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Collective Learning, Effective Demand, Loss of Work and Loss of Direction: The Growing Regional Divide in the UK

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Collective Learning, Effective Demand, Loss of Work and Loss of Direction: The Growing Regional Divide in the UK

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For Peer Review Only

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6 Collective Learning, Effective Demand, Loss of Work and Loss of Direction: The
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8 Growing Regional Divide within the UK
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Abstract

The local economy relies on a division of labour that develops highly specialised skills. In searching for an understanding of the growing work gap within the United Kingdom, emphasis is placed on recessions that connect to loss and redundancy of physical and human capital. High levels of regional unemployment following deindustrialisation convert into high levels of regional nonwork in later years. Loss of economic base leaves a gap in the community and economy that people struggle to bridge. Market forces work strongly against certain groups in society, including those at some disadvantage in the labour market.

JEL: E65, J23, J24, R58

Key words: Regional Development, Fiscal Policy, Labour Demand, Human Capital

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3 Collective Learning, Effective Demand, Loss of Work and Loss of Direction: The
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5 Growing Regional Divide in the UK
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10 1. Introduction
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15 “There is no craving or demand of the human mind more constant and insatiable than
16 that for exercise and employment” (Hume,[1752] (1963), p.189)
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22 “Human capital deteriorates when it is idle, because unemployment impairs the skills
23 that workers have acquired” (Schultz, 1961, p.13)
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29 Work builds us (Hume), unemployment and inactivity reduce us (Schultz). We are
30 what we do and we are more content and lively when we are employed in systematic,
31 sustained, methodical labour. Work adds to mental vigour and harnesses hidden
32 potential: it is a civilising influence that satisfies our craving for involvement, adds to
33 the quality of leisure and shields us from unhealthy appetites. The potential return
34 from work is central to Hume’s political economy and to his understanding of human
35 nature and civil wellbeing.
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46 The key argument for full employment, Beveridge (1944, p.19) claimed, is
47 that “A person who cannot sell his labour is in effect told that he is of no use”. In the
48 United Kingdom economy, the problem of lasting loss of contact with work is wider
49 than measured unemployment. There has been a strong shift from unemployment to
50 inactivity. It is enduring loss of contact with work that has an adverse effect on skill,
51 discipline, good habits, self-confidence and self-respect. It is inability to find work
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3 and particularly loss of contact with the labour market that has an adverse effect on
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5 labour quality and labour potential.
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8 Economics and wealth creation embrace more than the efficient use of known,
9
10 scarce resources. Also important is resource creation, the employment and
11
12 improvement of resources of unknown potential. In Smith's *Wealth of Nations*,
13
14 capital and knowledge accumulation provide the keys to growth. Capital includes
15
16 "the acquired and useful abilities of all the inhabitants of the nation" (Smith, 1776,
17
18 p.264). Adam Smith insists that it is combined labour that adds to human capital, to
19
20 productivity and to wealth. Labour's productive power, "the greater part of skill,
21
22 dexterity and judgement ... [are] the effect of the division of labour" (Smith, 1776,
23
24 p.51). The division of labour depends on the extent of the market and this, in turn,
25
26 depends on 'effectual demand' for goods and services. The division of labour is
27
28 dynamic and it is central to acquiring skill and knowledge. We learn by doing and
29
30 output and earnings are raised by knowledge of fellow workers, by experience in
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32 work and by improved understanding of the best way to do things. The learning
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34 process is a voyage of discovery and the local economy relies on a division of labour,
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36 both within and between firms, which develops highly specialised skills and
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38 perceptions.
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45 This article concentrates on trends in male work, unemployment and
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47 permanent sickness since 1971. It draws on contrasts between the Keynesian Golden
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49 Age, 1950-73, and later years. Part 2 concentrates on data from the 2001 Census of
50
51 Population. The 2001 data show considerable regional variation in work (effective
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53 demand) levels and in regional inactivity, but little variation in regional
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55 unemployment. Those who find it difficult to compete in low opportunity labour
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57 markets lapse onto sickness benefit, or are eased onto other forms of inactivity. In
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slack labour markets, labour supply (employment, self employment and measured unemployment) is lower than potential labour supply.

In searching for an understanding of the growing work gap within the United Kingdom, parts 3 and 4 of this paper places considerable emphasis on recessions that connect to loss and redundancy of physical and human capital. The recession of 1973-74 is important because it signals a move to lower growth levels in most, if not all, mature industrial economies. But it is the recession of 1979-83 that contributes to a substantial divide in regional unemployment and economic opportunity. Creative Destruction is Schumpeter's elegant description of structural change (Schumpeter, 1943). Economic growth is not more of the same, Schumpeter insists, and the elimination of the old is part of progress. It is, however, sensible to try and avoid concentrated, cumulative loss. The themes of orderly retreat, phased decline, and regional balance were not part of economic policy in the early 1980s. The unemployment increases of 1979-86 developed from steep decline in industrial employment and they were unevenly distributed and convert into high levels of regional nonwork in later years (see Part 4) Part 5 considers the year-by-year evolution of a substantial work, wage and productivity gaps within the UK. Part 6 concludes. Human capital deteriorates when people are idle and in low opportunity labour markets many are excluded. Loss of economic base leaves a gap in the community and economy that people struggle to bridge.

2. The 2001 Census, Effective Demand and Measured Sickness

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3 'Movement out of the statistical labour force when demand is low may be regarded as
4 a form of concealed unemployment,' (Dow 1964, p. 338).
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11 Retreat from effective regional policy across a number of European countries,
12 Läßle (1985) claims dates from around 1973 - the end of the Keynesian Golden Age.
13
14 Regional imbalance became severe when nation states silently and to some extent
15 reluctantly abandoned commitment to both full employment and effective regional
16 intervention. In Table 1, the 3 poorest regions in Britain (Wales, North East and
17 North West) are combined as one unit, Wales and North and are compared with the 3
18 most prosperous British Regions, the Inner Region Core (IRC) comprising London
19 and its 2 major commuting regions, the East and South East. By the end of the
20 Keynesian Golden Age output per head in Wales and North was 84% of the IRC
21 level, by the turn of the century only 69%. The output gap between the poorest and
22 most prosperous parts of Britain doubled. Since output (value added) feeds income
23 and supports expenditure it is no surprise to discover that other regional data
24 including earnings, household expenditure and work levels also identify a
25 substantially enhanced regional divide. But there are two striking results in Table 1.
26
27 Firstly, comparing Census data for 1971 and 2001, in Wales and North the share of
28 the male work age population (excluding students) in work falls from 90% in 1971 to
29 only 75% in 2001, but the male unemployment levelⁱ is lower in 2001 than in 1971.
30
31 Second, comparing 1971 and 2001, there is a growing work gap between IRC and
32 Wales and North, but the unemployment gap falls. Census unemployment data fails
33 to register the growing regional divide.
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3 Table 1 goes here
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8 The answer to the puzzle connects to the discouraged worker effect; the
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10 substitution of inactivity for unemployment. Movement out of the labour force
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12 ensures that labour supply (employment, self-employment and unemployment) falls
13
14 below potential labour supply when demand is low. The discouraged worker effect is
15
16 highly sensitive to effective demand for labour in the local, regional, or national
17
18 economy. In low opportunity labour markets where competition for jobs is fierce,
19
20 some workers lose faith in job search and lose contact with the labour market. The
21
22 potential workers who retreat from the labour market may retire early, continue in
23
24 education, return to education, accept government training, substitute household work
25
26 for search for employment, or lapse into debility and measured sickness. By the
27
28 beginning of the 21st century, the discouraged worker effect is more substantial than
29
30 measured unemployment and dominated by those out of work who describe
31
32 themselves in the as permanently sick or disabled (see MacKay and Davies, 2008).
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53 Given the Keynesian approach, effective demand depends on the demand for
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55 goods and services produced by the economy. Effective demand failures take two
56
57 forms. First, the potential availability of workers is not an actual demand for goods
58
59 and services. Unemployed and discouraged workers cannot encourage the product
60

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3 (and labour) market to recognise that they embody hidden, unsatisfied demand that
4
5 will only become effective when workers are employed. Second, private investment
6
7 in technically specialised, invention-vulnerable, market-dependent, concrete and
8
9 durable plant and equipment is, by its very nature, volatile, capricious, unreliable.
10
11 Investment depends on a future that is more than uncertain, it is unknowable. Since
12
13 future returns are vague, confidence is unstable and investment depends on intuition,
14
15 on the news, on animal spirits and on an urge to action rather than inaction. The
16
17 natural consequence is that investment 'fluctuates widely from time to time' and from
18
19 region to region (Keynes, 1973c, p.118).
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24
25 In Figure 1, regional work levels for males are the indicators of regional
26
27 effective demand. Work is employment and self-employment. As we move from left
28
29 to right in Figure 1 (as work levels rise) permanent sickness and unemployment fall,
30
31 but permanent sickness is notably more sensitive to variation in regional work
32
33 (effective demand) levels. Simple regressions suggest that each 1% rise in male work
34
35 level reduces permanent sickness by 0.63 percentage points and unemployment by
36
37 0.26 percentage points. Similar patterns are observed for women. Figure 1
38
39 demonstrates that in regions of low levels of effective demand for labour there is a
40
41 strong tendency for limited opportunity to take the form of measured sickness rather
42
43 than measured unemployment. The greater the degree of labour market disadvantage
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45 (the lower the work level) the less appropriate is unemployment as a measure of
46
47 labour market slack.
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55 Figure 1 goes here
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60 3 Full Employment No More: An End to Regional Balance.

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‘Several million men in England will – unless another war breaks out – never have a real job this side the grave’ (Orwell, 1936, p. 162).

‘If we can cure unemployment for the wasted purpose of armaments we can cure it for the productive purposes of peace. Good may come out of evil’ (Keynes, 1973b, p. 532).

The war proved that the jobless were capable of work and it provided a rationale for regional policy and also for full employment. Rearmament and the strategic needs of the war economy encouraged relocation of industry to less vulnerable and more remote parts of the United Kingdom. That experience and ‘the euphoria’ of the post war years encouraged continued relocation between 1945 and 1951 (Hennessy, 1993, p.209). Careful comparisons of relative cost in parent and branch plants came to the conclusion that there were teething and adjustment costs, but no continuing cost disadvantage attached to plant movement (Luttrell 1962). Relocation within a notably compact and confined nation state was an acceptable and low cost response to ‘the task of shifting men from industries where they are permanently redundant’ (Keynes, 1973a, p.89). Economic growth is a learning process, employees have specialised and specific skills and there is collective learning: but, given investment and opportunity, workers grow into a different culture. Strong regional policies in the years 1945-51 and 1963-73 demonstrated that workers from farms, mines, quarries, shipyards and steel adapted readily to the needs of growth industries.

Growth depends on innovations and these destroy even as they create. Creation and destruction are component parts of economic development, but they tend to be geographically separate. The innovators do not habitually emerge from the firms and industries that linger on ‘in the fatally deepening dusk of respectable decay’

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2
3 (Schumpeter, 1939, p45). Growth that relies on the spontaneous evolution of
4
5 innovational investment is highly uneven: market-driven capitalism can produce deep
6
7 regional divisions; it is 'lopsided, discontinuous, disharmonious by nature'
8
9
10 (Schumpeter, 1939, p. 102). Creation and innovation, the introduction of new
11
12 methods and new products, is embedded in new plant and equipment designed to
13
14 introduce best-practice techniques and new plant and new capital equipment have a
15
16 productivity advantage akin to the most fertile land (Salter, 1969). The carrots
17
18 (financial inducements) and sticks (location controls) of regional policy encouraged
19
20 relocation of innovative growth industries and connected the high unemployment
21
22 locations to a more optimistic dynamic (MacKay and Thompson 1979).
23
24
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27 Keynes (1973b,p.386) described regional policy as the search for 'a rightly
28
29 distributed demand', the Board of Trade equivalent was 'a proper distribution of
30
31 industry'. A regional policy that sought to influence the location of industrial
32
33 expansion was heavily dependent on both full employment and manufacturing
34
35 growth. Spatial redistribution declined as the national economy drifted to higher
36
37 levels of unemployment in the late 1960s and early 1970s. It became notably less
38
39 significant after the oil price shocks of 1973 and 1974. Commitment to full
40
41 employment followed from the shared sacrifices of the war years, but it also relied on
42
43 the Keynesian Revolution in economic thought and understanding. Keynes (1973, p.
44
45 VIII) described the evolution of his ideas as a 'long [and laborious] struggle of
46
47 escape' from assumptions and thought processes that guaranteed market clearing.
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51 The most important determinant of output and employment is aggregate effective
52
53 demand. In the first 18 years of the Golden Age, 1950-67, we have a sellers market
54
55 for labour (Table 2). Given growth and low unemployment, a great deal of structural
56
57 decline could be absorbed by natural wastage (voluntary quits and retirements). Low
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1
2
3 unemployment added to constructive labour mobility, to adaptability and to
4
5 flexibility. Up to the late 1960s control of inflation was guided by workers and
6
7 unions who placed a high value on job security and were willing to accept wage
8
9 restraint because they remembered the hard times in the 1930's and in the war years
10
11 (see Phelps Brown, 1983; Worswick, 1992). In due course control over the Union
12
13 movement shifted to a more militant generation with experience only of full
14
15 employment and who believed that governments feared unemployment and would
16
17 continue to accept responsibility for the level of effective demand. There was a jump
18
19 in the rate of money wage increases in a number of European countries in the late
20
21 1960s; the revolution of rising expectations was seen not only in pay increases, but
22
23 also in a wave of industrial unrest and civil protest which was international. In the
24
25 years from 1968 the UK and other European countries began to lose touch with full
26
27 employment.
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36 Table 2 goes here
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41 The real substantial check to output growth and the end of the Keynesian
42
43 Golden Age comes in 1973. Prior to the oil price increases, most people expected
44
45 continued growth; after 1973 there was doubt and uncertainty. The reduction in
46
47 growth and the increase in unemployment were international. Maddison (1991)
48
49 provides data for 16 capitalist economies. In his 16 prosperous economies, the
50
51 arithmetic average for annual improvement in real GDP per head was 3.8% in the
52
53 years 1960-73 and only 1.9% between 1973 and 2001. In the UK average annual
54
55 growth fell from 2.5% 1950-73 to 1.7% 1973-2001. The oil price increases added to
56
57 inflation and unemployment. With inflation at uncomfortable levels demand
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2
3 management was difficult. A price standard (low and stable inflation) emerged and,
4
5 in time, displaced the labour standard of full employment. With inflation seen as the
6
7 main threat, demand management was 'not available to sustain output and
8
9 employment' (Worswick, 1992, p.61).
10
11

12
13 The major step to high unemployment and a buyers' market for labour comes
14
15 with OPEC recession 2 (oil prices doubled in 1979-1980) and deindustrialisation. By
16
17 the mid 1980s, full employment was a distant memory. The growing influence of the
18
19 price standard (low inflation) is a product of historical circumstance, but it also owes
20
21 a great deal to the Counter Revolution in economic ideas that developed as a critique
22
23 of the Keynesian Revolution and demand management. The Counter Revolution has
24
25 three articles of faith: (1) markets, including labour markets clear – only
26
27 misinformation and confused signals prevent labour markets from arriving at market
28
29 clearing wages; (2) private expenditure is good, public expenditure is bad; (3)
30
31 voluntary unemployment can be reduced by making unemployment less attractive. In
32
33 his contribution to the Treasury Report on Monetary Policy, Friedman concluded that
34
35 'only a modest reduction in output and employment will be a side effect of reducing
36
37 inflation to single figures by 1982' (Treasury, p. XXXV1). Friedman also claimed
38
39 that reduction of Government spending by one sixth 'is not a major magnitude'. It
40
41 makes people available for productive employment and most 'would be absorbed in a
42
43 fairly brief period' (Friedman, 1977, p.47). Tobin was less optimistic. In a summary
44
45 of his evidence to the Treasury Committee, Tobin warned that disinflation would be a
46
47 'lengthy and costly' process, 'characterised by deep recessions, stunted recoveries and
48
49 high and rising unemployment' (Tobin, 1983, p.297). Tobin anticipated
50
51 unemployment that was deeper and more distressing than the Counter Revolution
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2
3 anticipated: the recovery powers of the market could easily be exaggerated. Table 2
4
5
6 points to the significant rise in unemployment in the first half of the 1980s.
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10 4. Deindustrialisation – A Lasting Impact

11
12 ‘In major recessions under employment results in the deterioration and premature
13
14 scrapping of physical equipment ... the capital stock, physical and intangible ... takes
15
16 time to build up and its destruction cannot be made good rapidly ... the destruction is
17
18 quasi-permanent’ (Dow, 1998, p.369).
19
20
21

22 When opportunities for joint and cooperative labour are removed, income and
23
24 expenditure (as well as training) are lost and expenditure loss reaches out from the
25
26 economic base to embrace the service sector. Decline is contagious and cumulative in
27
28 the absence of early and decisive response (Keynes, 1973a, p.225). When the
29
30 economic base that defined communities withers, other doors also close. In major
31
32 recessions previously created productive forces are destroyed and even vigorous,
33
34 creative firms that might have had a lasting impact will perish (Schumpeter, 1943).
35
36 Growth is not more of the same, so there is no point ‘in trying to conserve obsolescent
37
38 industries indefinitely’, Schumpeter argues, but there are good economic and social
39
40 grounds ‘to avoid their coming down with a crash and in attempting to turn a rout,
41
42 which may become a centre of cumulative, depressive effects, into orderly retreat’
43
44 (Schumpeter, 1943, p.90). The idea that pace of decline matters is common sense and
45
46 it connects to the Keynesian prediction that involuntary unemployment will always be
47
48 ‘troublesome [if] allowed to develop’ (Keynes, 1973, p.118). Orderly retreat, regional
49
50 balance, phased decline of dying industries, the role of the financial sector and credit
51
52 in encouraging a new economic base, the importance of natural wastage in easing
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1
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3 structural change and early response to employment loss did not inform the Counter
4
5
6 Revolution..

7
8 In the early 1980s the combined effect of monetary and fiscal policy was
9
10 severely contractionary (see Dow, 1998 and Treasury, 1981). Disinflation via gradual
11
12 destruction of monetary demand, committed 'the government not to deal with a
13
14 recession no matter how deep it [became]' (Okun, 1981, p. 358). Male
15
16 unemployment in the United Kingdom increased by 8.2 percentage points between
17
18 1979 and 1986, reaching a peak of 13%. By 1986, long-term unemployment
19
20 (continuous unemployment of over one year) accounted for 45% of male
21
22 unemployment and reached even higher proportions in the regions with the highest
23
24 levels of unemployment. The decisive impact of deindustrialisation in enforcing
25
26 substantial increase in spatial inequality is demonstrated in figure 2. Whilst the IRC
27
28 was not excluded from the effects of a changing industrial structure, male
29
30 unemployment rose by 10 to 12 percentage points in the regions of severe
31
32 deindustrialisation. The pattern is that deindustrialisation and unemployment increase
33
34 concentrated on the regions where unemployment was high, even prior to recession.
35
36 It is no surprise to discover that decline (like prosperity) can be self-perpetuating.
37
38 Loss of work spreads through the economic base and loss of trade reaches out from
39
40 the base to embrace the construction and local service sectors (see MacKay, 1994).
41
42 Every kind of unemployment induces further unemployment is the Schumpeter
43
44 emphasis (Schumpeter, 1939, p.515). Employment beyond the reach of those who are
45
46 reduced by severe economic and social dislocation adds to unemployment and also
47
48 encourages workers to drop out of the labour force.
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Figure 2 goes here

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3 Weitzman (1982) argues that increasing returns to scale, interpreted broadly,
4 is the key to understanding why the unemployed cannot produce on their own; and
5
6 also why the 'self correcting forces' of the market are 'weak or non-existent'
7
8 (Weitzman, 1982, p.804). The division of labour relies on plant and equipment
9
10 designed for the joint use of a number of employees and builds from extension of the
11
12 market. Moreover, productivity resides in the job and it depends on Adam Smith's
13
14 joint and co-operative labour. Increasing returns also include external economies that
15
16 connect to ease of contact and communication: to skills and know-how: to the
17
18 emergence of specialist firms and working relationships within and between firms
19
20 (see North, 1998). Physical and human capital – previously created productive power
21
22 – is inherited. Loss of relevance can be sudden, devastating and have lasting effects.
23
24 The destructive component of creative destruction is real and it hurts. There is an
25
26 element of truth in Veblen's claim that the 'Right of Investment' confers 'a legal
27
28 right' to sabotage employment and 'so make the community's workmanship useless'
29
30 (Veblen, 1978, p.130). Specialisation implies interdependence. The earning power of
31
32 the individual is at the mercy of a division of labour that adjusts to competitive forces
33
34 beyond the control of the individual and the local community. With wealth can come
35
36 uncertainty and unemployment and nonwork are 'a story about effective demand
37
38 failures' that connect to increasing returns and specialisation (Weitzman, 1982,
39
40 p.781).
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51 Collective learning is North's term for the 'accumulated stock of knowledge'
52
53 that emerges over time (see North, 1998, p84). Physical capital has specific
54
55 properties and human capital develops particular skills. The essence of division of
56
57 labour is that we cannot 'know, or do everything' (Richardson, 2002, p.38).
58
59 Deindustrialisation is at the heart of unemployment increase in the early 1980s. But
60

1
2
3 deindustrialisation and closure of firms is deeper than temporary loss of jobs. Given
4
5 steep decline, there is loss of collective learning and loss of direction for capital and
6
7 labour. Substantial checks to development may have lasting effects. Dow (1998)
8
9 refers to loss of business confidence. Weitzman (1982, p.803) speculates that 'low
10
11 expectations of aggregate demand become ingrained' and turn into a major cause of
12
13 continuing low levels of activity. Collective learning includes the labour force. In
14
15 households that lose contact with work children have a more difficult start in life and
16
17 attitudes to school, further education, qualification, training, employment counselling
18
19 and government placement are not uniform across labour markets. Ambition,
20
21 involvement, commitment and aspiration expand with opportunity (Ashton and
22
23 Maguire, 1986). Moreover, loss of jobs reduces training opportunities since learning
24
25 by doing depends on work. One important consequence is that young adults lose out
26
27 on the opportunity to build human capital at an important stage of their working lives.
28
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33
34 The division of labour and increasing returns point to the importance of
35
36 organic interdependence, the whole is more than the sum of the parts. The Keynesian
37
38 Revolution placed strong emphasis on prompt and vigorous measures to encourage
39
40 recovery when markets are lost. Severe, intense structural decline produces not only
41
42 capital, but also human obsolescence. The reality is that the individual is given little
43
44 indication of the forms of investment (response) that are likely to yield an acceptable
45
46 return. Given severe decline it takes time and capital to provide a new direction for
47
48 collective learning and employment. However, the longer the delay the more likely it
49
50 is that cumulative forces of decline will be set in motion that prove difficult to check
51
52 until they have run their course. Effective demand failures have an impact that reaches
53
54 well beyond the short-run business cycle; the growth of the economy is path
55
56 dependent. Dow (1998) claims that there is a significant reduction in productive
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1
2
3 potential in the 1980s and that this follows from recession and loss of confidence.
4
5
6 Figure 3 shows that high levels of male claimant unemployment in 1986 translate into
7
8 high levels of nonwork in 2001 (the correlation coefficient is 0.93). Male nonwork
9
10 levels in 2001 vary from 16% of the work age population in IRC to 28% in the North
11
12 East. The regional economies that suffer most heavily in the recession of the 1980s
13
14 do not demonstrate strong powers of recovery. Figure 3 also shows the relationship
15
16 between male regional unemployment in 1986 and male measured sickness in 2001.
17
18 High levels of regional unemployment in 1986, convert into high levels of permanent
19
20 sickness and disability in 2001 (the correlation coefficient is 0.88). By 2001,
21
22 permanent sickness rates for non-student males of work age vary from over 11% in
23
24 Wales, to less than 5% in IRC.
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32 Figure 3 goes here.
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36 Detached and/or discouraged workers are products of limited opportunity.
37
38 Measured sickness is critical to loss of contact with work. The areas that ‘experienced
39
40 large scale job losses in the 1980s and 1990s, especially from traditional industries’,
41
42 dominate league tables for incapacity benefit and ‘real’ unemployment (see Beatty,
43
44 Fothergill, Gore and Powell, 2007, p.12: also Table 1 p.13 and Table 4 p.23). Many
45
46 of the locations that head these tables used to be heavily dependent on the traditional
47
48 industries of mining, steel and ship building and large concerns dominated local
49
50 labour markets. In both league tables there is strong geographical concentration,
51
52 notably on Wales, the North East and North West. Beatty and Fothergill (2007)
53
54 identify the continuing problems that flow from closure and job loss. Their survey
55
56 evidence for incapacity benefit claimants in Barrow and Furness (major shipbuilding
57
58
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1
2
3 closures in early and mid 1990s) shows that those interviewed in 2007 were more
4 demoralised and remote from the labour market than those interviewed in 1999.
5
6
7
8 'Initial willingness to consider employment [has been] gradually replaced by a
9
10 complete detachment from the world of work, rationalised in terms of largely
11
12 insurmountable health problems' (Beatty, Fothergill, 2007, p.616). The continuity of
13
14 low levels of work is critical to our understanding of the movement from
15
16 unemployment to inactivity in general and measured sickness in particular. Low
17
18 levels of work do not add to labour quality and motivation and inability to compete in
19
20 slack labour markets promotes a drift out of the labour force. Job loss ensured that
21
22 'sickness which was previously hidden became visible' (see Beatty, Forthergill,
23
24 Macmillan, 2000 p.622). The realities of weak labour markets added to measured
25
26 sickness and concealed unemployment in the last quarter of the 20th century.
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34 5. Conflicting Objectives

35
36 'There is ... a perplexing ... apparent asymmetry between Inflation and
37
38 Deflation' (Keynes, 1973, p. 291).

39
40
41 'Our profession is in no small measure responsible for the confidently held
42
43 view that public announcement of resolute irreversible monetary disinflation will so
44
45 alter expectations in the private sector that our inherited wage and price inflation will
46
47 melt like snow in spring sunshine. This proposition is not based on empirical
48
49 evidence'. (Tobin, 1983, p.297).
50
51
52

53 The Keynesian asymmetry ensures that expansion beyond (or even short of)
54
55 full employment will have a major effect on wages and prices. Deflation by contrast
56
57 has a major effect on output and employment and a disappointing impact on wages
58
59 and prices. Tobin's evidence to the Treasury Committee on Monetary Policy
60

1
2
3 demonstrates that the Keynesian asymmetry has content. United States experience
4 indicated that 90% of the year one response to a spending shock (cut) would end up in
5
6 output reduction and only 10% in price reduction (see Treasury 1980-81, 163-II,
7
8 Vol.2, question 760). Reducing entrenched inflation by monetary disinflation would
9
10 entail deep cuts in output and large increases in unemployment. Tobin's carefully
11
12 stated, but pessimistic view of the UK's 'interesting ... but risky experiment in
13
14 macroeconomic and monetary policy' was strongly influenced by Okun's work on
15
16 wage setting. Okun (1981) argued that wage bargaining developed in the context of a
17
18 long-term relationship between firms and employees. Jobs are specialised and labour
19
20 inside the firm is different to labour outside the firm. Implicit contracts (invisible
21
22 handshakes) of indeterminate but often extended duration ensure that the labour
23
24 market is not and cannot be an auction market (Okun, 1981). The unemployed cannot
25
26 'insist on being offered work', even if they would accept lower wages (Keynes, 1973,
27
28 p. 291). Moreover, aggressive wage cutting is not the natural response of firms to
29
30 excess supply of labour. The wage paid is important to the firm's reputation and
31
32 standing in the labour market and fair treatment is designed to build morale and
33
34 motivation. The wage is part of a long-term relationship that brings benefits to firms
35
36 and workers.
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45
46 Laidler claimed that 'none of us [the us refers to monetarists] expected the
47
48 implementation of a monetarist strategy ... to have significant adverse effects on
49
50 output and employment, none of us expected the deep and prolonged depression that
51
52 ensued.' (Laidler, 1985, p.35). There were clear warnings, not only from Tobin and
53
54 Okun, but also from Galbraith and 364 academic economists who claimed that
55
56 demand deflation would deepen depression and erode the industrial base (see The
57
58 Times, 30th March, 1981; for Galbraith, see Observer, 31st August 1980 and Times,
59
60

1
2
3 3rd March 1980). Deindustrialisation in the early 1980s created a substantial regional
4 divide, with that separation remaining powerful up to 2008. Figure 4 shows work
5 levels (employment and self employment) per 100 men of work age in IRC and Wales
6 and Northⁱⁱ. In 1974 the work level in Wales and North was 88 jobs per 100 men of
7 work age: in 2008 the work level was only 79 jobs per 100 men of work age. In the
8 1970s the work gap between Wales and North and IRC was modest, but by 1986 it
9 was substantial.
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22 Figure 4 goes here.
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27 The normal pattern for UK recessions is that employment decline concentrates
28 on the regions of low opportunity. However, the 1989-93 recession was the product of
29 an unsustainable property boom that had been driven by unrealistic expectations of
30 continued house price increases and employment loss was heavily biased towards the
31 more prosperous parts of the country (Audas and MacKay, 1997). A speculative
32 market that is driven by the psychology of the market rather than real values is not
33 likely to prove consistently reliable. The recession of the early 1990s had a major
34 impact on IRC work levels, a less pronounced effect on Wales and North. However,
35 recovery in the most prosperous part of the country was impressive. By 2001 male
36 work levels in IRC were not too distant from those experienced in the 1970s. In 2001,
37 the work gap between Wales and North and the IRC was close to its highest level.
38
39 Whilst a sustained period of economic expansion contributed to the narrowing of the
40 work gap up to 2006, movement towards recession contributed to a widening of the
41 work gap to 10 jobs per 100 men of work age by 2008.
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Figure 5 shows output and earnings in Wales and North in relation to the IRC. Output per head in Wales and North was 85% of IRC level in the mid 70s, only 65% in 2008. The relative strength of the circular flow of output, income and expenditure shifts strongly against Wales and North. Most families are heavily dependent on income from work. Figure 5 shows that earnings, as well as work levels, move strongly against Wales and North. In 1979, Wales and North male earnings in full-time work were 92% of the IRC level, by 2008 only 77%. In the years 1973-79 the average wage in rest of UK was 91% of the IRC level; in the years 1980-89 the average fell to 86%; in the years 1990-2001 the average fell to 80%; and in the years since 2001 the average has fallen again to 76%. The large work gap is accompanied by a substantial and growing wage gap. In a buyers' market for labour, (low levels of opportunity) firms can place a greater reliance on casual and contract work (see Tilly and Tilly, 1998). The weaker the labour market the more likely it is that employers offer unattractive work at low wages and hire workers for short-run jobs. 'The employers survive only because they can thrust the burden of unstable business on a casual labour force' (Solow, 1982, p. 158). Different levels of reliance on unstable and low wage employment are important to our understanding of the growing regional disparities that are illustrated in Figure 5.

Figure 5 goes here.

1
2
3 6. Conclusions
4

5 'If, as Smith maintains, the division of labour maximises the development of
6 very specialised skills, it also greatly increases the risk of losing much human
7 capital if a particular occupation becomes redundant' (Pagano, 2003, p.636)
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15 Questions of practical policy monopolised Keynes' considerable abilities. He was
16 convinced that we should not tolerate the levels of unemployment that emerged from
17 'capitalistic individualism' in the 1930s (Keynes, 1973, p. 381). There was, he
18 argued, no automatic market mechanism that would ensure full employment. This
19 was true, even if wages and prices were fully flexible and Keynes consistently worked
20 against those who blamed the depression of the 1930s on high wages for labour.
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Stabilising an unstable system is difficult and fine-tuning is not a serious possibility, but there needs to be some method for guiding the 'invisible hand'. Automatic stabilisers (tax reductions and public expenditure increases in recession) became the natural substitutes for the 'invisible hand' of the market in the post-war years.

History matters in two senses. First, past events have a lasting influence. Second, what works and is appropriate at one stage of economic evolution may be ineffective later. There are two relevant examples. First, relocation of industry depended on manufacturing expansion and also full (or over full) employment in prosperous regions. Second, post-war reconstruction, cheap oil and wage restraint encouraged by the memory of the Great Depression provided a favourable environment for demand management in the Keynesian Golden Age. Keynes was well aware that a move to sustained full employment would, in time, breed its own new needs, problems and demands. Hicks argued that economic policy had adopted a dangerously rigid 'labour standard' in the post-war years when maintenance of full

1
2
3 employment became, if not the only desirable objective, certainly the litmus test that
4
5
6 came before all others (Hicks, 1955).
7

8 In later years an inflation standard and free market fundamentalism substituted
9
10 for the 'labour standard'. A cautious approach to macroeconomic policy has a major
11
12 effect on real as well as nominal (price) variables. The steep rise in unemployment
13
14 and the significant shift to spatial inequality takes place in the years 1979-86 (see
15
16 Parts 3 and 4). Regional unemployment increases connect to deindustrialisation and
17
18 low opportunity regions do not demonstrate strong powers of recovery in later years.
19
20 The connections are unlikely to be the product of chance. The size of the market
21
22 determines the development of capital and increasing returns to scale (internal and
23
24 external) ensure that 'change [growth and decline] becomes progressive and
25
26 propagates itself in a cumulative way' (Young, 1928, p.533). Cumulative causation
27
28 accounts of economic development point to the possibility of growing regional
29
30 imbalance. The economically successful regions generate profits and easy access to
31
32 credit and these will encourage further investment (Sawyer, 1995; MacKay and
33
34 Molyneux, 1996). There is an ever present danger that markets will tend to settle
35
36 demand and new growth on the wrong places (Beveridge, 1944).
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43 Employability is not independent of employment and it is difficult to
44
45 encourage transfer when there is little to transfer to. Early response to job loss is
46
47 critical if we seek to avoid cumulative decline. High levels of nonwork connect to
48
49 collapse in the underlying industrial structure. Loss of work is 'a serious disruption in
50
51 workers' lives', it leaves a gap, or space, that communities, families and individuals
52
53 struggle to bridge (Piore, 1987, p.1836). The problems that follow from loss of work
54
55 connect to community and social values and there are problematic inter-generation
56
57 effects. Disguise and camouflage of measured unemployment has added to the costs
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1
2
3 of dependency (sickness benefit is more generous than unemployment benefit) and
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5
6 has encouraged lasting divorce from the labour market.
7

8 The evolution of an appropriate institutional structure for mixed economies is
9
10 not a narrow, technical problem (see Sawyer, 1995; Minsky, 1986). There is, Kalecki
11
12 warned, a difficult political economy problem that connects to full employment and
13
14 its shift in the balance of power: the political function of sound finance and low
15
16 inflation is to ensure that economic policy is driven by the short-term needs of
17
18 business (see Kalecki, 1943; Sawyer, 1995). The Keynesian Revolution was not a
19
20 sudden flash of revelation. Keynes was a careful observer and his ideas, thought
21
22 patterns and General Theory evolved over time, in response to the evidence of
23
24 instability provided by the Great Depression. Even more important, the Keynesian
25
26 Policy Revolution (with its combinations of public and private, collective and
27
28 individual) owed much to post-war cohesion and a sense of shared sacrifice and
29
30 purpose. The values, attitudes and power structures that inform the Counter
31
32 Revolution to Keynes are notably different, but there are three important themes we
33
34 can touch, if not fully explore.
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40
41 A 'wisely managed' capitalism would, Keynes (Keynes, 1973a, p.294)
42
43 predicted, be notably more effective in delivering goods and services than any
44
45 alternative system on offer. He did, however, stress that the good life and the
46
47 responsible society depended on more than output and wealth. As we grow more
48
49 productive and affluent, the important tests for mixed economies connect to the
50
51 opportunities they offer workers and citizens 'to develop their own potential, express
52
53 their identity and create their own future' (Bronck, 2009, p.305; Keynes, 1973a,
54
55 p.326-332). The second theme comes from Schumpeter. An economic system that
56
57 uses resources of given potential effectively is not necessarily ideal in developing
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1
2
3 resources whose potential is unknown. Schumpeter drew attention to the ruthless and
4
5
6 unstable energy of capitalism. 'Our capacity to innovate and make the right moves in
7
8
9 the endless battle to create the next generation of dominant goods [and services] and
10
11 technologies is far more important in the long run than the efficient allocation of
12
13 today's resources' (Bronck, 2009, p. 302-3). The third theme is that a sensible
14
15 political economy would recognise that the untempered operation of markets has to be
16
17 moderated by intervention. Unemployment (open and disguised) is an economically
18
19 and socially inefficient control mechanism (Keynes, 1973a, pp. 86-125). Moreover,
20
21 markets have limits and economics is not confined to market solutions. There is no
22
23 grand theory that decides the balance between private and public, but there are
24
25 products and services that markets do not provide effectively and efficiently (Keynes,
26
27 1973a pp.272-94). Private investment and private insurance are not consistently more
28
29 reliable than public investment and social insurance. The substitution of private
30
31 monopoly for private monopoly can add to capital cost, to contracting cost, to
32
33 uncertainty. The rules of engagement are different in public and private sectors
34
35 precisely because nonwork is expensive for the economy and the tax payer.
36
37
38 Schumpeter and Keynes both claimed that forms of investment 'more suited for
39
40 public than ... for private enterprise' have an important stabilising role (Schumpeter,
41
42 1943, p.120).

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Loss of confidence, increase in uncertainty, reluctance to invest, the dimming
of animal spirits and a shift from boom to bust should not come as a complete surprise
in capitalist economies. Loss of direction increases when 'enterprise becomes the
bubble on a whirlpool of speculation' (Keynes, 1973, p.159). There are deep
problems when speculation crowds out investment in 'nationally productive channels'
(Keynes, 1973a, p292). Schumpeter (1934, p.116) makes a similar point when he

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3 argues that the all important function of credit and capital is to ‘divert the factors of
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5 production to new uses [and so dictate] a new direction to production’. The
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8 Keynes/Schumpeter observations connect to recent claims that the financial sector has
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10 become irresponsible and socially useless. A successful, balanced economy capable
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12 of generating new opportunities requires a financial system which serves the needs of
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14 the productive sector, not vice versa (see Sawyer 1995)
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17 Adam Smith argued that ‘the love of our country seems ... to involve ... an
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19 earnest desire to render the conditions of our fellow-citizens as safe, respectable and
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21 happy as we can’ (Smith 1759, p.231). Sympathy and empathy, as well as self
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23 interest, are important components of human interaction. Those who argue for market
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25 forces on the grounds that they create sufficient income to spread throughout society
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27 have been slow to recognise that the discipline of individual contribution, if strictly
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29 applied, works strongly against certain groups in society, including those at some
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31 disadvantage in the labour market. Minsky’s value judgment is relevant, ‘the humane
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33 objective of stabilization policy is to achieve a close approximation to full
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35 employment’ (Minsky, 1986, p. 308). In the years following the Keynesian Golden
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37 Age, instability, insecurity, inequality and underemployment increased. Without
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39 some sympathy for those displaced by structural decline, closure and redundancy
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41 there is little substance to the nation state or to regional balance.
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For Peer Review Only

Table 1: IRC Compared with Wales and North

	1974-75	2000-01
Output per Head ^a	84%	69%
Male Earnings ^a	92%	79%
Household Expenditure ^a	86%	78%
	1971	2001
Male Work Level ^b		
GB	91.6%	80.2%
IRC	93.2%	83.7%
Wales and North	90.4%	75.1%
Work Gap	2.8%	8.6%
Male Unemployment Level ^c		
GB	5.2%	5.3%
IRC	4.1%	4.6%
Wales and North	6.7%	6.2%
Unemployment Gap	-2.6%	-1.6%

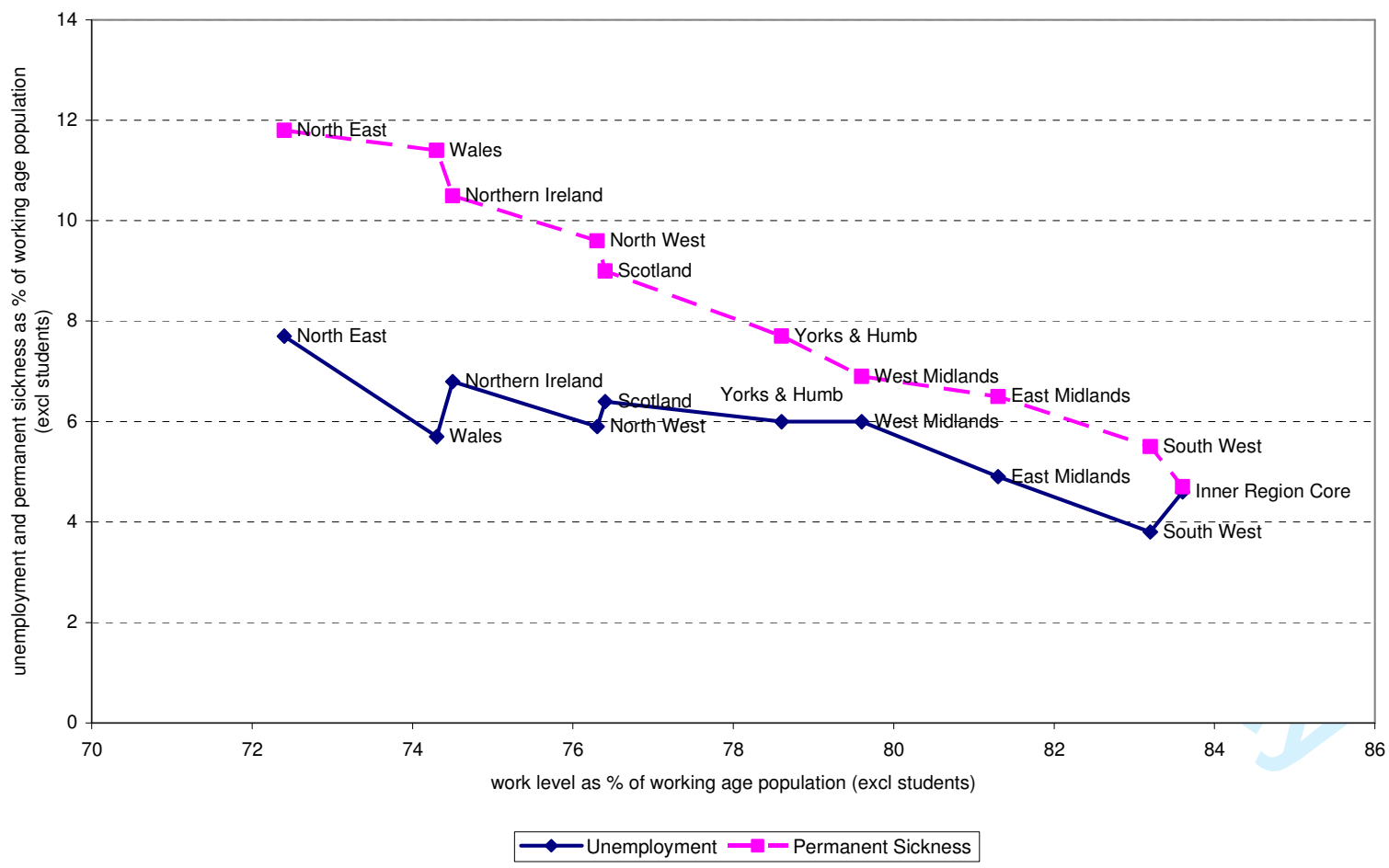
Notes:

- a) Wales and North as a percentage of IRC
- b) Employment and self employment as a percentage of non-student working age population

Table 2 UK Unemployment – 3 Steps to a Buyers' Market for Labour

Years	Male Claimant Unemployment Rate	Comment
1950-67	1.8%	Sellers' market for labour. Annual unemployment never above Beveridge target of 3%
Step 1 1968-72	3%	The years following the Phelps Brown hinge, or tipping point, with unemployment above 3% in 1971 and 1972
Step 2 1973-79	4.7%	The years following the first OPEC recession, with unemployment below 3% in only 2 years.
Step 3 1980-86	11.3%	The years following the second OPEC recession and including major deindustrialisation. Unemployment more than 6x the 1950-67 average and Long-Term unemployment a growing proportion of the unemployed.

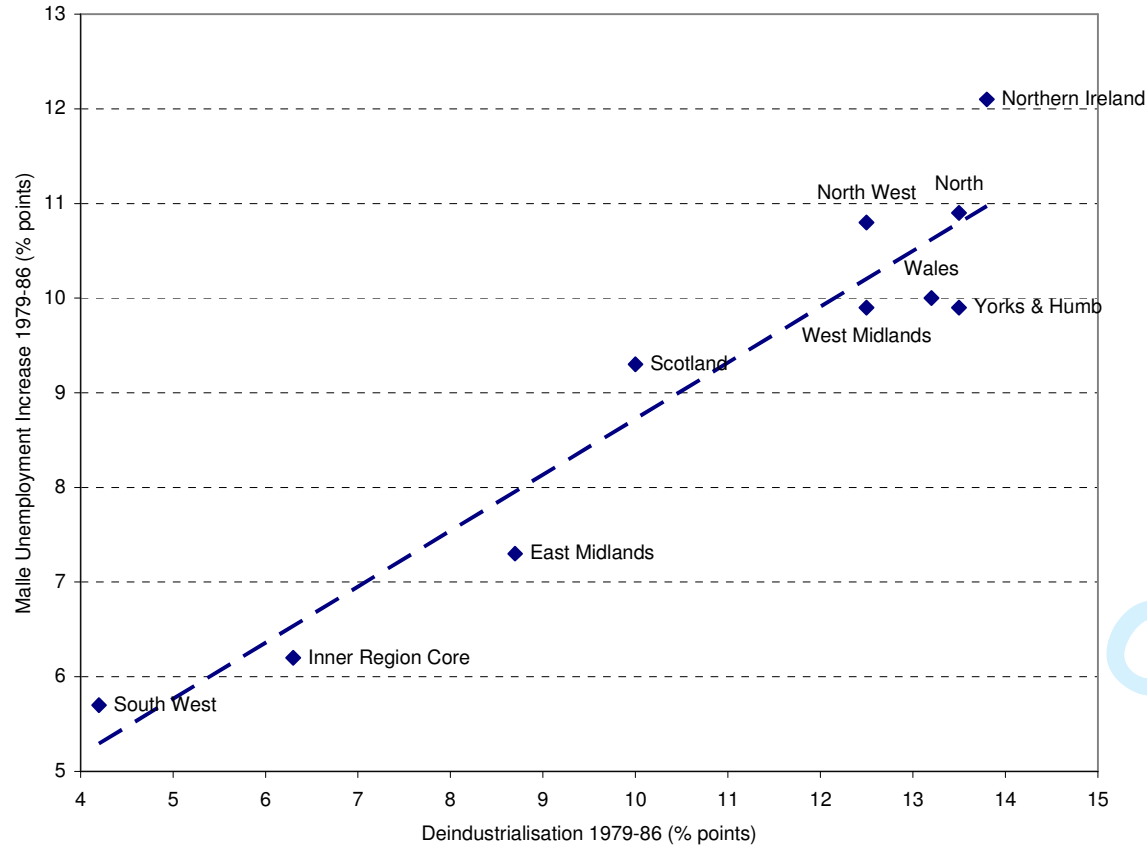
Figure 1: Work, Permanent Sickness and Unemployment: 2001



Source: 2001 Census

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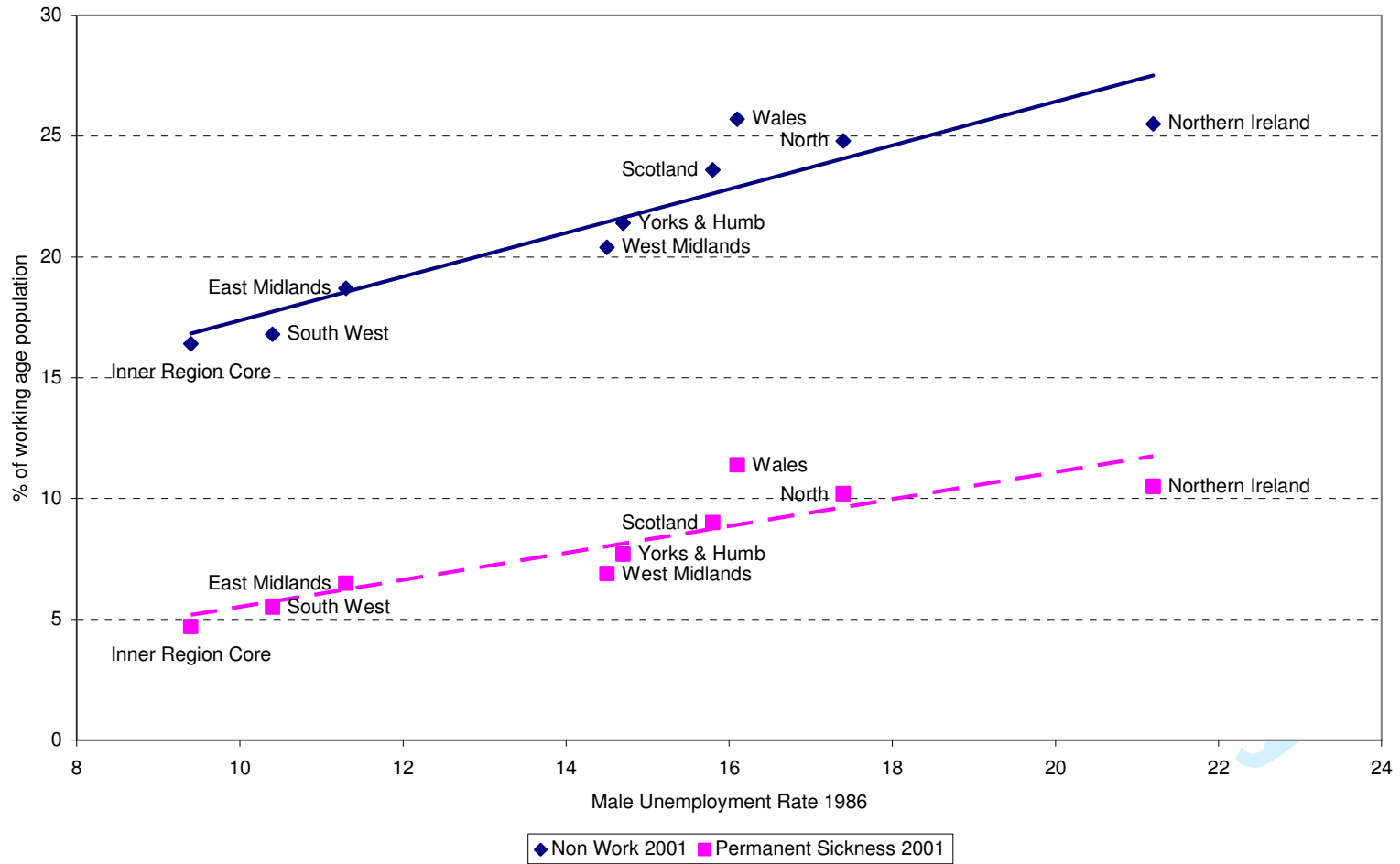
Figure 2: Deindustrialisation and the Growth of Unemployment



Source: Employment Gazette

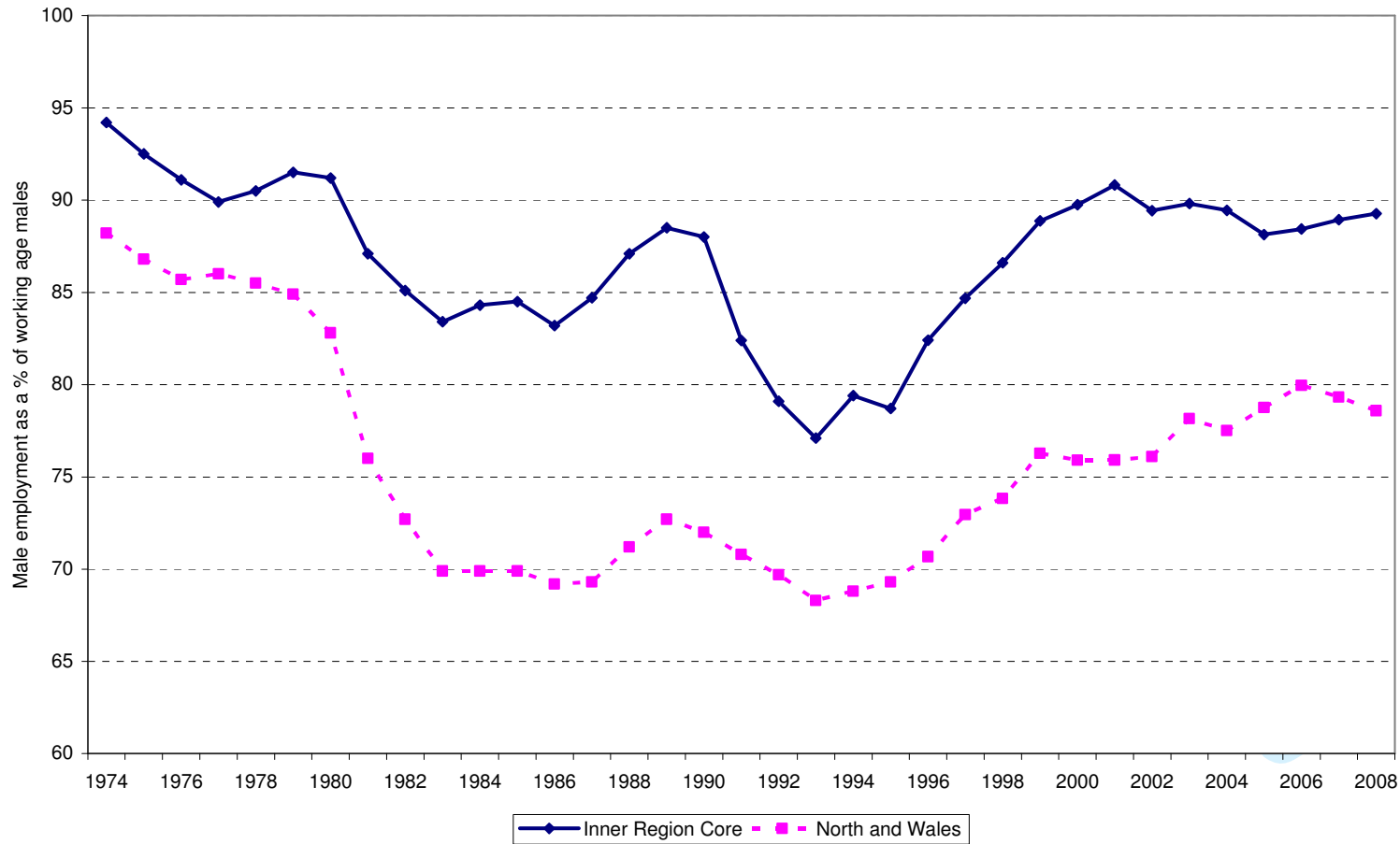
Notes: Deindustrialisation is defined as reduction in production industries between 1979 and 1986 as percentage of total employment in 1979. Increase in unemployment is based upon the claimant count.

Figure 3: Regional Continuity in Male Unemployment and Non-Work



Source: Employment Gazette, 2001 Census.

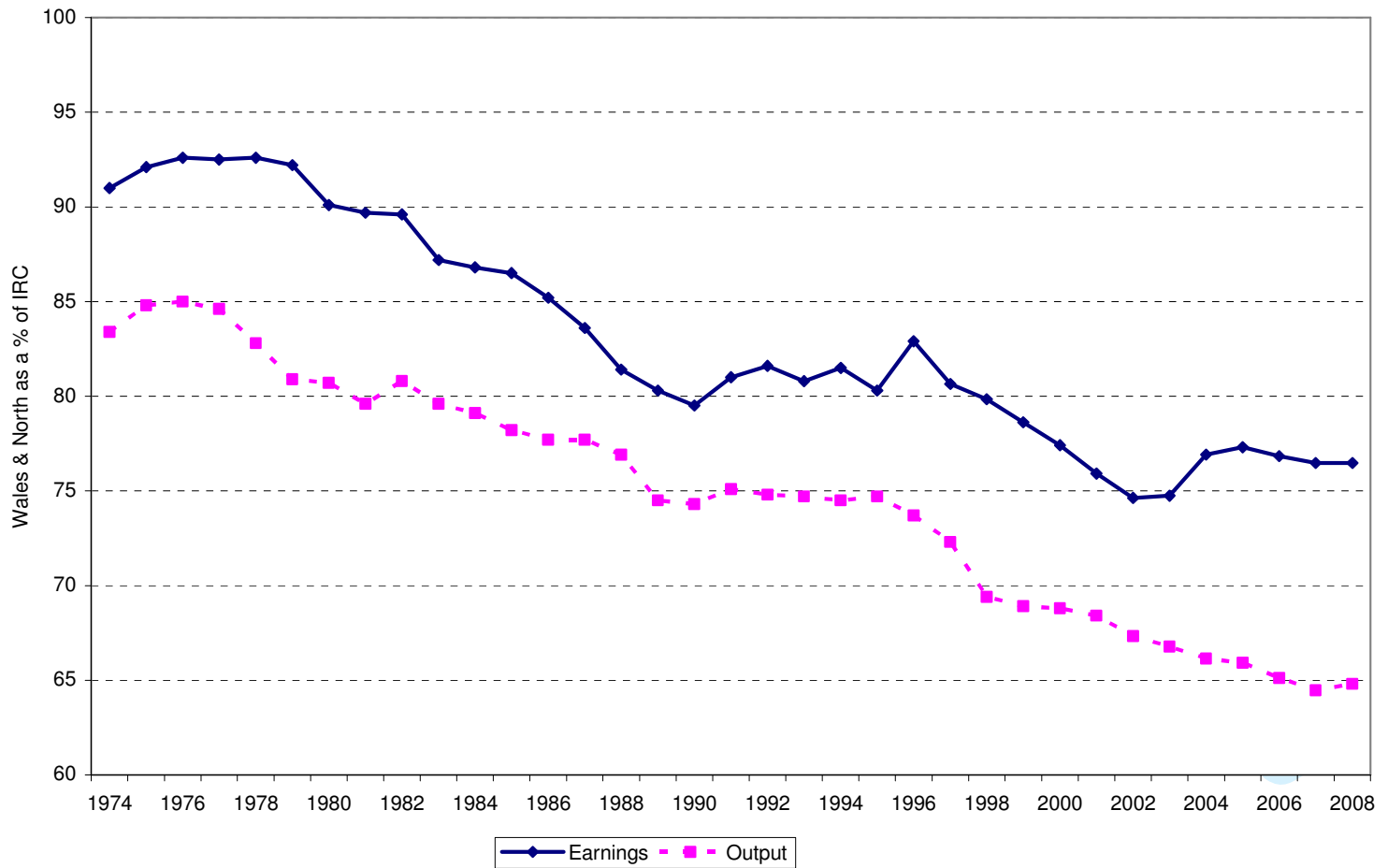
Figure 4: The Evolution of the Male Employment Gap



Source: Workforce in Employment, Employment Gazette; Mid-Year Population Estimates, NOMIS

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Figure 5: Earnings and Output Inequality



Source: New Earnings Survey, Annual Survey of Hours and Earnings, Regional Trends, ONS Time Series

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ⁱ In 1971, the Census Unemployed are those without work who are seeking and available for work. In 2001, the Census Unemployed are those who are not in employment, are available to start work within the next 2 weeks and have either looked for work in the last 4 weeks or are waiting to start work. This is equivalent to the ILO definition. ILO and Census Unemployment are higher than the numbers claiming unemployment related benefits in the UK – the ‘Claimant Count’.

ⁱⁱ Derived from Estimates of the Workforce in Employment, some men have two jobs and some jobs are taken by men aged over 64.

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