



# Youth Unemployment in Australia

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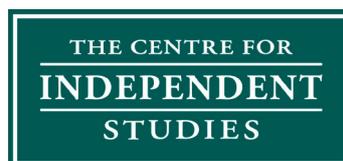
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# **Youth Unemployment in Australia**

Dr Patrick Carvalho



**Research Report 7**

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Recommendation 1: Implement structural reforms aiming to lift economic growth

Recommendation 2: Introduce local discounts to the nationally regulated pay floors

Recommendation 3: Introduce long-term unemployment discounts to the nationally regulated pay floors over a fixed period

Recommendation 4: Adopt an actuarial long-term management of the welfare system to rationalise the use of public funds and maximise effective outcomes

Recommendation 5: Lift numeracy and literacy skills of school-leavers to improve employability

Recommendation 6: Investigate innovative ways to increase the accountability of tertiary and VET institutions with respect to job market outcomes

## Acronyms

ABS Australian Bureau of Statistics

AWE Average Weekly Earnings

COAG Council of Australian Governments

GFC Global Financial Crisis 2007/8

HILDA Household, Income and Labour Dynamics in Australia

ILO International Labour Organization

NCA National Commission of Audit

OECD Organisation for Economic Co-operation and Development

NEET Not in Education, Employment or Training

PC Australian Government Productivity Commission

VET Vocational education and training

UN United Nations

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## Executive Summary

### The rising youth unemployment problem

- Every year a large number of young Australians aged 15–24 enter the labour market but quickly discover that finding a job is tough and keeping one is not getting easier.
- Youth unemployment has nearly doubled since mid-2008, with around 300,000 youth now unemployed in Australia, accounting for over a third of total unemployment.
- Youth unemployment has averaged 13.5% in the past 12 months, more than twice the adult unemployment rate.
- Full-time youth employment positions have been severely reduced for both teenagers and early 20s in the past seven years, with current levels still below the pre-GFC period.
- Worse still, two-thirds of the recent surge in youth unemployment rates was due to the increased number of teenagers looking for part-time jobs.
- Many of the 360,000 young Australians who are currently not in employment, education or training — also known as NEETs — are not even being

technically classified as unemployed, because they are not actively looking for a job.

- Data shows that, although the number of teenager NEETs aged 15–19 has been in sharp decline due to higher Year 12 attainments, the number of early 20s NEETs aged 20–24 has solidly grown since the GFC, reaching the highest peak since 2003.

### Lift economic growth

- There are many causes of youth unemployment, but the main factor behind current jobless youth figures is the lack of robust economic growth.
- A low-skilled, inexperienced young workforce with great emphasis on part-time and casual jobs is particularly vulnerable to adverse economic conditions in the job market, which leads to youth unemployment being higher and more unstable than overall unemployment.
- **Recommendation 1:** Australia must implement structural reforms aiming to lift economic growth to combat the recent surge in youth unemployment (particularly tax reform, reducing barriers to competitive markets and adopting a job-creation oriented workplace relations strategy).

## Smart regulation

- Another impediment to youth job creation in Australia is counterproductive workplace regulation, in particular high minimum wages and industry-specific award rates.
- At high levels, regulated pay floors can be detrimental to job creation, making it difficult for young jobseekers lacking job experience, and the long-term unemployed, to get into the workforce.
- There has been a steep increase in the number of long-term unemployed since the GFC. Currently there are more than 50,000 young Australians currently failing to find a job for more than 12 months.
- **Recommendation 2:** the government should introduce local discounts to nationally regulated pay floors, taking into account diverse intra- and inter-state living costs and disparities in youth unemployment across the country.
- **Recommendation 3:** the local discount to minimum wages should be coupled with fixed-period discounts to all nationally regulated pay floors for those who are long term unemployed.

## Combat welfare dependence

- Some jobseekers, particularly youth with disadvantaged backgrounds, genuinely struggle to get access to the job market regardless of pay floor levels or job search efforts.
- Welfare payments should be structured to enable and incentivise recipients to return to the workforce as quickly as possible, including well-designed activity tests that effectively improve the chances to land a stable job.
- Effective welfare assistance for some disadvantaged groups at risk of long-term income support reliance

can require a considerable amount of public resources, however targeted intervention through transition-to-work programs could be a sound investment decision.

- **Recommendation 4:** adopt an actuarial long-term management of the welfare system, following the New Zealand model to rationalise the use of public funds and maximise effective outcomes.

## Boost skills

- Analysis of Australia's Beveridge Curve shows a growing mismatch between young jobseekers and current job vacancy positions.
- A good foundation of numeracy and literacy skills directly enhances productivity at work, and can help lower skill mismatches in the job market by better equipping young workers with the basic skills needed to learn new skills.
- Although lifting Year 12 or equivalent attainment rates is laudable, more important is to make sure that, while at school, students are actually learning the basic educational skills in order to boost their employment prospects.
- **Recommendation 5:** lift numeracy and literacy skills of school-leavers to improve employability.
- The current demand-driven system incentivises educational institutions to enrol as many students as possible, regardless of their suitability or job market demands, lowering admission standards and reducing responsibility to teach subjects that improve human capital in the job market
- **Recommendation 6:** investigate innovative ways to increase the accountability of tertiary and VET institutions with respect to job market outcomes.



## Introduction

Every year a large number of young Australians enter the labour market. But they quickly discover that getting a job—or even maintaining one—is not straightforward. And worse, the prospect is not getting easier. Youth unemployment has progressively taken a hit after the latest Global Financial Crisis (GFC), practically doubling since mid-2008. At an average rate of 13.5% in the past 12 months, the jobless rate among those aged 15 to 24 has reached worrying levels once thought to be left behind in a distant past. Currently, there are around 300,000 youth unemployed in Australia, accounting for over a third of total unemployment.

As this study shows, youth unemployment rates tend to always be higher and have larger swings than adult rates. Most young jobseekers are inexperienced, with low skill levels, undermining their employability. In addition, younger workers are more exposed to less secure forms of employment contracts—in Australia, around two-thirds of working teenagers are in casual jobs as opposed to less than one-fifth of workers in other age brackets.<sup>1</sup>

Unemployment is largely responsive to economic cycles, and therefore a worsening of youth rates is a direct corollary of economic downturn following the

GFC. Yet, in comparison with previous recessions, this time is different (**Box 1**). Unemployment rates have not receded after an initial spike; quite the opposite, if anything.<sup>2</sup> Unemployment rates in Australia have been in an upward trend since the end of 2008—and should economic conditions not improve, other surges may follow suit.

Australia is not alone when it comes to the harsh socioeconomic consequences of the GFC, which hit youth harder than any other group. Since 2008, the worldwide number of young jobseekers has seen the largest increase on record.<sup>3</sup> There are more than 75 million young people looking for a job globally, constituting 40% of the world's unemployed.<sup>4</sup> In the OECD alone—a group of mostly 34 rich nations of which Australia is a member—the number of employed youth fell by more than 7.5 million over the same period.<sup>5</sup> In summary, youth unemployment is a global issue.

This report investigates the increasing phenomenon of youth unemployment in Australia, with a focus on the recent developments since the GFC. The future rests on the young generation, and Australia cannot miss the chance of getting it right when facing the challenges of youth unemployment.

### Box 1: This time is different

The history of youth unemployment in Australia typically follows the booms and busts of economic activity. The usual pattern is: at the onset of every activity slowdown, there is a strong hike in the unemployment rates, followed by an easing period as the economy revives.<sup>6</sup>

But this time is different.

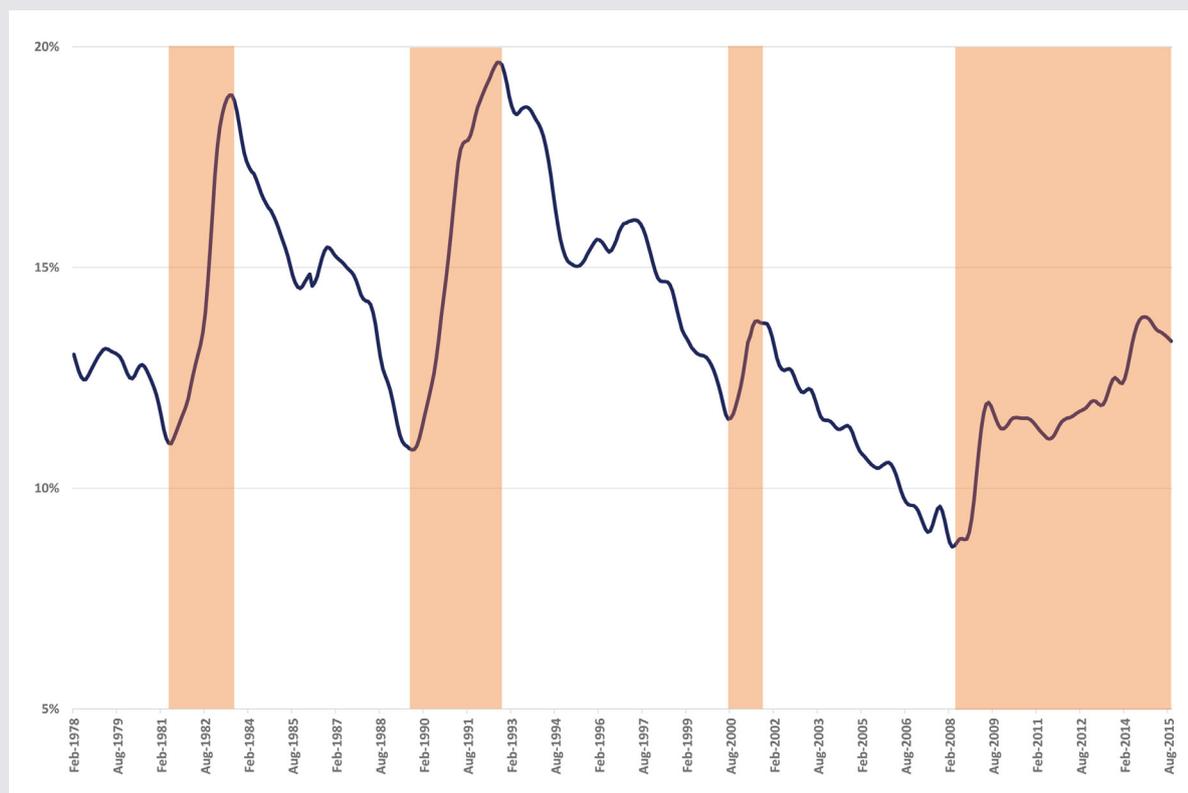
**Figure 1** shows Australia’s youth unemployment trend rates based on Australian Bureau of Statistics (ABS) data.<sup>7</sup> The shaded areas represent the biggest hikes in jobless youth, and match Australia’s main economic downturn periods: a global recession in the beginning of the 1980s, mainly due to international efforts to fight the lingering stagflation crisis; the 1990s ‘recession we had to have’; the short-lived dotcom crisis in 2000-01; and the GFC. In all but the last crisis, youth unemployment rates have eased following an initial surge.

The difference this time regards the current difficulties in dealing with the driving forces of economic upheaval. In all previous crises we were able to tackle the underlying issues in the economy, paving the way to recovery. The same cannot be said about the GFC. After years of fiscal and monetary largesse, leading to unprecedented levels of central banks’ money base expansion and indebted governments, the global economy is still struggling to find its way to prosperity.

And worse, if another major international financial blowout happens in the near future — and there are increasing risks pointing in that direction — the global ability to respond is significantly reduced. Not only do most of the elements that set the GFC still linger, but governments seem unable to advance a sensible round of economic reforms.<sup>8</sup>

In short, the GFC is not over yet, neither is its impact on Australia’s youth unemployment rates.

**Figure 1: Youth Unemployment Rate in Australia**



Source: ABS, Labour Force, Australia; Trend data.



## The Australian Evidence

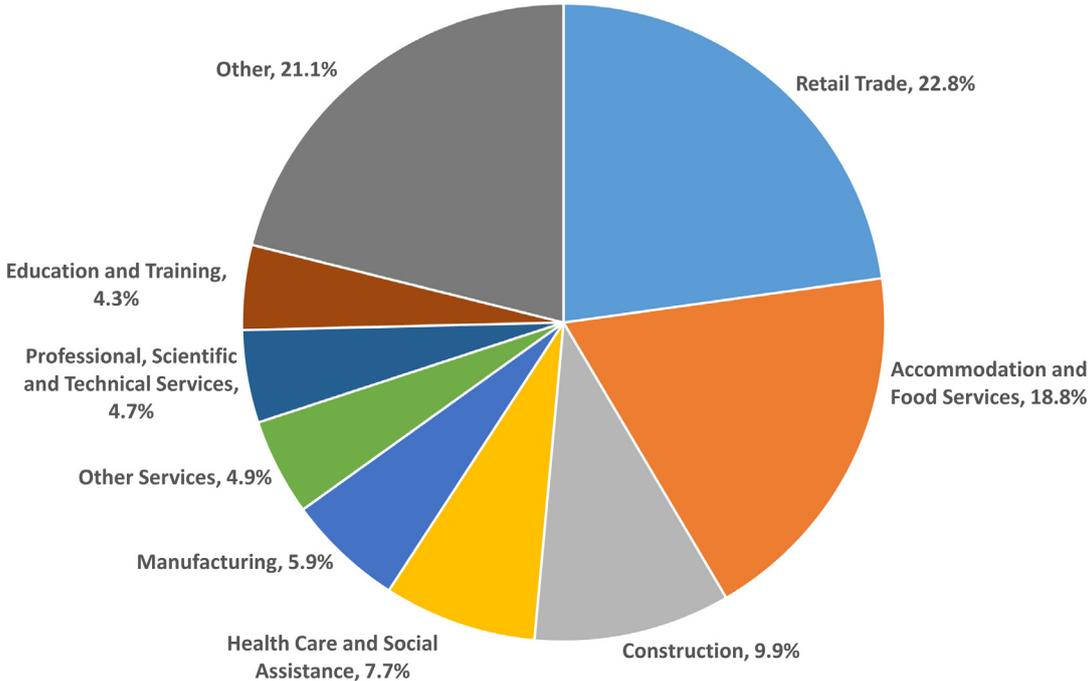
### The Youth Labour Market

With the ageing of the Australian population, the ratio of the youth population has been in a slight decline in past decades—undermining claims that youth unemployment in Australia is partly due to an allegedly high immigration intake (**Box 2**). Currently, there are around 3.1 million Australian residents aged 15 to 24 years, representing 13% of the population; as opposed to almost 15% two decades ago and 17% in the 1980s.<sup>9</sup>

Youth is overly represented among the unemployed, with around 300,000 people aged 15 to 24 not able to find a job, accounting for over a third of the total jobseekers in Australia. For reasons outlined later in more detail, the low levels of skills and lack of job experience make it particularly hard for youth to get a toehold in the job market.<sup>10</sup>

Regarding those in the workforce, 1.8 million young people are currently employed, accounting for 15% of working Australians. **Figure 2** displays how the 15- to 24-year-old workers are largely concentrated in a few industries. The most common youth jobs are in retail trade (22.8% of all young workers), accommodation and food services (18.8%), construction (9.9%), health care and social assistance (7.7%), and manufacturing (5.9%). It is worth noting these industries are heavily covered by modern awards regulation, that—as will be outlined below—impose high entry barriers and costs that are counterproductive to raising youth labour utilisation,<sup>11</sup> and therefore make it harder to address youth unemployment.

**Figure 2: Share of Youth Employment by Industry**



**Source:** Department of Employment (2015).

## Box 2: The Lump of Labour Fallacy in Australia

The search for youth unemployment culprits has prompted a range of incorrect conjectures that struggle to find supportive evidence. One in particular is the 'lump of labour' fallacy, which is underpinned by a notion there is a fixed amount of work to be shared by all job market participants.

According to this view, there is a zero-sum assumption in the labour market, implying someone's gain necessarily means someone's loss. This assumption is often cited in arguments against migration. Indeed, a disproportionate migration intake could inadvertently increase the domestic labour supply, and—assuming labour demand is constant—unemployment could rise. Nonetheless, this rationale ignores the positive impact of migration to stimulate growth and job creation.<sup>12</sup>

Further, it is important to recognise that Australia's migration is highly responsive to overall jobless rates, which promotes an endogenous foreign worker intake balance: in times of good economic performance, and low unemployment, net migration numbers are propped up; the converse also holds true with fewer migrants entering Australia when domestic unemployment rates are high.<sup>13</sup>

Moreover, Australia's demographics keeps disproving the relationship between the number of potential young workers and youth unemployment. The proportion of young Australians has been declining in past decades with no correlation to the ups and downs of youth unemployment—in particular with the steep increase in youth jobless rates since the GFC.

There are many examples where the much-vaunted 'lump of labour' belief has failed to materialise. For instance, the French government introduced the 35-hour working week in 2000 in a botched attempt to reduce unemployment; it has the opposite effect, as the measure increased labour costs.<sup>14</sup>

Another example is the wrongheaded support for early retirement to tackle youth unemployment. Such a policy has been vehemently rejected by the OECD, which presents solid data countering the fanciful notion that fewer workers means more jobs for the unemployed.<sup>15</sup> Indeed, the share of youth in the working-age population in developed countries has consistently decreased in the last 40 years, without alleviating the youth unemployment plight, which means that from a policy perspective, reducing unemployment should not be about reducing the supply of workers.<sup>16</sup>

The 'lump of labour' fallacy, although flawed, is persistently and opportunistically brandished in populist discourse. In Australia, much of the argument has been used against immigration—despite data supporting the argument that immigrants make a net contribution to Australia's economy.<sup>17</sup>

For instance, the Australian Council of Trade Unions advocates for Australia to clamp down on the number of backpackers and other foreigners receiving working visas (in particular 457 visas) in order to "allow more opportunity for young Australians to enter the workforce".<sup>18</sup>

Such claims, time and again, have been discredited by evidence of a decreasing youth labour supply trend.<sup>19</sup> Nonetheless, for instance, there has still been support for the new federal Budget decision to disproportionately raise income tax for holiday visa workers.<sup>20</sup> Not surprisingly, there have been anecdotal reports that some backpackers and international workers are already turning their backs on Australia with adverse outcomes on some local communities.<sup>21</sup> Most holiday workers tend to spend their (hard) earned money locally in Australia, supporting business struggling to find willing helping hands, while also boosting the community retail industry.<sup>22</sup>

Contrary to the 'lump of labour' fallacy, each immigrant contributing to the economy does not translate into an Australian being pushed out of the labour market. Data shows that the periods with the highest intake of migrants are usually correlated with low rates of unemployment.<sup>23</sup> In fact, the uninterrupted economic growth of the last 24 years largely relies on the hardworking ethos of a vibrant and diverse pool of immigrants.<sup>24</sup>

For the sake of Australia—and Australians—we should remain open to a productive and economically rewarding skilled pool of migrants. Unfairly blaming migrants for youth unemployment does not help the cause, and indeed it might worsen the problem.

## The GFC Impact on the Youth Labour Market

The Global Financial Crisis hit the labour market prospects of the young demographic particularly hard. Australian youth labour force participation rates have dropped from 71.3% of youth either working or unemployed in March 2008 to around 66.2% (the lowest historical level) in the beginning of 2014, followed by a slight improvement to the current 67.6% levels (**Figure 3**). Lower participation rates mean many jobless young Australians could not technically be considered unemployed, since they stopped looking for jobs, and therefore, were considered as being outside the labour market.<sup>25</sup>

Notwithstanding lower participation rates, youth unemployment (in particular for Australian teenagers) kept increasing from 2009 onwards and has suffered two major blowouts since the GFC (**Figure 4**). The first steep increase started from August 2008, when the trend rate was just under 9% (the lowest historical level), and quickly climbed to around 12% in mid-2009. After a relatively stable period, the trend data series presented another sharp surge in 2014, reaching close to 14%—the highest level since the beginning of the century, mainly in response to a higher labour market participation as depicted in Figure 3 (i.e. more young Australians looking for jobs).

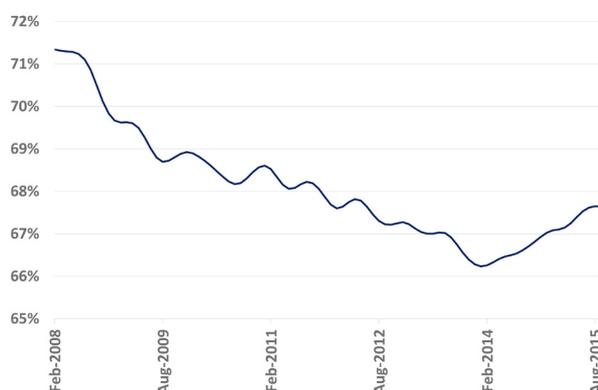
To fully understand the dynamics in the youth labour market force since the GFC, it is important to disaggregate the data into two separate cohorts, covering teenagers aged between 15 and 19 years old, and the older segment between 20 and 24 years old (early 20s). Teenagers and early 20s are quite different segments, with different demands and expectations.

Whereas the former is usually enrolled in an educational institution with a preference towards part-time work, the latter is more focused on full-time careers. As a result, each cohort faces different challenges and opportunities.

**Figure 5**, depicting the number of unemployed youth, shows that right at the start of the GFC, the number of those looking for full-time positions quickly rose for both teenagers and early 20s. This explains the first bump in the overall youth unemployment rates. However, the second surge in youth unemployment rates in 2014 is mostly due to the increased number of teenagers looking for part-time jobs, accounting for two thirds of the total increase in unemployed youth.

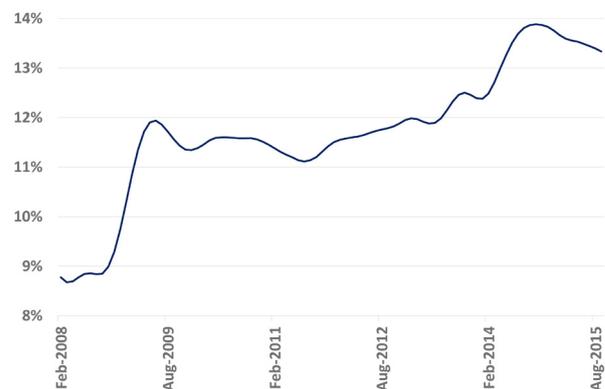
On the other side, **Figure 6** shows a consistent decline in the number of employed youth since the end of 2008, with manufacturing, construction and retail trade industries accounting for most of the job terminations. For teenagers in particular, overall employment is still currently below pre-GFC levels—dropping from 748,000 job positions in August 2008 to 646,000 in September 2015. In addition, the numbers of teenagers working both full- and part-time decreased over the period, although a bigger blow was felt in full-time positions, accounting for nine out of 10 teenage job losses. Yet, when it comes to the early 20s cohort, most of the vanishing full-time jobs were transformed into part-time ones, which is a sign of possible underemployment. In August 2008, there were 813,000 early 20s in full-time positions in comparison with only 705,000 currently; whereas during the same period, part-time jobs for this cohort increased by 123,000 positions up to 482,000 part-time employed in August 2015.<sup>26</sup>

**Figure 3: Youth Labour Force Participation Rate**



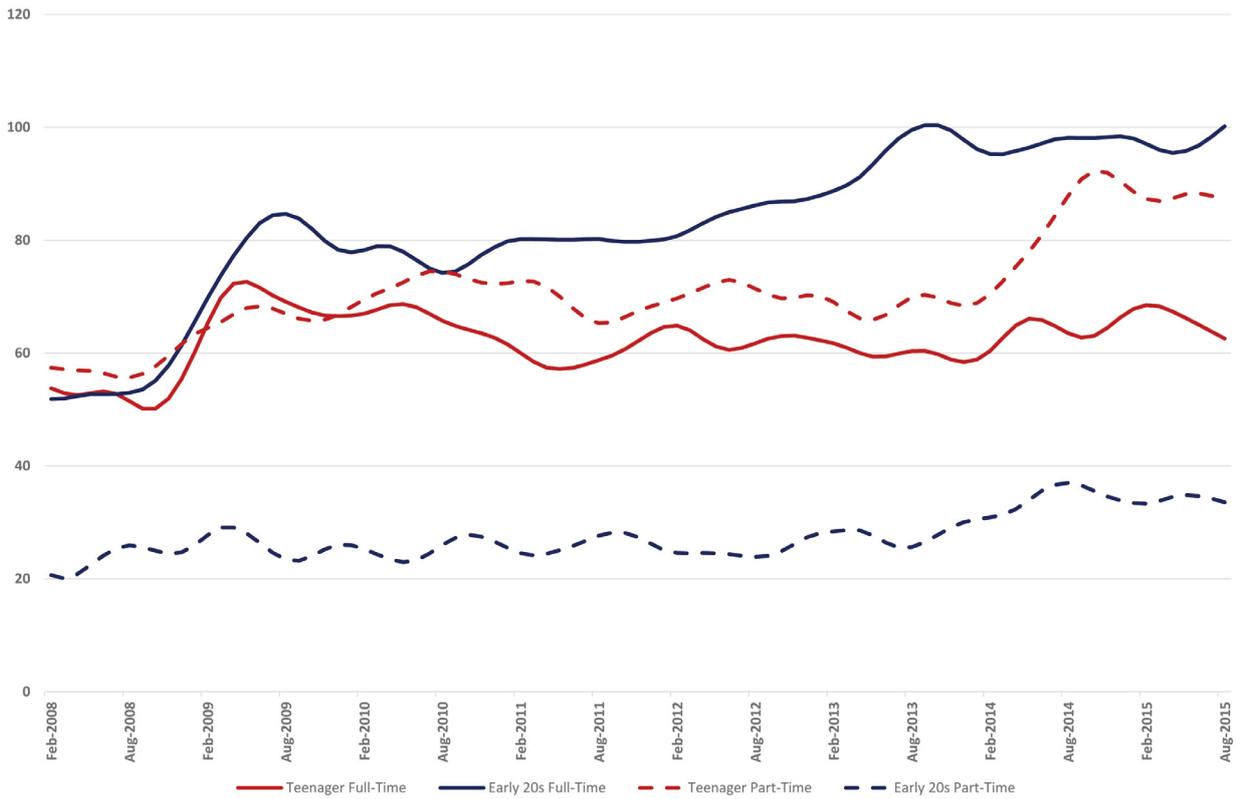
Source: ABS, Labour Force, Australia; Trend data.

**Figure 4: Youth Unemployment Rate**



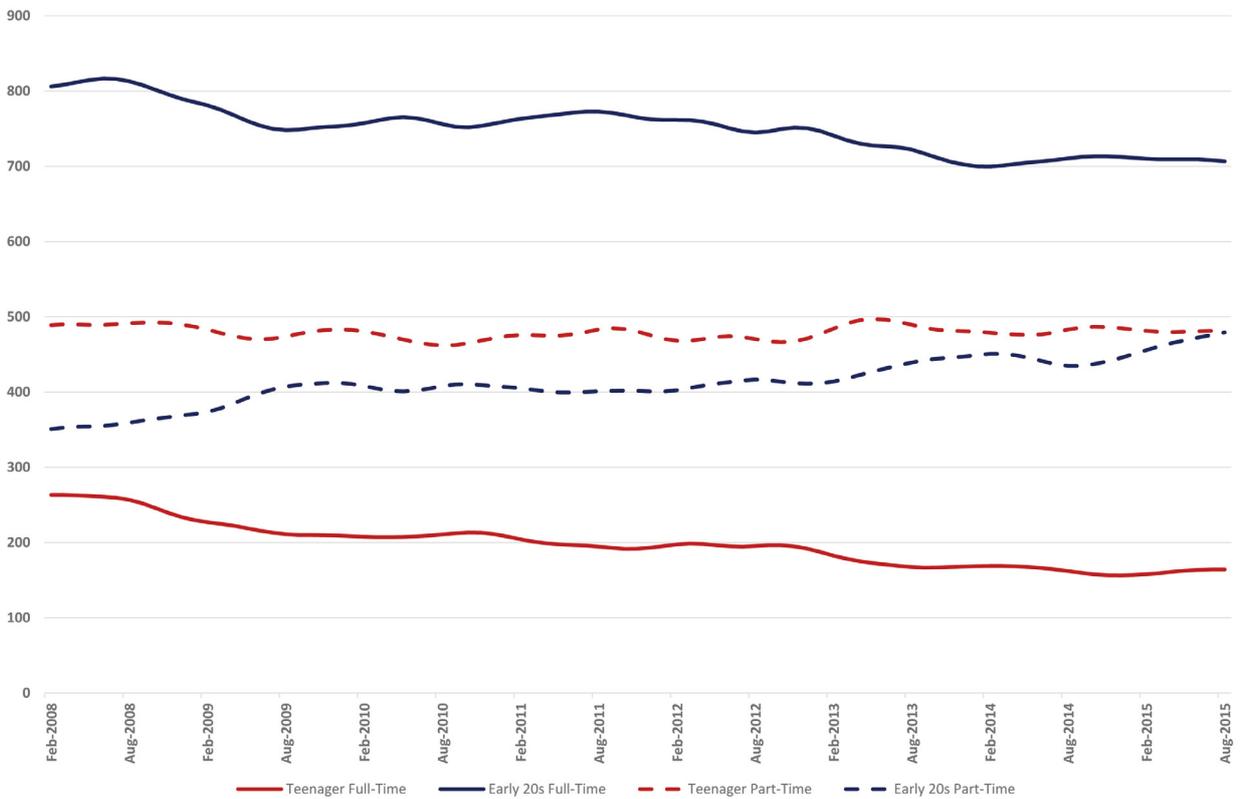
Source: ABS, Labour Force, Australia; Trend data.

**Figure 5: Youth Unemployed ('000s)**



Source: ABS, Labour Force, Australia; Trend data.

**Figure 6: Youth Employed ('000s)**



Source: ABS, Labour Force, Australia; Trend data.

## Labour Market Mismatches: The Beveridge Curve Relationship

Labour market mismatches occur when there is a gap between the supply and demand of workers, in particular when employers seek a certain set of skills that do not correlate with the skills offered in the supply of jobseekers. This imbalance between the supply and demand of skills (i.e. skill mismatches) may ultimately constitute an important determinant of youth unemployment. In particular, this is the case when job positions require skills learned through work experience, which by definition a first-time young jobseeker does not possess. In short, the greater the mismatch, the longer a job position will remain open.<sup>27</sup>

In economics, the relationship between unemployment and job vacancy rates is captured by the Beveridge Curve—named after economist William Beveridge’s research on the topic<sup>28</sup>—which neatly summarises both the cyclical and structural components of unemployment. The downward slope characterises the negative cyclical correlation between unemployment and job vacancies through the business cycle. In good times, unemployment is low and the job offerings are high; in bad times, the converse applies.

The structural component of unemployment is captured by the position of the curve, representing deeper underlying trends in the structure of the economy where skill mismatches might arise, such as sectoral changes (e.g. the transition from a manufacture-based economy towards a service-oriented economy), adverse policy decisions (e.g. higher mandatory minimum wages or counterproductive red tape measures) and demographic movements (e.g. an ageing population). In this sense, a rightward shift of the curve represents a worsening of the efficiency of job matches.

**Figure 7** shows the Beveridge Curve for young jobseekers in three distinct periods in Australia, with the dotted lines representing their respective linear trends. The first cluster of points in orange refers to the quarterly data prior to the GFC, from 2003 to 2008, which constituted the best job market outcome in the last 30 years. The grey dataset shows the period after the GFC up to the present. Lastly, the blue cluster of points represents the quarters following the 1990’s ‘recession we had to have’.

The indisputable—and concerning—outward shift of the trend line after the GFC represents a worsening in Australia’s labour market for young Australians, with a growing mismatch between young jobseekers and potential positions. The phenomenon is not unexpected, and indeed is similar to the picture for overall unemployment rates.<sup>29</sup>

There are many forces at play behind the shift. A deterioration in job search matching is not unusual after an economic crisis. For one, businesses are often more reluctant to fill vacant positions due to economic uncertainty, particularly with regards to less skilled and less experienced workers.<sup>30</sup>

Furthermore, Australia’s intricate modern awards system implemented in 2009 imposes counterproductive labour costs, exacerbating the risks of a bad hiring,

and therefore leading business to be more cautious whenever expanding the payroll.<sup>31</sup>

Another reason could be skill mismatches in the labour market.<sup>32</sup> As a result of difficult times, many companies are forced to downsize, or simply shut down; sometimes even entire industries collapse. In the meantime, workers with a particular skill set are laid off and cannot quickly enough learn new ones required by existing vacant positions. Economists generally believe the labour market should adjust to such imbalances, especially over time.<sup>33</sup>

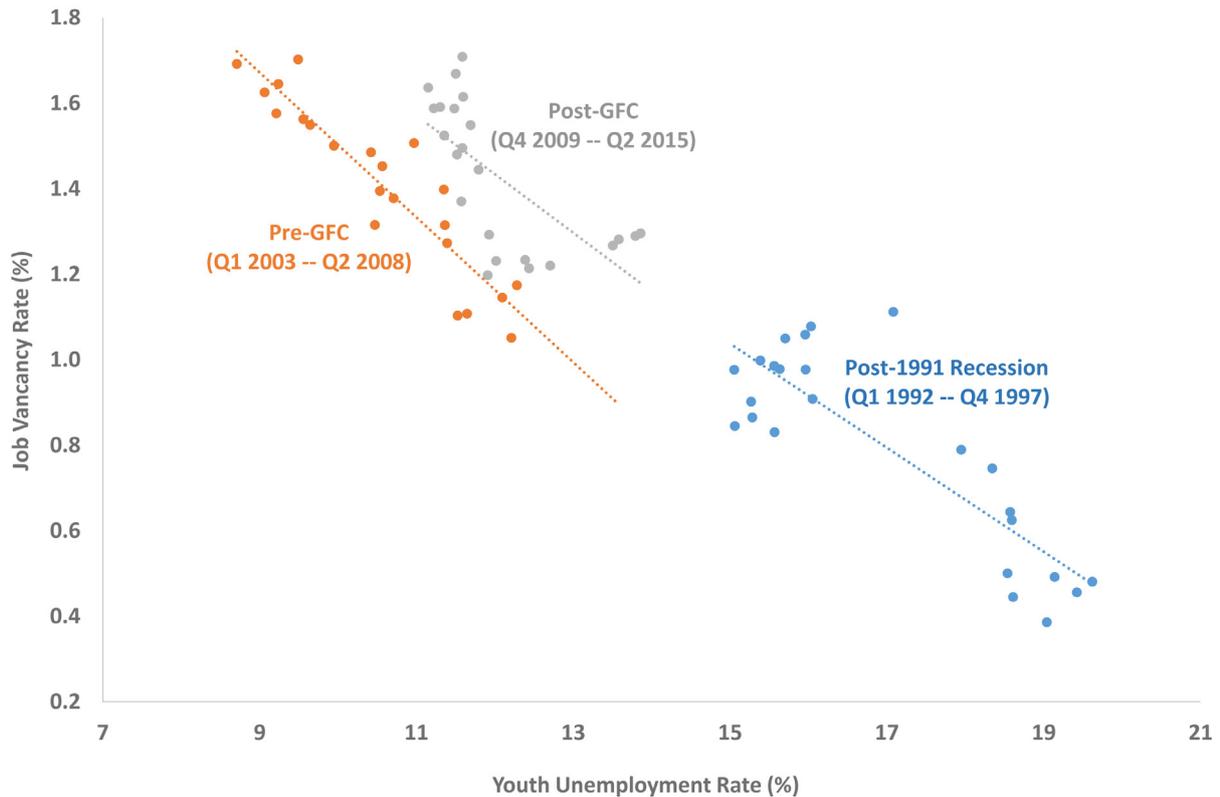
However, the persistence of the current misallocation might point to a bigger phenomenon at play: the very nature of modern jobs is changing.

A service-oriented, highly specialised economy, such as Australia’s, with increasing degrees of automation and information systems, requires a new breed of workers to perform an increasingly challenging set of tasks—increasing the role of education as a decisive factor for employability. Additionally, high job turnover rates discourage firms from offering on-the-job training.<sup>34</sup> This all leads to a wider gap in the supply and demand of skills in the labour market, with the low-skilled, experienced youth hit harder. If this proves to be the case, investments in education and training of young jobseekers might help alleviate current youth unemployment levels.

In any case, a silver lining appears in the current outward movement in the Beveridge Curve for young Australians when examining the post-1991 recession dataset cluster. Recovery back then was much more painful, with lower job vacancies and higher unemployment rates. Additionally, it seems that with strong economic activity—such as experienced between 2003 and 2008—it is possible to reverse unfavourable shifts in the Beveridge Curve movements in the near future.

Hence, it is best to address the matter on two fronts. First, it is crucial to implement a much-needed series of productivity-enhancing reforms in order to return towards a sustainable higher economic growth path. Second, potential skill mismatches could be effectively addressed by improving the efficiency of schooling, with a focus on foundational skill learning rather than content learning. Aiming at measurable indicators—such as the PISA international results on numerical literacy, reading and problem-solving skills (in all of which Australia has regressed in recent assessments) or NAPLAN results—would be integral to a sensible and more flexible solution. This strategy would enable Australia to effectively tackle the educational impairments that might act as hurdles preventing the market equalising demand and supply through price signalling (i.e. higher wages). Hence, by empowering young workers with solid foundations on which they can build to learn trade skills (rather than dictating what content to learn), skill mismatches will tend to have a shorter lifespan—whatever the skills demanded in the coming future may be.

**Figure 7: The Beveridge Curve for young Australians**



**Source:** ABS data; Author’s calculation.

### Long-term Unemployment among Youth

Long-term unemployment presents a real menace to young Australians, possibly leading to years—if not a lifetime—of struggle to get a stable, well-paid job. In addition to the income forgone from not actually working, the longer a person stays unemployed, the greater risk of losing important working skills. Moreover, long spells of unemployment send the wrong signals to potential employers, further undermining the prospects of landing a job.<sup>35</sup>

Data on young jobseekers experiencing long unemployment duration shows the situation has considerably deteriorated since the onset of the GFC, with more than 50,000 young Australians currently failing to find a job for more than 12 months.

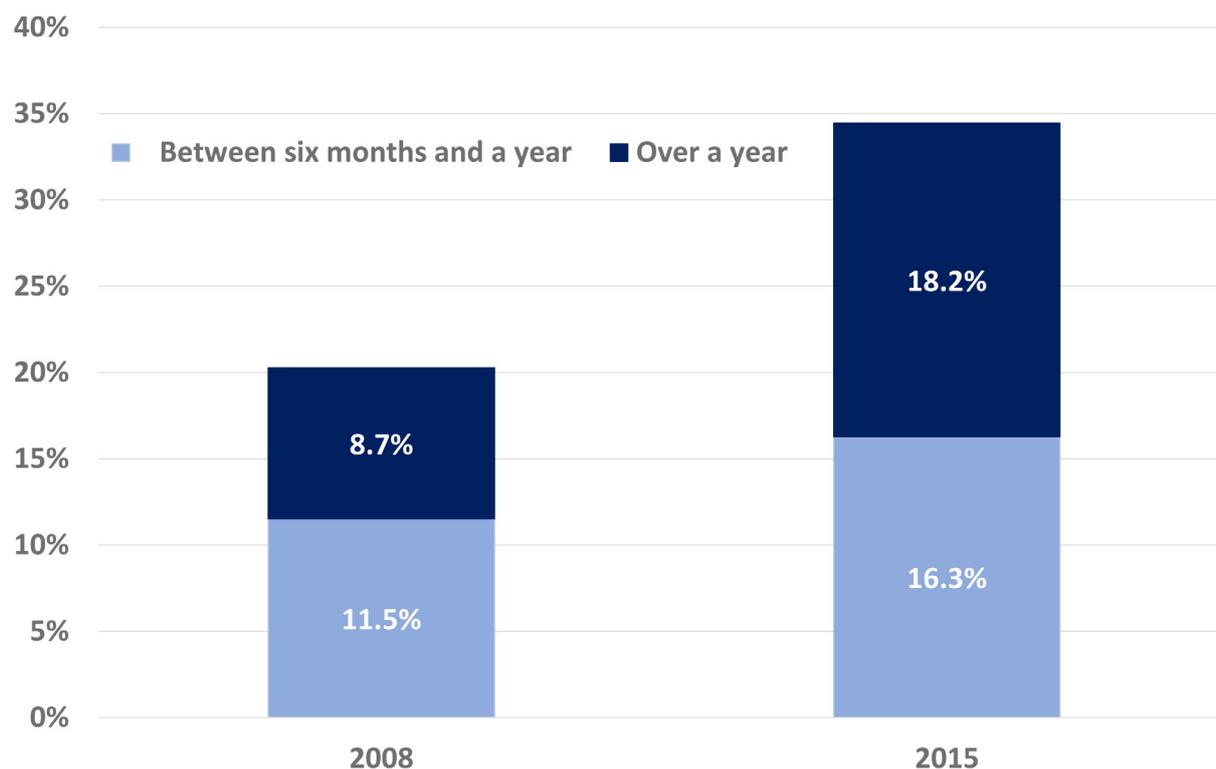
**Figure 8** depicts the share of Australian young people with long unemployment spells that exceed six months and a year.<sup>36</sup> The traditional definition of long-term unemployment refers to spells of 12 months or more.<sup>37</sup> By this measure, the average proportion of young long-term unemployed has more than doubled in the last seven years, from 8.7% of the total pool of young jobseekers in 2008 to 18.2% in 2015. This is

particularly concerning as the current proportion of long-term unemployed youth is near its highest level since 1999. Additionally, one in three young Australians experiencing long-term unemployment could not find a job in the past two years, severely increasing the risk of lifetime welfare dependence.

For those young jobseekers not technically considered long-term unemployed but still experiencing long spells of unemployment duration between six months and a year, the same dangerous patterns arise: from 11.5% in 2008 to 16.3% in 2015—and again, the highest levels since the beginning of the respective ABS time-series.

Hence, the overall percentage of young jobseekers on long durations of unemployment increased from 20.3% in 2008 to 34.4% in 2015. That is, roughly one in three young jobseekers have at least a six-month duration of unemployment. Such worrying statistics should urgently foster a mature debate on the main impediments of youth job creation—in particular with respect to minimum pay floors that disproportionately price long-term jobseekers out of the market.<sup>38</sup>

**Figure 8: Share of young jobseekers on long durations of unemployment**



**Source:** ABS, Labour Force, Australia; Author’s calculation; 12-month average; Share as a percentage of the total pool of young jobseekers.

### Young Australians Not in Employment, Education or Training

The share of youth neither in employment nor in education or training—known as NEET—constitutes a relatively new indicator that has been gaining attention in the policy debate. From a little-known concept in early 2000s, the indicator now prominently features as a sole target in the ongoing discussions of the upcoming United Nation’s Sustainable Development Goals, which vows to “by 2020 substantially reduce the proportion of youth not in employment, education or training”.<sup>39</sup>

NEET rates are an important measure of a detached youth cohort at risk of becoming alienated from social and professional lives, and possibly heading for a lifetime welfare dependence trap. As another measurement of jobless youth, the NEET concept can better capture not just those looking for a job (unemployed NEETs), but also those completely discouraged from participating in the workforce (inactive NEETs)—**Box 3** explores further the many nuances regarding unemployed youth.

From a gender perspective, young women tend to present higher NEET rates, with the OECD average gender gap at five percentage points.<sup>40</sup> Among many potential drivers for this gender gap, single parenthood constitutes an important factor—especially among inactive NEETs (i.e. completely detached from the labour force)—as in most cases it is the single mother who bears the burden of raising a child.<sup>41</sup>

Since the GFC, the overall number of NEETs in Australia has increased by more than 21%, from a 12-month average of 299,000 at the end of 2008 to 360,000 in September 2015 (**Figure 10**).<sup>42</sup> Whereas young NEET females outnumbered males by a third in 2008 (171,000 female NEETs vs. 128,000 Male NEETs), NEET levels are currently very similar in gender terms (186,000 female NEETs vs. 174,000 Male NEETs) due to a strong surge in unemployed NEET males in the past seven years.

### Box 3: Fifty Shades of Youth Unemployment

Not everyone who is out of work is technically classified as unemployed. The International Labour Organisation (ILO)—a United Nations agency specialising in labour market matters—prescribes a three-criteria checklist for a person to be considered unemployed. That is, the person needs to be: i) *without work* (i.e. not in paid employment or self-employment); ii) *currently available for work*; and, iii) *seeking work*.<sup>43</sup>

Following this methodology, the Australian Bureau of Statistics identifies unemployed youth as the set of people aged 15 to 24 years, not employed in the reference week, and either actively looking for work (and available to work in the reference week) or waiting to start a new job.<sup>44</sup>

The most traditional measurement is the youth unemployment rate, which is defined as the 15-to-24-year-old unemployed percentage of the labour force for that age group. That is,

$$\text{Youth Unemployment Rate} = \frac{\text{Young unemployed people}}{\text{Young labour force}}$$

However, the youth unemployment rate ignores a considerable portion of those who would like to—or could—be working, but is discouraged from even seeking work for a range of reasons. That is, young people at working age who are outside the labour force (**Figure 9**). In addition, unemployment figures also exclude those who are working only minimal hours, but are counted as employed. While some jobless people choose to devote their time mainly investing in human capital (i.e. studying or training); others are completely ignoring the opportunity to either work and/or study. The latter constitutes a worrying subset of young people not captured by youth unemployment statistics. Hence, a careful analysis of the issue should also include measurements of young people not in education, employment or training (NEETs). In particular, it is important to separate the active NEETs (unemployed youth not studying/training) and inactive NEETs (completely outside the labour market and education/training).<sup>45</sup>

Research also highlights the perils of focusing too much on the youth unemployment rate, at the risk of missing the bigger picture.<sup>46</sup> Youth unemployment rates might overstate the unemployment problem, since the young labour force—the denominator of the youth unemployment rate—is severely constrained by the large proportion of youth enrolled at education/training and not interested in working.<sup>47</sup> In this respect, it is important to add other statistics to the analysis menu. The first is the youth unemployment-to-population ratio, or most commonly called the youth unemployment ratio, which considers the number of jobless youth as a percentage of the respective young population.

$$\text{Youth Unemployment Ratio} = \frac{\text{Young unemployed people}}{\text{Young population}}$$

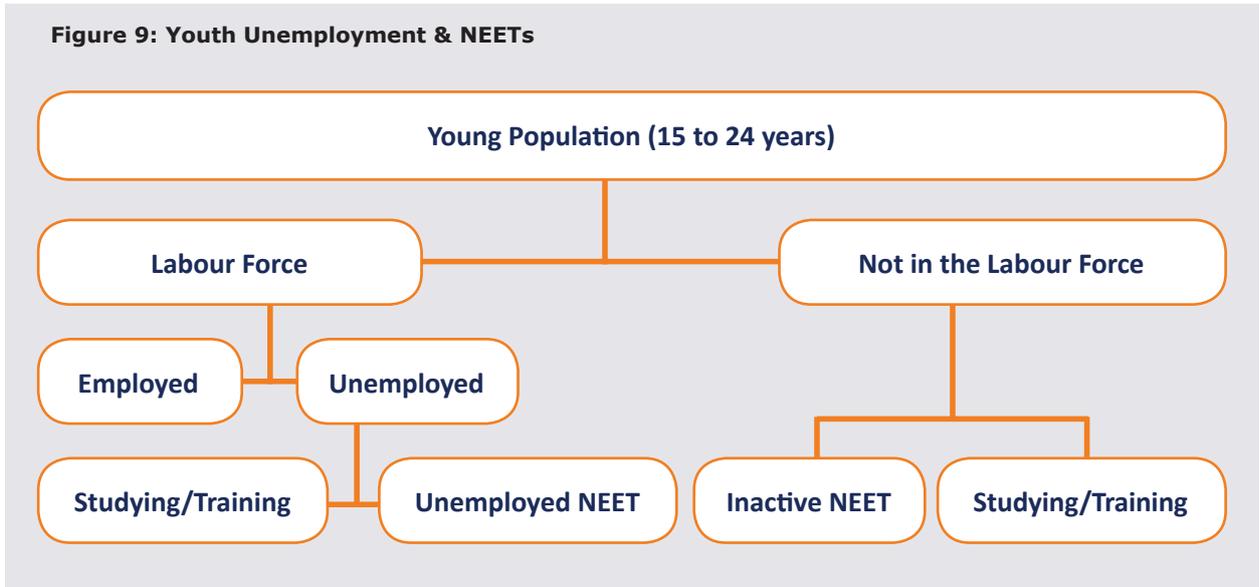
Measurements regarding NEETs (including the distinction between unemployed and inactive NEETs) can help devise targeted policies, since the youth unemployment rate (or ratio) does not reveal potential problems with those who are not in education, employment or training—particularly questions of how many are outside the labour force, and why.

$$\text{NEET rate} = \frac{\text{Unemployed NEETs} + \text{Inactive NEETs}}{\text{Young population}}$$

There are many other measurements that assist with the analysis of youth unemployment. For instance, the ratio of youth-to-adult unemployment rates help identify any deviations from both historical and cross-country perspectives; long-term youth unemployment, which measures those at risk of being completely alienated to lifetime welfare dependence; age subsets (15-to-19 / 20-to-24 years old); gender and regional differences; and so on.

The important message is that there is no single statistic able to fully inform about the youth unemployment topic. The issue comes in many shades, shapes and sizes, with no black-and-white, one-size-fits-all picture.

**Figure 9: Youth Unemployment & NEETs**

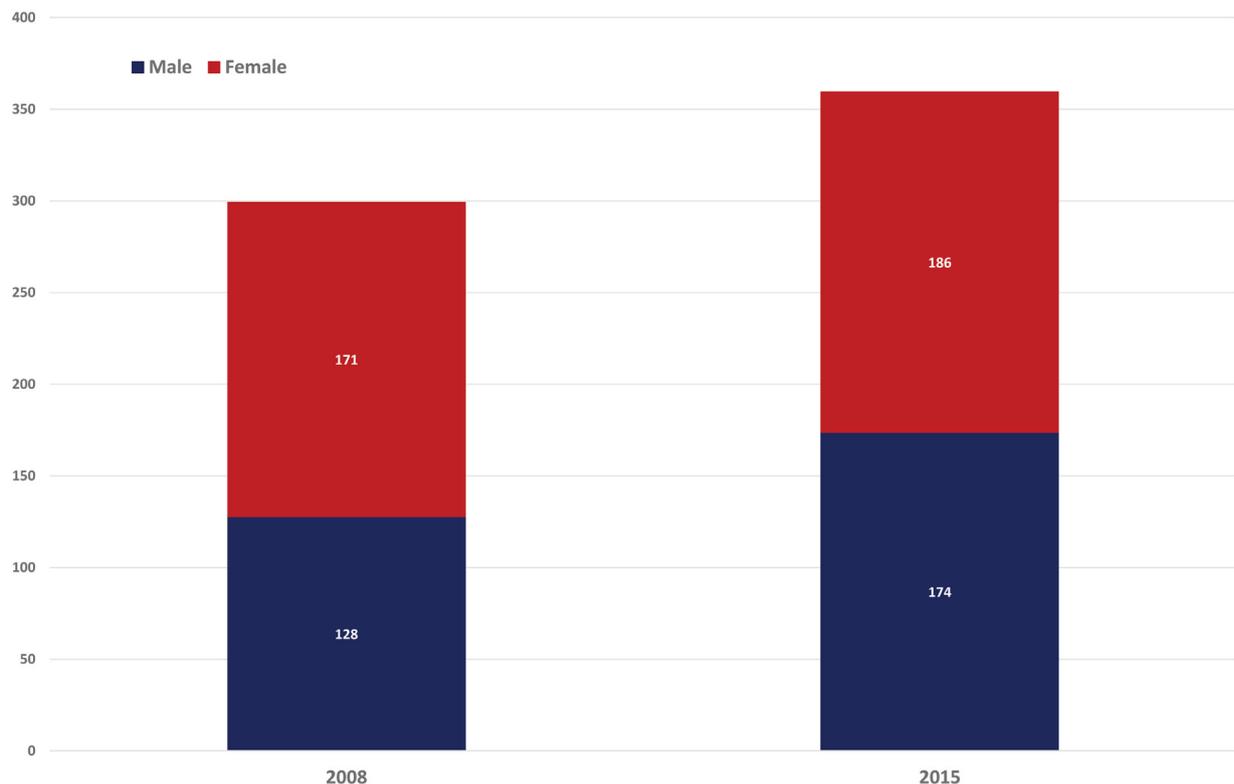


The NEET concept sparks a wide range of issues—such as school drop-outs, unemployment or simply work discouragement—that might lead to social alienation among youth.<sup>48</sup> High NEET rates can be a result of increasing difficulties in finding a job, disengagement with educational studies at a high school or tertiary levels, or lack of affordable vocational training—or most likely a combination of all these factors.<sup>49</sup> In this context, it is useful to analyse the NEET contingent not just by gender, but also by differentiating among teenagers and early 20s, as different dynamics underpin each cohort. Although internationally Australia has performed well in maintaining relatively low levels

of NEETs,<sup>50</sup> there is still much room for concern. In particular, the Australian NEET rates for the 20–24 age group have considerably increased since the GFC, as opposed to the significant improvement among the teenager rates.

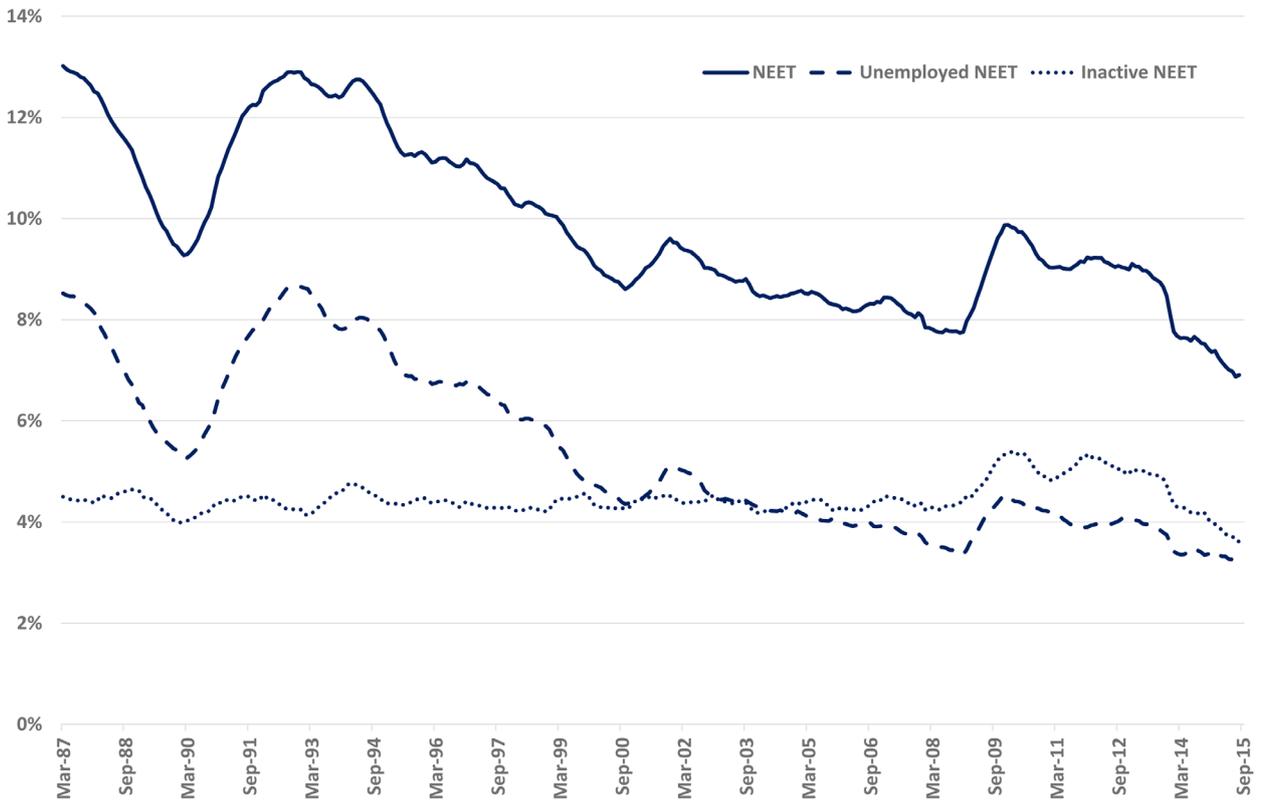
As **Figure 11** shows, the 12-month average proportion of Australians aged between 15–19 years old who are not in employment, education or training has consistently decreased since mid-1990s, despite short hikes after economic slowdowns in the early 2000s (i.e. the dot-com crisis) and the GFC. Currently at 6.9%, this is the lowest rate on record.

**Figure 10: Australian NEETs by gender ('000s)**



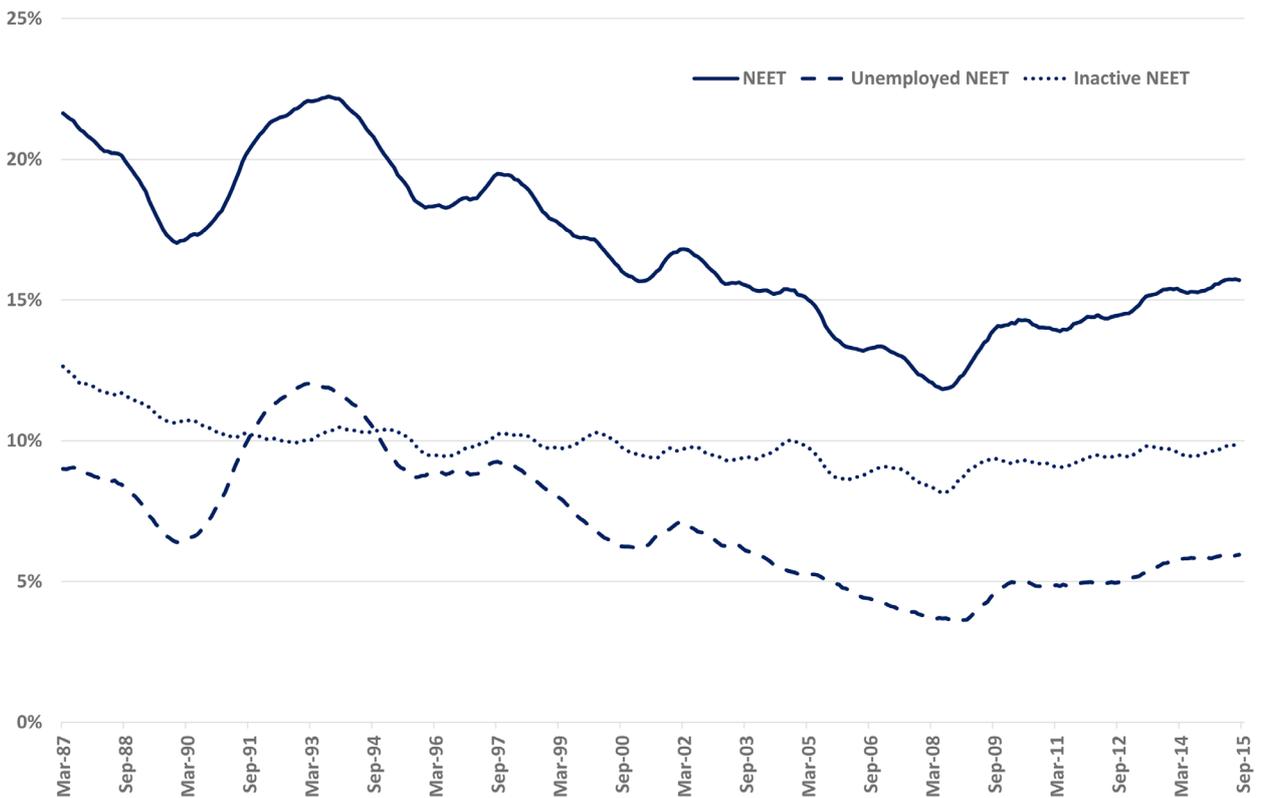
**Source:** ABS, Labour Force, Australia; Author’s calculation; 12-month average.

**Figure 11: Teenager NEET rates in Australia**



**Source:** ABS, Labour Force, Australia; Author's calculation; 12-month average; Percentage of all Australian teenagers aged 15 to 19.

**Figure 12: Early 20s NEET rates in Australia**



**Source:** ABS, Labour Force, Australia; Author's calculation; 12-month average; Percentage of all young Australians aged 20 to 24.

The fact that teenage unemployment rates have gone up since the GFC (predominantly pushed by those looking for part-time jobs) while teenage unemployed NEET rates decreased suggests that most of the new contingent of jobseekers aged 15 to 19 are at least enrolled in full-time education or training. This is a welcome impact of the national effort to increase Year-12 attainment,<sup>51</sup> although doubts remain about the effectiveness of the approach for learning outcomes.<sup>52</sup> Another important inference from the data regards the sharp decrease in the teenage inactive NEET rates since the 5.4% peak in mid-2010 down to the current 3.6% (the lowest rate on record), possibly as a result of 'earn or learn' activation policies in recent years.<sup>53</sup>

On the other hand, **Figure 12** presents the evolution of early 20s NEET rates in Australia since the end of the 1980s. Conversely to the teenager rates, the number of young Australians aged 20–24 not in employment or

any form of full-time education has been in an upward trend since the GFC. The early 20s NEET rates are at the highest peak since 2003, currently at 15.7% (that is, 5.9% unemployed plus 9.7% inactive). Such an overall increase in early 20s NEETs is explained by an escalation in the unemployed numbers (in particular by those looking for full-time jobs) as well as by the complete alienation of inactive youth in this age bracket who are outside the labour force and not enrolled in any full-time education or training program. The latest data on unemployed NEETs points to more than 98,000 early 20s looking for a job—nine out of ten aiming at full-time positions—which is almost double the amount of unemployed youth in the same situation back in 2008. Moreover, there are currently around 160,000 inactive NEETs aged 20–24 years old in comparison to the 132,000 at the onset of the GFC. This indicates that more work needs to be done to activate this portion of early 20s cohort back to the labour force or, where appropriate, back to the classroom.

## Disparities among Australian Regions

Australia is a continental country with very different climates, ecosystems and indeed economies. Hence, it is natural for its six states and two major territories to experience quite different levels of youth unemployment rates, currently ranging from a 12-month average of 16.2% in Tasmania to 10.1% in Northern Territory (**Figure 13**). Some large discrepancies are also found across greater metropolitan areas, with Hobart, Melbourne and Adelaide leading the highest youth jobless rates among Australian capital cities (**Figure 14**).

In **Tasmania**, youth unemployment is a widespread phenomenon, with rates almost doubling since the GFC. Current youth unemployment rates in the state are leading the ranking across the nation, from 14.9% in Hobart to 26.0% (Australia's highest 12-month average) in the south east of the State.

**South Australia**, which was the state with the highest youth jobless rates in 2008, now appears in second place with 15.4%. Despite all regional areas currently presenting double-digit youth unemployment rates, there is much heterogeneity in the state, ranging from 12.7% in West Adelaide to 19.2% in the Barossa region.

Rates in **Victoria** are also alarming with average unemployment rates for youth between 15 and 24 years old surging from 9.4% in 2008 to 14.9% in 2015—which is in line with rates in greater Melbourne area. In the rest of the state, Geelong and Hume are the biggest concerns, with current youth unemployment rates above 18%.

**Queensland** comes in fourth place, with youth unemployment rates at 13.9% in 2015, which is still slightly above the national average. In greater Brisbane—as most of the other state areas—the GFC hit youth hard, with jobless rates in the capital jumping from 7.0% in 2008 to just over 12.5% at the present.

In regional areas, Wide Bay, Townsville and Cairns are among the highest youth unemployment areas in Australia, as one in five youth struggle to find a job.

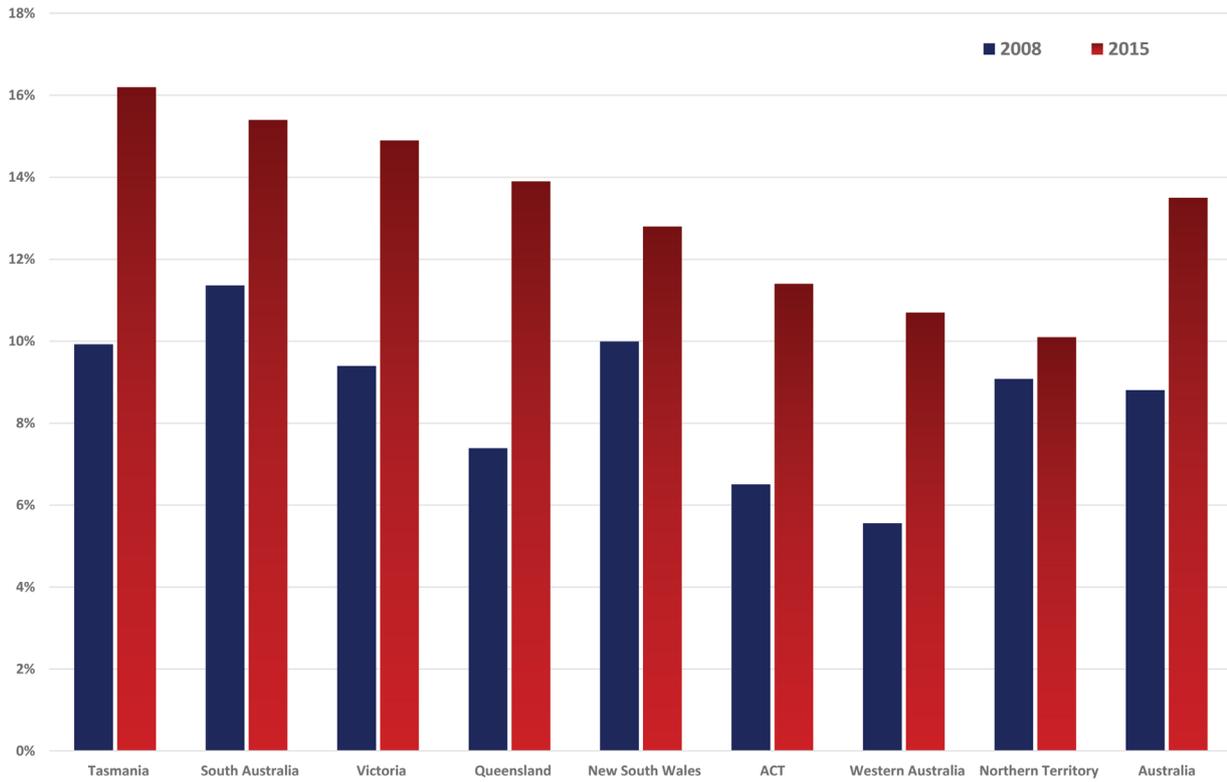
Rates in **New South Wales** have not seen much deterioration in the past seven-year cycle, from 10.0% in 2008 to 12.8% in 2015—which is below the national average. The same could be said about the greater Sydney area, although at some points such as the Central Coast, Blacktown and the Inner South West, current youth unemployment rates are over 15%. A particular concern in the state is the Hunter Valley region, where youth jobless rates have tripled in the period, from 6.7% in 2008 to 21.3% in 2015.

**Western Australia** is the best-performing state, currently at 10.7%. Yet the state was not able to go through the past years unscathed as commodity prices plummeted and the mining boom fades—echoed in the state's youth unemployment rate rise from 2008's 5.6%.

Among the two major territories, although rates in the **Northern Territory** have slightly increased since 2008, Darwin has been the only Australian capital city to see its youth unemployment decrease in the period, and has become the best performing capital with current youth unemployment rate at 8.3%—as opposed to the second highest rate among capital cities before the GFC. In Canberra, youth unemployment is at its highest levels since 2002, at 11.4%. In particular, rates have increased quite strongly since the beginning of 2013.

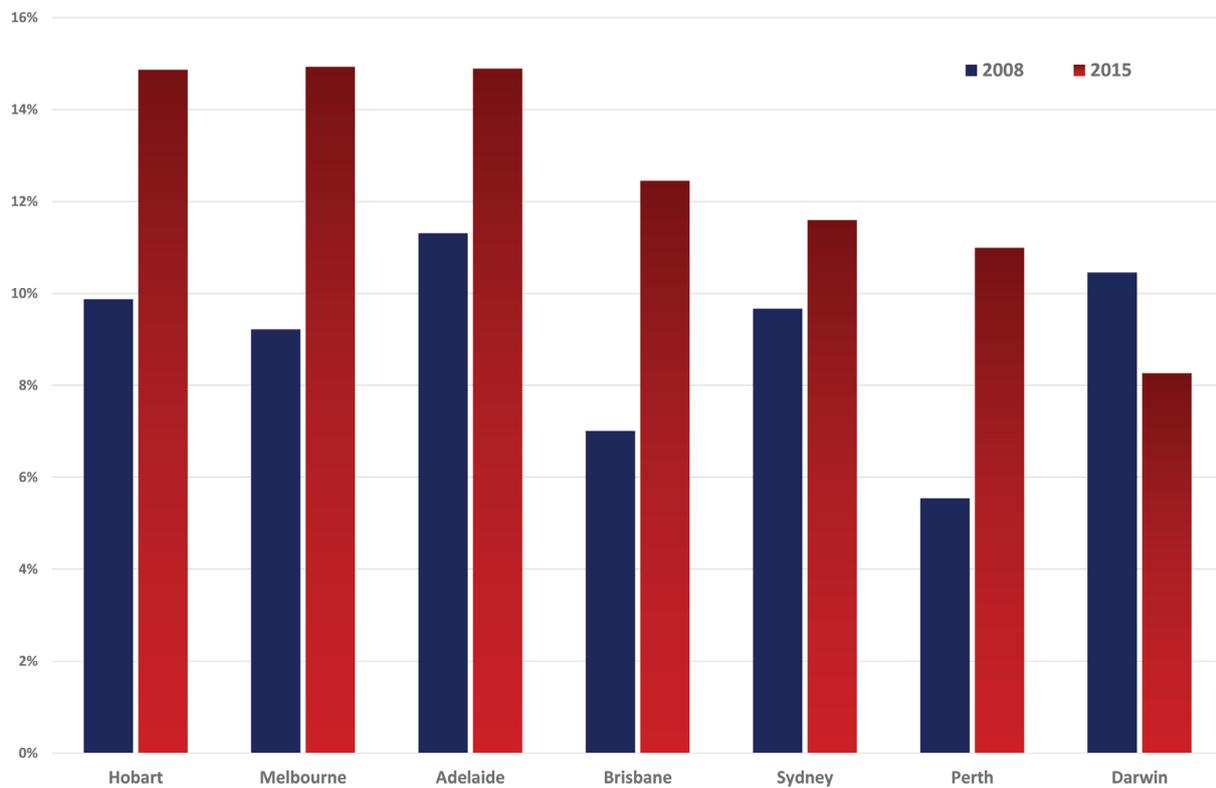
Disparate youth unemployment figures throughout the nation are just another indication of how heterogeneous economic conditions currently are in Australia.<sup>54</sup> As shall be discussed later, such a continental and diverse economy demands adjustments to the national workplace relations framework, which currently imposes identical pay floors no matter the specificities and regional living costs.

**Figure 13: Youth Unemployment across Australian States and Territories**



**Source:** ABS, Labour Force, Australia; Author's calculation; 12-month average.

**Figure 14: Youth Unemployment across Australian Metropolitan Areas**



**Source:** ABS, Labour Force, Australia; Author's calculation; 12-month average.



## A Global Issue

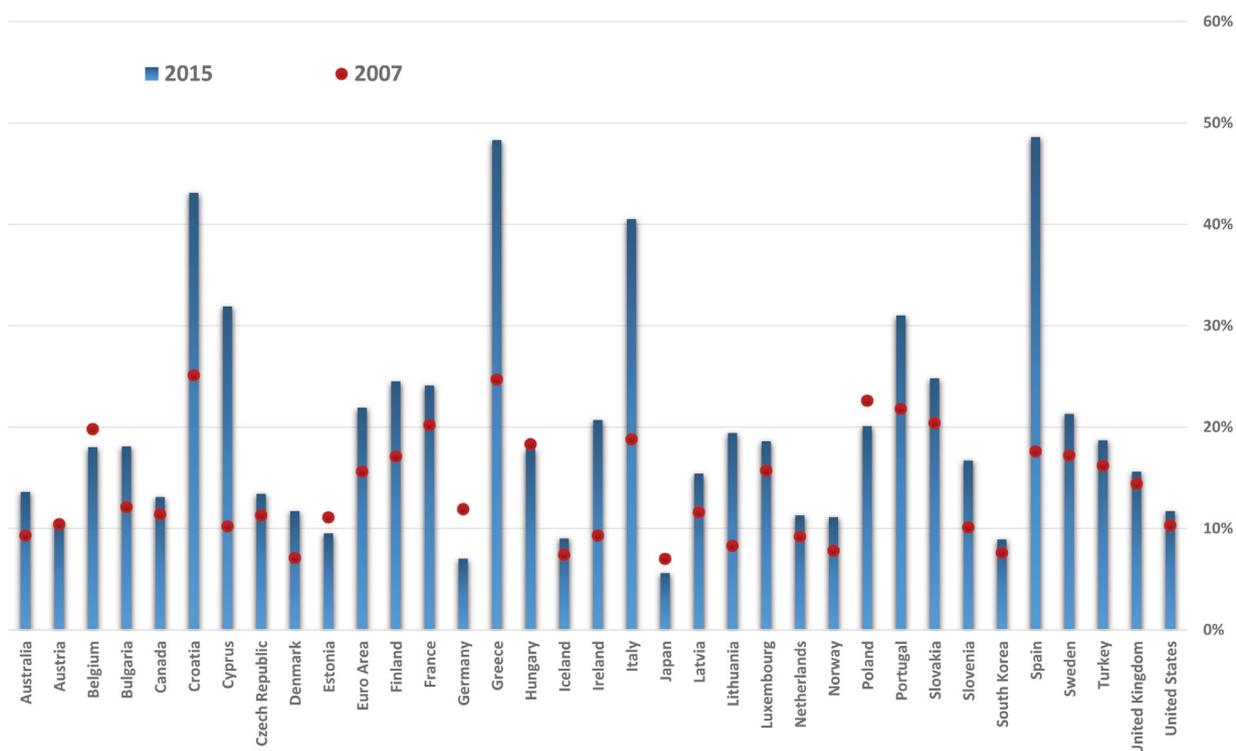
Youth unemployment is a global issue, with varying levels of severity across countries. The International Labour Organisation (ILO) recently estimated 75 million young people worldwide are out of work,<sup>55</sup> launching a global 'call for action' agenda, creating an open forum for national governments to discuss and share best practices.<sup>56</sup> Most importantly, it recognises that there is no one-size-fits-all solution, given the diverse regional backgrounds to the issue.

A global jobless youth cohort is not a new problem, but numbers have steeply increased with an extra ten million jobless young people added since the onset of the GFC.<sup>57</sup> It is little surprise that G20 leaders made youth employment a global priority in the 2013 Saint Petersburg Summit.<sup>58</sup> **Figure 15** depicts youth unemployment rates for a wide range of selected countries in 2007 and 2015. With few exceptions, most notably Germany, Poland and Japan, countries

have experienced a severe deterioration. In particular, Europe is still struggling to bring its unemployment rate back to pre-crisis levels, down from a peak in early 2013—when it reached 24.6%—to the current 22.3%, which is practically a third higher than the 2007's level. The worst cases can be found in Spain, Croatia, Cyprus, Greece and Italy, which are facing extreme risks of an entire cohort of unemployed young people.

Even though most of the recent escalation is due to lacklustre global economic growth,<sup>59</sup> all of these countries already started at very high levels of youth unemployment even before the GFC struck. On the other hand, the United States and the United Kingdom have both managed to pull down their peak rates after the GFC—of 19.5% and 22.3%, respectively—to original pre-crisis levels, mainly due to their rebounding economies.<sup>60</sup>

**Figure 15: Youth Unemployment Rates in selected countries**



**Source:** Trading Economics Database. Values for 2015 are based on the latest data available as of October 2015.

### Continuing evidence of GFC impact

There are other labour market measures to corroborate the view that the current young cohort was severely hit by the GFC, especially in developed countries. For instance, rising NEET rates in OECD nations—from 14% in 2007 to 16% in 2012—mostly reflect higher unemployment among youth, as the inactive NEET rates remained steady at 9% over the same period.<sup>61</sup> Such evidence is important to designing policy; trying to identify different measures to lift youth employability on the demand side, and on the supply side to encourage at-risk youth who are completely shut out of the labour force.

**Table 1** summarises a list of other annualised labour market indicators for youth in the OECD and Australia, which indicate a significant deterioration in youth

access to employment throughout the developed world from 2007–2014. The labour market participation among young people has fallen in nearly all OECD countries, with the average rates falling from 49.2% to 47.2%. In Australia—with a strong tradition of part-time jobs among the youth attending school/tertiary institutions—participation rates have also displayed the same trend, winding back from 70.8% in 2007 to 66.6% in 2014. The combined effect of rising unemployment and declining labour force participation indicates that, first and foremost, discouraged youth are struggling to find work. Not surprisingly, the employment to population ratio has dropped in the short span since the GFC, from 43.2% to 40.1% in the OECD and from 64.1% to 57.7% in Australia.

**Table 1: Labour Market Indicators for Youth in OECD and Australia**

	Labour Force Participation Rate		Employment to Population Ratio		Unemployment Rate	
	2007	2014	2007	2014	2007	2014
OECD	49.2%	47.2%	43.2%	40.1%	12.0%	15.0%
Australia	70.8%	66.6%	64.1%	57.7%	9.4%	13.3%

**Source:** OECD database.



## The Scarring Effects

In addition to the short-term hardships associated with a lack of a reliable source of income, the damaging effects of youth unemployment can persist into adulthood, with different intensity and longevity depending on the length of the unemployment period and on individual conditions such as education levels and socioeconomic background.<sup>62</sup> There is no minimal or safe threshold regarding the length of early unemployment experience. As a general rule, the longer a person is unemployed, the longer the perverse effects are likely to last.<sup>63</sup> Such negative long-term consequences of early jobless spells are commonly referred to in the literature as the *scarring* effects.

Empirical studies provide strong evidence of the lasting impact of being unemployed. In technical terms, it is referred to as state dependence, i.e. being jobless today increases the chance of being jobless in the future.<sup>64</sup> For instance, Mroz and Savage (2006) show that early youth unemployment affects both future job displacement and earnings for up to 10 years in the US.<sup>65</sup> A similar British study found wage penalties of 9% to 21%, lasting up to 20 years later.<sup>66</sup> Accordingly, an analysis of the Household, Income and Labour Dynamics in Australia (HILDA) survey suggests the likelihood of being unemployed later in life is three times as high if one experienced unemployment spells in their youth, which might give rise to a welfare dependence trap.<sup>67</sup>

There are many forces behind the scarring effects of unemployment, with self-reinforcing features playing in extended reverse causality cycles. For instance, unemployment spells can present a direct threat of poverty, potentially leading to social exclusion—which further impacts the future likelihood of being unemployed. Such a feature is more specifically damaging to youth as there is no solid previous working experience to rely upon in the immediate future. Other potential impacts include the consequences on health. Disengaged youth such as NEETs tend to be much more affected by health problems than other youth. According to the OECD estimates, the share of young individuals with poor health status in Australia almost doubles if one is not in employment, study or training—a typical case of reverse feedback between health problems and social exclusion.<sup>68</sup>

The impact on mental health due to unemployment is also documented. Knabe and Ratzel (2011), for example, suggest that past unemployment not only ‘scars’ but also ‘scares’, by reducing a person’s current life satisfaction even after the person has become

reemployed.<sup>69</sup> Other studies also point to further mental health issues associated with youth unemployment—with causation going both ways; unemployment may lead to drug abuse, domestic violence and crime involvement, and *vice-versa*.<sup>70</sup>

Other sources of trouble are the deterioration of skills and the forgone work experience, which also contribute to further alienate the possibility of re-entering the working force. These effects can be felt even more strongly during long spells of unemployment, as all reasons mentioned above are intensified as the period of unemployment lengthens. In particular, there is the tendency of employers to heavily discriminate against those with long spells of unemployment.<sup>71</sup>

In many cases, poor signalling rather than human capital depreciation itself is the main reason for the enduring difficulties in finding a job.<sup>72</sup> Since skills are not easily detectable, employers generally use other information, such as educational attainment and work experience history, as signalling proxies.<sup>73</sup> In a recent US study, researchers have fictionally created false jobseekers to apply for several vacancies in different industries, where the main difference in these fabricated applicants was their unemployment duration periods. Results show that applicants indicating six or more months of unemployment were rarely contacted for an interview.<sup>74</sup> The jobless youth facing long-term unemployment therefore are quite often put at a severe disadvantage in the job market.

Furthermore, although evidence shows that unskilled youth are especially hurt by these factors,<sup>75</sup> recent studies point to the increasing share of young graduates hard hit by economic downturns.<sup>76</sup> According to OECD estimates, the share of highly educated youth among NEETs is low, but has risen since the GFC—with the share of highly educated among NEETs in Australia rising from 14% to 18% since 2007.<sup>77</sup> In addition, domestic surveys among graduates in Australia point to a considerable reduction of bachelor degree graduates in full-time work four months after completing their degree—the worst since the 1992–93 recession.<sup>78</sup>

The bottom line is that youth unemployment is a serious problem that goes beyond obvious financial hardship. The scarring effects of youth disengagement are proven to outlast the initial inactivity period, eroding future career prospects and having implications on health and other social issues.<sup>79</sup> Hence, minimising youth unemployment rates today will let us reap compounding beneficial effects for many years to come.

# Employment

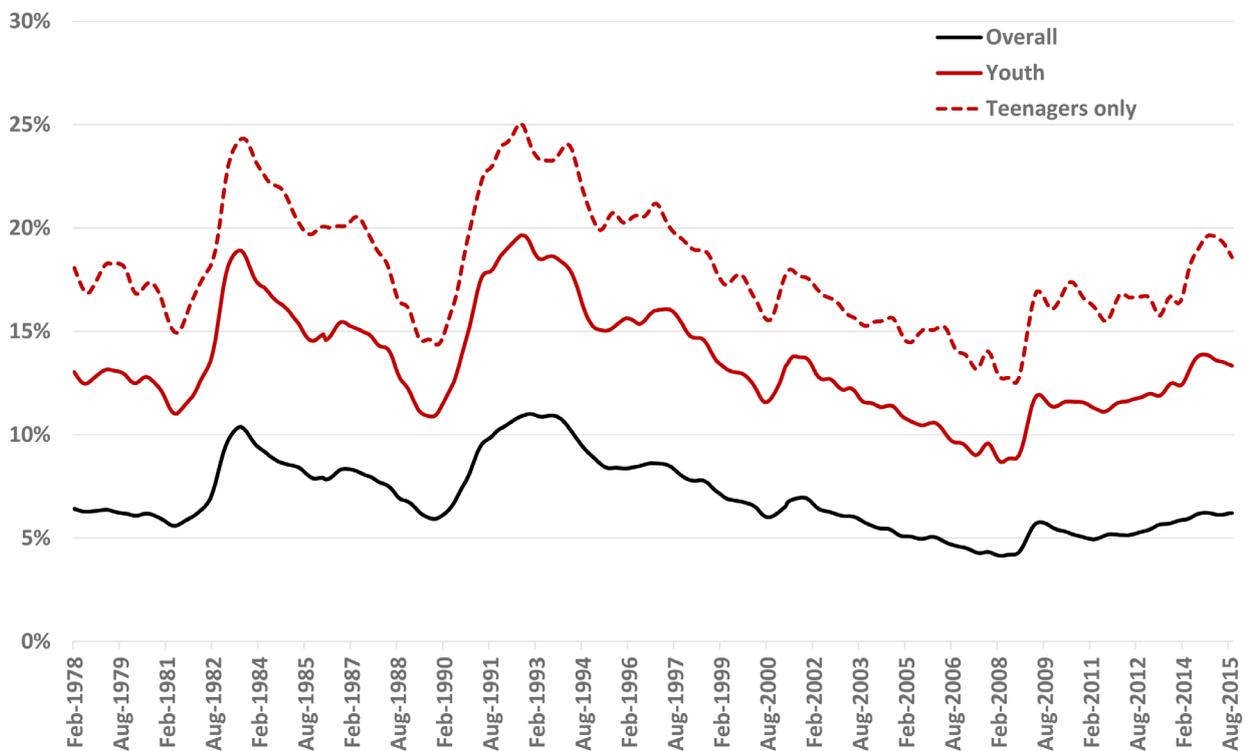
## The Root Causes and Policy Recommendations

### Lack of Economic Growth

Youth unemployment is a multifaceted issue underpinned by a broad web of causes. But lack of economic growth can be singled out as the most imperative force behind large swings in the jobless youth contingent.<sup>80</sup> A low skilled, inexperienced young workforce with great emphasis on part-time and casual jobs is particularly vulnerable to adverse economic conditions in the job market,<sup>81</sup> which leads to youth unemployment being not just higher than overall employment but also a super-cyclical variable (i.e. highly responsive to fluctuations in the economic cycle).<sup>82</sup>

**Figure 16** shows the ABS trend data on unemployment rates for overall population, youth (aged 15–24 years) and its subset of teenagers (15–19). All three unemployment rates seem to move in tandem, with close relationship to overall economic activity. In addition, the super-cyclical aspect of youth unemployment is also captured; i.e. the younger the cohort, the higher the level and the larger the swing in the respective unemployment rate.

**Figure 16: Unemployment rates (1978-2015)**



**Source:** ABS, Labour Force, Australia, trend data.

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## Recommendation 1: Implement structural reforms aiming to lift economic growth

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The synchronised movements between the three jobless data series is crucial to understanding two key facts about youth unemployment in Australia. First, there is no isolated youth unemployment issue; in fact there is a worsening of unemployment figures, with the most vulnerable in our society—such as youth—being hit harder. Second, the most effective way to tackle youth unemployment—and for that matter, reduce all levels of unemployment—is by growing the economy. The unprecedented downward trend in unemployment from 2001 until 2008, with all three series reaching their lowest rates on record on the eve of the GFC, is best explained by the roaring Australian economy at the height of the mining boom years. Conversely, the initial spike in the unemployment rates from the final quarter of 2008 until the third quarter of 2009, followed by an upward trend in all three series, can best be explained by the lingering effects of the GFC and the sharp fall in Australia's terms of trade (i.e. commodity export prices) especially in the last two years.

In short, growth matters.

This leads to the **Recommendation 1** of this report: the implementation of much-needed structural reforms aiming to unleash our economic growth potential. If Australia is serious about addressing the recent escalation in youth unemployment, it must for instance legislate towards a more efficient tax system, dynamic competitive markets and job-creation oriented workplace relations.<sup>83</sup>

The relationship between economic growth and unemployment is intuitively straightforward. A higher level of production, other things being equal, requires a larger pool of workers. Of course, such a relationship may be affected by levels of productivity, expectations on economic outlook, investments, and so on. Yet there is nothing more effective to job creation than increased output itself.<sup>84</sup>

Okun's Law states that positive changes in output growth lead to reductions in unemployment.<sup>85</sup> The robustness of Okun's law has been confirmed many times, although measurements can significantly vary among countries and sample periods.<sup>86</sup>

Young jobseekers are hit especially hard by cyclical changes in economic growth. Such super-cyclicality is clearly captured in the data, with youth unemployment being more responsive than the overall jobless

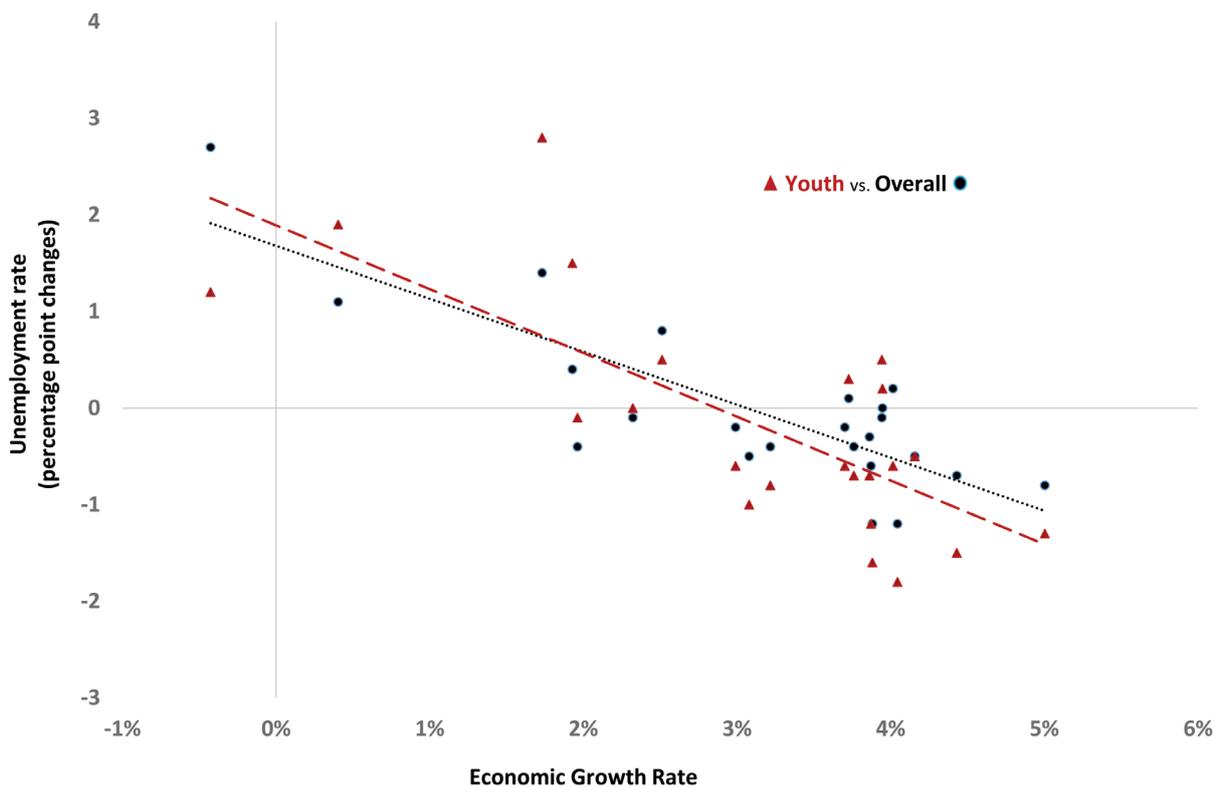
rates to changes in output production throughout the business cycle. According to an OECD study, one percentage change in the growth rate of potential GDP leads to a change of 1.4 percentage points in youth unemployment—an impact that is more than double the 0.65 percentage point change in adult unemployment.<sup>87</sup> Using only the Australian data, another study calculated that whereas the impact on adult unemployment is in line with the OECD average, the super-cyclicality of youth unemployment is even more pronounced, leading to a 2 percentage point change in youth unemployment for every percentage change in potential output.<sup>88</sup>

To better capture the relationship between job creation and economic growth, **Figure 17** shows a quick visual representation of the forces behind Okun's law in Australia for an annual sample from 1991–2013 for both overall and youth unemployment rates. This plots Australia's annual economic growth rate (i.e. real percentage change in GDP) on the horizontal axis and annual percentage point changes in the unemployment rate on the vertical axis.

A few conclusions can be inferred from each cluster of points representing youth and overall unemployment. First, as expected, both datasets indicate a negative relationship between economic activity and the respective jobless group: higher or lower output growth is associated respectively with decreasing or increasing unemployment rates. Additionally, a trend line is drawn for each group representing the best fit for the respective cluster of points.<sup>89</sup> The dash line refers to the youth unemployment dataset, whereas the dotted line shows the overall unemployment. This figure shows output changes have a higher impact on the youth unemployment rate, confirming the super-cyclicality nature in the OECD study cited above.

Moreover, both trend lines cross the horizontal axis at reasonable output growth rates, around 3%, which might constitute a silver lining for policymaking. While macroeconomic performance is the key determinant of unemployment, past data shows that reducing the problem does not require unreasonable levels of output growth. In short, the youth unemployment solution requires economic growth that is within our reach—if we manage to advance structural reforms conducive to higher productivity and competitiveness.

**Figure 17: Economic growth and unemployment in Australia (1991–2013)**



**Source:** The World Bank Data; Author’s Calculation.

### Regulatory Constraints

Some onerous, counterproductive regulatory constraints can act as serious obstructions to job creation,<sup>90</sup> especially for the low-skilled, inexperienced part of the labour force—and not surprisingly, young jobseekers are among the most affected. There are two avenues through which misguided regulation can undermine labour demand—and hence are often referred to as demand-side barriers to job creation. First, regulation can impose pay floors (e.g. national minimum wages and other forms of Modern Awards rates) that effectively price out low-skilled, inexperienced jobseekers—see **Box 4** on the Modern Awards’ mandated penalty rates, for instance.<sup>91</sup> Second, legal instructions can unnecessarily increase indirect labour costs, which again can reduce the overall demand for labour, especially among the most vulnerable. For instance, one could argue that excessive pay floors, minimum hour requirements, disproportionate lay-off protections (including high severance payments), not to mention burdensome payroll taxes, can all contribute to increased unemployment levels.<sup>92</sup>

In the case of Australia’s industrial relation institutions, there is an ongoing debate on whether workplace regulations are conducive to job creation and labour utilisation.<sup>93</sup> This report sides with the view that there is much room for improvement when it comes to

reducing demand-side barriers to employment, which is outlined in previous work published by the Centre for Independent Studies.<sup>94</sup> Australia would benefit from the adoption of a more flexible workplace relations framework that values freedom to contract in the mostly competitive Australian labour market.

Recommendations 2 and 3 are aimed at reducing demand-side barriers to job creation in Australia with the introduction of local and long-term unemployment discounts to nationally regulated pay floors (e.g. minimum wages, federal junior pay rates, Modern Awards wages including penalty rates) to prevent low-skilled, inexperienced jobseekers—in particular young ones—from being summarily priced out of the labour market.

There is much debate on the effects of minimum wages on the availability of low-skilled jobs.<sup>95</sup> On the one hand, it is safe to state most in the academic debate—even those in favour of minimum pay floors—agree that, at high levels, pay floors can be detrimental to job creation, particularly making it difficult for young jobseekers lacking job experience and working skills.<sup>96</sup> According to the OECD, “*too high a minimum wage can reduce employment opportunities for vulnerable groups, notably low-skilled youth*”.<sup>97</sup>

#### Box 4: Penalty rates are penalising young jobseekers

The penalty rate system in Australia, introduced in 1947, was designed to compensate employees for working unsociable hours, i.e. outside the conventional 9-to-5 working day. However in contemporary times, the concept of conventional working hours is outdated.

Further, penalty rates not only burden employers' costs (with the undesirable consequence of reduced hiring capacity), but also potentially penalise young and unskilled jobseekers.<sup>98</sup> The current system benefits the lucky few employed on weekends and other nonconventional shifts at the expense of severely undermining the chances of low-skilled jobseekers i.e. the most vulnerable in our society getting a foothold in the workforce.

For young students, weekend and night shifts are predominantly the only feasible shifts that do not clash with class times. For someone who is not in employment, education or training, and probably struggling to make ends meet, a Sunday work shift cannot be deemed a plausible inconvenience.

For instance, under our current penalty rate regime, even after discounting for junior pay rates, the minimum casual pay for a 20-year-old in the lowest employee level in the fast food industry is \$29/hr on a Sunday (or a substantial \$46/hr on public holidays). Similar pay levels (if not higher) can also be found in many other industries that are a gateway for young job starters.

Such excessive price floors certainly do not help the youth unemployment cause. On the contrary, penalty rates in Australia end up penalising those who most need assistance to enter the labour market.

**Source:** Carvalho (2015), "Young jobseekers are suffering the ultimate penalty", Business Spectator, May 11<sup>th</sup>.

However, there is a great deal of contention about what exactly constitutes high minimum pay levels.<sup>99</sup>

Australian minimum wages are some of the highest among OECD members, only behind Luxemburg, Netherlands and Belgium in purchasing power.<sup>100</sup> Even taking into account the overall earnings of full-time workers, Australia's national minimum to median wage ratio, at 54%, is still high for OECD standards.<sup>101</sup> And much higher pay floor rates are enshrined in Australia's Modern Awards system.<sup>102</sup>

The concern is that high minimum wages can significantly affect the employability of the most vulnerable youth, even when considering the age discount factors of the minimum wage system, namely the Federal Junior Pay rates. Such junior pay rates—often superseded with much higher pay dictated by Australia's Modern Awards<sup>103</sup>—are limited to young people aged under 21, with very low discounting rates for those approaching the age limit. For instance, a 20-year-old under a federal junior pay rate is only a few percentage points below the adult national minimum wage (**Table 2**).

**Table 2: Federal Junior Pay Rates**

Age	Share of Adult national minimum wage	Value per hour	Amount per 38 hour working week
Under 16	36.8%	\$6.36	\$241.74
16	47.3%	\$8.18	\$310.71
17	57.8%	\$9.99	\$379.69
18	68.3%	\$11.81	\$448.66
19	82.5%	\$14.26	\$541.94
20	97.7%	\$16.89	\$641.79
21+	100.0%	\$17.29	\$657.02

**Source:** Annual Wage Review 2014-15—National Minimum Wage Order 2015 FWC. Values as at September 2015.

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## Recommendation 2:

### Introduce local discounts to nationally regulated pay floors

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Even more concerning is the fact that none of the components of the nationally regulated pay floors consistently takes into account disparate living costs and economic conditions observed across continental Australia—which, as outlined above, features very different labour market conditions including diverse youth unemployment rates. A more sensible approach would be to allow for pay floor discounts in local disadvantaged areas, whenever high minimum pay levels might constitute a demand-side barrier to youth job creation. For instance, what might be considered a fair (and affordable) pay in major Australian cities such as Sydney, Brisbane and Perth might be economically prohibitive—and indeed unfair to those left without a job as a consequence—in inner Tasmania or regional Queensland.

Accordingly, **Recommendation 2** calls for the introduction of local discounts to nationally regulated pay floors.

Diverse nominal local pay floors do not necessarily translate into great disparities of minimum wages' purchasing power (i.e. ability to consume), as cost of living (e.g. housing, transport, dining out) may significantly vary between localities. That is, different nominal local pay floors do not necessarily disagree with the long established principle of 'equal remuneration for work of equal or comparable value'. As highlighted by the recent Productivity Commission draft report on workplace relations, "*jobs yielding the same monetary benefits may provide quite different non-monetary benefits for workers, and the value (in terms of the wellbeing gained) of a particular quantum of money is likely to vary from one person to the next, and from one place to the next, given differences in preferences and living costs. Equalising monetary remuneration will thus not equalise the benefits people gain from work 'of equal value', and in some cases may inhibit efficient matching of workers with jobs.*"<sup>104</sup>

Indeed, a more flexible approach with respect to local pay floors can prove to be a make-or-break factor in reversing high youth unemployment rates in some Australian regions, where high regulated wages might prevent business from hiring more staff and, consequently, jobseekers from getting a fair chance to find employment.<sup>105</sup>

From an international perspective, countries with large regional economic discrepancies such as Canada, Russia, India, Brazil, Indonesia, Japan, Mexico and United States already concede different wage floors, which is considered by the OECD standards to be best practice and a useful tool to avoid the potential negative impacts of minimum wage regulation on employment creation.<sup>106</sup> Indeed, the recently released OECD Employment Outlook 2015 advises, as a key policy principle, allowing

minimum wages to vary by region to reflect differences in economic conditions.<sup>107</sup>

Varied regional minimum wages are part of a recurrent debate in Australia. The 2014 Report of the National Commission of Audit (NCA) indeed recommends "*minimum wages be set on a State basis to better reflect local labour market conditions and cost of living expenses.*"<sup>108</sup> In particular, the report suggests the regional minimum wage should be, after a transitional period, set at 44% of the average weekly earnings (AWE) in each jurisdiction.

Although a step in the right direction by recognising that minimum pay floors could have a varying negative impact on employment (particularly youth employment) in disparate economic regions, the NCA neglected to address some important points. First, as largely documented, differences in labour market conditions and cost of living expenses are mostly felt within states, rather than between states and territories.<sup>109</sup> As outlined in this report, for example, youth unemployment rates in state capitals tend to be more homogeneous than when compared to some inner state areas—which is why discount on minimum wages should apply to local targeted areas rather than states and territories.

Second, the NCA recommendation is silent with respect to other forms of national minimum wages such as those granted in the national Modern Awards system, including its penalty rate clauses. Hence, even if the proposed regional 44%-AWE minimum wage were implemented, it would not be of any help to lift youth unemployment when most hospitality and retail award wages are rigidly set at national level, with little room for exceptions. A better provision would be to provide the same discount applied to the federal minimum wage to all forms of nationally regulated pay floors.

In addition, the NCA report failed to take into account the interplay between varying regional minimum wages and national unemployment benefit payments. This factor could potentially generate low incentives to work and forgo welfare benefits in states where the new 44%-AWE minimum wage rule significantly lowers the gap between the pay floor and unemployment benefits. A better solution would be to bind the unemployment welfare payments with the same local discount granted to minimum wages, as the basis for calculation should be geographic economic conditions including living costs.

The Productivity Commission (PC) in its recent draft report on workplace relations also contemplated the introduction of non-uniform national minimum wages. In its key points, the PC recognises that "*nationally uniform minimum wages do not account for differences*

*in living costs and labour market conditions in different places” and that most of the variations in economic conditions occur intra-state.<sup>110</sup> Nevertheless, in criticism of the model recommended by the NCA report, the PC concludes that “both state and regionally based models could have several drawbacks, associated with their interactions with the national tax-transfer system and with national awards, compliance costs and questionable constitutionality. The Productivity Commission does not recommend them.”<sup>111</sup>*

**Recommendation 2** addresses many of the concerns raised in the PC report. First, pay floor discounts would be intended at local rather than state level. Second, for integrity purposes, the extension of local discounts is recommended not just on federal minimum wages, but also on all other forms of nationally regulated pay floors as well as the national unemployment welfare payments. Third, instead of a fixed formula as proposed by the NCA 44%-AWE minimum wage rule, local discounts should be decided according to the Fair Work commission adjudication before soliciting pleas

from legitimate external parties such as trade unions, employers’ associations or local councils.

Furthermore, regarding the questionable constitutionality of non-uniform minimum wages, the PC report warns that “setting different regulated wages for enterprises engaged in interstate trade may represent a barrier to such trade”,<sup>112</sup> which could violate section 92 of the Australian Constitution. In addition, the PC also highlights a possible violation of section 99 in the Constitution, which states “The Commonwealth shall not, by any law or regulation of trade, commerce, or revenue, give preference to one State or any part thereof over another State or any part thereof”. Although these arguments are worth noting, it does not seem plausible that local minimum wages could be framed either as a barrier to interstate trade or preferential treatment from the Commonwealth—yet it would be up to the High Court to have a final say on the matter. In any case, the risk of constitutional challenge has not prevented Australia from pursuing previous contentious policy implementations that were later deemed to be constitutionally legal.<sup>113</sup>

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### Recommendation 3:

#### Introduce long-term unemployment discounts to nationally regulated pay floors over a fixed period

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As seen above, the scarring effects of unemployment—in particular youth unemployment—are more pronounced the longer the jobless spell through the deterioration of working skills and a higher level of discrimination in recruiting processes. Both factors increase the risk of long-term jobseekers being priced out of the labour market due to potentially high nationally-regulated pay floors.

Accordingly, **Recommendation 3** calls for the introduction of long-term unemployment discounts to nationally regulated pay floors over a fixed period. For the long-term young jobseeker, this recommendation will particularly assist those aged over 21, who no longer can access pay floor discounts present in federal junior pay rates. Hence, such a measure would increase the incentive to hire long-term unemployed, especially helping to alleviate the record high levels of long-term unemployment among youth in Australia.

Reducing the demand-side barriers to hiring long-term unemployed is not a new concept. In Australia, employers can apply for wage subsidies under specific work placement programmes (e.g. The National Work Experience) to help disadvantaged jobseekers, in particular the long-term unemployed, obtain a permanent job. The 2015-16 Federal Budget allocated \$1.2 billion to a national wage subsidy pool, with the amount and timing of payments directly negotiated between *jobactive* providers and employers up to \$6,500 over

a 12-month period.<sup>114</sup> Despite the government pledges to simplify and make more flexible arrangements for business to access wage subsidy payments, more data is needed to evaluate the effectiveness of the implemented procedural changes.

A more simplified, omnibus and transparent way to increase the incentives to hire long-term unemployed is to provide a discount to their mandated pay floors over a fixed period. This is what Germany did when implementing a new minimum wage legislation in January 2015—but in this case a complete exemption from the federal minimum wage was granted. According to German law, long-term unemployed jobseekers, who have been registered with the Federal Employment Agency or a Job Centre for more than one year, can be paid below the minimum wage for up to six months after taking up a job. The decision to exempt the long-term unemployed from the minimum pay floor was not without contention, but in the end lawmakers accepted that it was in the best interest of long-term unemployed people to reduce the demand-side barriers to employment caused by statutory pay floors.<sup>105</sup>

In Australia, a six-month period discount also seems a reasonable period for the new worker to acquire the skills, experience and confidence lost after a long jobless period. In addition, a six-month period discount is in line with the exemptions enshrined in the unfair dismissal provisions, further reducing the risk of a bad hiring, which

particularly stigmatises the long-term unemployed. With respect to the size of the discount, further debate and consultation is needed to reach the optimal rate, bearing in mind that Australia's unemployment payments already provide a natural lower boundary for the discount.

Not all cases of youth unemployment are due to demand-side barriers imposed by counterproductive workplace regulation, in particular by high-price nationally regulated pay floors. An unwarranted number of jobless

youth are indeed prevented from successfully joining the labour market due to other root causes such as poor schooling, mental health problems and disadvantaged backgrounds. Nonetheless, the low levels in youth unemployment experienced in the booming years before the GFC show that labour demand (either instigated by proper economic growth and/or more job-creation-oriented workplace regulations) can be fundamental to reduce the jobless contingent of young Australians.

## Welfare Dependence Trap

Another oft-cited barrier to employment is the welfare dependence trap, where the welfare recipient has little motivation to move into the workforce.<sup>116</sup> Despite plenty of anecdotal media reports on shirking behaviour from welfare recipients,<sup>117</sup> there are no precise figures about the proportion of youth unemployment that is due to the welfare dependence trap in Australia. However, public policy should always aim to improve the set of incentives for welfare recipients to get back to the workforce as quickly as possible, including well-designed activity tests that effectively improve the chances to land a stable job. In this regard, the recent announcement by the federal government to establish a tax and transfer group to examine barriers to work is a welcome initiative.<sup>118</sup> As recent Productivity Commission research shows, welfare recipients might face considerable tax disincentives when entering the workforce.<sup>119</sup>

The difficulty in establishing the right levels of social assistance is to fine-tune the welfare payments to alleviate short-term periods of financial hardship without compromising the general principle of the individuals' responsibility to provide for themselves.

Providing appropriate levels of assistance to jobseekers might be economically rational if job match efficiency is boosted.<sup>120</sup> Due to asymmetric information in the job market—for instance, employers and jobseekers do not have perfect information about the supply and demand of skills and job vacancies—job search frictions arise. In this scenario, financial assistance might cover necessary job search opportunity costs in order to provide better job match outcomes, raising productivity and economic growth as a result. Further, in accordance with OECD standards, the introduction

of mutual obligations requiring welfare recipients to observe activity tests on top of other income and asset tests is considered best practice—and indeed part of the Australian welfare system.<sup>121</sup> For instance, welfare recipients on unemployment benefits in Australia must demonstrate a genuine effort to get out of the welfare payments by diligently looking for a job or attending full-time education.<sup>122</sup>

Nonetheless, when welfare payments are excessive or mutual obligations requirements are ineffective, incentives might arise to game the system. In this case, some welfare recipients might extend their use of public funds without a genuine effort to find a job. In Australia, the main welfare payments targeting the jobless youth are the Youth Allowance and the Newstart Allowance.<sup>123</sup> Although both payments are subject to eligibility requirements and activity tests, the efficacy of these support allowance programs to get youth entering the workforce is up for debate. In particular, the ability of the activity tests to improve the chances of finding a job should be under further scrutiny (see **Box 5** on the arrangements for the recently devised National Work Experience Programme in Australia).

Moreover, a steady stream of welfare payments—albeit at low levels (see **Table 3** for selected welfare allowances available to eligible youth)<sup>124</sup>—can act in some cases as a disincentive to successfully move to the workforce, especially when taking into account all the costs involved during job search and the after-tax wage remuneration<sup>125</sup> as well as the possibility of earning some extra income through unreported cash-in-hand work.

**Table 3: Selected Welfare Allowances for Eligible Youth**

<b>Youth Allowance</b>	
Financial help for people aged 16–24 years who are studying full time, undertaking a full time Australian Apprenticeship, training, looking for work, or sick.	<b>Maximum fortnightly payment</b>
Single, with no children, younger than 18 years, and living at parental home	\$233.60
Single, with no children, younger than 18 years, and required to live away from parental home to study undertake training or look for work	\$426.80
Single, with no children, 18 years or older and living at parental home	\$281.00
Single, with no children, 18 years or older and required to live away from parental home	\$426.80
Single, with children	\$559.20
Member of a couple, with no children	\$426.80
Member of a couple, with children	\$468.70
Single jobseeker principal carer granted an exemption from Mutual Obligation Requirements because you are either a registered and active foster carer, providing home schooling for your children, facilitating distance education for your children, caring for a large family, where you are the principal carer of 4 or more dependent children younger than 16 years, or a child in secondary school aged 16 to 19 years, or caring for a child and you are a relative, other than a parent, as directed by a Parenting Order made through the Family Court.	\$725.40
<b>Newstart Allowance</b>	
Financial help for people aged 22 years or older who are looking for work or participating in approved activities that may increase your chances of finding a job.	<b>Maximum fortnightly payment</b>
single, no children	\$519.20
single, with a dependent child or children	\$561.80
single, aged 60 or over, after 9 continuous months on payment	\$561.80
partnered	\$468.80 (each)
Single principal carer granted an exemption from mutual obligation requirements for either foster caring, non-parent relative caring under a court order, home schooling, distance education or large family	\$725.40

**Source:** Department of Human Services, Australian Government. Values as at September 2015. Recipients may be entitled to other welfare payments, services and benefits.

## Box 5: The National Work Experience Programme

The National Work Experience Programme plan to allow jobseekers to do a part-time month of unpaid work experience might be a step in the right direction to get long-term unemployed into the job market. However, there need to be safeguards to avoid abuse and maximise the chance of leading to a permanent job. We cannot have a situation where unscrupulous employers are able to exploit free labour from desperate jobseekers.

The NWEPP consists of an \$18 million, five-year job activation plan allowing unemployed people aged 18 and over to do up to 25 hours per week of unpaid work experience for up to four weeks. During the 'working trial' period, the jobseeker will continue to receive income support, and a fortnightly \$20 supplement to cover transport. Most importantly, the NWEPP will be voluntary, whereas the current Work for the Dole scheme, introduced in 1998, is not.

The Work for the Dole scheme largely relies on the mutual obligation concept, under which unemployment assistance is conditional (i.e. compulsory) on activity tests, including undertaking work such as gardening and maintenance works or warehouse duties—strictly at not-for-profit organisations and government agencies. However, the difficulty with most activity tests lies with what economists call the principal-agent problem: the mismatch of incentives for contracting parties. The government (the principal) wants to nudge the dole recipient back to the workforce, penalising welfare rent-seeking behaviour. Some—yet by no means necessarily the majority of—welfare beneficiaries (the agent) will do the bare minimum to continue qualifying for the dole; especially if there is no real prospect of getting hired or, some might argue, even gaining effective employment skills.

The NWEPP, also dubbed by then prime minister Tony Abbott the 'real' work for the dole, promises to fix this principal-agent problem. First, not only is the program voluntary, but places are limited to around 6,000 jobseekers. One would need to make a good amount of effort to be placed on the trial period. Additionally, there is a good selection bias: there is no extra financial advantage to be under the program—meaning those selected demonstrate a real intention to enter the workforce.

Further, in contrast to the original Work for the Dole scheme, participants have a genuine chance to be hired by learning useful skills and proving their abilities to the potential employer. Ultimately, it is entirely in the participants' interests to do a good job—otherwise why bother; they could just remain on welfare and be subject to the less effective conventional activity tests.<sup>126</sup>

On the other side, NWEPP offers potential employers the right incentive to take a chance on hiring someone who has been out of the workforce for an extended period. Under other circumstances, the risk (and cost) of making a bad hiring are seen as being unjustified, as long-term unemployed are generally not well perceived by potential employers.<sup>127</sup>

The 25 weekly hours for a month form a reasonable trial period for a business to gauge someone's ability. Since the firm does not have to pay wages, the overheads consist mainly of training and adaptation costs. Plus, there is even a possibility to qualify for an extra wage subsidy for ongoing employment contracts.

Good policy is achieved by a good design mechanism where all participants have a genuine incentive for making it work. The NWEPP seems to be the case.

For the jobseeker, it is a real, long-awaited chance to put a foot in the job market. For the potential employer, it offers a strong subsidy on new hiring costs. For the government, it could work as a successful transition for people from welfare to employment, generating savings on future welfare benefits and alleviating the social scarring effects of unemployment.

Having said that, the success of the NWEPP will rest on its execution. Accountability is the key to avoid business rorting the system to get a free ride on unpaid work without regard for the true aim of the program, namely the real possibility of an unemployed person securing a permanent job. Firms attempting to game the program must be subject to strong sanctions, including the possibility of hefty fines.

**Source:** Carvalho (2015), "Work for the dole encore: will it work?", *The Canberra Times*, May 30<sup>th</sup>.

## Disadvantaged Background

Not all youth unemployment is derived from demand-side barriers to job creation or low incentives to move from welfare dependence into the workforce. Some young jobseekers with disadvantaged backgrounds genuinely struggle to get access to the job market regardless of pay floor levels or genuine job search efforts. Troubled families, domestic violence, impoverished households, mental and physical health issues, drug abuse, school dropouts, lack of a close supportive network, unreliable income stream—all contribute to a strained first transition to work.<sup>128</sup> In Australia, for example, there are major imbalances, with indigenous youth employment rates being half of non-indigenous.<sup>129</sup> Regional areas are also more affected by the lack of jobs for the young.<sup>130</sup>

Consistent with the poverty trap literature,<sup>131</sup> inadequate access to a pool of resources (including education and credit lines), and occasionally outright discrimination, might undermine the chances of those with low socioeconomic status to thrive. One defining issue is the lack of a stable household unit to emotionally and financially support young people in their education achievements and initial job search, which can have a detrimental impact on their early career prospects.<sup>132</sup>

Research shows that parents of NEETs tend to be less educated, providing evidence of the link between low levels of education through different generational cohorts.<sup>133</sup> Additionally, the incidence of single parenthood among NEETs (particularly affecting young women) is much higher—in Australia, NEETs are five times more likely to be single parents than the overall youth cohort.<sup>134</sup> Furthermore, other studies in Australia have also indicated some minorities face deeper

challenges when it comes to entering the labour market, due to discrimination.<sup>135</sup>

Overall, the take-away message is that jobless youth is not just an economic problem, but also a social one, with self-perpetuating features. One key strategy is aiming to reduce discrimination in the market place and increase access to a variety of resources—from good quality education and cost-effective social counselling to broader job market opportunities. Not an easy start, but a necessity if one is to succeed.

**Recommendation 4** supports the adoption of an actuarial long-term management of the welfare system, which follows the New Zealand's initiative after its own major review in 2011 (**Box 6**). Such an evidence-based support system is also advocated as part of the 2015 McClure Report on welfare reform, which states an "investment approach *would provide necessary support to those who are at significant risk of long term income support reliance and have capacity for self-reliance through work with the right support and intervention.*"<sup>136</sup>

International evidence shows that effective welfare assistance for some disadvantaged groups at risk of long-term income support reliance can require a considerable amount of public resources.<sup>137</sup> Hence, an actuarial approach could assist in making the case for these targeted transition-to-work programs as sound investment decisions with effective intervention in early career stages. This could benefit a struggling disadvantaged youth at risk of lifetime welfare dependence, provided they receive appropriate resources to become fully integrated back into society.

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### Recommendation 4:

Adopt an actuarial long-term management of the welfare system to rationalise the use of public funds and maximise effective outcomes

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#### Box 6: The New Zealand Investment Approach

New Zealand has implemented a series of welfare reforms since 2012, including the introduction of an investment approach for the long-term management of its income support system. Through this new approach, actuarial valuation is used to determine the most effective forms of support to empower recipients into a successful transition from welfare dependence towards the workforce. In short, public money and services are targeted where the return in future savings on welfare spending is the greatest. Further, in order to provide more flexibility with the use of welfare funds, a multi-category appropriation (MCA) was introduced since 2014, allowing the government to direct resources where they can be most effective.

The 2013 Benefit System Performance Report, which is the first internal actuarial report produced under the new structure, estimated the total lifetime costs (forward liabilities) of the New Zealand's welfare system were reduced from NZ\$86.8 billion in 2012 to NZ\$76.5 billion in 2013. Out of this total reduction, NZ\$1.8 billion was claimed to be directly linked to initially targeted welfare interventions that promoted a higher than expected number of welfare recipients going off benefits as well as a lower number of new recipients coming on to benefits.

The report has also identified youth as a particular group of interest, since "more than 70% of the forward liability is in respect of people who first received a benefit before age 20, indicating that many remain vulnerable to benefit dependency for their entire lives".<sup>138</sup> This and other findings in the report will help to give traction for more and better evidence-based interventions and locally designed services to alleviate youth unemployment. In the document's words: "A strong focus on youth is needed to help reduce the inflow of new people who are at risk of long-term benefit receipt".<sup>139</sup>

## Skill Mismatches

Skills are undeniably important for labour market outcomes. Economic research shows that higher human capital leads to higher labour productivity, and therefore, higher and more stable pay.<sup>140</sup> However, not just the level of human capital is important, but also the appropriateness of a particular set of skills to do the job.<sup>141</sup> In this respect, increasing educational levels serves two purposes. First, a better educated population acquires more skills, including the vital skill of learning new skills. Second, since skills are hard to identify, educational credentials can provide a key signalling mechanism.<sup>142</sup>

For the young and inexperienced jobseeker, there is enough evidence that formal education can be a dealmaker in the labour market<sup>143</sup>—especially when there is hardly any other job-related experience or training. Less-educated youth are disproportionately more represented among the unemployed.<sup>144</sup> Moreover, the level of education is the most important determinant of a young person's hourly earnings.<sup>145</sup> As a result, global educational attainment rates have consistently increased over the years. Currently, a third of employees in developed countries have a tertiary degree, as opposed to a fifth in 1970.<sup>146</sup> In Australia, not only have tertiary degree enrolments increased, but the proportion of young adults with Year-12 attainment or equivalent has gradually improved in the last decade, from 71%

in 2001 to 78% in 2010, with the aim to achieve up to 90% in the near future.<sup>147</sup>

Notwithstanding higher educational levels, there are growing concerns about possible skill mismatches in the global labour market.<sup>148</sup> Although the issue affects workers of all ages, young people are particularly impacted. In our fast-paced, service-oriented economy, a more complex set of skills is required, with an additional toll on those at the start of their careers. In addition, automation keeps squeezing the availability of low-skilled jobs that used to be the door to the labour market (**Box 7**); and in most developed economies, globalisation has also shifted away much of the manufacturing low-skilled jobs. Moreover, a dynamic labour market environment with higher turnover has undermined employers' commitment to company-provided training, further worsening the skill mismatch issue.<sup>149</sup>

In this scenario, it is vital to empower young workers with the ability to properly and quickly adjust to a constantly-changing demand for skills, enabling the market to equalise demand and supply through efficient price signalling (i.e. higher wages). Hence, two recommendations are suggested to deal with lifting the skills of young jobseekers, and most importantly, how effective schooling can address possible growing skill mismatches in the Australian youth job market.

### Box 7: The Impact of Automation on Youth Unemployment

Automation is one of the many pressures modern-day workers have to face, with the increasing utilisation of automatic machinery performing tasks previously undertaken by humans.

Yet low-skilled jobs are not the only ones threatened by automation. In an influential 2013 paper, Carl Frey and Michael Osborne predicted almost half of 702 detailed skilled occupations known today—from accountants and financial advisers to real estate agents and drivers—are at high risk of giving way to technology displacement in the next decade or so.<sup>150</sup> Similar predictions claim that more than five million jobs in Australia will simply disappear due to computerisation and technology in the same period.<sup>151</sup>

The threat of automation is real and many jobs will potentially become extinct as a consequence. Yet this is not the end of the story. All these predictions of job losses fail to quantify the new jobs created by the same technological spring.

On the one hand, technology keeps raising the bar of initial entry-skill levels, increasing the role of education as a decisive factor on employability. On the other hand, a cornucopia of new job roles will keep springing up, with automation potentially raising the productivity of workers, and ultimately, their respective remuneration as well.

An often forgotten—and concerning—aspect is the interplay between automation and counterproductive government regulation; the first being the populist impulse to forbid the unstoppable course of technological advancements, such as seen in opposition to sharing economy phenomena such as Uber.

Moreover, government regulation on minimum pay floors (e.g. national minimum wages and Modern Award rates including penalty rates) can artificially speed up the rate of automation, making it particularly difficult for workers to adapt to the technological wave. Recent research provides empirical evidence that higher statutory wages may prod companies into substituting human labour by automation.<sup>152</sup>

For young jobseekers, the best help comes from a solid educational base, with a strong focus on foundational skill set such as numeracy and literacy that empower them with the basic skills needed to learn new skills. In our fast-changing working environment, mushrooming demand for new specific occupational and trade skills are the rule, and the ability to quickly adjust someone's skills is paramount for a successful professional career. In this respect, numeracy and literacy skills are the baseline foundation of skill learning abilities; able to effectively improve the employability of young Australians.

With solid foundational skills, young workers should not fear automation, which could be seen both as a threat as an opportunity.

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## Recommendation 5:

### Lift numeracy and literacy skills of school-leavers to improve employability

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**Recommendation 5** regards lifting numeracy and literacy skills of school leavers to improve employability. Despite the increase in Year 12 completions, Australian school leavers have not achieved substantial improvements in foundational skills such as numeracy and literacy, according to the National Assessment Program – Literacy and Numeracy (NAPLAN) results.<sup>153</sup> In addition, Australian pupils have performed less well relative to other international peers over the years, as the Programme for International Students Assessment (PISA) attests.<sup>154</sup> Further, a recent report from the Centre for Independent Studies indicates there are thousands of Australian students showing very low levels of literacy after spending four or more years at school.<sup>155</sup>

Although lifting Year 12 or equivalent attainment rates is laudable, more important is to make sure that, while at school, students are actually learning the basic educational skills in order to boost their professional lives. A good foundation of numeracy and literacy skills directly enhances productivity at work. In addition, such foundational skills also have the potential to lower skill mismatches in the job market by better equipping young workers with the basic skills needed to learn new skills. In our fast-changing working environment, mushrooming demand for new specific occupational and trade skills are the rule, and the ability to quickly adjust one's skills is paramount for a successful professional career. In this respect, numeracy and literacy skills are the ground foundation of skill learning abilities, improving the employability of young Australians.

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## Recommendation 6:

### Investigate innovative ways to increase the accountability of tertiary and VET institutions with respect to job market outcomes

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**Recommendation 6** calls for the investigation of innovative ways to increase the accountability of tertiary and Vocational Education and Training (VET) institutions with respect to job market outcomes. At the moment, tertiary and VET students under certain conditions can apply for income-contingent loans through the Higher Education Loan Programme (HELP) that have to be repaid to the government through the taxation system once taxable income is above the repayment threshold—currently at \$54,126 for the 2015-16 financial year.

The HELP scheme accounts for a sizeable impact on the federal budget. The annual cost of the programme is around \$1.5 billion, amounting to over \$30 billion in total accumulated debt stock.<sup>156</sup> Around a fifth of the new annual loans are expected not to be repaid due to several factors ranging from people failing to reach the repayment threshold or moving overseas to deceased debtors, with the size of doubtful debt increasing in the past years.<sup>157</sup>

Although Australia's higher education income-contingent loans constitutes a laudable initiative to assist thousands of Australians every year to pay for their higher education, some of its mechanism needs revisiting. In particular, under the current demand-driven system,

educational institutions have the incentive to enrol as many students as possible, regardless of job market demands and suitability of students. This arrangement not only promotes lower admission standards, but also does not create a responsibility to properly teach subjects that might improve the human capital in the job market.

This is against the students' interests and a potential misuse of taxpayer funds.

Hence, it is imperative to investigate forms of outcome-driven funding to increase the accountability of tertiary and VET institutions with respect to job market outcomes. That is, there must be an open public debate on the introduction of a better system of incentives (and perhaps sanctions) to ensure the material taught at these institutions—which benefit from a government-subsidised funding system—translates into a higher human capital pool of workers facing Australia's labour market demand of skills. Not an easy task, but a necessary one. This will help prevent young Australians from being lured into debt under the dubious promise to lift their career prospects and make sure that the time and effort—and taxpayer's funds—invested in further formal education is indeed a good investment.

## Concluding Remarks

This report shows that youth unemployment is a pressing issue in our national policy landscape. Since the onset of the GFC at the end of 2008, the contingent of jobless young Australians—especially those suffering long spells of unemployment—has been in a steady rise. Currently, there are around 300,000 youth failing to find a job. Further, youth disengagement captured by swelling NEET rates among early 20s also highlights that youth unemployment is a multifaceted problem requiring a set of targeted policies.

First and foremost, rising youth unemployment in Australia is due to a tepid economic environment. There is no other more compelling reason for the increasing mass of jobless youth in the last seven years. In short, growth matters—as the Okun’s law relationship between economic activity and job creation attests. Hence, Recommendation 1 draws attention to the much-needed implementation of a new round of structural reforms to lift economic growth in Australia. If we are serious about reducing youth unemployment, there must be political will to boost the institutional enablers and incentives conducive to growth and job creation.

Evidence also shows that much can be done in other policy areas to alleviate the plight of jobless youth. For one, demand-side barriers to employment could be eased by allowing targeted discounts on nationally regulated pay floors (e.g. national minimum and Modern Award wages, including penalty rates). In this respect, Recommendation 2 advises local discounts to low socioeconomic geographic areas, and Recommendation 3 calls for a lower pay bar entry for those affected by long-term unemployment. These measures could help prevent the most vulnerable in our society, such as the

low-skilled, inexperienced youth, from being summarily priced out of the labour market.

Moreover, youth unemployment is a socioeconomic issue with scarring, long-lasting effects. An unwarranted number of jobless youth are indeed prevented from successfully joining the labour market due to other root causes such as poor schooling, mental health problems and disadvantaged background. Recommendation 4 reinforces the need for an evidence-based investment approach to welfare expenditures, where actuarial methodology could raise public awareness on the effectiveness of public funds targeting the most in need in our society, largely represented by the youth.

This report also presents data on the deterioration of Australia’s relationship between job vacancies and youth unemployment rates, which highlights potential skill mismatches in the job market. In this scenario, it is vital to empower young workers with the ability to properly and quickly adjust to a constantly-changing demand for skills, enabling the market to equalise demand and supply through efficient price signalling. Accordingly, Recommendation 5 stresses the role of numeracy and literacy skills as the baseline foundation of skill learning abilities, helping to shorten the life span of skill mismatches. Further, Recommendation 6 calls for more accountability of tertiary and VET institutions with respect to job market outcomes.

The future rests on the young generation, and Australia cannot miss the chance of getting it right when facing the challenges of youth unemployment.

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