

**CPB-ROA Conference on Flexibility of the
Labour Market**
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Flexibility, Dualism and the Great Recession
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comments
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The content of the presentation



- This is an impressive presentation that draws from an even more impressive draft chapter for the *Handbook in Labour Economics*
- It provides:
 - An account of labour market reforms in OECD countries (part of a detailed inventory of reforms, very useful for policy analysis)
 - A taxonomy of these reforms along two main criteria:
 - Scope : Two-tier vs. Complete
 - Size: Incremental vs. Discrete
 - An extension of the policy-augmented MP job search model to allow for two-tier reforms, leading to different results than complete reforms on flows and levels
 - A reflection on possible links between financial and labour frictions to shed light on the effects of the Great Recession on labour market outcomes
 - And a “way forward” reduce/eliminate dualism

The main messages (1)



- A large number of labour market reforms in all countries
 - Net changes hide significant more dynamism with some changes undoing previous reforms
 - Partial reforms dominate in the labour market:
 - Two-tier reforms account for more that 50% of all reforms;
 - Incremental reforms account for vast majority; much more than in other markets, e.g. Product Mkt; Financial Mkt.
- Some remarks
 - The size dimension captures the “potential” relevance of each reform episode, but a series of consistent incremental reforms could be not only more feasible politically but also important → consistency of subsequent reform episodes
 - In some cases, two-tier reforms are needed to treat sub-groups (e.g. extension of UBs to previously non-covered groups; elimination of early retirement schemes, strengthening activation from previously excluded groups (e.g. disability benefits))
 - Important interactions may magnify the impact of individual reforms

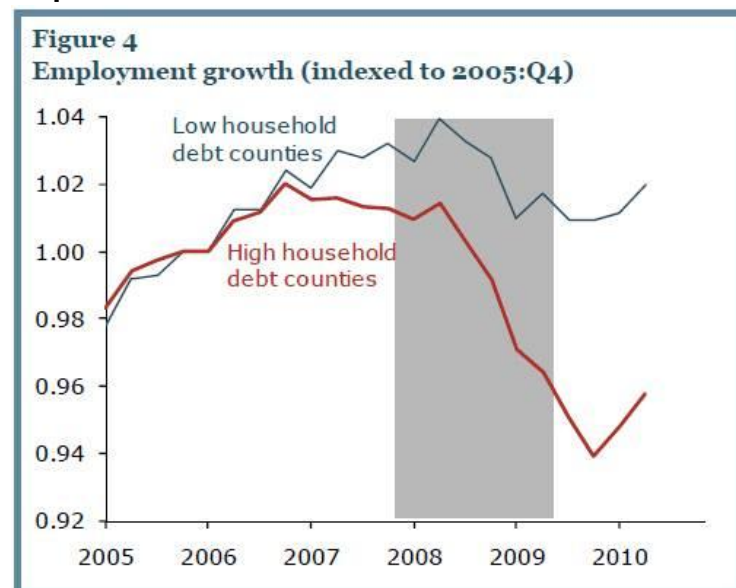
The main messages (2)



- An extended MP equilibrium search model with endogenous job creation and destruction:
 - Two-tier regimes generate two wage equations (outsiders or entry jobs and insiders), with insiders enjoying higher wages and avg. lower productivity
 - This setting leads to different results *vis à vis* complete reforms, e.g.:
 - An increase in UB generosity does not necessarily raise U; it may actually reduce it if accompanied by a decline in generosity for those on entry jobs;
 - An increase in firing costs may increase turnover. E subsidies for entry jobs may increase churning on that margin.
- Some remarks
 - The model does not consider budget constraint: i.e. an increase in UBs will have to be financed with e.g. higher taxes or lower E subsidy with counteracting effects
 - Policy endogeneity, difficult to model but important in practice (e.g. Court rulings; UB coverage, ALMP responding to LM conditions, business cycle)

The main messages (3)

- Financial crisis and labour market dynamics:
 - While financial deepening reduces churning and E volatility, in major financial crises strong impact on JD by highly leveraged firms (L demand)
 - Financial deepening promotes worker mobility but in a fin crisis with collapse of house prices mobility is reduced (L supply effect).
 - The combination of high-leverage and dualism (or low EPL) magnifies job destruction in deep recessions.



Mian and Sufi, FRBSF, *Economic Letter*, Jan. 2011

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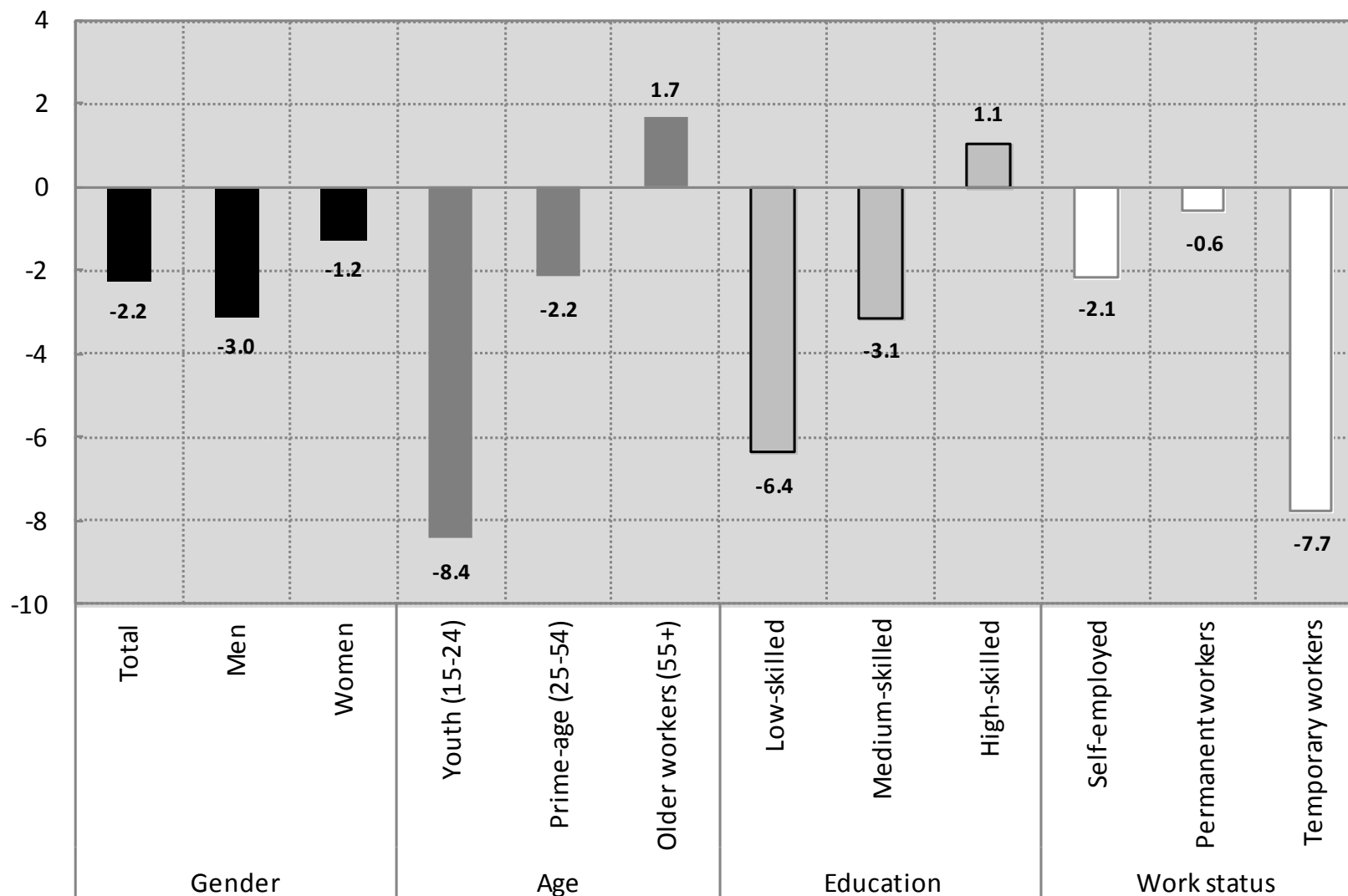


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- Some remarks
 - The two-tier model fits the evidence well, even during the GR
 - The GR, more than in the past, showed endogenous policy responses with significant effects on LM dynamics (e.g. Widening coverage of UBs; STWs; increase in ALMP; hiring subsidies etc.)

Job losses have been concentrated among youth, the low-skilled and men



Percentage change of employment over 2008 Q4 to 2009 Q4*



* Data on employment by work status refer to the period 2008Q2 to 2009Q2.

The main messages (3)

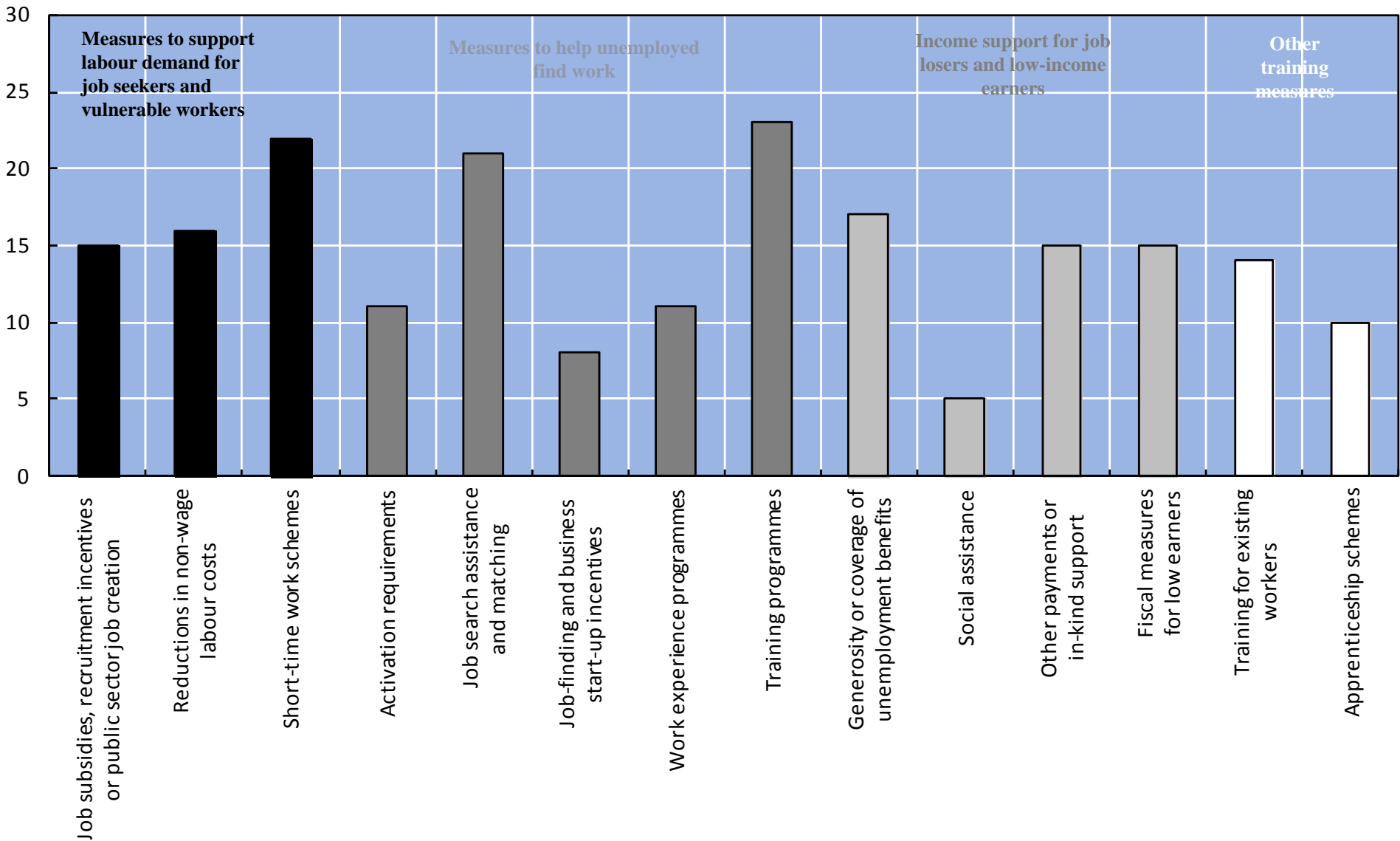


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Discretionary changes in labour market policy in response to the economic downturn (2009)

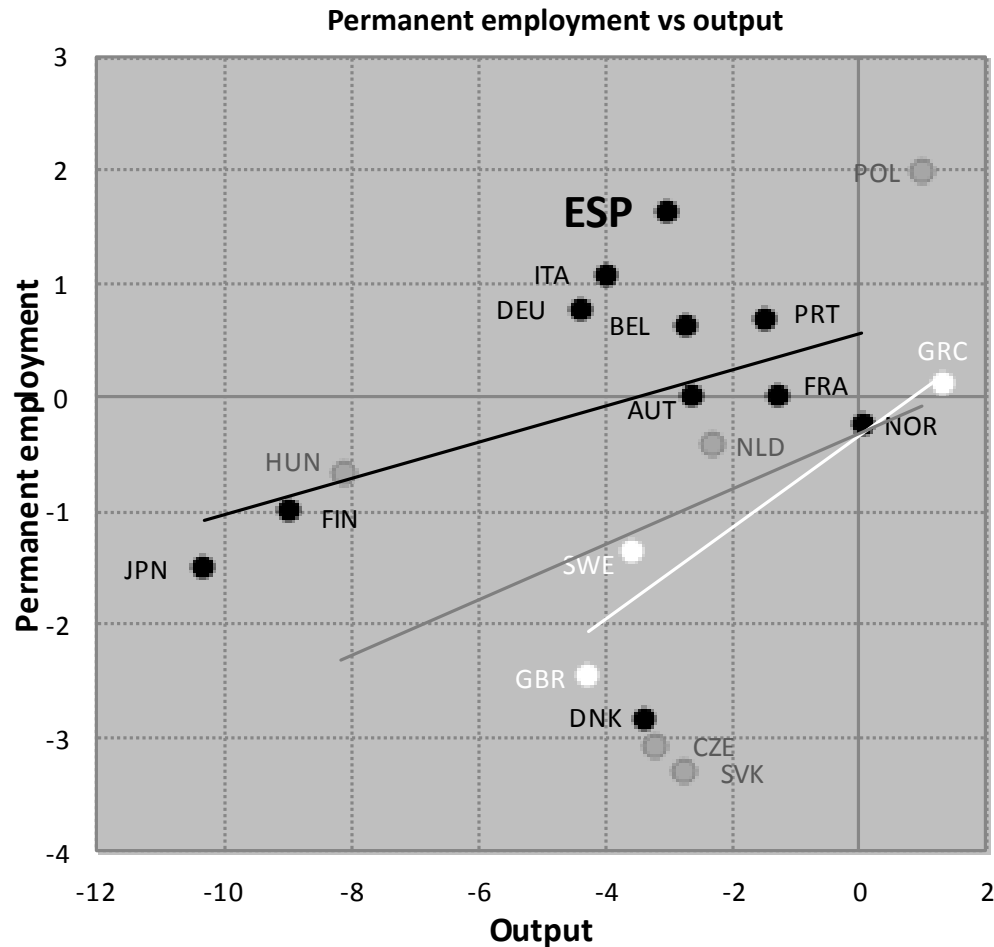
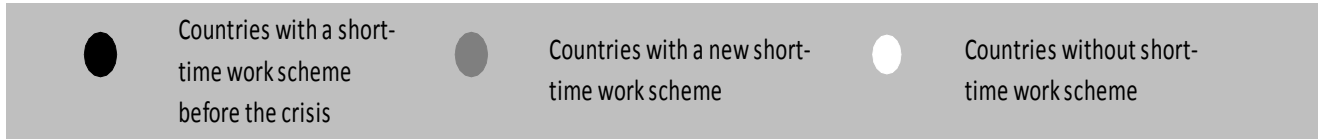


Number of OECD countries that have taken different types of measures



Did short-time work schemes affect labour market adjustment during the 2008-09 recession?

Percentage change between 2008 Q3 and 2009 Q3



The main messages (4)



- The need for a “smart” reform to go beyond dualism: a *contrat unique*?
 - Tenure track to stable jobs with protection increasing with tenure
 - Firms would enjoy flexibility at entry
 - Set a well defined path to stability for workers
 - Better than rebalancing EPL by raising protection for temp while relaxing it for permanent

Some remarks

- Flexibility at entry important; but also needed among those on open-ended contracts (stringency of open-ended contracts also important)
- Consider any reform of EPL as part of a package that involves adequate UBs coupled with activation and mutual obligations