



# Pointmaker

## MORE PRODUCERS NEEDED

### WHY TACKLING WORKLESS HOUSEHOLDS CAN LEAD TO GROWTH

PETER WARBURTON AND JOANNA DAVIES

#### SUMMARY

- A large percentage of UK adults, particularly men, has either never worked or has not sustained continuous paid employment for several years.
- The UK has one of the highest ratios of workless households (ie those in which no adult member is working) in the EU. The social and economic challenges this poses are inextricably linked.
- In 1979, the UK economy was invigorated by the privatisation and liberalisation of nationalised industries, public corporations and local authority housing. In 2010, it is socialised households that require “privatisation”.
- As more paid employment became available between 1992 and 2007, far more jobs went to households where there was already someone working than to people in workless households.
- A 10% drop in the number of workless households represents a potential 3% increase in the number of working households. Even if these transitional households were initially only half as productive as existing working households, this would add around 1% to GDP.
- A crucial policy objective should therefore be to move unproductive and poorly-performing households to the private sector. The challenge is to transfer the practices and attributes of very productive households to those that have become isolated from the world of work.
- This can be achieved through the use of local initiatives, appropriate incentives and enforcing an obligation to accept offers of suitable work.
- The recovery of their latent contribution will bring about both personal and national economic transformation.

## 1. INTRODUCTION

The employment pattern of UK households is unstable, with a high concentration of work in all-working households but with far too many unproductive households. At 11.5%, the UK has the highest incidence of adults in workless households of the six largest EU economies, as Table 1 shows.

**Table 1: EU jobless household rates**

	1998	2009
UK	12.5%	11.5%
Spain	10.2%	10.8%
France	11.3%	10.5%
Italy	12.0%	10.4%
Germany	11.1%	9.2%
Netherlands	8.8%	6.0%

Note: data show the share of persons aged 18 to 59 who are living in households where no one works.

<http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tsisc090>

The increasing indebtedness of the UK economy from the early 1990s created an illusion of prosperity and allowed an improvement in living standards beyond that consistent with sustainable growth. At the same time, the apparent health of public finances promoted the false notion that social welfare expenditures could be allowed to expand without adverse economic consequences. The inadvisability of funding permanent increases in public spending programmes from volatile streams of tax revenue, emanating from the financial services and ancillary service sectors, was pointed out by one of the authors in a CPS pamphlet co-authored with Maurice Saatchi in 2000.

Latterly, the credit crisis and ensuing economic slump have punctured these fallacies, exposing the unsustainability of the UK's economic structure and leaving behind a gaping hole in the public finances. In 1976, Robert Bacon and Walter Eltis published a

provocative and well-argued thesis entitled *Britain's Economic Problem: Too Few Producers*. They highlighted the situation where the surplus-producing sectors of the economy had become too small to sustain the surplus-consuming sectors. The key insight, following François Quesnay, was that everyone who produces anything that is marketed – sold into a commercial market – produces a potential surplus:

“Quesnay, a farmer's son, believed that agricultural rents provided the surplus which supported the Court at Versailles, the French aristocracy, the armed forces and the church. Their often luxurious consumption depended on the surplus that the farmers produced, but agriculture could only produce enough to buttress the Ancien Régime if the farmers used expensive farm capital. Without this, they could only produce enough to feed themselves, with nothing left over for the Court, the church and the aristocracy.”

Quesnay correctly predicted that the French monarchy was in a vicious cycle, taxing the farmers to the point where they were forced to sell their farm capital and reduce their production. Its collapse duly arrived in 1789.

Once the non-market sector of the economy, loosely defined as the activities financed directly or indirectly by the public sector, has become too large, the temptation of politicians is to raise taxation in order to finance the bloated expenditures. However, the effects of a higher tax burden on the surplus-producing sectors tend towards the dissipation of effort, the reduction of profitability and of re-invested private capital. In the end, the inability to finance replacement fixed investment reduces the productive potential of the economy and living standards decline across the board.

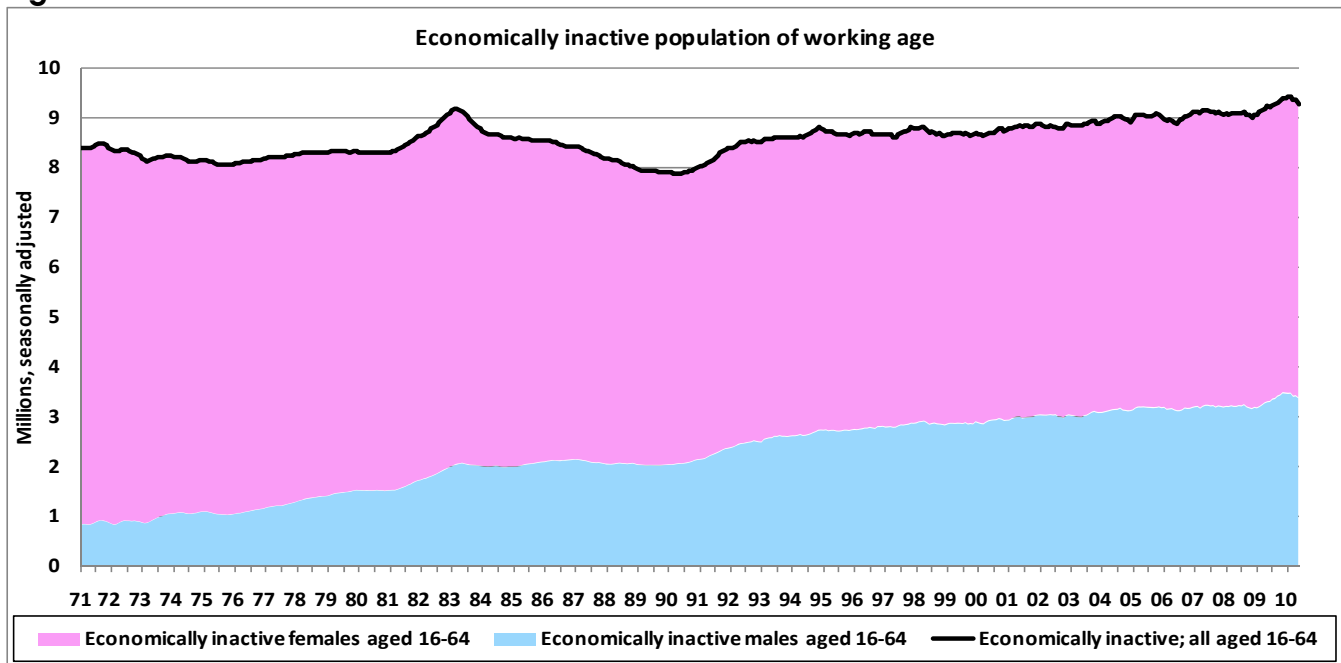
The challenge – to boost the UK’s producer surplus – that Bacon and Eltis posed was accepted by the Conservative Government that took office in 1979. Its programme of liberalisation and privatisation brought about a transformation of the supply potential of the UK economy. This transformation was effected by the transfer of economic decision-making from the state sector to the commercial sector and the replacement of state-run oligopolies and monopolies with more competitive market structures.

In 2010, the path to a more productive economy lies primarily in a transformation of households, rather than industries and firms. Socialised households need to be returned to the private sector as a matter of urgency. For more than 20 years, the UK has had far too many unproductive households but the economic slump has aggravated the situation. In the year to April-June 2010 the number of workless working age households rose by 4% to 3.9m, or 19.2% of all working age households. These workless households contain 5.4m adults (58% of all

inactive adults) and 1.9m children. The economic slump has returned us to a rate of worklessness last recorded in 1999.

Of all the avenues open to the UK to break free of the supposed speed limit of a 2.25% trend annual growth rate (as assumed by the Office for Budget Responsibility), the scope for a substantial improvement in household workforce participation and productivity must rank high on the list. If 10% of workless households were transferred to the ranks of all-working households, this would swell their numbers by 3.2%. Even if these households were initially only half as productive as existing working households, this would add more than 1% to GDP. In particular, the low levels of male working-age economic activity, as compared to 30 or 60 years ago, represent both a huge challenge and a remarkable opportunity: the mobilisation of even 250,000 inactive males of working age would add 1% to the employed workforce.

**Figure 1**



Source: Labour market statistics, Office for National Statistics

## 2. INACTIVE PEOPLE AND WORKLESS HOUSEHOLDS

The expansion of the UK economy between 1992 and the onset of the credit crisis in 2007 owes a great deal to the growth of households in which everyone works. These all-working households increased from 50% of all households in Spring 1992 to 58% in Spring 2007, receding to 54% in Spring 2010.

**Table 2: UK household employment rates (%)**

<b>Old basis</b> (Aged 16-59/64)	Spring 1992	Spring 2007	Spring 2010
WWAHs	17.4	16.0	17.4
HWAHs	32.2	25.9	28.5
AWAHs	50.4	58.1	54.1

Notes: Data does not allow for the change in female state pension age or the new method of imputation for non-responders.

<b>New basis</b> (Aged 16-64)	Spring 2007	Spring 2009	Spring 2010
WWAHs	17.5	18.5	19.2
HWAHs	26.5	27.7	27.8
AWAHs	56.0	53.8	53.0

Notes: Data covers those aged 16-64 for both men and women. The imputation of non-responders has also been modified. At the time of publication revised data was only available for the second quarter from 1997 onwards. For more information visit: <http://www.statistics.gov.uk/cci/article.asp?ID=2346>

1992 was the date that the ONS first undertook detailed analysis of employment by household.

WWAHs: workless working age households  
 HWAHs: hybrid working age households  
 AWAHs: all-working working age households  
 Source: ONS, *Work and worklessness among households* 2010. <http://www.statistics.gov.uk/pdfdir/work0910.pdf>

By 2007, over 70% of all employment income was concentrated in fully employed households. This proportion receded over the first two years of the credit crisis, but is likely to regain the lost ground as the economy recovers from the slump.

### *Strong second earner incentives*

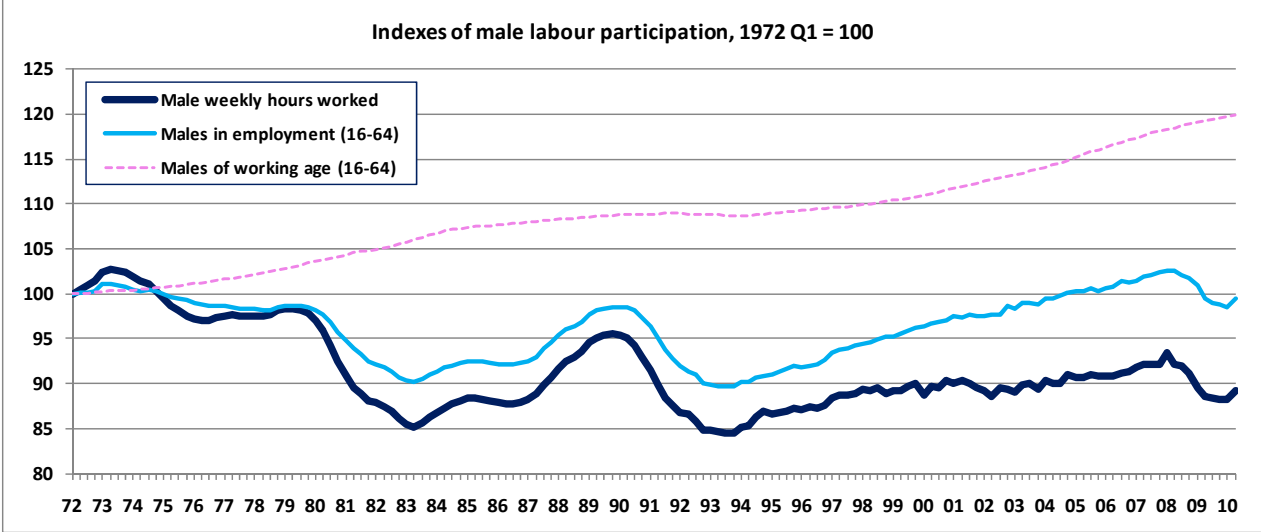
An important explanation of the concentration of work in all-working households is the comparative reward to labour for a subsequent earner as compared with a sole earner. Once the first worker has negotiated the unemployment and poverty traps, the second worker faces a more palatable marginal deduction rate (income tax and National Insurance) of around 30%, as compared with the 70%-plus rates for the first earner.

In parallel to the concentration of work and earned income in all-working households, it is clear that the incremental employment in these households has accrued to females rather than to males. The male share of total weekly hours worked peaked in 1973 at 72.3%. By 1992, it had fallen to 64.4%; by 2007, the share had dropped to 62% and in the second quarter of 2010, the share was 61.2%.

Behind this rebalancing lies a sombre reality: total weekly male hours worked have declined by more than 13% since 1973 despite a 19.5% increase in the male population of working age during these years (figure 2). Male working age economic activity rates fell by 2.8 points between 1992 and 2007, including a 13.6 point drop for those aged 16-17 and a 5.4 point decline for the 18-24s. Activity rates for over-50s males have risen marginally over this time span. These patterns contrast with the progressive trends in female labour participation (see figure 3).

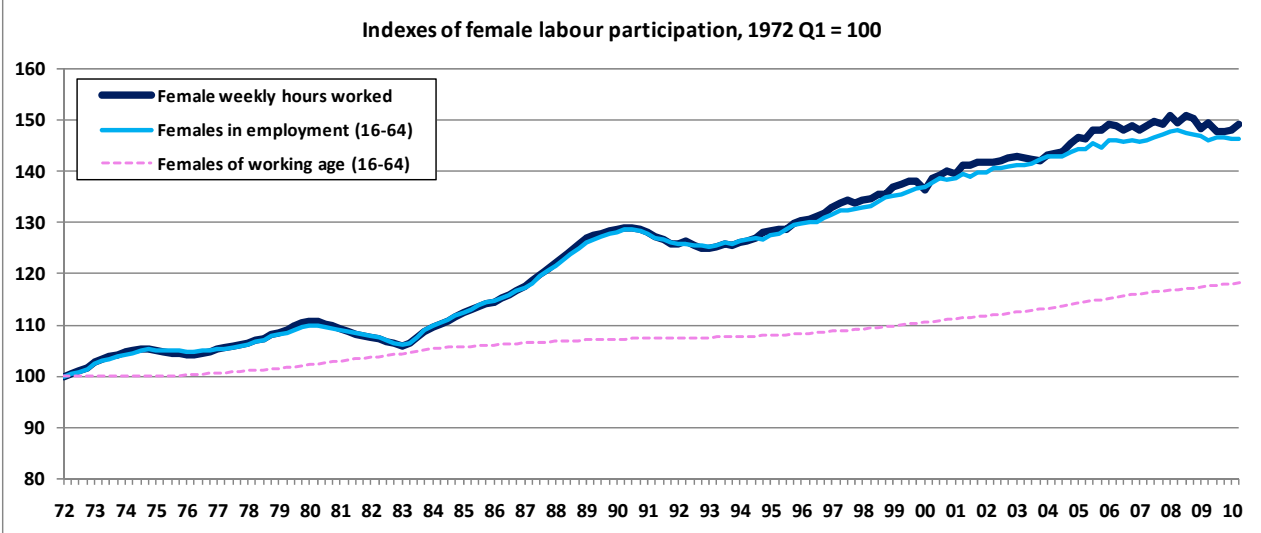
At the heart of the WWAH phenomenon are entrenched patterns of worklessness among young males, despite a long, unbroken sequence of economic growth. In the 2008-09 Family Resources Survey it was revealed that the unemployment rate among 16-24 year-old men was 12% on the ILO definition with a further 4% inactive and not in full-time education. Among these unemployed, 42% had never worked, 7% had not worked for more than two years and a further 7% had not worked for more than a year.

**Figure 2**



Source: Labour market statistics, Office for National Statistics

**Figure 3**



Source: Labour market statistics, Office for National Statistics

### **3. POSSIBLE EXPLANATIONS OF WORKLESSNESS**

Plausible explanations of worklessness in working-age households include:

1. Changing occupational structures that discriminate against unskilled and less-skilled labour, and with a disproportionate adverse effect on male employment.
2. Changing patterns of employment with expansion in knowledge-based employment skewed to southern and eastern England.
3. Increased competition for low-skilled work from migrant workers, especially from Eastern Europe.
4. Changes to the tax and benefit structure that make entry-level jobs less rewarding and which penalise individual effort with punitive marginal deduction rates.
5. Loss of stable household structures that support continuity of employment.
6. Persistent low levels of basic skills (literacy and numeracy) in poorer households.

Worklessness, particularly among working-age males, has afflicted most western industrialised economies in the past 30 years and vast resources have been deployed in its analysis and attempted remedy. There are helpful lessons to be learned from the experiences of other countries, but there are also UK-specific aspects to the worklessness phenomenon that demand bespoke solutions.

### **4. VARIATIONS IN WORKLESS HOUSEHOLDS**

In terms of workless households, the UK displays some dramatic contrasts between household types, ethnic origins and geographic regions. For example, the incidence of household worklessness in Spring 2010 was 5.4% for couples with dependent children but 39.7% for lone parents with dependent children.

There were also strong ethnic variations (determined by the ethnicity of the head of household): 11.1% of households of Indian origin were workless compared to 30.8% of black African households.

Regional variations were similarly strong: 14.2% of households in the South East of England were workless, compared to 24.3% in the North East.

Despite these marked contrasts, there are striking similarities between many workless households: they seem frequently to lack the basic social infrastructure, and the capital, to hold down a job for any length of time; much less to assist the rising generation in meeting the challenges and disciplines of regular employment.

### **5. HOW GOVERNMENT POLICY REDUCED SOCIAL MOBILITY**

Despite numerous government initiatives and huge expenditures (£75 billion for various tax credit schemes and New Deal projects since 1997) designed to reduce youth unemployment, it is even more prevalent in 2010 than in 1997. For 16-17 year olds, the unemployment rate was 33.1% in the second quarter of 2010 compared to 20% in 1997 quarter two. For the 18-24 age group, the increase is from 13.1% to 17.5%. Indeed, to the extent that social mobility occurs as a result of innate ability, then a number of policies pursued in the UK in the past 20 years have been misconceived. For example, the Labour Government:

- greatly expanded the size of public administration, creating more “middle class” jobs;
- raised the tax burden and the generosity of welfare benefits (including tax credits) thus creating additional dependency on the state through deepening the poverty trap.

Empirical studies also indicate that there is an inter-relationship between worklessness, social disintegration and the incidence of criminal activity and drug use. While living in a dysfunctional household, having a criminal record and/or a drug addiction constitute serious obstacles to finding and sustaining employment, long spells of unemployment or inactivity also contribute to these negative social attributes.

Labour MP Frank Field, head of a new independent review of UK poverty, commented last year that:

“The record of each of the New Deals is depressing, in particular the government’s flagship New Deal to end youth unemployment.... At the top of the boom, two-thirds of New Dealers failed to find and remain in a job for at least 13 weeks.”

If the economic and social potential of these under-25s is to be salvaged – and their contribution to the wider economy fulfilled – then some drastic re-thinking of employment options for young people is required. Harder still is the challenge of rescuing older people, particularly men, from lifetimes of intermittent or non-existent work.

In a recent review of the effectiveness of welfare-to-work policies in the US, Lawrence Mead, professor of politics and public policy at New York University summarised what had been learnt from 30 years of US attempts to tackle the problem of getting poor men into work.

“The key was... to change the nature of government in order to have it focus on employment. We also had to shift away from thinking in terms of rights and freedoms towards thinking in terms of obligation, linking benefits with work requirements, help not hassle... .. It does appear that for men, unlike women, we probably have to guarantee work in some form...”

The policy challenge is thus to reattach unproductive and poorly-performing households to the private sector economy through the use of local programmes, appropriate incentives and microeconomic initiatives, but also through the reinstatement of the moral obligation to accept offers of suitable work. In plain terms, this requires paid work not only to be more plentiful and economically worthwhile for all working age adults, but also to be the confident expectation of every school leaver and university graduate.

## **6. STRATEGIES TO REDUCE INCIDENCE OF WORKLESS HOUSEHOLDS**

### ***a. Household consolidation, not proliferation***

There is an important respect in which households differ from businesses: generally speaking, the greater the number of private enterprises per head of population, the better its economic health, if not necessarily its productivity or profitability.

For households, the same cannot be argued. The proliferation of households in the post-war period, in relation to the size of the adult population, should be viewed with concern. The expansion in the number of working-age households (reflected in figure 4 overleaf) has many explanations – increased prosperity, social disintegration and familial alienation – but a common implication. Households with fewer members represent less proficient economic units, implying greater duplication of physical infrastructure and less social infrastructure available to support stable employment patterns.

There is also now much evidence that the traditional family unit does tend to secure better economic outcomes, including higher educational attainment, lower levels of crime, better health and higher standards of living.

In addition, contrary to received wisdom, capital formation in the form of dwellings is a comparatively unproductive use of scarce resources. Over the past 30 years, an increasing

proportion of the increase in the net capital stock has been devoted to private house building in order to accommodate the proliferation of very small households.

The recent unsustainable improvement in living standards reinforced the trend towards smaller households. If, as seems likely, aggregate real personal disposable incomes stagnate over the next few years, or even recede, then household consolidation offers a way of stretching real income through shared consumption of amenities.

The re-direction of net capital formation from new dwellings towards business investment and infrastructure renewal will take time to bear fruit in a higher growth rate of productive potential. However, it could form an integral part of the UK higher growth strategy.

**b. Strengthening the basic social infrastructure**

To aid the ability of individuals to meet the challenge of holding down a job, creative solutions are needed to improve the basic social frameworks that they lack. Various strategies are possible. One model might involve the construction of enterprise parks adjacent to housing estates where worklessness is rife. Another is the development of mentoring

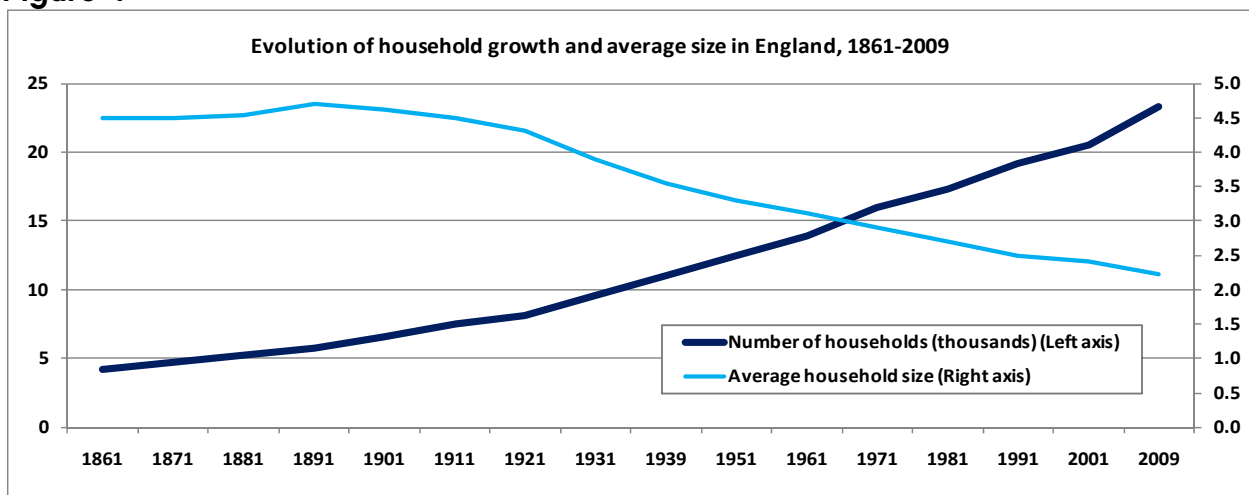
schemes that bridge the gulf between full-time education and training, and full-time continuous employment. The objective is to make it easier for alienated individuals to sustain the employment opportunities that come their way through the provision of social infrastructure and other forms of support that are lacking currently.

**c. Improving the rewards to paid employment**

Marginal withdrawal rates can be as high as 95% for some households. This clearly removes much incentive for workless households to find employment.

The Coalition Government's proposals to increase the individual tax allowance to £10,000 will take millions of low-income individuals out of the income tax and National Insurance systems altogether. Their total deduction rates derive only from the withdrawal of tapered welfare benefits in the lower income ranges. This will do much to encourage the re-entry of low earners into employment. Similarly, simplification of the benefit system along the lines currently proposed by the Coalition is also essential if the advantages of paid employment are to be clear to workless households.

**Figure 4**



Source: Department for Communities and Local Government

<http://www.communities.gov.uk/housing/housingresearch/housingstatistics/livatables/>



#### ***d. Generating more manual employment***

There has been a noticeable decline in the proportionate commitment of UK net investment to manufacturing, utilities and extractive industries, particularly in the past two decades, as these activities have migrated overseas.

In many industries, the outsourcing and offshoring of production may well be permanent. While global competitive pressures offer one reason for the relocation of certain economic activities abroad, this falls short of a complete explanation. For example, it is far from clear why the UK remains in persistent non-fuel materials deficit when the country has ample reserves of mineral and coal deposits and under-utilised arable land: relative prices of materials and food look set to continue on rising trends. Domestic extraction of biomass, minerals and coal has declined almost 40% since the 1973 peak. 70% of the nation's coal requirements are now imported. While some moves have been made to reactivate coal mines in the country, it should be recognised that these sectors have the capacity to deliver the much-needed diversity of employment opportunity.

#### ***e. Local, not central, support***

Benefit levels, welfare programmes, wages (for many public sector employees) and labour market programmes are mostly set nationally. As a result, they tend not to reflect local variations in employment patterns and cost of living across the country.

Local benefit and unemployment programmes could be far more effective. Efficient local authorities can respond to local needs and opportunities far more quickly and effectively than any national effort. It is essential that local authorities share in any success they have in encouraging their workless residents back into work.

## **7. POLICY SUGGESTIONS**

### ***Policies to support entry into the labour market***

- While the Labour Government's New Deal policies were not successful, other OECD countries have had far greater impact with active labour market policies. Recent experience (such as that reviewed by Mead and Llewellyn) suggests that, to be successful, sanctions need to be imposed on claimants for non-compliance with, for example, retraining programmes.
- Introduce greater regional pay flexibility for public sector employees in order to help to address the geographical contrasts in worklessness.

### ***Policies to remove the bias against marriage***

- Remove the penalisation of couples in the tax and benefit system and incentivise marriage.

### ***Policies to restore incentives to employment***

- Encourage local authorities to target those households which have the worst long-term employment records with a full package of intensive support. Bringing individuals from these households into the labour market could, while being expensive initially, pay great dividends both in reduced welfare and social costs. As noted above, it is essential that successful local authorities share in the success of their efforts.
- Restructure the personal income tax and National Insurance systems to favour the returns to low-paid work.
- Curtail entitlement to benefits, including housing benefits; restrict income range over which working tax credits can be claimed; introduce time-limits on spells of unemployment and other benefits; introduce lifetime limits; and limit the maximum amount of benefits paid to a single household, according to composition.

***Policies to regenerate employment opportunities in the lesser-skilled occupations***

- Expand local public-private partnerships for regeneration activities such as housing renovation and environmental improvement. These partnerships could offer significant numbers of local apprenticeships and trainee jobs (which have waned in recent years).
- Encourage project-based employment, including open-door projects where there is less insistence on formal work disciplines. These could be more tolerant workplace environments for those who face additional difficulties in engaging with the world of work, with the aim of moving people on to more formal settings later.
- Review regulation with a view to reducing restrictions on outdoor employment. This could generate employment opportunities in agriculture, forestry, fishing, quarrying and other land-based industries. A further benefit could be to reduce and ultimately eliminate the UK's materials trade deficit.
- Encourage greater exploitation of the UK's mineral wealth.
- Reduce immigration of low skilled workers wherever possible.

***Policies to facilitate the transition to regular work***

- Implement a pilot scheme of enterprise parks located adjacent to large housing estates with a high incidence of worklessness. The aim will be to ease the transition into full-time work. Businesses would be given incentives to locate to these parks, which would serve a dual role as training facilities. Enterprise parks would offer lengthy work experience placements for students in their final two years of full-time education. These parks would also contain clusters of serviced offices and workshops to encourage their use as an alternative to long-distance daily commuting.

**CONCLUSIONS**

There can no longer be any pretence that a booming economy will solve the structural problem of worklessness which has plagued the UK for more than 20 years, much less an ailing economy. As more paid employment became available between 1992 and 2007, the jobs and the incomes accrued disproportionately to working households.

A new approach is required, which targets the expansion of employment opportunities in reasonably paid entry-level jobs using local agencies and initiatives, funded entirely from the social security budget.

The failure of the New Deal in placing young people into continuous employment brings great urgency to the task. If there is to be a single priority for long-term growth, the objective must be to offer a choice of jobs to all school leavers, who have decided not to continue their formal education, with a stronger moral obligation on the students to accept one of the jobs on offer. The cycle of worklessness must be broken at every stage of working life, but particularly at its very beginning.

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## THE AUTHORS

Peter Warburton is Director of Economic Perspectives, an international consultancy, and economist at Ruffer LLP, an asset manager. He was previously the economic adviser in the equity research division of Chase Manhattan, having joined Robert Fleming in 1989 as Chief Economist. He is a member of the Shadow Monetary Policy Committee at the Institute of Economic Affairs; is the author of *Debt and Delusion* (Penguin, 1999); and is the co-author (with Maurice Saatchi) of *The War of Independence* (Centre for Policy Studies, 1999), *The Bad Samaritan* (CPS, 2000) and *Poor People! Stop Paying Tax!* (CPS, 2001).

Joanna Davies is a Research Economist at Economic Perspectives Ltd. She graduated from the University of Kent in 2009 with an honours degree in Economics and Criminology.

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978-1-906996-28-4

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