

## TRANSCRIPT

### The Work Goes On

**Guest:** Richard Layard

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#### **Richard Layard:**

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#### **Orley Ashenfelter**

Welcome to [The Work Goes On](#), a podcast from the [Industrial Relations Section at Princeton University](#). I'm your host, [Orley Ashenfelter](#), the Joseph Douglas Green 1895 Professor of Economics at Princeton University. In this podcast series of conversations with leading thinkers and practitioners, we are creating an oral history of an entire generation of industrial relations experts and labor economists whose contributions to their fields have been absolutely extraordinary. Our guest today is [Richard Layard](#), formally known as the Right Honorable Lord Layard, who is the founding director of the [Centre for Economic Performance](#) at the [London School of Economics](#). He is renowned for his work in labor economics and especially for his work on the economics of higher education, unemployment, and mental health and life satisfaction. He has been a member of the House of Lords since 2000. Richard, welcome to [The Work Goes On](#).

#### **Richard Layard:**

Hi, delighted to be with you.

#### **Orley Ashenfelter**

I'm so glad we could have you come. Let's begin the discussion by talking about your background. Where did you grow up?

#### **Richard Layard:**

I grew up in Oxford because we were moving out of London to avoid the Blitz and it was a fortunate move, I suppose, because I went to a prep school in Oxford, which was preparing people for this scholarship for Eaton College. I won a scholarship there. I studied an awful lot of classics, but also fortunately history. I went on to study history at Cambridge and I went on from that to teach history in a state comprehensive school, but I was going to the LSE in the evening just to broaden my education. And the result of that was that I was invited to be the research officer for a major government committee on the future of higher education, chaired by Lord Robbins.

And I had a great experience there with one of your former colleagues, Bill Bowen. He was young in those days and he'd been on leave at LSE and he came and gave us a talk on how you should think about public investment in terms of cost benefit analysis. And I thought this was absolutely amazing. Partly for that reason, when I was invited to go to the LSE as a researcher, I said yes. But of course I then had to

turn myself into some kind of an economist by taking courses and acquiring my masters. I never got a PhD. I was told that wasn't necessary.

**Orley Ashenfelter**

I guess that's the old days that's for sure.

**Richard Layard:**

It is.

**Orley Ashenfelter**

You're very well known for many things. And of course, the [Robbins Commission](#) had a big influence on higher education in the UK. Can you describe that influence with a few words?

**Richard Layard:**

I can in a way because what was interesting was the second day I got that, onto my desk came a memo from the treasury, the government Treasury Department saying that we now had four percent of the population going to university and did we really need more than two percent? And indeed, shouldn't the money be better spent on renovating the decaying cities of the north of England? That was what we were up against. There was also the so-called pool of ability argument. There was a limited number of people who could benefit even if the jobs were there. I think I did contribute a bit in demolishing the pool of ability argument, which as we've seen in the decades that followed was completely illegitimate. The [Robbins] committee recommended a quite sharp expansion and that's what happened in the years that followed.

**Orley Ashenfelter**

It did. I know people have different ways to describe the so-called provincial colleges and universities, but many of them turned out to be very good. I visited one myself, University of Bristol and had a very good visit there. I would like to turn to the second area that you've done so much work in the past with Richard Jackman and Steve Nickell and that's inflation and unemployment. We seem to have a period again after a very, very long quiet period where there was very little inflation. We seem to have a new period where there's both inflation and relatively low unemployment. Do you think that work that you did then is relevant today?

**Richard Layard:**

I think it is the right model. When we were setting up the center that you mentioned, unemployment was going up quite rapidly, especially in European countries and all kinds of implausible explanations were being offered which when you check them out, there was something wrong in that explanation. We thought, "Let's find a simple model where we can put in all the factors that would be affecting the relation between unemployment and inflationary pressure." And basically, we just had a two-equation model, one for prices, the markup on wages and the other wages and markup on prices and unemployment ended into the wage equation. And therefore, what was in the wage equation was very important [in] determining the level of unemployment which would reconcile the markup of prices over wages and wages over prices. And that was what we did. We put into the wage equation really all the relevant factors.

We particularly put in the system of bargaining, which at that time was particularly relevant in Europe, union coverage, union centralization of bargaining. Then we have of course the product market competitiveness, which helps to reduce wage pressure. And then we had all the shocks like we're getting now in terms of trade shocks, either short run things, but terms of trade shocks, tax wedge shocks, shocks to productivity growth. And then, this was perhaps the biggest thing we did, was the importance of how unemployed people are treated in affecting wage pressure. You've got the replacement ratio, you've got the period for which benefits continue to be paid, you've got the conditions attaching to the payment of benefit. Then you've got what you might call active labor market policies, things that the government is doing to help unemployed people to get work and all of these things when they were put into the wage equation provided quite a good explanation of both the level of unemployment in different countries and the movement of unemployment over time in its relation to inflationary pressure.

But there was one other thing which we were particularly pleased about because you could think of these variables affecting how unemployed people are treated as determining how effective unemployed people are as fillers of vacant jobs. But of course you can get a direct measure of that if you use a third equation, which is a hiring equation where you are thinking of hiring depending on unemployment and vacancies. And if you see that equation moving around that shows there's some change in the effectiveness of the unemployment, unemployed people at filling these vacancies. And you've got these extraordinary pictures that we used a lot that I remember showing them to Bob Solow. He was really interested and encouraging about it. You could see that this relationship simply moving out in almost all European countries from the 70s and into the 80s. And we basically said, "The problem for governments is how to bring that curve back," which means dealing with some of these things to do with how unemployed people are treated.

And in particular, we found that that effectiveness measure was hugely affected by how long people had been unemployed. If a lot of people had been unemployed for a long time, the unemployed had become rather ineffective at filling vacancies. And you could also find this from the micro data. Having written our book, we started advocating policy change and we certainly had some impact in Britain. We had the so-called "New Deal" from Tony Blair, which was an active labor market policy to try and get all young people at least into work in less than a year. We were always hoping that would be extended properly to adult people, but it only was to a degree. Then we saw the same, similar changes in Norway, Denmark. But in Germany in particular, we were really excited by the [Hartz reforms](#) which greatly increased the conditionality of benefit. And probably are the main explanation of why German unemployment had been so much lower in the last 20 years than in the 20 years before that.

And I have been told, I can't check this, that our work was really influential behind that policy. Thinking of the relevance of this today, you've got these terrific terms of trade shocks affecting European countries at the moment. And I think we are going to see, we haven't yet got unemployment high while inflation is still high, but we are probably going to have a lot more unemployment. And it's a very interesting question as to how much that unemployment will bring down the inflation. And I think this is a big unknown.

### **Orley Ashenfelter**

Very interesting. I know you, actually, I remember, I think remember correctly that you and Steve Nickell, maybe Richard Jackman too, organized a march across England for the unemployed.

### **Richard Layard:**

We did. In support of these active labor market, support for unemployed people. You're right. It was the [Hands Across Britain](#), although actually it only went from London to Liverpool. I remember Larry Summers and his whole family turned up at the London end, to be in London. That was a great moment. And I think this did have an effect. This was in 1987. That did have an effect even on the conservative government. They started paying more attention to how they were both using conditions on unemployed but also providing support for the unemployed.

**Orley Ashenfelter**

I have a couple more questions, but I do want to turn to the work that you've done on life satisfaction and mental health, which I think has been one of the major preoccupation of yours in the last 20 years, including [the book](#) of course, that on satisfaction and I gather.

**Richard Layard:**

You don't seem to the word happiness.

**Orley Ashenfelter**

Happiness, that's fine too. Happiness, satisfaction. You all sound good to me.

**Richard Layard:**

I was actually rather pleased when you used the word satisfaction because many people have told me that they can take this work seriously if you call it wellbeing, and they can't take it seriously if you called it happiness. There you go.

**Orley Ashenfelter**

Satisfaction is an intermediate good, I guess.

**Richard Layard:**

Exactly.

**Orley Ashenfelter**

But I know that you have been very active in policy aspects associated with these issues, especially in the mental health area. And I don't think that's very well known to very many of the labor economists out there, probably more known to those who are in the medical community. Can you tell us about that?

**Richard Layard:**

I suppose the first point is that if you are thinking about satisfaction as the measure of the success of a society, which is the measure we use, for example, in the World Happiness Report, based on the Gallup World Poll, you need to have a clear picture of what are the main factors affecting it. And of course, income is an important factor. And we were able to tie down actually the functional form of that quite well, so that you see the satisfaction is a linear function of log income, which is what you might expect from ordinary psychophysics if you like. But the main point of this whole science is that whether people are satisfied with their lives depends on so much else besides income. It depends on obviously physical health, but even more in terms of the explained variance of satisfaction within the country.

The biggest single factor is simply whether you've ever been diagnosed with anxiety disorder or depression. That's a single most powerful explanatory variable. Physical health is also powerful. Then comes work, particularly the quality of work, which varies enormously and is really important to people, and only then comes income. I felt, having written the book you mentioned, that I should try and do what I could about the most important thing causing misery, which was mental illness. In particular, because of course, mental illness is a huge factor in the labor market in causing people to be out of the labor force in the first place, or if they have a job to be absent or if they are even present not to have their minds on the job. It was quite easy to make the case, even to somebody who didn't think that wellbeing was that important.

This is a really good way of saving public money. And it now turns out there's another very interesting thing that's become more and more clear, that treating people with mental health problems, who have comorbid physical health problems, which is about a third of them, saves a huge amount of money on the treatment of the physical problem. We basically showed to Tony Blair that if you were to have a program to treat anxiety disorders and depression by psychological therapy, it would pay for itself in terms of the savings on benefits and lost taxes and then pay for itself to a large extent a second time in terms of saving on physical healthcare costs, which is also of course important in an administrative sense because it's the same people who are paying for psychological therapy and for physical healthcare.

We set up this program and we is really David Clark, who is a wonderful clinical psychologist, one of the world's leading ones, set up this program which involved training about 1,500 new people each year in [inaudible] psychological therapy, placing them in newly created services where they can be properly supervised and then continue to be employed, and also to measure the outcomes by having a person complete a questionnaire before every session.

We actually know for everybody, this has never been done in psychology before for everybody, even if they drop out, where they've got to before they dropped out. And we have an improvement rate of 75 percent, what we call a recovery rate; that's crossing a frontier of over 50 percent. And we actually maintained it during the lockdowns online, which was really surprising. We maintained the volume and the success. That's been a very satisfying outcome of all this work.

But I want to get satisfaction or wellbeing, whatever word you like, to be the criterion for all public policy, not just in that area. And it bothered me when I hear the phrase health and wellbeing as if wellbeing isn't an overarching good. That is the justification for everything from income, environment, law and order everything else, as Jeremy Bentham said. I'm pursuing the Jeremy Bentham agenda. First thing was to get all governments, which we have got most OECD governments now to measure the wellbeing of their people, but then of course to address their policies to improving it. And that requires a really massive information base. We made a first shot at this in a book, which we called, I hope you like the title, *The Origins of Happiness*, guess where that came from?

And the aim is to provide policymakers with thousands or even tens of thousands of coefficients that they can use to evaluate the cost effectiveness of policies in terms of wellbeing changes achieved per dollar. And we are moving forward on that. There's a lot more interest. The OECD and EU have said that their members should be making people and their wellbeing the centerpiece of policy design, which is a step forward. The British Treasury have authorized the use of direct measures of wellbeing in the analysis of policy. And what we are looking for now is politicians who are ready to go for this. And you can imagine which party is more likely to do this in Britain than which other one. But, if I may say so, we're also realizing that unless the public is carried along with this idea, this is not going to happen.

Two other things that I've been involved in are grassroots movement of people who are trying to create a happier world called Action Happiness and a top-down movement, which we are just launching this

year called the World Wellbeing Movement, which is targeting, directly targeting policymakers and business leaders. But what I'd most like of all, of course, would be for economists to take these direct measures of wellbeing seriously. I had a lovely debate actually at the AA meetings in, I think it was 2018, with Joe Stiglitz and Alan Krueger and Bill Nordhaus. And I do think that we do use answers to questions. We measure unemployment by answers to questions. We shouldn't shy away from measuring utility by answers to questions.

### **Orley Ashenfelter**

We're coming to the end here, and obviously, you're very, very involved in that discussion, and it's very interesting to hear what your involvement has been. I am curious about one more housekeeping issue. You've been a member of the House of Lords for a while. There are quite a few economists in the House of Lords. I don't know how many. I know several. I'm curious, do you act together when it's time to think about economic issues? I realize that some are Tory Lords, and some are Labor Lords and some are cross-benchers, but is there a sense in which the economists get together in the House of Lords?

### **Richard Layard:**

There's an Economic Affairs Committee, which is I think the most prestigious of all the committees. And at the moment it's got four LSE economists on it, or former LSE economists on it, and one other non-LSE economists out of 12 members. That works quite well. You'll also be pleased, Orley, that our current terms of reference are to investigate the shrinkage in labor force participation in Britain, which is apparently rather unique compared with every other country coming out of COVID. Labor economics is still the fore.

### **Orley Ashenfelter**

It is. I think you're absolutely right. It's probably back more than it ever has been for all those reasons. Richard, that's been a pleasure to talk to you. Our guest today has been Lord [Richard Layard](#), the [Centre for Economic Performance](#) at the [London School of Economics](#). Please join us again for the next episode of [The Work Goes On](#), an Oral History of Industrial Relations and Labor Economics from the [Industrial Relations Section at Princeton University](#), when we will speak with [Claudia Goldin](#), the Henry Lee Professor of Economics at Harvard University. I'm your host [Orley Ashenfelter](#). Thanks for listening.

### **Announcer:**

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