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Lessons for President Trump from a comparison of living standards and inequality in the US and the UK

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January 2017

Acknowledgements

The author would like to thank Harris Eppsteiner (Council of Economic Advisers), Steve Hipple (Bureau of Labor Statistics) and Brian Smith (Bureau of Economic Analysis) for their advice on use of US data. All errors remain the author's own.

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Executive Summary

"I will be the greatest jobs producer that God ever created. And I mean that, I really, I'm going to work very hard on that" was Donald Trump's promise at his last press conference before being inaugurated as the 45th President of the United States. This is a bold ambition, and one that few would discourage – but what should working hard on that mean for 21st Century America?

Donald Trump's election victory last year followed hot on the heels of the UK's vote to leave the European Union, leading to a common perception that the US and the UK are moving in step with each other politically. Certainly electorates on both sides of the Atlantic rejected the "establishment" and voted for significant change. For sure there are important differences underpinning the votes in the two countries – as previous Resolution Foundation work has shown – but there are many commonalities too, including the impact that longer term economic disparities had on the likelihood of votes for Mr. Trump or for Leave.

But, as this report will show, the economic performance of the two countries is much less similar than the political changes imply. Indeed, as Donald Trump takes office and looks to address the long-standing economic failures, which were in part drivers of his election victory, his focus will be on the very thing the UK economy has proved hugely successful at - getting people into work.

This report sets out how labour market trends have differed in the US and the UK in the years leading up to the election of Donald Trump. What's clear is that the two countries have followed very divergent paths.

Between 2008 and 2015 per capita employee income increased by just 0.6 per cent a year in the US and fell by 0.2 per cent a year in the UK. But it's not just the scale of this disappointingly low growth that has varied; the extent to which these outcomes have been driven by changes in employment and hourly pay has also differed significantly. **Since 2008, per capita employee income has *only* been boosted by increases in real pay in the US and has *only* been boosted by increases in employment in the UK**. This striking difference is reflective of the relative strengths (and weaknesses) of the two economies.

The relatively poor US employment situation has been driven by continued falls in labour market participation, most worryingly among prime age (25-54 year old) adults of both genders. This decline is often painted as an inevitable response to the unstoppable spread of automation and rise of globalisation. Yet the very different experience of the UK, where participation continues to rise and employment rates stand at historic highs, cautions against such economic determinism. Policy failures not fate explain the shift from the US being the envy of the developed world on employment to performing significantly below the levels seen in the UK and in some parts of Northern Europe. **Overall, if the US employment rate was a high as the UK's, 11 million more people would be in work than is currently the case.**

From the UK's perspective, the remarkable story on jobs appears to have involved a trade-off in the short term. Pay's long term driver, productivity, has weakened in both countries since the financial crisis, but the UK has suffered a bigger productivity hit than the US. This weakness is reflected in, and in part caused by, the UK's terrible pay performance. **Weekly pay for full-time workers would be £30 a week higher in the UK than it is today if it had returned to its pre-crisis peak, as has already happened in the US.**

But these very different experiences should not be taken as evidence of a binary choice between pay and employment. **Over the longer term higher labour market participation does not require weak pay – in fact the opposite may be true.**

The different paths trodden by the US and the UK in recent years have generated different outcomes in relation to one of the key elements of voter discontent: inequality.

Income inequality is high by international standards in both countries, having increased sharply over the course of the 1980s. Yet the picture of ever widening inequality – which has stimulated much debate in the US since Trump's election victory – has been much truer of the US in the last two decades than it has in the UK. **Indeed the UK's post-crisis performance shows a clear link between increasing labour market participation and reductions in inequality, with lower income households benefitting most as employment has increased beyond pre-crisis levels.**

Turning around the US's employment performance is central to the President's pledge to 'Make America Great Again'. Mr. Trump may have been criticised for many of the things that he said on the campaign trail, but he was right to highlight the long-run problems with employment in the US.

As his administration looks for policy ideas to help "bring back" jobs to the US, it could do worse than turn to the UK for an example of a country that, although similarly exposed to the forces of globalisation and the rise of automation in the workplace, has recorded rising prime age participation in recent years. UK policy over the past two decades has improved the incentive to enter work, supported lower-activity groups into work and has created a regulatory framework considerably more encouraging of maternal employment than in the US. Rather than devoting attention to building a wall or stopping international trade in its tracks, Donald Trump should look across the Atlantic for inspiration as to how he might bring back America's jobs.

Section 1

Introduction

This year marks a decade since the onset of the financial crisis. Starting in the US but with global implications, the impact of the collapse in confidence and demand that struck the global economy in late 2007 and early 2008 is still felt in the US and the UK today. Its effects were undoubtedly present in the votes for Donald Trump and to leave the EU last year. As previous Resolution Foundation research has shown[1], the economic situation did matter – along with other demographic and cultural factors – in both of these political events.

The financial crisis may have emerged from the US housing market but, looking back now, it's clear that it had more of an effect on output here in the UK than in the US. GDP fell further in the UK (by 6.3 per cent) than in the US (by 4.2 per cent) in the immediate wake of the crisis. The US has also recovered faster, growing by 16.5 per cent since the second quarter of 2009 compared to growth of 15.4 per cent in the UK. The UK economy has failed to catch-up with the US after experiencing a sharper fall in output in 2008-09.

Yet, despite a relatively strong recovery in output, the US has recorded a similarly poor living standards experience to the UK post-crisis. In the US, typical household incomes have fallen in almost every year between 2007 and 2013[2] and in the UK, although typical household incomes have now surpassed their pre-crisis levels, the living standards recovery has been poor in historical terms.

In the UK much of the recent income growth is a product of continued increases in pensioner incomes

Looking underneath the overall experience, however, reveals a significant divergence in income gains for working age and pensioner households in the UK. Typical working age households are still no better off than they were before the financial crisis, whereas typical pensioner incomes have risen by 13 per cent.[3]

Figure 1 compares the US and UK experiences over the same time period. It shows that between 2008-09 and 2013-14 typical working age incomes in the UK fell by an average of 0.8 per cent a year while pensioner incomes rose by an average of 0.7 per cent a year. Growth in pensioner incomes also outstripped growth in working age incomes between 2000-01 and 2008-09 in the UK; median pensioner income increased by an average of 3 per cent a year, almost twice as fast as median working age incomes.

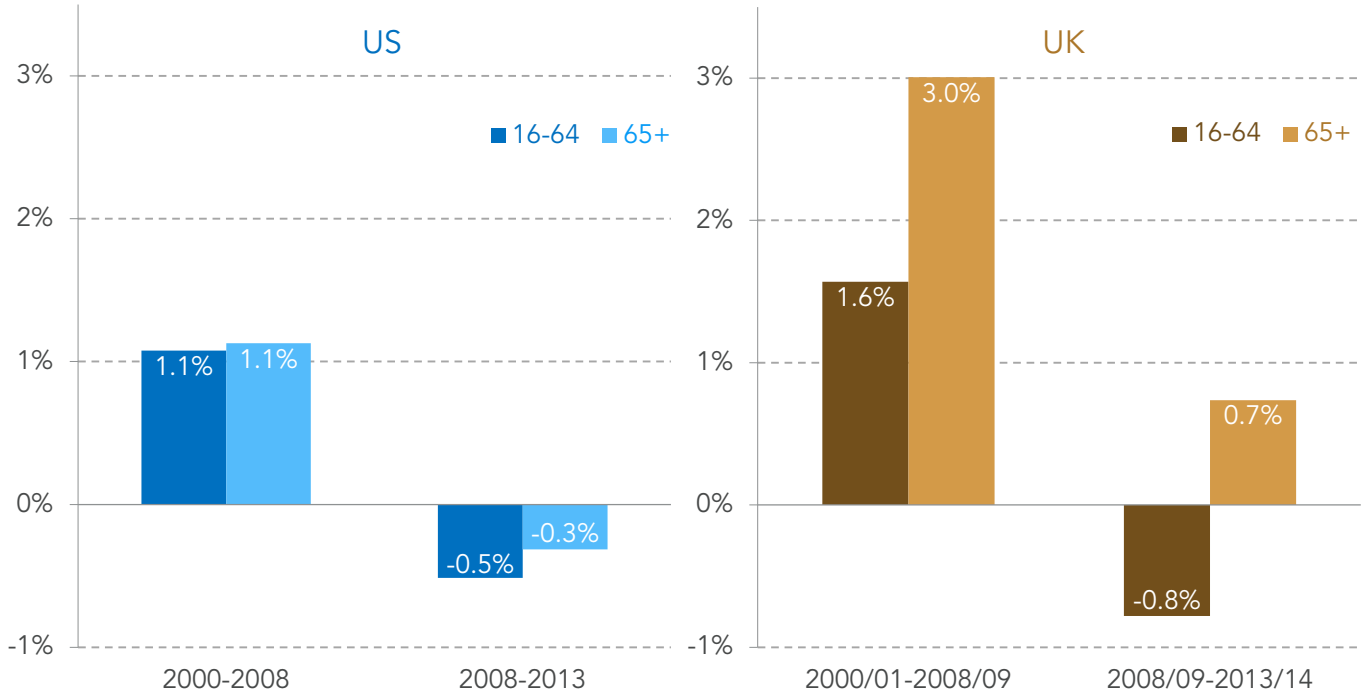
[1] S. Clarke & D. Tomlinson, In the swing of things, Resolution Foundation, November 2015

[2] The latest year for which we have comprehensive – post-tax – income data for the US. More recent data on household incomes is calculated on a pre-tax basis. Median income on this "Money Income" measure saw a significant increase in 2015, but not significant enough to push median incomes above their 2007 peak.

[3] Household disposable income and inequality in the UK: financial year ending 2016, ONS, January 2017

Figure 1: Working age and pensioner incomes since the millennium: US & UK

Average annual growth in median net household income



Notes: Deflated by the CPI-BHC adjusted (UK) and CPI-U-RS (US). Before housing costs. US data shows incomes of the middle quintile, not adjusted for household size. UK data shows incomes of the median, adjusted for household size.

Source: CBO, "The Distribution of Household Income and Federal Taxes, 2013.", Supplemental Tables 12, 13 and 14; RF analysis of DWP, Family Resources Survey

The future, too, is unlikely to provide working age households in the UK with strong income growth. The combination of cuts to working age welfare, higher inflation and the slowing of employment gains is likely to lead to a broad decline (from already low growth rates) in income growth and to falling incomes in the bottom third of the income distribution.[4]

Contrary to the UK situation, the age-based divide in income growth has not been replicated on the other side of the Atlantic. In the US there has been next to no difference in the income experiences of younger and older households. With both groups experiencing weak income growth pre-crisis (of 1.1 per cent a year) and falling incomes post-crisis (-0.5 per cent and -0.3 per cent respectively).

Of course, despite strong growth in pensioner incomes in the UK, it is still the case that median pensioner income remains lower – by £78 a week in 2013-14 – than median working age income when measured before housing costs.[5] This is also the case in the US, where median pensioner income was $123 a week lower than median working age income in 2013.

Since 2008, employment has done all of the work in the UK as earnings have done all of the work in the US

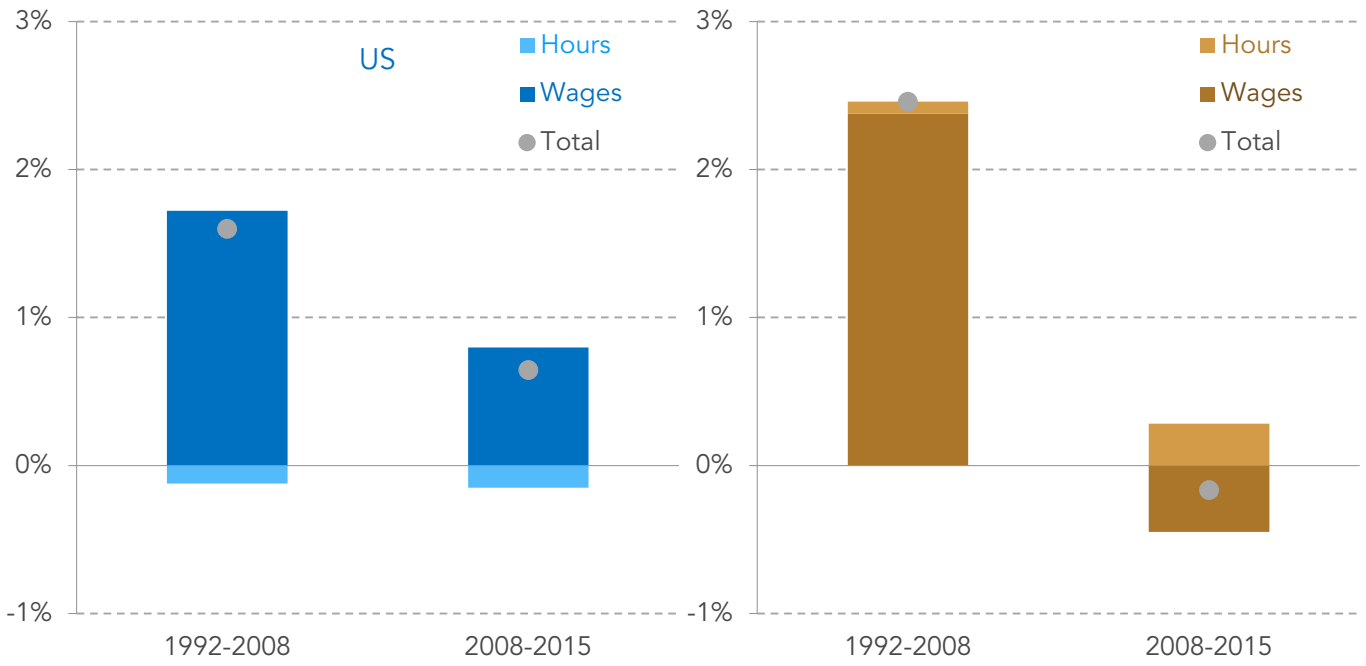
While both the politics and headline economics appear similar in the US and the UK, if we dig deeper we find that recent drivers of income growth have differed significantly across the two countries.

[4] A. Corlett et al., Bending the rules: Autumn Statement response, Resolution Foundation, November 2016

[5] Using after housing costs measures, median pensioner incomes have been slightly higher than median working page incomes since 2011.

Household income has a number of different sources, some more important than others. Employee income – the wages and salaries earned by employees – is the most important source in both the US and the UK. Dividing total employee income by the working age population (plus those over 65 in work) lets us create a per capita measure of this. Change in this per capita employee income can then be decomposed into changes in hours worked (a reasonable proxy for employment changes on a per capita basis) and changes in the hourly wage. Figure 2 sets out the results for the UK and the US in the sixteen years before the financial crisis and the eight years since.

Figure 2: Contributions to average annual growth in real per capita employee income: US & UK



Sources: ONS; BEA; BLS

Notes: Total wages and salaries divided by 16-64 population plus the 65+ employed population

The first thing to note is the significant slow down in per capita employee income growth recorded in both countries over the past seven years. Between 2008 and 2015, average annual growth rates collapsed to 0.6 per cent in the US and -0.2 per cent in the UK. This reflects the fact that pay has performed much worse than incomes in the UK.

Second, Figure 2 shows how growth between 1992 and 2008 was almost entirely driven by hourly pay in both countries. Increases in hourly pay provided all of the increase in per capita employee income in the US and all but 0.1 percentage points of the increase in the UK. In the US, hours provided a drag on growth pre-crisis, which is suggestive of a longer-run problem with employment and participation (as explored further in Section 2).

Hours continued to drag on average annual growth in per capita employee income in the US between 2008 and 2015, but the boost provided by hourly pay contracted somewhat. Nevertheless, this continued to explain all of the overall increase in per capita employee income. In contrast, hourly pay dragged on overall growth in the post-crisis period in the UK, with rising hours providing a partial offset.

This analysis shows that since 2008 per capita employee income in the UK has *only* been boosted by increases in employment and that in the US it has *only* been boosted by increases in real pay, implying that the US and the UK have had entirely different wage and hours experiences since 2008.

It is this big divergence, and the extent to which it reflects longer term economic trends, that the following sections of this report will explore in detail. The remainder of this report is laid out over four sections:

- The following section, Section 2, focuses on trends in employment and participation in the US and the UK. Showing how the US has fallen behind the UK on employment, largely as a result of the continuation of the pre-crisis trend for falling labour market participation.
- Section 3 considers pay and productivity. It highlights the slowdown experienced in both countries post-crisis, with the UK faring especially badly. It also shows how the US economy has been less adept at translating productivity gains into increases in the pay in the pockets of the typical worker.
- Section 4 brings the US weakness on employment together with another long-standing US problem: inequality. Looking to the UK post-crisis experience as an example, it shows how Mr. Trump's ambition to raise US employment could also have the effect of turning the tide on ever increasing US inequality.
- The final section, Section 5, concludes by setting out the lessons that President Trump could take from the UK's employment strength.

Section 2

Employment, unemployment and participation

President Obama has overseen the longest sustained period of US job growth on record. However, the US still has lower employment rates, and significantly lower participation rates, than either the UK today or its own past. In fact, participation rates among prime-age workers – both male and female – have been falling throughout the 21st century in the US. If the employment was as high in the US as it is in the UK almost 11 million more people would be in work.

President Trump's focus on jobs – "When I win on November 8th, I am going to bring back your jobs" – is certainly correct but it is important to look beyond the rhetoric to consider how and for whom Mr. Trump needs to deliver. We argue in this section that if the new President wants to solve the US participation problem he would be wise to the look to the UK's policy landscape, rather than to blueprints setting out the size and length of the wall with Mexico, for guidance.

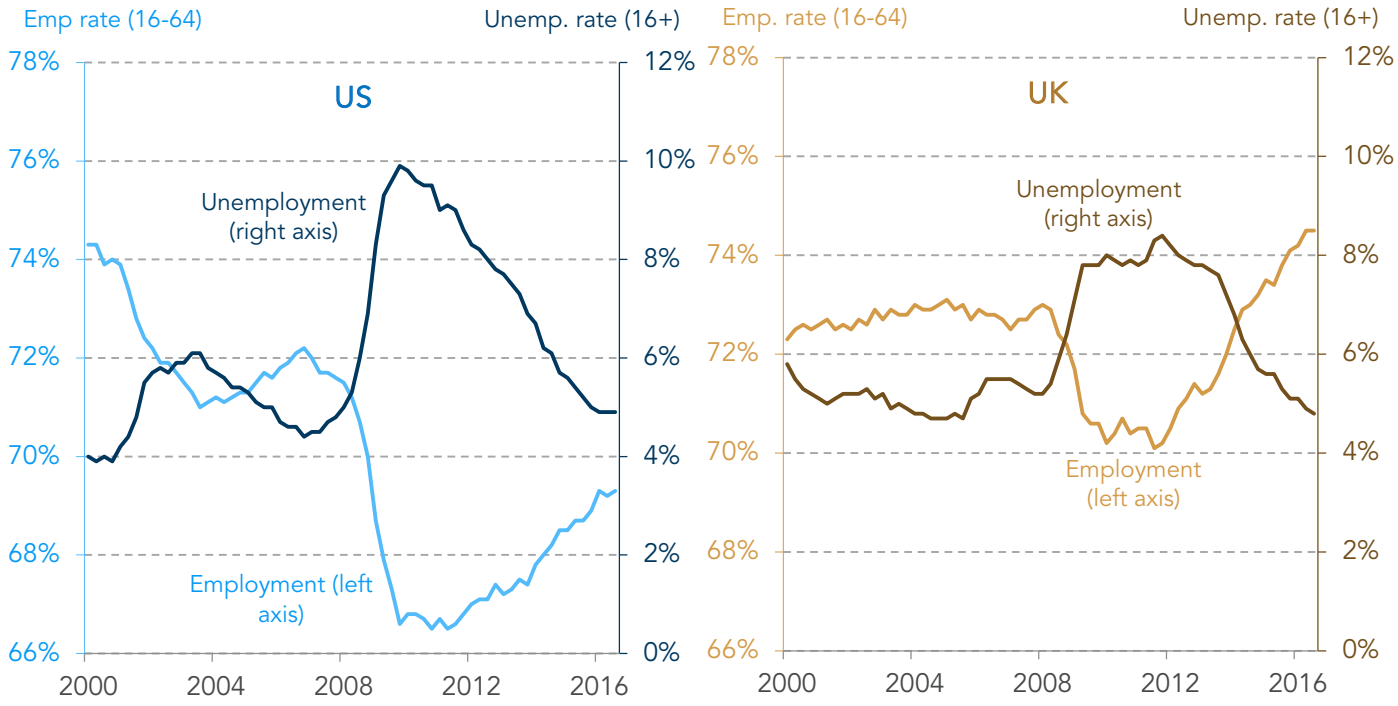
The US employment position has deteriorated, as the UK has surged ahead

The US has traditionally been seen as a better job creating machine than many European economies, including the UK. But, when compared to the UK today its current performance places it a distant second.

As Figure 3 illustrates, before the onset of the financial crisis the UK was only in a slightly stronger position on employment than the US. The UK employment rate averaged 72.7 per cent, 0.6 percentage points higher than the US average, between 2000 and 2007. On unemployment, the US was slightly ahead with an average unemployment rate of 5.0 per cent, compared to 5.1 per cent in the UK.

Figure 3: Employment and unemployment rates since the millennium: US & UK

Percentage of 16-64 year olds in employment (LHS axis), percentage of the 16+ labour force in unemployment (RHS axis)



Source: ONS, dataset identifier codes: ZXDX, MGSX, A48Q, LF24

However, this slim advantage in the pre-crisis years was lost towards the end of 2008 as unemployment rose faster, and to a higher level, in the US than in the UK. Unemployment peaked at around 8 per cent in the UK, and just shy of 10 per cent in the US, where it remained above 9 per cent for two and a half years.

Mirroring the sharper rise in unemployment, the US employment rate fell much further (by almost six percentage points), to a low of 66.5 per cent, than the UK employment rate (which fell by three percentage points). More recently the UK employment recovery has been remarkable with the employment rate surpassing its pre-crisis peak in mid-2014 and continuing to a record high of 74.5 per cent today.[6] That employment has reached a record high in the UK is, in part, a product of increasing self-employment (See Box 1 for more detail on trends in self-employment in the US and the UK).

[6] To a small extent this move to record employment rates will have been affected by the raising of the State Pension Age for women from 60 to 65 since 2010.

i Box 1: Trends in self-employment

The UK's strong employment performance of late has been driven, in part, by significant growth in self-employment. In fact, self-employment has been growing as a share of total employment through the whole of this century in the UK. In the US, however, self-employment has been steadily falling as a share of total employment throughout the 2000s and 2010s.

A remarkable 45 per cent of the growth in UK employment since 2008 has been a result of rising self-employment. As Figure 4 shows, self-employment now accounts for 15 per cent of all UK employment, up from 12 per cent at the turn of the century. In contrast, self-employment accounts for 10 per cent of employment in the US, down from a peak of almost 11.5 per cent in the mid-2000s.

Figure 4: Self-employment as share of total employment: US & UK

Source: ONS, BLS

It's not clear what has driven this stark divergence in trends. Employees in the US may have been less willing to give up their relatively secure status and switch to riskier self-employment in the years immediately following the financial crisis, in which unemployment was significantly higher in the US than in the UK. This, however, cannot account for the continued divergence more recently. Instead, it could be the case that the tax system and the lack of employment rights for the self-employed have incentivised self-employment to a greater extent in the UK than in the US. In addition, much of the growth in self-employment in the UK of late has been driven by greater numbers of older workers choosing to work in this way rather than retire[1]; a trend which has moved the other way in the US recently.

The so-called gig economy is often cited in the UK as a reason for the continued growth in self-employment. However, with studies concluding that "independent work" accounts for a larger share of employment in the US than the UK[2] and many of the larger gig economy businesses having started in the US it is more likely that other factors have driven up UK self-employment. In addition, as Figure 4 shows, these trends began long before many of the biggest businesses in the gig economy were even formed.

To date, reliable estimates of how much work is carried out in the gig economy are few and far between in both the US and the UK. However, this will change in the coming year as the US Bureau of Labor Statistics collects a new version of its "contingent worker survey" (which was last published in 2005). And in the UK the ONS is also investigating how it can best measure the sharing economy, from adding questions to existing surveys to making better use of use of administrative data. These moves are welcome; more detail on how many people are working in the gig economy and the extent to which its rise is affecting the magnitude of the self-employed population is needed.

[1] Trends in self-employment in the UK: 2001 to 2015, ONS, July 2016

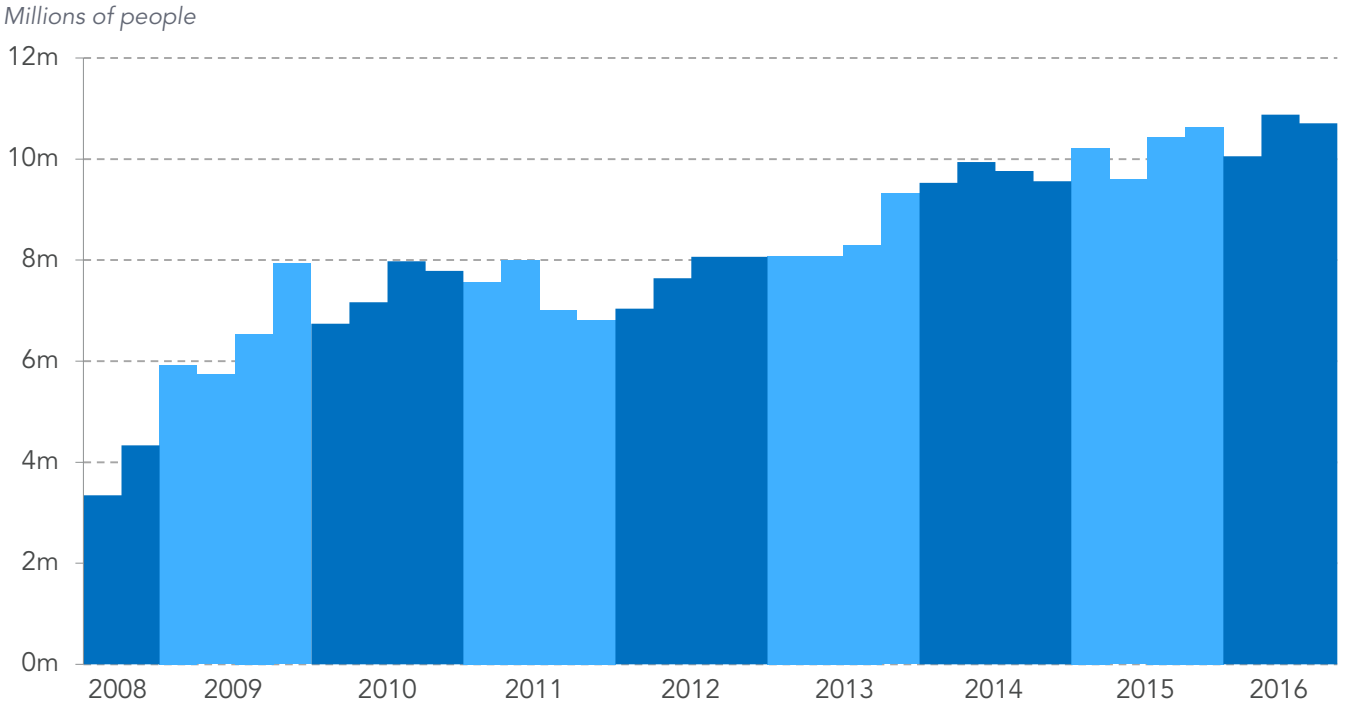
[2] Independent work: Choice, necessity and the gig economy; J. Manyika et al.; McKinsey Global Institute; October 2016

Even though Obama oversaw 75 months of sustained job growth (the longest period on record) and passes on a strong job market to his successor[7], the US employment rate is still 2.8 percentage points below its pre-crisis peak. This poor employment levels performance relative to the UK can be quantified by calculating how many more people would be in work in the US if it had the same employment rate today as the UK. As Figure 5 shows, **if the US had the same employment rate as the UK, there would be 11 million more people in work in the United States**. This isn't just a story of a few percentage points, 11 million people is equivalent to the population of Georgia – the 8th most populous state in the US.[8]

[7] See: Jobs Report: 2.2 million jobs gained in 2016; Unemployment ends year at a low 4.7%, On the Economy, Jared Bernstein blog, January 2017

[8] 2015 population estimates, US Census Bureau

Figure 5: Increase in US employment levels if the US employment rate (16-64) matched the UK's: 2008 Q3-2016 Q3



Source: ONS, dataset identifier code: LF24; BLS dataset identifier codes: LNU02075600, LNU02075379, LNS12000000

Downward trends in prime-age participation in the US are not, at all, reflected in the UK experience

Participants in the labour market are classed as either employed or unemployed (without a job but actively seeking work). Those without a job but not currently looking for work are classed as economically inactive – and are not included in unemployment statistics.

As there is now virtually no difference between the UK and the US in terms of unemployment rates (see Figure 3), the driver of the large employment gap between the two countries is, therefore, differences in trends in labour market participation.

The proportion of the population not in the labour force has been increasing since the turn of the century, a fact that Mr. Trump himself raised on the campaign trail:

> *5.3 percent unemployment - that is the biggest joke there is in this country...The unemployment rate is probably 20 percent, but I will tell you, you have some great economists that will tell you it's a 30, 32. And the highest I've heard so far is 42 per cent.*[9]

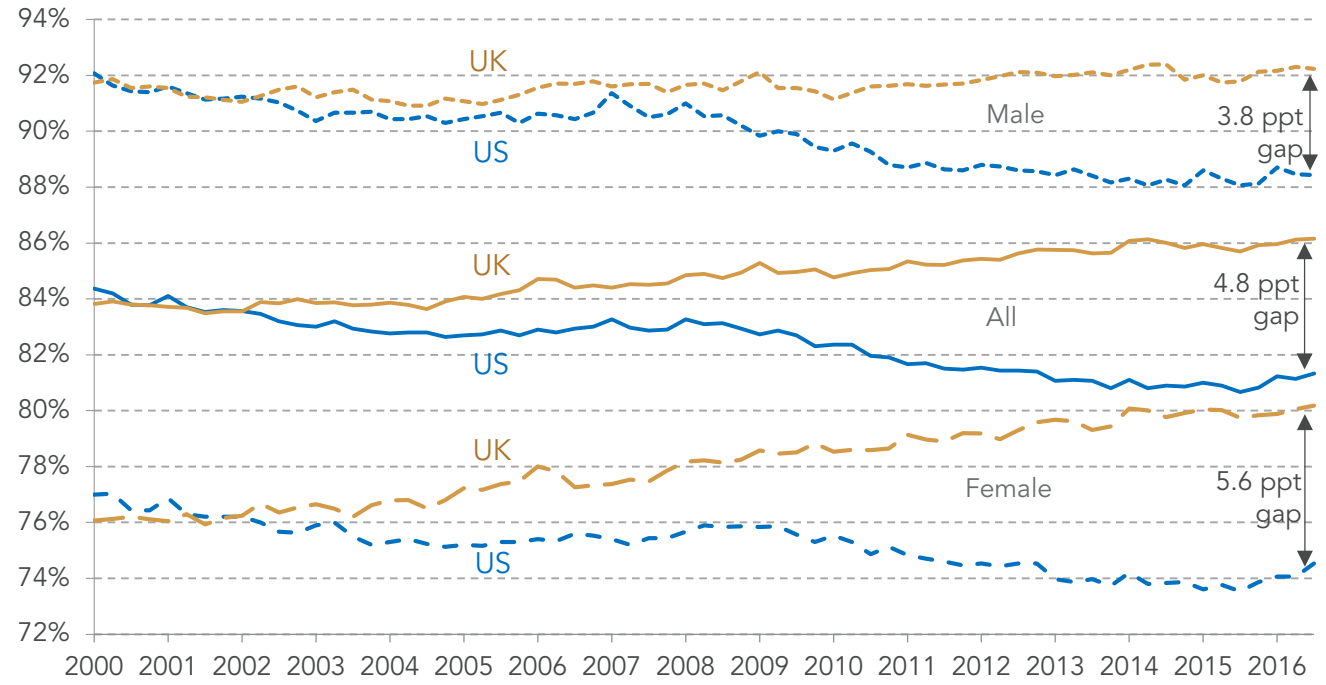
Mr. Trump's grasp of internationally agreed measures of unemployment rates isn't first class, but his estimate of "42 per cent" is close to the overall non-participation rate in the US. The proportion of the adult population outside the labour force in the US stood at 37.3 per cent in December 2016.

[9] Donald J. Trump, press conference on 28th September 2015

Of course, many of those not participating in the labour market are doing so for broadly positive reasons, most notably because they are in education or retirement. Demographic change and policy choices relating to the start and end of the working life can, therefore, have quite a significant effect on overall participation rates. But these factors are much less of an issue for those of 'prime age', aged between 25 and 54. As such, the fall in participation of this group of workers in the US is all the more remarkable. As the lines in the middle of Figure 6 show, the labour market participation rate those aged 25 to 54 in the US has fallen by almost 3 percentage points since 2000, from 84.4 per cent to 81.3 per cent in the third quarter of 2016. Participation rates have fallen for both men (by 3.6 percentage points since 2000) and for women (by 2.5 percentage points).

Figure 6: Trends in prime age labour market participation: US & UK

Labour force participation rate, 25-54 year olds



Source: ONS, Labour Force Statistics, BLS (LNS11300061, LNS11300061, LNS11300062)

Prime age participation rates have fallen across all races and ethnicities in the US too, despite significant differences in *levels* of participation. For example, 91 per cent of Hispanic and Latino men aged 25-54 are in the labour force, compared to 90 per cent of White men and just 81 per cent of Black and African American men. In contrast, prime age participation is highest among Black and African American women, at 76 per cent, and lowest among Hispanic and Latino women, at just 66 per cent.

Overall, even though the fall in prime age participation seems to have been halted over the past year, a large participation gap between the US and the UK remains. The stand out feature of Figure 6 is that the trends moved in totally different directions in the two countries since 2000. Prime age participation in the UK has risen by 2.3 percentage points since 2000, driven almost entirely by rising participation among women. Prime age female participation in the UK has risen by four percentage points since 2000, whereas male participation has increased by 0.5 percentage points.

Falling participation among prime age men is a trend that has continued for 60 years in the US. This had led some to the conclusion that this fall is a secular trend. However, that the trend in the UK is so notably different should provide pause for thought for those who hold the view ever increasing non-participation is an unavoidable future for modern labour markets in open economies. [10] The UK experience demonstrates clearly that the forces of globalisation and automation need not imply declining labour force participation.

Mr. Trump deserves credit for putting the low rates of participation at the centre of his economic pitch to voters. But, if the focus of his rhetoric to date forms the sole basis of policy action his administration will miss the gains to be had from raising female labour force participation rates.

Contrary to popular belief, the US has a larger participation gap with the UK among prime-age women than prime-age men

"Skilled craftsmen and tradespeople and factory workers have seen the jobs they loved shipped thousands of miles away."[11]

For President Trump, America's jobs problem is closely bound up with the impact that globalisation has had on America's manufacturing sector. His focus on the lack of jobs in the US economy is almost exclusively focused on the jobs that have traditionally been carried out by men. This strategy bore fruit in the election, Mr. Trump only won because he managed to swing states like Wisconsin and Michigan, with high rates of manufacturing employment, into his column. But a relentless focus on men's jobs will miss the fact that it is actually among female prime age workers that the US has a larger participation gap with the UK.

In the second quarter of 2016 prime age female participation was 5.6 percentage points lower in the US than the UK. This difference is one third larger than the male prime age participation gap. **If participation rates for each gender were the same as the UK in the US, there would be 5.4 million more people aged 25-54 in work in the US – 3.3 million more women and 2.1 million men.**[12]

To understand why this gap exists we can look at the reasons cited for non-participation. As Figure 7 shows, the increasing proportion of 25-54 year olds that cite 'home responsibilities' as the reason they are out of the labour force accounts for one quarter of the increase in economic inactivity between 2000 and 2015 in US.[13]

[10] For an example of this viewpoint see: L. Summers, Men Without Work, blog post, September 2016

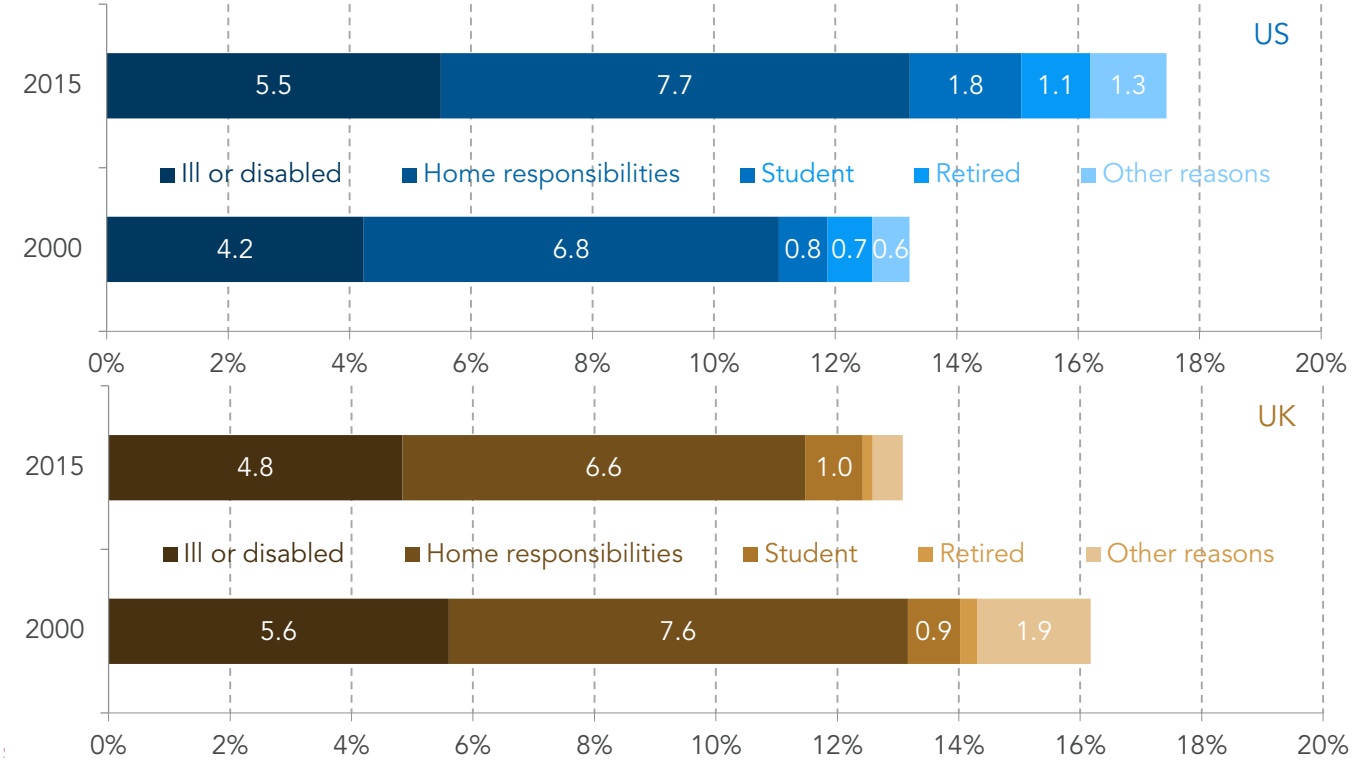
[11] D. Trump, speech, 28 June 2016

[12] Assuming that the rates of employment per participant in the labour market remain constant.

[13] In 2015 92 per cent of those who cite 'home responsibilities' as the reason for their non-participation in the labour market were women, down from 96 per cent in 2000.

Figure 7: Reasons for economic inactivity among the prime-age population: US & UK, 2000 & 2015

Proportion of 25-54 year old population not in the labour force, by reason



Notes: US and UK series are not directly comparable. US series based on Annual Social and Economic Supplement to the CPS, representing those who have been out of work for one year. UK series based on quarterly LFS, representing those who are out of work in the LFS "reference week".

Focusing on female participation, we find that 14 per cent of all women aged 25-54 were economically inactive with home responsibilities in the US in 2015, up from 12.9 per cent in 2000. In the UK, the statistics have moved in the other direction – from 14 per cent in 2000, to 11.9 per cent today; women have become more likely to be in work in the UK, and more likely to be looking after the home in the US over the past 15 years.

The proportion of prime age workers out of work with an illness or disability has increased in the US and fallen in the UK

As Figure 7 also shows, the proportion 25-54 year olds out of the labour force with an illness or disability increased from 4.2 per cent to 5.5 per cent between 2000 and 2015 in the US at the same time as it declined in the UK from 5.6 to 4.8 per cent.

The impact that rising disability has had on inactivity rates in the US has been well documented of late,[14] with new research from Alan Krueger suggesting that the health of prime-age men may be a significant contributing factor to declining US participation rates. He presents findings that show 47 per cent of economically inactive prime-age men take pain medication on a daily basis (which is more than double the rate of employed and unemployed men). Krueger also shows that 40 per cent of this group report that pain prevents them from working full-time in a job for which they are qualified.[15]

[14] See: J. Guo, The shocking pain of American men, Wall Street Journal, 13 October 2016

[15] A. Krueger, Where have all the workers gone?, Princeton University and NBER, October 2016

Some have suggested that causality might in fact run the other way, with Social Security Disability Insurance (DI) encouraging non-participation in the US. Nicholas Eberstadt (and others) have argued that disability benefits are incentivising worklessness, citing evidence that 57 per cent of economically inactive men live in households receiving some form of disability benefit.[16] However the fraction of prime-age men receiving disability insurance increased by 2 percentage points between 1967 and 2014, at the same time as participation among this group fell by 7.5 percentage points. The previous President's Council of Economic Advisers report into declining participation suggests that increasing receipt of DI accounts for, at most, 0.5 percentage points of this overall decline.[17] Cutting Disability Insurance is unlikely to provide a boost to participation rates in the US.

In the UK disabled employment rose throughout much of the 1980s and 1990s, demonstrating that policy failure can itself cause labour market problems. However, since the late 1990s the trend is moving in the right direction. Since then, falling rates of health-related inactivity have been a feature of the UK labour market. However, there is still more that can be done to boost employment rates of disabled people. As previous Resolution Foundation research has shown, the UK still has a large disability employment gap relative to other European countries. Halving this gap, as the government has pledged to do, would require a 1.5 million increase in the number of disabled people in work.[18]

More generally, changes in policy and pay have worked against higher participation rates in the US, and worked in favour of higher participation in the UK

Although certainly informative, the categorisation in Figure 7 does not fully capture the underlying causes of non-participation. For example, someone may be out of work providing childcare but they would be in work if the financial reward from entering work was higher or employment opportunities available to them matched their skill set.

These underlying causes are heavily influenced by the policy choices made by governments. In the UK the policy direction has been pro-participation over a prolonged period of time, this has not been the case in the US. [19]

In three areas, the UK government has acted in ways that have encouraged higher labour market participation – particularly among groups with traditionally low rates of activity.

First, successive UK governments have designed welfare programmes in order that they incentivise, and support, a move into work. Active labour market programmes, from the New Deal to the Work Programme, have successfully focused on improving the employment outcomes of specific groups facing long-standing challenges with accessing the labour market. [20] These programmes are considerably less common in the US; it spends just 0.1 per cent of GDP on active labour market policies, compared to an OECD average of 0.6 per cent of GDP.[21] Receipt of unemployment benefit in the UK has also been tied to job search activity for the past two decades. There is a debate as to the correct level and extent of conditionality that should be attached to benefit receipt, but it is clear that a link between the actions of the claimant and the receipt of payments has been beneficial for employment outcomes in the UK.

[16] N. Eberstadt, Men Without Work, Templeton Press, September 2016

[17] The long-term decline in prime-age male labor force participation, Council of Economic Advisers, June 2016

[18] L. Gardiner & D. Gaffney, Retention Deficit, Resolution Foundation, July 2016

[19] A. Corlett & P. Gregg, An Ocean Apart, Resolution Foundation, June 2015

[20] P. Gregg & L. Gardiner, The Road to Full Employment, Resolution Foundation, March 2016

[21] The long-term decline in prime-age male labor force participation, Council of Economic Advisers, June 2016

Second, the reward from low-paid work has increased in the UK over the past two decades. The wage floor in the UK has increased relative to median earnings, and is planned to increase further still over the rest of the decade, unlike in the US (for more detail see Box 2). In addition, in-work financial support in the form of tax credits has acted to increase to increase the incentive to move into work. Its successor, Universal Credit, is intending to continue this progress; however, recent cuts to this welfare reform cast doubts on how effective it will be at achieving this.[22] Evidence from the US suggests that these inequality reducing policies, such as tax credits and minimum wages, are likely to have had an impact on participation, finding that when wages towards the bottom are further below median wages, prime-age males are more likely to opt-out of the labour force.[23]

Third, in recent years the UK has acted to improve employment regulation, placing more requirements on employers to support mothers.[24] These policy changes have coincided with welcome increases in employment rates among this group. And in particular, for single parents the combination of regulation and improved financial incentives appears to have helped dramatically increase employment. In the US, there has been no such updating of policies and regulations. For example, maternity leave law is unchanged from legislation passed in 1993. It is still unpaid, can last for a maximum of just 12 weeks and doesn't apply to those working for small employers.[25] The US has been steadily falling behind other developed economies in terms of parental leave, part-time work and childcare provisions.[26]

Other economic trends may also be relevant, one of the more notable changes in the labour markets of both the US and the UK over recent decades is the decline in what were previously mid-skill jobs, so-called "hollowing out". In both countries mid-skill jobs have fallen as a share of the total over the past two decades, with the UK proving more adept at creating high-skilled jobs in their place than the US.[27][28] The reduction in mid-skill jobs is of relevance to participation because, as research by Foote & Ryan (2012) has shown, US workers with a mid-skill level who become unemployed rarely re-enter employment in either low or high skilled roles.[29] Mid-skill workers in the US are either more unwilling, or less able, to transition to jobs with different skill levels – and are increasingly likely to move from unemployment to non-participation, rather than back into work.

Taken together, these factors are all likely to have contributed to falls in prime age participation rates in the US, and the inverse outcome in the UK. There are other narrower, but still potentially significant, issues that may also be of relevance, most notably the high rates of male incarceration in the US; which some posit may be a significant driver of continued falls in male prime age participation, particularly among the African American population.[30] And more recently, the rise of video gaming in the US has also been linked to falling participation among men (though, why the

[22] D. Finch, Universal Challenge: Making a success of Universal Credit, Resolution Foundation, May 2016

[23] The long-term decline in prime-age male labor force participation, Council of Economic Advisers, June 2016 A. Corlett, Robot Wars, Resolution Foundation, July 2016

[24] P. Gregg & D. Finch, Employing New Tactics, Resolution Foundation, January 2016

[25] Family and Medical Leave Act, United States Department of Labor

[26] F. Blau and L. Kahn, Female Labor Supply: Why is the US Falling Behind?, NBER Working Paper No. 18702, January 2013

[27] A. Corlett, Robot Wars, Resolution Foundation, July 2016

[28] D. Autor, Why Are There Still So Many Jobs? The History and Future of Workplace Automation, Journal of Economic Perspectives, 29(3), p3-30, Summer 2015

[29] C. Foote & R. Ryan, Labor-Market Polarization Over the Business Cycle, Public Policy Discussion Papers No. 12-8, Federal Reserve Bank of Boston, December 2012

[30] See: J. Fox, Out of Prison, Out of Work, Bloomberg View article, 3 October 2016

same link doesn't hold in the UK is yet to be explored).[31]

Ideas from the Obama administration to better support unemployed and inactive workers were encouraging. For example, proposals for wage insurance that replaced up to 50 per cent of the lost wages of laid-off workers who enter lower paid roles would have helped with increasing the financial reward for returning to work. And more recently, the trend towards declining prime age participation in the US looks to have started slightly reversing. That said, the US is still performing poorly relative to the UK and other Northern European countries.

Mr. Trump's administration would be wise to look to the UK's success in this policy area as it seeks to increase employment and help inactive workers back into the labour force. Doing so might well bear more fruit than building a wall or threatening a trade war.

While the US has fared badly on employment, its recent record on pay and productivity is markedly better than the UK's. In the next section we contrast the two countries and consider whether lower pay is inevitable in an economy characterised by high employment.

[31] E. Hurst, Video killed the radio star: How games, phones and other tech innovations are changing the labor force, Chicago Booth Review, September 2016

Section 3

Pay and productivity

In the long run, it is productivity growth that drives growth in pay. Part of the underlying strength of the American economy that its productivity rates compare favourably to those of other developed economies, including the UK. Although the UK's productivity growth had kept pace with the US's in the decade before the financial crisis, since 2008 the long-standing US-UK productivity gap has widened significantly as productivity has declined in a much more dramatic fashion in the UK.

Taking a closer look at earnings growth before and after the financial crisis in the UK, we find that this productivity weakness is reflected in significantly weaker earnings growth. Over the past four decades, however, the UK has recorded a considerably smaller divergence between pay and productivity than the US.

Productivity growth has slowed in the US since the crisis, and ground to a halt in the UK

Between 2000 and 2007 productivity grew at a similar, but largely unremarkable pace, in both the US and the UK. Average annual productivity growth was 1.9 per cent in the UK and 1.8 per cent in the US.

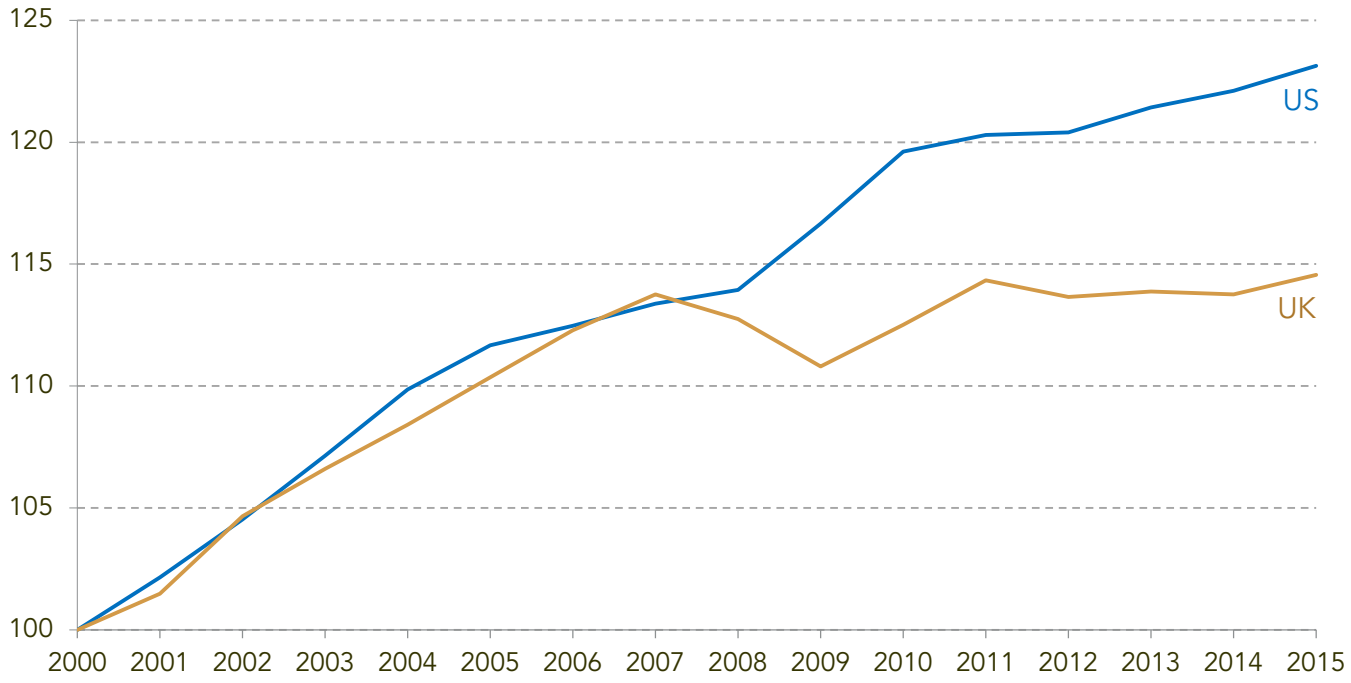
However, since 2008 productivity growth rates in the two countries have diverged significantly. Both countries have experienced a productivity slowdown but whereas productivity grew at an average rate of 1.1 per cent a year in the US between 2008 and 2015 it grew by just 0.2 per cent a year in the UK.

As a result, output per hour worked is less than one percent up on its 2007 peak in the UK, whereas it has risen by 8 percent in the US over the same time period, as shown in Figure 8. This rise is disappointing by historic standards, but is still the largest rise experienced by any county in the G7. The divergent productivity experience of the two countries means that the long-standing productivity gap between the US and the UK has widened since the crisis; productivity is now 30 per cent higher in the US than in the UK.[32]

[32] International Comparisons of Productivity, ONS, October 2016

Figure 8: Productivity growth since the millennium: US & UK

Output per hour worked, Index: 2000=100



Source: ONS, International Comparisons of Productivity

The reasons for weaker UK productivity growth since the financial crisis have presented somewhat of a puzzle to economists,[33] a puzzle that has only increased in recent years as productivity growth has continued to dissapoint even as the UK has returned to growth. This continued trend has meant that economic forecasters, including the OBR, are now becoming less confident that the UK will return to productivity growth rates seen before 2008.[34]

In the years immediately following the financial crisis, the UK's more significant producitivty slowdown was attributed, in part, to the impact of the recession playing out differently in different countries. Unemployment rose less in the UK than in the US (see Section 2) and, as UK firms maintained labour to a greater extent than was anticipated in the face of markedly weaker demand, productivity fell in the UK whereas it rose (at a relatively fast pace) in the US. However, with ongoing productivity underperformance other factors – such as reduced investment in, and inefficient allocation of capital – are likely contributors to continued anemic producitivty growth in the UK.[35]

In comparison to the UK, producitivty growth in the US since 2007 looks remarkable. However, since 2010 US labour producitivty has grown at just 0.6 per cent a year, significantly slower than the long-run (1948-2007) average growth rate of 2.2 per cent. Research from the previous President's Council of Economic Advisors suggests that this slowdown is primarily a product of negative capital deepening; the amount of capital available per hour worked has declined in the US since 2010, dragging down on labour productivity growth.[36]

[33] A. Bryson & J. Forth, The UK's Productivity Puzzle, NIESR Discussion Paper No. 448, 2015

[34] Supplementary forecast information release, Office for Budget Responsibility, 23 November 2016

[35] A. Barnett et al., The UK Productivity Puzzle, Bank of England Quarterly Bulletin, Vol. 54, No. 2, pages 114–28, June 2014

[36] J. Furman, Speech: Productivity Growth in the Advanced Economies: The Past, the Present, and Lessons for the Future, July 2015

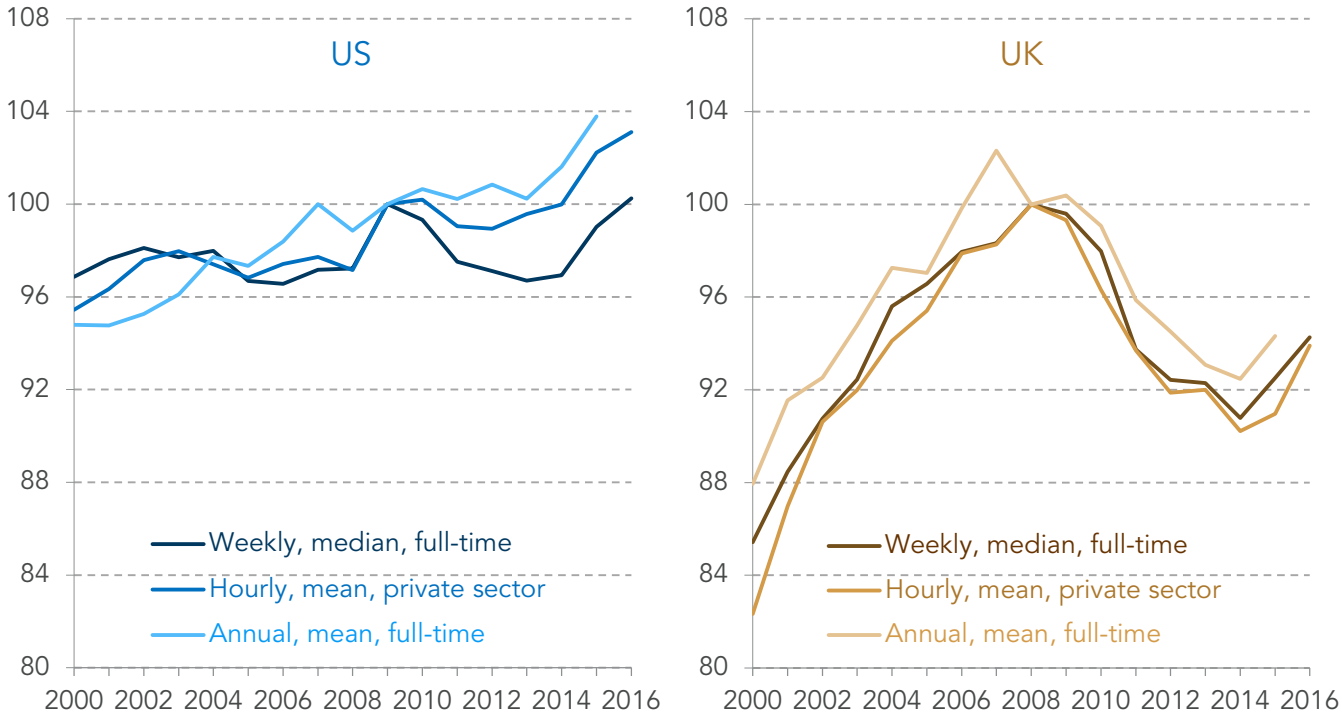
The UK's productivty weakness is reflected in a poor earnings performance since 2008

In the long-run, productivity increases are the main drivers of increases in earnings. This has certainly held true in so far as the UK has experienced both a weaker productivity performance and a weaker earnings performance than the US since 2008. Indeed the relationship between pay and productivity may run both ways with cheaper labour discouraging firms from investing in capital.

In total contrast to the employment picture in the US, earnings have relatively quickly recovered from their small post-crisis fall in the US but are still substantially below pre-crisis levels in the UK. Between 2009 and 2014 median weekly earnings fell almost three times further in the UK than in the US, as shown in Figure 9. Strikingly, mean hourly earnings (for private sector employees) were flat in the US, but fell by over 9 per cent in the UK.

Figure 9: Real earnings since the millennium: US & UK

CPI-adjusted, 2015 prices. Index: 2009=100 (US), 2008=100 (UK)



Sources: BLS, Average hourly earnings of all employees, total private (post-2006), production and non-supervisory employees (pre-2006) & Median weekly usual earnings. Series IDs: CES0500000008, CES0500000003 & LES1252881500); OECD, Real average annual wages; RF analysis of ONS, Annual Survey of Hours and Earnings

More recently, both countries have recorded a return to real earnings growth – but big differences in recent performances remain. US median earnings are now just above their pre-crisis peak yet, in stark contrast, UK earnings are still more than 5 per cent down on their 2008 level. If median earnings for full time employees in the UK had recovered the lost ground since the crisis, as has happened in the US, weekly pay for the typical full-time worker would be over £30 a week higher than it currently is.[37]

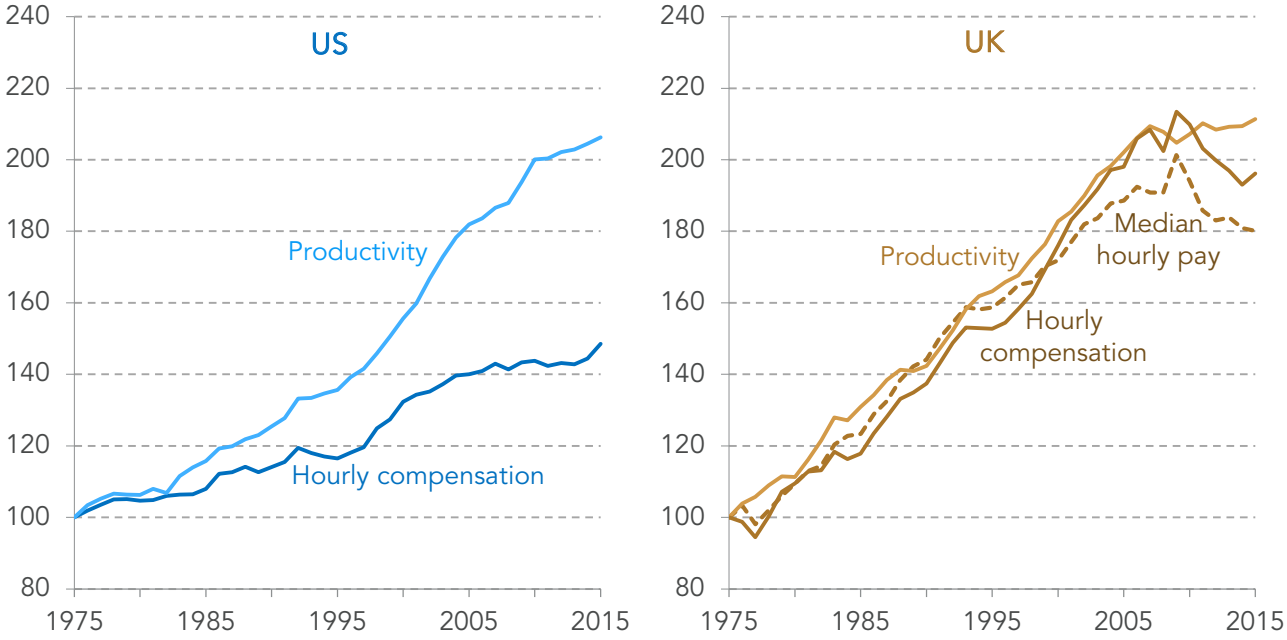
[37] This figure does not control for the impact of changes in hours worked. However, average hours worked by full-time employees has increased slightly between 2008 and 2016 (from 37.0 in 2008, to 37.5 in 2016). Therefore, controlling for hours worked would have acted to boost this figure.

Although, the US has a long-standing problem with earnings failing to keep up with productivity

Over the medium term, the US's relatively strong productivity performance has not translated into stronger earnings growth. Specifically, US weekly median earnings have increased by just 3.6 per cent between 2000 and 2016. In contrast, the equivalent UK measure has increased by just over 10 per cent over the same time period.

This is, in fact, far from a new phenomenon. As Figure 10 shows, a large gap has opened up between productivity and compensation in the US over the past 40 years. US productivity has doubled since 1975 while mean hourly compensation increased by half as much.

Figure 10: Productivity & compensation and pay: US & UK, 1975-2015



Notes: Productivity series deflated by the GVA deflator, US hourly compensation by the CPI-U-RS, UK median hourly pay and hourly compensation by the RPIJ

Source: US Bureau of Labor Statistics; RF analysis of ONS, National Accounts, Annual Survey of Hours and Earnings & New Earnings Survey

Hourly compensation is used on the left hand side of Figure 10, rather than pay, because employer provided benefits make up a larger proportion of the amount that employers spend on their staff in the US than the UK.[38] In particular, as noted by the Economic Policy Institute, the rising cost of healthcare relative to other goods and services means that an analysis of pay alone could understate the growth in the amount received by US employees.[39]

Before 2000 almost all of the gap between productivity and compensation was accounted for by different price deflators – the prices that consumers faced increased at a faster rate than the prices faced by firms – while after 2000 the majority of the gap can be explained by a fall in labour's share of income.[40] It is of course highly likely that if this analysis was carried a step further to include

[38] International Labor Comparisons, Bureau of Labour Statistics

[39] J Bivens & L Michel, Understanding the Historic Divergence Between Productivity and a Typical Worker's Pay, Economic Policy Institute, September 2015

[40] S. Fleck et al., The compensation-productivity gap, Monthly Labor Review, BLS, January 2011

the gap between median pay and productivity the wedge would be larger still as a result of the relatively weak income growth experienced by households in the middle of the income distribution in the US.

In contrast, in the UK productivity and hourly compensation have grown broadly in line with one another since 1975. However, as the chart on the right hand side of Figure 10 shows, a gap has opened up between productivity and median hourly pay over the past two decades. As previous Resolution Foundation research[41] has shown, this is largely a result of increases in pay towards the top and bottom of the income distribution outpacing increases at the median in the 1990s. From the 2000s, however, wage distribution effects have ceased to play a large role as variation in wage growth has evened out across the income distribution.

i Box 2: Minimum wages

Minimum wage policies in the US and the UK are undergoing something of a revolution of late. The main wage floor (for those aged 25 and over) in the UK is on a path towards 60 per cent of a typical (over-25) worker's hourly wage by 2020, after the announcement in July 2015 of the new National Living Wage. In total contrast the US federal minimum wage has not increased since 2009, meaning that voter led campaigns to increase state and city minimum wages have increased in importance in recent years.

The UK minimum wage was introduced in 1999 at a cash value of £3.60 an hour – equivalent to just over £5 an hour in 2016 prices – and after increasing significantly above inflation for a number of years, most notably in 2016, the minimum wage (for those aged 25 and over) in the UK is now at £7.20 an hour. The bite of the national minimum wage – the minimum wage as a proportion of median hourly earnings – increased from 47 per cent in 2000 to just shy of 60 per cent in 2016.

The US minimum wage policy landscape is more complex. The federal minimum wage (FMW) applies only where there is no state minimum or where the FMW is higher than the state minimum. There are currently 21 states in which this national minimum, currently set at $7.25, applies.

The FMW is not increased annually and so the bite[1] of the wage varies substantially depending on how recently an increase has taken place. It fell to just 25 per cent in 2006, rising to 33 per cent in 2009 (just after the most recent increase) and has been falling steadily over the past five years. The bite in 2016 was just 28 per cent, on a comparable basis the bite of the UK's National Living Wage is substantially higher at 47 per cent.

However, local – either city or regional – minimum wages apply across much of the US. The FMW may not have increased this year but a number of local minimums have. At the turn of the year minimum wages increased in 19 US states, providing a pay boost for over four million workers.[2] The impact of these local wage floors is likely to increase in the coming years as the work of the 'Fight for $15' campaign bears fruit. The grass roots campaign has secured commitments from many City and State governments to increase minimum wages to $15 an hour in the years ahead. For example, the minimum wage in New York State will reach $15 an hour by 2021. It has been estimated that local minimum wages will boost the "effective" minimum wage in the US by over $1 an hour this year,[3] a figure that is likely to continue growing if the FMW remains at $7.25.

[1] Calculated here as the minimum wage as a proportion of mean hourly private sector pay

[2] J. Jones, The new year brings higher wages for 4.3 million workers across the country, blog post, Economic Policy Institute, 3 January 2017

[3] J. Furman; Inequality: Facts, Explanations and Politics; lecture delivered in October 2016

[41] M. Whittaker, A recovery for all?, Resolution Foundation, September 2015

While the US has much to learn from the UK on employment it is clear that the UK has its own challenges on productivity and pay. On both of these metrics the UK performance has been poor both compared to other countries, and to previous recovery phases in its own economic history. The inverse of this weakness is that the UK employment rate is currently higher than it has ever been.

Longer term it is evident that there is not a binary choice between pay and employment increases; we know that tightening labour markets are usually accompanied by rising pay. However, in the short term it does look as if a trade-off did exist in the UK. Falling real pay may well have allowed employers to maintain, and then increase, employment levels with a smaller cost than would have been the case if real pay growth had not eluded the UK economy for five years.

In thinking about the consequences of pursuing a high employment strategy it is worth considering how the different experiences of the US and the UK have played out not just in terms of overall income growth, but across the distribution. That is what we turn to in the next section.

Section 4

Inequality and a pledge to "bring back our jobs"

Although Donald Trump himself has rightly focused on the need to increase employment in the US, much of the post-election debate has been focused on another problem: inequality. With the US recording one of the highest levels of income inequality anywhere in the world it's not hard to see why this might have been the case. There's a sense that dissatisfaction with the current economic order played a part in the anti-establishment nature of the votes in the US and the UK in 2016.

Yet, as with the picture on employment and pay, the inequality experiences of the US and the UK have diverged over the past two decades. While US inequality has risen consistently from the early 1980s onwards, in the UK inequality plateaued (at a high level) from the early 1990s and has fallen slightly recently. This has been driven by a number of factors, but the UK's superior performance on participation – especially in the post-crisis period – is likely to have played a key role.

In this section we consider these trends in inequality and how they relate to labour market outcomes. Showing that the UK experience highlights how increasing labour market participation and reducing inequality can be two sides of the same coin.

Income inequality increased in both the US and the UK in the 1980s and has continued increasing in the US. It changed little in the 1990s and 2000s in the UK, until it started to fall more recently

Regardless of the intentions of the man in the White House, the point in the economic cycle or the method of measurement used – inequality has risen in almost every year since 1979 in America. The disposable income of the top 10 per cent of households increased by 50 per cent between 1979 and 2010. At the same time, the income of those at the bottom of the distribution fell by 12 per cent.[42] America has been growing unequal for 35 years.

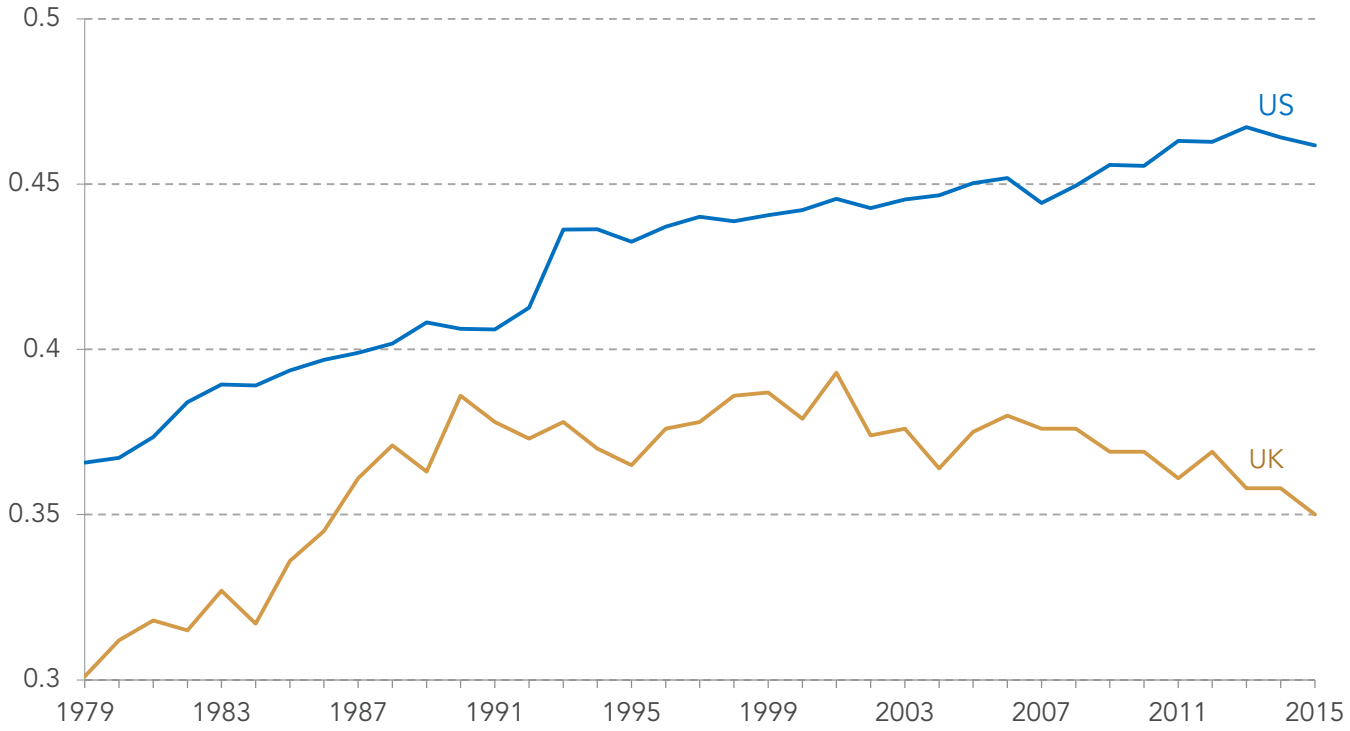
The Gini coefficient is one method used to capture the extent of inequality in a country. It can range from 0 which indicates perfect equality (a situation in which all households share total income equally) to 1 which indicates perfect inequality (where one household has all the income and all other households have none). On this measure, inequality in US gross household incomes increased by one-quarter (from 0.37 to 0.46) between 1979 and 2015. This rise is depicted in Figure 11 below. According to the OECD, the US now has one of the most unequal income distributions in the world; with only Chile and Mexico exhibiting higher levels income inequality.[43]

[42] RF analysis of S Thewissen, B Nolan and M Roser, Incomes Across the Distribution Database, INET, May 2016

[43] OECD Income Distribution Database: Gini, poverty, income, Methods and Concepts

Figure 11: Trends in inequality since 1979: US & UK

Gini coefficient, gross (pre-tax) income, 1979-2015



Source: US Census Bureau; ONS

In contrast to the US experience, the level of inequality in the UK – although still high in historical and international standards – has been largely flat over the past two decades and has fallen modestly more recently.[44]

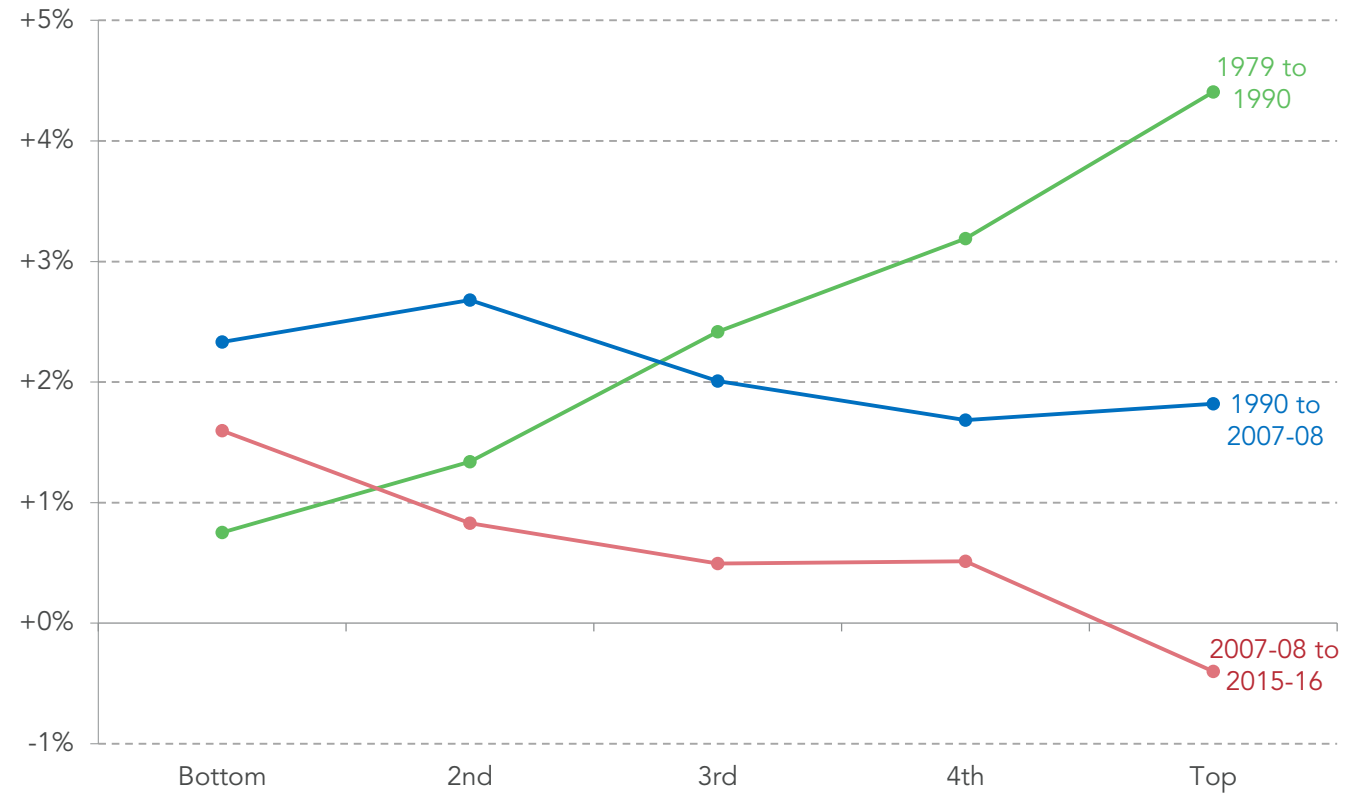
Rising employment has contributed to falling income inequality in the UK

Household income inequality changes from year to year depending on how incomes grow, or shrink, across the income distribution. A welcome trend since 2007-08 is that households at the bottom of the income distribution have experienced the fastest growth in incomes – leading to falling inequality. Less welcome, though still contributing to this fall, is the way in which income growth has fallen at the top of the income distribution. These trends are set out in Figure 12.

[44] Trends in income inequality as measured by the Gini coefficient can show a somewhat different picture depending on the measure that is used. It is worth noting that the Gini coefficient based on the larger Family Resources Survey shows income inequality has fallen more marginally in recent years. That data source also allows incomes to be measured after housing costs. Using this approach the Gini also continued to rise, albeit very slowly, after 1990.

Figure 12: Household income growth over selected time periods: UK, 1979-2015-16

Average annual growth in median equivalised household disposable income in each income quintile



Notes: Deflated by the CPIH

Source: ONS, The Effects of Taxes and Benefits on Household Income

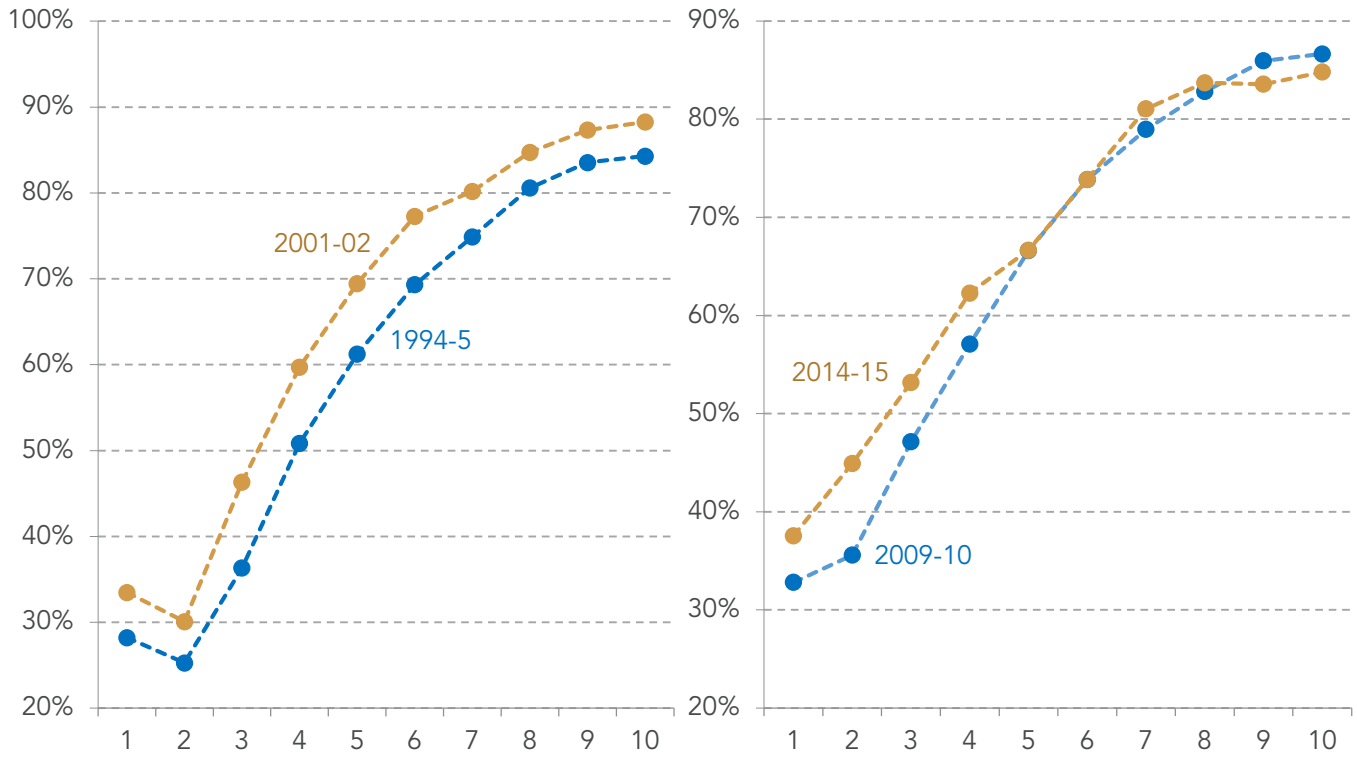
Falling household income inequality in the UK is a product of a range of factors. Including the impact of changes in the tax and benefits system, the relatively strong growth in pensioner incomes (which are lower, on before housing costs measures, than the incomes of working-age households) and the way in which increases in employment have been concentrated among lower income households[45] – it is this last factor that is of most relevance to this paper.

As Figure 13 demonstrates, the employment gains in the UK since 2009-10 have largely been a product of rising employment rates among those households in the bottom half of the income distribution. The proportion of households that contain no-one in work has declined rapidly since early 2010, falling from 19.2 per cent to 14.9 per cent in the second quarter of 2016.

[45] C. Belfield et al., Two decades of income inequality in Britain: the role of wages, household earnings and redistribution, IFS Working Paper W17/01, January 2017

Figure 13: Employment rates by decile of the 16-69 year old equivalised net household income distribution

Employment rates by decile of the 16-69 year old equivalised net household income distribution



Notes: Households are included in this analysis if they contain at least one adult aged 16-69.

Source: RF analysis of DWP, family resources survey

A comparison between the two sides of Figure 13 makes clear that employment growth is not always concentrated among low-income households. In the late 1990s, employment gains were enjoyed across the household income distribution. And, of course, the pattern shown in the right-hand side of Figure 13 will, in part, reflect the way in which households containing people who lost work moved down the income distribution but, all else equal, it is still the case that this employment recovery has been inequality reducing.

However, the UK's high employment rate does not mean that labour market policy makers can relax. Reaching full employment in the UK would still mean, on a stretching target, an additional two million people in work.[46] More can still be done to boost labour market participation. In addition, the rise in the number of households experiencing in-work poverty and, linked with this, a growth in the number of insecure jobs are both concerning trends. But, the inequality reducing effects of the UK's employment growth should be celebrated.

The US experience on employment and inequality isn't inevitable

As set out in Section 2, the UK experience demonstrates that modern, open, economies can increase employment even in the face of overseas competition and ongoing automation. With the right policy mix, these forces need not lead to a decline in the overall number of jobs. Predictions

[46] P. Gregg & L. Gardiner, The Road to Full Employment, Resolution Foundation, March 2016

that, for example, one-third of prime age males in the US will be out of work by 2050[47] are highly unlikely to come to pass. And if they do, it will be a product of damning policy failure rather than inevitable forces.

Relatedly, the inexorable rise of household income inequality in the US is trend that can be reversed. It is well documented that the lack of redistributive power of the US state is one important reason why inequality is so high in the US.[48] But, if the new President and the Republican controlled Congress are not inclined towards greater redistribution – the UK's recent experience shows another way to decrease inequality: boost employment.

Over half of all the workless households in the US are in the bottom fifth of the household income distribution.[49] So, even though many of these will be pensioner households, it is a reasonable assumption that employment gains from raising the US's labour market participation are likely to be tilted towards those households towards in the lower half of the income distribution. If this were to be the case, the impact of boosting employment may actually have more of an inequality reducing effect in the US than in the UK, due to the relative generosity of the UK's welfare provision for those out of work.[50] There is a lot that the US, and the households within it, has to gain from an about-turn in trends on labour force participation.

[47] See blog post by L. Summers, Men Without Work, 29 September 2016

[48] J Gornick & B. Milanovic, Income Inequality in the United States in Cross-National Perspective: Redistribution Revisited, LIS Center Research Brief (1/2015), May 2015

[49] RF analysis of US Census Bureau, Current Population Survey, HINC-01

[50] A. Corlett & P. Gregg, An Ocean Apart, Resolution Foundation, June 2015

Section 5

Conclusion

Donald Trump winning the keys to the White House was as unexpected an event as any we've seen this century. And in economics, as in politics, this report has shown that the unexpected can happen. A few decades ago, the US was seen as a shining example of an economy structured to deliver high employment rates; now it is languishing a long way behind the UK and other Northern European countries on employment (despite remaining a much richer country). Similarly, the UK was seen as an economy destined for rising inequality but – though still at a comparatively high level – UK inequality has been flat or slowly falling for a number of years.

In this vein, even if the forces of globalisation and automation have led some to expect nothing other than continued rises in non-participation, it would be unwise to conclude that the US's employment position cannot be turned around once more. The UK experience shows that this is possible and that by boosting participation the new President may find that he reverses the trend towards ever higher household income inequality.

That is the optimist's case. Less positively, it is not clear that building a wall, cutting taxes for the rich or punishing businesses for using overseas production is a policy platform that provides the best route for raising employment. Instead, lessons should be learned from the UK's policy landscape which has undoubtedly contributed to its recent success on employment. Three broad areas of policy change (forming an acronym – D.J.T. – that the new President may appreciate) worth focusing on are:

1. *Designing welfare policies that encourage entry into work*

The UK's welfare system has made increasing use of active labour market programmes, designed to reduce the incidence of long term benefit receipt. These programmes have been targeted at specific groups with lower rates of labour market activity, providing training and support to help improve their employment prospects. The receipt of unemployment benefits in the UK is now specifically tied to claimants' ability to demonstrate that they are looking for work and single parents' Income Support is now withdrawn once their youngest child reaches 5 years old. Introducing more support and conditionality to the US welfare system would likely act to increase labour market participation.

2. *Jacking-up the financial reward from entering low-paid work*

The UK's current system of in-work support was based on the US Earned Income Tax Credit (EITC), but it now has a greater coverage, and greater generosity than its US forerunner. Tax Credits have acted to boost the incentive to enter work. In addition, as set out above, the UK now has a significantly stronger minimum wage than the US. For both of these reasons, the financial reward for entering work on lower wages has increased over the past 20 years in the UK; Mr. Trump should consider how he might replicate this trend in the US.

3. *Tackling the maternity challenge*

Over the past 20 years, the UK has developed a strong suite of policies to support maternal employment. Maternity leave and statutory maternity pay have been expanded and the extent to which parents have to bear childcare costs has been reduced too, with 30 hours of free childcare for 3 and 4 year olds being introduced later this year. In contrast, US maternity legislation has

remained largely unchanged since 1993. Overall, Blau and Kahn (2013) suggest that policy changes across OECD countries account for 29 per cent of the fall in the US female labour force participation rate relative to other developed economies between 1990 and 2010.[51] If the US could match the UK in this policy area the gains in terms of high labour market participation could be substantial.

Of course, the US is not alone in facing economic and living standards challenges. Closer to home, Theresa May's focus on a new industrial strategy for the UK is welcome. However, words will not be enough. Governments have repeatedly set out to boost productivity and improve the underlying performance of the UK economy, but most have failed to deliver. The UK's low – and stagnant – productivity should be the economic trend of most concern to economists in Whitehall; boosting productivity through increasing investment in the physical and human capital in the UK would be a good place to start.

Further, policy makers in the UK should seek to build on the relative success of the UK labour market. With the employment rate at a record high further employment gains will be more difficult to achieve through economic growth alone. Depending on the impact of the UK's exit from the European Union on the labour market, policy measures that help low-activity groups – particularly disabled people – into employment will increase in importance in the years ahead.[52] More broadly, the government's planned cuts to Universal Credit – which were reduced to a very small degree at the 2016 Autumn Statement – are a worrying reversal of the pro-participation trend in labour market policies in the UK.

[51] F. Blau and L. Kahn, Female Labor Supply: Why is the US Falling Behind?, NBER Working Paper No. 18702, January 2013

[52] For detail see: P. Gregg & L. Gardiner, The Road to Full Employment, Resolution Foundation, March 2016 *and* L. Gardiner & D. Gaffney, Retention Deficit, Resolution Foundation, July 2016

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- *undertaking research and economic analysis to understand the challenges facing people on a low to middle income;*
- *developing practical and effective policy proposals; and*
- *engaging with policy makers and stakeholders to influence decision-making and bring about change.*

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