



## **PREVENTING UNEMPLOYMENT AND UNDEREMPLOYMENT FROM BECOMING STRUCTURAL**

Report prepared for the G20 Labour and Employment Ministerial Meeting  
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## Executive Summary

### Key challenges

In many advanced economies and some emerging economies, the persistence of high levels of unemployment following the crisis, and the build-up of long-term unemployment in particular, have raised concerns around a possible rise in structural unemployment. In emerging economies, there are long-standing concerns about high levels of under-employment, with many workers trapped in low-paid, informal jobs which fail to develop and fully utilise their skills and capacities. Some groups, e.g. the youth and people from migrant backgrounds, are at particular risk. These trends have reinforced social disparities in income and access to productive and rewarding jobs which are causing much hardship for individuals and families and undermining the growth potential of G20 economies.

Underlying these trends has been the substantial transformation in the sources of job growth and the types of jobs that are being created as a result of increased globalisation, technological change, economic and social development, and demographic change in all G20 countries. These long-run forces have contributed to skills mismatch and skills shortages and will continue to put pressure on labour markets to be more adaptable but also on policies to provide more effective support to jobseekers to avoid a structural increase in unemployment and under-employment.

### Key policy messages

While the exact choice and combination of measures will depend on each country's specific institutions and circumstances, dealing with these challenges will require a mutually reinforcing approach that seeks to, first, **strengthen growth and encourage greater job creation**, and, second, **tackle structural barriers in the labour market** that are preventing individuals from finding productive and rewarding jobs that correspond well with their skills and capacities.

#### *In the short-run*

In order to tackle the negative impact of the crisis on employment and social outcomes, and prevent the large cyclical rise in unemployment from translating into higher structural unemployment, countries should consider:

- Boosting stronger aggregate demand and promoting the creation of quality jobs, including through greater investment in productive infrastructure where there is fiscal space and in measures to encourage the development of small and medium-sized enterprises.
- Avoiding unnecessary dismissals and stabilising employment by facilitating and encouraging firms' use of internal flexibility instruments.
- Providing adequate income support to the unemployed, but combined with effective re-employment services and strict mutual obligations.
- Maintaining, and where possible expanding, cost-effective active labour market measures.
- Enhancing and, where necessary, improving employment services effectiveness.
- Ensuring that the skills of the unemployed are developed, maintained and/or adapted to changing needs.

#### *In the long-run*

In the face of long-run economic and social transformations affecting all G20 economies, structural reforms will be required to make labour markets more adaptable, resilient and inclusive through improving access to rewarding and productive jobs and by providing the skills needed in these jobs. This requires action in several areas:

- Develop and/or extend social protection systems which both help and encourage people to find work in the formal sector.
- Particularly in emerging economies, develop an integrated strategy to facilitate the transition of informal enterprises and workers in informal jobs into the formal economy in both rural and urban areas.

- Ensure close coordination of public employment and benefit administration services, developing partnerships with the private sector and introducing greater performance management to increase effectiveness.
- Tackle in-work poverty through adequately-set minimum wages and the use of in-work benefits, while containing the non-wage costs of hiring for certain categories of workers.
- Design employment protection to facilitate labour market adjustment and mobility of workers towards better job opportunities while reducing labour market duality.
- Remove obstacles to geographical labour mobility within countries, and maximise the benefits of migration by helping migrants achieve better employment outcomes.
- Help individuals obtain and maintain the skills required by the labour market through better anticipation of emerging skill needs, the provision of accurate and up-to-date labour market information and greater responsiveness in the provision of education and training. A special focus should be devoted to young people with low skills for whom access to productive employment is difficult in all G20 countries.
- Strengthen and expand quality apprenticeship programmes and other work experience programmes.
- Promote entrepreneurship and self-employment to unlock new sources of job growth.
- Ensure a good coordination in the delivery of labour market and social services at the national and local levels, and strengthen social dialogue.

## Introduction<sup>1</sup>

1. The persistence of high levels of unemployment following the crisis in many advanced economies and in some emerging economies, as well as the build-up of long-term unemployment, have raised concerns around a possible rise in structural unemployment – *i.e.* the permanent or persistent component of unemployment that is invariant to the economic cycle. At the same time, many emerging economies have struggled with chronically high levels of underemployment, with many workers trapped in low-paid, informal jobs which fail to fully utilise their skills. These trends have resulted in significant social and economic costs. Besides the tremendous hardship it has caused to individuals and families, it presents a waste of scarce economic resources, including human capital, and reduces the long-run growth potential of economies.

2. This paper starts by setting out the key challenges faced by policy-makers in G20 countries both in the short-term as a result of the crisis and sluggish recovery in many G20 countries, and in the longer term as a result of ongoing economic, demographic and social transformations. The second part of the paper then sets out the policy responses that should be considered to address these challenges. While the choice and combination of measures will depend on each country's specific institutions and circumstances, a blend of short- and long-run measures is likely to be needed that simultaneously seek to strengthen growth and encourage job creation, while also tackling structural barriers in the labour market.

## The key challenges for policy

### *A sluggish recovery in advanced economies, with signs of rising structural unemployment*

3. **The global financial and economic crisis resulted in the destruction of millions of jobs across the globe**, as firms closed or downsized. Six years since the onset of the crisis, unemployment remains high in many G20 countries (Figure 1). The European Union (EU) as a whole has been worst affected with 10.8% of the labour force currently unemployed, still 3.8 percentage points higher than the pre-crisis level of 7.0%. There are large differences across the EU countries, but for a number of them as well as for the US this has been by far the weakest recovery of the past four decades.

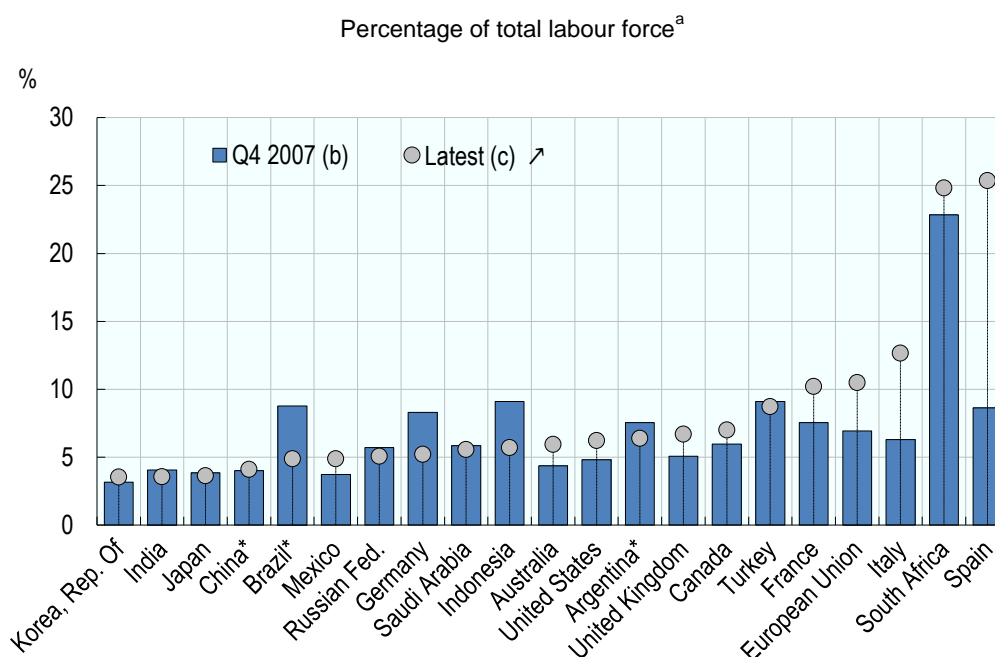
<sup>1</sup> This report has benefitted from comments by the ILO and the World Bank Group.

The persistence of high levels of unemployment not only represents considerable hardship and a waste of valuable human resources but is also of concern as it can lead to rising structural unemployment.

4. **But labour markets in some countries have been more resilient.** Unemployment is close to, or below, 5% in many of the emerging economies and also remained low (or even fell) in Australia and Germany. In some countries, however, unemployment affected 25% or more of the active population (South Africa and Spain) while it exceeded 10% in Italy and France. In addition, some groups of workers, many of whom already faced higher unemployment rates prior to the crisis, were more affected than others. The employment situation of youth and the low-skilled remains particularly depressed. These differences across countries and groups in labour market outcomes partly reflect differences in labour market and social policies and thus highlight the potential role these policies have to play in making labour markets more inclusive and resilient.<sup>2</sup>

5. **Long-term unemployment has risen and remains high in many countries** (Figure 2). This increase has been particularly marked in Spain (+29.3 percentage points), but also in the United States (+16 pp) and the United Kingdom (+12.5 pp). Some countries, on the other hand, experienced significant falls in the incidence of long-term unemployment over the same period (e.g. in Brazil as well as in Germany, but from a very high level), while in many emerging economies (including Argentina and the Russian Federation) there has been little or no change.

**Figure 1. Unemployment remains high**



\* Selected urban areas.

a) Persons aged 15-64 for South Africa, 15-72 for the Russian Federation and 16 and over for the United States.

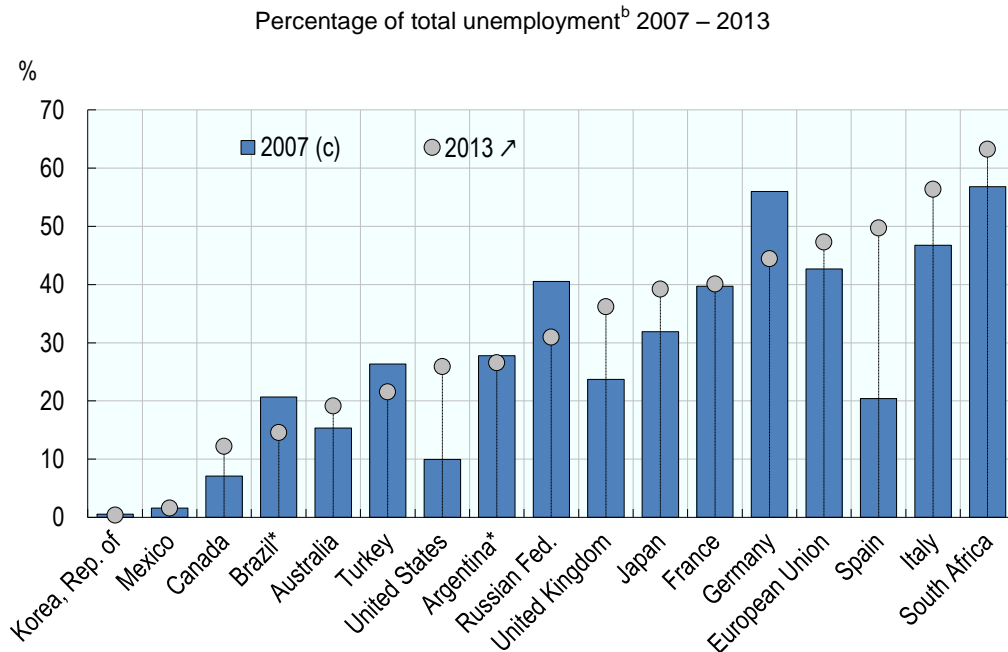
b) 2007 for China; 2007-08 for India; Q3 2007 for Indonesia and Saudi Arabia; and Q1 2008 for South Africa.

c) 2012 for China; 2011-12 for India; Q3 2013 for Saudi Arabia; Q4 2013 for Argentina and Turkey; and Q2 2014 for Canada and the United States..

Source: OECD Short-term Labour Force Statistics Database and ILO, Short-term Indicators of the labour Market.

<sup>2</sup> The role of different policy settings in explaining differences across countries in labour market resilience is explored in OECD (2012).

**Figure 2. Long-term unemployment is a major concern<sup>a</sup>**



\* Selected urban areas.

a) Persons unemployed for one year or more.

b) Persons aged 15-64 for South Africa, 15-72 for the Russian Federation and 16 and over for the United States.

c) 2008 for Argentina and South Africa.

Source: OECD estimates based on various national surveys and ILO Statistics, Short-Term Indicators Database.

6. **The persistence of aggregate unemployment and the build-up of long-term unemployment have raised concerns around a possible rise in structural unemployment in some G20 countries,** making it more difficult to bring unemployment down to pre-crisis levels. Measuring structural unemployment is not easy. One way of gauging this is by means of the Non-Accelerating Inflation Rate of Unemployment (NAIRU), which provides an estimate of the rate of unemployment below which inflation would start to rise. For those G20 countries where these estimates are available, there is some evidence of a structural rise in unemployment but, with the exception of Mexico, only in those countries where there has been a large and persistent increase in unemployment following the crisis. This rise has been modest in many cases at less than one percentage point in the case of France and the UK but somewhat higher for Italy at between one-and-a-half to two percentage points and more substantial in Spain.<sup>3</sup> Regardless of the changes in structural unemployment in recent years, it is important to recognise that some countries had higher levels of structural unemployment even before the financial and economic crisis.

<sup>3</sup>

Another way to assess whether there has been a rise in structural unemployment is to examine the relationship between the unemployment rate and the vacancy rate (job vacancies divided by the labour force). During economic downturns, unemployment rates will tend to rise as the vacancy rate falls, *i.e.* as job openings dry up. The reverse will be the case in upturns. Therefore, there will be an inverse relationship observed between unemployment and vacancies over the economic cycle (the so-called Beveridge curve). A rise in structural unemployment shows up in an outward shift in this relationship such that a given vacancy rate is associated with a higher unemployment rate than was previously the case. For those countries where these data are available, the evidence suggests that structural unemployment has risen in Spain and the United Kingdom (consistent with the NAIRU estimates) but also in the United States (see the Chapter 1 on “Waiting for the Recovery: OECD Labour Markets in the Wake of the Crisis” in *OECD Employment Outlook 2012*).

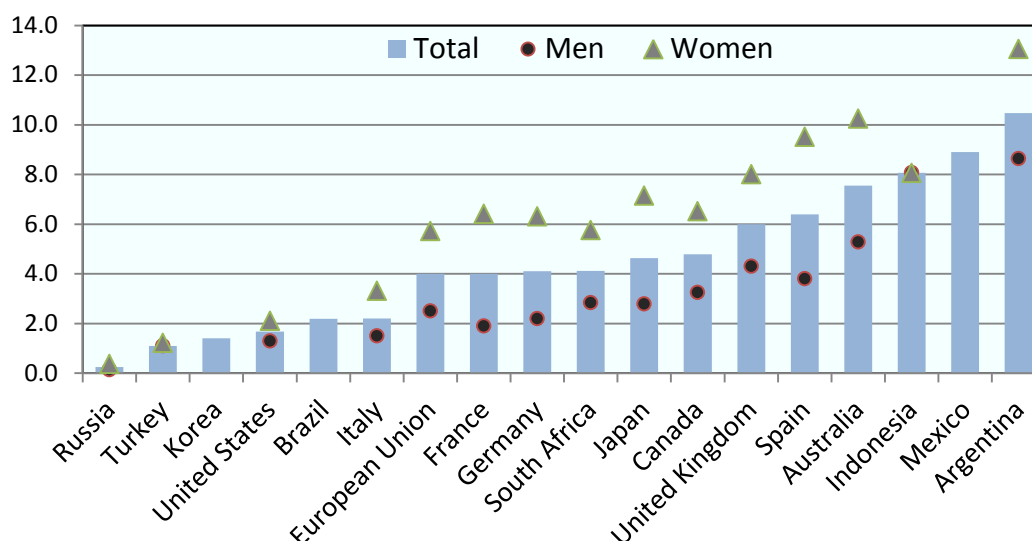
7. **In some countries, the high prevalence of temporary contracts could lead to more unemployment in the long-run.** The high incidence of temporary employment in some countries is primarily a concern from a job quality perspective. However, through its effect on higher turnover, it also raises frictional unemployment and may contribute to longer-term unemployment, as there is evidence that employees on non-regular contracts are less likely to benefit from employer-sponsored training (OECD, 2014a). Fewer opportunities to maintain and/or upgrade their skills mean that temporary workers face greater difficulties when looking for work, which in turn raises their risk of (long-term) unemployment. If firms invest less in non-regular workers, this may also depress productivity growth and therefore future job creation.

### *Chronic underemployment*

8. **In many emerging economies the crisis has lowered the pace of poverty reduction and formalisation, leaving many still facing chronically high levels of structural underemployment.** Underemployment covers different aspects of the underutilisation of potential labour resources in each country, including working fewer hours than desired and not fully utilising the available pool of skills and talent. The first of these aspects – sometimes referred to as time-related underemployment – can be captured by a measure of the share of the labour force working less than full-time hours for involuntary reasons (Figure 3).<sup>4</sup> While the data are not strictly comparable across countries because of differences in the exact definition used, time-related underemployment accounts for a significant share of the labour force in many advanced and emerging economies, reaching more than 8% in Argentina, Indonesia and Mexico. It is also quite high in Australia, reflecting the high incidence of part-time employment in Australia. In general, it also tends to be much higher for women than men.

**Figure 3. Time-related underemployment is substantial in some G20 countries**

Percentage of the labour force working part-time involuntarily in 2013<sup>a</sup>



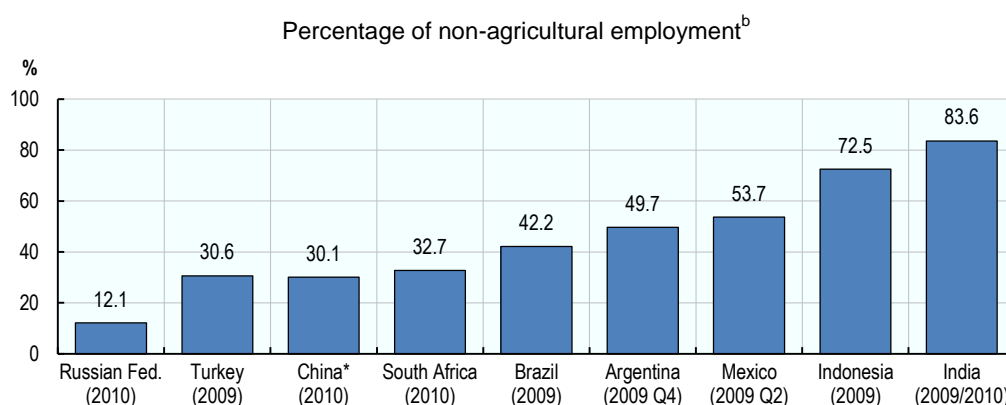
a) Involuntary part-time work refers to all persons in employment who are working less than a given number of (full-time) hours and who are both willing and available to work additional hours. The data are not strictly comparable across definitions because of differences in definitions. The data refer to 2012 for France, Korea, Mexico and Russia.

Source: OECD Labour Market Statistics Database; and ILOSTAT database.

<sup>4</sup> Time-related underemployment, or the similar concept of involuntary part-time work, can be defined as all persons in employment who are working less than a given number of (full-time) hours and who both willing and available to work additional hours.

9. **Underemployment in the emerging economies also manifests itself more generally through the prevalence of low-productivity, informal jobs and working poverty.** More than 4 in 5 workers in India occupy informal jobs, while the rate of informality exceeds 30% in all other countries (with the exception of the Russian Federation) (Figure 4).<sup>5</sup> Working in an informal job not only implies lower social protection and less employment security than working in a formal job, but often also means lower participation in training which may reinforce the likelihood of remaining stuck in a low-paid, precarious job. In developing and emerging country contexts, an important dimension of underemployment is “working poverty”: despite working for long hours, frequently in multiple jobs, workers do not earn enough to lift themselves and their families out of poverty.

**Figure 4. Informal employment<sup>a</sup> is common in G20 emerging economies**



a. For all countries, with the exception of the Russian Federation, informal employment refers to persons in informal employment (i.e. the sum of informal jobs in formal enterprises, informal sector enterprises, and households producing goods for own consumption or hiring paid domestic workers). For the Russian Federation, informal employment is defined as persons employed in the informal sector (i.e. informal jobs in informal enterprises plus formal jobs in informal sector enterprises).

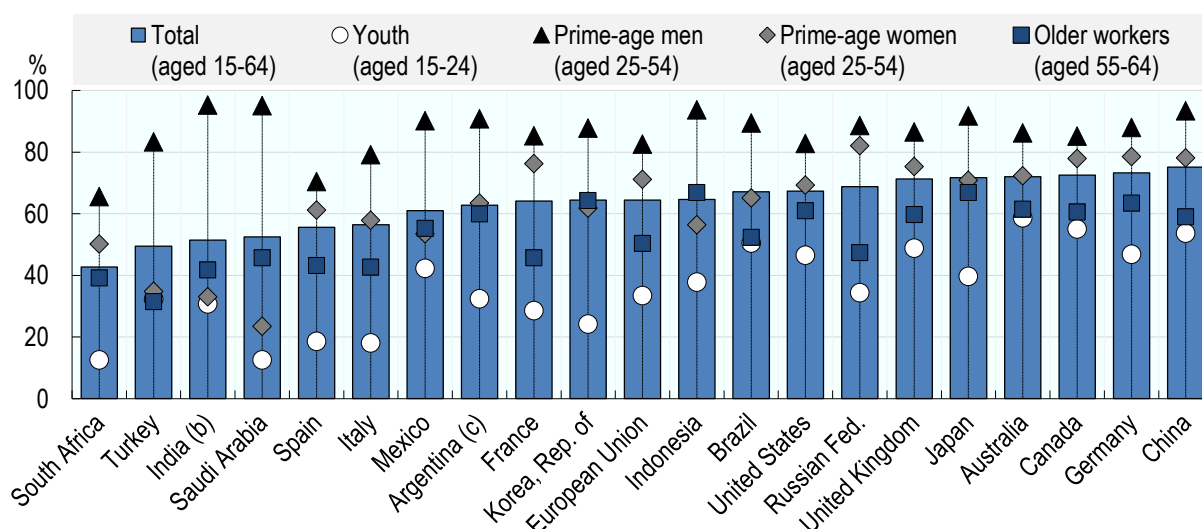
b. Data for the Russian Federation corresponds only to persons employed in the informal sector.  
Source: ILO/WIEGO Informal Employment Database.

10. **There is considerable underutilisation of labour resources more generally.** Underemployment not only shows up in the share of workers who are employed in poor quality jobs or working fewer hours than desired, but also in the underutilisation of labour resources more generally with some groups excluded from jobs altogether because of a range of barriers. While the employment rate (*i.e.* the share of the population in each group that is employed) for men aged 25-64 is quite similar across G20 countries, there are much larger differences for other groups such as women, youth, older workers and the low-skilled (Figure 5).

<sup>5</sup> The data for Russia are not strictly comparable with those shown for the other countries because they refer to persons employed in the informal sector rather than to all persons working in informal jobs, irrespective of whether these jobs are in the formal or informal sector.

**Figure 5. The employment rates of certain groups are particularly low**

Employment rate by gender and age groups, as a percentage of the population of the indicated group, 2013<sup>a</sup>



Countries are shown by ascending order of the total employment rate.

a. 2010 for China and 2011-12 for India.

b. Older workers refer to person aged 55 and over and total to persons aged 15 and over.

c. Selected urban areas only.

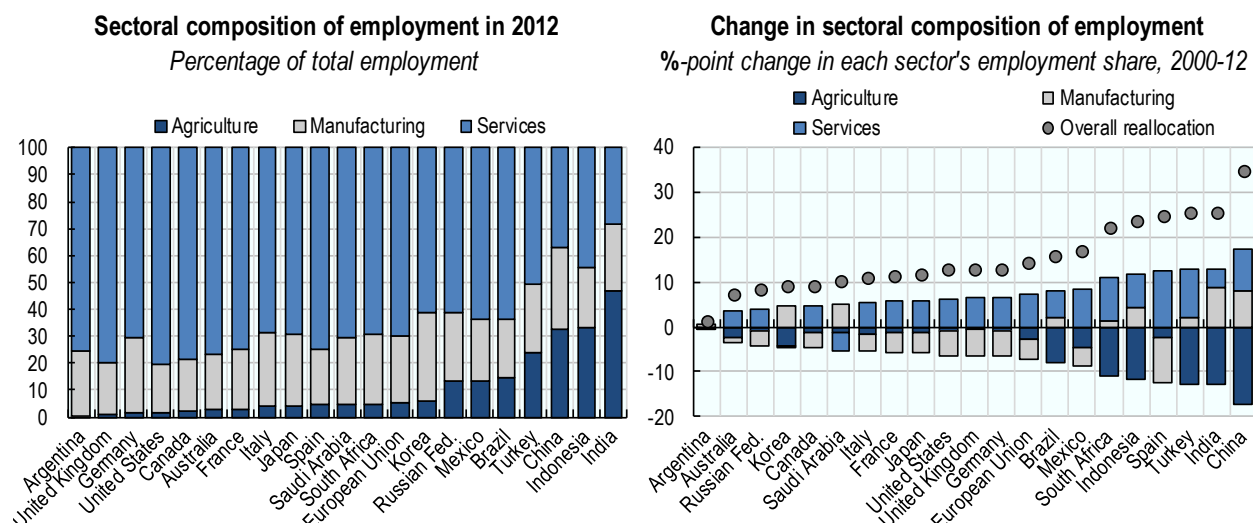
Source: OECD Labour Force Statistics Database and national labour force surveys.

### *Longer-term economic and social transformations*

11. **Tackling structural unemployment and underemployment will also require ensuring that labour markets are able to adapt to the substantial transformations that are occurring in the sources of job growth and the types of jobs that are being created.** These transformations are being driven by economic and social development, increased globalisation, technological change and demographic change. In emerging economies, these trends have given rise to a substantial shift over the past decade out of low-productive jobs in agriculture into more productive jobs in manufacturing and services (Figure 6). In China, for example, this shift has been accompanied by substantial internal migration from rural areas to urban areas, putting pressures on the provision of housing, employment and social services for these migrants. The system of household registration, the *hukou*, has restricted access to some of these services for these migrants and affected their labour market integration, but a number of policy measures have been put in place recently to ease these restrictions. In other economies, various barriers to geographical mobility have also hindered the reallocation of labour across sectors.



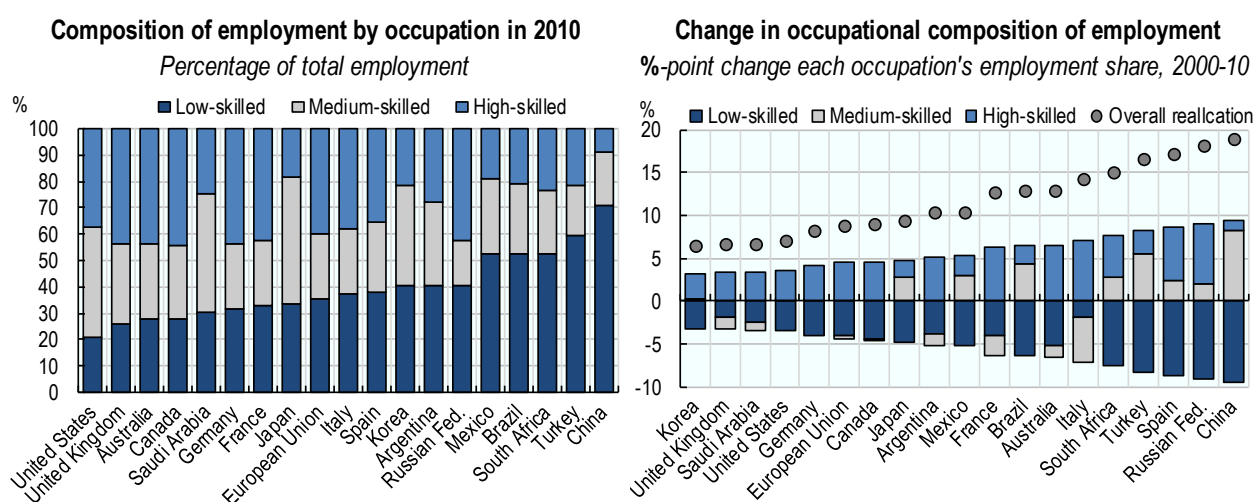
**Figure 6. Employment shifts between sectors have been considerable**



Source: OECD calculations based on data taken from ILO (2014), *Global Employment Trends 2014*.

12. **Across all G20 countries, technological change and globalisation have also changed profoundly work organisation practices and skill demands of employers.** In general, over the past decade, the demand for more skilled works has outpaced the demand for low-skilled workers with the share of total employment in managerial and technical and professional jobs increasing significantly (Figure 7). These changes are likely to intensify in the face of on-going process of innovation and diffusion of the information and communication technology (IT) and could result in further displacement of jobs that involve routine tasks (manual or cognitive). Not all of these changes are fully predictable in terms of their impact on labour demand, but what is clear is that good information is required on changing skill needs in order to guide the provision of, and participation in, education and training.

**Figure 7. Employment is shifting substantially towards high-skilled jobs**



a) Occupations grouped according to the ISCO-88 classification as follow: High-skilled refers to codes 1 to 3 (Legislators, senior officials and managers; Professionals; and Technicians and associate professionals); Medium-skilled to codes 4 and 5 (Clerks; and Service workers and shop and market sales workers); and Low-skilled to codes 6 to 9 (Skilled agricultural and fishery workers; Craft and related trade workers; Plant and machine operators and assemblers; and Elementary occupations).

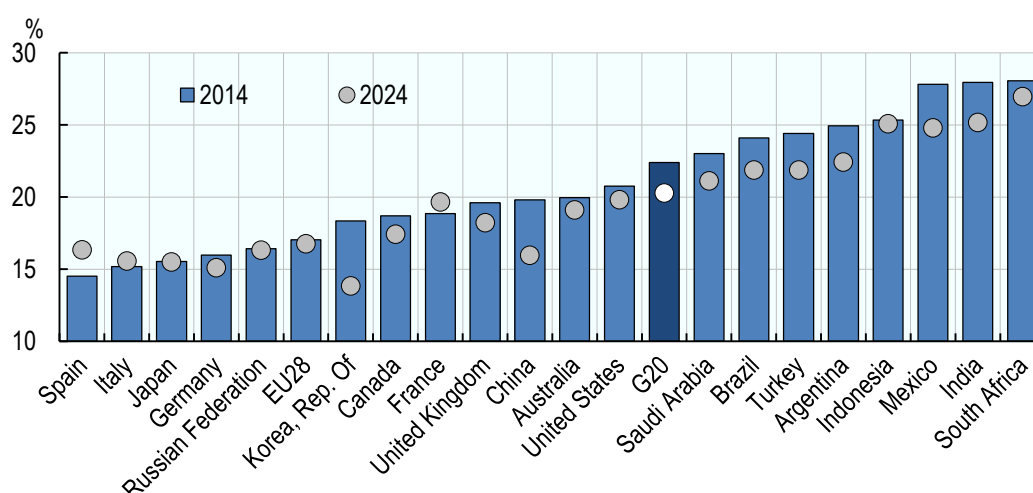
b) 2000-09 for Argentina; 2001-10 for Turkey; and 2002-10 for Brazil and the European Union.

Source: OECD calculations based on data taken from ILO online database ILOSTAT and national labour force surveys.

13. **Demographic change will also open up both challenges and opportunities for tackling structural unemployment and underemployment** (Figure 8). In several of the emerging economies, young people aged 15-24 will continue to account for a large proportion of the working-age population and the challenge will be to ensure that these large cohorts of youth do not experience prolonged periods of joblessness or employment in low-paid precarious jobs when entering the labour market. In advanced economies, with a high share of older workers, the employment of the latter is a crucial challenge for the future. Allowing people to stay active as they grow older and to continue contributing to society is key to tackling the challenge of demographic ageing and mitigating the potential negative impact of rapid population ageing on growth. Even in these countries with older populations, however, one-third of unemployed youth have been out of work for a year or more – an unprecedented high.

**Figure 8. Substantial demographic change will take place over the next 10 years**

Percentage share of 15-24 year-olds in the population aged 15-64, 2014 and 2024



Source: OECD Population and Labour Force Projections Database.

### ***Skills mismatch and skills shortages***

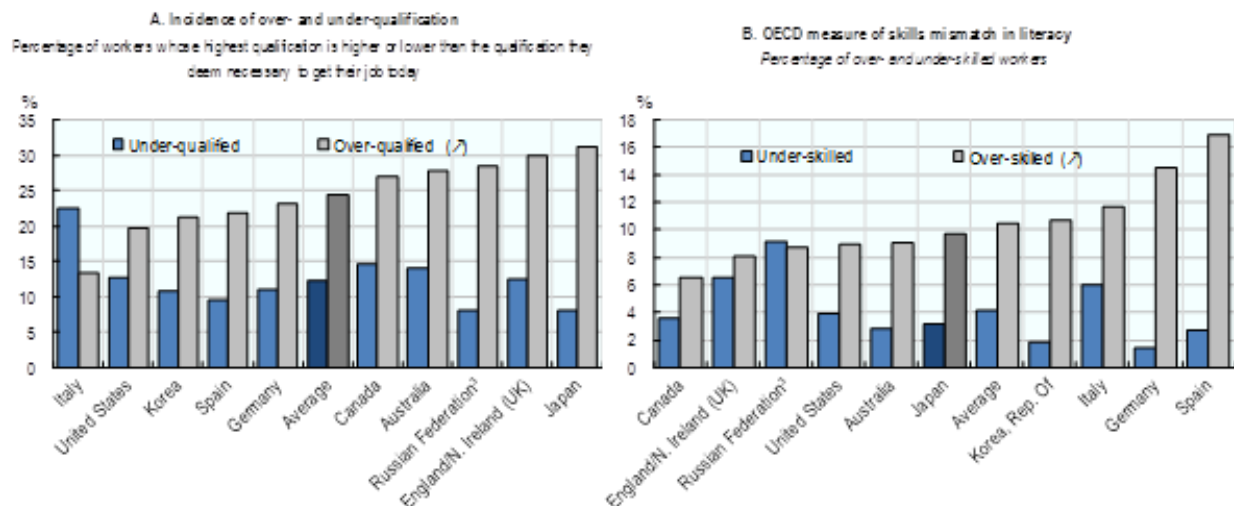
14. **These economic and demographic transformations can give rise to both skills mismatch and shortages if countries fail to correctly anticipate and respond to changing skill needs.** Close to one in four workers in the G20 countries that participated in the *Survey of Adult Skills* (PIAAC) have higher qualifications than what they believe is required to be hired for their jobs and 13% are under-qualified (Figure 9). However, this measure tends to overstate the actual extent of skills mismatch.<sup>6</sup> A more direct measure of skills mismatch shows much smaller but still sizeable proportion of workers in jobs that are not well-matched with their skills. These mismatches may have worsened during the crisis, with the large stock of current job seekers facing few job opportunities and frequently accepting jobs that are not well-matched to their skills. At the same time, while international surveys of employers such as by Manpower suggest

<sup>6</sup> Actual skills mismatches in the workplace are less widespread than qualification mismatch, and the overlap between the two kinds of mismatch is limited. This is because qualification mismatch only imprecisely reflects the link between workers' skills and the skill requirements of their jobs. Some instances of qualification mismatch may occur when workers have lower skills than would be expected at their qualification level, either because they performed poorly in initial education or because their skills have depreciated over time. Over-skilling is also found to have smaller negative effects on hourly wages than over-qualification, suggesting that employers learn about their employees' skills over-time and adapt job content to use them more efficiently.

that recruitment difficulties declined in most countries between 2007 and 2013 as the global financial crisis brought about a sharp rise in unemployment, many employers continue to report difficulties in filling job vacancies. However, it is difficult to distinguish in these surveys the actual extent of skill shortages from general recruitment difficulties faced by firms because they are not offering the going market wage or attractive working conditions.

**Figure 9. Qualifications mismatch affects a large proportion of workers**

Percentage of workers whose highest qualification is higher or lower than the qualification they deem necessary to get their job



1. The graph shows the share of workers who are over- and under-qualified is computed by comparing each worker's highest educational attainment to the educational attainment that the worker deems necessary to get his/her own job.

Source: Survey of Adult Skills (PIAAC), 2013 – [www.oecd.org/site/piaac](http://www.oecd.org/site/piaac).

**15. Skills mismatch and shortages can contribute to structural unemployment and underemployment as well as reduce the growth potential of the economy.** Skill mismatch puts into question the ability of societies to capitalise on their stock of human capital. Skills are also a critical asset for individual workers and firms in a rapidly changing globalised world. Situations where individuals have substantially more skills than jobs require prevent those individuals, enterprises and economies from reaping the benefits of their investment in skills in terms of higher wages, productivity growth and innovation. In some developing and emerging countries, an under-skilled workforce can lead to skill shortages and compromise economic development, leaving low-skilled workers stuck in low-paid, precarious jobs. In some advanced and emerging economies, significant investments in education have not been accompanied by job growth leading to high rates of graduate unemployment and qualification mismatch.

### **Polices to tackle structural unemployment and underemployment**

**16.** Tackling structural unemployment and underemployment requires a mutually reinforcing approach that seeks to: first, strengthen growth and encourage greater job creation; and, second, tackle structural barriers in product and labour markets that are preventing individuals from finding productive and rewarding jobs that correspond well with their skills and capacities.

17. Much of the rise in unemployment can be explained by the crisis and weak recovery and, therefore, in the short-run, policies aimed at the expansion of aggregate demand, including boosting investments in infrastructure, where there is fiscal space, and in promoting small and medium-sized enterprises, should remain the number one priority. However, in the long term, such policies will not be sufficient in countries where structural unemployment is on the rise or remains at a high level. In addition, given that monetary policy is already fairly accommodative and that the space for supportive fiscal policy is limited in most countries hit by the crisis, placing more emphasis on structural reforms will be essential for promoting greater job growth and a durable reduction in unemployment and underemployment. This will require reforms of anti-competitive product market regulations that hamper the creation of new businesses, restrict output, keep prices artificially high and reduce employment in affected sectors. It will also require tackling structural barriers in the labour market so that people and firms can take advantage of, and adjust quickly to, changes brought about by technological advances, economic development, demographic transformations and globalisation.

#### ***Tackling weak aggregate demand and boosting the creation of quality jobs***

18. **While structural unemployment may be on the rise in some countries, unemployment remains primarily cyclical and will therefore require continued efforts to boost demand and job creation in the short-run to mitigate the possible impact on long-term and structural unemployment.** While global activity and trade are projected to strengthen in the next two years, the recovery is likely to remain modest and growth in the large emerging economies is expected to remain subdued by past standards. As a result, monetary policy needs to remain very accommodative, especially in the euro area, where deflation risks have risen, while the pace of fiscal consolidation should be slowed given the state of public finances and the economic outlook.

19. **There needs to be a renewed commitment to increased public investment in infrastructure that will not only boost growth but also promote employment and productivity.** Many G20 countries, including the high income ones, face significant infrastructure deficits. Yet, past evidence has shown that investment in physical infrastructure often has a bigger impact on long-term economic performance than other kinds of physical investment, while contributing to raising employment in the short term. Several G20 emerging economies have innovative public employment programmes (e.g. NREGA in India, Expanded Public Works Programme in South Africa) that combine infrastructure development with job creation and social protection in communities with high levels of poverty and under-employment.

20. **In addition to continuing to tackle weak aggregate demand and boosting job creation in the short-run, countries should therefore seek to address structural unemployment and/or underemployment** through a combination of reforms that are tailored to their own national circumstances in the following areas: (i) product markets; (ii) social protection systems and activation policies; (iii) public employment services; (iv) wage-setting institutions; (v) employment protection legislation; and (vi) skills and training.

#### ***Encouraging greater product market competition***

21. **Promoting product-market competition can support job creation and boost real wages.** Model simulations have suggested that product market reforms contribute more to growth than labour market reforms and infrastructure investment (IMF, OECD and the World Bank, 2014). Legal impediments to entry of new firms should be removed in all areas where competition is feasible, and administrative burdens on business start-ups should be reduced. Start-up costs should be lowered and administrative procedures for the creation of new businesses simplified so as to nurture an entrepreneurial climate. There is also further scope to reduce restrictions on international trade and investment in goods and services, and competition-restraining state control of business operations should be reduced.

### *Designing effective and employment-friendly social protection systems*

22. **The economic and financial crisis has highlighted the need for adequate social protection systems.** Over the last few years, many G20 countries have extended the coverage and duration of unemployment benefits to help individuals through a difficult time while they searched for a new job. This policy changes has helped job losers in their job search and cushioned the effects of the crisis on household income. One of the main arguments against extending benefits, i.e. that it may reduce job-search intensity, is weaker during periods of recession, as vacancies are scarce and the pool of job-seekers is large.

23. **Adequate social protection systems can support the emergence of a dynamic and inclusive labour market.** Social protection is needed not just in a pursuit of social justice and equity, or to provide all citizens with a minimum acceptable livelihood and protection against risk, but also because they can empower and encourage individuals to invest in their human capital, pursue productive opportunities when they arise and contribute to supporting consumption and aggregate demand in times of economic downturns. This is particularly important in emerging economies, where many workers continue to be employed informally with little or no protection. In those countries, extending social protection coverage would help address persistent poverty, tackle income inequality, but also contribute to improved labour market outcomes.

24. **In emerging economies, with less developed tax-benefit systems, conditional cash transfers and/or social protection floors<sup>7</sup> can provide the most vulnerable with a basic social floor, with little or no adverse effect on work incentives.<sup>8</sup>** There are a number of reasons why such programmes tend to have little adverse impact on incentives to participate in the labour market of recipient households: cash transfers in emerging countries are usually not conditional on labour force status (unsurprisingly, given the high rate of in-work poverty); due to administrative constraints, the means-tests benefit eligibility are often loosely and irregularly applied, implying that additional income from work is not taxed away as a result of benefit withdrawal; and levels of transfer are usually low relative to household income. As a result, the implicit tax of cash transfers on working tends to be rather low in emerging economies. Moreover, by alleviating liquidity constraints, these conditional cash transfers appear to have allowed individuals to engage in more optimal job search and find better job matches.

25. In countries with more developed social protection systems, **well-designed activation policies can allow countries to maintain reasonably generous benefits while achieving low unemployment and high labour market participation.** This requires measures to ensure that the unemployed are actively looking for work and encouraged to find new jobs, and that it pays to work rather than stay on benefits. Underlying such an approach is the principle of mutual obligations: governments assume the responsibility to provide job seekers with effective re-employment services, counselling, training and financial incentives to enable them to find work, while beneficiaries are required to take active steps to find work or improve their employability, or else face the risk of (moderate) benefit sanctions. Such initiatives work particularly well in combination with tax-benefit reforms, including in-work benefits, to make work pay. While there is less of a case for exerting strong pressure on jobless people to search for a job when macro-economic or local economic conditions are temporarily depressed, there is also a risk that weak labour markets and a lack of job search activity reinforce each other. In countries where unemployment benefit programmes are

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<sup>7</sup> ILO Recommendation 202 Concerning National Floors of Social Protection sets out a global agreement on sets of basic social security guarantees which secure protection aimed at preventing or alleviating poverty, vulnerability and social exclusion.

<sup>8</sup> These labour market effects for selected G20 emerging economies were analysed in Chapter 2 “The Labour Market Effects of Social Protections Systems in Emerging Economies” in *OECD Employment Outlook 2011*.

relatively generous, job search incentives and spending on activation programmes should be kept at an adequate level to minimise the risk of deteriorating work incentives and long-term unemployment.

26. In this respect, **it is important to persevere with reforms aimed at introducing or extending work-related requirements for groups such as lone parents, unemployed older workers and people with partial work-capacity.** These reforms have proved to be successful in helping these groups return to work even if initially they may result in some increase in “open” unemployment as these groups lose their inactive status (Box 1). However, care is needed to avoid overloading employment services with new client groups. In particular, the transfer of workers with restricted work capacity to unemployment benefits risks a build-up of long-term unemployment, and this could divert resources that are needed to contain levels of unemployment among workers with full capacity to work. Activation requirements may be targeted on new claimants to test and refine new provisions, and only extended later to people who were already on the inactive benefit at the time of the policy reform.

#### **Box 1. Welfare reforms for low-income parents**

A long standing concern with means-tested social welfare payments for low income families with school-age children is that they can reduce incentives to participate in the labour market, potentially leading to long episodes of welfare dependence, depreciation of human capital, and ultimately exacerbating rather than alleviating poverty. Policy makers across the OECD have responded to this concern by reforming programs to encourage or compel welfare-recipient parents of all but the youngest children to either re-enter the labour market or to engage in activities aimed at maintaining or improving their employability. For example, widespread reforms along these lines were introduced across **US states** in the 1990s. These US welfare reforms have been extensively evaluated, and the bulk of evidence suggests they resulted in large and statistically significant falls in welfare caseloads along with increases in employment.

A recent (2007) welfare reform in **Australia** required low-income parents to engage in 15 hours per week of paid work or work-related activity for those in receipt of Parenting Payment (PP) – the main income support payment for this group – with a youngest child aged seven or older. The reforms involved a substantial tightening of payment conditionality, broadly in line with the additional conditionality introduced by a number of US states as part of the 1990s welfare reforms.

Although these welfare reforms are closely based on the US reforms of the 1990s, Australia offers a rather different labour market context, with comparatively high minimum wages and employment rates for mothers of pre-school-age children that are comparatively low. The welfare system is also rather different in Australia compared to the US welfare system of the 1990s, with other welfare payments, not all of which have similar activity requirements, also potentially available. This raises the possibility that tightening one part of the welfare system may end up shifting claimants onto other forms of welfare payment.

As was the case for the reforms introduced by US states in the 1990s, however, the Australian welfare reforms have been estimated to have had large and positive impacts on the probability of exiting the Parenting Payment. Two thirds of these exits were exits from welfare altogether, while and one third were exits to other welfare payments.

*Source: Fok, Y.K. and D. McVicar (2013), "Did the 2007 welfare reforms for low income parents in Australia increase welfare exits?", IZA Journal of Labor Policy, Vol. 2/3, IZA, Bonn.*

27. **Active Labour Market Policies (ALMPs) have a key role to play in containing the risk of rising structural unemployment.** In the context of a weak economic recovery following a severe economic downturn, active labour market policies have a twofold role to play in containing the risk of rising structural unemployment. First, they can play a preventive role by helping job losers find their way back into work as quickly as possible and helping those at risk of long-term unemployment by maintaining their skills through the provision of (temporary) work opportunities that make use of their existing skills. This can prevent skills depreciation among the unemployed and reduce the risk that they become discouraged and drop permanently out of the labour force. From this perspective, active measures that are

likely to be most effective include job-search assistance (e.g. face-to-face interviews, individual action plans, job clubs) and employment subsidies (e.g. gross hiring subsidies, reductions in employer social-security contributions, marginal employment subsidies). Second, the role of ALMPs can be remedial by addressing structural bottlenecks that prevent unemployed job seekers from getting back into work. This may be because their skills have become obsolete or depreciated as a result of prolonged joblessness. Active measures that can help to remedy structural labour market difficulties faced by the unemployed include training and work-experience programmes.

### ***Investing in effective employment services***

28. **A successful activation strategy will require effective employment services.** Employment services are at the core of the mutual obligations approach but this requires maintaining a close contact with people on benefits in order to deliver the necessary support services to them and to monitor their job-search behaviour so as to ensure that efforts are being made to return to work. As part of an effort to improve service delivery, some countries have made increasing use of private employment agencies, most notably in Australia and the United Kingdom. This could be particularly relevant in emerging economies, where the capacity of the public employment services is limited. The effectiveness of both public and private employment services can be improved through performance management based on measures of employment outcomes that are adjusted for jobseeker and local labour market characteristics.

29. **Implementing a successful activation strategy may also require institutional reforms** such as co-ordinating the administration of benefits and job-search assistance as well as funding arrangements at the national and local levels. The UK experience suggests that merging the public employment service and benefit agency has improved employment outcomes and services for clients and has been cost-effective (Box 2). Experience from other countries, such as Finland, Ireland, Switzerland and Australia, suggests partnership approaches between organisations and agencies (including those in the private and not-for-profit sector) can improve the co-ordination of service delivery, especially for disadvantaged client groups or high-unemployment areas. In Finland, the alignment of institutional incentives, as national government and local governments agreed to share the cost of benefit payments to the target group, accompanied the development of jointly managed service centres for the very-long-term unemployed.

### ***Ensuring that wages and labour costs respond to labour market developments, while tackling in-work poverty and the rise in earnings inequality***

30. **The adaptability and resilience of labour market also depend on the degree to which wages are allowed to respond to labour market developments.** The challenge for policy-makers is to provide mechanisms for wage adjustments that are consistent not only with high aggregate demand, good economic performance and low unemployment, but also allow productivity gains to be shared fairly, tackle in-work poverty and prevent earnings inequality from increasing. Wage adjustments can provide an important channel for accommodating temporary fluctuations in demand as well as for adapting to structural changes in the economy in the longer term. However, the importance of wage adjustment goes well beyond the interests of employers since it is also a key determinant of the level of unemployment, household income and private household consumption. Policy makers can influence wage setting using minimum wage policies and by shaping incentives and providing information to social partners on the context in which collective bargaining takes place. They can also intervene *ex post* through the use of in-work benefits, reductions in social charges, or the progressivity of the tax system.



### Box 2. Work-focused institutional integration in the United Kingdom - Jobcentre Plus

Before 2002, employment services and benefits (except for unemployment benefits) for working-age people in Britain were delivered through two separate agencies. In April 2002, these agencies were merged to form Jobcentre Plus (JCP). This new agency provided a single point of delivery for cash benefits and activation services for about 4.5 million working-age claimants.

The agency inherited a network of 1 500 offices and 90 000 staff. In the new service delivery model, benefit claims were administered through a network of “contact” and “benefit delivery” centres, with benefits paid directly into each recipient’s bank account. Employment services and the monitoring and enforcement of activity requirements were handled through some 800 integrated front line Jobcentres. Full-time equivalent staff numbers fell to about 69 000 by 2008 when the reorganisation was complete.

The objective was to create an employment-first front-line service. New benefit claims are made on-line or via telephone, with free phones being available in Jobcentres. Nearly all claimants are required to attend a Work-focused Interview with a Personal Adviser, usually within three to four working days. The task of the Personal Adviser is to assess employability, identify barriers and provide employment assistance. This may include matching and submitting the individual to vacancies. Claimants are then subject to activity requirements related to their benefit, with unemployed claimants subject to full conditionality.

The direct cost of JCP’s modernisation was GBP 1.9 billion, some GBP 300 million below the original budget. A detailed evaluation of impacts, based on tracking outcomes as the JCP model was rolled out in different areas of the country over a four-year period, supplemented by macroeconomic modelling, found that the reorganised delivery agency had helped to reduce the number of people on all the main working-age benefits and increase the effective labour supply. The net contribution to GDP was estimated in various ways and in all cases the JCP investment appeared to have been more than self-financing, with one estimate showing a net increase of 0.1% of GDP worth a cumulative GBP 5.5 billion by 2015.

In 2011, JCP’s Executive Agency status was revoked. A staff total for the regional and national offices and the 31 contact centres and 79 benefit processing centres is no longer cited; however, in the recession, front-line services were given priority and there were in 2011/12 nearly 37 000 staff in local jobcentres, an increase of more than 50% on the level in early 2008.

*Source:* Coleman, N., E. Kennedy and H. Carpenter (2005), “Jobcentre Plus Service DeliveryWaveTwo: Findings from Quantitative Research”, Department of Work and Pensions Research Report, No. 284; Work and Pensions Committee (2006), “The Efficiency Savings Programme in Jobcentre Plus”, Vol. 1, Second Report of Session 2005-06, House of Commons, available at [www.publications.parliament.uk/pa/cm200506/cmselect/cmworpen/834/834i.pdf](http://www.publications.parliament.uk/pa/cm200506/cmselect/cmworpen/834/834i.pdf); NAO – National Audit Office (2013), Department of Work and Pensions: Responding to Change in Jobcentres, available at [www.nao.org.uk/publications/1213/jobcentres.aspx](http://www.nao.org.uk/publications/1213/jobcentres.aspx); Riley, R., H. Bewley, S. Kirby, A. Rincon-Aznar and A. George (2011), “The Introduction of Jobcentre Plus: An Evaluation of Labour Market Impacts”, DWP Research Report, No. 781, National Institute of Economic and Social Research for the Department for Work and Pensions, London; and Daily Hansard Written Answers, 26 November 2008 and 28 January 2009.

31. **Minimum wages play an important role in addressing in-work poverty and inequality, but may also have a negative effect on (formal) employment of certain groups if set inappropriately.** The evidence suggests if set at an adequate level and regularly revised taking account of both social and economic considerations, the minimum wage can contribute to reduce in-work poverty and does not undermine employment. If the statutory minimum wage is set as a relatively high proportion of the average or median wage, consideration could also be given to a sub-minimum wages for low skilled youth entering the labour market, to promote youth employment in a manner that is consistent with the principle of equal remuneration for work of equal value.

32. **Equally, high payroll taxes and social charges can reduce employment, or lead to informality,** especially among low-productivity workers. Several countries have therefore reduced employers’ social security contributions on low-wage employment and, when this has led to a fall in total labour costs, countries have been rewarded with stronger hiring of such workers (or their formalisation) (Box 3).



### Box 3. Reducing non-wage rigidities in Turkey

With an employment rate that has fluctuated between 40%–50%, Turkey's labour market performance has been amongst the poorest in Europe over the past decade. The divergence in employment rates between Turkey and the EU can be ascribed primarily to the very low female employment rate in Turkey, with only about one in five women of working age in employment, equivalent to around one third of the EU average. In addition, informal employment in Turkey account for 45% of total employment.

A number of national and international surveys had blamed high non-wage costs, particularly social security contributions, for placing a heavy burden on employers and discouraging employment creation in the formal sector, while encouraging informal employment. While the average tax wedge in Turkey for average income earning singles and couples without children is comparable to that encountered in EU countries, Turkey ranks well above the EU average as family size gets larger and income levels decrease. According to OECD data, the tax wedge in Turkey is the highest in the OECD for low-income families with two children.

In response, the Turkish government introduced a new law in May 2008 (the "employment package") that reduced employer social security contributions for the hiring of young men (aged 18 to 29 years) and women (aged over 18 years) between 1 July 2008 and 30 June 2010. The exemption would gradually be phased out over a 5-year period. More specifically, the Unemployment Insurance Fund would pay out 100% of employers' social security contributions for the first year, 80% for the second year, 60% for the third year, 40% for the fourth year and 20% for the fifth and final year. Employers could only benefit from this subsidy if, and only if, the individuals they hired from the target group were de facto employed within one year following the effective date of the regulation and in addition to the average number of workers that had been declared in the one-year period preceding the effective date of this regulation. The law also stipulated that the newly hired workers should not be included among the previously registered insured workers in the six-month period preceding the effective date of the regulation. Finally, in a further attempt to ensure additional hiring only, the law banned circulation of workers within sub-companies of the same employer; switching workers between direct or indirect partnerships; and situations in which an employer closes his company, opens another one and transfers his workers from the old to the new one.

The reform led to a positive and significant effect on formal employment for women in the periods shortly after the policy announcement. After the global economic crisis hit the Turkish labour market, a second employment package, extending the duration of the incentives for one more year, was introduced. Likewise, to overcome the detrimental effects of the crisis on the labour market, similar employment incentives were introduced in August 2009 covering all new hires, regardless of gender and age, for a six-month period.

Source: Ayhan, S.H. (2013), "Do non-wage cost rigidities slow down employment? Evidence from Turkey", *IZA Journal of Labor Policy*, Vol. 2/20, IZA, Bonn.

33. **It is also important to promote a stronger social dialogue and cooperation between the social partners.** Having good regulatory settings is a necessary, but not sufficient, condition for improving labour market outcomes. Industrial relations tend to be deeply embedded in the cultural and social fabric of modern economies and influence many different aspects of work, including not only pay but also working time, occupational health and safety and labour conflicts. Healthy industrial relations and strong labour market performance are more likely when there is trust between the social partners and when the latter are broadly representative. This not only helps to promote job quality, commitment and productivity but facilitates outcomes that are in line with economic conditions at the macro and micro level and which can take account of the interests of those on the margins of the labour market who are at greatest risk of exclusion. While employers face changing market conditions and are constantly under pressure to improve competitiveness, this will be more difficult to achieve if labour relationships are weak between then social partners. All of the key stakeholder have a responsibility to adapt well to change and achieve better functioning workplaces and industries.

#### Box 4. Germany's labour market performance

In the late 1990s and into the early 2000s, Germany's economic growth averaged only about 1.2 percent per year (from 1998 to 2005), including a recession in 2003, and unemployment rates rose from 9.2 percent in 1998 to 11.1 percent in 2005. Today, after the Great Recession, Germany is described as an "economic superstar". The number of unemployed people fell from 5 million in 2005 to 3 million in 2008, and its unemployment rate had declined to 7.7 % in 2010 and to around 5% today. In other words, in contrast to most of its European neighbours and the United States, Germany experienced almost no increase in unemployment during the Great Recession, despite a sharp decline in GDP in 2008 and 2009.

One common explanation for Germany's success is the so-called "Hartz reforms" implemented between 2002 and 2005. The reforms were set out in four laws which together aimed at strengthening job-search activities for the unemployed, providing job-acceptance incentives, and encouraging labour force participation, particularly among women and older workers. In addition, measures were taken to: reduce the maximum duration of unemployment insurance benefits; close options for early retirement; lower employer social security contributions; and increase the scope for use temporary contracts.

However, a more recent and alternative explanation for Germany's resurgent economy lies in the specific governance structure of the German labour market institutions, which allowed them to react flexibly in a time of extraordinary economic circumstances. Wage setting in Germany has become more decentralised. Since the mid-1990s, there has been an increase in the number of firm-level deviations from industry-wide union agreements. This has led to decentralisation of the wage-setting process from the industry to the firm level, which has led to wage restraint.

At the same time, however, there has been a significant decrease in real wages at the lower end of the wage distribution. The rise in inequality in Germany has led to an intensive debate about its social consequences, and its effect on poverty and social justice. For example, recent negotiations between employers and employee associations in Germany suggest that future wage settlements will try to make up for the loss in real wages many workers experienced in recent years. It is also likely that certain aspects of labour and wage regulations will in the future be "put in legislative stone." As one example, the new coalition government in Germany has decided to introduce a nationally legislated minimum wage.

Source: Dustman, C., B. Fitzenberger, U. Schönberg and A. Spitz-Oener (2014), "From sick man of Europe to economic superstar: Germany's resurgent economy", *Journal of Economic Perspectives*, Vol. 28/1, pp. 167-188.

#### *Employment protection regulations need to be consistent with the need for labour market dynamism*

34. **A careful balance is required between ensuring adequate employment protection for workers while not hindering the required labour mobility, reducing the dynamic efficiency of the economy and restraining job creation.** On the one hand, employment protection legislation is needed to protect workers from arbitrary actions and have firms internalise at least some of the social costs of labour turnover. When a firm dismisses a worker, the worker loses income, tenure-related fringe benefits and, potentially, accumulated job-specific skills and experience. If it takes a long time to find another job, the worker may experience depreciation of human capital and the negative health effects associated with prolonged unemployment. Society as a whole also bears some of the costs of labour turnover: unemployment or social assistance payments, spending on job-search assistance and active labour market programmes, just to name a few. Stricter employment protection may also have positive impacts for firms by encouraging longer working relationships between firms and workers, facilitating industrial stability and the build-up of firm-specific human capital.

35. **On the other hand, firms need to have room for adjusting the level and composition of their workforces to adapt to changing demand conditions and technology.** This is vital for effective businesses operation and therefore for productivity and economic growth. Overly strict employment protection rules effectively raise the cost of hiring workers since they increase firing costs for employers.

They may therefore worsen job prospects of certain groups, like young people, women and the long-term unemployed. They may also contribute to increased informality if employers hire workers informally in order to avoid the costs imposed by stringent rules around hiring and firing.

36. Moreover, **governments should aim to reduce labour market duality by reducing the gap between the level of protection afforded to permanent and temporary contracts.** Job losses during the financial crisis were disproportionately concentrated among those on temporary contracts, affecting youth and the low-skilled in particular, and resulting in increased inequality in labour market outcomes and incomes. In some countries, this reflects the fact that past reforms in this area have been partial where restrictions were eased on temporary contracts but maintained on permanent contracts. These reforms may have helped to promote job creation in the short-term, they also induced the creation of dual labour markets, consisting of a core of relatively stable, high-quality jobs and a secondary tier with low-quality, high-turnover jobs. Some countries such as Spain and Italy have therefore sought to reduce the gap in the level of protection between workers on permanent contracts and those on temporary contracts (Box 5). A similar phenomenon may be present in some emerging economies. While the reasons for widespread informal employment in emerging economies are many and various, strict employment protection in some emerging countries may limit hiring in the formal sector, driving a wedge between formal-sector employees and their counterparts in informal employment.

#### **Box 5. The 2012 Labour market reform in Spain**

The global financial and economic crisis hit the Spanish labour market particularly hard. The harmonised unemployment rate in Spain reached 26.7% in October 2013, the second highest in the OECD area (only exceeded by Greece) and more than three times the OECD average (7.9%). Since the start of the crisis, the number of unemployed has increased by more than 4 million persons in Spain. Even more worryingly, long-term unemployment – defined as those unemployed for 12 months or more – as a share of all unemployment has risen from 19.1% in in fourth quarter of 2007 to 50.4% in the third quarter of 2013.

A comprehensive reform of the Spanish labour market was undertaken in 2012. As part of the reform, dismissal regulations have been modified, redefining the conditions for fair dismissal, reducing monetary compensations in the case of unfair dismissal and eliminating the requirement of administrative authorisation in the case of collective redundancies. Moreover, a new permanent contract for full-time employees in small firms has been introduced with an extended trial period of one year.

The reform has contributed to promote hiring, in particular on permanent contracts. The reform has also contributed to containing the duration of the unemployment spells, in particular due to faster transitions into permanent contracts for those workers entering unemployment after a temporary job. The analysis also shows some signs that separations decreased after the reform, especially for temporary contracts, possibly resulting from the greater use of internal flexibility measures as an alternative to contract termination. All these findings point to a positive effect of the reform in dampening the widespread segmentation of the Spanish labour market, although the impact is so far small and it will take time before the duality of the labour market is considerably reduced.

Reforms of dismissal regulations, by enhancing labour reallocation, have the potential to boost productivity growth in the long-run. Drawing from a simulation exercise based on the experience of OECD countries over a long period of time, the OECD has estimated that the reform could potentially boost labour productivity growth in the long run by about a ¼ of a percentage point annually in the business sector (excluding agriculture, mining, fuel and professional services).

Overall, the 2012 labour market reform appears to have brought more dynamism into the Spanish labour market and is a step towards the reduction of its widespread segmentation and the increase of the competitiveness of the Spanish economy in the medium term.

*Source: OECD (2013f), The 2012 Labour Market Reform in Spain: A Preliminary Assessment, OECD Publishing, Paris.*

37. **Moving forward, governments in countries where employment protection rules are overly restrictive should aim to protect workers, not jobs** by facilitating hiring and firing decisions, while also providing efficient re-employment services, such as intensified job-search assistance, and income support to workers in the event of lay-off. Complementing reforms of employment protection rules with investments in public unemployment insurance schemes in countries that do not have such schemes in place, or where such schemes do not provide adequate protection against the risk of unemployment, is particularly important in the context of emerging economies. Indeed, in contrast to previous crisis episodes, job loss during the global financial crisis tended to be concentrated in the formal sector, thereby exposing the problems of not having an effective system of unemployment insurance in place.

*Internal flexibility instruments provide important mechanisms to avoid dismissals of workers in the first place*

38. **The adaptability and resilience of labour markets not only depends on the degree to which wages and the number of employees are allowed to respond to labour market developments, but also on the extent to which firms are capable of using internal flexibility instruments to avoid dismissals.** In many G20 countries firms resorted to instruments of internal flexibility during the crisis to limit employment losses. A particularly important margin along which such flexibility has been applied is hours worked, and participation in short-time work (STW) schemes, for example, has increased dramatically since 2007. These programmes (also referred to in some countries as ‘partial employment’ or ‘temporary lay-offs’) are public schemes that are intended to preserve jobs at firms experiencing temporarily low demand by encouraging work-sharing, while also providing income-support to workers whose hours are reduced due to a shortened workweek or temporary lay-offs. The use of internal flexibility to preserve employment is an area where government can play an important role through legislation and regulation. However, it is also one where social partners are key for the implementation of such schemes - reinforcing the earlier message about the need for building trust between the social partners.

*Removing obstacles to geographical labour mobility and effective migration*

39. **In many countries, there are persistent regional disparities in employment performance, which can be partly addressed through policies that promote local development as well as geographical labour mobility.** There are countries where labour shortages in certain regions coexist with continuously high unemployment in other regions. Similarly, within Europe, there is wide variation in the extent of unemployment across countries. Demand-side factors seem to play a significant role in explaining such regional disparities, (OECD, 2005), and therefore policies to enhance job creation in depressed regions is required. At the same time, however, a mobile labour force should be able to help address regional labour market imbalances. Removing obstacles to internal migration may therefore be an important policy issue, especially in countries where regional disparities are pronounced. In this respect, consideration should be given to housing, but also to healthcare and education policies. In addition, financial assistance for moving, particularly for the unemployed, could be used.

40. **International migration can also be an equilibrating force in the labour market, but poor labour market outcomes of migrants mean that the benefits of migration are not always fully exploited.** Population ageing, particularly in the advanced G20 countries, is expected to translate into shrinking workforces and lead to increasing labour and skills shortages – despite the high unemployment rates observed in some countries. At the same time, young people aged 15-24 will continue to account for a large proportion of the working-age population in several of the emerging economies. International migration can therefore act as a pressure release valve in some countries, while allowing others to equip their workforce with the skills required to cope with demographic and occupational changes and to contribute to competitiveness and continued economic growth.

However, while global migration has continued to rise during the economic and financial crisis (OECD and UN-DESA, 2013), migrant workers have been hit disproportionately hard by the crisis and much of their potential benefit is therefore left unutilised. Long-term unemployment of migrants is becoming a serious challenge in many OECD countries and raising their employment rate to that of the native-born is a policy priority that would entail substantial fiscal benefits for many economies.

### *Improving incentives to create formal jobs*

**Tackling informality requires a coherent and comprehensive set of policies. These include economic support measures to boost incomes, productivity, access to finance, infrastructure and markets, an enabling legal and regulatory framework with adapted and effective enforcement mechanisms and extension of social protection coverage.** Working in informal jobs can take many forms and reflects a variety of barriers to the creation of formal jobs. Thus, co-ordinated action across a number of fronts is necessary to reduce informal employment. These need to combine incentives to transit to formality with improved governance and enforcement of compliance, including through sanctions. In particular, greater efforts to strengthen tax and labour inspections are needed, since undeclared work among employees is to some extent explained by the weak tax assessment regime for small businesses and the self-employed. Enforcement can be strengthened by reinforcing tax inspection services and improving the exchange of information among the various government departments concerned, as well as through better cooperation with the social partners. Two additional ways to strengthen employers' incentives to properly declare labour earnings (which otherwise will be taxed as net profit) are to: i) make value added the relevant tax base; and ii) focus the tax collection strategy on upgrading business record-keeping and accounts, rather than on the detection of work relationship.

### *Supporting entrepreneurs and the self-employed*

41. **Promoting entrepreneurs and the self-employed can provide new sources of employment.** It has been estimated that entrepreneurial businesses account for a large share of all employment in most G20 economies (Ernst and Young, 2013). Fostering entrepreneurship is therefore an important element of any strategy aimed at tackling unemployment, and could be particularly so for certain groups such as women, young people, seniors, ethnic minorities and people with disabilities, who are currently under-represented in entrepreneurship and self-employment (OECD and EC, 2013). Promoting entrepreneurship and self-employment will require simplified business regulations, particularly for micro firms, and social security systems that do not discourage business creation and self-employment. Entrepreneurship skills also need to be developed through extending and improving entrepreneurship education, offering stand-alone entrepreneurship training courses, and offering advice and coaching using mentors from the same communities. Finally, where entrepreneurs face barriers in accessing finance, these need to be removed.

### *Helping individuals maintain their skills and adapt to changing skills needs*

42. **Long spells of unemployment increase the risk that individuals' skills become obsolete** and, because of shifts in labour demand, unemployed workers may find they lack the skills required to find a new job even during the recovery. The young and the low-skilled are particularly at risk: the former because there is very strong evidence that starting one's career in a recession and experiencing unemployment can lead to long-term 'scarring' effects; and the latter because they are at a higher risk of losing their jobs during a crisis and are likely to be replaced by more skilled workers in the recovery.

43. **Countries therefore need to invest in high-quality lifelong learning opportunities.** Such policies can help ensure that individuals maintain their skills or are able to re-train and adapt to changing skills needs.

But access to training is distributed very unequally over the adult workforce, and those with the least education and skills participate much less in training and tend to receive less employer-sponsored training. Second-chance opportunities can offer these workers a way out of the low-skills/low-income trap.

44. **On-the-job training programmes are likely to be the most effective.** Evaluations show that, on the whole, training programmes tend to have modestly positive effects on employment outcomes. Their effects are more noticeable in the medium- than in the short-run. Also, not all training programmes tend to be equally effective. Work-based programmes in particular tend to perform better than those that are classroom-based and/or deliver basic education.

45. **Training programmes are also most likely to be effective where they are demand-led** (Box 6). The involvement of employers has often been identified as a key to the success of training programmes. One of the best ways of achieving this is by ensuring an element of co-financing in the provision of training. It is also important that employers as well as trade unions are involved in the design and implementation of training courses, to make sure that the skills they impart on participants are in line with those demanded by the labour market.

**Box 6. The impact of job training: Evidence from Mexico's *Probecat* programme**

*Probecat*, which started in 1984, aims to increase the employability of disadvantaged youth through short-term, demand-driven courses that are complemented by internships, emphasising on-the-job training. Its most salient feature is that it does not rely on training institutions to provide the courses. Instead, the programme provides a stipend equivalent to the minimum wage to beneficiaries while the private sector businesses provide the training and the internship (for a minimum of three months) and cover the training costs: this is the in-firm training modality. To participate in the programme private firms have to agree to keep for one year at least 70 percent of the trainees.

*Probecat*, along with the *Chile Joven* programme, was one of the first of a new generation of training programmes for disadvantaged youth implemented in South America. These programmes broke with the past by offering a new model where training was essentially demand-driven, and the three functions of financing, planning and providing training were separated. The other key feature of these programmes is the internship phase that follows the training and which allows the participants to gain valuable experience in a formal sector job.

The evaluation evidence for these programmes has generally been very positive, with employment effects ranging from modest to meaningful (increasing employment rates by about 0 to 5 percentage points – although they tend to be higher and more significant for some groups, such as women. Also, there is often a larger and significant impact on job quality, measured by the likelihood of obtaining a formal sector job, having a contract, and/or receiving health insurance as a benefit.

Source: Ibarraran, P. and D. Rosas (2009), "Evaluating the impact of job training programmes in Latin America: Evidence from IDB funded operations", *Journal of Development Effectiveness*, Vol. 1/2.

46. **Skill mismatches call for a comprehensive strategy involving all key stakeholders.** The adjustment of skills to changing labour market needs requires a two-pronged, long-term and systematic approach. First, action is needed to reduce the gap between knowledge generated in the education system and the skill demands of employers. Second, continuing intervention throughout each person's working life, targeting the continuous development and use of skills, is necessary for both the employed and the unemployed.

47. **Students should be encouraged and supported to complete their schooling with the essential skills needed to find work.** Governments should support participation in education at least until the completion of upper secondary schooling. In developing and emerging economies, where financial barriers play a key role in explaining school drop outs, this could be achieved by introducing schemes that provide financial incentives for school attendance.

Empirical evidence confirms that informal employment, a category considered as “non-standard” in traditional literature, is in fact “standard” among young workers in developing economies. Based on school-to-work transitions surveys in 20 countries examined in 2012-2013, three-quarters of young workers aged 15-29 are currently engaged in informal employment (Shehu and Nilsson, 2014).

48. **The responsiveness of the education system to the needs of the labour market has to be improved and requires close collaboration between employers, trade unions and public authorities.** Preparing young people for a successful entry into the labour market requires close cooperation between public and private sectors so that education and training can respond quickly to labour market needs and provide suitable opportunities to learn in the workplace. Guiding students in their choices of field of study, promoting their transition from school to work and maintaining and improving skills throughout the working life will ensure that the full potential of each individual’s skills is exploited and that the skill needs of enterprises are effectively met. Many sectors are characterised by rapid transformations, rendering it increasingly important to better prepare guidance workers and counsellors to understand labour market information and job demands. This should be part of the policy agenda for responsive education and training.

49. **Good labour market information can help match labour demand and supply.** The demand for skills is changing rapidly as a result of increased globalisation and rapid technological change. The need for accurate information on existing skill needs and for forward-looking information on how the labour market and the demand for skills might change is therefore critical. Employers need to plan their current and future workforces; young people and workers need to know which skills offer the best job prospects; education providers need to adapt their curricula and ensure they remain relevant; and policy-makers need to ensure they institute the necessary changes in education systems, labour markets and migration policy in a timely fashion.

50. **It is essential that employers help workers maintain their existing skills by fully utilising them.** The notion that new recruits will arrive at the workplace with all the job skills they will need over their career is unrealistic. Employers must ensure that their workplaces offer attractive working conditions and learning opportunities and that their recruitment strategies efficiently attract and select talent. Trade unions, through social dialogue, can also promote high quality jobs and stable employment relationships as well as help employers and workers recognise the importance of continuous skills development. The support of trade unions is crucial in developing relevant qualifications and curricula and in expanding internship and apprenticeship schemes for youth and unemployed to learn on the job.

51. **Skills shortages can be address through an appropriate mix of training provision, increased labour force participation as well as migration.** Government should support employer-provided training with financial incentives, particularly for occupations in shortage or for workers that would otherwise not benefit from training. They should also promote labour force participation of groups with high inactivity rates, such as women and older workers. Inactivity represents a major waste of human capital investment and individuals must be given the means to work while reconciling it with their family life or their particular situation. Finally, a well-designed and managed migration policy is also important in tackling skill shortages.

## **Conclusions**

52. Structural unemployment and underemployment represent a major challenge for G20 countries. In some countries, the immediate challenge is to prevent high and persistent levels of unemployment from translating into an increase in structural unemployment. In others, a high level of structural unemployment predates the crisis and reflects a failure of policies and institutions to adapt to ongoing economic, technological, demographic and social change. In many emerging economies, underemployment remains stubbornly high with many workers unable to find full-time work and often stuck in low-productive, low-paid informal jobs with little, if any, social protection. Responding to these challenges requires a mutually reinforcing set of policies that are tailored to each country's national circumstances and which seek to, first, strengthen growth and encourage greater job creation, and, second, tackle structural barriers in the labour market that are preventing individuals from finding productive and rewarding jobs that correspond well with their skills and capacities.



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