Economic costs of unemployment

- Loss of earnings for the unemployed, leading to lower living standards.
- More difficulty getting work in the future, as the unemployed lose 'on-the-job skills' and may become less attractive to future employers.
- Stress and health problems of being unemployed.
- Increased government borrowing. The government spends more on unemployment and related benefits, and receives less income tax.
- Lower GDP for the economy and possible negative multiplier effect.
- Increased social division between the unemployed and employed.

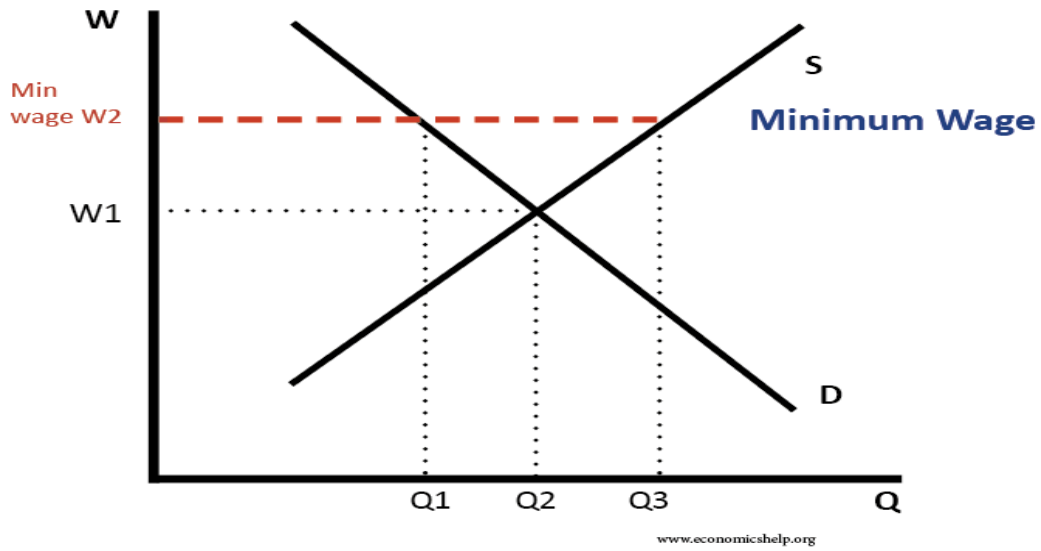
Causes of unemployment

1. Frictional unemployment. This is unemployment caused by people moving between jobs, e.g. graduates or people changing jobs. There will always be some frictional unemployment, as it takes time to find a job.

2. Structural unemployment. This is unemployment due to a mismatch of skills in the labour market. It can be caused by:

- **Occupational immobility**. This refers to the difficulties in learning new skills applicable to a new industry. For example, a former manual labourer may find it hard to retrain in a new, high-tech industry.
- **Geographical immobility**. This refers to the difficulty in moving regions to get a job, e.g. someone unemployed in South Wales may find it difficult to move to London, where housing is expensive. We often see higher unemployment in depressed regions.

3. Classical or real-wage unemployment. This occurs when wages in a competitive labour market are pushed above the equilibrium. This could be caused by minimum wages or trade unions.



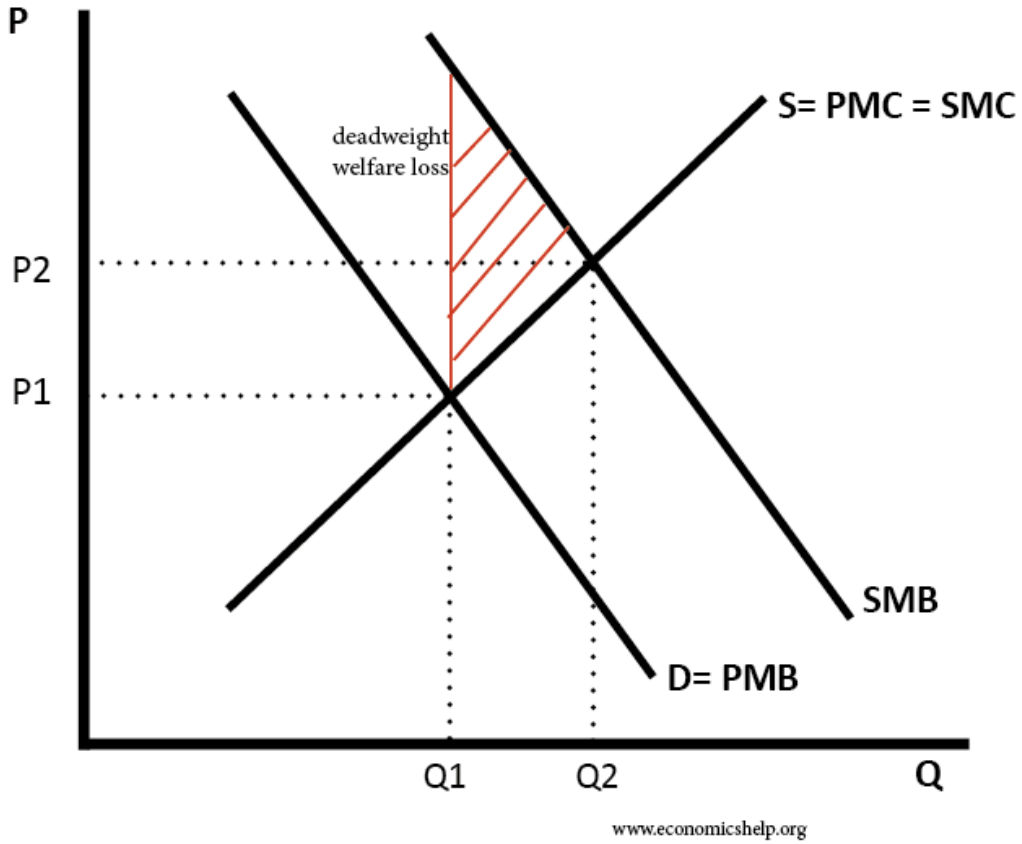
In a competitive labour market, a minimum wage above the equilibrium will cause real-wage unemployment of Q3-Q1.

Positive externality

A positive externality in consumption occurs when there is a benefit to a third party from your consumption.

- For example, if you cycle to work (rather than drive), other people benefit from reduced congestion and pollution.

Diagram of positive externality in consumption



In a free market, the equilibrium will be at Q1, P1, where supply (S) = demand (D).

- However, this is socially inefficient.
- At Q1, the SMB is greater than the SMC, leading to an area of deadweight welfare loss.
- With a positive externality, there is **under-consumption**.
- Social efficiency occurs at Q2, where SMB=SMC.

Positive externality in production

- When producing a good causes a benefit to a third party.
- For example, if you keep bees, then a nearby apple farmer benefits because your bees help to pollinate his apple trees.