Where are the Workers?

A new diagnosis of economic inactivity in Britain

BY KARL WILLIAMS

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Introduction

In his Budget speech on Wednesday, Jeremy Hunt is widely expected to focus on the problem of economic inactivity.[1] The reason is simple: this has become one of Britain's most pressing economic problems.

There are currently 516,000 more inactive people aged 16-64 than was the case pre-pandemic. The total now stands at 8.89 million – around 21.4% of the potential workforce.

The UK is also an international outlier. In most countries, economic activity has fallen significantly since the pandemic. Only seven other OECD countries seen it rise, and only three have seen it rise more quickly than the UK – and of those three, only one is an advanced economy similar to our own.

This is happening at a time when the total number of job vacancies across the UK economy stands at over 1.1 million, still 42% above pre-pandemic levels. The inability of employers to fill vacancies is arguably the main constraint on short-term economic growth.

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Why is this happening? Two damaging myths have arisen in recent months. The first is that this is exclusively a problem of the elderly – to the point where the House of Lords Economic Affairs Committee explicitly excluded younger cohorts in its otherwise excellent recent study of the problem. The second is that it is driven by the impact of the pandemic, and in particular the strains that it has imposed upon the NHS. Those leaving the workforce, under this argument, are predominantly the long-term sick, who cannot get the treatment they need because of the mess, or so it is alleged, that the Government has made of the health service.

This paper will argue that the truth is far more complicated. For example, while the 50-64 age cohort does account for more than 60% of the increase in economic inactivity, this is driven as much by financial circumstances and early retirement as by the performance of the health service. Changing pension rules that discourage people from working is a key part of the solution here. In particular, we need to raise the pension lifetime allowance (LTA), which is now 60% lower in real terms than in 2010.

1 C. Wheeler & H. Yorke, 'Rishi Sunak's Budget Big Bang to keep us all working past 50', The Times (5 March 2023). Link.

Meanwhile, though the numbers are smaller, it is the 18-24 group that has actually seen the largest increase in its inactivity rate, and which stands to suffer the worst long-term damage to its prospects as a result – despite the focus on people remaining in higher education, the number of 'NEETs' rose by 28% in Q4 2022, by far the sharpest increase on record. We show that youth inactivity is being driven not just by the pandemic but by an alarming increase in the proportion of young people suffering from mental health issues. This is part of a wider rise in measured disability, which has been driven in part by the structure of the benefits system.

'In total, there are around 400,000 more working-age men economically inactive now than pre-pandemic, and around more 116,000 women – a 77:23 split'

Furthermore, there is a clear and alarming gender divide in terms of how inactivity has developed since the onset of the pandemic. In total, there are around 400,000 more working-age men economically inactive now than pre-pandemic, and around more 116,000 women – a 77:23 split.

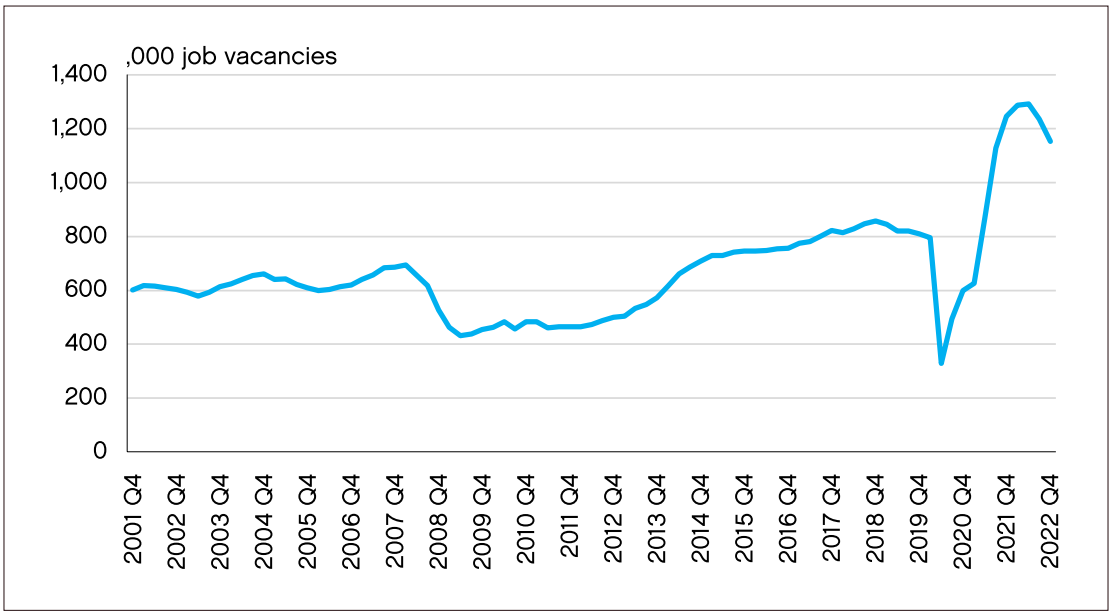
We need to ensure that rising inactivity remains a transient or cyclical problem, rather than becoming a persistent or structural issue. However, there is no silver bullet – no simple incentive or reform – that is going to get people back into work. Rather, we need a whole range of solutions to address the very different drivers of inactivity in different parts of the economy.

1. Where have the workers gone?

Britain has got a jobs problem – or rather, a vacancies problem. Put simply, there are far more jobs than there are workers. And this means we have a growth problem and an inflation problem too.

According to the latest ONS data, the total number of (seasonally adjusted) job vacancies across the UK economy stood at 1.15 million in Q4 2022.[2] This was down by 11% on the record 1.29 million vacancies recorded in Q2 2022, but still well above pre-pandemic levels: 42% higher than in Q4 2019 (0.81 million) and 76% higher than the average in the decade since the financial crisis (0.66 million). There is a severe supply-demand imbalance in the labour market. Indeed, ONS surveys consistently show more firms having problems recruiting the staff they need than intending to lay them off.[3]

Vacancies in the UK by quarter (seasonally adjusted)



This state of affairs is obviously a constraint on economic growth. If an employer cannot find a suitable worker to fill a vacancy, they will be unable to grow their business, and may even have to scale back existing operations, supplying less of the goods and services consumers want. These consumers may include other business further along the supply chain, so the bottleneck effect of an unfilled job can cascade through the economy.

2 ONS, 'UK Vacancies (thousands) – Total' (14 February 2023). Link. Vacancies are defined as positions for which employers are actively seeking recruits from outside their business or organisation, and a job as an activity performed for an employer or customer by a worker in exchange for payment. Note that the number of jobs is not identical to the number of people in employment, as of course a person may have more than one job.

3 ONS, 'Business insights and impact on the UK economy' (23 February 2023). Link.

In time, investment in productivity-enhancing technologies can substitute for labour in many areas, and indeed, this is crucial for long-run economic growth. But right now, with Britain facing recessionary headwinds,[4] this is of scant comfort.

Ahead of Jeremy Hunt's Bloomberg speech on the economy, his colleague Michelle Donelan claimed that unfilled roles were holding back £100 billion of growth.[5] Taking that number at face value, filling these vacancies would add around 4.5% to annual GDP. Perhaps more realistically, getting vacancies back down to pre-pandemic levels would still add 1.3% to GDP – enough to swerve a recession.

'Ahead of Jeremy Hunt's Bloomberg speech on the economy, his colleague Michelle Donelan claimed that unfilled roles were holding back £100 billion of growth'

There is also the inflation angle to consider. Barring further geopolitical shocks, the outlook is reasonably encouraging. The UK money supply is tightening, energy markets are adjusting (helped by a mercifully mild winter) and with China having ditched its zero Covid policy, supply chain disruptions are expected to ease further.[6] The OBR forecasts inflation falling back to around 7% by mid-year, and to under 2% by the same point next year.[7] Meanwhile, markets expect the Bank of England base rate to top out at under 5%.[8]

But the labour market is the fly in the ointment. While a full-blown 1970s wage-price spiral seems unlikely, there is a real risk that labour shortages will continue to feed through into higher prices for some time, slowing down the rate at which inflation falls and prolonging the cost of living crisis. That is partly why the Government is right to resist exorbitant public sector pay demands, even though – emboldened by a tight labour market – striking unions are further constraining economic output and deepening the general sense of malaise.

What are the root causes of the imbalance in the labour market?

One factor is undoubtedly pent-up consumer demand from the pandemic. Households had accumulated an extra £200 billion in savings by June 2021, with the household savings ratio – the proportion of disposable income not spent on consumption – peaking at 27.8 in Q2 2020, double the previous record.[9] The vaccination programme and the ditching of pandemic restrictions then unleashed a tidal wave of savings into the wider economy – at last people could enjoy a meal out with friends, go on holiday, get a haircut, go shopping, have a nice day out and so on.

The result was a classic case of too much money chasing too few goods and services. As businesses sought to meet the rush of consumer demand, job vacancies

4 IMF, 'Projections Table', World Economic Outlook: Update (January 2023). Link.

5 J. Hunt, 'Chancellor Jeremy Hunt's speech at Bloomberg' (27 January 2023). Link.

6 K. Williams, 'The Bleak Midwinter: the impact of the energy Price Crisis', CPS Economic Bulletin (September 2022). Link.

7 OBR, 'Overview of the November 2022 Economic and fiscal outlook' (17 November 2022). Link.

8 BoE, 'Yield curves' (06 March 2023). Link.

9 ONS, 'Households (S.14): Households' saving ratio (per cent): Current price: £m: SA', UKEA (22 December 2022). Link.

soared. In this respect, the UK was far from an outlier – the same pattern was seen across many developed economies.[10] Churn as people moved jobs and switched careers post-furlough also probably helped to boost vacancies for a time.

However, heightened employer demand for employees only goes so far in explaining the persistently high level of vacancies, given the cost of living pressures on consumer spending over recent months. As the House of Lords Economic Affairs Committee and other authorities have noted,[11] 'reduction in labour supply… is probably playing a more significant role than pent-up demand and churn'.[12] **Indeed, the real challenge for Britain almost certainly lies on the supply side of the equation.**

Several factors have been adduced as explanations for labour supply shortages in the UK. One is, inevitably, Brexit – on the basis that it can be blamed for just about everything these days.

It is true that many EU workers returned to their home countries, and that the Brexit deal made it harder for unskilled EU workers to live and work in the UK. But given the Government's generous approach to legal immigration, this cannot be the whole story. After all, net migration is higher than it has ever been, even excluding Ukrainian refugees and Hong Kong BN(O)s.[13]

> **'So while motivated reasoning is leading some people to blame labour shortages and hence record vacancies primarily on Brexit, in reality we have to be more nuanced than that'**

It is true that there has been a change in the composition of immigrant workers. Under the new points-based system, many of those arriving are classed as 'skilled', and work in different sectors to those which employed large numbers of EU labourers, such as agriculture and logistics. This is causing some friction. However, businesses which previously relied on cheap, unskilled migrant labour are in the process of adapting to this new reality, according to the Migration Advisory Committee's 2022 annual report.[14]

The MAC has also noted that 'the pattern of increasing vacancies is consistent with other developed nations… suggesting that whilst ending Freedom of Movement (FoM) may have contributed to higher vacancies, or at least slower turnover, it is not the sole cause'.[15] **So while motivated reasoning is leading some people to blame labour shortages and hence record vacancies primarily on Brexit, in reality we have to be more nuanced than that.**

Another supply-side factor, highlighted by the Centre for Policy Studies at the start of 2022, is a change in how people generally weigh the desirability of certain

10 OECD, 'Registered Unemployed and Job Vacancies' (6 March 2022). Link.

11 Including the ONS and, if reports are to be believed, the OBR.

12 House of Lords Economic Affairs Committee, 'Where have all the workers gone?' (20 December 2022). Link.

13 See for example analysis in: N. Timothy & K. Williams, 'Stopping the Crossings' (December 2022), pp.18, 23-4. Link.

14 MAC, 'Annual Report' (December 2022). Link.

15 Academics at the Oxford University based Migration Observatory have also come to a similar conclusion.

jobs and career paths in the wake of Covid.[16] It would be surprising if there were not a lingering aversion to working in sectors such as hospitality, high street retail, transport and tourism, given how they were hammered by restrictions. What we could be witnessing, in other words, is 'a permanent structural shift towards a post-Covid economy', to which business owners would have to adapt.[17]

However, probably the most significant cause of labour shortages and hence record job vacancies is a massive and persistent increase in economic inactivity, which is almost unique to Britain.

> **'The UK still has a lower inactivity rate than the OECD total (26.8%) or median (22.7%), not to mention G7 countries such as Italy (34.4%), France (26.3%) and the US (25.9%). But since the pandemic, the numbers have moved sharply in the wrong direction'**

At 75.6%, the employment rate in the UK is still one percentage point lower than it was before Covid, according to ONS data.[18] In a normal economic cycle, that would tend to mean a rise in unemployment. But due to the Government's furlough scheme, large parts of the economy were artificially preserved in aspic through the pandemic. The unemployment rate eventually peaked at 5.2% – far lower than in the wake of the financial crash. Post-pandemic, it has fallen to under 4%, a level last seen in the early 1970s, during the Barber Boom.

Instead, we are today seeing people dropping out of the labour market altogether, becoming 'economically inactive'.

People are classified as economically inactive when they are of working age but are neither in work nor actively looking for work.[19] This group can include students, the short- or long-term sick, early retirees, people with care responsibilities and even the just plain apathetic.

Overall, the UK still has a lower inactivity rate than the OECD total (26.8%) or median (22.7%), not to mention G7 countries such as Italy (34.4%), France (26.3%) and the US (25.9%). But since the pandemic, the numbers have moved sharply in the wrong direction. Around 21.4% of the workforce – just under 8.9 million out of 41.6 million people aged 16-64 – are now classified as economically inactive. This is down slightly from a peak of 21.7% in early 2022, as a record number of people moved from inactivity into work between Q3 and Q4 2022, probably because of cost of living pressures. However, the rate of inactivity was still 1.2 percentage points higher than before the pandemic.[20]

To put it another way, there are 516,000 more economically inactive people than there were just before the pandemic in absolute terms, and around 483,000 adjusting for population changes. If all of these people were to enter the labour

16 K. Williams & R. Colvile, 'Is There Any Money Left?: The UK Economy After Covid', CPS Economic Bulletin (February 2022). Link.

17 R. Colvile, 'Never mind the by-election bloodbath – it's Rishi who faces a real nightmare', The Times (19 December 2021). Link.

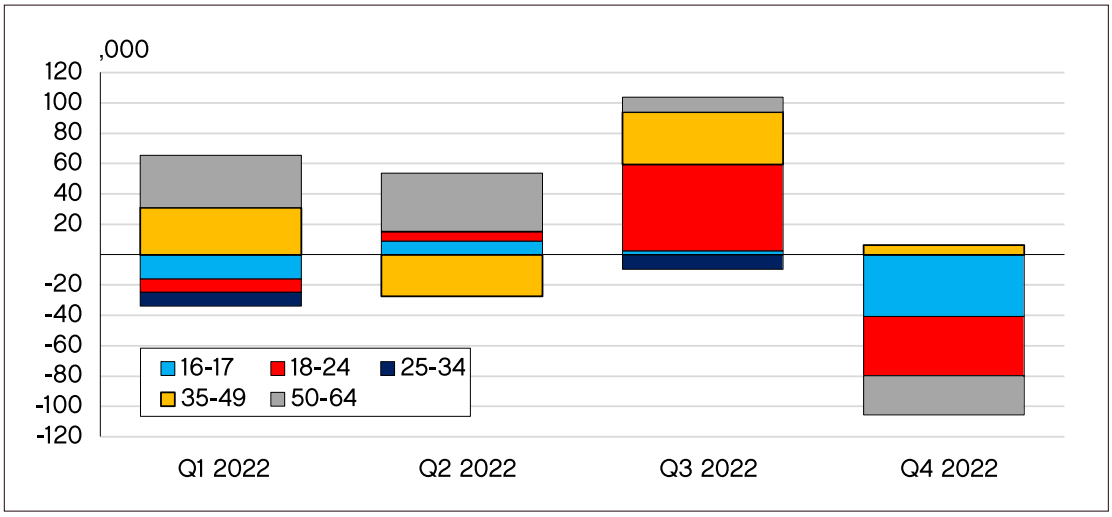
18 ONS, 'Labour market overview, UK: February 2023' (14 March 2023). Link.

19 The precise definition used by the ONS is: 'People not in employment who have not been seeking work within the last 4 weeks and/or are unable to start work within the next 2 weeks'.

20 Note that ONS labour market data is seasonally adjusted.

market and find a job, the number of job vacancies would more than halve, to below pre-pandemic levels.

Quarter on quarter change in inactivity numbers in 2022



Yet even with the jobs market overheating so intensely, these people are unwilling or unable to find work. This state of affairs has been dubbed the 'participation puzzle' by the ONS,[21] and has been identified by the Bank of England and many others as a major drag on growth, as well as a possible structural problem in the making.[22]

Again, Britain is very much an international outlier here. Pretty much every developed country saw an initial rise in economic inactivity during the ravages of the pandemic. But this generally proved transient. As the graph overleaf shows, most OECD countries now have a lower rate of economic inactivity than before the pandemic, as demand for workers surged during the economic bounce-back from Covid.[23]

Of the three countries where inactivity has increased more than in the UK, only Switzerland – a developed country with a large services sector – is really in any way comparable. In Switzerland there are high marginal tax rates and childcare costs which might be contributing to greater inactivity post-pandemic and which might have their parallels in the UK, but given how policies vary between cantons in Switzerland's extremely localised form of democratic government, it is hard to generalise.[24]

For the most part, there seem to be factors specific to the UK economy or workforce which are sustaining our relatively high level of economic inactivity. But this also suggests, reassuringly, that economic inactivity is amenable to policy solutions.

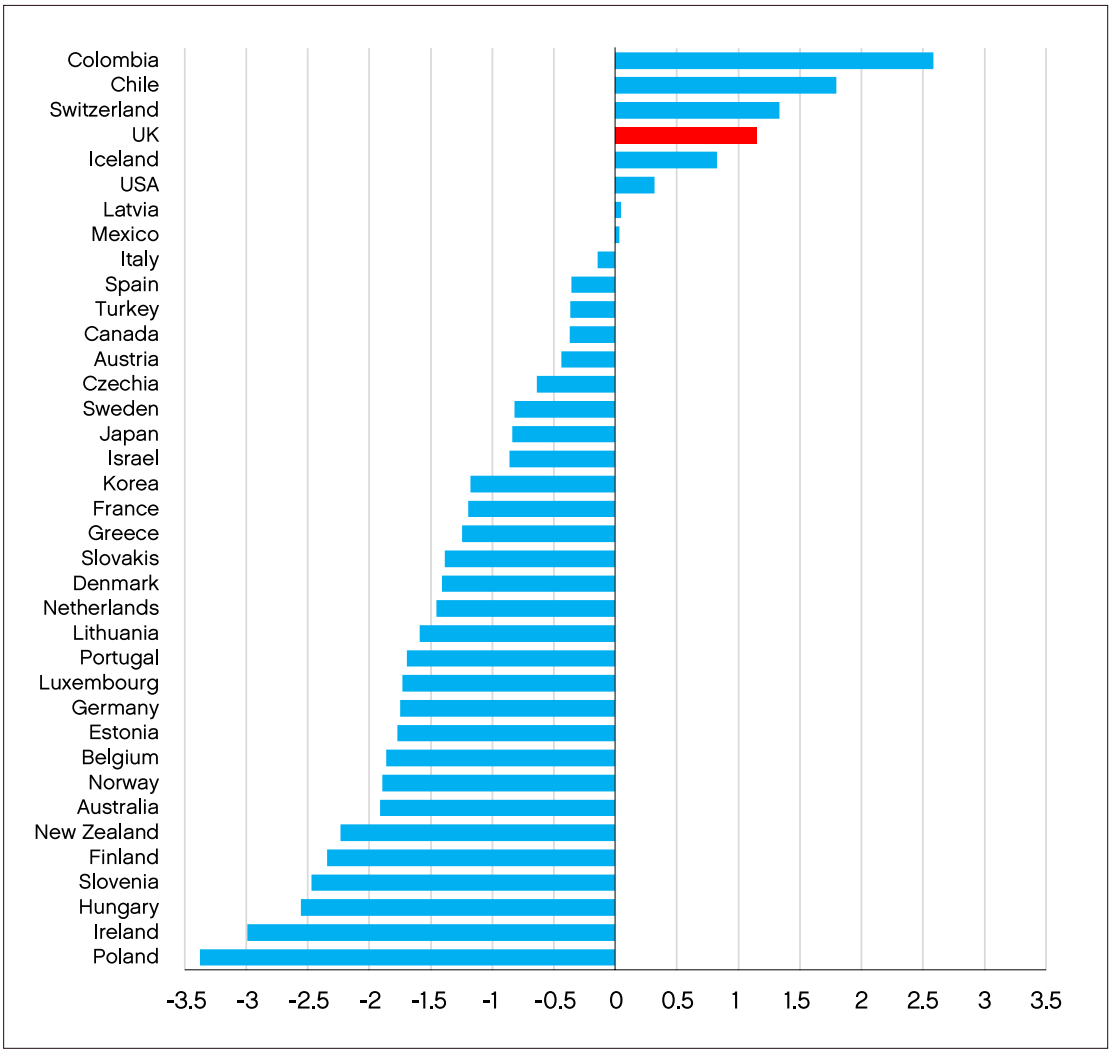
21 ONS, 'The participation puzzle', Worker movements and economic inactivity in the UK: 2018 to 2022 (19 December 2022). Link.

22 Reuters, 'Bank of England's Bailey speaks after interest rates rise to 4%', Reuters (2 February 2023). Link.

23 OECD, 'Inactivity Rates', Short-Term Labour Market Statistics (6 March 2023). Link.

24 OECD, 'Fostering a strong labour market to support the recovery and sustain growth', OECD Economic Surveys: Switzerland 2022 (20 January 2022). Link.

Change in economic activity, Q4 2019 to Q3 2022



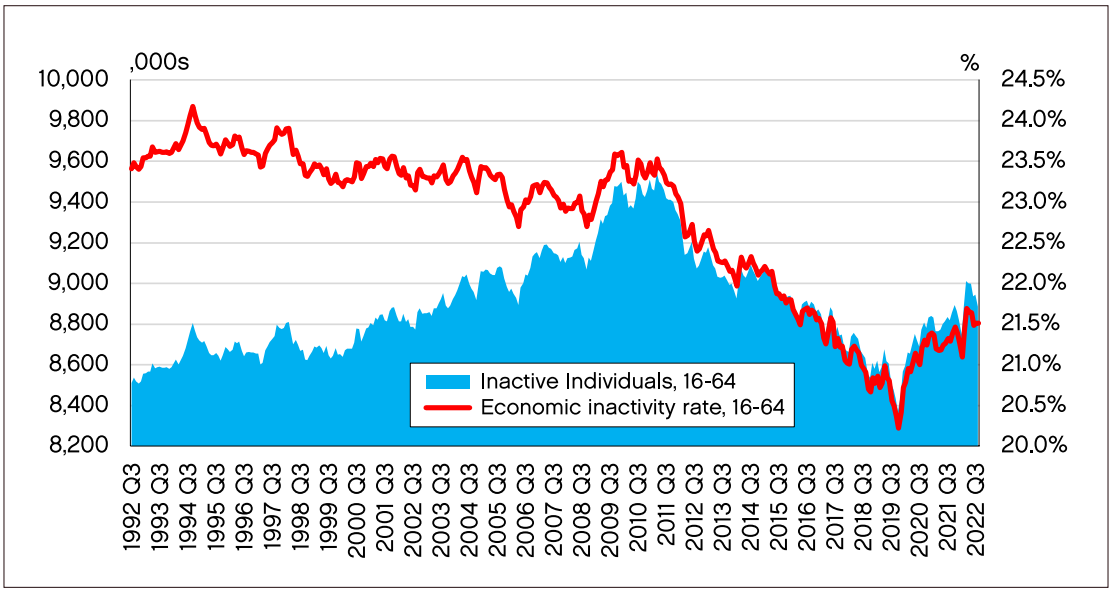
It is worth pausing here to consider the wider context. As mentioned above, the UK has traditionally been a strong performer in terms of economic inactivity. But demographically, as we shall see, we are always running up the down escalator.

From 2011 to 2019, the inactivity rate declined from around 23.5% to 20.2%, resulting in a million fewer economically inactive people and the lowest rate of inactivity in decades (and possibly ever, given greater female participation in the workforce). In 2019, the UK had a lower rate of economic inactivity than all but six OECD countries.[25]

But this came about despite multiple countervailing trends tending to push economic inactivity rates up. For example, raising the school leaving age to 17 in 2014 and then 18 in 2015 resulted in the inactivity rate among 16- to 17-year-olds rising from 65% to 70%. The lowering of the pensions cap (the Lifetime Allowance) from £1.8 million in 2011 to £1 million by 2015 may also have hastened the retirement of some older workers. And underlying everything is the ageing population, with numbers in older age groups, with lower rates of labour market participation in normal times, constantly increasing relative to people of prime working age.

25 Japan, New Zealand, Sweden, Netherlands, Switzerland and Iceland.

Economic inactivity, aged 16-64



Of course, one factor that helped to push down the economic inactivity rate was net migration averaging around 250,000 a year, largely due to freedom of movement rules for EU workers. Yet that cannot entirely account for the trend: the number of economically inactive people also fell in absolute terms, even as the population of England and Wales grew by 6.3%.

In fact, the key factor driving down inactivity and more than offsetting countervailing trends seems to have been the economic recovery and the welfare reforms begun in the Coalition era. It is easy to overlook this now, but low levels of unemployment and inactivity were genuine Conservative achievements in the years before the pandemic. Encouragingly, this also shows that policy can help with economic inactivity, at least for some people.

With that in mind, we can begin digging into what is driving the reversal of the long-term trend and the UK's singular experience with economic inactivity since the pandemic. Crucially, we need to look at who exactly has left the workforce and their reasons for doing so, insofar as we can – which means busting a few myths about who exactly the economic inactive are.

2. Who are the economically inactive?

There are three main ways we can slice the available data on economic inactivity in the UK – by age, sex and reason for inactivity. To some extent, the data allows us to cross-slice these categories too. In this section, we take a zoomed-out look at who has left the workforce, to identity the key demographics and get a sense of where our priorities should truly lie, in terms of getting people back into the workforce and boosting growth.

First though, we need to consider a slightly arcane point of data interpretation. The UK's working age population (16-64) is not static. Each year, around 735,000 64-year-olds turn 65, thereby shuffling out of the benchmark inactivity timeseries, while around 765,000 15-year-olds turn 16. On a quarterly basis, that's roughly 184,000 people exiting and 191,000 people entering the various datasets.[26]

> **'Each year, around 735,000 64-year-olds turn 65, thereby shuffling out of the benchmark inactivity timeseries, while around 765,000 15-year-olds turn 16'**

This inevitably has an effect on inactivity rates at the two ends of the age range. There are an increasing number of people who are choosing to work (generally part-time) beyond the state pension age – as of Q4 2022 the number stood at 1.40 million.[27] These workers are not captured by the standard inactivity statistics. Likewise, the state pension age itself is officially increasing, meaning that the population captured by 'working age' statistics will be shifting.

At the other end of the scale, those entering the timeseries will tend to have higher inactivity rates, simply because so many of them are in school, training or at university – the average inactivity rate is 67% for the 16-17 cohort, vs 27% for the 50-64 cohort. So all other things being equal, the fact that more young people are entering the dataset than old people leaving it will tend to mean that inactivity rates gradually increase.

This does not mean that Britain does not have an inactivity problem – with the inactivity rate at 21.4%, there are still 516,000 more inactive working-age people than before the pandemic, and the total number of working-age people not in the labour market stands at around 8.89 million. But we should be aware that there are

26 This calculation of course assumes that birthdays are uniformly distributed throughout the year, which is not the case. In reality, as the ONS notes, there is a slight peak in September, probably due to parents planning to have children at the start of the school year. However, the broad point still stands.

27 ONS, 'A05 SA: Employment, unemployment and economic inactivity by age group (seasonally adjusted)' (14 February 2023). Link.

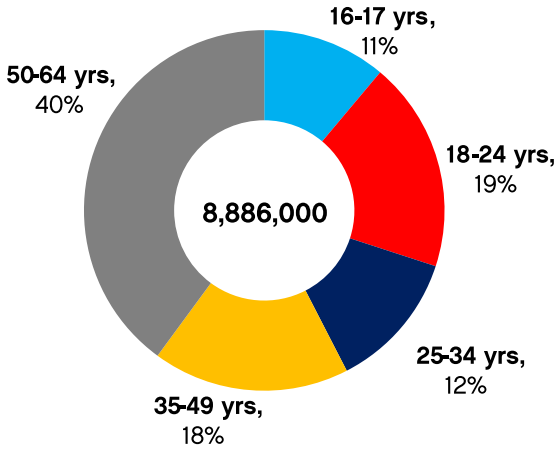
underlying shifts in the demographic composition of the workforce that do have an impact on the figures.

With that proviso, it is clear that **economic inactivity has always tended to be concentrated at either end of the age spectrum:**

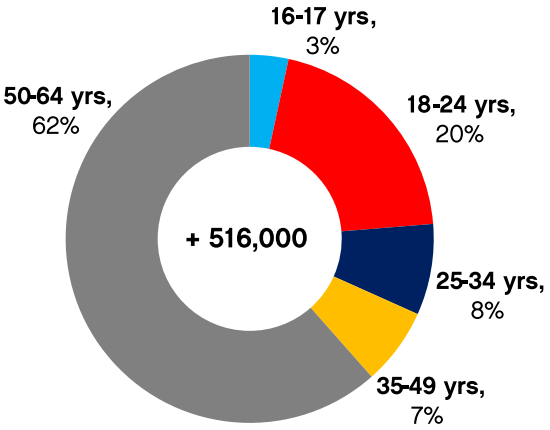
- The 50-64 cohort, with an inactivity rate of 25.2% before the pandemic and 27.1% now, accounts for 40% of the economically inactive population.

- The 18-24 cohort, with an inactivity rate of 28.8% before the pandemic and 31.3% now, accounts for 19% of the economically inactive population. (Of course, many of these individuals will be full-time students.)

Economic inactivity by age



Change by age during pandemic



The highest inactivity rates are, as mentioned above, among the 16-17 cohort. This accounts for 11% of economically inactive people with an inactivity rate of 68.7% before the pandemic and 67.1% now. But of course, people in this cohort will still be in school; those in work will be in part-time work. So from a labour market policy perspective, this cohort is not going to be at the top of the priority list.

Economic inactivity rates are much lower among people of prime working age, as we would expect: 11.9% and 12.3% before and after Covid for the 25-34 cohort, and 12.1% and 12.3% for the 35-49 cohort. While we should not ignore the slight decrease in labour market participation in these groups, the raw age data suggests that our primary focus should be elsewhere (although the picture will look more complicated when we cut across the data by gender).

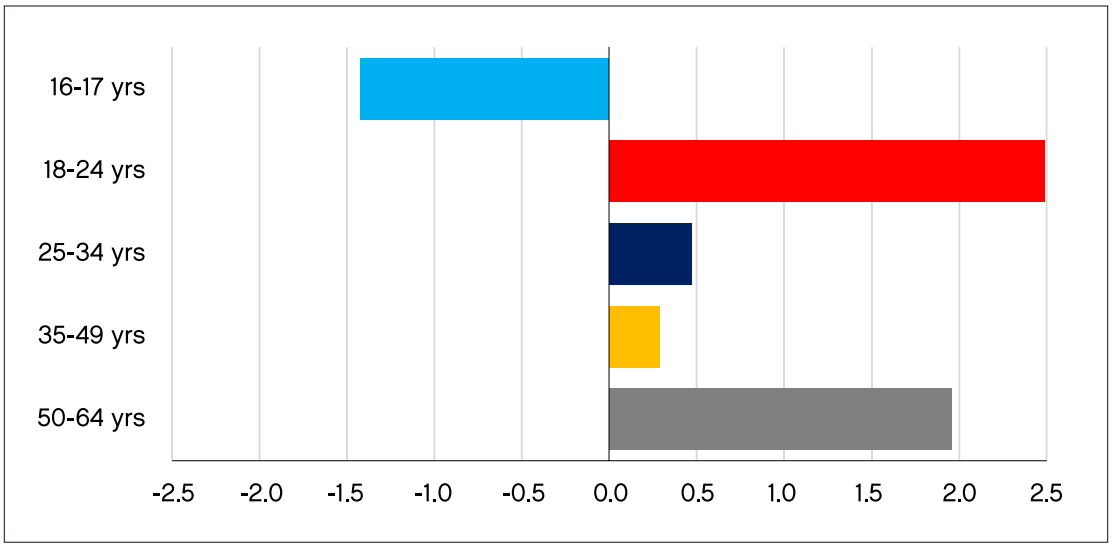
Much of the national conversation so far has focused on the most elderly cohort, and understandably so. **In absolute terms, the 50-64 group has seen the largest absolute increase in economically inactive people since before the pandemic, accounting for 62% of the total increase in economic inactivity** – 318,000 of the missing 516,000 (this is of course a net figure: there will be more who actually left, while others rejoined).

There is an ongoing debate about what is driving this trend, either more people retiring early or more people with persistent medical conditions including 'long Covid', and we shall dig into this in more detail in the next chapter.

On a related note, one often overlooked facet of the job vacancies problem is economic inactivity among those aged 65 and over.[28] The number of elderly people in the workforce has been trending upwards recently – but having reached a record high of 1.50 million in Q2 2022, it fell back by almost 100,000 to 1.40 million in Q4, the latest for which there are records available. The group's economic inactivity rate is still 0.5 percentage points higher than it was before the pandemic at 88.7%. Given that the population of those aged 65+ has grown by around 300,000 over the last two years, getting the activity rate back to the pre-pandemic rate would mean there were about 55,000 more people in the workforce, equivalent to around 5% of job vacancies.

Obviously in most cases those in this age group will simply be enjoying their retirement, but older workers are often among the most skilled and productive, who remain in work – often self-employed or part-time – because they enjoy their work and derive a sense of satisfaction, purpose or identity from it. So when we are thinking about the 50-64 cohort, it is worth bearing in mind that measures used to encourage them back into work might also bear fruit among pensioners.

Percentage change in inactivity rates since the pandemic



One of the key arguments of this paper, however, is that the debate often focuses too much on the most experienced workers. As the graph above illustrates, **it is actually the 18-24 age group which has seen the biggest rise in the inactivity rate** – a chunky 2.5 percentage point increase, with 105,000 fewer individuals in the labour market. This relatively small cohort (spanning six years rather than the 10 or 15 of older cohorts) accounts for 20% of the additional economic inactivity compared to pre-Covid days.

Much of this has been put down to an increase in student numbers, but we should be wary of this easy narrative.

28 As discussed above, with the school leaving age now set at 18, and the state pension age at 66 and moving up towards 68, there is a strong case for rethinking the headline numbers we use when talking about economic inactivity.

True, the overall number of people enrolled in higher education courses in the UK was up by 330,000 in 2021/22 on 2019/20, according to the Higher Education Statistics Agency (HESA).[29] But this includes a 123,000 increase in international students. The figure also includes people of all ages, as well as people studying part time. According to data from the Office for Students,[30] the full-time equivalent (FTE) increase in students enrolled in higher education was a rather more limited 175,000 – but that includes the 123,000 international students, who are eligible to work up to 20 hours a week alongside their studies.

In fact, if we move away from the high-level ONS inactivity data, and instead dig down into the often neglected underlying Labour Force Survey (LFS) data published through Nomis, further complications emerge.[31] Compared to 2019, there are only around 77,000 more people whose reason for not participating in the workforce is being a student, of whom around 61,200 are aged 16-24 (with 14,800 aged 25-49 and 2,000 aged 50-64).[32] That is just a shade under half of the total increase in economic inactivity among those aged 16-24.

‘In Q4 2022 there was a 28% increase in the number of those aged 18-24 who were not in education, employment or training (the so-called NEETs), with about 65,000 people – split equally between men and women – moving into the unemployed category’

Given the limits of the official data, it’s hard to come up with a definitive picture of what is going on here. Reasons for part-time study could vary – some might have caring responsibilities, for example, and so cannot work part-time alongside their studies. But just assuming that elevated economic inactivity among 18- to 24-year-olds is because of a (temporary) uptick in student numbers seems like unwarranted complacency. As we will discuss later, in Q4 2022 there was a 28% increase in the number of those aged 18-24 who were not in education, employment or training (the so-called NEETs), with about 65,000 people – split equally between men and women – moving into the unemployed category. This is by the sharpest quarter-on-quarter increase since current records began in 2001.[33]

Of course, the unemployed are distinct from the economically inactive. But unemployment is a classic route into inactivity in time. And it shows the dangers of complacency about the problems of the youth – of the kind demonstrated by multiple previous investigations into economic inactivity, including by the House of Lords Economic Affairs Committee and the Office for National Statistics.

29 HESA, ‘Higher Education Student Statistics: UK, 2021/22 - Where students come from and go to study’ (19 January 2023). Link.

30 OfS, ‘2021-22 student numbers’, Official statistics (February 2023). Link.

31 Nomis, ‘Dataset: annual population survey – regional – economic inactivity by reasons’, Annual Population Survey/Labour Force Survey (27 January 2023). Link.

32 Unfortunately, while the publicly available Nomis data does allow for a degree of cross-slicing, it is also less granular than the timeseries processed and published by the ONS, as reflected in the broader age categories and date ranges. The comparison ranges here are Jan-Dec 2019 versus Oct 2021-Sept 2022.

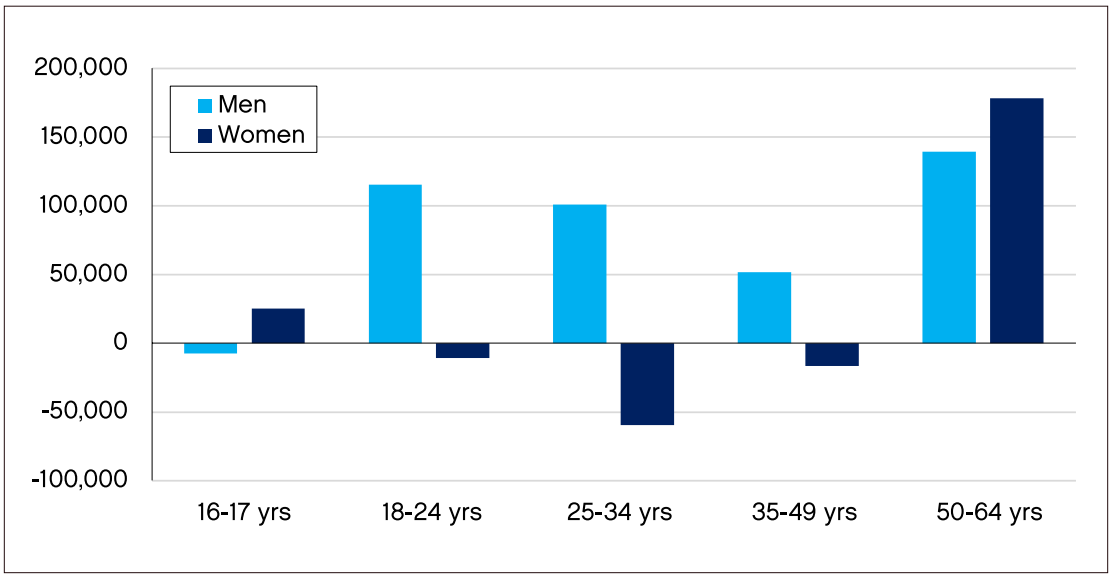
33 The previous record, 15% was in Q3 2020, so during the depths of Covid. Before that, the record was 12%, back in Q3 2011, when the economy was still climbing out of the recession caused by the financial crisis. ONS, ‘Young people not in education, employment or training (NEET), UK: February 2023’ (23 February 2023). Link.

Overall, however, the findings above suggest that **if we are going to move the dial on economic inactivity, then we should focus firstly – but not disproportionately – on those aged 50-65; secondly on those aged 18-24; and finally on people of prime working age.**

But as well as looking at how the increase in economic inactivity breaks down by age, we need to consider how sex differences cut across age categories. **In total, there are around 400,000 more working-age men economically inactive now than pre-pandemic, and around more 116,000 women – a stark 77:23 split.**

Moreover, whereas an overwhelming proportion of the net increase in inactivity among working-aged women is accounted for by women aged 50-64, **the pattern of increased inactivity among working-age men is broad-based.** Some 35% of the increase in male economic inactivity is accounted for by those aged 50-64, but the smaller group of men aged 18-24 account for 29% of the increase, and the 25-34 group for 25%.

Change in economic inactivity by sex and age



The divergence in the experiences of younger millennial men and women is particularly striking. **There are now 60,000 fewer economically inactive women aged 25-34 than pre-pandemic, but 101,000 more men.** In fact, the number of economically inactive people is about 10% lower than would otherwise be the case, were it not for the influx of younger millennial women into the workforce.

This influx seems to belie one of the main narratives about increased economic inactivity – that high and rising childcare costs are resulting in more women taking time out of work to look after young children. Yet this explanation for inactivity has been seized on by Tory MPs and, more recently, by the Resolution Foundation.[34]

If that theory were true, we would expect to see an increase in economic inactivity among women aged 25-34, as the mean age at which women become mothers is

34 Resolution Foundation, 'Tweet: Instead of persuading older workers to 'unretire', Government efforts to boost Britain's workforce should focus on supporting more mothers into work and helping older workers and those with a disability stay in work', Twitter (21 February 2023). Link.

now 30.7 years.[35] In fact, the flow is in the other direction. The lack of an obvious footprint in the data suggests that perhaps childcare is not a fundamental driver of increased economic inactivity since the onset of the pandemic.

Men			
Age range	Share of increased male inactivity	Share of increased inactivity within cohort, male and female	Share of increased inactivity, 16-64 male and female
16-17 Years	-2%	-43%	-1%
18-24 Years	29%	110%	22%
25-34 Years	25%	244%	20%
35-49 Years	13%	147%	10%
50-64 Years	35%	44%	27%
Total, 16-64 Years	**100%**	**77%**	**77%**

Women			
Age range	Share of increased female inactivity	Share of increased inactivity within cohort, male and female	Share of increased inactivity, total 16-64 male and female
16-17 Years	22%	143%	5%
18-24 Years	-9%	-10%	-2%
25-34 Years	-51%	-144%	-12%
35-49 Years	-14%	-47%	-3%
50-64 Years	153%	56%	35%
Total, 16-64 Years	**100%**	**23%**	**23%**

High childcare costs are of course a cost of living burden and a drag on family formation, with the sector in dire need of supply-side reform, as set out by the Centre for Policy Studies in our report 'Solving the Childcare Challenge'[36] But examining the data by gender as well as age allows us to focus our policy priorities even more tightly. It suggests that in the 50-64 cohort, the change in labour market participation is roughly the same, but in the 16-24 cohort, withdrawal from the labour market is overwhelmingly a male phenomenon. A similar pattern is evident among the 25-34 and 35-49 cohorts too.

35 ONS, 'Childbearing for women born in different years, England and Wales: 2020' (27 January 2022). Link.

36 E. Dunkley, 'Solving the Childcare Challenge', Centre for Policy Studies (4 July 2022). Link.

3. Why are people economically inactive?

We have already seen that some of the things everyone thinks they know about the increase in economic inactivity are not true. It is not just a problem of the old. Among those of working age, the increase does not seem to be driven by childcare costs – extortionate though they are.

But there are plenty more misconceptions that need to be addressed – because it is only by getting a proper picture of the data that we can come up with appropriate solutions.

In this section, we will first take a look at the reasons people give for their economic inactivity,[37] then drill down into the key demographics and debates where policy changes might actually move the dial on labour market participation.

The overall picture

In the official data, there are seven main explanations for inactivity which are put to those surveyed: being a student, looking after family or home, temporary sickness, long-term sickness, being discouraged/apathetic, retirement and 'other'.

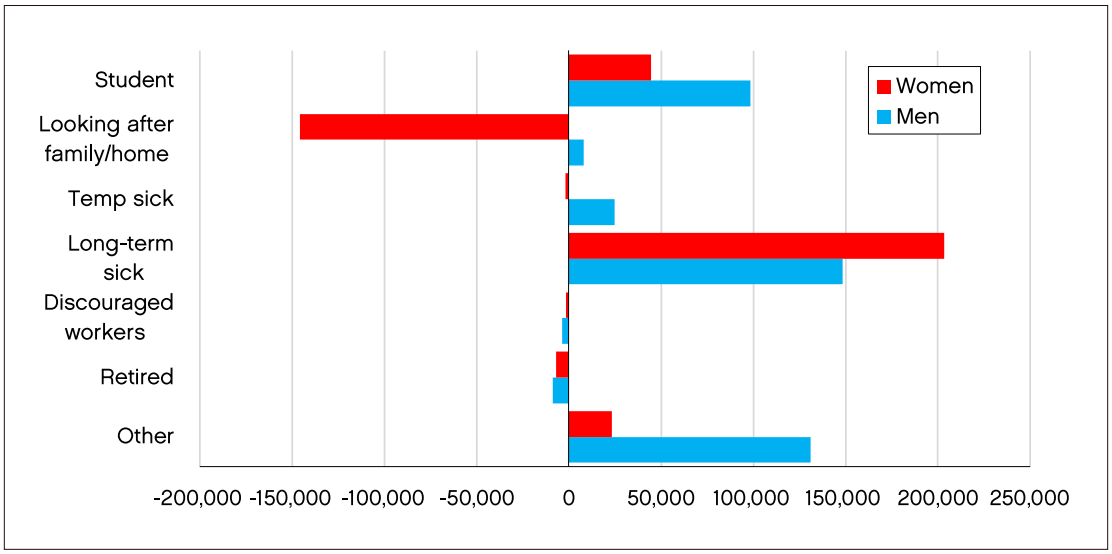
'There are an additional 352,000 individuals now economically inactive for reasons of long-term sickness compared to before the pandemic, a startling 17% rise'

The most obvious thing to say is that there is a slippery element of subjectivity inherent to the LFS data. For example, in the ONS definition, the 'other' category includes people who: have not yet started looking for work, do not need or want employment, have given an uncategorised reason for inactivity or have not given a reason at all. It is by its nature opaque, though the category might include those who have effectively retired early, i.e. those who do not need or want employment, but since they are not of state pension age, do not see themselves as formally retired. It has also been suggested that people with long-Covid may be putting themselves into the 'other' category.[38]

37 ONS, 'Dataset: INAC01 SA: Economic inactivity by reason (seasonally adjusted)' (14 February 2023). Link.

38 See House of Lords Economic Affairs Committee (December 2022), p.17. Link

Change in economic inactivity (16-64) by reason since pre-pandemic



As has been widely publicised, **the inactivity reason which has seen the biggest increase since the onset of the pandemic is long-term sickness.** This appears to account for 68% of the net increase in economic inactivity, with temporary sickness accounting for another 5%. As the graph shows, that means **there are an additional 352,000 individuals now economically inactive for reasons of long-term sickness compared to before the pandemic, a startling 17% rise.** That brings the number of people not working or looking for work because of long-term sickness up to 2.47 million – this is down from 2.52 million in mid-2022, but still unprecedented in the three decades before the pandemic.

This has led in some quarters to a simplistic explanation for the rise in economic inactivity – it is driven by people who want to work but cannot, because of long Covid or other health conditions. Many in turn blame this on the state of the NHS, and its perceived neglect by the Conservative government.

> **'In fact, fully 69% of those moving into long-term sickness were already out of the labour market for another reason'**

But the actual data challenges any such easy narrative. Of all those economically inactive for reasons of long-term sickness in Q4 2022, 77.3% did not want a job (79.8% among women and 74.4% among men). That compares to 72.8% before the pandemic (74.1% of women, 71.4% of men). Combined with the increase in the number of people giving long-term sickness as a reason for inactivity, that means that notionally, there are now an extra 368,000 people with medical conditions who do not want to work. That number effectively accounts for 71% of the increase in economic inactivity.

And the plot thickens even further. As the ONS has noted in a deep dive into long-term sickness data, more detailed quarter-on-quarter flows show that **most of those who became inactive due to long-term sickness were also inactive, albeit for different reasons, in the quarter prior to their change of status.**[39] They were not moving from activity to inactivity.

39 ONS, 'Half a million more people are out of the labour force because of long-term sickness' (10 November 2022). Link.

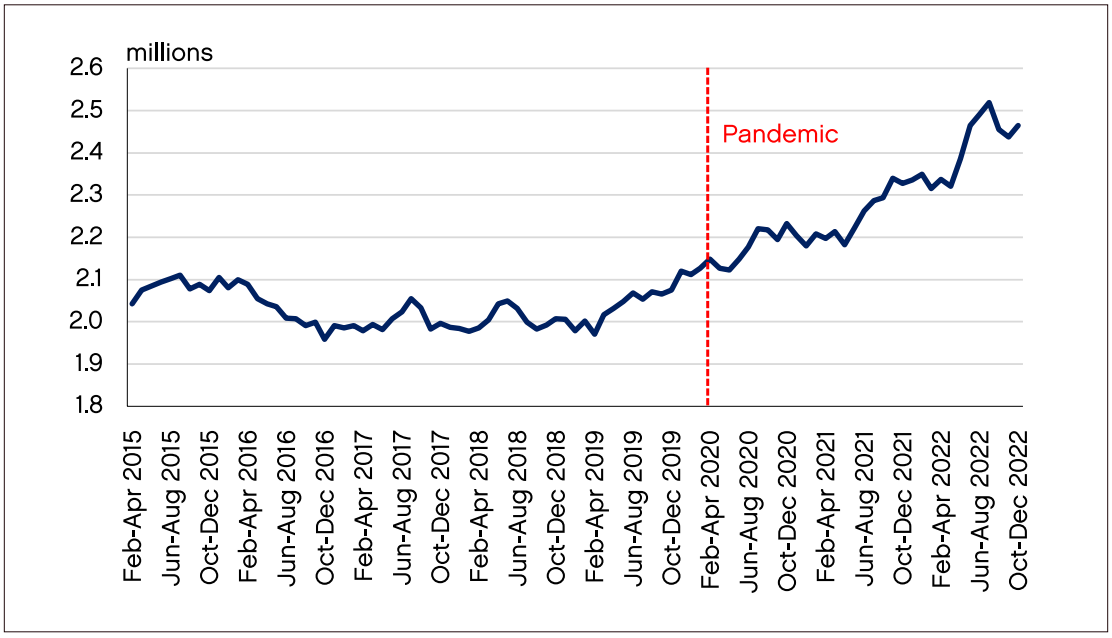
In fact, fully 69% of those moving into long-term sickness were already out of the labour market for another reason. About a fifth of these people were inactive through short-term illness or injury, so the progression makes sense. Another fifth, however, had previously been looking after family or home, while almost as many had described themselves as retired, and about 12% as students.

For many of these people, it is not clear whether their concrete circumstances actually changed. It could be instead that people changed the way they saw and described themselves, as new messaging and norms around public health and working patterns took hold in the pandemic. Tellingly, of those whose who moved out of the long-term sickness category in 2021 and 2022, 63% remained inactive for another reason. So there is some fluidity in how people conceptualise their incapacity for work, perhaps influenced by incentives within the welfare system. And even if their conditions could be treated, or better managed, it is by no means clear that huge numbers of these people would choose to charge back into the workforce.

How much of this is actually about the pandemic?

As discussed above, it is clear that the rise of long-term sickness has been a major driver of economic activity. But it is also clear that this is a phenomenon that began before the pandemic.

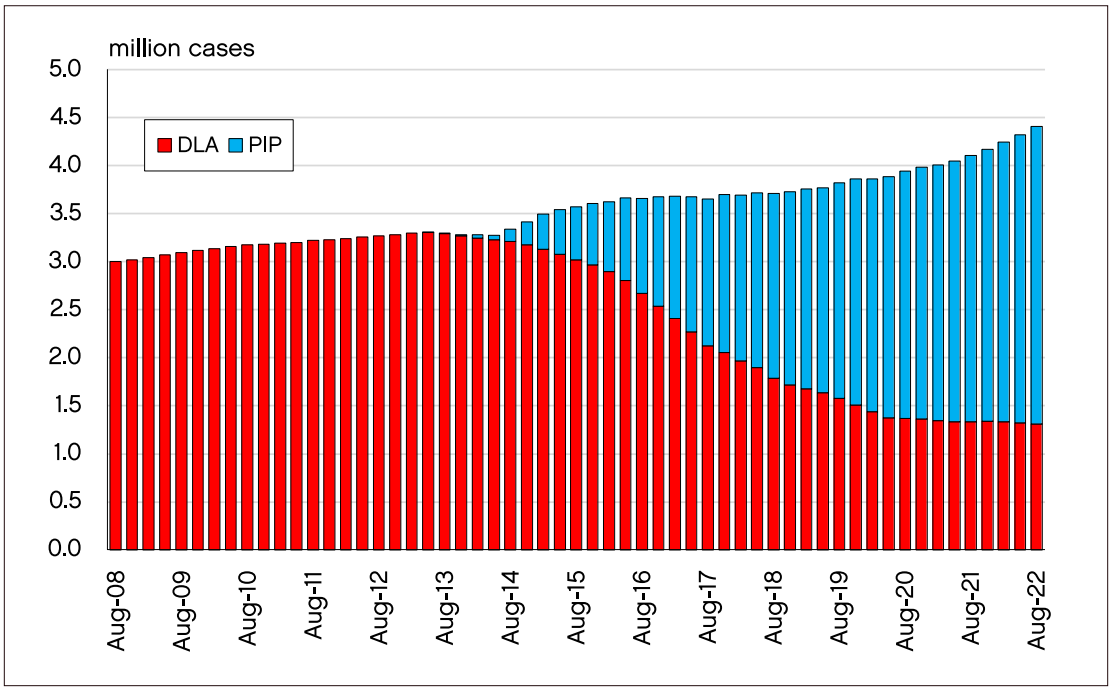
Economically inactive (aged 16-64) due to long-term sickness



Indeed, one major area of concern for policy experts before the Covid crisis was the inexorable rise in the number of people claiming disability benefits, especially for mental health conditions. When incapacity benefits were first introduced into the welfare system in 1971, in the guise of Invalidity Benefit, the idea was that only a small and relatively stable number of people would ever be able to access these benefits. But the numbers claiming various forms of incapacity or disability benefits drifted upwards in the following decades, from the hundreds of thousands into the millions.[40]

40 Nor has it always been in the interest of governments to get people out of incapacity and back into the workforce – not if they are going to show up in the unemployment statistics.

Live DLA and PIP cases



Today, annual expenditure on benefits for working age people (aged 16-64) in England and Wales amounts to £86 billion, equivalent to around 4% of UK GDP, or around 40% of total expenditure on benefits. At least 4.3 million people of working age are in receipt of at least one benefit, with the Department for Work and Pensions administering a total of 20.4 million benefits for working age people.[41]

Due to the consolidation of various benefits into Universal Credit, there is no straightforward way to work out how much of the expenditure is allocated. However, before the introduction of Universal Credit (which began in 2013), Disability Living Allowance was responsible for 13% of expenditure, more than any other form of working-age benefit bar housing benefit.

As the chart above shows, the introduction of the new Personal Independence Payment (PIP) saw the number receiving such benefits rise from 3 million to just under 3.5 million on the eve of the pandemic, and even higher since then. One explanation is that Cameron-era reforms to disability payments eliminated what was essentially a middle status between 'fine' and 'unable to work', in which people were assessed as able to do some work or work-related activities. **The aim of course was to push more people into work, but in fact the opposite has happened, with fewer people doing part-time/limited work, for fear of losing more in benefits than they could reliably earn.**

In other words, the new PIP assessments created perverse incentives for people to remove themselves from the workforce. If they were to lose their job, they would have to go through the entire assessment process again, but with clear evidence they were able to work – even if their condition had since deteriorated to the point where they could not work anymore – it would be much harder to claim the full benefits available to a person 'unable to work'. For many people, the path of going back into work was just too risky without a more nuanced fallback position within the benefits system.

41 DWP, 'Benefit expenditure and caseload tables 2022' (24 May 2022). Link.

The PIP assessment process therefore needs reforming to create a more graduated pathway back into work for the unwell or those living with disabilities, with fewer downside risks if they then become unable to work at all.

Another factor that has been underreported is benefit fraud. Although official reports on economic inactivity tiptoe around the issue, the House of Commons Public Accounts Committee (PAC) noted last November that benefits fraud has risen to record levels in the wake of Covid.[42] **Around £8.5 billion in benefits was lost to fraud or paid out in error in 2021-22, almost double the annual total pre-pandemic.** Ironically, the PAC also noted that benefit fraud had become more of a problem because the tight labour market meant the DWP was struggling to hire enough suitably qualified staff to fight fraud.

> **'At least 4.3 million people of working age are in receipt of at least one benefit, with the Department for Work and Pensions administering a total of 20.4 million benefits for working age people'**

None of this is to say that the rise in long-term sickness since the pandemic is not genuine. For example, the 14,000 extra patients aged 16-34 with cancer and other serious progressive illnesses are certainly not faking it.[43] But the fact that the firm upwards trend in inactivity because of long-term illness began fully one year before the pandemic, in early 2019, suggests that something else is going on here – which we shall return to when we look at the younger cohorts in more depth.

Economic inactivity among the elderly

As noted above, it is those aged 50-64 who are responsible for the bulk of the increase in economic inactivity. The key question is what is driving this – in particular, is it illness or affluence?

As Xiaowei Xu of the IFS has pointed out, the reasons people give for inactivity change over time, with the state pension age representing something of an inflection point.[44] Someone who has de facto retired before reaching 65 for whatever reason – their own health, or to care for a partner or parent for example – will often give another reason for inactivity until they reach state pension age. This is handily illustrated by the change in women's state pension age. In 2019, the share of women who said they were inactive because of long-term sickness fell from 15% at age 64 to 5% at 66. In the 2018 data, the fall happened between 63 and 65.

In other words, as noted above, we have to be cautious about the subjectivity in the high-level LFS data. Fortunately, several more searching studies of the older cohort have been carried out over the last year. These include the ONS's Over 50s Lifestyle Study (OLS), conducted in two waves, in February and August 2022. This study focused on economically inactive people aged 50-54, 55-59 and 60-65 who had left or lost their job during the pandemic.[45] An advantage of this study is that

42 C. Smyth, 'Record levels of benefit fraud after Covid', The Times (9 November 2022). Link.

43 ONS, 'Half a million more people are out of the labour force because of long-term sickness' (10 November 2022). Link.

44 X. Xu, 'Twitter thread', Twitter (14 February 2022). Link.

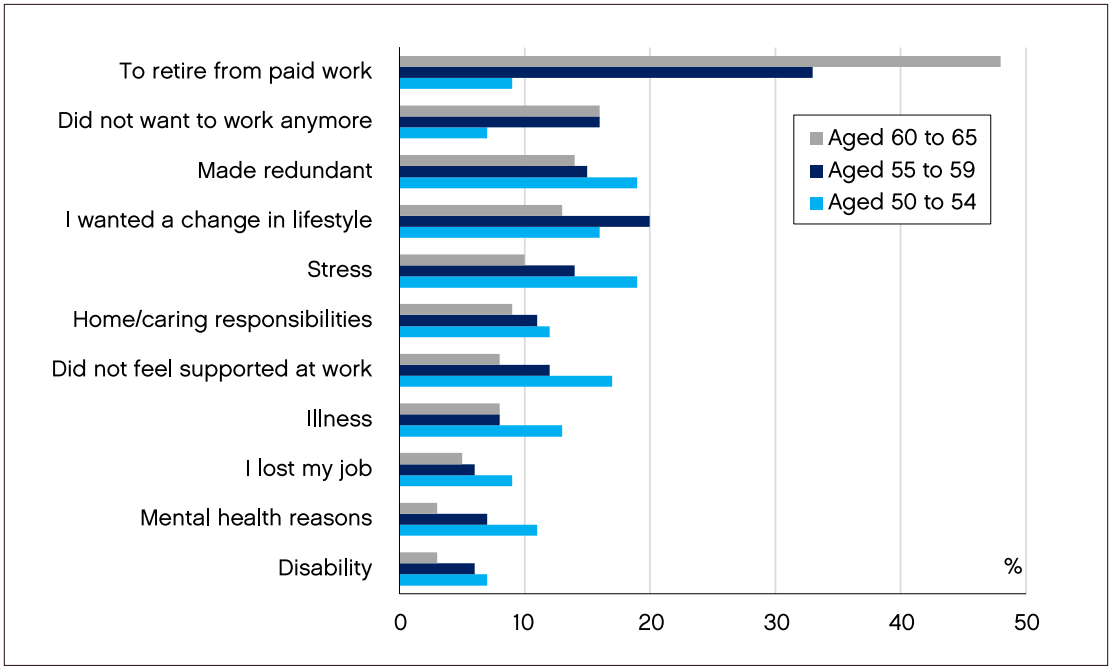
45 ONS, 'Reasons for workers aged over 50 years leaving employment since the start of the coronavirus pandemic: wave 2' (27 September 2022). Link. Unlike the main inactivity time series, this study covers 65-year-olds.

it allowed people to give multiple reasons for why they were not in work and not looking for work, capturing more of the complexity of people's decision-making.

One thing that leaps out from the results is what we could term an 'age-inactivity gradient'. As you'd expect, the chances of someone being economically inactive increase the closer they are to 65. But there is also a shift in the reasons given. The closer someone is to 65, the more likely they are to give 'to retire from paid work' as the reason for inactivity – five times more likely than someone aged 50-54. They are also twice as likely to say, 'I did not want to work anymore'.

By contrast, reasons such as 'stress', 'illness', 'mental health reasons', 'looking after the home or caring responsibilities' and 'I was made redundant at my workplace' were much more common among those aged 50-54 than those aged 60-65. Indeed, illness-related reasons for inactivity were twice as common among the 50-54 group as 60-65s.

OLS, reasons for inactivity



Again, there is still going to be an element of subjectivity in these self-reported assessments. But the ONS also found compelling non-subjective factors. For example, the majority of people who had not returned to work after the pandemic owned their own home, and were more likely to be debt-free – 61% versus 42% for those who had returned to the workforce after a period of pandemic-induced inactivity.

Similarly, among those who were still economically inactive, those aged 50-54 were generally less financially resilient than those aged 60-65, being less likely to own their home outright and more likely to have outstanding credit card debt, for example. And whereas 38% of inactive people aged 50-54 said they were 'somewhat confident' or 'very confident' that their retirement provisions would meet their needs, 55% of 60- to 65-year-olds said the same. This was also reflected in the fact that inactive people in the younger cohorts were more likely to say they would consider returning to work: 86%, 65% and 44% for the 50-54, 55-59 and 60-65 cohorts respectively. So it looks as if, for many people, inactivity is a lifestyle choice enabled by financial security.

From a separate ONS study,[46] we also know that those aged 50-65 who left their job during the pandemic but who have since returned to work were more likely to have left their previous job because of factors outside of their control – redundancy (33%), the pandemic (26%) or through having lost their job (17%). In other words, they suffered an involuntary loss of earnings and were motivated to return for financial reasons. Those who had not yet returned but who would consider returning were also less likely to be able to afford an unexpected expense than those who would not consider returning (61% vs 77%) and less likely to own their own house outright (57% vs 78%).

Furthermore, in December 2022, the ONS published the results of a logistic regression model on the correlates of inactivity.[47] These findings pointed towards the same conclusion. **Health was a strong predictor of inactivity – but so too were financial indicators.** The modelling found that men aged over 50 who owned their own home were 1.8 times more likely to be inactive then men in the same cohort who rented, while the equivalent figure for women was 1.6 times more likely.

We can also take the 11 reasons for inactivity used in the OLS and group them to get an idea of the balance of reasons for inactivity, as per the table below.[48] As mentioned above, people were allowed multiple answers, so the totals will come to more than 100%.

	Aged 50-54	Aged 54-59	Aged 60-65	Average
Lifestyle	49%	81%	85%	**72%**
Health	50%	35%	24%	**36%**
Made unemployed	28%	21%	19%	**23%**
Caring	12%	11%	9%	**11%**

Arguably 'caring' could be lumped in with health, as many of those with caring responsibilities will be looking after partners out of work or elderly parents with health needs – long-term sickness can be an indirect cause of economic inactivity. We also need to recognise that for some people, not feeling supported in their job might be health related, but conversely, for others people 'stress' might not be a mental health factor, but a lifestyle one.

But even making these adjustments, among the multiplicity of sometimes parallel reasons for inactivity given by those aged 50-65, lifestyle reasons seem to be around 1.6 times to twice as important as health related reasons, and over three times as important as being made unemployed. And as we have seen, these lifestyle choices seem to be strongly connected to financial wellbeing.

46 ONS, 'Returning to the workplace – the motivations and barriers for people aged 50 years and over, Great Britain: August 2022' (19 December 2022). Link.

47 ONS, 'Worker movements and economic inactivity in the UK: 2018 to 2022' (19 December 2022). Link.

48 Lifestyle includes: 'To retire from paid work', 'I did not want to work anymore', 'I wanted a change in lifestyle' and 'I did not feel supported in my job'; Health includes 'Stress', 'Illness', 'Mental health reasons' and 'Disability'; made Unemployed includes 'I was made redundant at my workplace' and 'I lost my job'; Caring is 'Looking after the home or caring responsibilities'.

In other words, it seems that **financial factors are, on the whole, playing a bigger role than medical conditions in sustaining elevated inactivity rates in the 50-65 group** (though individual circumstances will obviously vary).[49] This is not to say that long-term sickness is not an enduring and worsening issue that needs to be addressed, especially as Britain's population continues to age. But early retirement among the relatively affluent seems to be the more significant factor since the pandemic.

> **'Financial factors are, on the whole, playing a bigger role than medical conditions in sustaining elevated inactivity rates in 50-65 group'**

The House of Lords Economic Affairs Committee came to a similar conclusion. Its members argued that the experience of home working and furlough during the pandemic probably induced lifestyle changes which persuaded affluent individuals winding down towards retirement that they should go early rather than working for a few more years until they hit the state pension age. As argued below, particular features of the UK tax system and pension arrangements may have facilitated this – which might help explain why the UK experience with inactivity has been so different to that of other developed nations.

There is now a fairly widespread view that lifestyle choices have driven a significant share of activity across the 50-64 cohort. But this also suggests that we are unlikely to get enough of these people back to work to move the economic dial.

We have already seen that the people aged 50-65 who have returned to work since the pandemic are generally those who lost their jobs, not those who voluntarily left work. As the Bank of England notes: 'Those who have taken early retirement might not be expected to return to the labour market, unless there is a significant change in their preferences or circumstances.'[50]

True, the number of inactive people aged 50-64 fell by around 26,000 between Q3 and Q4 2022, and the overall number of people inactive for reasons of retirement fell by 50,000. This might indicate that cost of living pressures are compelling some of the older cohort to return to work. Inflation peaked at over 11% last year, and pensioners on fixed incomes are particularly vulnerable to inflation eating away at their standard of living.

However, a statistical artefact might be flattering the figures here somewhat. As mentioned earlier, around 735,000 64-year-olds turn 65 each year, thereby shuffling out of the benchmark inactivity timeseries. On a quarterly basis, that's roughly 184,000 people exiting the scope of the headline labour market timeseries, including the inactivity series, through ageing.[51] At the same time, around 225,000 people are turning 50 and entering the final cohort. The inactivity rate for people turning 50 is less than half what it is for people turning 65. So on the whole, we would expect

49 Compare also the IFS: 'Overall, it does not seem as if poor health is the primary driver of these increases in economic inactivity rates'.

50 BoE, 'Monetary Policy Report - February 2023' (2 February 2023). Link.

51 This calculation of course assumes that birthdays are uniformly distributed throughout the year, which is not the case. In reality, as the ONS notes, there is a slight peak in September, probably due to parents planning to have children at the start of the school year. However, the broad point still stands.

inactivity in the 50-64 cohort to fall naturally over time, as long as we assume that so many more people entering inactivity in their 50s and 60s was a pandemic-era one-off and not a new structural feature of the labour market.

In short, it is not at self-evident that older people are returning to the labour market in any great number – it could just be that they are ageing out of the labour market timeseries. Extensive polling by Public First in an investigation into the 'Great Retirement' also found limited evidence of people returning to the workforce, with a combination of negative attitudes towards work (benchmarked against attitudes in Germany and the USA) and relative financial comfort through homeownership underpinning economic inactivity in the 50-64 cohort.[52]

On the whole then, the evidence suggests that **people who voluntarily retired early during Covid are mostly not going to come back into the workforce. So government should perhaps focus less on getting retirees to return, and more on stopping early retirement from becoming a new norm in the post-Covid world.**

> **'People who voluntarily retired early during Covid are mostly not going to come back into the workforce. So government should perhaps focus less on getting retirees to return, and more on stopping early retirement from becoming a new norm in the post-Covid world'**

Of course, there certainly are some levers the Government could pull to make working up until the state pension age (and even beyond) a more appealing prospect. But this does raise something of a philosophical quandary.

If people have worked hard and earned enough money to retire early, spend more time with their family, volunteer in the local community and live the good life, why should they not do so? They are under no obligation to be revenue-maximisers for the state; individuals do not live solely for the convenience of Treasury mandarins. In this vein, conservative commentator Henry Hill has sounded a note of caution about 'Conservative Stakhanovism'.[53]

On the other hand, Conservative politicians ought to be responsible stewards of the public finances. The pensioner share of the population who has gone up from 16% to 18% over the last decade, and is projected to reach 20% in a decade's time.[54] Working-age people will be footing the growing bill for pensioners' welfare payments and NHS usage, and unless we can remove Britain's many barriers to economic growth, this will mean higher taxes. If early retirement becomes an established feature of labour markets, it will only further tilt the balance of tax and spend towards the grey vote.

So there really is a macroeconomic imperative, even beyond the short-run economic calculus, to – if not exhort or force people to return to work – then at least to remove any impediments to them doing so. And sure enough, our current tax system contains many such impediments.

52 Public First, 'What is driving the Great Retirement?' (19 December 2022). Link.

53 H. Hill, 'Conservative Stakhanovism – or the perils of a simplistic crackdown on the economically inactive', Conservative Home (12 January 2023). Link.

54 ONS, 'Principal projection – UK summary', Population projections (12 January 2023). Link.

The most important of these is probably the lifetime allowance (LTA). This is the amount of savings you can take from your pension schemes without facing a tax charge. If you exceed this, a 25% charge is applied to excess benefits, and 55% if the excess is taken as a lump sum.

Back in 2010/11, when the Coalition government came to power, the LTA was £1.8 million, up from £1.6 million when it was first introduced in 2006. But this was gradually sliced away during George Osborne's tenure as Chancellor. By 2016/17 it had fallen to £1 million. **The lifetime allowance now stands at £1.07 million – whereas that 2010/11 figure would have a real-terms value of £2.4 million.** In other words, **the pension cap has more than halved in real terms in a decade.** As a result, more people are bumping up against the cap earlier in their careers. Once they reach the cap, they face less of an incentive to save for their retirement, and hence less of an incentive to carry on working.

> **'The lifetime allowance now stands at £1.07 million – whereas that 2010/11 figure would have a real-terms value of £2.4 million. In other words, the pension cap has more than halved in real terms in a decade'**

At the same time, **older workers can come up against very high marginal tax rates – as high as 96% in some cases.** This is thanks to the complicated way in which the tax and benefits systems interact, for example around the withdrawal of child benefit. In the words of the Centre for Policy Studies Research Director and Head of Tax, Tom Clougherty, this is 'a problem that pops up all over the tax and benefit system – you can suffer seemingly random spikes in your marginal tax rate whether you're rich, poor, or in the middle'.[55]

While we should work to remove the weird kinks and traps within the tax system over the longer term, in the short term, the Chancellor should simply raise, or just abolish, the LTA, particularly as there is already an annual limit on the amount people can put into their pensions. Creating more headroom might forestall more people within the 50-64 cohort from leaving the workforce – and perhaps even entice some back, if they are allowed to resume adding to their pension schemes.

Indeed, one profession often bedevilled by high marginal rates and where people tend to come up against the LTA early is the medical profession. It is likely that these distortions have contributed towards the propensity of GPs to take early retirement. **In September 2017, the number of GPs in England aged 55-59 was 4,702. By September 2022, all of these individuals would have fallen in the 60-64 age bracket. Yet in fact there were just 2,279 of them left.**[56] That represents an attrition rate of 52%.

Some of these individuals will have moved elsewhere in the healthcare profession, but not over half of the cohort.[57] Given the crisis in the NHS, and the roll of long-term sickness in economic inactivity, these are exactly the sort of skilled workers we most want to see staying in the workforce. Yet as things stand, financial incentives are not conducive to this end.

55 A. Phillips, '50,000 middle-class families to be caught in 96pc tax trap', The Telegraph (28 December 2022). Link.

56 NHS Digital, 'General Practice Workforce, 31 January 2023' (23 February 2023). Link.

57 Note that the attrition rate for GPs between the 50-54 and 55-59 age groups over the same period was 18%. For admin and non-clinical staff – who on average are paid much less than senior GPs, the attrition rate over this period was just 5%.

In December 2022, the Government launched a consultation on changes to the NHS Pension Scheme, including proposals for flexibilities allowing retired and partially retired staff to return to work or increase their working hours without having payments to their pension reduced or suspended.[58] In light of the economic inactivity problem – which is in part driven by long-term sickness, let us not forget – this is an extremely welcome initiative.

However, the Government should also go much further in reforming public sector pensions more broadly. As things stand, with public sector employer pension contributions of 24.5%, **highly paid public sector workers simply accrue too much pension too fast. Once the clawback arrangements kick in, the reduced tax relief makes it feel as though they are being punished for working.** Civil servants and others on around £80,000-90,000 a year can reach this point by their mid-50s.

Unlike much of the private sector, you can rarely take salary in lieu of employer pension contributions, and there are barriers to leaving the scheme, such as loss of the life insurance. So public sector workers who reach this point often retire, go part-time or set up as a freelancer, doing non-pensionable work.

> **'Highly paid public sector workers simply accrue too much pension too fast. Once the clawback arrangements kick in, the reduced tax relief makes it feel as though they are being punished for working'**

So as well as raising the LTA across the board, public sector employer contributions should be lowered and the rate at which benefits are accrued reduced (as public sector pensions are defined benefit schemes) in exchange for higher up-front salaries, and people should be able to suspend further contributions when they do reach the cap without having to leave their pension scheme.

These measures would not result in any net transfer of money to the over-50s (though it would have an upfront cost to the Government) but would significantly shift the incentives away from early retirement. Such a course of action would help to keep more public sector workers in work for longer. In turn, this would mean less recruitment demand in the public sector, easing the pressure on labour markets and making it easier for businesses to fill vacancies.

However, while the policy focus should be on forestalling higher rates of early retirement from becoming structural feature of the labour market, there are some things we could try which might help get more older workers back in the short-term too. Aside from realigning saving and retirement incentives across the public and private sectors, we need to think making workplaces more attractive for people over 50. As Public First found, a negative attitude towards work has been a key factor in older workers deciding to retire. This finding echoes reasons given for retirement in the OLS such as 'I did not feel supported at work' and perhaps 'stress'. The onus here is on employers to invest in their workers and adapt to new expectations – around hybrid working, for example. We also welcome the Government's reported support for measures such as mid-life MOTs and other measures to engage and motivate employees, as suggested by Guy Opperman MP in his report for the Centre for Policy Studies, 'All Hands on Deck'.[59]

58 DHSC, 'NHS Pension Scheme: proposed amendments to scheme regulations' (5 December 2022). Link.

59 G. Opperman, 'All Hands on Deck', Centre for Policy Studies (27 November 2018). Link.

Skills could be a key barrier here, however. The ONS has found that those who feel they do not have the skills to get a new job are more likely to report reasons other than retirement for being out of the labour market – often health-related reasons. They are also generally more open to the idea of returning to work than those who gave retirement as a reason for opting out. This tendency was particularly pronounced at the younger end of the 50-65 cohort.[60]

> **'The step-change in economic inactivity among people aged 50-64 since the pandemic has mainly been driven by lifestyle choices'**

So there is a pool of several tens of thousands of older workers who could, with active engagement and retraining, potentially return to the workforce. One proposal floated by the Government, to have occupational therapists or job centre personnel placed in GP surgeries, with GPs encouraged to prescribe work as a therapeutic, could help. Likewise, greater engagement with SMEs on occupational therapy could yield progress at the margins,[61] though we would hesitate to endorse direct subsidies, not least because of the Government's poor record in clawing back money lost to fraud during furlough.

More generally, the Government is right to see upskilling the British workforce as a key priority – not just to help with inactivity, but also to boost economic growth, wages and living standards in the long run. The Centre for Policy Studies will be publishing more on this imminently.

In summary, **the step-change in economic inactivity among people aged 50-64 since the pandemic has mainly been driven by lifestyle choices** – in particular, the early retirement of the relatively affluent. Based on just the raw numbers, this group is where a change in policy could move the dial the most on inactivity. But in reality, most of those who have left the labour force since Covid are not likely to come back. The focus instead needs to be on forestalling more people from retiring early. Healthcare interventions are undoubtedly part of the solution here, and getting NHS waiting lists down is necessary for all sorts of reasons, but changing incentives around pension schemes and improving workplace opportunities are likely to have the bigger effect on activity rates in the 50-64 cohort, among both men and women.

Economic inactivity among the young

The second key cohort we will consider is the 18-24 group, i.e. those who should for the most part be entering work after school or further/higher education.

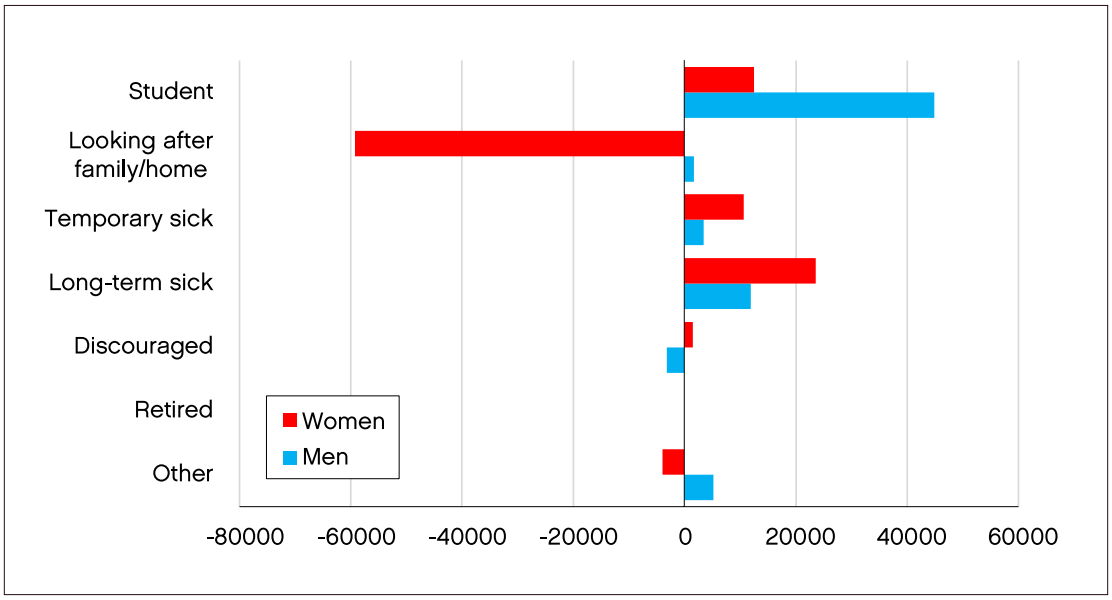
As mentioned above, the raw numbers in this cohort are not that high, at least when compared to the 50-64s. But this is the cohort where the increase in economic inactivity has been highest, up by 2.5 percentage points, and also where it can do the most long-term damage. As research into the aftermath of past recessions has shown, economic inactivity at this age can seriously affect lifetime earnings potential.

60 ONS, 'Returning to the workplace – the motivations and barriers for people aged 50 years and over, Great Britain: August 2022' (19 December 2022). Link.

61 C. Wheeler & H. Yorke, 'Rishi Sunak's Budget Big Bang to keep us all working past 50', The Times (5 March 2023). Link.

Unfortunately, the recent spike in inactivity among this age group has been largely neglected. The House of Lords Economic Affairs Committee, for example, explicitly eschewed any focus on younger cohorts from the outset of its investigation into inactivity. So we have the standard data from the ONS for young people not in education, employment or training (the NEETs), but nothing bespoke as we do for the 50-64 cohort. We are therefore reliant on the cruder LFS data, as per the graph below, if we want to slice across the different data categories.[62]

Change in economic inactivity, 2019 versus 2022, age 16-24



As we have seen, many people have simply ascribed this to an increase in student numbers, as young people ride out the pandemic and recession by extending their time in education. But as demonstrated above, this is responsible for at best 55% of the increase in inactivity in this cohort. And even this trend is in itself a bit concerning. The prevailing assumption is that this is essentially a neutral or perhaps even slightly positive trend: people will stay in education longer during Covid due to uncertainty in the jobs market, and will return as their courses finish, bringing with them enhanced skills and greater employability. Meanwhile, with the pandemic over, student numbers will revert to the long-term trendline. This is what happened with the economic shock of the Great Recession of 2008/9.[63]

In fact, however, members of this current cohort are likely to bear the economic scars of the Covid period for the rest of their lives. In the first place, A-Levels and degrees awarded since summer 2020 have been devalued by grade inflation, making it harder for people in their early twenties to compete in the jobs market against their slightly older peers (and in due course, the people coming up through the education system behind them).

62 This graph is based on the LFS data available through Nomis, and compares the January 2019 to December 2019 12-month period against October 2021 to September 2022. The precise numbers therefore differ from the ONS numbers drawn from tighter date ranges, but are still reflective of the relative magnitude of the changes across different reasons.

63 A. Mont'alvao et al, 'The Great Recession and Youth Labour Market Outcomes in International Perspective', Young People's Development and the Great Recession (20 October 2017). Link.

Second, the huge expansion in the university sector over recent decades has often come at the expense of course quality and employment outcomes, as extensively charted by the Centre for Policy Studies in its paper 'The Value of University'.[64] So at least some of those staying in education for longer because of Covid are going to accrue more debt, but not necessarily gain any enhanced earnings potential. Academic research into past recessions indicates **that those coming of age and entering the workforce during economic downturns tend to take longer to achieve adult milestones in both their professional and personal lives, earning less over their lifetimes and starting families later.**[65] Longitudinal studies of the American workforce, for example, have found white males who graduated during the 1980s recession had a statistically significant wage loss of 2.5% compared to cohorts graduating in more prosperous eras.[66]

> **'This 28% increase is by the sharpest quarter-on-quarter increase in unemployed NEETs since current records began in 2001'**

And obviously, for many of those not going to university the picture is even worse. Notably, there was a sharp increase in the number of NEETs (aged 18-24) in Q4 2022, as about 65,000 people – split equally between men and women – moved into the unemployed category, primarily (we might infer, given the timing) from education or training.[67] **This 28% increase is by the sharpest quarter-on-quarter increase in unemployed NEETs since current records began in 2001.**[68] Unemployed NEETs are distinct from economically inactive NEETs, but as mentioned above there is a real risk that many of these young people will drift into inactivity. It definitely suggests that staying in higher education for longer has not given this generation any extra edge in Britain's labour markets, even with vacancies at a record level. (Potential explanations for this include the cancellation of internship programmes, a classic route into employment after university, or the social isolation of lockdowns meaning that people missed out on socialisation away from home, and hence the chance to develop many of the soft skills that employers value.)

We urgently need an inquiry into what is going on in the 18-24 demographic vis-a-vis economic inactivity. In many areas, from welfare spending to housebuilding, the political economy of the UK is already unfairly tilted against younger generations. Focusing the entire conversation on economic inactivity, and any policy interventions that follow, solely on those aged 50 and above risks further deepening this imbalance.

In the short term, the Government should set about identifying precisely who these 65,000 NEETs are, with a view to identifying what additional support they need to get into work. The longer these people are not in work, the harder it will get for them to find jobs. Indeed, if all these people were to drift into economic inactivity, it

64 C. Walsh, 'The Value of University', Centre for Policy Studies (7 November 2021). Link.

65 F. Fiori et al, 'Employment insecurity and mental health during the economic recession: An analysis of the young adult labour force in Italy', Social Science & Medicine 153 (March 2016), pp.90-98. Link.

66 L. Kahn, 'The long-term labour market consequences of graduating from college in a bad economy', Labour Economics 17 (April 2010), pp.303-316. Link.

67 ONS, 'Young people not in education, employment or training (NEET), UK: February 2023' (23 February 2023). Link.

68 The previous record, 15% was in Q3 2020, so during the depths of Covid. Before that, the record was 12%, back in Q3 2011, when the economy was still climbing out of the recession caused by the financial crisis.

would increase the overall inactivity number by 0.7%, and lift the increase since the pandemic by 13%. Among just the 18-24 cohort, it would lift the inactivity number by 4% and increase the post-pandemic surge by 62%.

Getting these people into work would not reduce inactivity now, but it would help to prevent it rising further among this cohort, especially as more Covid student cohorts leave education. Prevention is, as ever, better than cure.

However, there are also other things going on in the youth employment market that should give us cause for concern. Foremost among these is a worrying rise in long-term sickness captured in the LFS data.

> **'Mental health accounts for 15% of the increase in inactivity among 16- to 34-year-olds since before the pandemic, and 70% of the increase for reasons of long-term sickness'**

Compared to 2019, on average over the last year there have been an extra 12,000 men and 24,000 women not participating in the labour market for this reason. Temporary sickness adds another 4,000 and 11,000 men and women to these figures.

Again, we need to be careful about self-reported reasons for inactivity, but some of the numbers are striking for younger people. ONS analysis shows that **among 16- to 34-year-olds,**[69] **there was an 69% increase, albeit from a low base, in people inactive because of progressive illnesses such as cancer between 2019 and 2022 – an extra 14,000 people.** These 14,000 individuals represent 9% of the additional economic inactivity among those aged 16-34. This shocking figure might reflect restricted diagnostics during the pandemic and record NHS waiting lists, meaning there is a backlog of people awaiting treatment.

However, the largest component of economic inactivity due to long-term sickness among younger people is mental health – specially 'mental health, phobias and nervous disorders', and 'depression, bad nerves or anxiety'. This accounts for 15% of the increase in inactivity among 16- to 34-year-olds since before the pandemic, and 70% of the increase for reasons of long-term sickness.

It is reasonable to suppose that much of this was driven by the stresses of the pandemic, including social isolation during lockdowns, which exacerbated the mental health impacts beyond similar trends observed in the wake of the 2008/9 financial crisis.[70] However, as we saw earlier, inactivity due to long-term illness in the general population began trending upwards fully a year before the pandemic began, increasing by 7% in the year to February 2020 (before increasing by another 17% through the pandemic). Mental health appears to have been an important driver of this trend. For example, the number of people in contact with NHS funded secondary mental health services increased by 9% in 2018/19 and 6% in 2019/20.[71] And as a rule of thumb, the

69 ONS, 'Half a million more people are out of the labour force because of long-term sickness' (10 November 2022). Link. More granular data is not publicly available.

70 R. Thomson & S. Katikireddi, 'Mental health and the jilted generation: Using age-period-cohort analysis to assess differential trends in young people's mental health following the Great Recession and austerity in England', Social Science & Medicine 214 (October 2018), pp.133-143. Link.

71 NHS Digital, 'Mental Health Bulletin Dashboard' (6 March 2023). Link.

younger the cohort, the more prevalent mental health issues are relative to older cohorts.

As discussed above, there has been a wider surge in disability due to mental health conditions across the population – which is doubly alarming since remaining in work is generally hugely beneficial for people's wellbeing. But there is a widespread

'Inactivity due to long-term illness in the general population began trending upwards fully a year before the pandemic began, increasing by 7% in the year to February 2020 (before increasing by another 17% through the pandemic)'

concern, not just in the UK, that teenage mental health problems and unhappiness is increasing – driven, many argue, by the rise of the smartphone.[72]

However, the problem in trying to diagnose the causes of this increase – and ensure that we are able to support those with mental health issues to remain in and/or rejoin the workforce – is that many of the most popular theories cut against each other.

For example, the increase in mental health diagnoses and treatment coincides with concerted mental health awareness campaigns carried out by the NHS since 2018,[73] preceded by regional campaigns overseen by Public Health England.[74] It could be that such campaigns succeeded in raising awareness of existing but hitherto ignored mental health conditions. But some academics have also suggested that mental health awareness campaigns are triggering hyperawareness about mental disorders, leading people to pathologise regular stress and anxiety – the so-called 'prevalence inflation hypothesis'.[75] Others have suggested that celebrity self-disclosure about mental health struggles has glamorised mental health and inspired youths to usurp a diagnostic label as a form of identity,[76] or in some cases to claim benefits.[77] (Under the Work Capability Assessment (WCA), claimants can get fast-tracked on to benefits if they express suicidal ideation or are judged at risk for self-harm, even if not found otherwise unfit to work. So there are incentives to inflate mental health problems in order to qualify for benefits – but we have no idea at all of the extent to which this might or might not be being abused.) Or it could be that all of these factors have coincided with, and been swamped by, the rise of the smartphone and social networking.

Fairly obviously, the policy solutions to these issues vary hugely depending on which of them is right. If the first explanation is preponderant, then we probably need to pump more funding into mental health resources, and perhaps have a direct clinical referral pathway from job centres and/or as part of the WCA or PIP, so that people who would not otherwise seek help with mental health have more opportunity to do so. In effect, this would mean incorporating mental health triage into job centres. (Various interventions aimed at the non-clinical population of people with mental illnesses have already been developed and backed up by peer-reviewed

72 N. Smith, 'Honestly, it's probably the phones', Noahpinion Substack (2 March 2023). Link.

73 NHS England, Every mind matters (December 2018). Link.

74 Se for example: PHE, 'New mental health campaign launched across the Midland's (10 October 2018). Link.

75 L. Foulkes & J. Andrews, 'Are mental health awareness efforts contributing to the rise in reported mental health problems? A call to test the prevalence inflation hypothesis', New Ideas in Psychology 69 (April 2023). Link.

76 F. Deboer, 'Mental illness doesn't make you special', UnHerd (29 April 2022). Link.

77 R. Lane, 'Expanding boundaries in psychiatry: uncertainty in the context of diagnosis-seeking and negotiation' Sociology of Health & Illness 42 (December 2019), pp.69-83. Link.

randomised controlled trials (RTCs),[78] including apps developed by UK mental health researchers.[79]) But if the prevalence inflation hypothesis is right, then this very approach could end up doing more harm than good.

As a first step, the DWP and DHSC should jointly commission a study on the effects on the UK population, and especially the young, of mental health and the impact of mental health policy. This should also be used to inform any revisions to how mental health is assessed for benefit purposes.

In summary, the 16-24 cohort is the second largest component of the increase in the economically inactive population since before the pandemic, with a net increase in inactivity of 105,000 people, accounting for 20% of the total. This group also saw the largest increase in its rate of economic inactivity. Yet this group has largely been overlooked in investigations into the post-pandemic persistence in economic inactivity. We urgently need to rectify this oversight. In particular, we should focus on the sharp increases in NEETs and avoid complacency about elevated student numbers; and we should try to get a better understanding of how exactly mental

> **'The 16-24 cohort is the second largest component of the increase in the economically inactive population since before the pandemic, with a net increase in inactivity of 105,000 people, accounting for 20% of the total'**

health is holding back young people from participating in the labour market.

But there is one more striking aspect of inactivity among the young that we have not yet discussed. That 105,000 figure is misleading, because in fact there are now around 11,000 more women of this age in the labour market compared to pre-pandemic – due in part to the sharp fall in women looking after their homes or families seen in the chart above – but 116,000 fewer men. And this, as we shall see in the next section, is far from unique. The final underexplored factor this paper will examine is that when we talk about a rise in economic inactivity among those under 50, we are largely talking about a rise among men. So what is driving it? And how do we fix it?

Why are so many working-age men economically inactive?

One of the most striking and under-discussed aspects of the economic inactivity crisis is that – with the crucial exception of the 50-64 cohort – the decrease in labour market participation since the pandemic has overwhelmingly been driven by men, not women.

The 18-24s are not alone. In fact, **in each of the 18-24, 25-34 and 35-49 age groups, the number of inactive men increased by 116,000, 102,000 and 52,000 respectively, whereas the number of inactive women actually fell by 11,000, 60,000 and 17,000.**

The large flow of women into the workforce represents a one-off boost to female labour market participation – but it is part of a trend that has been playing out for

78 J. Huberty et al, 'Efficacy of the Mindfulness Meditation Mobile App "Calm" to Reduce Stress Among College Students: Randomized Controlled Trial', JMIR Mhealth Uhealth 7 (June 2019). Link.

79 P. Garety et al, 'Digitally supported CBT to reduce paranoia and improve reasoning for people with schizophrenia-spectrum psychosis: the SlowMo RCT', Efficacy and Mechanism Evaluation 8 (August 2021). Link.

decades.[80] On average, women have been outperforming men in education for a couple of decades now, and the higher education participation rate for women was, until the pandemic narrowed the gap slightly, 12 percentage points higher among women (up from nine percentage points higher in 2006/7).[81]

There is reason to think that this educational trend has been starting to manifest in career outcomes at a structurally significant scale in recent years, with less-educated male workers struggling to compete against their (on average) better-educated female counterparts. At the same time, there has been an ongoing flow of women into many jobs that were traditionally male-dominated – but the flow has been much less pronounced in the other direction.[82]

Sadly, this is an area where the data is simply not good enough for us to draw definitive conclusions. Amid intensifying competition within certain sectors, more men might be opting out of work, especially if they do not perceive opportunities to retrain or move career. This might be reflected in the fact that, **of the extra 155,000 people aged 16-64 now economically inactive for the nebulous reason of 'other', 131,000 (85%) are men.** This category accounts for a third of the newly inactive men,

> **'Of the extra 155,000 people aged 16-64 now economically inactive for the nebulous reason of 'other', 131,000 (85%) are men'**

and indeed 15% of the total, versus 20% and 11% of women.

There is also probably some sort of psychological dimension to this which needs exploring, given the well-known and documented links between work and conceptions of masculinity, and negative feedback loops which can further lower employment prospects over time.[83] Prior to the pandemic, time spent on video games, enabled by dependency on their parents, was linked to young men withdrawing from the workforce in the US, with their annual game time increasing by 50% from 2004-2015.[84] In the UK, the housing crisis is resulting in record numbers of people living with their parents at age 30, which might be creating similar dependency patterns and forms of escapism from working life. So lifestyle changes and norms in popular culture, as reflected in the Reddit 'antiwork' forum and similar online communities, might be relevant to the male-dominated inactivity trend we are seeing.[85]

It should be stressed that without more detailed data about these missing men, this is mostly just informed speculation and inference from some of the things we do know about how education, working and lifestyle patterns have evolved over the last couple

80 It may also have a particular ethnic dimension, as we have long known that female labour market participation is relatively much lower in Bangladeshi and Pakistani communities than the national average, for example. So far however, little research has been done to see whether the economic shock of the pandemic has played out differently in different communities.

81 See for example: HEPI, 'Mind the gap: gender differences in higher education' (7 March 2020). Link.

82 The definitive exploration of these trends is to be found in R. Reeves, 'Of Boys and Men' (2022).

83 E. Roosmaa et al, 'Meanings of work in the narratives of Italian, Estonian, and Polish young people who experience labour market insecurity', Social Exclusion of Youth in Europe (2021). Link.

84 National Bureau of Economic Research, 'Declining Work Hours and the Rise in Young Men's Gaming', The Digest 9 (September 2017). Link.

85 Reddit, 'r/antiwork'. Link.

Conclusion

Ultimately, there is no simple answer to why, unlike in most other developed countries, economic inactivity in the UK is still so much higher than before the pandemic. The headline figures are the net product of countervailing trends in different age and sex demographics. And we haven't even been able to consider in a statistically rigorous way whether there are variations by household socio-economic stratification, though there does seem to be a white-collar/blue-collar divergence. Elevated economic inactivity is a complex phenomenon.

That also means that there is no silver bullet – no simple incentive or reform – that is going to get people back into work and stop rising inactivity from become in a persistent or structural rather than a transient or cyclical problem. We instead have to attack the problem from several angles, recognising that different policy responses will have efficacy on different groups over varying time periods.

> **'If we forget the young, and the male, in our response to problems in the labour market, we will just store up problems for the future – problems we cannot afford in an ageing society, and which will scar the lives of those affected for decades to come'**

But we also have to stop telling ourselves stories that are simply wrong – for example that this is being driven by the collapse of the NHS, or that this is predominantly a problem among women or the elderly.

As we have seen, the key groups that we need to focus on in the short term are the 50-64 cohort, and the 18-24 cohort. In the case of the former, policy changes – whether around health in the workplace, pensions or out of work benefits – will probably only be able to get a relatively small number of workers back. But they will be important nevertheless to ensure that higher rates of inactivity among older workers do not become the new norm, reversing the last decade of progress.

Among the young, we need to focus on the things that are holding people back from finding jobs, whether that is economic or psychological scarring from the pandemic, or more deep-rooted trends which the pandemic has merely boosted or accelerated. And in particular, we need to understand better what is going on with younger men. If we forget the young, and the male, in our response to problems in the labour market, we will just store up problems for the future – problems we cannot afford in an ageing society, and which will scar the lives of those affected for decades to come.

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