

Boeri & Garibaldi: Beyond Eurosclerosis

Discussion and Comments



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- **Summary of the main findings according to the labour market view**
- **What would a macro-economic view tell us?**
- **Some methodologies twists**
- **Policy conclusions**



- **The paper provides an original analysis of the impact of labour market institutions on European unemployment flows and spells.**
- **However, the policy conclusions lack more concrete backing in the data. In particular, the call for better remuneration for increased labour market risk is likely to undermine the success of the current reforms.**



The labour market view of European unemployment dynamics...

- **The paper argues for an end of Eurosclerosis:**
 - Unemployment rates have come down substantially over the 1990s
 - Unemployment declined most in those countries with highest initial levels (unemployment convergence)
 - Regional variation of unemployment rates declined as well
- **An analysis of unemployment flows rather than stocks**
- **The paper analyses typical labour market institutions:**
 - The success in bringing unemployment down was mainly the result of new policy design
 - Reduction in employment protection regulation
 - Reforms of unemployment benefit systems: duration of benefits, replacement rates, degressive design of benefits



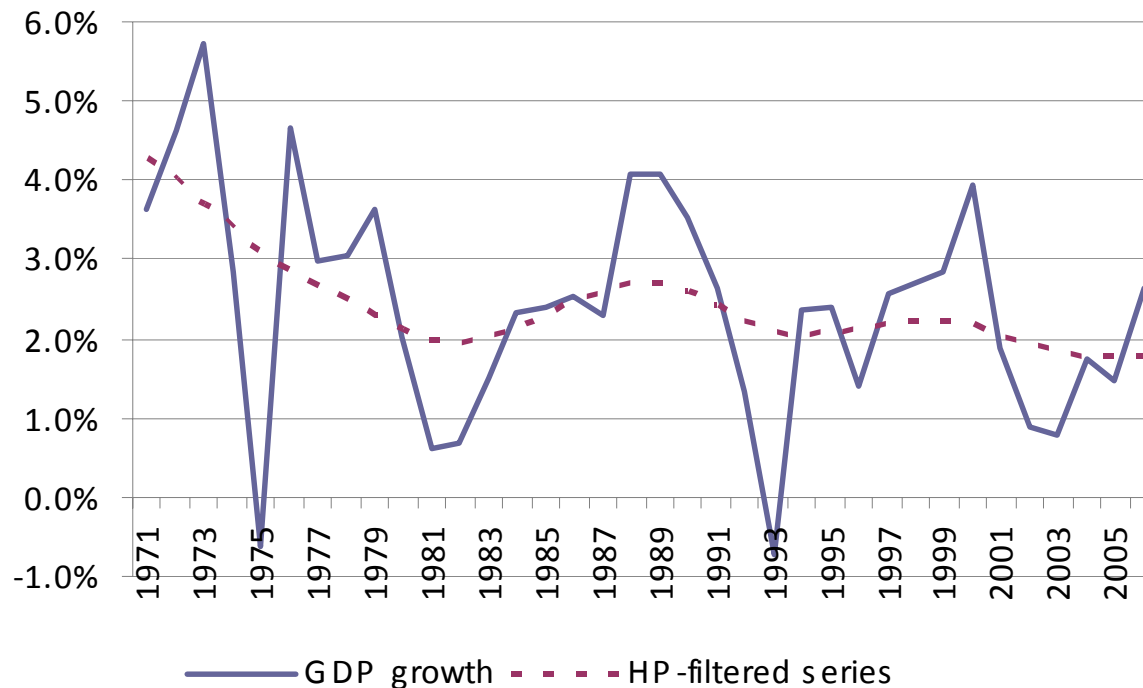
...stresses the importance of institutional factors.

- **Alternative explanations for the change in unemployment:**
 - Labour migration: large inflows of migrants in certain countries
 - If anything, this would have increased unemployment rates, although it may have decreased structural unemployment rates
- **Ageing societies:**
 - Unemployment rates are typically higher for younger than for older workers
 - With a compositional shift due to population ageing this could have brought down average unemployment rates
- **Policy factors dominate these alternative explanations:**
 - Large drop in employment protection regulation in the second half of the 1990s
 - Trend decline in an unemployment benefit index, mainly due to increased conditionality of benefits
 - Constant rise in unemployment turnover and job mobility that cannot be explained by these alternative hypotheses



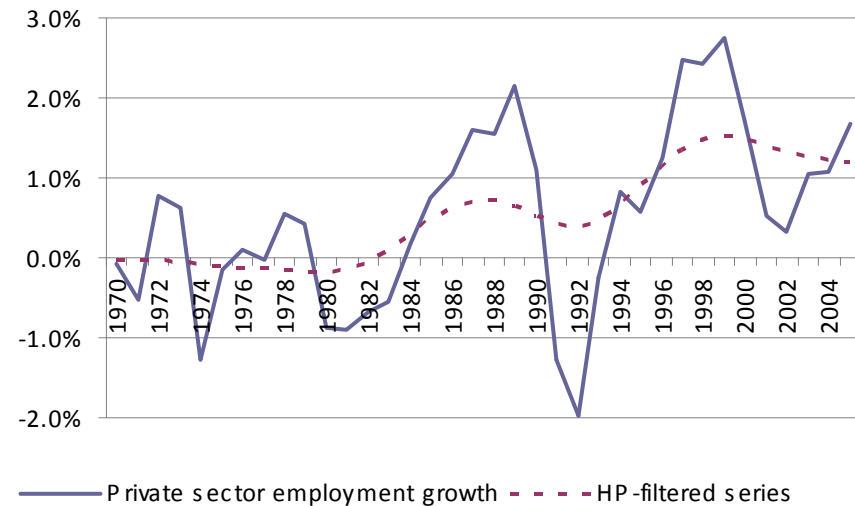
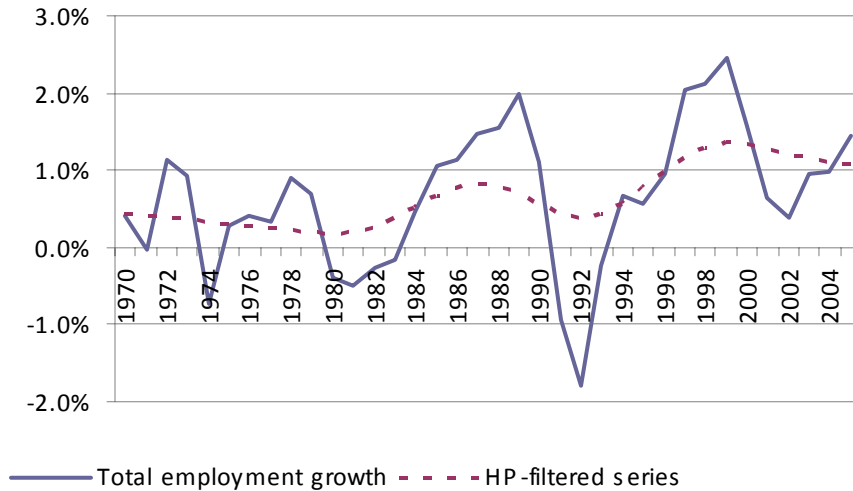
The macroeconomic view on unemployment....

- The European unemployment story can also be told from a macro-economic point of view
- Growth has been stable (from trough-to-trough) between the 1980s and the 1990s in the euro area (EU-12)
 - 1981-1993: 2.4% p.a.
 - 1993-2002: 2.3% p.a.



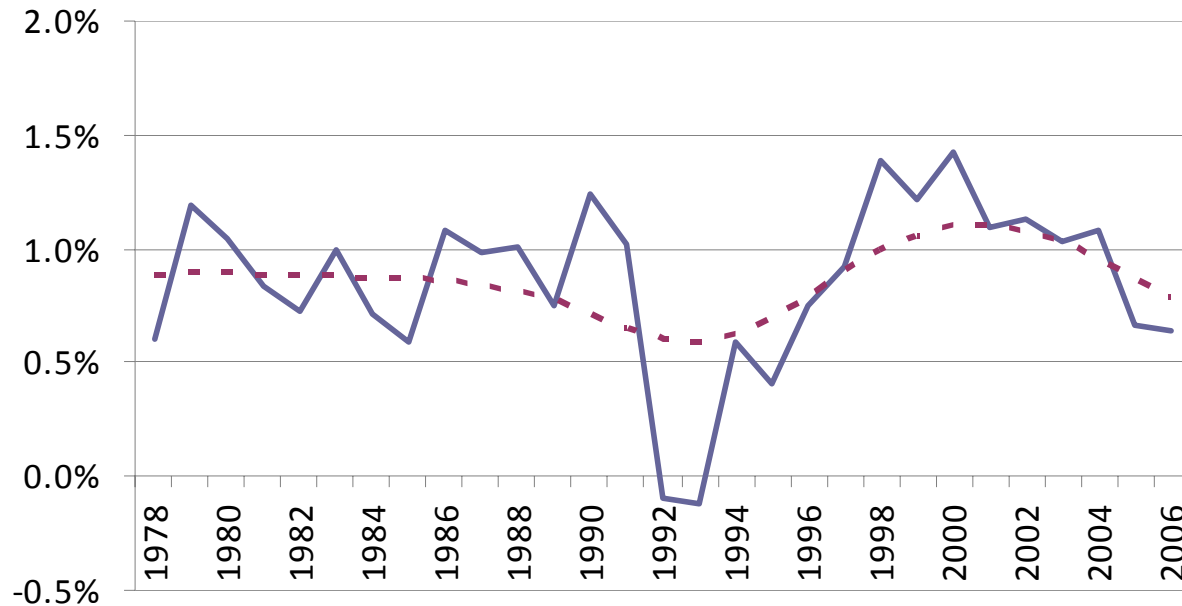
...confirms the dynamics of private sector employment growth....

- Employment growth has accelerated over that same period, mainly thanks to private sector job creation



...which was mainly driven by demand not supply....

- Labour force growth cannot account for this acceleration as it has been stable throughout

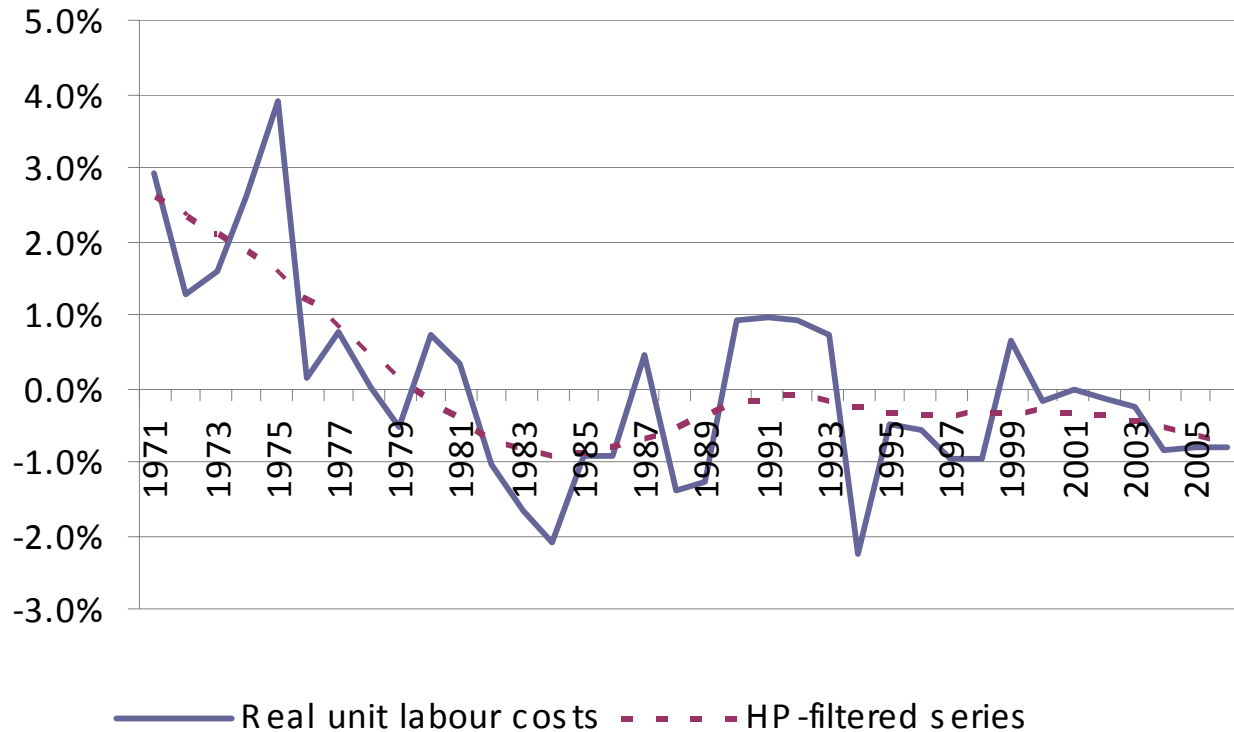


— Labour force growth - - - HP-filtered series



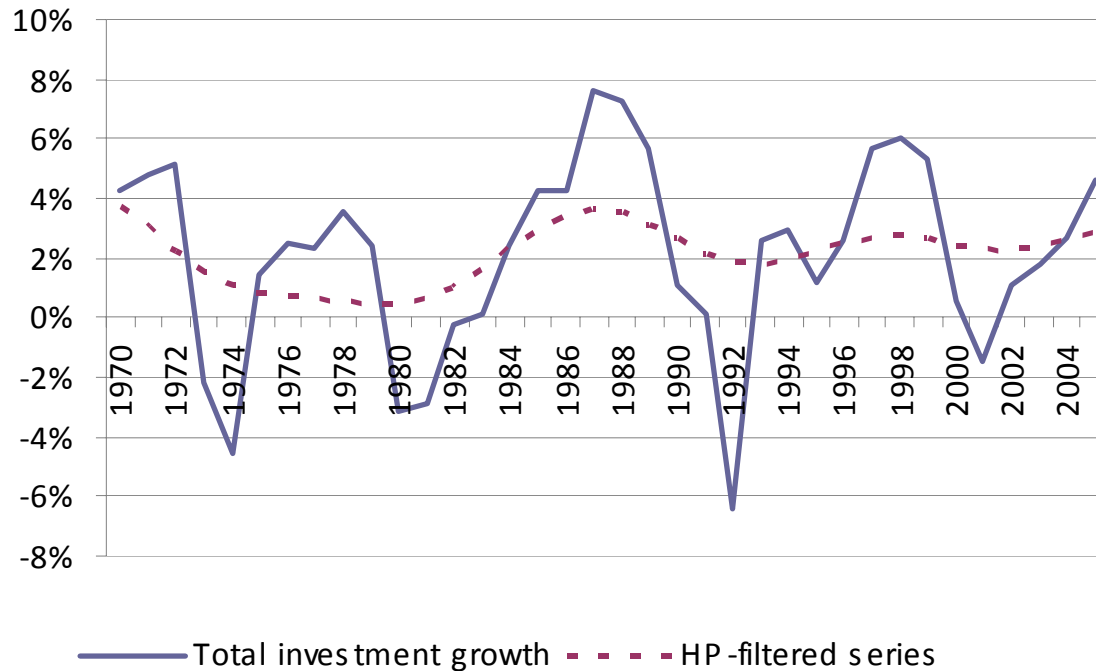
...and can be attributed to a fall in real wages and the labour share....

- Real unit labour costs have declined constantly over the 1990s
- A similar picture arises for the labour share



...but aggregate demand and investment dynamics are also important...

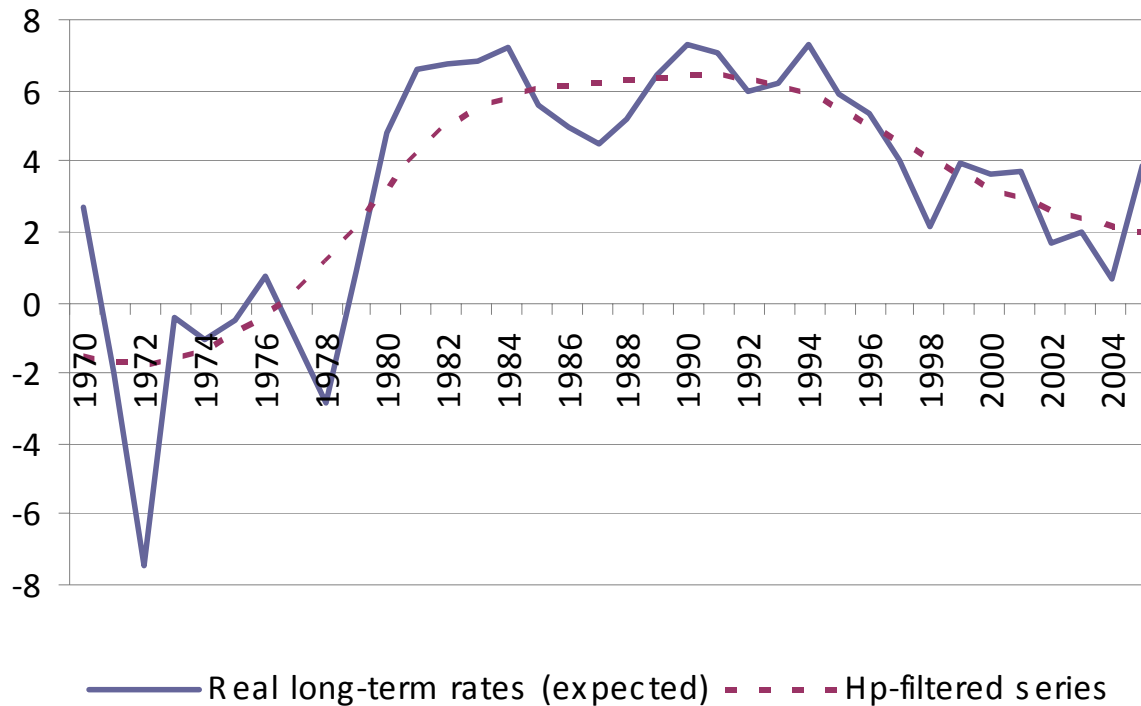
- Investment growth has accelerated over the same period:
 - 1981-1993: 2.2% p.a.
 - 1993-2002: 2.8% p.a.



...mainly due to improved monetary and financial conditions.

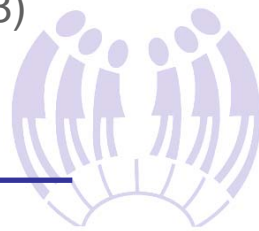
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Lessons from the macroeconomic view

- **The unemployment benefit story is mainly relevant for wages, less for labour supply**
 - Lower unemployment benefits have lowered the fall-back option for wage earners
 - Reduces wage demand during negotiations
 - Has led to improvements in RULC
 - Labour supply has barely moved, even though effective labour supply may have increased due to higher unemployment turnover
- **Preparation for EMU and the global savings glut have produced benign financial conditions**
 - Convergence of risk premia has led to a strong reduction of interest rates
 - Long-term rates have especially benefited from the benign global environment at the end of the 1990s and the early 2000s.
- **The role of the real interest rate has stressed by others in the literature**
 - Ball (1999), Gianella et al. (2008), Stockhammer and Sturn (2008)

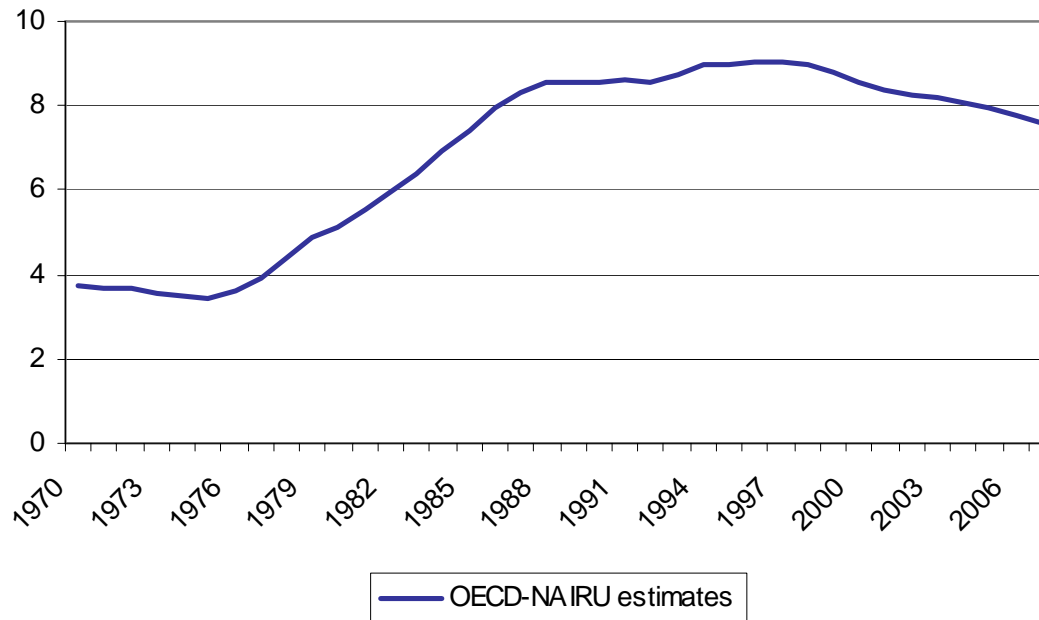


- **Unemployment persistence (hysteresis):**
 - Mobility scores
 - Unemployment turnover
 - Job-to-job shifts
- **Alternatives**
 - Univariate measures of persistence (similar to inflation persistence)
 - How do these individual mobility indices affect persistence in the level of unemployment?
- **Does this tell us anything about the factors influencing the level of unemployment?**
 - Possible, but:
 - Different variations of the unemployment rate are consistent with the same level of unemployment (Nickell, 1978): Shifts in the Beveridge-curve are relevant not movements along the curve.
 - Gross figures constructed out of net data (similar to Shimer, 2005)
 - No analysis of hysteresis in the paper



Methodological issues - II

- **How does labour mobility related to structural unemployment?**
 - Is labour mobility enough to measure changes in the level of unemployment?
 - The structural unemployment rate has started to fall only in the early 2000s
 - Wrong timing? The decline in the NAIRU took place after the rise in employment and mobility dynamics in the late 1990s (lags?)



- **The paper argues that now is the time for improvements in working conditions:**
 - Two-pillar approach: Deregulate first, clean-up the mess later
 - In Europe: Make labour markets flexible by introducing temporary labour contracts, but leave the core labour workforce untouched
 - Nevertheless, sentiment of insecurity has increased across the board, with likely consequences for human capital formation and effort.
 - Paper suggests to higher remuneration through increase in productivity growth and more generous unemployment benefits (by keeping the conditionality)
- **Is such a strategy viable?**
 - Employment gains have been partly achieved by improvements in real unit labour costs: stronger remuneration (especially higher unemployment benefits) would forgo these gains
 - The negative link (in Europe) between higher labour market turnover and lower productivity growth is not fortuitous. Moving towards a US-style innovation system is likely to take time and requires large-scale changes in the university, research and financing landscape.
 - Be aware of policy complementarities: Different institutional combinations lead to similar employment effects (see e.g. recent WoW report 2008)



- **The analysis of European unemployment dynamics requires both the macro- and the labour market view:**
 - Aggregate demand dynamics and financing conditions are responsible for an acceleration in investment over the 1990s
 - This complements the improvement on labour markets and has helped bringing unemployment rates down
 - Hysteresis effects imply that changes in aggregate demand may produce medium-term variations in (structural) unemployment
 - These effects should be analysed more carefully in the paper to derive broader policy conclusions
 - More importantly, shifts in the institutional environment will require shift in aggregate demand management

