in Germany. How high is inactivity in Germany compared with here? Can you shed any light on that? Is that a comparison we should be looking at?

Ian Stewart: It is worth looking at the international data on inactivity. It is interesting. Most countries have seen inactivity decline over time. Germany had very big labour market reforms under Chancellor Schröder in the early part of this century, which had a very big effect on the German labour market. That helped bring in a period of lower German unemployment and rising activity.

This is a global phenomenon. We are in a world where, as populations age, it is sensible to believe that one effect of that will be an increase in labour market activity. The cohort of 50 to 65 year-olds will be more likely to work in future than they are at the moment. If we look at Japan, its demographics are much more negative than those of western Europe,

but in some respects it leads. Activity rates in the Japanese labour market are very high indeed, including for older cohorts. The numbers are significantly higher than in Europe or the United States.

With the reduction of state pension provision and longer longevity, it is probably right to believe that we will see a resumption of the rise in participation rates.

Q53 Lord Rooker: I want to follow up on the previous question before I come on to trends. I know it is a bit hypothetical—or maybe it is not so hypothetical. Let us say that it was government policy in the UK to encourage the return of as much of the manufacturing industry as possible, which in the past we have exported to China, because the carbon capture would be lower as we do not have the coal-fired power stations China is using and we could reduce the carbon on our imports. From what you have said, we would be stuffed in terms of being able to find the workforce for that increase in manufacturing. Is that right or not?

Ian Stewart: The manufacturing workforce has declined over time. It has in all economies as a share of total employment, including in Germany over recent years. It is partly, as you say, the shift of production to lower-cost areas, but it is also about productivity. Productivity growth is extremely high in manufacturing. We have a manufacturing sector that has shifted away from a lot of basic manufacturing, such as steel and heavy engineering—which China, for instance, is itself now trying to get away from—and towards higher-tech, higher-skilled, high-productivity and lower-employment sectors.

Yes, if we saw a dramatic overnight increase in manufacturing opportunities and jobs in manufacturing in the UK, it would be a huge problem. It is already the case that there is a persistent shortage of skills in manufacturing, irrespective of the economic cycle. That is a slightly different question, but it would clearly create a problem because our economy has reshaped itself for a much smaller and different type of manufacturing sector.

Lord Rooker: That question came to me as I was listening to your answers to the other question. On the issue of labour supply trends, could you separate those that are likely to be temporary effects due to the pandemic as opposed to those that are longer lasting? Is there a way to separate those out? Is there a specialism issue or a geography issue? We are a very unequal country in the sense of where our population is. Is it possible to separate the trends into long-lasting and temporary?

Hannah Slaughter: Looking at the groups of workers who have become economically inactive can tell us a bit about this. Starting with older workers, particularly the over-50s who have left the workforce, we know from past experience that it is very unlikely that that group will return to work. Essentially, people do not unretire once they have chosen to leave the workforce in a way they see as permanent.

As far as I can see, there is no reason to believe that will happen to future cohorts. Yes, it is reasonable to believe that the over-50s who

have left the labour force since the pandemic will not return but, given that this was a pandemic-induced shock, future over-50s will not be retiring early, as far as we can tell.

On the health side, we have a big group of workers who are inactive because of long-term sickness. It is a bit uncertain because it depends where that is coming from. We have not quite bottomed out whether that is because of long Covid, which could become more endemic in the economy, or because of pressure on NHS waiting lists, which could reduce, although there is a lot of uncertainty there.

The one health matter I would bring up is mental health. Over the last 10 years or so, we have seen a big rise in mental health conditions among the population, particularly among young people, which is concerning. That seems to be a longer-term trend.

We have seen quite a large rise in inactivity among people who are full-time students. It is worth saying that that is a slightly different case, in that it is temporary inactivity. There are benefits to people being in education, building human capital and so on. We also think a lot of that is related to people who, when the pandemic hit, went into education or stayed on longer in education to ride out the storm of a tough labour market. That would be a cohort factor. Once that group has returned to the workforce after their studies, we will not necessarily see future cohorts taking more education.

Ian Stewart: I completely agree with those points. I just have two others. On labour supply, I wonder whether we will look back at the period from the mid-1990s to the EU referendum in 2016 as being a period of exceptionally strong growth in foreign migration to the UK. In terms of the contribution to the growth of the labour force, the numbers have been extremely strong. Since 2016, EU migration has slowed quite considerably.

Among the dynamics behind very strong EU migration during that period was catch-up in central and eastern Europe, which had high unemployment rates and relatively low wage rates. It is quite striking now that unemployment rates in places such as Poland and the Czech Republic are lower than in the UK, and that there has been a narrowing if not an elimination of the wage differential.

What we can see is a labour market in which there are probably lower trend levels of growth in the foreign-born workforce but a shift towards non-EU workers, which we have seen in the last five years.

The Chair: We heard in written evidence and in the previous session, as you just said, that non-EU migration is potentially making up for quite a lot of the departure of EU workers during the pandemic and post Brexit. The Glassdoor evidence suggested that the employment rates between EU and non-EU workers are quite different. To what extent, therefore, is the arrival of non-EU workers not compensating for the departure of the EU workers?

Lord Rooker: They are doing different jobs, in other words.

Ian Stewart: I am not au fait with the inactivity rates. On the face of it, you would believe that if you substitute a system in which you have uncontrolled migration or free movement of people from the European Union with a system of visas that focuses on skills, however they are measured, you will end up with, on balance, probably less migration but, on average, higher-skilled migration.

Certainly, to look at the numbers for non-EU migration since the referendum, they are growing much more strongly than in the period before the referendum and they are growing much more strongly than EU migration.

There is one other point, which we have not touched on. So far, there is no evidence that it has had any effect on supply, but the change in the nature of work caused by the shift to working from home or hybrid or agile work is a very big change, which we ought to expect to have quite significant effects on potential labour supply. It breaks down the relationship between the location of the employer and where the work can be done.

Like the changes in the organisation of work in terms of maternity pay, for instance, it provides an opportunity for people who are outside the labour market to get into it. We may look back on the shift towards hybrid work as one of the big structural changes in our labour force because the numbers seem to have stuck at quite high levels. It will have to be tested through a downturn.

Lord Rooker: May I follow up on the point about Poland? I was at the Home Office in 2001 when we decided not to put any limits on the eight countries—the Accession 8—that then came into the EU in 2004. Other countries did. We allowed an open door straightaway. The effect of that was a large input; it was huge compared to what was estimated.

What you have said is that those countries are now in a much better economic position than they were in 2004. You mentioned the unemployment rate in Poland. There is less incentive for them to come back. There was a push in the UK economy in that period from 2004 to 2016, which is where you drew the line. We could look at that period as quite a different period of growth. Is that right?

Ian Stewart: It is. I have felt for quite some time that two of the really big changes in the UK labour market in the last 25 years are the growth in the cohort of older workers, the over-50s, and the growth in the non-UK-born workforce. That growth is very much faster than anything seen in the decades prior. There was always migration, inward and outward, but the net numbers were much stronger.

It is probably the case that these levels of migration seem the norm because they have run for a very long time. It may be partly for these reasons. Poland, for instance, had a very large Ukrainian migrant workforce prior to the war precisely because they could not fill their own

jobs. A more sophisticated view of the European labour market would move away from the notion that central and eastern Europe will be a huge supplier of labour to the UK in the way it was.

Lord Livingston of Parkhead: I have two questions, drilling down on the issue with the over-50s. Ian, you were quite clear that it was financially secure people who were exiting the market because they had pensions and assets, if I am not misquoting you. The statistics seem to say something different. The Labour Force Survey and the University of Essex say two things. To cite the University of Essex's evidence, it is the over-50s who rent rather than own their home, with medium levels of education and in lower-paying industries who have seen the largest increase in inactivity.

If we look at the Labour Force Survey and at the quartiles, the lowest quartile has seen a reduction in inactivity and the upper, middle and highest have seen really not much increase in inactivity. There has been a huge increase in inactivity in the lower-middle wage group. It seems to be saying something quite different—I ask this as a question—to the hypotheses you have put forward, which I have heard from many other people, that it is a very different group. Do you have any thoughts on marrying that up?

Ian Stewart: Yes. You are absolutely right. I must say that I struggle with some of the data because there are contradictory trends. The established narrative is that there has been a big rise in sickness and disability and a big rise in inactivity in the over-50s; therefore, either there are a lot of over-50s who have long Covid—which seems a bit implausible because it has not happened in other countries—or, more likely, there are bottlenecks in the NHS that are affecting healthcare.

The reason I find this slightly difficult is that the Institute for Fiscal Studies has done a very good analysis of a subset of data from the Labour Force Survey, which enables it to look at individuals over time, instead of taking the cross-sectional data. Their data suggest that, by and large, the over-50s who have left the workforce have done so not because of illness but because they have the wherewithal to leave. It is to do with owning their own homes, having private pensions or having partners who are in work.

The ONS itself does a survey of the over-50s, which it has done twice in the last 18 months. That has rather similar findings. I must say that I find it rather at odds with the headline picture from the Labour Force Survey data, which suggest a clear relationship between illness and inactivity.

Lord Livingston of Parkhead: Hannah, I have a different question for you, unless there is anything you want to add to that, reflecting the fact that Resolution makes recommendations on policy. What would be your recommendation for how we should reverse the position with the over-50s that we have seen happening as we come out of the pandemic? How can we get participation up? Although we could even ask whether we

should be. What policy measures would you recommend?

Hannah Slaughter: That is an important question. Should we be trying to increase activity? There is a macroeconomic argument about keeping the skills in the workforce, increasing the size of the workforce and all the issues that we have been talking about.

The group of over-50s is such a plural group. As you know, there will be some people within that group who have chosen to leave the workforce, who are able to do so and who have the assets or other sources of income that mean they are able to do so. Perhaps, for that group, we should leave them be.

Where we should be more concerned is, first, people who both are over 50 and have had a health condition driving that choice to leave the labour force, whether that is the main reason or just a contributory factor, and, secondly, people who are just struggling to find a job.

On the first group, a big thing that would help people with health conditions to re-enter the workforce is flexibility of work. Your question before made me think about higher earners staying in the workforce. Perhaps part of that is driven by higher-paying jobs and being more likely to be able to do them remotely. We know that hybrid work, remote work and other forms of flexibility, whether that is part-time working or being able to vary your hours, can be really helpful for people across different age groups but particularly for those with health conditions and indeed caring responsibilities.

One thing we have not touched on is the fact that over-50s may have caring responsibilities, whether that is for their grandchildren or for elderly parents or partners.

Lord Livingston of Parkhead: That very point came up in our last evidence session.

Hannah Slaughter: Flexibility at work is really important for that group. There are then those people who are struggling to find another job, particularly one that fits their skills and experience. We know from our past research that, when older workers lose their job, they find it much more difficult than those from other age groups to find a new job. It takes them longer and, when they do find one, they are more likely to have to take a pay cut.

We need to make sure that older workers in particular have tailored support to help them find a job. Someone who has left a job where they have had 20 years of experience, built up loads of skills and had relatively high levels of pay is not going to want to be told by a work coach, "Here is a minimum wage job in hospitality" when they have been doing a completely different job beforehand. Having that tailored support to make sure they find jobs that fit their skills and experience is really important.

Q54 **Baroness Noakes:** I am going to shift to long-term sickness. I know Mr

Stewart was in our session earlier, so he heard the discussion we had on that. For Ms Slaughter's benefit, we are really trying to find out what is happening with the increase in long-term sickness. The panellists described the data as a relatively new phenomenon and said that we do not know whether this is cyclical or structural.

I was trying to tease out what we know about the increase in long-term sickness, the source of it and whether we can see it having an impact on the employed sector of the workforce as well, ie, impacting on those who are in work. It seems implausible that you would have an increase in long-term sickness in the economically inactive unless it was an economy-wide phenomenon.

In summary, we did not detect any strong datapoints or sources of data earlier, but I would be interested in both of your views on how to tackle understanding what is happening to this element of our inactive workforce.

Hannah Slaughter: One of my colleagues did some work a couple of weeks ago looking at longer-term trends in workers with disabilities in the labour market generally and looking both at people who are not working and people who are working. Basically, there has been a longer-term rise in ill health, which has affected both the employed population and people who are not in work.

We have seen, for example, the disability employment gap narrowing. The difference between the employment rate for people with and without disabilities has been narrowing, but that is partly because we have had a rise in the number of people in work reporting a disability. That is a longer-term trend as well.

As I mentioned earlier, mental health has been a particular driver of health issues both in and out of work. It is important to bear that in mind as well. How can we best support people in employment who may have specific needs that their employer needs to meet or who might need part-time work, for example?

There was a recent paper on this by Jonathan Haskel and Josh Martin at the Bank of England, which mentioned the cohort of people who are in work but might be on long-term sick leave. That will be affecting labour supply, not through the headline numbers of who is in employment, who is inactive and who is not, but in the average hours that people who are employed are working. You probably have a cohort of people who are employed but are being affected by the same health trends that we are seeing among inactive people. In the shorter term at least, people will not necessarily just leave their jobs; they will be on sick leave, but will still count as employed in the data.

Ian Stewart: The ONS does surveys of the effect of long Covid. The last one that I looked at suggested that there were about 400,000 people in the UK whose lives have been limited a lot by long Covid. That might seem to provide the explanation for the rise in inactivity and sickness.

Baroness Noakes: That is not just for this year, though, which is when it became very marked.

Ian Stewart: Yes, exactly. The reason it is probably not long Covid is that other countries have not had it. When the Institute for Fiscal Studies looked at it, it seemed to find a stronger relationship between people taking sick leave, rather than exiting the labour force, and long Covid.

I am thrown back to the argument that this seems more likely to be related to a subject I know you have discussed, which is waiting lists and the capacity in the NHS.

Baroness Noakes: We do not have data on that.

Ian Stewart: I am sure you have lots of witnesses who say, "This needs more research" but, having looked at this, that is exactly the feeling I have.

Baroness Noakes: Is there anything that we know from other countries that would help us to understand what is happening to us?

Ian Stewart: Not that I am aware of, no.

Hannah Slaughter: No, not that I am not aware of either.

Q55 **Lord Monks:** Can we look in a bit more detail at the position of young people—the 16 to 24 year-olds who have become more economically inactive since the start of the pandemic? I am interested to know whether you expect that to change, given the difficult macroeconomic outlook. In a way, young people are usually affected first by major labour market changes. If unemployment is going up, it goes up more quickly among young people than it does among prime age people. If it is coming down, youth unemployment tends to come down more quickly.

What are the reasons for their economic inactivity? Is that likely to change? I appreciate that it is difficult to say very much without having a view on the macroeconomic outlook.

Hannah Slaughter: As you say, particularly at the start of the pandemic when lockdowns hit, we definitely saw a big impact, with young people losing their jobs or being furloughed, largely due to the sectors they tend to work in and because they are more likely to be on insecure contracts, such as temporary jobs or zero-hours contracts, where it is easier to let people go. When the economy reopened last year, sectors such as hospitality and retail opening up meant that, as with other workers, we did not see as much of an unemployment hit to young people as we were concerned about.

A lot of the inactivity among young people has been driven, as I was saying earlier, by people studying. That is an established phenomenon: people ride out the storm by entering education. That is good for them because entering the labour market during a recession can be really bad for your pay and employment prospects in the longer term. It is a good thing for those young people to have done that, to have chosen to study for longer or to have gone to university when they were not planning to,

for example. That might largely be a cohort effect. Once that cohort of people has fed through and re-entered work after that, that effect will ebb away.

In terms of how easy young people will find it to re-enter work, the fact that we have lots of vacancies in sectors such as hospitality will help young people, in the sense that there will be entry-level jobs for people to go into. The question is, first, whether there will be high-quality and well-paying jobs for them to progress into. As we are in a period with lots of economic fluctuations, the second question is whether demand will keep up in those sectors and whether the level of vacancies that we see now will last.

In the last set of GDP data out earlier this week, we saw a weakening of economic activity, particularly driven by consumer-facing services, which is understandable as the cost of living crisis starts to bite and people start to change their spending patterns. In some sectors that traditionally have been an entry point for young people into the labour market, the opportunities might start to dry up as businesses start to struggle. There is a concern about that as well.

Ian Stewart: There are two things that are encouraging. The proportion of young people who are not in education, employment or training has not risen much. It has been trending down over time. There has been a slight uptick but not an enormous one. There are still over 500,000 people in that category, but it has not risen massively.

In the financial crisis, unemployment for the under-24s rose very significantly. It took about eight years for the unemployment rate for that group to get back to where it was before the financial crisis. Unemployment rates particularly for 18 to 24 year-olds have fallen sharply, and they are at record lows. So there is encouragement for younger people: the education story and the unemployment story are quite reassuring.

Q56 Lord Layard: Can you make a brief comment on the impact of the cost of living? Will that make, or has it already made, more people become active?

Hannah Slaughter: We have not seen any evidence of that so far. In the last couple of months of labour market data, we have seen further rises in inactivity. It is certainly something that we are looking out for.

After the financial crisis, we definitely saw the effect of what the Resolution Foundation termed "feel poor, work more". As households took an income hit from falling real wages and rising unemployment, we saw an increase in labour supply and economic activity particularly among second earners in couples. From the data, it was generally women upping their hours where they were able to or entering the workforce if they were not working previously. It is definitely something that we are looking out for.

There are two caveats to that. First, the people who have left the workforce during the pandemic are often people with long-term health conditions, for example, who may not be able to enter the workforce. Secondly, to what extent will employer demand be there? Will there still be the high levels of vacancies that we see now?

There is in fact a third caveat that I will add. During the pandemic itself, we saw an increase in people who were previously inactive because of caring responsibilities entering the workforce again, particularly younger women and mothers with young children. It may be the case that the people who might have had the scope to up their labour supply in response to a household income shock have already done so. There might not be that much more scope for people to do it.

Ian Stewart: I completely agree with that. Consumer sentiment about their own finances has never been lower in the 55-year history of the GfK survey that tracks it. Households are extraordinarily negative about their own situation, and yet that does not seem to have driven a rise in participation, as Hannah says.

The other thing is that participation is generally cyclical. High participation falls in recessions. If the economy slows, we tend to expect participation rates to weaken, not increase.

The Chair: This is very interesting. To pick up on the point made by Lord Livingston about the demographics of the over-50s who have left and are now inactive, you would have thought that, while their sentiment is very low, exactly as you were saying, they would start to come back. You are saying they may not.

Ian Stewart: Yes. It goes exactly to this point about how solid the finances of this group are. After the financial crisis, we were surprised by the rise in participation rates by older workers, which was widely attributed to the loss of capital that took place in the financial crisis. I am very struck and surprised that we have not seen more of a response in terms of participation rates, given how strong the labour market is and the pressures on household incomes.

Q57 **Lord Griffiths of Fforestfach:** May I ask a very general question to conclude? You are specialists in this area; we are generalists. We are birds of passage, really. We migrate into a subject and then we fly away and move on. You do not. If there was one thing in our report about which you would say, "That was a great report by the House of Lords Economic Affairs Committee", what kind of thing would it be?

Ian Stewart: That is a good question—I needed notice of that question. I have an answer, but I am afraid it is not a very original thought. One thing that has occurred to me in thinking about this is how impressed I have been by the way in which the Office for National Statistics changed the way it produced data at the start of the pandemic. It shifted to using a lot of experimental high-frequency data from third parties. There was a

very quick response, and it started running ad hoc surveys on particular issues. Its management of the data around Covid was absolutely superb.

To me, what comes out of this, I am afraid, is that there are still quite big gaps in our understanding of really fundamental things, particularly around skills mismatches over the role of illness in inactivity.

The final thing, which will be a hugely important area, is understanding the effect of hybrid working on productivity. Lots of surveys have been done on it, but they are typically done on routine work such as call centres or coding. There is very little evidence on the effect on cognitive unstructured work. If this is the shape of work to come, understanding that will be very important.

Hannah Slaughter: This is something that has struck me during this session and in general. We have been talking about this one big problem of labour supply. It is a major challenge that we are facing, but there are so many drivers and reasons for it. We have talked about lots of them today, and I am sure you are talking to others and reading lots of things.

I would just take into account that we are talking about a pluralistic group of people and, therefore, there are different solutions that will apply. There is no one-size-fits-all approach or one-size-fits-all definition of the problem either. We need to take that into account.

The Chair: Thank you both very much. We have tried to unearth some answers. We have more questions, but it has been a very good discussion. Thank you both very much for your time.