Labour Market Scarring

Key Messages

- A “scarring effect” is the link between unemployment and negative future experiences in the labour market.
- COVID-19 has had a significant effect on the labour force, and youth unemployment is more than twice the unemployment rate of the overall workforce.
- At its peak in Q2 2020, the unemployment rate had risen to 31.5% while youth unemployment was 67.4%.
- In July 2021, an estimated 75,000 young people are still Not in Education, Employment, or Training (NEET)
- Contact-intensive industries (hospitality, construction, retail) have been the worst affected sectors, accounting for the majority of PUP recipients.
- The long-term unemployment rate has increased from 1.3% to 1.7% between Q1 2020 and Q1 2021.
- The impacts of long-term unemployment are particularly severe for young people, estimated at a lasting wage penalty of 8-10% and an employment penalty of 6-9%.
- The long-term scarring effects on individuals come in the form of limited career prospects, reduced earnings, diminished skills, social exclusion, and health problems.
- The withdrawal of income supports could lead to a labour market with greater demographic inequality, rising poverty, and fewer jobs.
- For workers in firms and sectors that are no longer viable, the policy focus will shift to re-skilling so that these workers can transition to other sectors and prevent long term scarring.

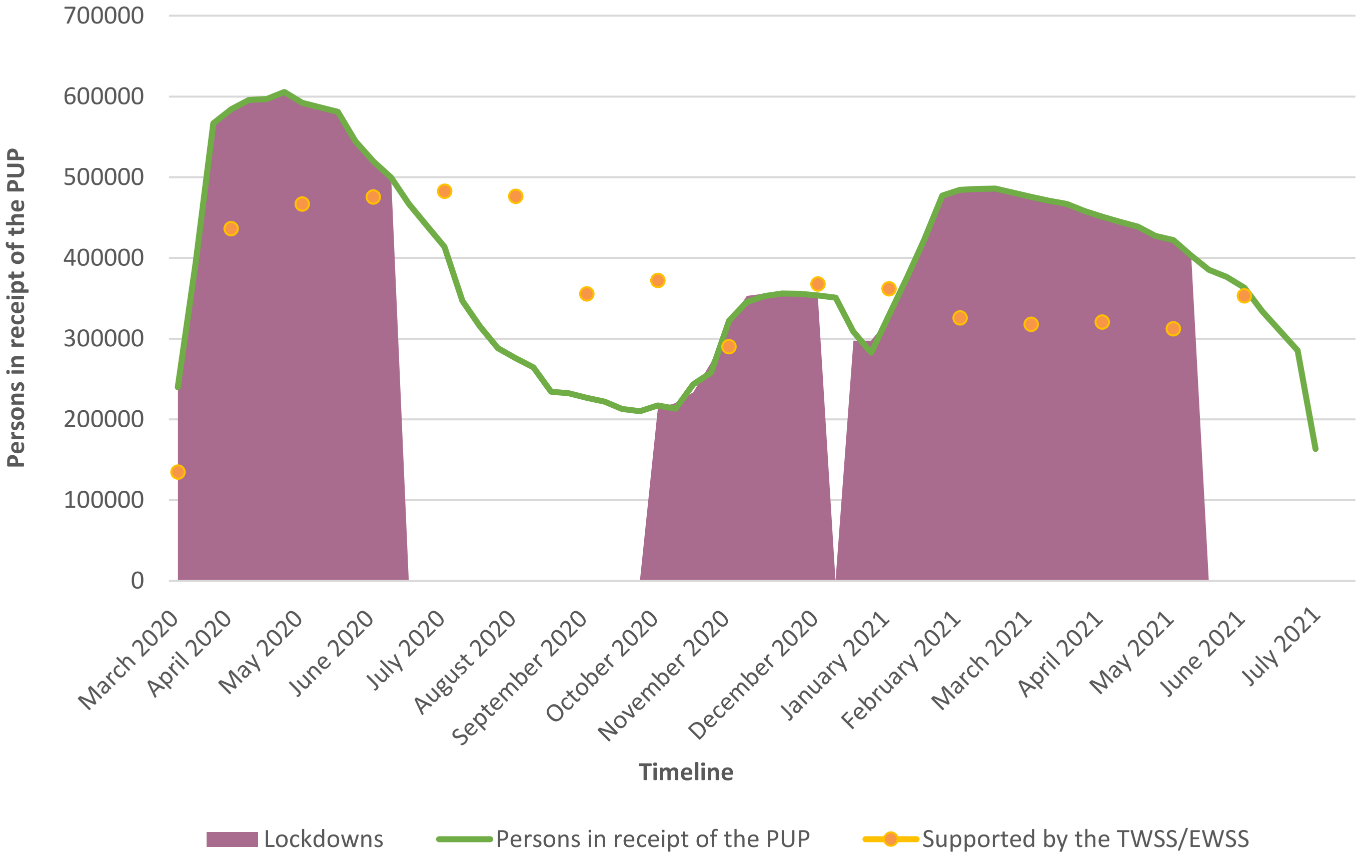
Introduction

The COVID-19 pandemic has caused major disruption to the economy and society more generally. While the easing of health restrictions has allowed many businesses to reopen, the link between unemployment and negative future experiences in the labour market (scarring effects) will be evident for years to come. Since March 2020, the implementation and loosening of public health restrictions on businesses have led to large fluctuations in the unemployment rate, surpassing 31% in April 2020.

The spike in COVID-19 infections and associated lockdowns resulted in a sudden rise in unemployment, causing a significant decline in the labour force participation rate and worker’s earnings. To combat this, in March 2020, the government introduced new schemes to assist those who were affected, the most notable of these being the

Pandemic Unemployment Payment (PUP) and Temporary Wage Subsidy Scheme (TWSS)/Employment Wage Subsidy Scheme (EWSS). In May 2020, PUP recipients peaked at 605,542 before dropping over 65% to 210,127 in September, the lowest number of monthly recipients in 2020. After that, rising Covid-19 case numbers led to a second national lockdown in October. In late December, a brief lifting of restrictions led to a reduction in PUP recipients before a third lockdown was introduced and PUP claimants reached 485,810 in February, the highest point of 2021. PUP claims have steadily declined since this point as vaccines have been rolled out and health restrictions eased.

Figure 1: Income support during lockdown



Source: CSO

The impact of the pandemic was not evenly distributed across sectors or age groups. Contact-intensive sectors (hospitality, construction, retail) and young workers (15-24-year olds) were the worst affected. At the same time, job losses were limited in sectors most conducive to remote working, such as ICT/finance. Office workers have seen a shift from a daily commute to working from home, while other sectors, E-Commerce, and IT services, have seen a surge in growth. The expansion in these sectors are unlikely to offset overall job losses which will result in a new cohort entering long term unemployment[1]. The long-term scarring effects on individuals of this, come in the form of limited career prospects, reduced earnings, social exclusion, and health problems.[2] This was prevalent in the aftermath of the 2008 financial crisis when unemployment reached at 16.2% in February 2012. The scarring effects caused by the pandemic will have long-term implications for the economy and will result in higher long-term unemployment and lower output.

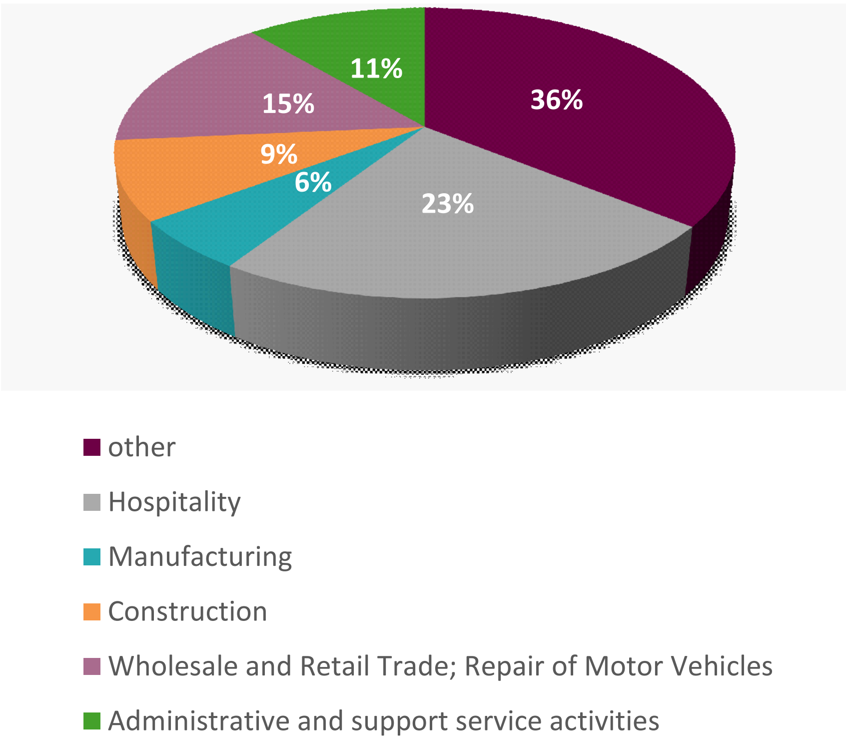
1 Lund, S. (2021, February 18). The future of work after COVID-19. Retrieved from McKinsey:
2 Pohlan, L. (2019). Journal of Economic Behavior and Organization. Unemployment and social exclusion, 273-299.

Sector Impact

Prior to the Covid-19 pandemic, conditions in the Irish labour market were close to full employment. In Q4 2019 the unemployment rate was 4.7%[3], youth unemployment was 11% and long-term unemployment was 1.6%. By Q2 2020, the unemployment rate had risen to 31.5%, youth unemployment was 67.4% and long-term unemployment had declined to 1.3%. The long-term unemployment rate has since increased from 1.3% to 1.7% between Q1 2020 and Q1 2021[4].

The sectors most affected by the pandemic are hospitality, retail, and construction. Since March 2020, jobs that require high physical proximity have experienced the most disruptions. This trend is likely to continue as health restrictions are slowly eased. The main challenge to these sectors will be to create a safe environment for both workers and customers to operate. Restrictions on all sectors were partially relaxed in May, and since then, the number of PUP recipients has fallen by 42%. Former hospitality, retail, and construction workers accounted for the biggest drop- off in PUP recipients, with a decline of 52%, 45%, and 41%, respectively, between May and July for each sector. While many of the restrictions were lifted, in July, there were still 91,037 claimants from the hospitality, retail, and construction sectors, accounting for 47% of PUP recipients.

Figure 2: PUP Recipients by all sector July 2021



Source: Department of Social Protection

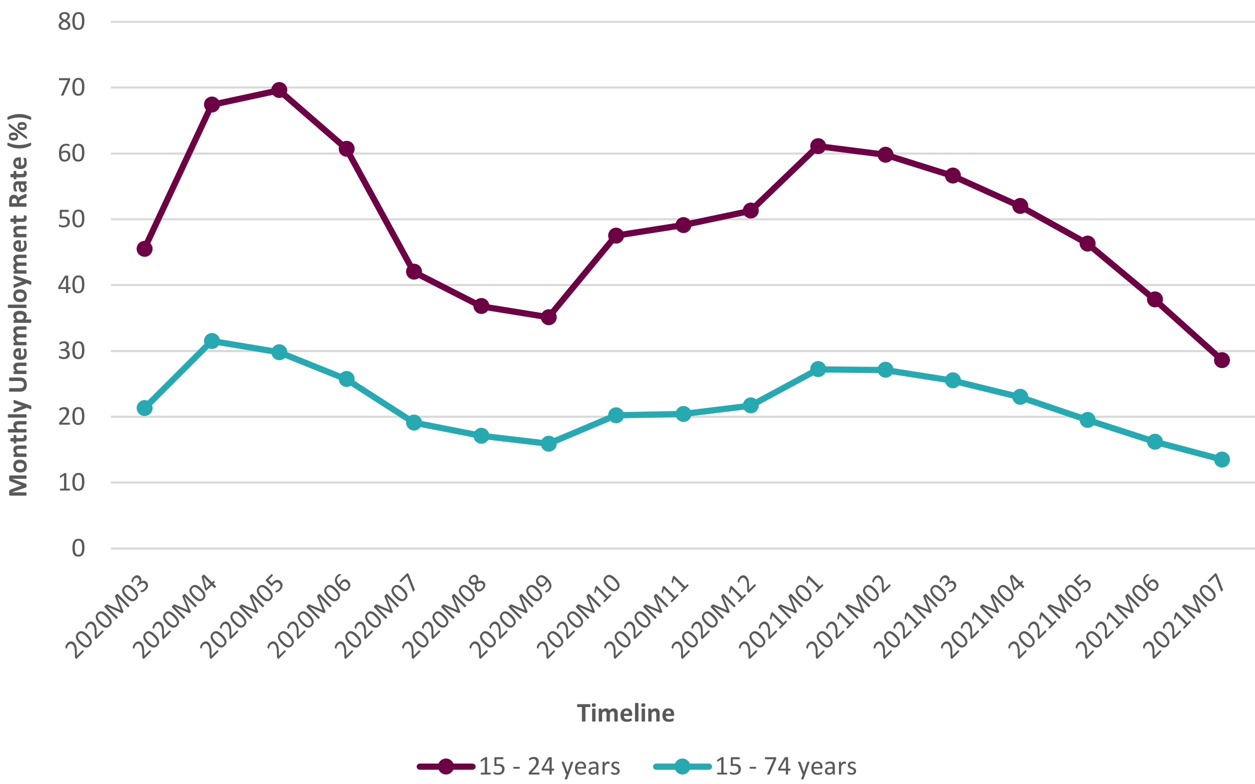
3 CSO Labour Force Survey (LFS) Quarter 4 2019
4 CSO Labour Force Survey (LFS) Quarter 1 2021

The pandemic also caused many behavioural changes that will have a permanent impact on certain sectors of the economy if they continue. For example, Covid-19 has shifted the outlook for the retail sector from the physical to the virtual marketplace. During the lockdown, the closure of physical stores accelerated the growing trend towards online retail, with 68% doing more online shopping now than before the pandemic[5]. The savings glut that developed during the pandemic, has afforded consumers additional disposable income to fund their pent-up demand, which drove online sales. The digitalisation of services has boosted growth in E-commerce and the delivery economy; however, these increases are unlikely to offset the job losses in stores or other sectors[6].

Furthermore, according to the National Remote Working Survey, over 95% of workers favour a hybrid working model[7]. In January 2021, the government published its National Remote Work Strategy, confirming its support to remote working given the positive benefits associated with it e.g. better work-life balance, positive environmental impact, and money savings. It is worth noting that continued remote working will reduce the return of the "spin off" effect, this will materialise through lower foot traffic and reduced demand for the service sector.

Youth unemployment

Figure 3: Upper Bound (COVID-19 Adjusted MUR) Youth unemployment



Source: CSO

5 Savage, N. (2021, March 31). Irish consumer trends post-COVID. Retrieved from KPMG
6 Lund, S. (2021, February 18). The future of work after COVID-19. Retrieved from McKinsey
7 Miley, I. (2021, May 18). Over 95% of workers support some form of remote working - survey. Retrieved from www.rte.ie

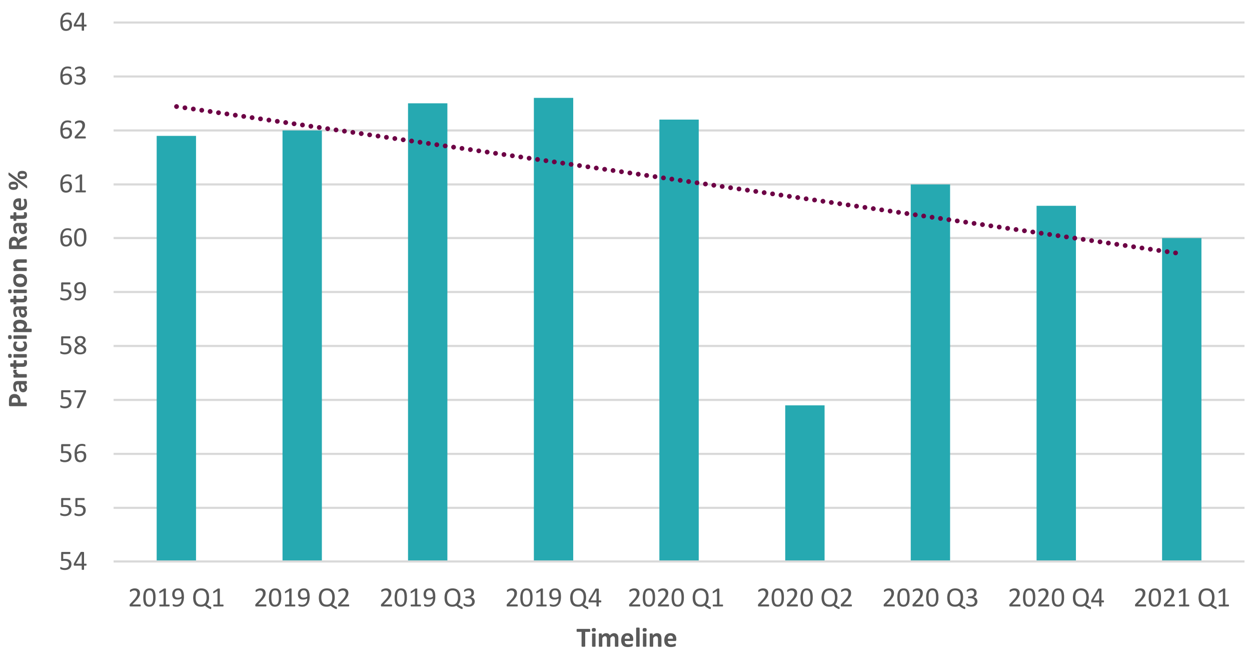
The Covid-19 crisis has hit prospects for young workers particularly hard and risks long-term "scarring" of employees and businesses[8]. Sectors such as construction, retail, and hospitality where young people were heavily employed cut thousands of jobs during the first lockdown, causing a spike in youth unemployment. Figure 3 shows the disproportionate effect on unemployment the pandemic has had on young workers versus the labour force. Since the beginning of the pandemic, youth unemployment has been more than twice the unemployment rate of the overall workforce.

Figure 3 also shows the high percentage of young adults in the labour force suffering from long-term unemployment (i.e., unemployed for 12 months or more). Since the introduction of the PUP scheme, young adults have made up a growing proportion of its recipients. In April 2020, young adults were responsible for more than 20% of PUP claimants, before peaking at nearly 26% in May 2021. Since this peak, the proportion of young adults claiming the PUP has declined steadily and is likely to proceed in a downward trajectory as restrictions are eased, and demand for labour rises.

The CSO recently announced that an estimated 75,000 young people are without education, training, or employment (NEET). In Q1 2021, 9.2% of Irish people aged 15-24 were classified as NEET, compared to the EU average of 11.3%. Many young workers begin their careers working service jobs but have been unable to obtain employment due to the pandemic. Young adults limited work experience will count against them when they are applying for part time/entry-level jobs, creating structural barriers, and preventing career development opportunities later in life[9]. When people are unemployed, their skills may diminish, their participation in the labour market may decline, and their mental health may suffer[10]. The impacts of long-term unemployment are particularly severe for young people, estimated at a lasting wage penalty of 8-10% and an employment penalty of 6-9%, relative to workers with similar characteristics[11].

Participation rate

Figure 4: Participation rate 15 years and over



Source: CSO

8 OECD. (2021). Labour market developments: The unfolding COVID-19 crisis
9 ILO. (2020). Global Employment Trends for Youth. International Labour Organisation.
10 Portes, J. The lasting scars of the Covid-19 crisis: Channels and impacts (2020, June 01).
11 OECD. (2021). Labour market developments: The unfolding COVID-19 crisis

The labour force participation rate (LFPR) hit one of its highest points of the decade in Q4 2019 with a rate of 62.6%, before reaching a record low of 56.9% in Q2 2020. The dotted purple line in Figure 4 represents the downward trend of the LFPR. Unemployment has risen especially for females, young adults, and workers without a tertiary education. There were 2,401,100 people in the labour force in Q1 2021[12], a fall of 60,800 (-2.5%) since Q1 2020. Longer unemployment spells tend to lead to an actual or perceived (by the employer) depreciation of a worker's human capital[13]. Long-term unemployment also has a substantial influence on a person's willingness to participate in the labour market[14].

Female workers and employees aged 55+ may face the greatest challenges in returning to non-supported employment. These groups have exhibited a higher propensity to receive pandemic-related income supports, suggestive of a higher potential flow into post pandemic unemployment or inactivity when the supports are phased out[15]. The flow to inactivity coupled with difficulties in job matching[16] due to skills mismatch, human capital loss, and other scarring effects may lead to negative implications for the labour force participation rate throughout the recovery period for some groups.

Withdrawal of supports

The extension to and gradual phasing out of the EWSS and PUP supports until December 2021 and February 2022, respectively, should help to avoid a significant cliff-edge unemployment event. As this occurs, the fog will begin to lift on which firms and sectors are viable in the 'new normal'. As the recovery takes hold in the second half of 2021 and into 2022, there will likely be a slower rate of job matching once people begin to seek employment and income supports are phased out.

The withdrawal of income supports could lead to a labour market with greater demographic inequality, rising poverty, and fewer jobs[17] for workers in hospitality, construction, retail. Workers in receipt of EWSS are vulnerable to unemployment when the supports are phased out, causing scarring effects that could last years in the form of lost human and economic potential. As the economy recovers and government income support is phased out, workers aged 55+, who account for 14% of income support recipients[18], may be at risk of becoming long-term unemployed or no longer participating in the labour force. For workers in firms and sectors that are no longer viable, the policy focus will shift to re-skilling so that these workers can transition to other sectors.

12 OECD. (2021). Labour market developments: The unfolding COVID-19 crisis
13 Lund, S. (2021, February 18). The future of work after COVID-19. Retrieved from McKinsey
14 ILO. (2020). Global Employment Trends for Youth. International Labour Organisation
15 CBI. (2021). Quarterly Bulletin 03. Dublin: Central Bank of Ireland.
16 Job matching refers to how well an individual's cognitive abilities, interests, and personality traits match those required for success in a particular job.
17 ILO. (2021). Update on the youth labour market impact of the COVID-19 crisis. International Labour Organisation.
18 CBI. (2021). Quarterly Bulletin 03. Dublin: Central Bank of Ireland

Upskilling

In the Government's July 2020 stimulus plan, an additional funding of €47.5 million was provided for higher-education skills-related programmes designed to enable people across the country to refresh or re-skill in their employment. 35,500 places were added to the higher and further education sector as part of these measures. In July 2021, just over €0.45 billion was allocated to the Education sector between the Departments of Education and of Further and Higher Education, Research, Innovation and Science. In the 2021 revised estimates for public services, an estimated €2.68 billion euro will be spent on skills development, higher education, research, and innovation (9.6% increase on 2020 estimates). The goal of these supports is to provide opportunities for Up-skilling and Re-skilling that meet the needs of individuals and the labour market.

The COVID-19 adjusted unemployment rate currently stands at 12.4% (August 2021)[19]. This high level of unemployment will require a detailed and co-ordinated strategy to help people back to work. Those in the most exposed sectors, in particular younger workers, have been the most significantly affected by the pandemic. To guide the labour market through the ongoing unemployment challenge and mitigate the long-term scarring effects, there will need to be a focus on reskilling and upskilling through further education and training. Embracing this would minimise the long-term scarring effects of the pandemic on the labour force.

19 *Department of Finance, Fiscal Monitor*: August 2021, (September 2021)