

Economic crisis, welfare-labour market settings and unemployment in Europe

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With Economic crisis, welfare-labour market assets and unemployment in Europe¹ we cover a first step of a general project which aims at analysing, from a macro-micro perspective, the effects of different policies/strategies of LM adjustments on unemployment (levels, composition, stickiness) across EU countries/LMs.

The specific goal of this work is to shed light on determinants of heterogeneous effectiveness of national LM settings in responding to the recent (and partly ongoing) economic downturn. Indeed, we argue that the economic crisis provides an interesting example of a protracted exogenous shock, common among different European countries and whose consequences in terms of overall employment trends have been filtered (and smoothed) to different extents by structural, regulatory and institutional features characterizing distinct national labour markets.

In this work we look at the evolution of workforce's exposure to (long unemployment) risks during the 2009-2011 downturn in 15 European countries, namely DK, FI, NO, SE (clustered as "Northern Countries"), AT, BE, FR, DE, NL (clustered as "Continental Countries"), GR, IT, PT, ES (clustered as "Southern Countries") UK, IE (clustered as "Liberal Countries").

We start by showing descriptively the (somehow tentative) national policy responses undertaken during the economic crisis, both in terms of adjustment levers (wage adjustment, external flexibility, internal flexibility) and in terms of policy tools (EPL(epl-gap) settings, PLMP expenditure, ALMP investment). With respect to wage adjustment, we document a weak response capacity of European LMs, with a decreasing Phillips curve relationship between changes in compensation per employee and unemployment changes at the country-level during economic downturn. With respect to policy response on the regulatory aspects, we show, once again, an overall stability in EPL of both permanent and temporary workers.

A somehow differentiated strategy to cope with increasing unemployment has instead been documented with respect to the trend of national expenditures in PLMP and ALMP, with an increased weight of passive measures in Southern and Liberal clusters and a moderate increase of ALMP in Continental and Northern LMs. Moreover, we document how 2008-2011 economic downturn led to a further raise of temporary employment shares in European national LMs, mirroring both a "first out first in" employment dynamic over the economic downturn time span and the presence of a progressive substitution of temporary workers for permanent ones. Last but not least, we look at the "effect" of economic downturn changing the workforce exposure to part time schemes, documenting a moderate increase of these contractual arrangements especially in Northern and Continental countries.

Goal of the empirical contribution provided in this first step of the research is to test, from a macro level standpoint, the impact on overall unemployment of two alternative strategies of internal vs external flexibility. More specifically, in this paper we analyse and disentangle the role played by main LM relevant regulatory and institutional elements such as the amount of investment in active/passive labour market policies and the implementation of alternative forms of flexibility or, say, models of social investment welfare state.

We argue indeed that different combinations of these aspects had a relevant role in shaping the occupational consequences of the economic downturn not only in terms of different occupational impact of the crisis across countries, but also in terms of distinct overall unemployment trends over

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time and in terms of unemployment risks among distinct social groups. Therefore, in the empirical analysis we pay particular attention to the distribution and the timing of negative effects on employment chances of workers / job-seekers in European Labour markets looking both at the micro and at the macro level.

The specific focus of the analysis concerns with the distributional effects of the recent economic downturn and on the role played by different LM assets in shaping workforce unemployment risks. We address this research question by looking at three different aspects.

1) Distributional effects: we ask whether and to what extent distributional effects of increased unemployment risks due to negative economic conjuncture differed across national LM, determining increasing polarization and weaker occupational prospects for those hardest hit, young and less qualified workforce.

2) Effectiveness of LMP as remedial policies: we ask whether and to what extent ALMP represented an effective tool in order to reduce workforce risks of experiencing long(unemployment) during the 2009-2011 crisis.

3) Adjustment capacity/workforce protection of internal and external flexibility: we compare national LM occupational response to the economic crisis given heterogeneous exposure of the workforce to part time or temporary employment arrangements.

We tackle these questions by drawing on a self-constructed pseudo panel dataset based on European Labour Force Survey, thus covering a longer time span (between mid90s and 2011) and coping with the need for a unified, cross country and longitudinal dataset of European countries. As regard methods, different kind of estimators have been used, depending on the specific research question to be tackled. First of all, we present the results of dynamic RE specifications, with the inclusion of “y at t-1” aimed both to reduce the role of unobserved heterogeneity at the micro level and to check for the inertia in the outcome variable. Where instead the analysis is not meant to provide a description of employment determinants, but rather to approximate a causal interpretation of the dynamics of unemployment trends in response to the changing levels of “internal / external flexibility” or national ALMP expenditure, FE estimator has been preferred in order to relax common RE assumptions, to control for time invariant unobserved heterogeneity and to allow for a causal interpretation of detected effects. Where relevant, crucial macro –nation specific- variables have been included with a time lag in order to minimize reverse causality between policy implementation and occupational trends.

With respect to empirical findings, we start documenting an overall process of increasing variability in workforce’s exposure to unemployment and long unemployment risks. Despite this overall trend, we nevertheless detect diverging occupational chances among social groups, with a more pronounced and more polarizing impact of negative economic downturn applying to Liberal and Southern countries.

Coming to multivariate results and to “causal” consequences of 2009-2011 economic downturn, on a macro level significant differences arise between the four clusters of countries. The effects on overall unemployment appear indeed to be moderate in Continental and Northern countries, with major concerns that apply to Southern and Liberal clusters, whose LMs experienced a more severe employment retrenchment. Moreover, regression results confirmed how micro level consequences in terms of polarization of unemployment risks follow the same pattern, with Southern and Liberal countries displaying the higher concentration of downturn effects on young and/or less qualified workforce.

The overall picture of results on possible policies aimed to reduce workforce exposure to unemployment indicates a minor but not negligible role played by LMP and national LM assets. ALMP confirmed to be an effective tool, while increasing internal flexibility levels resulted to represent in most countries the fairest possible compromise between the need for higher LM adjustment capacity and the protection of workforce from job losses.





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