

OECD EMPLOYMENT OUTLOOK
July 2004

TUAC EVALUATION

Overview

When OECD Employment and Labour Ministers met in September 2003 in Paris, they commissioned the OECD to reassess the *OECD Jobs Strategy*, which had been formulated almost ten years ago as a “blueprint for labour market reform” to cut high and persistent unemployment. Accordingly, the *OECD Employment Outlook 2004*, the OECD's annual review of labour market trends and issues, provides a number of building blocks contributing to the reassessment of the *Jobs Strategy*.

Paradoxically the press coverage in the French press focused on the national debate on the retreat from the 35 hour-week. However, the Outlook does not confront this directly, unlike some of the comments to the press.

It is worth noting that the approach chosen to reassess the *Jobs Strategy* provides a more balanced approach than some of the interpretations of the last ten years. It is emphasized that pursuing more and better jobs, the central objective of employment and labour market policy, “needs to be combined with other social objectives, in particular adequate social protection, a better reconciliation of work and family life, and equity outcomes” (p 12). Moreover, the OECD admits that at least some of the *Jobs Strategy* recommendations “pose a challenge to social protection” (ibid.).

The most important conclusions of the *Employment Outlook 2004* are the following:

- The continuation of the current growth, already quite strong in certain OECD member countries, would leave unemployment rates in many countries higher than they were in the 1970s and 1980s (11);
- Hours per capita and hours per worker developed very differently in most OECD countries during 1970-2000. In countries where data are available, the tendency for average hours per worker to decline during 1990-2002 was largely due to a rising incidence of part-time jobs. Moreover, OECD countries in which workers tend to work fewer hours tend to have above-average employment rates. (48-49);
- Countries with lower hours per worker tend to have also above-average productivity. This applies beside the US in particular to countries like France, Belgium, Germany, the Netherlands, Ireland and Italy. (29) Against this background the press emphasis on hours per capita is misleading;

- The study of the effects of employment protection legislation (EPL) fails to provide compelling evidence that EPL, considered by some to be a key factor in generating labour market rigidities, reduces overall employment rates and increases unemployment. In switching to a more balanced approach, the *Employment Outlook 2004* acknowledges that EPL is welfare-improving by protecting workers over a limited period of time against labour market uncertainties and causing firms to internalise some of the social costs of their dismissal decisions. The chapter concludes “that a combination of some employment protection provisions, aimed at avoiding those dismissals that would be socially ineffective, with active labour market policies and effective re-employment services aimed at enhancing hiring prospects, could contribute to a better functioning of the labour market”. (99);
- A detailed comparative analysis of the organisation of collective bargaining in OECD countries and on the evolution of these systems since 1970, provided by chapter 3 of the *Employment Outlook 2004*, leads to the conclusion that wage moderation is by no means a magic bullet to reduce unemployment. It is reported that the trend towards wage moderation as suggested by the evolution of aggregate wages in the majority of OECD member countries since the end of the 1970 was accompanied by an increase of earnings inequality and wage differentials in a number of countries. (129) However, the study also found that “high union density and bargaining coverage, and the centralisation/co-ordination of wage bargaining tend to go hand-in-hand with lower overall wage inequality”. (130);
- Chapter 4 of the *Employment Outlook 2004* tries to provide empirical evidence that can support the Jobs Strategy’s emphasis on adult learning. It finds that the importance of education and training for labour market performance is likely to have increased. This applies in particular to the individual level, where a strong association between training and employment outcomes was found. However, a clear impact of employee training on wage growth was only found in the case of young or highly educated employees. The study found also that there is a substantial correspondence between training and results at the aggregate and individual levels for employment and labour force participation, but this is not the case as regards the impact of training on unemployment. (185);
- The final chapter of the *Employment Outlook* examines so-called “informal”, “undeclared” or “underground” employment, employment which falls mainly outside the scope of taxation, social insurance and other regulations. It concluded not only that it is difficult to measure undeclared work but also that evidence for a trend increase in the size of the informal economy is mixed. It also found that high tax rates *per se* do not appear to influence levels of undeclared work in international (or time-series) comparisons. On the contrary, however, relatively ineffective social protection systems were found to be a major cause of undeclared work and large informal sectors. (228 p).

TUAC Comment on Treatment of Employment Protection Legislation

Against this background, TUAC has welcomed the fact that the *Employment Outlook 2004* acknowledges that employment protection legislation is welfare-improving by insuring the income of workers against labour market uncertainties over a limited period of time and causing firms to internalise some of the social costs of their dismissal decisions. It emphasizes

that employment security provided by EPL is conducive to investment in training by both employers and workers.

Like the 1999 review of alleged negative impacts of EPL, which was regarded in the OECD as controversial because of its conclusion that “EPL strictness has little or no effect on overall unemployment”, the new issue of the *Employment Outlook* does not provide evidence supporting the recommendation to remove strict EP. Neither the review of the theoretical analysis nor the review of empirical studies provides clear-cut answers on the effect of employment protection on overall employment and unemployment.

The same applies to the assertion “that EPL tends to depress labour market flows and thus slows down labour market adjustment”. Evidence related to labour market dynamics in Nordic countries gives a picture in striking contrast to the assertion that EPL is making it more difficult for jobseekers to enter employment. Despite a rather high level of EPL they tend to have relative high rates of outflows from out of unemployment. Moreover, the recent performance of the Nordic countries, in particular of Sweden and Finland, on productivity, growth and employment, as revealed by the *OECD Growth Study*, provides a serious challenge to the assertion that high levels of EPL are an impediment to the adoption of new technologies and innovation.

It is also worth noting that this concurs with recent studies on the impact of EPL on labour market dynamics and the ability of firms to hire workers do not suggest that strict EPL would reduce the re-employment chances of unemployed workers. A recent study focusing on the effects of EPL on the termination of employment relationships in Germany failed to provide evidence “that the current statutory protection against dismissals represents a considerable financial risk for employers desiring to recruit additional personnel”. The same study also found that between the years 1996 and 2001 labour turnover in Germany was not substantially lower than in other countries considered to have less strict EPL; labour turnover over that period ranged between 10 and 13 per cent, i.e. between 3.5 and 4.5 million jobs were terminated and an equal number of employees were given new employment contracts. Therefore, the study does not lend support to the view that EPL prohibits labour market flexibility. Moreover, the study concluded that easing EPL for small enterprises would not stimulate their willingness to increase employment.¹

A recent study on the role of EPL in determining firm size distribution, conducted by the research department of the Bank of Italy, reported similar findings. The findings suggest that EPL is unlikely to be a major determinant of cross-country differences in firm size. According to the study the effects of EPL on firm size distributions are quantitatively modest: Removing the threshold effect of a rather strict EPL for firms in Italy above the 15 employees threshold would increase average firm size by less than 1%.

Lessons for the reassessment of the *OECD Jobs Strategy*

The findings of recent studies on the effects of EPL lead to two important conclusions. Firstly, specific forms of employment protection legislation are consistent with good employment performance. Well-designed and decent systems of employment protection legislation do not prevent high rates of employment. Secondly, the current reassessment of the *Jobs Strategy*, the OECD blue print for labour market reform, must take into account the fact

¹ See the EIRO report “Study examines employment effects of statutory protection against dismissal”, at <http://www.eiro.eurofound.eu.int/print/2003/04/feature/de0304204f.html>

that efforts to implement labour market deregulation did not lead to an impressive performance regarding growth and employment as asserted. It must also address the issue of how can social security link best to adaptability in order to make both more compatible and mutually supportive? Above all it must examine the key linkage of growth-orientated macroeconomic policy and good employment performance.