YOUTH UNEMPLOYMENT IN AUSTRALIA

Why it's still a problem, and how to solve it.

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 secured 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. 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. 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. There are more than 75 million young people looking for a job globally, constituting 40% of the world's unemployed. 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. In summary, youth unemployment is a global issue.

Patrick Carvalho is a Research Fellow in the Economics Program at the Centre for Independent Studies, and has published in several Australian and international economics forums. Dr Carvalho was formerly Head of the Economic Studies Division at the Federation of Industries of Rio de Janeiro and a Lecturer in the Research School of Economics at the Australian National University.

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.

But this time is different.

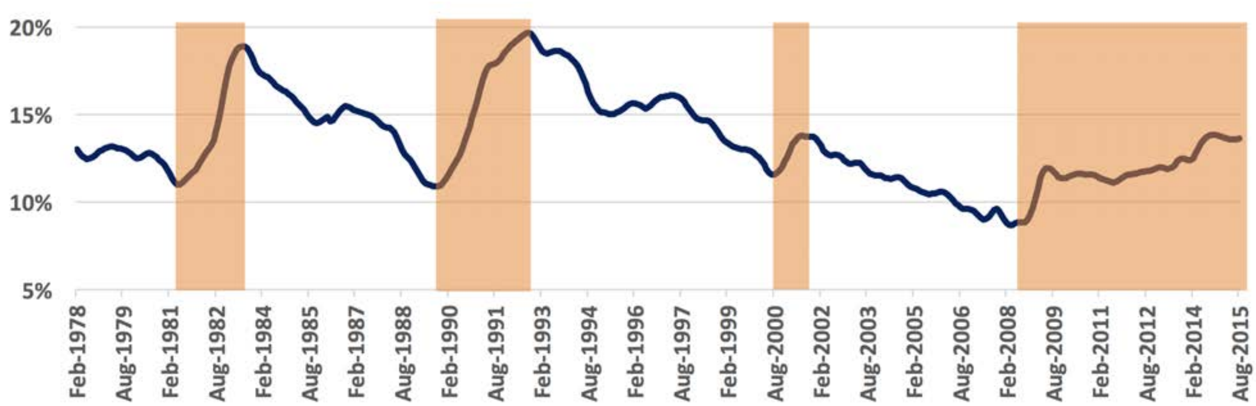
Figure 1 shows Australia's youth unemployment trend rates based on Australian Bureau of Statistics (ABS) data. The shaded areas represent the biggest hikes in jobless youth, and match Australia's main economic downturn periods: a global recession in the beginning of the 1980s, mainly due to international 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.

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

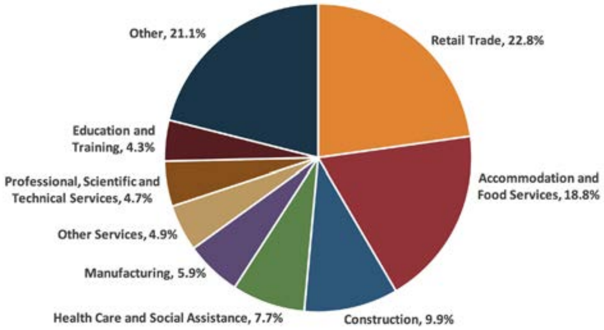
The Youth Labour Market

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.

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.

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, and therefore make it harder to address youth unemployment.

Figure 2: Share of Youth Employment by Industry



Source: Department of Employment (2015).

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 Australia 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 the 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.

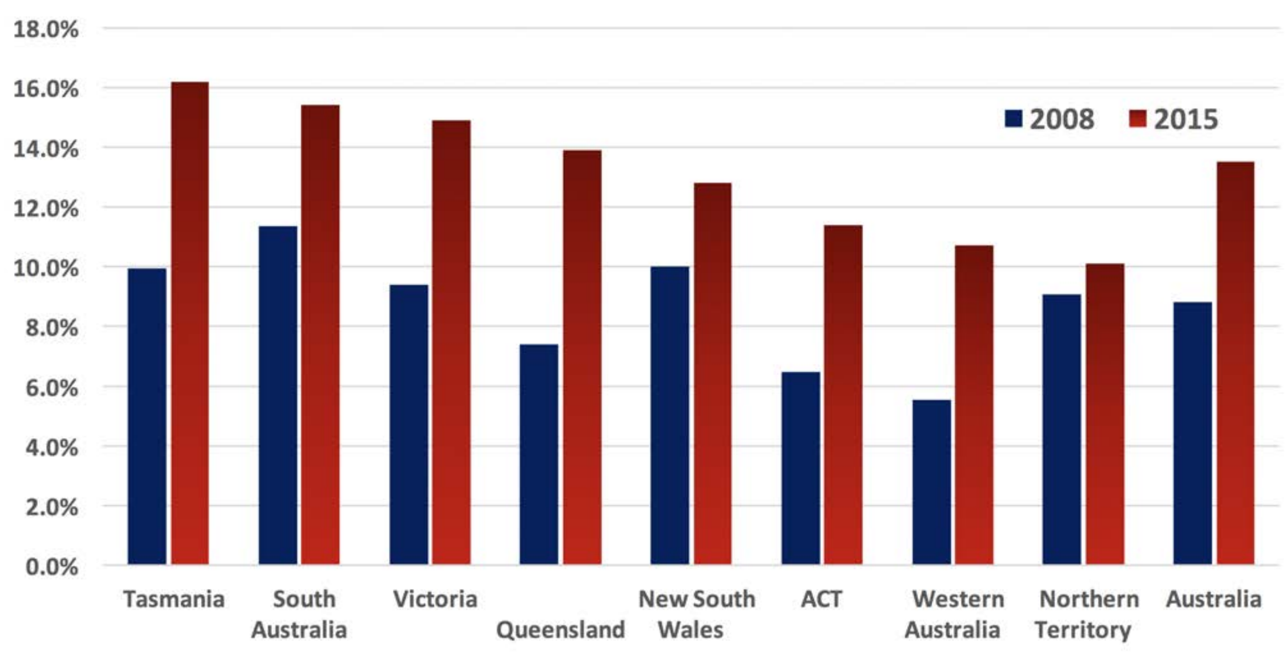
Rates in **New South Wales** have not seen much deterioration in the past seven-year cycle, from 10.0% in 2008 to 12.8% in 2015 — which is below the national average. The same could be said about the greater Sydney area, although at some points such as the Central Coast, Blacktown and the Inner South 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. 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.

The Root Causes and Policy Recommendations

Recommendation 1: Implement structural reforms aiming to lift economic growth

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

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. 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.

Recommendation 2: Introduce 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.*" 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.

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. 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.

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."* 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.

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

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. 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.

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

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*."

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. 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.

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

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. 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. 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.

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.

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

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.