
Is Unemployment or Unemployment Insurance the Problem in Atlantic Canada?

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In this wide-ranging critique of unemployment insurance (UI), Doug May asserts (co-author Alton Hollett, a government employee, absents himself from the policy discussion in Chapters 5 and 6) that “the major behavioral impact of Canada’s current UI system is on choices of occupation and education” (p. 105), but he provides no evidence to support this assertion other than a few anecdotes from rural Newfoundland. Is it true? Is there any statistical evidence that young Atlantic Canadians are now choosing to discontinue their education because of the incentives of unemployment insurance?

Table 1 presents data on the grade 12 retention rate in Atlantic Canada — the total number of students enrolled in grade 12 expressed as a fraction of the total number of students enrolled in grade 7 five years earlier. The big news of Table 1 is the dramatic change to higher school retention rates in Atlantic Canada in the 1980s. By 1992–93, the grade 12 retention rate in all four Atlantic provinces was over 90 percent.¹ Although the

¹ Table 1 does not include those who return to school as adults and get their GED certificate of grade 12 equivalency. Over the 1989–91 period, GED graduates numbered about 15 percent of average grade 12 enrollment in Nova Scotia. Since the rate of adult achievement of grade 12 equivalency reflects in part the rates of school dropout in previous years, one cannot simply add together the GED graduation rate and the grade 12 retention rate — but it is clear that the *eventual* rate of completion of high school equivalency is now rather high.

**Table 1: High School Retention Rates,
Atlantic Canada, 1965-92**

	Nova Scotia	New Brunswick	Prince Edward Island	Newfoundland ^a	
				Grade 11	Grade 12
			(percent)		
1992	94	91	106	96	90
1991	87	95	96	94	88
1990	82	92	94	88	79
1989	81	87	95	81	77
1988	79	83	89	79	74
1987	78	85	89	81	72
1986	73	81	86	77	71
1985	70	82	81	77	68
1984	72	81	79	73	66
1983	69	80	82	69	64
1982	63	74	77	72	—
1981	58	73	73	71	—
1980	57	69	69	69	—
1975	53	62	60	64	—
1970	52	na	56	68	—
1965	33	na	46	50	—

Note: Retention rates are obtained by dividing the enrolment in grade 12 by the enrollment in grade 7 five years previous. Rates may be overestimated during downturns in the economy, when students may return to school.

^a Before 1983, high school graduation in Newfoundland was after grade 11, with grade 12 being a university preparatory year. Beginning in 1983, students were required to complete grade 12 to graduate.

Source: Provincial departments of education.

grade 12 retention rate in the 1990s may be somewhat inflated by students who have returned to school to improve their grade 12 marks because no jobs were available in a recessionary labor market, there is no mistaking the dramatic upward trend in school retention rates during the 1970s and 1980s. A major advantage of the "grade 12 retention rate" as a statistic is that it has been collected in exactly the same way for a large number of years. By 1990, the vast majority of Atlantic Canadian youth did

Table 2: *Percentage of Population 20 Years and Older Who Have Attended University*

Age Group	Newfound-land	Nova Scotia	New Brunswick	Prince Edward Island	National
	(percent)				
> 20	17.2	24.6	18.8	21.7	24.4
20-24	31.9	34.7	33.0	35.7	29.9
25-34	20.5	27.1	22.1	24.9	26.3
35-44	19.4	26.8	21.8	27.4	27.9
45-54	14.4	19.1	16.7	18.8	21.7
55-64	7.5	13.1	10.8	13.4	13.3
65+	4.9	10.1	8.0	9.7	9.8

Source: Statistics Canada cat. 93-328, 24-29.

stay in school through grade 12 — in stark contrast to the school attendance figures before UI was liberalized in 1971.² Table 2 uses the 1991 census to examine the percentage of the population 20 years and older who had attended university. In the 20-24 age cohort, a *higher* percentage of Atlantic Canadians had attended university than the national average. For Nova Scotia, the percentage who had attended university compares well with the national average in each age group and overall for the population as a whole. However, in Newfoundland, New Brunswick, and Prince Edward Island, the relatively low percentage of older age groups who had attended university depresses the overall provincial average to a level below the national norm.³

2 The high school graduation rate has the same trend, but at a somewhat lower level than the grade 12 retention rate reported in Table 1, partly because some students drop out of grade 12 after enrollment numbers are counted in the fall and partly because some students fail their exams. Part of the reason for preferring attendance numbers to graduation rates as an indicator of student decisionmaking is that, although students decide if they will attend school, the school decides if they will pass — and a high school diploma would lose much of its economic value as an indicator of skills if grading standards were lowered to the point that all students could pass.

3 The greater propensity to emigrate of the university trained also implies that older cohorts still resident in the Atlantic provinces will have a lower percentage of the university educated.

Tables 1 and 2 illustrate that, in analyzing educational achievement, it is absolutely essential to distinguish carefully between the *flow* of new school leavers who are now entering the labor force and the *stock* of old school leavers who have been present in the labor market for many years. Since there *used to be* a rather low grade 12 retention rate in Atlantic Canada, the labor force as a whole is dominated by the educational characteristics of those older workers who entered the labor force many years ago. Someone who dropped out of school at age 16 in 1965 would still only be 46 in 1995, with almost 20 years of labor force participation remaining before normal retirement age. In 1965, only a third of those Nova Scotians who had been in grade 7 in 1960 were enrolled in grade 12. In the 1960s, dropping out of school before grade 12 was the "normal" thing to do — and jobs were available (often in the resource sector) for such high school dropouts.

People who made those decisions in the 1960s now have to live with the consequences in the 1990s. Across Canada, older workers who acquired industry-specific skills through on-the-job training but who have poor educational credentials face significant problems in adjusting to structural change — problems which are particularly acute in rural labor markets with few alternative employment opportunities. Whether it is a mine closing in Northern Ontario or a fish plant closing in rural Newfoundland, the people affected have much the same problem — practical skills which are now irrelevant to the labor market, poor educational credentials, limited local job alternatives, and the substantial "sunk capital" of past investments in housing equity and local community ties. However, although older workers dominate the statistics on the overall populations of UI recipients and nonrecipients that May and Hollett present, it is clear that the children of these workers are making very different decisions on educational attainment and occupational choice.

Those decisions undoubtedly are motivated in large part by the economic returns to education. Bar-Or et al. (1993) use successive waves of Statistics Canada's Survey of Consumer

Finance to examine the return to education over the 1971–90 period for Canada as a whole, and conclude that the wage premium for postsecondary education was fairly constant from 1977 to 1990. I come to the same conclusion (Osberg 1994) using census data for 1980, Statistics Canada's Labour Market Activity Survey data for 1990, and multiple regression techniques to compare the return to education in Atlantic Canada with the return to education elsewhere, controlling for age, industry of employment, other personal characteristics, and so on.⁴ The return to education in higher annual earnings in Atlantic Canada is in fact slightly greater than in the rest of Canada. In determining the relative probability of unemployment, postsecondary education plays a slightly stronger role in Atlantic Canada than elsewhere. In Atlantic Canada, all levels of postsecondary education reduce the probability of experiencing unemployment (holding other variables constant); elsewhere in Canada, those with only some postsecondary education were not shielded from unemployment in 1990 any better than high school graduates. The bottom line is that, in Atlantic Canada, it is abundantly clear that education pays, both in higher annual earnings and in a higher probability of avoiding unemployment.

Although Table 1 indicates that most young Atlantic Canadians are now staying in school, some do drop out. What factors influence the probability that young people will not complete high

⁴ Earnings usually increase with greater work experience, while greater seniority may protect older workers somewhat from unemployment. Earnings and unemployment probability also differ across industry, for firms of different size and for unionized and nonunionized workers. Since average educational achievement is also lower among older workers, in some industries, and so on, it is important to control for all these factors when measuring the return to education. Multiple regression techniques estimate the influence of each variable, holding constant the influence of all other variables. Because there is some tendency for workers with low educational levels to be hired in high unemployment industries (for example, construction), part of the lower unemployment rate of university graduates can, for example, be explained as an industry effect — but even after controlling for these effects, a significant return to higher education remains, in Atlantic Canada as elsewhere.

school? Audas (1994) uses the Labour Market Activity Survey to examine the determinants of school withdrawal among the 2,500 youth whose labor market behavior and school attendance was followed by the survey over the 1988–90 period. Youth in families where one or both of the parents were low-wage workers (that is, who earned less than \$5.25 per hour in 1988) or where one or both of the parents had experienced unemployment in the past year were more likely than others to drop out of school, but these effects were somewhat *offset* if someone in the household had received UI benefits. The positive impact of family UI benefits on school attendance can be explained as an “income effect” — by partially maintaining family income in poor families, UI benefits reduce the need for youth to quit school and try to get a job to augment family income. Audas investigates a number of alternative econometric specifications, and his results on the influence of parental wages, unemployment, and UI receipt are robust — as is his finding that there is no statistically significant difference between the Atlantic provinces and the rest of Canada in the determinants of high school dropout.⁵

In Nova Scotia, as in Newfoundland, some rural areas are characterized by low average educational attainment levels (for example, in the 1986 census, 69.9 percent of the adult population of Guysborough County, Nova Scotia, reported that they had less than high school graduation). However, the low schooling attainment of the population of these areas largely reflects the economic opportunities of past decades. At a time when forestry, mining, and fish plant jobs were available, it was possible to drop out of school and get a job that paid about the same as the jobs one’s parents had. Educational achievement was low because the fi-

⁵ The *level* of school withdrawal is somewhat higher in Atlantic Canada (although interprovincial differences are now fairly small) because more Atlantic Canadian youth have attributes (such as low family income or unemployed parents) that are correlated with school withdrawal — but the influence of those attributes is no different in Atlantic Canada than elsewhere. In other words, Atlantic Canadians respond to particular economic influences in exactly the same way as other Canadians — the differences in behavior that exist arise from the different sets of influences that people face.

nancial benefits to continued education were not obvious and the cost of continuing in school was a forgone paycheque. However, those days are long gone. During the 1980s, new resource sector jobs in fishing, forestry, and mining largely disappeared as these sectors shrank in size. As a consequence, rural school boards in Nova Scotia have realized very large increases in high school retention rates — in 1991–92, Guysborough County had a high school retention rate *above* the provincial average.⁶

The connection between unemployment insurance and choice of occupation/education is the essential part of May and Hollett's analysis, because they notably do *not* claim that Atlantic Canadians are turning down available jobs because of the work disincentives of unemployment insurance. On page 58, they cite O'Grady (forthcoming) as finding the "very high job commitment" of rural Newfoundland youth, while on page 57 they suggest that seasonal resource and construction workers in Atlantic Canada are willing to "put in additional hours if the jobs were available."⁷

6 Interviews with high school teachers in Guysborough County have convinced me that the high school withdrawal rate there — now about one-third of the provincial average (see Nova Scotia Department of Education 1993, 12) — is not because of any sudden surge in the love of learning, but because there are no jobs available locally and it is widely known that the chance of getting a job elsewhere depends on high school graduation. In an isolated rural area, there is also not much to do during the day other than school or a job, and one can go to school free until the age of 21. Even if school attendance is up for the unedifying reason of a lack of alternatives, the result still is an increase in the human capital of rural youth.

7 This suggestion is totally consistent with the literature on labor supply elasticities cited by Phipps (1993), since her point is that *desired* hours of work change only slightly as hourly wages increase, but many Canadians cannot now obtain all their desired annual hours of labor supply. In fact, the difference in average annual hours of work between the Atlantic provinces and other provinces arises entirely because a higher fraction of Atlantic Canadians are constrained by job availability in their labor supply decisions. Osberg and Phipps (1993) demonstrate econometrically that the differences between labor supply determinants in Atlantic Canada and the rest of the country are statistically insignificant if one controls correctly for the possible presence of labor demand constraints. Again, Atlantic Canadians respond to economic influences in the same way as Canadians elsewhere — but they face a different economic environment, in which jobs are simply not as easily available as they are elsewhere.

Beneath all the rhetoric on "UI dependency" and "addiction," therefore, the underlying economic analysis of May and Hollett is that there are not enough jobs in Atlantic Canada. As May states clearly on page 104, "there really is a shortage of available work in Atlantic Canada." What he complains about is the political pressures to create meaningless make-work projects and the social pressures to share jobs, and he recognizes that such pressures exist because there is not enough work available for the existing labor force. Make-work and job sharing give many people enough weeks of employment to be entitled to UI, but it is the lack of enough weeks of work that creates the unemployment, which means that people claim their UI entitlement. May and Hollett state quite clearly on page 59 that UI repeaters would take full-time, full-year jobs if they were available in rural Newfoundland.

In the current debate on social policy reform, commentators who use the "dependency" rhetoric usually argue for increasing work incentives as a "solution" to the social policy problem. In fact, among all the various proposals for social security reform now under consideration, this volume is somewhat unique in *not* emphasizing "work incentives." Indeed, May argues *against* an emphasis on work incentives because of the

fear that the primary effect of having "work incentives" in the program would be another series of makework projects or costly megaprojects. In rural areas in particular, work supplement schemes would simply mean more federal and provincial government action to provide jobs. (104.)

At bottom, therefore, the basic problem that May and Hollett perceive in Atlantic Canada is that there are too many people living in rural Atlantic Canada for the number of real (private sector) jobs available. They ascribe part of this excess population to insufficient emigration during the 1970s and early 1980s due to the income supplementation available through unemployment insurance usage — and they also mention government promises to increase employment in the fishery following the extension of fisheries control to the 200-mile territorial limit. For some reason,

however, May and Hollett shy away from recognizing explicitly that, if overpopulation is the problem, a long-run solution must necessarily involve rural depopulation and the closure of many existing rural communities — in particular, those whose economic *raison d'être* is a fish stock that no longer exists.

If this is what May and Hollett mean, they should say so explicitly. However, although almost all their discussion focuses on the problems of small rural fishing communities (particularly in Newfoundland), Atlantic Canada is much more than that. The Halifax-Dartmouth metropolitan area, for example, has approximately half the labor force of Nova Scotia and has, for many years, had unemployment rates, labor force participation rates, and average earning levels that place it consistently in the middle rank of other comparably sized Canadian urban areas. Since the mid-1970s, Halifax-Dartmouth has had an unemployment rate less than that of Montreal, while throughout the 1980s it also boasted better unemployment performance than metropolitan Vancouver. In the 1990s, Halifax-Dartmouth has had a lower unemployment rate than Toronto.

From the prevalence of anecdotes from the fishing industry and the fact that an entire chapter is devoted to its analysis, the unwary reader might think that fishing is what most Atlantic Canadians do for a living, yet fish-harvesting families account for only a small percentage of Atlantic Canadian families. May and Hollett make frequent reference to UI and “job sharing” — but although their anecdotal discussion emphasizes that job sharing only occurs in small communities with strong social pressures, they entirely ignore the fact that most Atlantic Canadians live in urban areas (see Table 5). One of the major problems in the analysis by May and Hollett is that it focuses so exclusively on the characteristics and problems of rural Newfoundland. Although the population of rural Newfoundland is less than 10 percent of the population of Atlantic Canada, May and Hollett continually generalize from the anecdotes of rural Newfoundland to the problems of the region as a whole.

The rural areas of Atlantic Canada *are* important, if only because they are the source of the differential in unemployment rates between Atlantic Canada and the rest of the country (since urban areas such as Halifax have unemployment roughly comparable to other urban areas). But it is essential to get beyond simple stereotypes of the region as a whole if one is to address the problems of the pockets of poverty and rural unemployment that dot the region.

However, even if the analysis is badly flawed, would the proposed policy prescription work? The original idea underlying negative income tax (NIT) schemes — like the proposed universal refundable tax credit (URTC) — was to improve work incentives by increasing the net hourly return to work (because the NIT has a lower taxback rate than social assistance now has). But May argues in Chapter 5 that, in the small, depressed rural communities that are the focus of the discussion, work incentives are beside the point. It is therefore entirely unclear how the proposed URTC will solve problems of “dependency.”⁸ In my view, it is in precisely these sorts of labor markets that one wants to think carefully about the long-run social implications of switching to a form of income supplementation that does *not* require work effort (such as the proposed URTC) from a system that now does have a work requirement.

For seasonal workers in rural areas, May and Hollett may well be right in thinking that unemployment insurance has become a form of income supplementation — but it is important to note that, as such, UI is much closer to “workfare” than to traditional social assistance. In requiring that individuals, even in very depressed local labor markets, somehow repeatedly come up with 12 weeks of paid employment, the UI system now forces individuals into repeated job search and repeated contact with employment (usually in the private sector). A purely passive income transfer system, like the URTC scheme proposed in

⁸ Leaving aside the fact that the volume offers no definition of “dependency.”

Chapter 5, does not require *any* job search or work effort. The danger created by the URTC is that transfer recipients will simply lose touch with the world of paid employment entirely. Is this desirable? In rural communities without enough jobs, switching to a universal refundable tax credit system would also eliminate any incentive to “job share” — but will the community be more viable when it is divided into those who are employed full time and those who are transfer dependent full time?

In the isolated rural labor markets that concern May and Hollett, the social implications of switching to a URTC are unattractive, but most Atlantic Canadians do not live in such communities. For them, and for the country as a whole, the main problem with the URTC is financial. As the authors are surely aware, negative income tax/guaranteed annual income schemes have been proposed many times before. Their key problem, from a budgetary perspective, is that, if the level of basic benefits is set at a survivable level and the tax rate on earned income is nonconfiscatory, these two parameters together imply that the “breakeven point” (the income at which transfers to families cease and taxation begins) is fairly high up in the income distribution — hence such schemes are often very expensive. The costing of such schemes is therefore crucial. Without such costing, one cannot reasonably comment on the realism of the proposal — but it is fairly easy to check that at a breakeven point of \$27,000 for a family of four, the percentage of Canadian families of this size that would receive transfer payments is substantially above the reciprocity rate under current UI and social assistance. The proposed program may therefore be expensive — even though the basic level of support that it offers to single adults (\$5,000) is below the level of support currently provided by social assistance in most Canadian provinces, which is itself very much below Statistics Canada’s low-income cut-off (see National Council of Welfare 1994).

May and Hollett are simply wrong in asserting that the educational choices of Atlantic Canadian youth have been biased

to an increasing level of high school dropout because of the incentives of unemployment insurance. It is absolutely clear that Atlantic Canadian youth in the 1980s and 1990s have been making very different educational choices from those of their parents. May and Hollett may be right in arguing that, in the 1970s, unemployment insurance was partly responsible for maintaining the overpopulation of rural Atlantic Canada and that we are now facing, in the 1990s, the social costs of the educational and occupational decisions of 20 years ago. But in one sense it now does not matter much whether it was UI or the excess optimism of the resource boom of the 1970s⁹ that led people to stay in rural areas of Atlantic Canada that cannot now support them. The problem for today is what to do with this excess rural population, which is "too old to move, but too young to retire." The problem is *not* how to motivate the young to continue in school or to emigrate — this is already happening.

The problem of unemployed or only occasionally employed older workers with few portable skills is the issue that needs to be addressed clearly. In the long run, it is the tough option of emigration (which May and Hollett do not want to consider) that is likely to equilibrate demand and supply in rural labor markets. Rural youth are now getting their educational credentials and *are*, in many cases, leaving (see Osberg, Gordon, and Lin 1994). As the young people leave, many of the rural areas of Atlantic Canada are increasingly dominated by retirees and older workers.

For older workers who have poor educational credentials and who can now only obtain intermittent employment, realistic options elsewhere are not attractive. As long as high unemployment persists in the rest of Canada, emigration for poorly educated older workers usually will mean their giving up the house, friends, and life they know for a position at the back of the urban

⁹ During the late 1970s, rising energy prices created plans for the expansion of Cape Breton coal mining and for Labrador hydro megaprojects. The federal government was then forecasting (see Canada 1981) *shortages* of rural labor in the occupations needed to build and run such energy megaprojects.

queue for insecure low-wage work and apartment living. Even if they have been retrained, older workers would be migrating to labor markets in which freshly minted graduates of colleges and universities already face significant problems in obtaining decent employment. If Canadian macroeconomic policy were to shift toward an emphasis on growth and full employment, jobs might be available for retrained older workers — but there is no sign that such a shift in macroeconomic policy is about to happen. Without vacancies elsewhere, many older workers will need some form of income supplementation program for some years to come. However, their basic problem is unemployment. UI receipt is the symptom, not the cause.

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