# *CHAPTER 1*

## How are young people faring in the jobs crisis?

*The 2008-09 recession and the resulting jobs crisis had a dramatic impact on youth unemployment. In the OECD area, the youth unemployment rate reached a post-war high of 19% in 2010. Even though a recovery is now underway, the youth unemployment rate is projected to decline only slowly. The current shift to fiscal consolidation in a growing number of OECD countries is challenging and calls for even better designed and targeted policies. The goals of facilitating the school-to-work transition and improving labour market prospects for all youth are more urgent than ever. If these goals are not achieved and the numbers of disadvantaged youth swelled significantly, there is a high risk of creating a large hard-core group of youth left behind with "scarring" effects and perpetuating poor employment prospects for youth in the longer term.*

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

After the severe economic downturn which began in late 2007/early 2008 in most OECD countries, the economic recovery began in the second half of 2009 in the majority of OECD countries. But economic growth remains rather modest and many countries are still facing strong headwinds coming both from the need to embark on fiscal consolidation and the severity of the jobs crisis. Young people have been particularly hard-hit by the recession and youth unemployment is likely to remain high well into the recovery. Prolonged unemployment and spells of inactivity may permanently lower their employability, particularly for low-skilled and inexperienced youth. This chapter analyses the recent trends in youth labour markets dominated by the economic and jobs crisis. Section A presents youth unemployment and employment trends up to 2011, while Section B explores the key factors at stake, including the risk of long-term negative consequences, the so-called "scarring" effects, on some groups of youth.

## A. Youth unemployment and employment trends

### 1. *Stylised trends in the OECD area over the past 25 years*

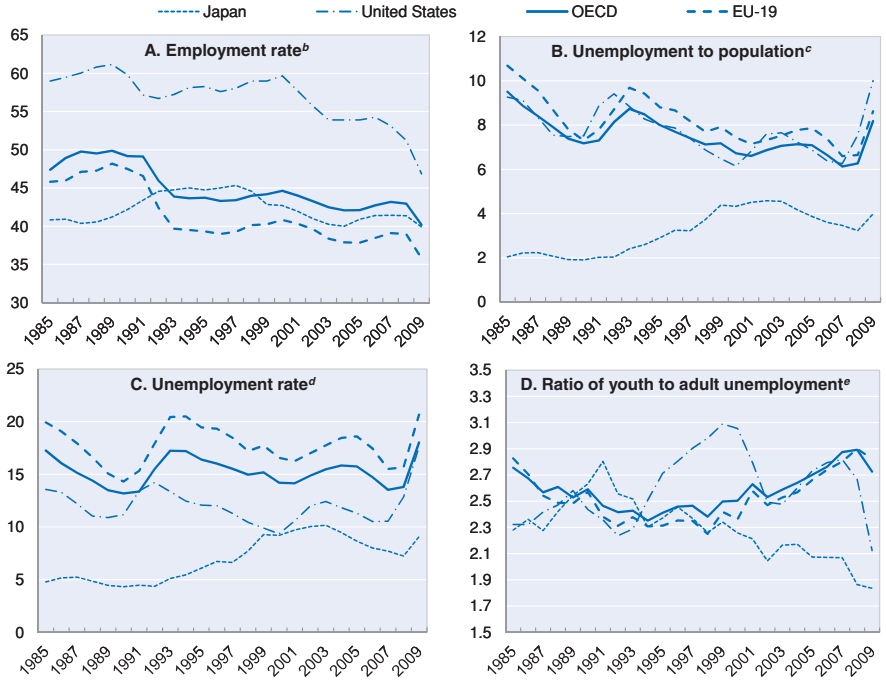
The 2008-09 recession[1] has hit youth hard in the OECD area. The OECD youth (15-24) employment to population ratio – the so-called *employment rate* – declined by 3 percentage points between 2007 and 2009 to a low of 40% while the OECD youth *unemployment to population ratio* at 8% in 2009 rose by 2 percentage points during the same period (Panels A and B, Figure 1.1). The most commonly used indicator of youth labour market performance, the youth *unemployment rate* – the share of unemployment in the youth labour force – increased sharply by 4.5 percentage points during the same period to reach 18% in 2009 (Panel C, Figure 1.1). This latter indicator measures the unemployment risk of youth who have already left the school system, sometimes with a lack of qualifications, which can explain why they have greater difficulties in the labour market. Before the onset of the recent recession, the OECD youth unemployment rate was close to its 1990 level (13%), its lowest level over the past 25 years. Finally, the *ratio of youth to adult unemployment rates* in the OECD area, an indicator of young people's relative vulnerability compared with adults, remained close to its highest level of 3 reached in the mid-2000s. This shows that on average in the OECD area, even in good times, young people tend to be much more vulnerable to unemployment than adults (Panel D, Figure 1.1).

Youth labour market performance indicators vary significantly within the OECD area when, for example, their levels and trends are compared between Europe, Japan and the United States (Figure 1.1). The past 25 years are marked by several periods of slowdown, in particular in the early 1990s and in the early 2000s. Over this period, Japan had an employment rate fluctuating between 40% and 45% while in Europe and the OECD, employment rates had fallen over time since their peak in the late 1980s. The employment rate of young Europeans, however, was consistently below the employment rate of young Americans (respectively 46% and 59% in 1985 and 36% and 47% in 2009). The youth employment rates in Europe, and particularly in the United States, never returned to their pre-recession peaks, yielding "youth jobless recovery periods". This is partly due to the fact that youth tend to spend more time in full-time education which is not necessarily a bad thing as it contributes positively to future human capital. Also, the rise in youth unemployment varies across countries. The recessions of the early 1990s and the early 2000s affected youth unemployment rates everywhere. However, the 2009 youth unemployment rate was the highest ever reached over the past 25 years in the United States (18% compared with 14% in 1992), whereas the rate in Europe was very

close to the peak in the early 1990s. By contrast, the 2009 youth unemployment rate of 9% in Japan was still below the level of 10% in 2003 after the so-called lost decade of the 1990s, when the overall contraction of labour demand resulting from the prolonged recession made it more difficult for many young Japanese to gain a secure foothold in the labour market and move up the career ladder.

Figure 1.1. **Youth[a] labour market indicators, 1985-2009**

Percentages




*a)* Youth aged 16-24 for Iceland, Spain, Sweden, the United Kingdom and the United States; youth aged 15-24 for all other countries.
*b)* Employed as a percentage of the population in the age group.
*c)* Unemployed as a percentage of the population in the age group
*d)* Unemployed as a percentage of the labour force in the age group
*e)* Unemployment rate of youth (15/16-24)/unemployment rate of adults (25-54).

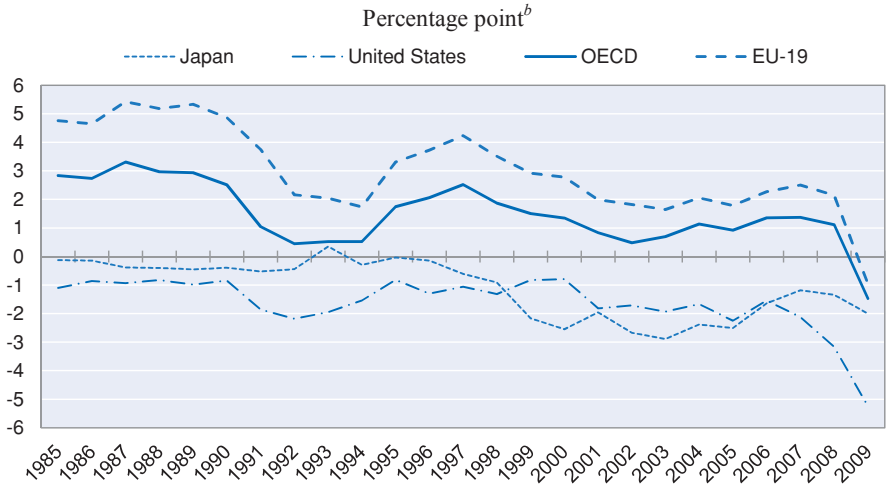
*Source*: National labour force surveys.

There were also large differences within the OECD area in the intensity and fluctuation of the relative youth/adult vulnerability to unemployment (Figure 1.1, Panel D). In 2009, the ratio was 1.8 in Japan, 2.1 in the United States and 2.8 in Europe. In Japan, this ratio has fallen since its peak of 2.8 in 1991, in contrast with Europe which has shown an upward trend since the early 1990s. The ratio varies more with the business cycle in the United States. The significant rise in the ratio that occurred in the United States relative to the European average between 1993 and 2001 is explained by the fact that adults in the United States recovered from the early 1990s slowdown at a much faster pace than adults in Europe (OECD, 2009g).

Figure 1.2 highlights the fact that the gender patterns to youth unemployment differ across the OECD area. Traditionally in the United States, the unemployment rate of young women is lower than the unemployment rate of young men and this phenomenon has been exacerbated in the current crisis when young men were harder hit by job losses

than young women. The same trend has become significant in Japan since the end of the 1990s. By contrast, in the OECD on average but more particularly in Europe, young women used to face a higher risk of unemployment than young men. However, this situation has reversed during the recent recession: the gender gap is now negative in Europe for the first time in 25 years.

Figure 1.2. **Difference in unemployment rates between young women and young men,[a] OECD, Europe, United States and Japan, 1985-2009**




*a)* Youth aged 16-24 for Iceland, Spain, Sweden, the United Kingdom and the United States; youth aged 15-24 for all other countries.

*b)* Unemployment rate of women – unemployment rate of men.

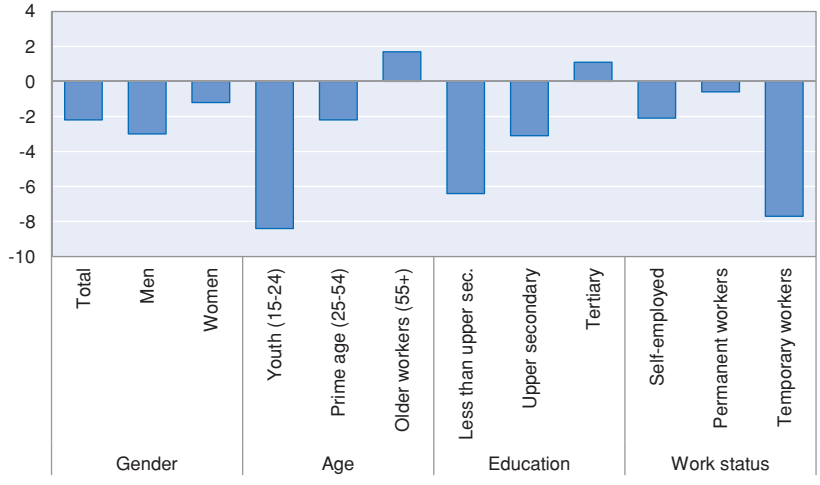
*Source*: National labour force surveys.

## *2. Youth have been hit particularly hard during the crisis*

The last issue of the *Employment Outlook* noted that the recent recession has been unusual in that employment has fallen significantly more for men than for women, probably due to the sectoral profile of the recession (*i.e.* especially large employment losses in mining, manufacturing, and construction) (OECD, 2010d). Continued employment growth for older workers during the recession is also a break with the past. However, as in past recessions, job losses have been relatively larger for some workforce groups than for others. Youth and workers with *temporary employment contracts* – groups that overlap to a considerable extent – have been hit particularly hard by the 2008-09 recession (Figure 1.3). On average for the OECD area, employment for both of these groups fell by around 8%, nearly four times the decline in overall employment. In marked contrast to the situation for youth, employment for prime-age workers decreased by only 2% in the OECD area, while employment for older workers rose by nearly 2%. The difference in the risk of job loss between temporary and permanent workers was also very marked, while employment for the self-employed fell by about as much as overall employment. As in past recessions, employment fell most sharply for the least skilled workers (6.4%, nearly three times the overall rate). Employment losses were also above-average for medium-skilled workers.

Figure 1.3. **Youth employment has been hit particularly hard during the crisis, OECD countries,[a] 2008-09[b]**

Percentage changes




*a)* Unweighted averages based on the following countries: Australia, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Korea, the Netherlands, Portugal, Spain, Sweden, the United Kingdom and the United States for gender and age groups; Austria, Belgium, Denmark, Finland, France, Germany, Italy, the Netherlands, Spain, Sweden, the United Kingdom and the United States for education; and Belgium, Denmark, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal, Spain and the United Kingdom for work status. See Figure 1.3, OECD (2010d).

*b)* Data refer to the period 2008-Q4 to 2009-Q4.

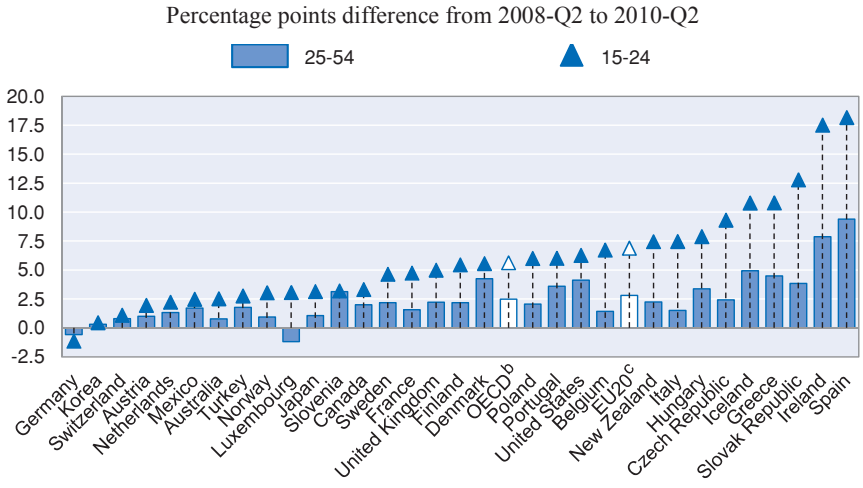
*Source*: OECD estimates based on the European Union Labour Force Survey (EU-LFS) and national sources.

The last issue of Education at a Glance indicated that during, the 2008-09 downturn, young people with a low level of education were hard hit (OECD, 2010f). The unemployment rate for those aged 15-29 who had not completed high school increased by 5 percentage points in the OECD on average. For young people aged 15-29 with tertiary degrees, by contrast the increase in unemployment rates during the same period was about 2 percentage points.

### *3. Recent quarterly youth unemployment trends country by country*

Available statistics up to the second quarter of 2010 suggest a marked increase in youth unemployment since the second quarter of 2008. On average, the youth unemployment rate has increased by almost 6 percentage points over this period but this average hides significant differences across countries (Figure 1.4). Only Germany experienced a slight negative difference for youth and the highest increases were recorded in Spain (18 percentage points), followed by Ireland (17.5 percentage points), the Slovak Republic (13 percentage points), Greece and Iceland (11 percentage points). In most countries, the youth unemployment rate has increased more than the adult unemployment rate: the average increase is slightly more than double (respectively 6 and 2.5 percentage points) and more than triple in six countries (Australia, Norway, France, Belgium, New Zealand and Italy).

Figure 1.4. **The unemployment rate has increased more for youth than for adults**[a]

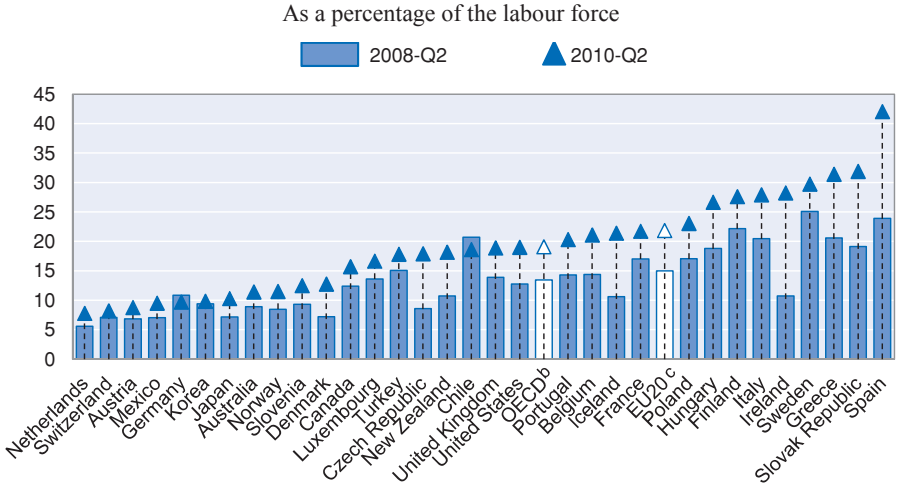



*a)* Non-seasonally adjusted data. Data for Switzerland refer to the second quarter 2009 and 2007.
*b)* Unweighted average of countries shown.
*c)* Unweighted average of the 20 OECD and EU member countries.

*Source*: National labour force surveys.

However, this increase combined with the fact that some countries had a high youth unemployment before the crisis led to youth unemployment rates exceeding 25% in eight countries (Spain, Slovak Republic, Greece, Sweden, Ireland, Italy, Finland, Hungary) (Figure 1.5). The highest rate is in Spain where 42% of youth who had entered the labour market were unemployed. By contrast, the youth unemployment rate is still at 10% or below in eight countries (Austria, Germany, Japan, Korea, Mexico, the Netherlands, Norway and Switzerland).[2]

Figure 1.5. **Youth unemployment rates have been increasing during the crisis in OECD countries**[a]

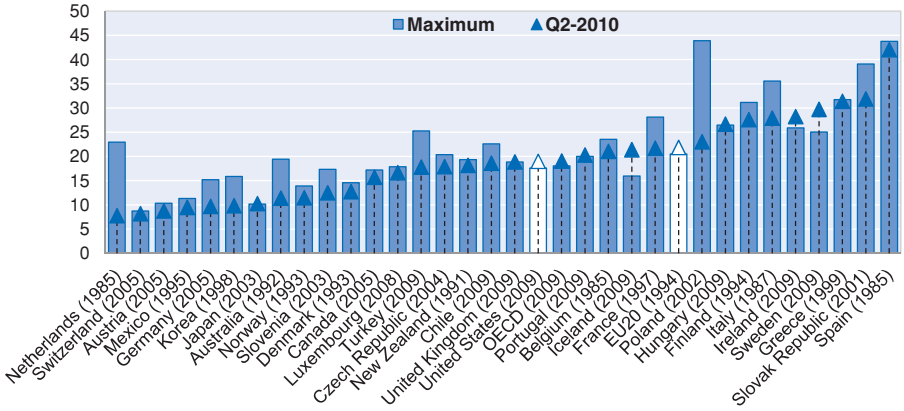



*a)* Non-seasonally adjusted data. Data for Switzerland refer to the second quarters 2007 and 2009.
*b)* Unweighted average of countries shown.
*c )* Unweighted average of the 20 OECD and EU member countries.

*Source*: National labour force surveys.

Consequently, the youth unemployment rates reached mid-2010 are close to or higher than the maximum level ever experienced in the past 25 years (Figure 1.6). On average for the OECD and EU countries, the current youth unemployment rate (respectively at 19% and 22%) is at its maximum. This is the case for seven countries (Japan, United States, Portugal, Iceland, Hungary, Ireland and Sweden). For the other countries, the current rate is close to (less than 3 percentage points) the maximum, except for nine countries (Netherlands, Korea, Germany, Australia, Turkey, France, Poland, Italy and the Slovak Republic).

Figure 1.6. **The current youth unemployment rate is often close to or higher than the maximum level ever experienced**[a]




*a)* The maximum level refers to the period since 1985 up to 2009. In brackets the year in which the maximum was reached.

*Source*: National labour force surveys.

## *4. Short-term prospects for youth unemployment*

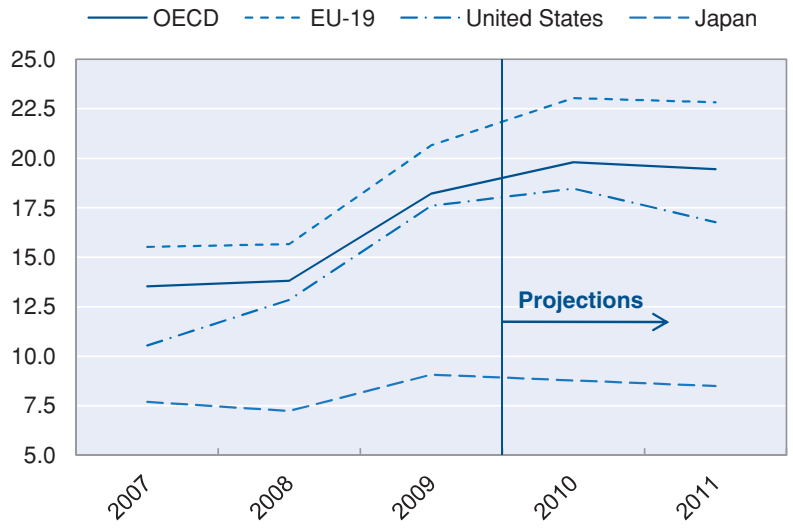
In 2011, OECD youth unemployment rates should be much higher than their pre-crisis levels. Figure 1.7 shows estimates of the likely evolution of youth unemployment rates in 2010 and 2011. These estimates are based on the latest OECD annual economic projections in Spring 2010 (OECD, 2010c), and on the assumption that the youth to overall unemployment rate remains constant at its 2009 level on throughout the projection period.

Starting from the low level of 13% in late 2007, the OECD unemployment rate rose to a post-war high of 19% in 2010, corresponding to more than 4 million additional unemployed young persons. The most recent OECD projections indicate that youth unemployment may well peak in 2010 but could decline only slowly and still close to 20% at the end of 2011. Should these projections prove accurate, it would mean that the OECD average impact of the 2008-09 recession on youth unemployment would be comparable to the deepest earlier recession in the post-war period, namely, that following the first oil shock in 1973.

Some easing is expected in youth unemployment, particularly in the United States in 2011. Japan is expected to experience a rather stable youth unemployment rate around 9% in 2010 and 2011. However, the unemployment rate in 2011 for Europe and the United States is projected to be higher than its pre-crisis level (of respectively 7.3 and 6.3 percentage points).

Figure 1.7. **Persistence of high youth unemployment rates in 2011[a]**

As a percentage of the labour force

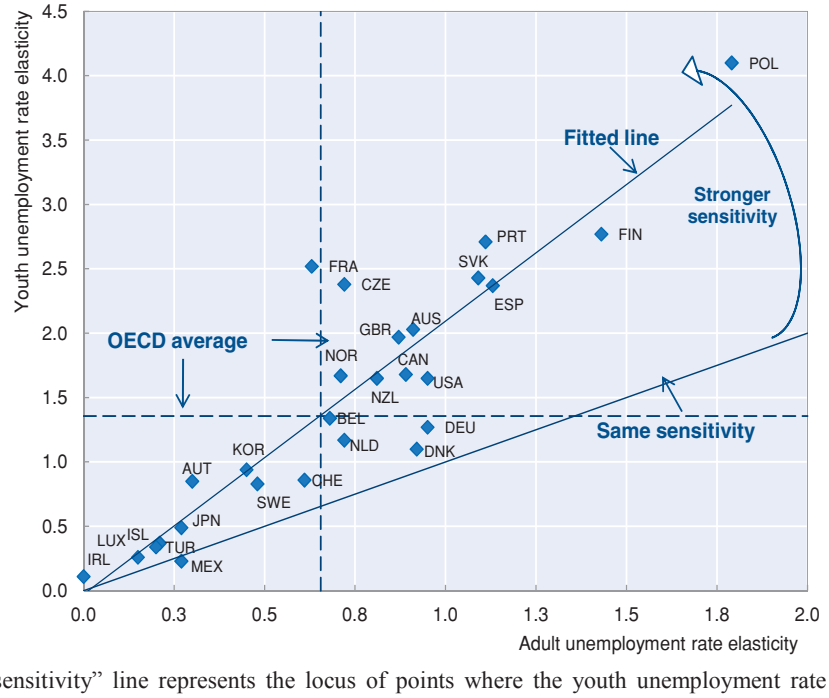



*a)* Projections of youth unemployment rates for the 2010 and 2011 are based on the latest OECD projections of the total unemployment rate assuming that the ratio of youth to total unemployment rate remains constant at its 2009 level.

*Source*: National labour force surveys and OECD (2010c), *OECD Economic Outlook*, No. 87.

Figure 1.8. **In OECD countries, youth unemployment is more responsive to the cycle than adult unemployment[a]**

Percentage point change in the response to a 1% point deviation from the growth rate of potential GDP, 1996-2007




*a)* The "same sensitivity" line represents the locus of points where the youth unemployment rate elasticity to the business cycle is the same as that of the adult unemployment rate. Countries above (below) this line have a higher (lower) sensitivity to the youth unemployment rate than to that of adults.

*Source*: Estimations based on national labour force surveys and *OECD National Accounts database*.

## B. Key factors at stake

### *1. A number of factors make youth particularly exposed in a major downturn*

Across the OECD area, youth unemployment is more responsive to the business cycle than adult unemployment, particularly in some of the continental European countries and the transition economies of eastern Europe (Figure 1.8). A number of factors contribute to explaining the higher business-cycle sensitivity for youth in the labour market, but the dominant interrelated factors are their disproportionate presence among those holding temporary jobs and their high concentration in certain cyclically-sensitive industries such as construction (OECD, 2009d). These factors are analysed in more depth in Chapter 5.

Other analysis focuses on the lags in response to the business cycle. For example, in Belgium an analysis based on administrative data shows that in the past, youth and adult unemployment responded quite similarly to the business cycle, but that the reaction of youth unemployment was much more rapid in a downturn (CSE, 2009). The analysis also finds that young people were the first to benefit from a recovery.

### *2. There is a risk of "scarring" effects for the most disadvantaged youth*

The idea that early labour market experiences can have a long-term effect on labour market performance both in terms of labour force participation and earnings is widespread. However, there is surprisingly little analysis to prove this point and most of it focuses on tertiary male graduates. Several studies in Canada, Japan and the United States have found that entering the labour market in an economic downturn reduces the wages of tertiary male graduates (Box 1.1). However, a number of questions remain open, including whether these effects are *permanent* or *transitory* and whether these findings are applicable to lower-skilled youth, female graduates and other European countries. Scarpetta, Quintini and Manfredi (2010) fill this gap by studying the long-term effects of entering the labour market in France, Germany, Italy, Spain, the United Kingdom and the United States. Table 1.1 shows the effect of the unemployment rate at labour market entry on annual earnings in these six countries.[3]

Annual earnings reflect both the hourly wage earned by a worker and the time spent in employment over the year. The initial negative effect on earnings of the unemployment rate in the year of leaving education is largest in the United Kingdom where a 1 percentage point increase in the unemployment rate at entry reduces earnings by almost 8%. This effect declines over time to just 2% ten years after entry and disappears thereafter. In the United States, the contemporaneous decline in earnings is just 2-3% and it dissipates within ten years of labour market entry. In France and Spain, not only is there a negative contemporaneous effect of 2-3% on earnings but this effect persists up to 15 years after labour market entry. Finally, in Germany, no contemporaneous effect is identifiable but a sizeable negative effect emerges as experience accumulates and is found to be quite persistent. There are no statistically significant effects for Italy.

### Box 1.1. **Existing evidence on scarring effects**

For the United States, Kahn (2009) finds that a 1 percentage point rise in the unemployment rate at the time of tertiary graduation translates into a wage loss of 6% to 7% in the first year of employment. The wage loss declines with time but, 15 years on, those who graduate in times of high unemployment still earn 2.5% less than their more fortunate counterparts. Kahn (2009) also finds that the unemployment rate at time of graduation has a modest negative effect on occupational attainment – measured by a so-called "occupation prestige score" – and a small positive effect on tenure, suggesting that youth graduating in a recession find it more difficult to move to better jobs when economic conditions improves. Contrary to the persistent effects found for the United States, Canadian studies find only transitory setbacks. Oreopoulos *et al*. (2006) study the effects of recessions on male college graduates and find short-run negative earnings effects that are similar in magnitude to those found by Kahn (2009) but dissipate within ten years of leaving school. Neither in the United States nor in Canada have researchers identified significant employment effects, but this may be due to the fact that studies focus on men and that labour market withdrawal effects may concentrate on other demographic groups.

Women who leave school in a downturn appear to suffer smaller wage scars than their male counterparts but are more likely to withdraw from the labour market (Hershbein, 2009; and Kondo, 2007). The results are less clear-cut for less-educated youth. On the one hand, some researchers find evidence that less-educated youth are more affected than high-educated youth because of lower geographical mobility due to credit constraints (Wozniak, 2006). On the other hand, some authors argue that low-educated workers are more likely to withdraw from the labour force over the course of their work life than their more skilled counterparts – which makes them lose the benefit of entering the labour market in good times – hence their wages are less affected by labour market conditions at school leaving (Kondo, 2007). In support of this latter view, Genda *et al.* (2008) find persistent negative effects of the unemployment rate upon leaving education for less educated Japanese men, suggesting that institutional features of the labour market may interfere with the persistence of scarring effects. Indeed, institutional links between employers and schools are a dominant feature of school-to-work transitions in Japan where firms recruit most of their new hires directly among school-leavers. In years of economic slowdown, this recruitment is much reduced, causing many school-leavers to become unemployed. When growth resumes, employers return to hiring among freshly-graduated school-leavers, creating a lost generation of unemployed youth.

Finally, the negative effects of completing education at a time of high unemployment may be countered in the long term by the fact that some youth may decide to enrol in higher-level educational qualifications to avoid unfavourable labour market conditions. Evidence to support this positive effect of economic downturns on human capital accumulation can be found in several US studies (Betts and McFarland, 1995; and Black *et al*., 2005).

Differences by skill level vary across countries. Scarpetta, Quintini and Manfredi (2010) find that in the United States, a high unemployment rate at entry has a large and persistent negative effect for low-educated men, while only a very small effect for tertiary graduates. The opposite is found in the United Kingdom where high-educated youth are the most affected by the unemployment rate at labour market entry.

Table 1.1. **Effect of the unemployment rate at labour market entry on future earnings,[a] men, 1990s**

| | Dependent variable: log earnings (OLS[b]) | | | | | |
|---|---|---|---|---|---|---|
| | United States | United Kingdom | France | Germany | Italy | Spain |
| | Regression coefficients | | | | | |
| $UR_{t0}$ | **-0.018** | **-0.077** | **-0.027** | 0.007 | -0.028 | **-0.02** |
| | (0.000)** | (0.000)** | (0.000)** | -0.602 | -0.55 | (0.000)** |
| $UR_{t0}$*$Exp_{it}$ | **0.001** | **0.005** | **-0.008** | **-0.232** | 0.001 | -0.029 |
| | (0.000)** | (0.000)** | (0.000)** | (0.000)** | -0.397 | -0.063 |
| | Fitted effects for selected years of experience | | | | | |
| Years since leaving education | | | | | | |
| 1 | **-0.017** | **-0.071** | **-0.034** | **-0.226** | -0.026 | **-0.028** |
| | (0.000)** | (0.000)** | (0.000)** | (0.000)** | 0.556 | (0.063)* |
| 5 | **-0.011** | **-0.05** | **-0.065** | **-0.202** | -0.021 | **-0.024** |
| | (0.000)** | (0.000)** | (0.000)** | (0.000)** | 0.584 | (0.062)* |
| 10 | **-0.005** | **-0.023** | **-0.103** | **-0.172** | -0.015 | **-0.019** |
| | (0.000)** | (0.000)** | (0.000)** | (0.000)** | 0.635 | (0.062)* |
| 15 | 0.002 | 0.004 | **-0.141** | **-0.141** | -0.009 | **-0.014** |
| | 0.38 | 0.232 | (0.000)** | (0.000)** | 0.72 | (0.065)* |
| Observations | 519142 | 57538 | 147228 | 6414 | 10172 | 10664 |
| R-squared | 0.274 | 0.31 | 0.556 | 0.562 | 0.212 | 0.284 |

P-values in parenthesis if significant at 1% (**) or 5% (*).

*a)* Monthly earnings for France and annual earnings for all other countries.

*b)* OLS results also include controls for immigration status (ethnicity and race in the United States), region, a quadratic in potential experience and contemporaneous unemployment rates. Controls for marital status, disability status and industry are also included for Germany, Italy and Spain.

*Source:* Current Population Survey, October Supplement for the United States (1979-2007), labour force survey for the United Kingdom (1993-2002), *Enquête Emploi* for France (1991-2002) and European Community Household Panel survey for Germany, Italy and Spain (1994-2001).

# Notes

1. Even though it is somewhat imprecise, this report will use "2008-09 recession" as a convenient, short-hand designation for the economic downturn associated with the global financial crisis that became acute following the bankruptcy of Lehman Brothers investment bank in September 2008. The turmoil in financial markets led to steep global declines in production and trade in the final months of 2008 and early 2009, but the rate of decline eased rapidly thereafter and an economic recovery began in most OECD countries during the second half of 2009. Although most OECD countries experienced a recession during 2008-09, the downturn in a few countries may not be considered to have been deep or long enough to qualify as a recession, whereas the recession had already begun in late 2007 or continued into 2010 for other countries.

2. However, in Mexico and in other lower-income OECD countries, youth joblessness is better captured by the proportion of youth neither in employment, nor in education or training (NEET) which is 22% in Mexico, double the OECD average of 11%.

3. To isolate the long-term effect of a recession on the earnings performance of new entrants, the following equation is estimated: $\log E_{it} = \alpha + \beta X_{it} + \pi UR_{it} + \lambda 1\ UR_{t0} + \lambda 2\ UR_{t0}\ Exp_{it} + \delta 1\ Exp_{it} + \delta 2 Exp2_{it} + u_{it}$. The dependent variable is log annual earnings, X is a vector of individual characteristics, $UR_{it}$ is the contemporaneous unemployment rate, Exp in the number of years since leaving education (*i.e.* potential experience) and Exp2 is its square. The relevant explanatory variables are $UR_{t0}$ – the unemployment rate at the time of leaving education – and $UR_{t0}$ Exp ¬ the interaction of the unemployment rate upon leaving education and potential experience. As a result, λ1 provides the initial effect of the unemployment rate upon leaving education on labour market outcomes while λ2 shows how the effect changes over time.

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