Regulatory and Labor Market Policy Reforms: What is Feasible?


Some issues for discussion

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Four points

- But before two caveats:
  - Difficult to generalize about LM policy and institutions given the huge heterogeneity and interactions
  - (Teal) the creation of more and better jobs depends on many factors outside the labor market

1. Micro data suggest large dynamism in the LM, with many jobs created and destroyed and large workers’ mobility
2. The LM regulatory framework: (beyond fundamental workers’ rights) de jure regulations tend to be relatively strict, but seldom enforced
3. The LM policy framework: income and other forms of support for the unemployed are limited
4. We should understand the political economy of the status quo and of reforms
Market economies require continuous reallocation of labor

- Enterprise data suggest sizeable job flows (20 OECD – 30 LAC, ECA)
- Because of sizeable entry and exit of firms (15-20%) involving 8-10% of employment (Foster et al. 2002; Bartelsman et al. 2004)
- Because of continuous process of adaptation of existing businesses to changes in market conditions and dev. In processes and products.
- Reallocation important for productivity growth, but under conditions: painful to workers and ineffective if regulations in different market distort flows.
All countries experience large job creation and job destruction

Manufacturing, annual job flows, 1988-2000

- JC by new firms
- JD by exit of firms
- JC by existing firms
- JD by existing firms
Labor reallocation is important for productivity growth

(contribution of entry and exit to labor productivity)

Larger mobility in developing countries

- Larger proportion of small firms and unskilled labor-intensive activities.
- Larger and frequent macroeconomic shocks
- But also because sizeable informal sector, where jobs tend to be more unstable
- Bottom line: we should look at dynamics in the labor market from both the firm perspective (job flows) and workers’ perspective (workers’ mobility using longitudinal H surveys)
Persistence in the different labor market sectors: informal more precarious

The probability of entering into unemployment is higher for informal than for formal workers

Protecting jobs, high *de jure* protection – but low *de facto* protection

- We now have synthetic indicators of *de jure* labor regulations for many countries (working time, hiring and firing, etc.)
  - They suggest that low income countries tend to regulate the LM more than middle income and industrial countries
- But surveys to firms often suggest that employers do not consider LM regulations as the most important constraints
  - Why: low enforcement even among formal firms
  - But if we go a step ahead and try to understand for which firms LM are a problem we discover that are not the very small nor the very big but generally medium-sized firms, innovative firms
- The question is: Are LM regulations -- that are strict on paper but seldom enforced -- an issue that is worth addressing, also given the high political capital involved in any labor reforms?
- The answer could be yes, to the extent these regulations discourage firm expansion, investment in technology and ultimately the creation of more and better jobs
Protecting jobs, high *de jure* protection – but low *de facto* protection

**Level of employment protection by region**

- **Industrial Countries Common Law**
- **Middle East and North Africa**
- **Sub-Saharan Africa**
- **East Asia and Pacific**
- **Industrial Countries Others**
- **Latin America and Caribbean**
- **South Asia**
- **Europe and Central Asia**

*Summary indicator of the stringency of Employment Protection Legislation (EPL)*

- Regular EPL
- Temporary EPL

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Protecting workers: limited support largely relying on severance pay

- We cannot look at LM regulations in isolation: we have to consider also the other pillar of LM intervention: active and passive LM policies.
- Income support for the unemployed – limited and available only to formal sector workers:
  - Relies in general on severance pay – do not pool unemployment risk; unreliable as they depend on the financial conditions of the firms.
- Active labor market programs:
  - training and retraining open to the unemployed (generally not the most vulnerable groups)
  - Limited experience on job counselling.
  - Limited experience on programs that target disadvantaged groups in the rural or informal sector. Some interesting experience of workfare programs.
Protecting workers: limited support largely relying on severance pay
Shifting protection from jobs to workers: is it feasible?

- Status quo of high *de jure* protection of jobs and little support to the unemployed
  - Does not necessarily reduce flows in the labor market but distort them, with negative effects on allocation of resources
  - Greater dualism (formal/informal, small/large firms, skilled/un-skilled)
- Fragmented and ineffective labor market policies
  - Large informal sector implies many workers not protected by EPL
  - Even for formal sector workers have to rely on severance pay which are often not available (e.g. when firms are in financial troubles)
- **What is feasible:**
  - Weak administrative capacity and limited resources → EPL may be the only way (e.g. Blanchard, 2002 EPL as proto-insurance)
  - In countries with some administrative capacity, shifts from EPL to income support (individual savings accounts)
  - But the issue remains of how to protect informal workers. U assistance and/or workfare programs?
We need more empirical evidence to guide policy

- Cross-country time series analyzes:
  - Several studies for OECD countries, less for developing countries
  - Measurement issues and omitted variable problems coupled with limited time series

- Difference-in-difference cross country sectoral studies:
  - Available data for growing # of countries (e.g. Micco, Pages, 2005; Haltiwanger, Scarpetta Schweiger, 2006)

- Micro/sectoral country studies
  - Exploit episodes of reforms (Kugler, 1999; Hopenhayn, 2004; Saavedra, 2003)
  - Exploit cross sectoral (e.g. Terrell, 2004) or cross-state variations (e.g. Besley & Burgess, 2004 Lemos, 2005, Almeida, Carneiro, 2006)
  - More micro data available (firm-level individual-level) allow to look at job creation/destruction, labor mobility
  - More panel data (Fields)