



Aalborg Universitet

AALBORG UNIVERSITY
DENMARK

Successful labour market approaches for dealing with the crisis

an introduction

Madsen, Per Kongshøj

Publication date:
2009

Document Version
Publisher's PDF, also known as Version of record

[Link to publication from Aalborg University](#)

Citation for published version (APA):

Madsen, P. K. (2009). *Successful labour market approaches for dealing with the crisis: an introduction*. Paper presented at Thematic Review Seminar on "Labour market policies in response to the impact of the economic crisis", Brussels, 19 May 2009, Bruxelles, Belgium. http://www.mutual-learning-employment.net/Downloads/Per_Kongshoj_Madsen_TRS_Paper.pdf

General rights

Copyright and moral rights for the publications made accessible in the public portal are retained by the authors and/or other copyright owners and it is a condition of accessing publications that users recognise and abide by the legal requirements associated with these rights.

- Users may download and print one copy of any publication from the public portal for the purpose of private study or research.
- You may not further distribute the material or use it for any profit-making activity or commercial gain
- You may freely distribute the URL identifying the publication in the public portal -

Take down policy

If you believe that this document breaches copyright please contact us at vbn@aub.aau.dk providing details, and we will remove access to the work immediately and investigate your claim.

**MUTUAL LEARNING PROGRAMME:
THEMATIC REVIEW SEMINAR – SPRING 2009**

**Successful labour market approaches for dealing with the
crisis: an introduction**

Thematic Review Seminar on “Labour market policies in response to the impact of the
economic crisis”, Brussels, 19 May 2009

A paper submitted by GHK

in consortium with CERGE-EI and Per Kongshøj Madsen

Date: 30 April 2009



This publication is supported for under the European Community Programme for Employment and Social Solidarity (2007-2013). This programme is managed by the Directorate-General for Employment, social affairs and equal opportunities of the European Commission. It was established to financially support the implementation of the objectives of the European Union in the employment and social affairs area, as set out in the Social Agenda, and thereby contribute to the achievement of the Lisbon Strategy goals in these fields.

The seven-year Programme targets all stakeholders who can help shape the development of appropriate and effective employment and social legislation and policies, across the EU-27, EFTA-EEA and EU candidate and pre-candidate countries.

PROGRESS mission is to strengthen the EU contribution in support of Member States' commitments and efforts to create more and better jobs and to build a more cohesive society. To that effect, PROGRESS will be instrumental in:

- *providing analysis and policy advice on PROGRESS policy areas;*
- *monitoring and reporting on the implementation of EU legislation and policies in PROGRESS policy areas;*
- *promoting policy transfer, learning and support among Member States on EU objectives and priorities; and*
- *relaying the views of the stakeholders and society at large*

For more information see: <http://ec.europa.eu/social/main.jsp?catId=327&langId=en>

The information contained in this publication does not necessarily reflect the position or opinion of the European Commission.

CONTENTS

1	KEY MESSAGES / EXECUTIVE SUMMARY.....	1
2	INTRODUCTION	2
3	EVEN IN TIMES OF CRISIS, THE LABOUR MARKET CREATES JOBS	3
4	DON'T PROTECT JOBS – PROTECT MOBILITY	4
5	IN THE LONG RUN, THERE IS STILL A NEED FOR INCREASED LABOUR SUPPLY.....	5
6	A HIGH LEVEL OF UNEMPLOYMENT WILL ITSELF REDUCE EFFECTIVE LABOUR SUPPLY. 6	
7	IN THE SHORT RUN, MACRO-ECONOMIC POLICY MUST CREATE THE DEMAND FOR	
	LABOUR.....	7
8	POLICY INTEGRATION IS OF UTMOST IMPORTANCE – ALSO IN TIMES OF CRISIS.....	8
9	FOCUS ON THE UPGRADING OF SKILLS	11
10	IMPLEMENTATION STRUCTURES ARE IMPORTANT	12
11	CONCLUDING REMARKS.....	13
12	REFERENCES	14

1 KEY MESSAGES / EXECUTIVE SUMMARY

The economic crisis has put the issue of labour market and employment policy high on the political agenda of both the individual member states and the European Union. Can dramatic increases in unemployment be avoided? Which are the most effective ways to create more employment? How can short-term and long-term targets for employment policy be combined?

The purpose of the present brief discussion paper is *not* to present a detailed inventory of the many concrete policies that can be applied in the present situation. Instead, the paper aims at setting the stage for more detailed policy discussions by presenting a number of general guidelines and principles that characterize the design and implementation of successful labour market approaches for dealing with the current crisis.

Seven such general guidelines are identified:

- A main focus for labour market policy should be to *strengthen “protected mobility”* through: (1) Training and retraining measures for the unemployed and those at risk of unemployment, (2) Adequate levels of income support to the unemployed which allow them to maintain a reasonable living standard, while being retrained and searching for a new job and (3) A well functioning system of public employment services that supports matching skills both in the short and the long run.
- *In the long run there is still a need for increasing labour supply in order to keep the balance between the active and the inactive population.* It is therefore important that the short-term measures to lower unemployment are not in conflict with this longer-term objective.
- *Allowing open unemployment to rise will in itself reduce effective labour supply and increase structural unemployment.* Therefore such increases should be avoided as far as possible.
- Labour market policy cannot in the short run create jobs. An *active macroeconomic policy* must therefore take responsibility.
- *Policy integration* is of the utmost importance – also in times of crisis. An important lesson from the discourse on ‘flexicurity policies’ is to support positive interactions in the form of virtuous circles between different policy elements, which can result in a win-win situation for all actors on the labour market. Job-rotation is a highly relevant strategy from this perspective.
- An economic crisis should be seen as an opportunity to reinforce the *upgrading of skills*, which will result in benefits both at the individual and societal level.
- The deliberations about successful policies should also deal with the *design of effective implementation structures* and the involvement of social partners and local actors.

2 INTRODUCTION

The economic crisis, which at present affects all European countries, has put the issue of labour market and employment policy high on the political agenda of both the individual member states and the European Union. Can dramatic increases in unemployment be avoided? Which are the most effective ways to create more employment? How can short-term and long-term targets for employment policy be combined?

The purpose of the present brief discussion paper is *not* to present a detailed inventory of the many concrete policies that can be applied in the present situation. The format of the paper alone makes such an attempt rather pointless.

Instead, the paper aims at setting the stage for such more detailed policy discussions by presenting a number of general guidelines and principles that in the author's opinion should characterize the design and implementation of successful labour market approaches for dealing with the current crisis.

3 EVEN IN TIMES OF CRISIS, THE LABOUR MARKET CREATES JOBS

One aspect of the popular media picture of the labour market is that it comes to an almost total standstill during an economic downturn. This is fortunately a misconception. Overall job-to-job mobility is always at a high level – also during economic downturns, although there is of course a cyclical element. The same goes for job destruction and job creation.

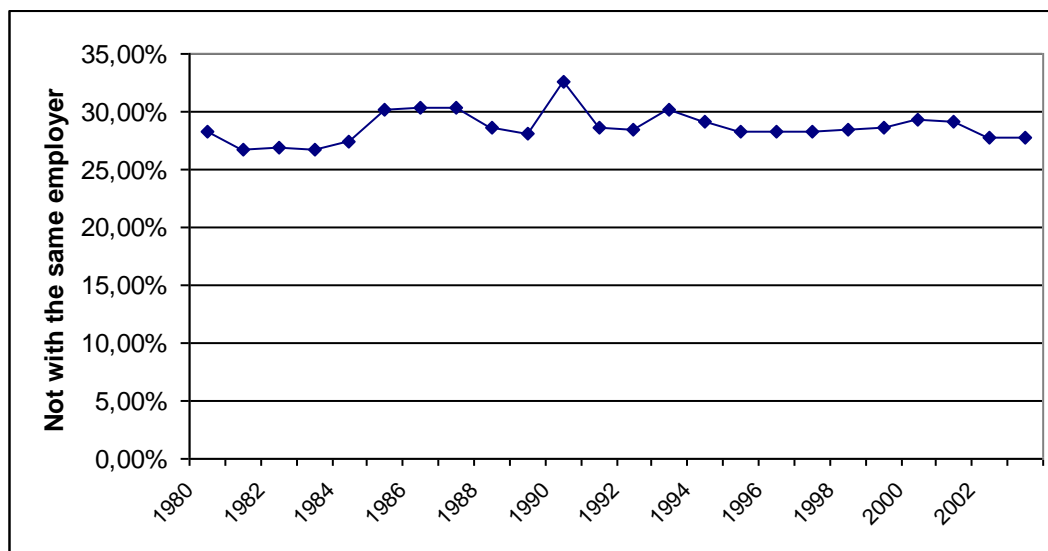


Figure 1: Job openings on the Danish labour market 1980-2003. Source: Bredgaard et al, 2009.

As an example, figure 1 shows Danish data for the share of employees that are not at the same workplace from one year to the next during the period 1980-2003 (based on register data). As can be seen, between 25 and 30 percent of all employees are mobile, when their status in year t and t+1 is compared. In the present context the main point is that the level of mobility – and thus the number of job openings - is high throughout the period 1980-2003, although some influence from the business cycle can be observed. While it is known that the number of labour market transitions on the Danish labour market is at a high level compared to other European countries, there is no reason to believe that the cyclical elements should be lower in Denmark than in other countries (cf. Danish Technological Institute, 2008).

4 DON'T PROTECT JOBS – PROTECT MOBILITY

Although it can be tempting to try to reduce mobility between jobs and overall job destruction during an economic downturn, the road to recovery is, however, not found by slowing down the processes of restructuring, but by supporting mobility towards sectors and firms with potential for growth. A main focus for labour market policy during an economic downturn should therefore be to strengthen 'protected mobility' through:

- Training and retraining measures for the unemployed and those at risk of unemployment (the latter identified through an early warning system putting demands on firms to announce their plans for collective dismissals).
- Adequate levels of income support to the unemployed that allows them to maintain a reasonable living standard, while being retrained and searching for a new job.
- A well functioning system of public employment services that can increase the transparency of the labour market and support the matching processes between potential employees and employers. In this respect it is important not only to consider the matching process in a short-term perspective, but also to apply effective measures for forecasting future skills requirements and for the implementation of findings from these processes.

These measures will therefore not only be beneficial in a short run perspective, but also underpin the potential for job-creation in the medium and long run by enhancing the economy's capacity for structural change in response to changing internal and external conditions (cf. for instance Bradley & Stephens, 2007).

5 IN THE LONG RUN, THERE IS STILL A NEED FOR INCREASED LABOUR SUPPLY

It is a recurring observation that an economic downturn and rising unemployment lead to calls for reducing labour supply, for instance by supporting the withdrawal of older workers from the labour market or the introduction of leave schemes.

In view of the long-term trend towards an ageing European population, it is important not to introduce schemes, which in the long run restrict labour supply by increasing permanently the economic incentives to early or temporary withdrawal from the labour market. This calls for a delicate balance and an awareness of the reversibility of the schemes that are introduced during times of high unemployment. Thus an important challenge in the present situation is to design and implement policies that are effective in the short run, while at the same time do not conflict with long-term objectives.

Denmark provides for interesting illustrations of the difficulties, but also the potential, with respect to balancing short and long terms consideration for labour supply.

On the one hand, the Voluntary Early Retirement Pay ("Efterløn") was introduced in 1979 as a response to the rise in unemployment during the 1970s. This scheme has since been the subject of various reforms aimed at reducing its negative effect on labour supply, but only with limited effects. Politically the scheme has developed into an integrated part of the Danish 'welfare package'. This has also been found to be true of early retirement schemes in other EU countries, whose impact has been difficult to reverse.

On the other hand, the leave schemes (Paid Leave Arrangements) that were introduced in 1993, were gradually phased out during the 1990s in line with the economic upswing and lower unemployment from the mid 1990s and onwards. They are therefore an example of an instrument, which proved to be reversible.

6 A HIGH LEVEL OF UNEMPLOYMENT WILL ITSELF REDUCE EFFECTIVE LABOUR SUPPLY

It is a standard argument of mainstream economics that 'supply creates its own demand' in the sense that an increase in labour supply will bring about a similar increase in employment. This is also the empirical argument behind the criticism of supply-restraining policies in times of rising unemployment. The argument goes that such policies will sooner or later lead to lower employment, not to lower unemployment.

However, the potential causation between labour supply and employment goes both ways. To some degree, effective labour supply is directly influenced by labour demand. This is an aspect of the concept of hysteresis, which was very popular during the 1980s, but seems to have been forgotten during the upswing in recent years. The main point in hysteresis is that short-term increases in unemployment lead to a lasting increase in structural unemployment. One reason is that the unemployed gradually lose their competences and thus become stuck in unemployment. Thus, changes in behaviour, knowledge and competence among the unemployed, such as forgetting the details of work or work behaviour, or losing interest or skill in getting new jobs, could lead to declining chances of becoming employed.

Also, the size of the workforce itself is influenced by labour demand. A strong economic upswing leads to a rising number of persons entering the workforce, often from among the 'weaker groups' of immigrants, older workers and disabled persons. The opposite development takes place during periods of depression and high unemployment. Keeping unemployment down is therefore in itself a policy, which directly stimulates labour supply and the inclusion of persons at the margin of the labour market.

Two important conclusions thus stem from these considerations. Firstly, one must be cautious to let the policies to reduce unemployment be guided by the empirically fragile concept of 'structural unemployment'.

Secondly, one important factor, which influences structural unemployment, is the demand for labour itself. If one therefore allows actual unemployment to increase, there is a risk that this rise in unemployment becomes 'structural' in the sense that the unemployed gradually loses their employability and therefore the capacity to influence wage bargaining. On the other hand, a strong demand for labour in itself stimulates labour supply and therefore allows for a higher level of employment.

7 IN THE SHORT RUN, MACRO-ECONOMIC POLICY MUST CREATE THE DEMAND FOR LABOUR

It is a simple, but important point, that *in the short run* labour market policy cannot itself create new jobs. If the demand for goods and services falls, a reduction in employment will follow, notwithstanding the efforts made within the realm of labour market policy. If on the other hand, sufficient demand is there, labour market policy can support the derived need for labour by stimulating effective labour supply. Furthermore, as already mentioned above, a well-designed labour market policy can in the medium and long term improve the capacity of the economy by improving the skills of the workforce and its allocation between occupations and sectors.

When it comes to means for supporting labour demand through macro-economic policy, the most effective manner to support job creation in the short run is through public investments. Firstly relative labour intensive production processes characterize the construction sector. Therefore the employment created per billion Euros invested is higher than in other sectors.

Secondly, public investments are superior to tax cuts, because the latter only becomes effective if they lead to higher private consumption, which is less likely in times of crisis, where consumers are reluctant to increase consumption at the expense of bolstering their savings. Public investments are also superior to public consumption and more public employment, which may be hard to redress, when the business cycle changes again.

Finally, the need for public investments can be argued not only based on the positive effects on employment, but of course also due to the beneficial effects of the investment projects themselves. Thus improvements in public building, roads, railways, sewer systems should of course be justified by the underinvestment in recent decades and by their general positive impacts on energy use, the environment and the quality of life of the citizens.

As a supplement to public investments one can argue the need for investments in private housing, which in many respects has the same beneficial effects on employment as public investment. The support to the housing sector can be argued on the basis of energy savings and a general need to increase the quality of, for instance, social housing.

Finally, one should also emphasize the longer-term benefits from immaterial public investment in R&D and education linked to support for structural change.

8 POLICY INTEGRATION IS OF UTMOST IMPORTANCE – ALSO IN TIMES OF CRISIS

An important lesson from the discourse on 'flexicurity policies', which entered the European political scene in recent years, is the importance of considering the employment policy not just as a collection of individual policy instruments. On the contrary, the secret to success is to support positive interactions in the form of virtuous circles between different policy elements, which can result in a win-win situation for all actors on the labour market.

For example, the achievements of the Danish 'model of flexicurity' cannot be attributed to its single elements, but to the successful interplay between the unemployment insurance system, active labour market policy and a labour market with a relatively low level of job protection for ordinary workers. Thus policy integration and the search for win-win-solutions is the key strategic message from the flexicurity-exercise.

Job-rotation is a characteristic example of a flexicurity policy that is geared to fulfil several goals at the same time by combining training of the workforce with integration of the unemployed into employment. Figure 2 illustrates the traditional approach to active programmes for the unemployed.

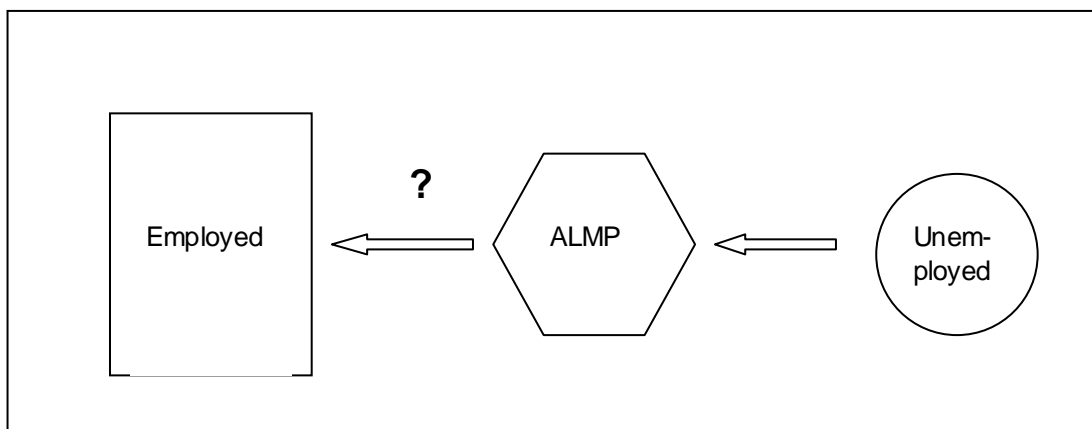


Figure 2: Traditional approach to integration of unemployed through ALMP

Here the unemployed are offered participation in various training activities with the ambition that they will improve their chances of re-employment. As is well known from a number of evaluations, the results from such reintegration programs are not always impressive, albeit of course depending on the target groups, the resources spent on the programmes and the overall situation on the labour market (Card et al, 2009, Martin & Grubb, 2001). One reason for the disappointing results could be that – in times of sagging labour demand - it is difficult to target the programmes with respect to the demand side.

The alternative approach of job-rotation, which gained some prominence during the 1990s, is shown in figure 3 (Compston & Madsen, 2001). The basic idea behind this integrative line of attack is to combine training-leave for employed persons with the creation of job openings for unemployed individuals that take their place as substitutions during the training period – perhaps after having themselves received some kind of specific training for the jobs that they enter as substitutes (as indicated by the question mark in figure 2). Compared to the traditional approach, job rotation schemes have a number of advantages:

It allows for targeted training activities for both employed and unemployed persons, because the job functions of the participants are known. Job rotation creates job openings for unemployed and allows them to overcome 'statistical discrimination' and get on-the-job training. The integrative schemes support innovation and structural change, while keeping employment high.

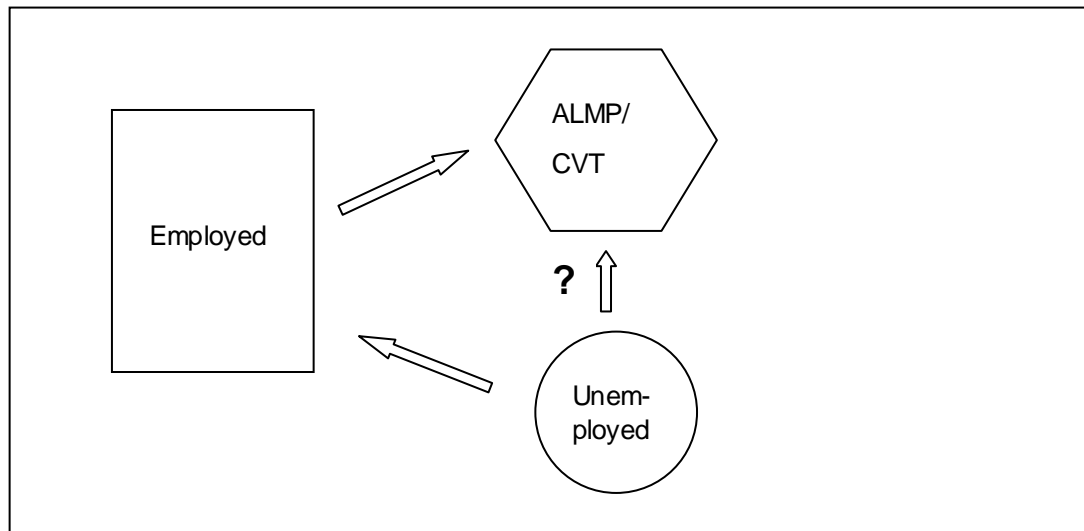


Figure 3 The integrative approach of job rotation

Furthermore, while job rotation is often applied in relation to training of the employed workforce, it can also imply that the employed persons get leave for other purposes such as a child-minding or sabbaticals. The Danish Paid Leave Arrangements, which gained some prominence during the 1990s, contained a number of such options.

In addition to the topic of job rotation, a number of flexicurity policies that are relevant in a recession has been pulled forward (Wilthagen, 2009). A number of examples are shown in table 1, which is structured in the format of the well-known Wilthagen-matrix. Thus creating and strengthening institutions that support transitions on the labour market and virtuous circles in the form of institutional complementarities is as important in times of crisis as during times of economic growth (Schmid, 2008).

Table 1: Examples of flexicurity-policies in times of crisis

	Job security	Employment security	Income security	Combination security (care and work)
Numerical flexibility (hiring and firing)	Temporary placement in other firms	Worker pools	Use of benefits as wage subsidy or educational support	Mortgage support
Working-time flexibility	Shorter working hours, work-time accounts	Joint employer ship	Part-time UB, Reduced working hours	Leave schemes
Functional flexibility (between job functions)	Job rotation	Internships in other firms, retraining	Retraining for new job	Accreditation of prior learning
Wage flexibility (variable pay)	Adjustment of wages	Supplement wage in new job	Extra UB as compensation	Increased family allowance

Source: Adapted from presentation by Ton Wilthagen at the conference on 'Implementing flexicurity in times of crisis', Prague, March 25, 2009.

9 FOCUS ON THE UPGRADING OF SKILLS

Both at the individual and at the societal level, the beneficial effects of higher skill levels are well documented. At the individual level, higher skills implies more employment over the life cycle, a lower risk of unemployment, higher pay and better job quality. For the same reasons, at the societal level, increased skills levels leads to a larger effective labour supply. From a longer term perspective, supporting both formal and informal skills formation is therefore an important element in employment policy.

An economic crisis implies both a threat and an opportunity for upgrading the skills of the workforce.

It is a *threat* for several reasons:

- If the workers that are dismissed during the crisis end up in long-term unemployment their existing skills may erode (along with one of the standard arguments of hysteresis).
- During the crisis a lack of economic resources in the firms may cause them to reduce the training activities offered to their staff.
- For vocational educations based on apprenticeship-systems or having a strong element of traineeships, the crisis will make firms more reluctant to take in apprentices. The outcome will be a lack of qualified workers, when the upturn comes.

On the other hand, the crisis can also be seen as an *opportunity* to further upgrade the skills of the workforce:

- In contrast to boom periods, there is actually idle capacity for training and education among the currently employed.
- The rising number of unemployed is an obvious target group for training and education.
- The traditional argument that training of the unemployed implies a risk of 'locking-in' effects carries less weight in times of a high overall level of unemployment.

Finally, one should stress that the faster speed of reconstruction, which follows from the crisis, will accentuate the *need* for retraining the workforce towards the new growth sectors. The issue is therefore not only to upgrade the skills level in general, but also to alter the skills in order to fit with the new composition of labour demand.

For these reasons, a more skills oriented profile of employment policy and active labour market policy is well founded during the economic crisis. Also for the reasons discussed above an integrative approach should be applied, which for instance – as exemplified by the concept of job-rotation – combines efforts directed at the employed and the unemployed.

10 IMPLEMENTATION STRUCTURES ARE IMPORTANT

Discussions about employment policies in times of crisis are most often cast in terms of giving priority to different instruments or designing innovative programmes for specific target groups. However, and as a final remark, it should also be stressed that the crisis puts a heavy strain on the political and administrative structures and actors involved in designing and implementing employment and labour market policy. A simple reason is that the number of unemployed that has to be handled by the systems increases. Furthermore the political demand on the system to deliver results increases. Considerations concerning improving both the policy networks involved in designing employment policy and the administrative systems made responsible for its implementation, should therefore be included in the discussions about successful labour market approaches for dealing with the crisis.

In brief, the key considerations should be:

- To include the perspective of policy integration and thus look beyond the traditional boundaries of for instance labour market policy, educational policy and environmental policy.
- To include a number of relevant factors including the social partners in the design of the responses to the crisis also at the local level in order to improve policy design and support a broad ownership to the policies, when they are implemented.
- To insist on some broad common guidelines for employment policy, but also to allow for a flexible adaptation to the local needs and conditions.
- To be willing to spend the necessary economic resources also on the administration and implementation of policies.

11 CONCLUDING REMARKS

No nation-state and no single economy are able to solve the economic crises and the employment problem on their own. Therefore we need joint European action, which supports protected mobility and job-creation through a well-designed macro-economic policy. In this perspective timing is important. If you do not act now there is a risk to lose thousands of jobs. In this context it could be advisable to look into the basic principles of the "Nordic Approach to Growth and Welfare" (Magnusson et.al. 2008) and to use those experiences in the Nordic countries that speak of interrelationships between labour market policy, general economic policy and the role of social dialogue.

12 REFERENCES

Bradley, David H.; Stephens, John D. (2007): "Employment Performance in OECD Countries. A Test of Neoliberal and Institutional Hypotheses", *Comparative Political Studies*, Vol. 40(12), pp. 1486-1510.

Bredgaard, T.; Larsen, F., Madsen, P.K. (2009): Flexicurity på dansk, CARMA Research Papers 2009:2.

Card, D.; Kluve, J.; Weber, A. (2009): "Active Labor Market Policy Evaluations: A Meta-Analysis", *IZA Discussion Papers* No. 4002.

Compston, H.; Madsen, P.K. (2001): "Conceptual innovation and public policy: unemployment and paid leave schemes in Denmark", *Journal of European Social Policy*, Vol. 11(2), pp. 117-132

Magnusson, L. et.al (2008): *The Nordic Approach to Growth and Welfare: European Lessons to be Learned?* ETUI, Brussels

Martin, J. P.; Grubb, M. (2001): "What Works and for Whom: A Review of OECD Countries' Experiences with Active Labour Market Policies", *Swedish Economic Policy Review*, Vol. 8(2), pp. 9-56.

Schmid, G. (2008): *Full Employment in Europe. Managing Labour Market Transitions and Risks*, Cheltenham: Edward Elgar