

**CPB-ROA Conference on  
«Flexibility of the Labour Market»  
The Hague  
20-21 January 2011**



# **Setting it Right: Employment Protection, Labour Reallocation, Productivity**

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# Focus of the Paper



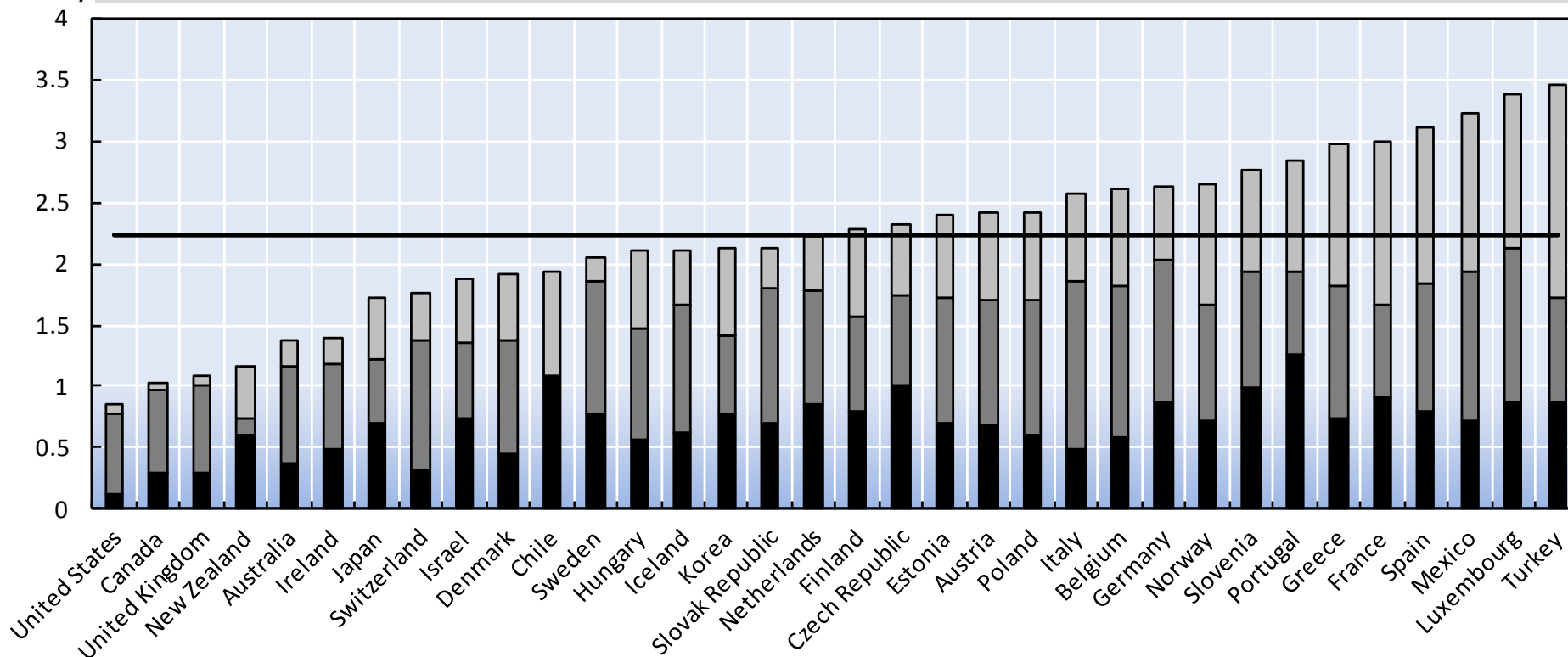
- Process of labour reallocation is a crucial factor in driving productivity growth
- Employment Protection (EP) is a potentially important determinant of labour reallocation and productivity growth
- Literature on the impacts of EP on labour reallocation is limited
- Paper reviews evidence on these links drawing on recent OECD work

# EP in OECD countries



2008  
(scale 0-6)

- Protection of permanent workers against (individual) dismissal
- Specific requirements for collective dismissal
- Regulation on temporary forms of employment



Source: Online OECD Employment database .

# REALLOCATION OF JOBS AND WORKERS



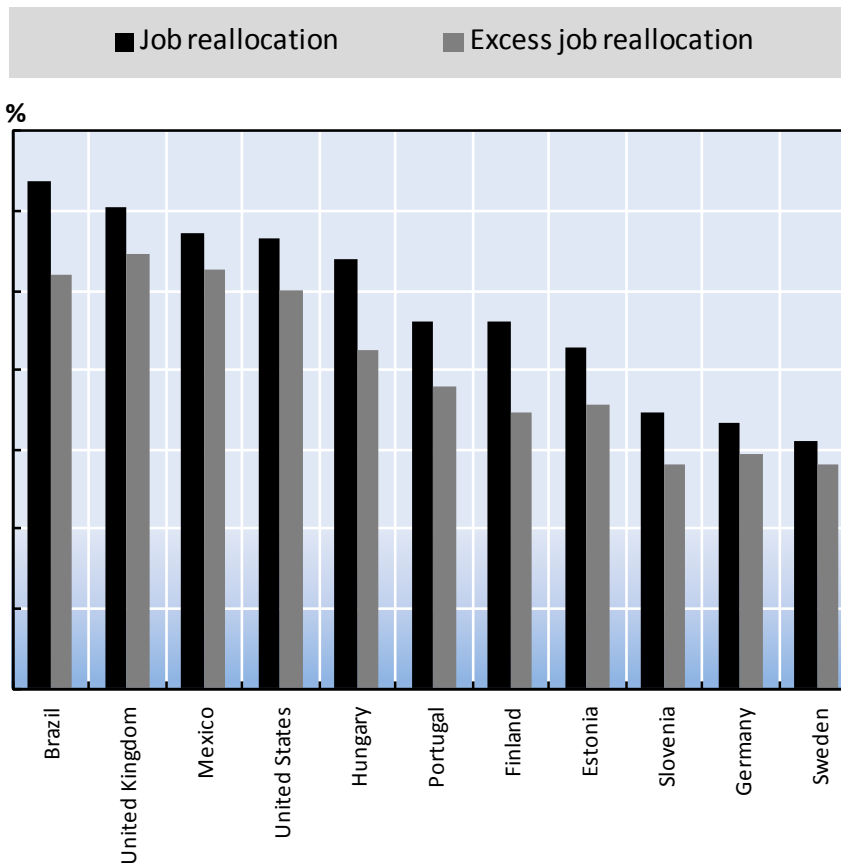
- Focus on both job creation/job destruction by firms (firm-level job reallocation) and hires and quits (worker reallocation)
- Job creation (JC) = net employment growth at new + expanding firms;  
Job destruction (JD) = jobs lost at exiting + contracting firms;  
Job reallocation = JC + JD  
Worker reallocation = hires + separations
- Data on job flows come from business registers/tax files - see Haltiwanger *et al.* (2006)  
Data on worker flows obtained from micro-data underlying national LFSs.

# REALLOCATION OF JOBS AND WORKERS

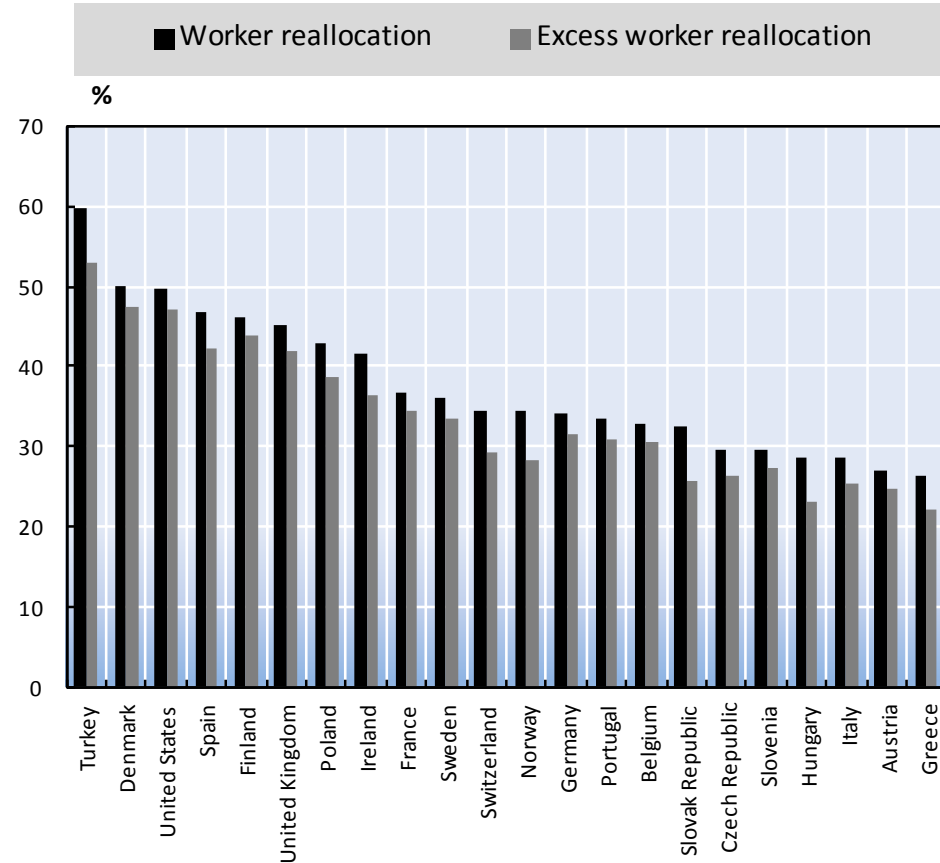


Country averages of job and worker reallocation rates expressed in percentages and adjusted by industry composition

**Panel A.** Job reallocation and excess job reallocation, 1997-2004



**Panel B.** Worker reallocation and excess worker reallocation, 2000-05



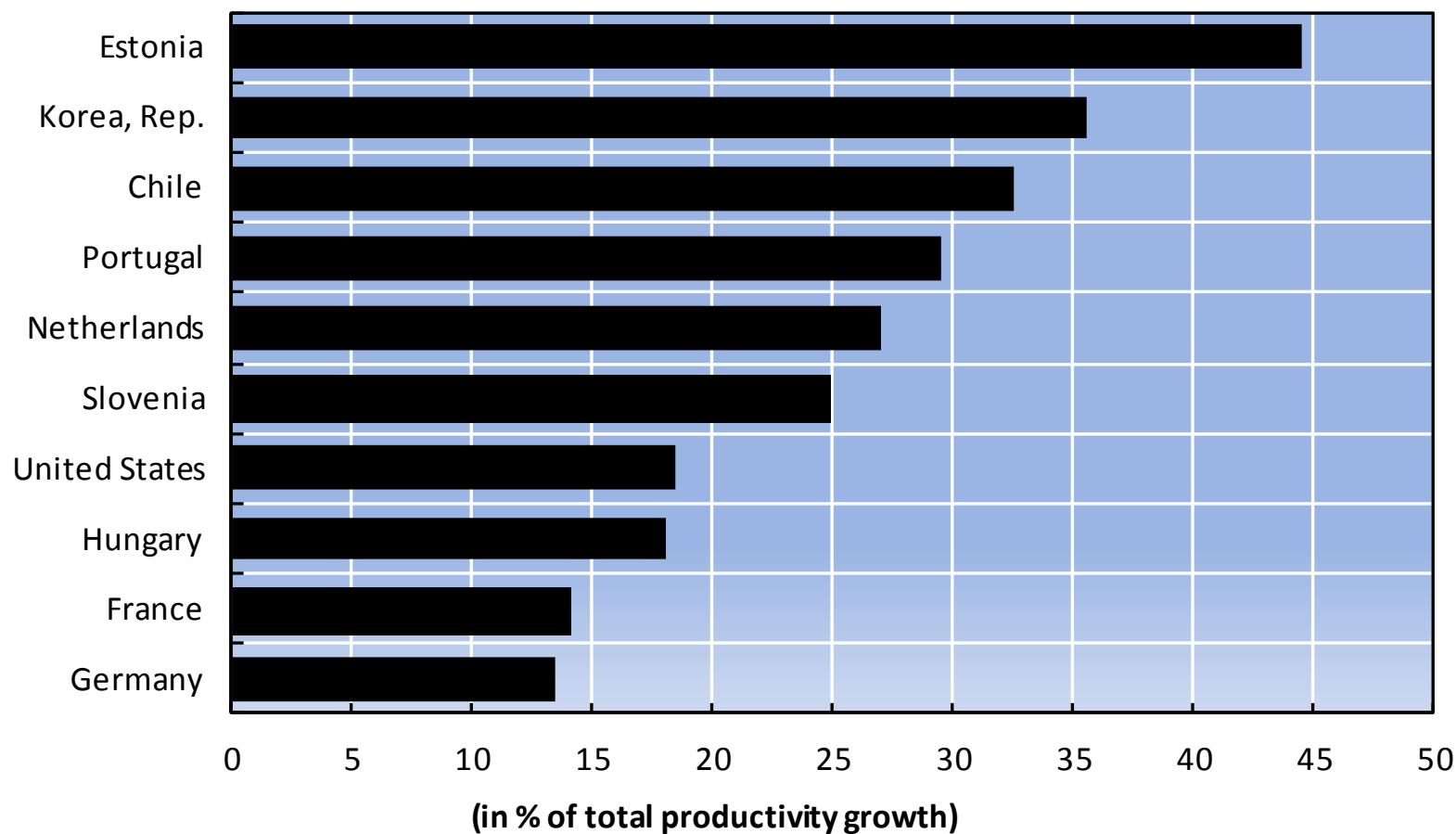
Source: OECD Employment Outlook 2009.

# THEORETICAL LINKS BETWEEN EP, LABOUR REALLOCATION AND PRODUCTIVITY



- Imposition of firing costs likely to hinder efficient workforce adjustment to shocks tending to lower labour reallocation (Mortensen and Pissarides, 1994; Bentolila and Bertola, 1990)
- Reform of EP via asymmetric liberalisation of temporary contracts leads firms to substitute temporary for permanent workers
- If EP raises costs of workforce adjustments and/or composition of employment between temporary and regular contracts, likely to have negative impact on efficient allocation of labour/productivity growth

## The effect of net entry on total labour productivity growth



# EVIDENCE ON LINKS BETWEEN EP AND LABOUR REALLOCATION



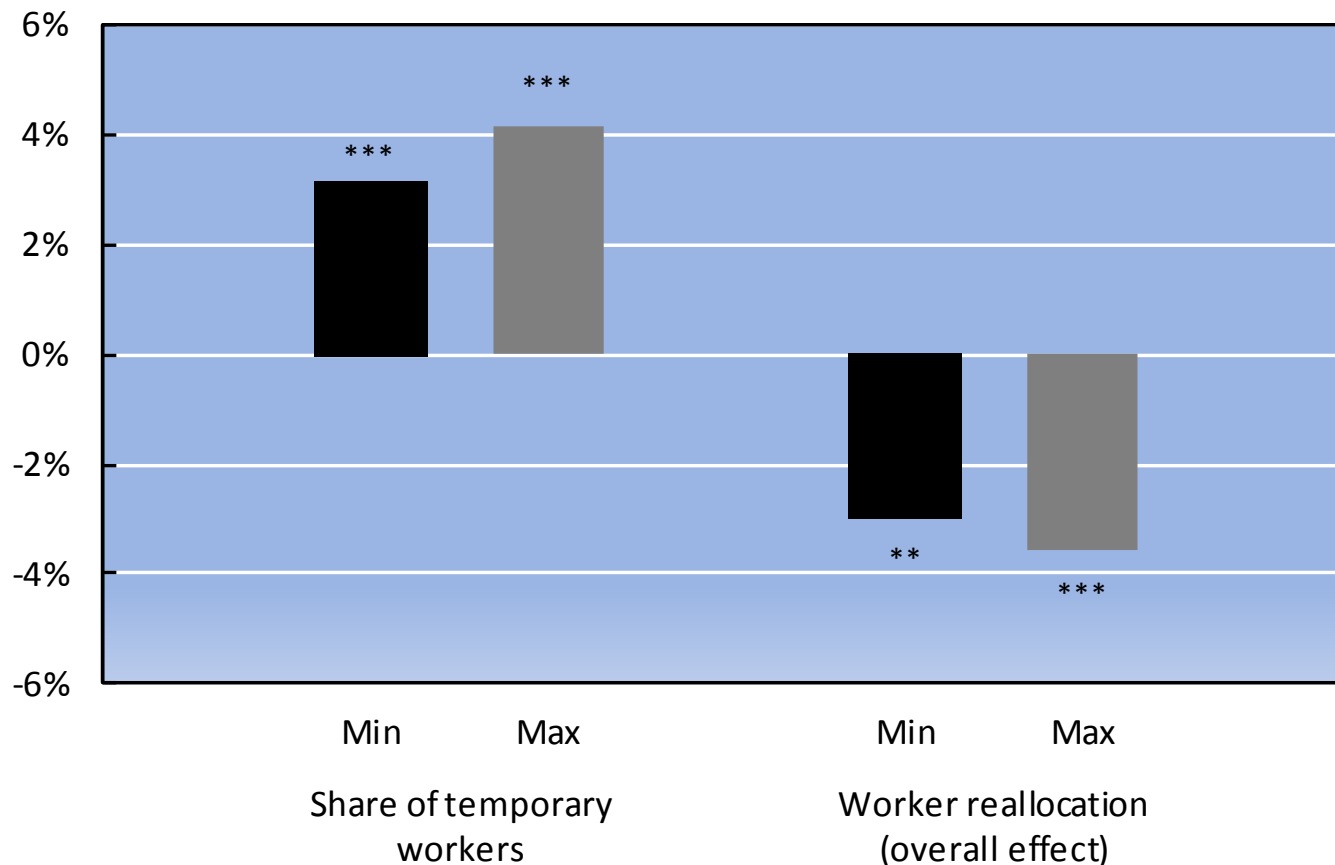
- Many country case studies (US, Italy, Spain, Turkey) provide supporting evidence
- Similar effects from cross-country panel studies, e.g. OECD (2010) which analysed worker flows using industry-level data for 24 industries and 24 countries
  - It uses a DiD approach, controlling for country and industry effects
- Results in OECD (2010) suggest that a 1 point increase in EP strictness for regular workers cuts worker reallocation by between  $5\frac{1}{4}$  and  $6\frac{3}{4}$  percentage points; similarly estimated to cut separation rates by  $2\frac{1}{4}$ -3 percentage points



# Regulation for individual and collective dismissals, share of temporary workers and overall impact on worker reallocation



## Regulation for individual and collective dismissals, share of temporary workers and overall impact on worker reallocation



# EVIDENCE ON LINKS BETWEEN EP AND PRODUCTIVITY

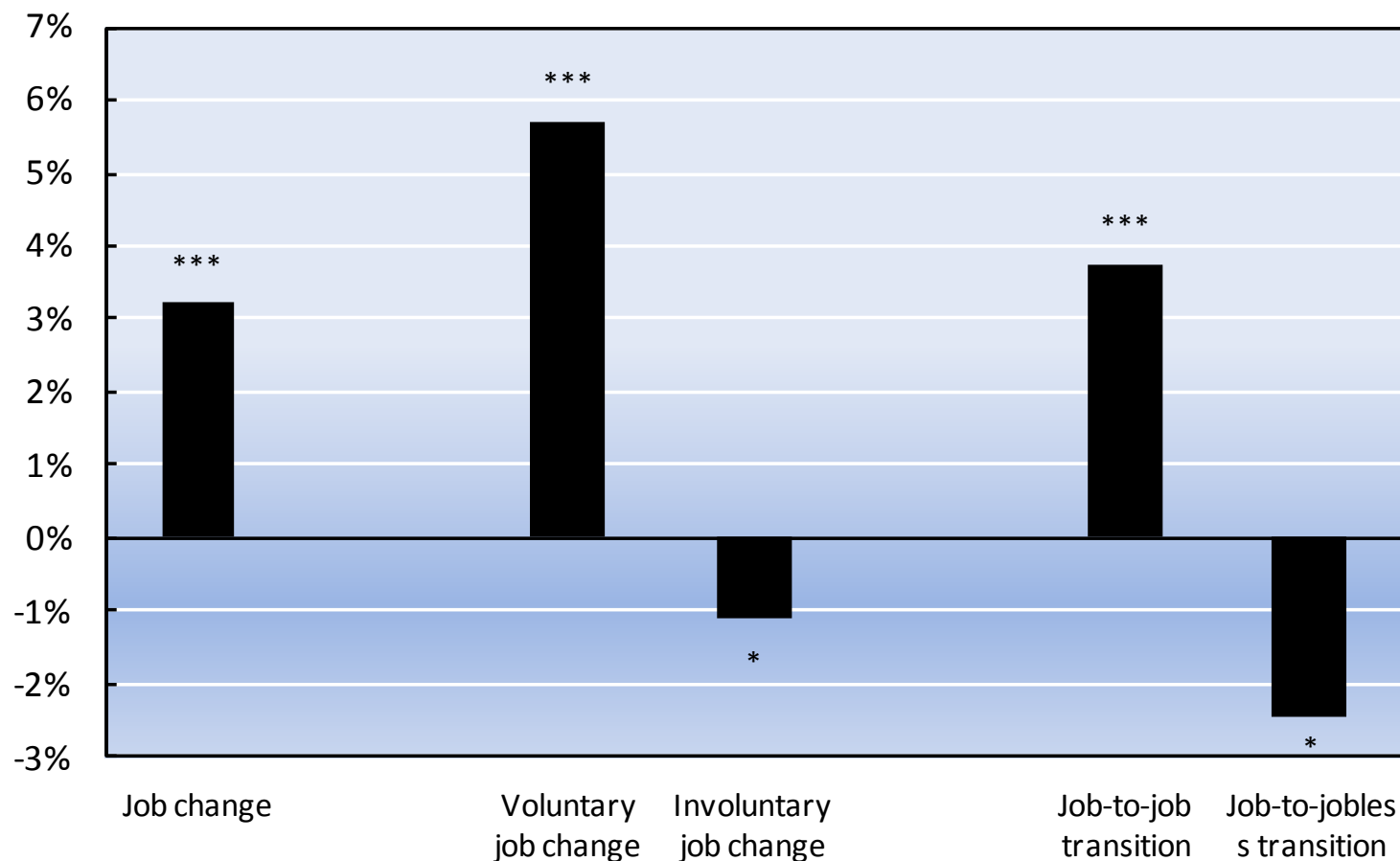


- Evidence from country case studies mixed on this key link
- But evidence from cross-country studies is more consistent: strict EP has a negative impact on TFP and labour productivity
- OECD (2007), Bassanini *et al.* (2009) use a DiD approach to data for 19 industries in 11-16 OECD countries over the period 1982-2003
  - Results show that strict EP for regular workers has a significant negative impact on labour productivity growth.

# DO WORKERS BENEFIT FROM MORE FLEXIBLE EP PROVISIONS?



Average wage premia to job change, 1995-2001



# POLICY CONCLUSIONS



- Reforms to EP should be part of a comprehensive strategy to create more and better jobs, see OECD (2006).
  - Must include appropriate macroeconomic policies; steps to increase product market competition; foster lifelong learning
  
- Comprehensive approach needs to secure a new “flexicurity-type balance” which includes:
  - Reasonably generous social safety net
  - Backed by effective activation regime
  
- Several different routes to reform of EP as part of a comprehensive reform package