

VII. RECENT LABOUR-MARKET PERFORMANCE AND STRUCTURAL REFORMS

The past three years have been marked by favourable conditions in labour markets in most Member countries. In the United States, employment has continued to expand at a fast rate, and the unemployment rate has fallen to its lowest level for a generation with only a modest rise in underlying inflation so far. In many European countries, job creation has been progressing at its fastest pace since the late-1980s boom. Canada and Australia have also recorded robust employment gains and falling unemployment rates. The most notable exception to these favourable developments is Japan, where the recession has driven joblessness to historical highs. The improving macroeconomic environment has been a major factor behind these developments, but structural reforms that have been implemented during the past decade have made an important contribution to better labour market performance. The first part of this chapter briefly reviews recent developments in labour markets in OECD countries, and the second part surveys structural reforms that have influenced them.

Conditions in labour markets of most Member countries have been favourable in recent years

Labour market trends since 1997

With the exceptions of Japan and Korea, the aggregate unemployment rate has declined notably in most OECD countries since 1997 (Table VII.1). In the United States, joblessness had already fallen strongly by 1997 as the economy recovered from the 1990-91 recession, but continued declines have taken the unemployment rate to its lowest since the 1960s. By contrast, the unemployment rate in the European Union (EU) started falling only in 1997. Although the unemployment rate has come down by 1½ percentage points, it still has some way to go to reach its 1990 level of just over 8 per cent, let alone the much lower levels of the 1960s and 1970s. The average for the European Union hides striking difference across the member countries. Italy has achieved only small reductions in its unemployment rate, while some of the other EU countries have seen major cuts in joblessness. Indeed, the unemployment rates in the United Kingdom, Denmark, Ireland and the Netherlands have fallen to their lowest levels since the 1970s.

Unemployment rates have fallen in most OECD countries in the past few years...

The reductions in unemployment in the United States and more recently in Europe have been driven by solid employment gains (Figure VII.1). In the United States continued increases in employment since 1997 have taken place against the background of surprisingly robust labour productivity growth at this mature stage of the expansion, which may reflect some fundamental changes in the economy.¹ In Europe, by contrast, the employment content of growth has risen compared to the 1980s, perhaps as a result of lower productivity workers becoming employed

... as employment has risen strongly...

1. See Chapter V, "Recent Growth Trends in OECD Countries".

Table VII.1. Unemployment rates and labour force participation rates

Per cent

	Unemployment rate ^a			Labour force participation rate ^b		
	1990	1997	1999	1990	1997	1999
United States	5.6	4.9	4.2	76.5	77.4	77.2
European Union	8.1	10.6	9.2	67.3	67.9	69.0
of which:						
Germany	4.8	9.9	8.7	68.4	71.0	71.2
France	9.0	12.3	11.3	66.0	67.1	67.8
Italy	9.0	11.7	11.4	59.8	57.7	59.6
United Kingdom	7.1	7.0	6.1	77.8	76.2	76.3
Spain	16.3	20.8	15.9	60.9	62.5	63.9
Netherlands	6.2	5.2	3.3	66.2	71.5	73.6
Belgium	6.7	9.4	9.0	58.7	62.6	64.6
Sweden	1.7	9.9	7.2	84.6	78.7	78.5
Austria	..	4.4	3.7	..	70.9	71.6
Greece	6.4	9.8	..	59.1	60.8	..
Portugal	4.6	6.8	4.5	70.9	69.8	70.6
Denmark	7.7	5.6	5.2	82.4	79.8	80.6
Finland	3.2	12.7	10.3	76.6	72.1	73.6
Ireland	13.4	9.9	5.8	60.2	62.7	66.3
Luxembourg	1.7	2.8	2.3	60.1	61.5	63.1
Japan	2.1	3.4	4.7	70.1	72.6	72.4
Canada	8.1	9.1	7.6	76.6	74.9	75.9
Australia	7.0	8.5	7.2	73.0	72.4	73.6
Korea	2.5	2.7	6.5	62.8	65.4	63.9
New Zealand	7.8	6.7	6.8	73.0	75.6	75.2
Switzerland	..	4.2	..	81.1	81.5	82.2

a) Standardised unemployment rates except for Korea.

b) For persons aged 15-64 years.

Source: OECD Employment Outlook, Paris, 2000.

(see below). However, employment gains have been unevenly distributed across member countries of the European Union. For example, employment levels in Germany were broadly unchanged in 1999 from 1997, whereas they rose by 18 per cent in Ireland over the same period.

... and participation rates have risen or remained unchanged

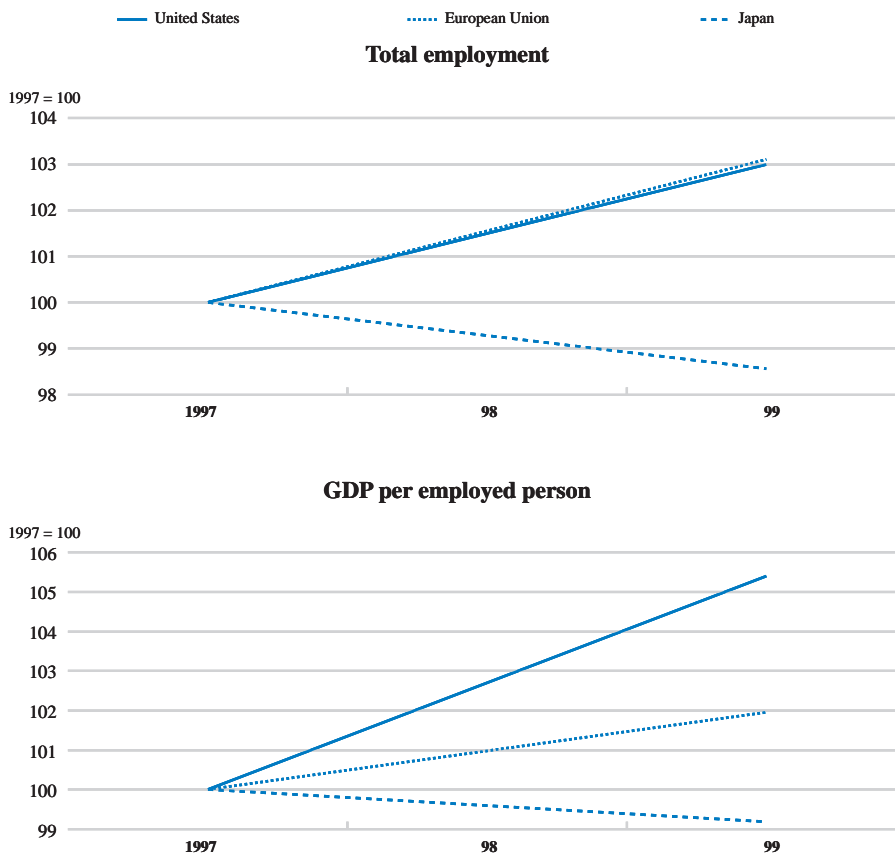
Labour-force participation rates have remained largely unchanged or risen somewhat in most Member countries over the past three years. In the United States, the record rates attained in 1997 have been maintained. In Japan, the long-term rise in participation rates also came to a halt in 1997, as the economy entered recession, and the persistent weakness since then has held down the rates. In most European Union countries, on the other hand, the share of the working-age population entering the labour market has continued to increase, though it still remains well below that in the United States and Japan (with the exception of the Nordic EU countries and the United Kingdom).

The situation for disadvantaged groups has generally improved with better aggregate performance...

Disadvantaged groups in the labour market have benefited from improved labour-market situations over the past three years, and in some cases their situation has improved more than for the labour market in the aggregate though their share in overall unemployment has not always fallen.

- *Long-term unemployed.* The share of the labour force that has been unemployed for more than six or 12 months has fallen in all the countries that have registered falling aggregate unemployment rates. However, measured as a

Figure VII.1. Employment and productivity



Source: OECD.

share of total unemployment, long-term unemployment has declined only modestly since 1997 in the majority of these countries (Figure VII.2). It has fallen notably (more than 5 percentage points) in Portugal, United Kingdom, Denmark, Netherlands and Norway, but increased significantly in Switzerland. It still remains very high in Italy and Belgium.

- *Young people.* With the exception of Belgium, Denmark and Switzerland, the unemployment rate for those under 25 years (Table VII.2) has fallen more than for the prime-aged labour force. In Spain, the youth unemployment rate has fallen by close to 10 percentage points since 1997; the reduction has been around 5 percentage points or more in Ireland, Sweden and Portugal. Notwithstanding the recent reductions in youth unemployment rates, they remain high in many European countries, notably in France, Italy and Spain. As the drop in youth unemployment has not been accompanied by reduced labour-force participation rates (except in the United Kingdom and Denmark), youth employment rates have increased significantly.
- *Older people.* Employment-to-population ratios for persons aged 55-64 have tended to rise modestly since 1997 (Figure VII.3). The increase has been most marked (over 3 percentage points) in the Netherlands, Ireland, Finland and Portugal, and, outside Europe, notable increases were recorded in

Figure VII.2. Incidence of long-term unemployment (12 months or more)

As a percentage of total unemployment

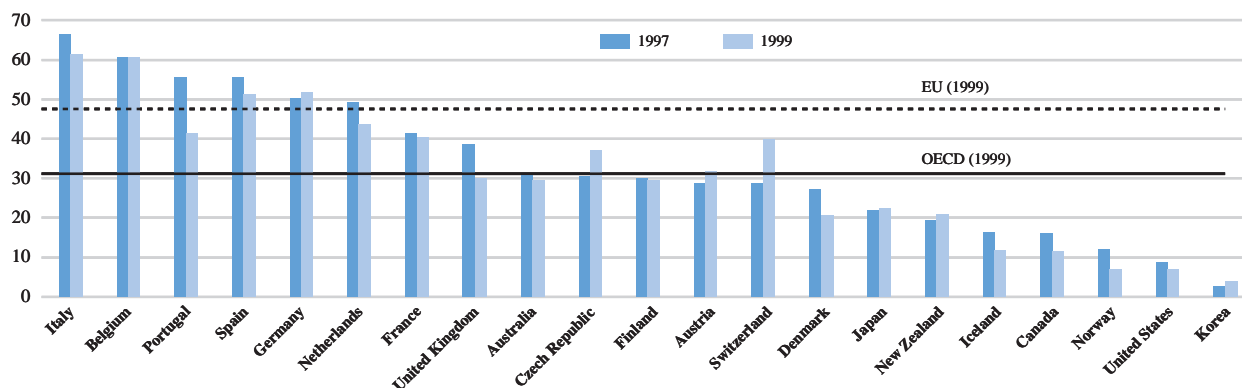
Source: OECD, *Employment Outlook*, Paris, 2000.

Table VII.2. Unemployment rates for young people and women

Per cent

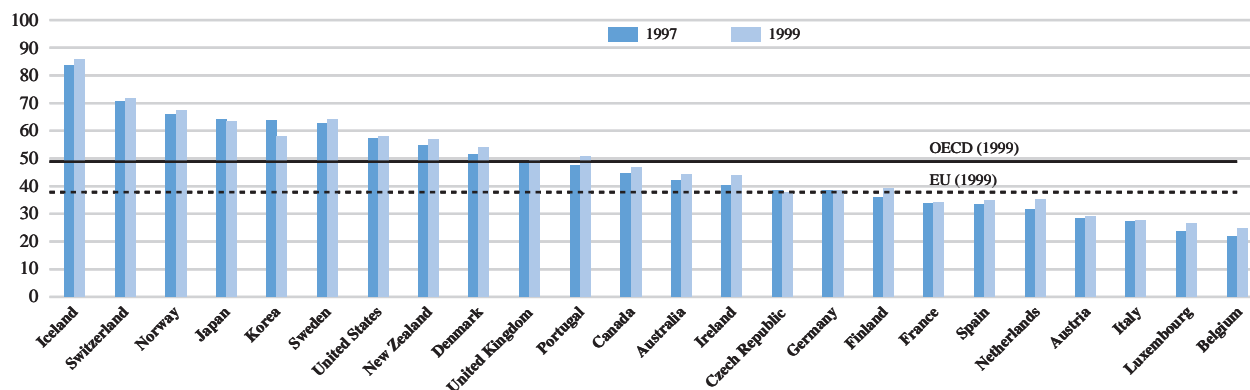
	Young people ^a			Women		
	1990	1997	1999	1990	1997	1999
United States	11.2	11.3	9.9	5.6	5.1	4.4
European Union	15.8	20.5	17.2	10.8	12.4	10.9
<i>of which:</i>						
Germany	5.6	10.2	8.5	7.5	10.7	9.3
France	19.1	28.1	26.6	12.1	14.2	13.7
Italy	28.9	33.6	32.9	15.8	16.8	16.4
United Kingdom	10.1	13.5	12.3	6.5	5.8	5.1
Spain	30.1	37.1	28.5	24.4	28.4	23.2
Netherlands	11.1	9.7	7.4	10.9	7.2	4.9
Belgium	14.5	21.3	22.6	11.5	11.6	10.3
Sweden	4.5	22.5	14.2	1.8	9.9	6.7
Austria	..	7.6	5.9	..	5.3	4.8
Greece	23.3	31.0	..	12.0	15.1	..
Portugal	9.6	14.6	8.7	7.0	8.2	5.3
Denmark	11.5	8.1	10.0	9.0	6.5	5.9
Finland	9.4	25.3	21.5	2.7	13.1	10.8
Ireland	17.6	16.1	8.5	14.0	10.4	5.5
Luxembourg	3.7	7.3	6.8	2.5	3.7	3.3
Japan	4.3	6.6	9.3	2.3	3.6	4.7
Canada	12.4	16.2	14.0	8.1	8.9	7.3
Australia	13.2	15.9	13.9	7.2	8.1	7.2
New Zealand	14.1	13.1	13.7	7.3	6.7	6.6
Korea	7.0	7.7	14.2	1.9	2.4	5.3
Switzerland	3.2	6.0	5.6	2.6	4.0	3.6

a) For persons aged 15-24 years.

Source: OECD *Employment Outlook*, Paris, 2000.

Figure VII.3. Employment rates for people aged 55 to 64

As a percentage of population aged 55 to 64



Source: OECD, *Employment Outlook*, Paris, 2000.

Canada, Australia and New Zealand. However, the increase was only marginal in Germany and Italy, and employment-to-population ratios are still very low in several countries, with more than seven of every ten persons aged 55-64 not working in Italy, Austria and Belgium.

- *Women.* The percentage-point fall in the unemployment rate for women (see Table VII.2) has been similar to that in the total unemployment rate in most countries. In some European countries (notably Belgium) there has been a slight tendency for female unemployment rates to drop more than the total unemployment rate. In spite of recent reductions, the unemployment rate for women continues to be very high in a number of European countries, notably in Spain. With their labour force participation rate either stable or rising, the employment rate for women has risen in most Member countries since 1997.
- *Lower-skilled and less-educated persons.* In the United States, robust employment growth for adults in the lowest education category (less than a high school diploma) has reduced the unemployment rate of this group by 1½ percentage points since end-1997 (to 6 per cent in early 2000).² Lack of timely data makes it difficult to assess the labour market situation for the less educated in Europe. However, there are signs in a few countries that some improvements have taken place in the latter part of the 1990s. Thus, in France the trend decline in the share of the lowest educated in total employment in the private sector was arrested in the mid-1990s and a small increase has taken place since 1997.³
- *Regional labour market disparity.* High-unemployment regions in Spain and the United Kingdom have benefited from improvements in the national labour market (Table VII.3). However, the unemployment rate in the south of Italy has risen slightly since 1997, and the unemployment rate in the new regions in Germany has fallen less than in the old regions.

2. See Table A-5 in US Department of Labor, *Employment & Earnings*, various issues.

3. See A. Gubian, "Six ans d'allègement de cotisations employeurs sur les bas salaires", in *Bilan de la Politique de l'Emploi en 1998, Les Dossiers de la Dares*, Numéro 3-4/99, La documentation Française 2000, *OECD Economic Surveys 1999-2000 – France*, Paris (forthcoming).

Table VII.3. Regional unemployment rates^a in selected countries

Per cent

	1997	1998	1999
Germany			
Old Lander	9.8	9.4	8.8
New Lander	18.1	18.2	17.6
Italy			
North	6.4	6.1	5.4
Centre	9.8	9.5	9.2
South	21.3	21.9	21.9
United Kingdom ^b			
High unemployment regions	8.8	7.9	7.6
Low unemployment regions	5.3	4.5	4.1
Other regions	6.8	6.4	6.2
Belgium			
Flandres	6.4	6.2	..
Bruxelles	13.4	14.3	..
Wallonie	12.4	13.5	..
Spain ^c			
South	29.4	27.5	24.5
East	17.6	14.9	11.6
North	18.5	17.0	15.1
Centre	18.5	17.1	13.8

a) Survey-based unemployment rates except for Germany.

b) High unemployment regions: North-East, Wales, Scotland, Northern Ireland and London; low unemployment regions: East, South East and South West; other regions: North West, Yorkshire and Humber, East Midlands and West Midlands.

c) South: Andalucia, Canarias, Extremadura, Ceuta y Melilla; East: Aragon, Baleares, Cataluna, Comunidad Valenciana, Murcia; North: Asturias, Cantabria, Galicia, Navarra, Pais Vasco; Centre: Castilla-La Mancha, Castilla-Leon, Madrid, Rioja.

Source: OECD.

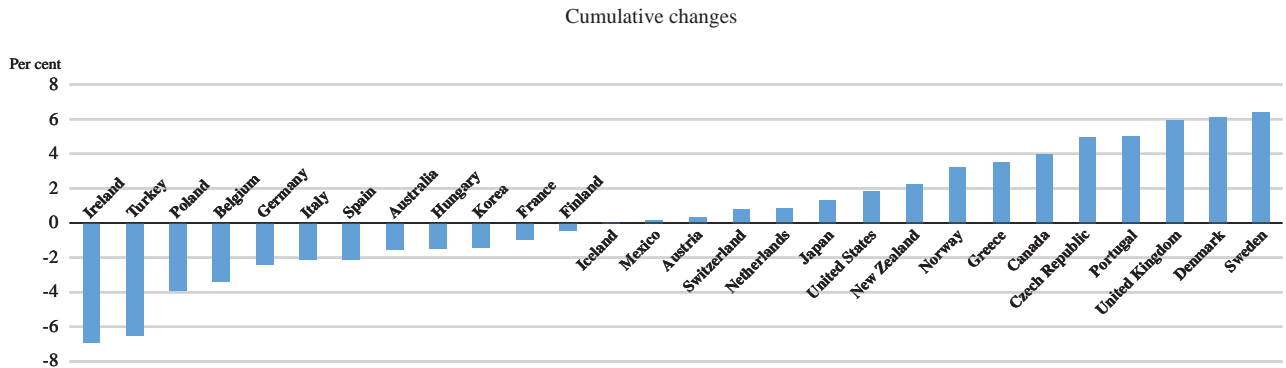
*... but disadvantaged groups
have been hard hit in Japan
and Korea*

The deterioration in labour market conditions in Japan and Korea since 1997 has affected all groups. Young people have been particularly hard hit, their unemployment rate rising more than twice as much as that for the prime-age labour force. The unemployment rate for those aged 55 to 64 has quadrupled in Korea, while the rise in Japan has been less than for the labour force as a whole. Common to both Japan and Korea is that the unemployment rate for women has risen less than the aggregate rate, but their participation rates have fallen in Korea while remaining stable in Japan. The incidence of long-term unemployment has risen only modestly in both countries.

*Real wage developments have
differed markedly across
Member countries*

Real labour cost developments have differed markedly across Member countries over the past three years. The growth in real wages and non-wage labour costs paid by employers has continued to be lower than the rate of growth of labour productivity in several European countries (Figure VII.4), including the large continental countries, and thus acted to encourage employment creation. This wage moderation has been most pronounced in Ireland, where labour productivity in the business sector has risen cumulatively by more than 6 per cent since 1996 while real labour costs per employee have only increased by 1 to 2 per cent. On the other side of the spectrum are a few European countries (Sweden, Denmark, United Kingdom and Portugal) where real compensation per employee has grown significantly faster than labour productivity growth over the past three years. Notwithstanding the starkly contrasting labour market performance in the United States and Japan over the past three years, labour costs in real terms in both countries have increased somewhat more than labour productivity in both countries.

Figure VII.4. Real wage growth minus labour productivity growth, 1996-99



Note: Real wages are defined as compensation per employee in the business sector divided by the business sector GDP price deflator; labour productivity is defined as GDP per employed person in the business sector.

Source: OECD.

The forces acting: policy reforms

The labour market developments discussed above have been influenced by government measures to encourage employment growth and reduce unemployment. In some cases, such policy reforms may swiftly show up in labour market performance. However, the experience with structural reforms indicates that it may take a long time before they translate into higher employment. For example, the beneficial effects of reforms aimed at increasing work incentives that are put in place when the economy is weak may only become apparent when economic conditions improve. Also, businesses may respond to lower employment costs implied by easier employment protection legislation only when demand picks up. For these reasons, the improvement of labour markets observed in the past three years may to some extent be rooted in measures that were implemented in the course of the 1990s and even earlier.

As reviewed in last year's report on implementing the *OECD Jobs Strategy*,⁴ progress in reforming both labour and product markets in the 1990s has been significant but uneven across countries, and differs across policy areas within individual countries. Given their high rates of unemployment, the need for reform has been most pressing in European countries. Selected features of reforms in some of these countries have involved reduction in labour costs for targeted groups, greater use of in-work financial support for low-wage earners, an adjustment of employment protection legislation for temporary and/or permanent workers, increased work incentives via more demanding entitlement conditions for unemployment benefits, and product market reforms.

A few European countries have taken measures to reduce labour costs for particular groups via cuts in employer social security contributions. These schemes have been used extensively in France (since 1993), Belgium (since 1993) and the Netherlands

Labour market improvements in the past three years partly reflect structural reforms pursued in the 1990s

In a number of European countries, employment growth has been stimulated by various policy reforms...

... cuts in payroll taxes on low earnings...

4. OECD, *Implementing the OECD Jobs Strategy – Assessing Performance and Policy*, Paris, 1999.

(since 1996). As discussed in *OECD Economic Outlook 66*,⁵ the schemes in France and the Netherlands in 1999 reduced total labour costs for minimum wage workers by 12-13 per cent. A large share of all employed persons was covered by these programmes in 1999: one-fourth in France, one-fifth in Belgium and one-sixth in the Netherlands. In the context of encouraging businesses to adopt a 35-hour working week, the French scheme was extended in the course of 1999 to cover workers earning up to 1.8 times the minimum wage and the rebate was increased. The United Kingdom reduced employer contribution rates on low earnings in 1999.

... and for other targeted groups...

Employer social security contributions have also been cut in Spain and Italy as an accompanying measure to other changes in labour market policy. To encourage the spread of new permanent contracts introduced in the 1997 Spanish reform (see below), employer social security contributions for workers on these contracts were temporarily reduced for two years (later extended to three years). The cuts varied from 20 to 60 per cent, reducing total labour costs for the average production worker by 5 to 14 per cent. In Italy, the 1997 reform reduced contribution rates for some categories of “atypical” work contracts by around two-thirds, implying the lowering of total labour costs for such contracts by more than 15 per cent.

... the introduction or expansion of in-work benefits or tax credits...

A few countries have attempted to encourage the employment of low-productivity workers by introducing or expanding in-work benefits or tax credits to top up low wages. The United Kingdom raised its in-work financial support with the introduction of the Working Families Tax Credit in 1999. The income threshold in the Irish Family Income Supplement scheme has been raised to strengthen employment incentives. An earned income tax credit and/or tax relief for childcare expenses have also been introduced or raised in Belgium, Finland, Italy and the Netherlands.

... an easing of regulations governing fixed-term contracts and temporary work agencies...

There has been a widespread easing of regulations governing fixed-term contracts and temporary work agencies in the course of the 1990s.⁶ For example, the number of permissible renewals as well as overall duration of fixed-term and temporary agency contracts were progressively extended in Germany and Belgium; restrictions on the use of fixed-term contracts were eased in Belgium and Sweden; and temporary work agencies were permitted in Spain and Sweden. The Italian (“*Pacchetto Treu*”) reform in 1997 permitted the opening of temporary work agencies, and allowed increased use of fixed-term work arrangements. Most of the employment growth since 1997 has involved such fixed-term contracts. More recently, the rules concerning the use of interim contracts for unskilled jobs have been simplified in Italy.⁷ The easing of regulations governing temporary work in many European countries is likely to have helped employment growth in the 1990s. However, the coexistence of strict employment protection legislation for permanent workers and minimal protection for temporary workers may not improve the functioning of the labour market in the longer run.⁸

... less-restrictive employment protection legislation for permanent workers...

While there has been little tendency to change employment protection legislation for regular workers in Europe, one of the few exceptions – the Spanish reform in 1997 – indicates the potential job-creation power of such changes. This reform introduced new permanent contracts with reduced severance payments for those

5. See Chapter V, “Making Work Pay” in *OECD Economic Outlook 66*, December 1999.

6. See e.g. Chapter 2 in *OECD Employment Outlook*, 1999.

7. See *OECD Economic Surveys 1999-2000 – Italy*, Paris, 2000.

8. See OECD, *Implementing the OECD Jobs Strategy – Assessing Performance and Policy*, Paris, 1999.

most exposed to unemployment or those with a weak employment record (youth, older workers, long-term unemployed) while the rules concerning fixed-term contracts were tightened somewhat. These new contracts have proven to be very popular with employers, with the cumulative number of persons with new subsidised contracts in 1998 and 1999 equal to 5½ per cent of all employed persons. There is little doubt that this has supported the overall employment gains in Spain, and, in particular, the strong job creation for young persons. However, it remains to be seen to what extent the popularity of these contracts is related to the temporary reduction in employer social security contributions rather than to the enhanced flexibility that such contracts offer. In Germany, the threshold for the size of companies that are exempt from employment protection legislation was raised from 5 to 10 employees, but this *de facto* easing of regulations was reversed in 1999.

Though the generosity and duration of unemployment benefits have not changed much over the 1990s, there has been a clear trend towards stricter eligibility criteria and tighter enforcement of such criteria in a large number of European countries. Some of the European countries that have been most successful in reducing unemployment in the 1990s have taken action in this area:⁹

... tougher eligibility criteria for unemployment benefits and stricter enforcement of such criteria,...

- In the United Kingdom, eligibility conditions for benefits have been progressively tightened. For example, stricter enforcement of eligibility criteria in 1994 led to a sharp increase in benefit sanctions, and a new comprehensive legal framework concerning eligibility requirements was introduced in 1996. The “New Deal” in 1998 stipulated compulsory contact with the public employment agency for some groups, with a refusal to accept recommended actions resulting in a withdrawal of benefits.
- In Denmark, the duration of the period in which job offers can be refused on grounds that they do not conform to previous occupation has been gradually reduced, the referral of unemployed persons to labour market programmes has been advanced, and its acceptance has been made compulsory. Much greater effort has been put into monitoring eligibility criteria, and ensuring that sanctions are applied when the criteria are not met.
- In the Netherlands, the authorities have raised the sanctions for rejecting suitable job or labour programme offers, and they have reportedly used such sanctions to encourage benefit recipients to find jobs.
- In Ireland, work availability and job search criteria were made specific in 1998. Young people have also been required to come to an interview at the public employment service after a certain length of unemployment, with a refusal of suggested interventions leading to a termination of benefits.

Tougher eligibility rules in these and other European countries have in particular acted to reduce measured youth unemployment and long-term unemployment

Widespread product market reforms in most European Member countries in the 1990s are also likely to have had beneficial effects on labour market performance. Competition in the European Union has increased in the course of the 1990s as a result of the single market programme and the establishment of a common currency among eleven of the 15 EU countries. Domestic competition in several countries has been spurred by

... and product market reforms aimed at enhancing competition

9. See Chapter 4, “Eligibility Criteria for Unemployment Benefits”, in *OECD Employment Outlook*, Paris, 2000, and *OECD Economic Surveys 1998-1999 – Ireland*, Paris, 1999.

tougher competition legislation and enforcement, and regulatory reforms, decided to a large extent at the EU level, have introduced or increased market discipline in several product markets, including parts of the old integrated network industries.

Reforms have also been implemented in the United States and other countries

The United States and some other non-European Member countries have also introduced reforms that have influenced recent labour market developments. The increased use of in-work tax credits for low-income earners in the United States has encouraged people with low earnings capacity to enter the labour market.¹⁰ Together with radical welfare reforms that have reduced work disincentives, the increased generosity of the Earned Income Tax Credit Programme has played an important role in increasing labour force participation rates of the target groups (*e.g.* lone parents with children). The overhaul of benefit systems in Canada in 1996 may have contributed to the strong growth in employment. In Australia reforms of the industrial relations system have continued, but the benefits are likely to be realised only gradually.

The reforms discussed above are clearly working towards reducing structural unemployment rates. Because some of the reforms have only been implemented recently, their full impact on structural unemployment rates will only materialise in coming years. Nevertheless, structural unemployment rates are still likely to remain high in many countries, notably in Europe, in the absence of additional reforms to better mobilise under-utilised labour resources. Continuing the process of product and labour market reforms is the surest way of increasing living standards in general and reducing the social cost related to high unemployment.

10. A simulation study indicates that the extension of the Earned Income Tax Credit in the mid-1990s increased labour market participation by 145 million hours on the assumption that entrants work 400 hours per year, which translates into an increase in the number of employed persons by around 360 thousand. The increase in total hours worked is much less since the tax credit implies disincentives for people already in work. See J.K. Scholz, "In-work benefits in the United States: The Earned Income Tax Credit", *Economic Journal*, 1996, 106, 156-169.