

Box 8

LABOUR MARKET MOBILITY AND TRANSITIONS IN LABOUR MARKET STATUS IN THE EURO AREA

One important goal of the Europe 2020 – which is aimed at achieving inclusive growth and strengthening employment – and Lisbon Agenda (2000-2010) strategies is to increase labour market flexibility, including the ease with which individuals can move from inactivity and unemployment into employment. Over the 2000-2009 period, there was an overall increase in labour market participation rates in the euro area of about 4 percentage points, essentially driven by the addition of those individuals recognised as being “marginally attached” to the labour market, such as women and young people. At the same time, the unemployment rate declined over most of this period, suggesting some positive progress in the performance of euro area labour markets.

This box presents information on alternative measures of labour market “flexibility” in euro area countries for the period from 1998 to 2008, based on Eurostat’s Labour Force Survey microdata.^{1,2} To illustrate the ease of transition among the labour market states of employment, unemployment and inactivity, measures of the probability of moving from or remaining in a particular labour market state over any two-year period are constructed, as is an overall summary index of mobility (see Shorrocks, 1978).³

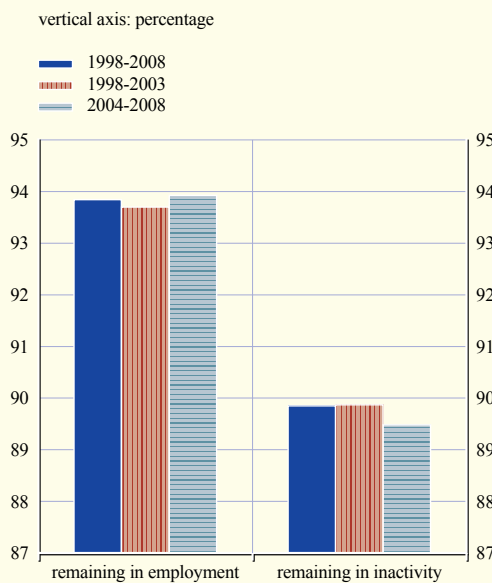
The results denote a high probability of remaining in the same labour market status over a two-year period, with average probabilities of remaining in employment and inactivity of 94% and 90% respectively (see Chart A). The probability of remaining in unemployment between one year and the next is around 61% over the whole sample period from 1998 to 2008. It decreased by around 5 percentage points between the 1998-2003 and 2004-2008 periods, from 62% to 57% (see Chart B), indicating an improvement in labour market flexibility

1 It focuses on the 15 countries belonging to the euro area in 2008 for which there is comparable information over time. Germany, Ireland and Malta are excluded (as data are missing for these countries), as are Spain and the Netherlands (as the information for these countries is only available for more recent waves of data).

2 Individuals’ labour market states are based on the subjective assessment of the respondent’s current and past working status.

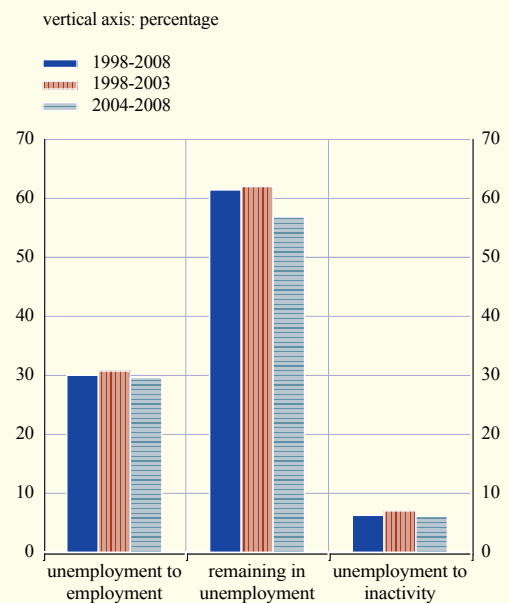
3 The Shorrocks index is a summary measure of labour market mobility. It captures the probability of moving across the three labour market states (employment, unemployment and inactivity) between the current and previous period. The index is bounded between zero and one, where a value of zero implies a zero probability of leaving any labour market state (i.e. no mobility) and a value of one implies full mobility. For more details, see Shorrocks, A.F., “The measurement of mobility”, *Econometrica*, Vol. 46, 1978, pp. 1013-1024.

Chart A Probability of remaining in employment and inactivity over a two-year period



Sources: LFS microdata and ECB calculations.
 Note: The charts exclude Germany, Ireland, Spain, Malta and the Netherlands. Observations are weighted averages according to the labour force share in each country over the euro area aggregate.

Chart B Probability of transitioning from unemployment to another labour market status over a two-year period



Sources: LFS microdata and ECB calculations.
 Note: The charts exclude Germany, Ireland, Spain, Malta and the Netherlands. Observations are weighted averages according to the labour force share in each country over the euro area aggregate. The bars for those moving from unemployment to inactivity exclude France.

over that time. Yet the probability of an individual remaining in unemployment over a two-year period is still particularly high, compared with the probability of transitioning from employment or inactivity into unemployment (20 times higher). This suggests that the number of people in unemployment is high, relative to the number moving into unemployment every year, with the result that, on average, European individuals tend to remain unemployed for a relatively long time.⁴

Despite the decrease in the probability of remaining unemployed over a two-year period, other labour market transitions have remained roughly constant over the last decade. For example, the transition from unemployment to employment remained at 30%, while the transition from unemployment to inactivity remained at about 6% (see Chart B). Considered together, these results suggest that euro area countries need to do more in their labour market reform efforts, for example through reforms to facilitate the transition from unemployment into work and from inactivity into employment, as well as to reduce flows out of the labour market.

The degree of labour market mobility according to the Shorrocks index (a summary measure of mobility, as defined in footnote 3) varies across euro area countries and groups of workers, indicating that there has been an increase in labour market “flexibility” over the last ten years in a number of countries. Labour markets in Spain, France, Luxembourg and the Netherlands seem to be more flexible on average, displaying mobility indices which are twice as high as those of

⁴ By comparison, an employed person is only around three times as likely as an unemployed person and 13 times as likely as an inactive person to remain employed in the following year.

Belgium, Greece, Italy and Slovenia (see Chart C). Moreover, Chart D shows that, on average over the whole period, labour market mobility is particularly high for people between the ages of 25 and 29, and for those who are highly educated.⁵

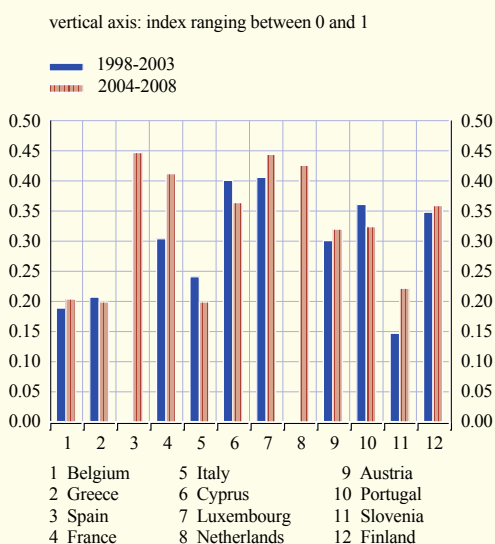
The countries with high mobility are also those with a higher percentage of temporary contracts and part-time work, as well as those with less stringent employment protection legislation. Although there is no clear correspondence between the unemployment rate and mobility, there are no countries with both low mobility and low unemployment rates, suggesting that a certain level of mobility is a necessary – albeit insufficient – condition for low unemployment.

Summing up, the results of this analysis suggest that the observed increase in mobility across labour market statuses is expected, all other things being equal, to (i) increase the efficiency of matching skills with job vacancies by speeding up the pace at which workers can find new jobs, (ii) under the same reasoning, reduce the cost to governments of long-term unemployment and (iii) increase labour market participation, which contributes to the potential output of the euro area over the longer term. Although the persistence of unemployment has fallen, it remains high, highlighting the need for labour market reforms aimed at increasing flexibility in euro area labour markets.

5 Moreover, breaking down this result by sub-period (not reported here) highlights the fact that mobility has generally increased for females, explaining why there are no significant differences in the mobility index by gender on a full-period average.

Chart C Labour market mobility index over time

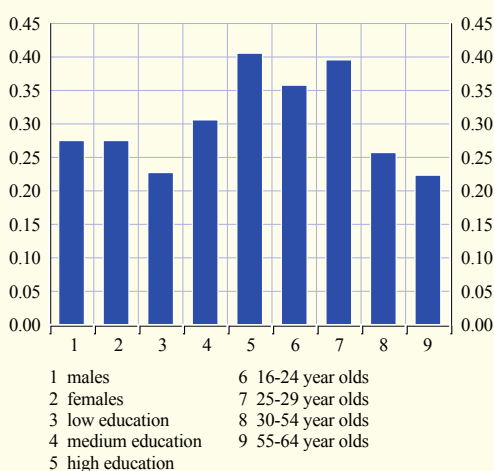
(1998-2003 compared with 2004-2008)



Sources: LFS microdata and ECB calculations.
Note: Measures based on the Shorrocks mobility index (see footnote 3).

Chart D Labour market mobility index by population group

(1998-2008 average)



Sources: LFS microdata and ECB calculations.
Note: Measures based on the Shorrocks mobility index (excluding Germany, Ireland, Spain, Malta and the Netherlands), as defined in footnote 3. The results are a weighted average of country results. Observations are weighted according to the proportion of each sub-category in the respective countries (i.e. males, females, highly educated, etc.) of the euro area as a whole.