

Box C

The Labour Force Participation Rate

The participation rate is an important indicator of the supply of labour. It measures the share of the working-age population either working or looking for work. The participation rate has risen over recent decades, peaking in late 2010 (Graph C1). However, over the past two years the participation rate has declined, owing to both structural and cyclical factors.

Graph C1
Participation Rate
Quarterly

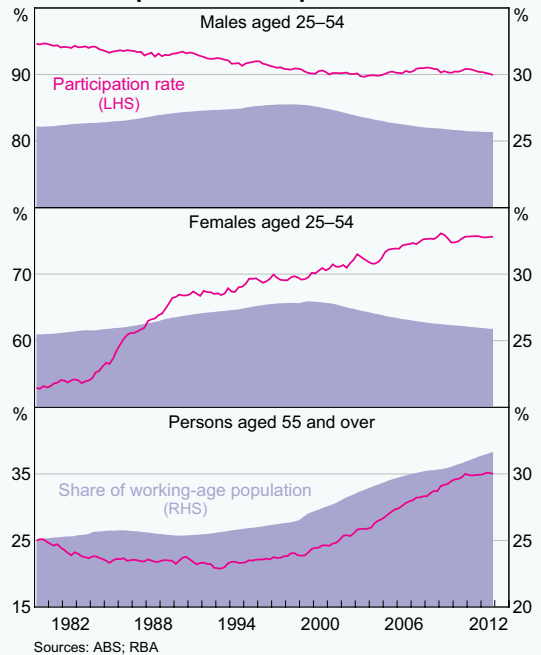


Source: ABS

The upward trend in the participation rate over the past three decades has primarily reflected increased participation by women and older people in the workforce (Graph C2).¹ Since 1980, the participation rate of females aged 25–54 has increased by over 20 percentage points, reflecting changing social norms, increased educational attainment, improved access to child care and more flexible work arrangements. Over the same period, the participation rate of people aged 55 and over has increased by 10 percentage points, in line with incentives to work longer, improved

¹ See Connolly E, K Davis and G Spence (2011), 'Trends in Labour Supply', *RBA Bulletin*, June, pp 1–8.

Graph C2
Participation and Population Shares



Sources: ABS; RBA

employment opportunities, and an increased share of employment in the services sector (where roles are typically less physically demanding), as well as better health and greater longevity.

Over this long period, the increased participation by women and older workers has more than offset the ageing of the population, which acts to reduce the participation rate. Although the participation rate of older workers has increased over time, it remains below that of prime working-age persons. Accordingly, the ageing of the population has, by itself, subtracted from the participation rate over the past decade, as a rising share of the relatively large baby boomer generation has moved into retirement.

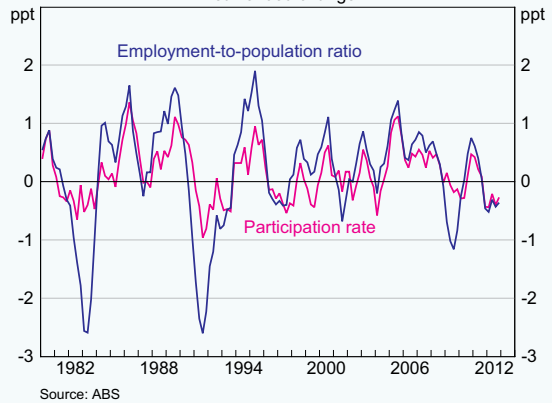
In contrast to these longer-term trends, over the past two years the participation rate has declined by around $\frac{3}{4}$ percentage point. The long-run forces mentioned above could well have continued to have had a net positive effect on the participation rate were it not for the reduced incentives to participate arising from softer labour market conditions. In periods of soft demand for labour, individuals that are willing and available to work may be less likely to actively search for a job, as they are less likely to be successful or the jobs they can get may be less rewarding. In this case, the participation rate will be lower than otherwise because such individuals do not satisfy the standard definition of unemployment.

Around one-third of the total fall in aggregate participation can be attributed to males aged 25–54, whose participation rate has declined by 1 percentage point since the end of 2010, to be at its lowest level since 2004. At the same time, the trend rise in the participation rates of women and people aged over 55 appears to have reached a plateau – at least temporarily. In addition, a $1\frac{1}{4}$ percentage point fall in the participation rate of younger workers aged 15–24 has accounted for around 30 per cent of the decline in aggregate participation during this period.

Although some cyclical in the participation rate is the norm, the participation rate typically varies by less than the ratio of employment to the (working-age) population (Graph C3). This means that a significant part of the cycle in the labour market is usually reflected in the unemployment rate rather than the participation rate. However, over the past two years the participation rate has declined by more than might have been expected, with the change similar to the decline in the employment-to-population ratio.

There are a number of possible reasons why participation may have fallen as much as it has, alongside the softer labour market conditions over the past two years:

Graph C3
Employment and Participation Rates
Year-ended change



- Some individuals may have been discouraged from searching for a job because of the divergence in conditions across industries, with the skills of those leaving jobs potentially not well matched to the expanding industries. Some of these individuals may be engaged in retraining outside of the workforce to obtain the necessary skills.
- The largest declines in employment over the past year have been in the area of public administration and safety. Reportedly, some of the workers losing public sector jobs received significant redundancy packages, which may have reduced their incentive to look for a job immediately.
- In the construction sector, there has been a sharp decline in self-employed workers, equivalent to over half of the peak-to-trough fall in employment in the industry. It is possible that some of these workers may not be recorded as actively seeking work, and hence they may not be counted in the labour force. To the extent that this is the case, it may help to explain the relatively large decline in the participation rate of male workers over the past couple of years.

- There have also been substantial declines in employment in industries exposed to discretionary spending, such as accommodation & food services and retail trade. These industries have typically employed younger workers, who may have decided to pursue further education rather than search for employment. Improved access to higher education in recent years may have also played a role, with government caps on university enrolments having been relaxed since 2010.

The recent experience stands in marked contrast to that of 2008–2009, during which a large fall in the employment-to-population ratio coincided with a relatively modest decline in the participation rate.² One key difference between the two episodes is that the decline in employment during the global financial crisis coincided with large falls in asset values, which prompted a pick-up in the participation rate of older workers, probably due to some of these workers deferring retirement. However, since the beginning of 2011 the trend increase in the participation of older workers has slowed, possibly reflecting the retirement of some of those individuals who chose to defer retirement or re-enter the labour force in 2008–2009. ✎

² See Plumb M, M Baker and G Spence (2010), 'The Labour Market during the 2008–2009 Downturn', *RBA Bulletin*, March, pp 1–6.