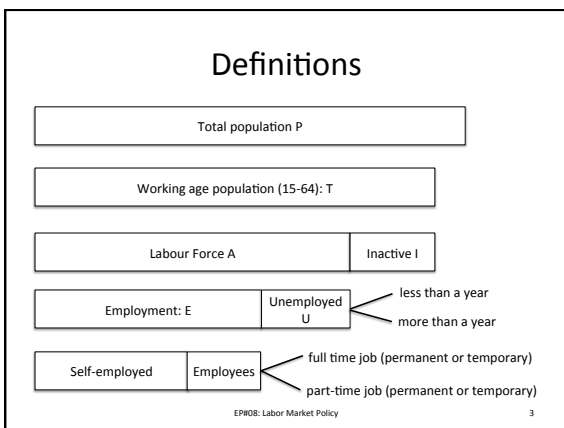


Economic Policy #08

Labour Market Policy

- ### Labour Market Policy
- Labor market: definitions and indicators
 - Efficiency of labor market
 - Policies
 - active labor market policies
 - regulations of labor market
 - labor taxation
 - social policy incentives
- EPR08: Labor Market Policy 2



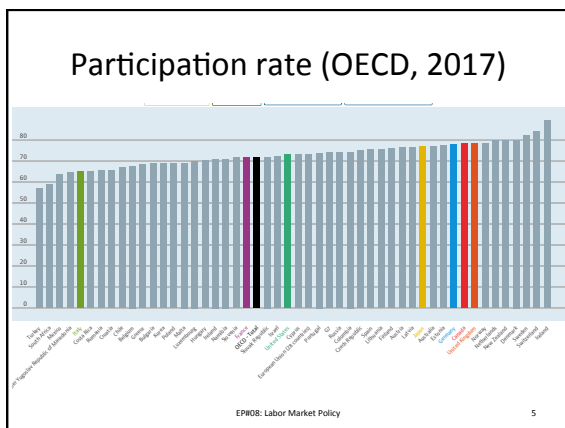
Basic indicators

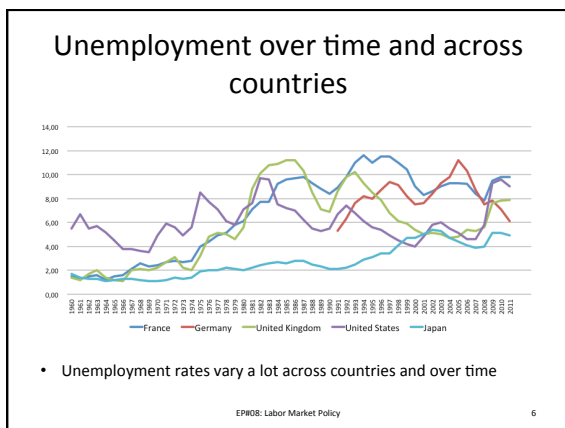
- **Participation rate:** A/T
- **Employment rate:** E/T
- **Unemployment rate:** U/A

EU-27 (2016)

- P = 510,3 mil.
- T = 333,2 mil. (15<age<64)
- A = 240,8 mil. $A/T = 72,2\%$
- E = 219,9 mil. $E/T = 66,0\%$
- U = 20,9 mil. $U/A = 8,7\%$

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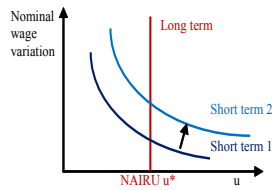
Efficiency of ALMP

- How to assess labor market efficiency?
 - NAIRU rate
 - Beveridge curve
- These policies may lead to opposite results through *displacement effect*, *deadweight effect* or *substitution effect*.

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The NAIRU

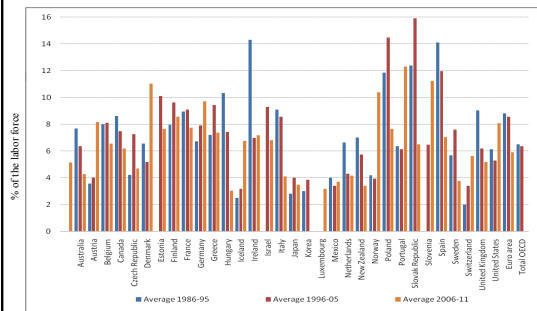


- Lower u^* => labor market policy, structural policy
- Move u closer to u^* => stabilization policy

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The NAIRU in OECD countries



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The Beveridge curve (BC)

The graph illustrates the Beveridge Curve (BC) in a labor market. The vertical axis represents Job vacancies (V) and the horizontal axis represents the Number of unemployed (U). Two downward-sloping curves, B_1 and B_2 , represent different states of the labor market. Points I, J, K, L, M, N are marked on the curves. A 45-degree line is shown, intersecting the curves at points A_1 and A_2 . The origin is labeled O .

- Cyclical fluctuations move up and down the unemployment-vacancy combination along given BC.
- Change in the efficiency of the labor market cause shift of the BC.

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The Beveridge curve in EU

The graph shows the Beveridge Curve in the EU from 2008Q1 to 2013Q4. The vertical axis is Job vacancy rate (%) and the horizontal axis is Unemployment rate (%). Two curves are shown: EU-28 (orange) and EA-19 (blue). A dashed line represents a 45-degree slope. The graph shows shifts in the BC over time, indicating structural changes in the labor market.

These shifts in the BC are suggestive of structural changes in the labor market.

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Labor market regulations

- Regulation of dismissal
- Minimal wages
- Taxation
- Social policy incentives

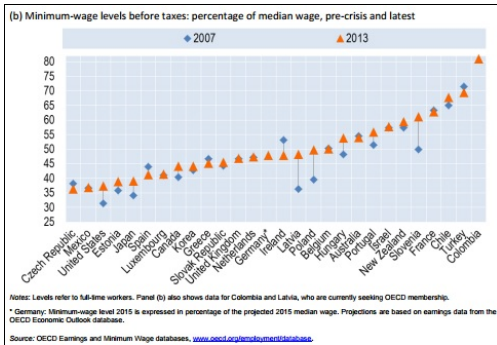
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Minimal wages

- Most countries in the world have some form of minimum wage, the scale, eligibility and operational details change from country to country.
- A large body of theoretical and empirical research examines the effects of the minimum wage
 - In theory: no clear-cut predictions (depends on competitiveness of labor markets)
 - Empirical results: also point in both direction – positive and negative effects of the minimum wage on employment

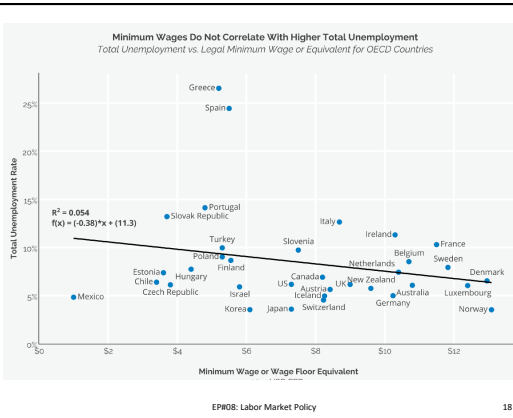
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CS. Studies based on natural experiments

- D. Card and A. Krueger: Minimum Wages and Employment: A Case Study of the Fast-Food Industry in New Jersey and Pennsylvania. American Economic Review 84(4), September 1994: 772-793
- Research question: How do employers in a low-wage labor market respond to an increase in the minimum wage?
- Approach: Compare employment of teenagers in New Jersey and eastern Pennsylvania before and after the increase in the minimum wage in NJ from \$4.25 to \$5.05 on April 1, 1992.

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CS. Studies based on natural experiments (cont.)

- Data: Phone survey of fast-food restaurants in NJ and eastern Pennsylvania
- Results of difference-in-differences approach:
Employment in Typical Fast-Food Restaurants

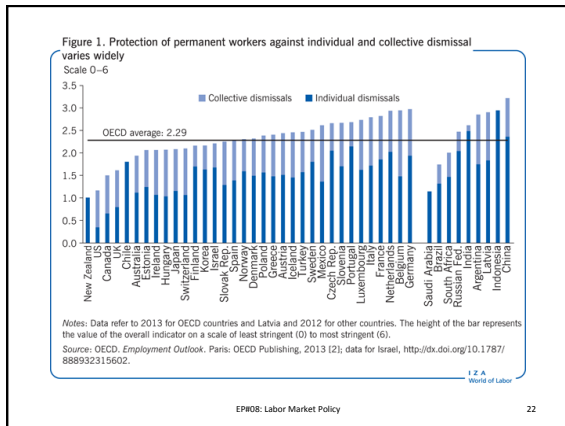
	NJ	E Penn
Before change	20.4	23.3
After change	21.0	21.2
Difference	0.6	-2.1
Difference-in-Differences = 0.6 - (-2.1) = 2.7		

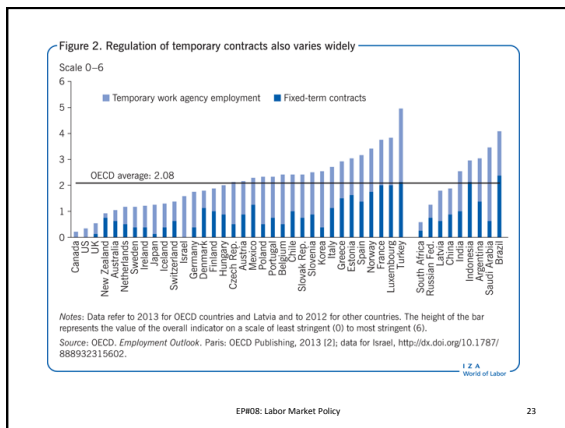
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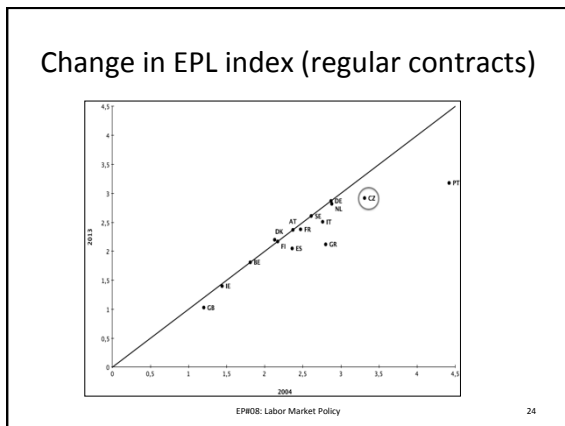
Regulation of dismissal

- Employment protection legislation (EPL): legal restrictions on dismissals and compensations to workers in case of early termination of employment contract
- The OECD uses following indicators:
 - Regulations under permanent contract
 - Strictness of collective dismissals
 - Regulations under temporary contracts

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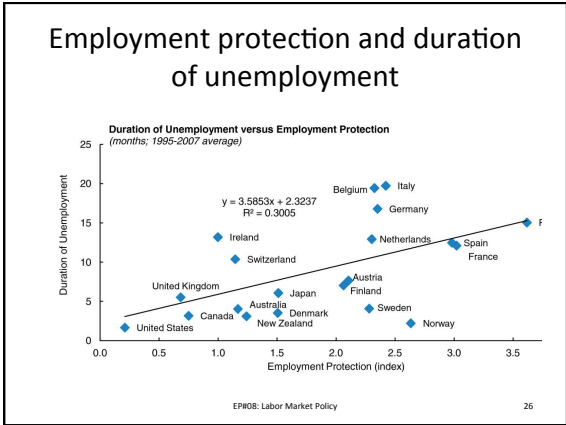




Employment protection legislation: consequences

- Severance regulations make it difficult for firms to reduce employment in the short run => firms are more reluctant to hire in good times
- Empirical results:
 - EPL negatively affects unemployment inflows and outflows
 - countries with stricter EPL display higher youth unemployment rates and lower unemployment among prime-aged groups

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Labor taxation

- Labor is subject not only to income taxes paid by households but also to a number of social security contributions by both employees and employers.
- Higher taxes raise the real cost of labor faced by firms, leading to lower employment in the sector that pays the tax.
- Net effect depends on the elasticity of labor demand and supply.
 - In Europe: wages are set in collective bargaining => flatter labor supply curve => stronger impact on employment

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C.S. Feasible supply-side policy: lessons from history

- **The case of Netherlands:**
- During the 70s the Netherlands was the mother of the Dutch disease, unemployment almost reached 12 % in 1983. A generous social system was proving unsustainable at those rates of unemployment.
- Wassenaar Accord in 1982: long-term agreement between social partners which moderated real wage growth, better treated part-time employment and lower labor taxation
- Employment agencies provided more carrot-and-stick incentives for the unemployed to return to work.

Source: Burda&Wyplosz (2012) EPW08: Labor Market Policy 31

C.S. Feasible supply-side policy: lessons from history

- **The case of Ireland**
- Anaemic growth rates, high budget deficits and unemployment reaching 18 % in the late 1980s.
- R. Dornbusch: *"Ireland is a sick man of Europe"*.
- In the late 1980s: programme of fiscal consolidation was adopted, social partners agreed on stipulating modest increase in money wages, government reduced labor taxation
- In the early 90s: ALMPs were implemented, products market deregulated.

Source: Burda&Wyplosz (2012) EPW08: Labor Market Policy 32

Results

Year	Netherlands	Ireland
1980	1.00	0.50
1982	1.00	0.55
1984	1.00	0.60
1986	1.00	0.60
1988	1.00	0.60
1990	1.00	0.65
1992	1.00	0.65
1994	1.00	0.70
1996	1.00	0.80
1998	1.00	1.00
2000	1.00	1.10
2002	1.00	1.20
2004	1.00	1.30
2006	1.00	1.45
2008	1.00	1.30
2010	1.00	1.10

Source: Burda&Wyplosz (2012) EPW08: Labor Market Policy 33
