AN IMPACT ANALYSIS OF ACTIVE AND PASSIVE LABOUR MARKET POLICIES WITHIN THE EUROPEAN UNION

Liana SON, Graţiela Georgiana CARICA
WEST UNIVERSITY OF TIMISOARA
FACULTY OF ECONOMICS AND BUSINESS ADMINISTRATION
Timişoara, 16 Pestalozzi Street, liana.son@feaa.uvt.ro, gratiela.carica@feaa.uvt.ro

Abstract:
The purpose of the paper is to analyse the European labour market outcomes under the impact of active and passive labour market policies. More specifically, the paper methodizes the main active and passive labour market policies and their role in reducing the level of unemployment. The policies that frame a more efficient unemployment insurance system are essential to increase security, while encouraging the unemployed to look for a job and to accept a job offer. The analysis is based on a set of specific labour market indicators and on applying the regression method. We found that high employment rates are generally associated with large expenses on active and passive labour market policies. The degree of influence and strong dependence between performance and policy labour market indicators are illustrated in various ways and discussed within the paper.

Key Words: *labour market policies, employment, labour productivity, job search, unemployment benefits*

JEL classification: *J08, J64, J65*

1. Introduction

Labour market policies represent public interventions within the labour market where the main activity of the participants is other than job search and where the attendance generally determines a change in the labour market status (Arpaia, Mourre, 2005). Specific labour market measures include basic interventions that secure temporary support for disadvantaged groups within the labour market, such as unemployed, vulnerable or at risk employees and inactive persons. The specific labour market policies and measures are classified according to the type of an activity and refer mainly to training, job switch or job rotation, direct job creation and uemployment benefits (Card et al., 2009).

The research performed within this paper, based on the critical review of literature, focuses on active and passive labour market policies, by analysing their impact upon the European labour market performance, defined through the level of employment or unemployment.

We thus analysed, through a set of specific labour market indicators and by applying the regression method, the main differences concerning active and passive labour market policy measures across EU Member States, by connecting different performance and policy indicators with outcome indicators and the overall EU labour market performance..

2. Active and passive labour market policies – literature review

Active labour market policies, unemployment benefits and employment protection legislation represent the most important elements of the European labour market

policies (Eichhorst, Konle-Seidl, 2005). On the one hand, they represent protection mechanisms against the specific labour market risks, which insure a certain income and employment protection, and, on the other hand, they have a major impact upon the labour market adjustment capacity to economic changes, mainly due to the fact that the institutional elements also affect the adapting strategies of economic agents (Venn, 2009). The insufficient adapting capacity of labour market generates a high persistent level of unemployment. Thus, a series of specific labour market policy measures are required in order to increase the adapting capacity of the European labour market.

Active and passive labour market policies refer to various categories, each having a different impact upon the European labour market performance. *Active labour market policies* mainly refer to the labour market integration of unemployed persons (Boone, van Ours, 2004). This type of policies includes various programmes, such as public employment services, training or employment subsidies. Heckman et al. (1999) highlights that active labour market programmes have a moderate impact upon the participant's employment opportunities. Card et al. (2009) reveals that job search assistance may have positive effects and that the employment subsidies for the private sector are usually more efficient than the specific public programmes, whereas training programmes can improve the employment opportunities for unemployed persons. Boone (2004) identified a significant effect of active labour market programmes, respectively that these programmes encourage workers to reduce their job search efforts and not to increase them. At the same time, Rovelli (2008) pointed out that what may be efficient for an individual unemployed, might not have the same effects upon the aggregated level of unemployment. The main categories of active labour market policies refer to public employment services, training programmes, such as institutional or vocational training, integrated training, apprentices support, as well as to job rotation, employment assistance and vocational rehabilitation of persons with low work ability, direct job creation and entrepreneurship programmes that encourage unemployed or inactive persons to set up their own businesses (Eurostat, 2006; European Commission, 2010).

Passive labour market policies mainly refer to *(i)* income support for the period without work, respectively to unemployment benefits granted to workers that comply with a series of criteria in order to benefit from unemployment benefit schemes, including the financial support ensured as a compensation for losing the salary due to fixed-term working arrangements, as well as to *(ii)* early retirement schemes, which facilitate total or partial retirement for older workers, having low possibilities to find a job. Both types of passive labour market policies have different and controversial effects upon the European labour market performance (Card et al., 2009).

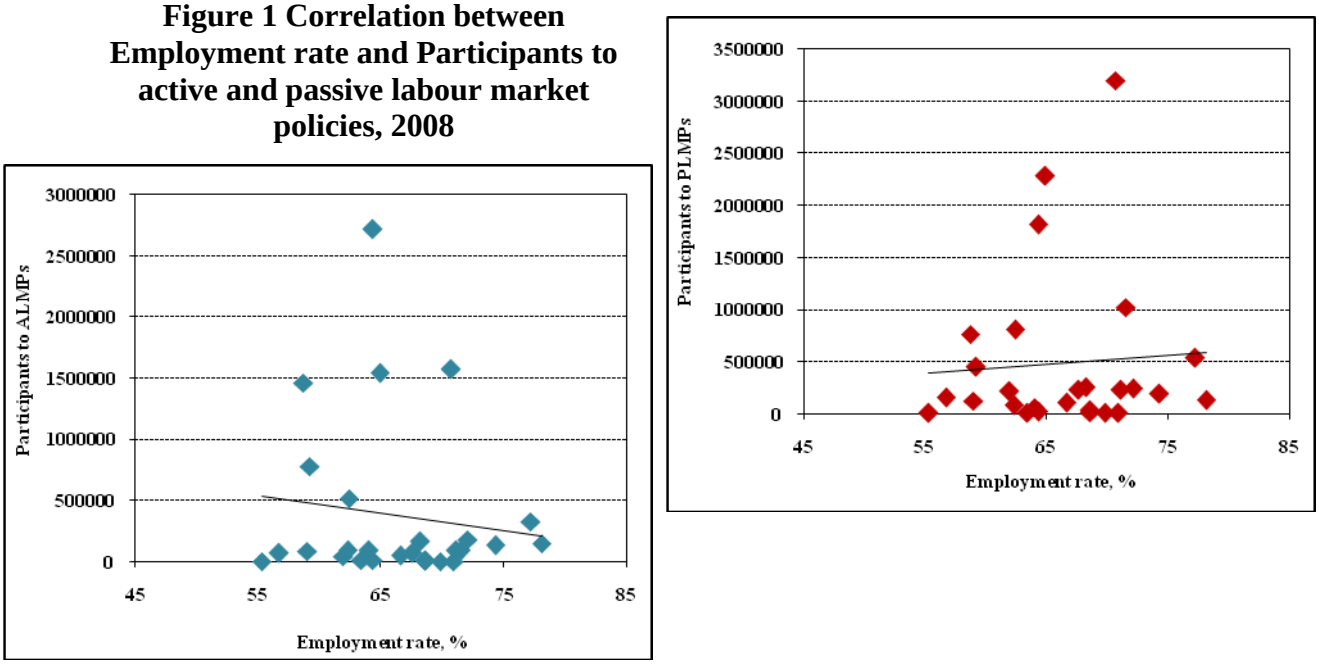
Several guidelines of these types of labour market policies refer to improving the compatibility between the labour market needs, respectively between labour demand and supply, as well as to promoting an increased coherence between macroeconomic, structural and employment policies and to improving labour quality and productivity.

3. A framework analysis of active and passive labour market policies impact upon the European labour market performance

In order to analyse the active and passive labour market policies and to assess their impact upon the European labour market performance, we used a specific methodology developed by the European Commission and available through LIME Assessment Framework, LAF Database, a specific database established by the Lisbon Methodology Working Group. At the same time, we used the regression method in order to establish to what extent the European labour market performance is influenced by active and

passive labour market policies. Thus, we obtained a series of results that point out different situations from one Member State to another by correlating the employment rate with total expenses on labour market policies for the EU Member States. Certain states with low percentage of GDP assigned for labour market policies also have low employment rates (Malta, Hungary, Romania, Greece and Slovakia), respectively high level of unemployment (especially for Slovakia), except for Spain that still has the highest unemployment rate, even if the percentage of GDP for expenses on labour market policies is high compared to other Member States (2.517% in 2008).

Figure 1 Correlation between Employment rate and Participants to active and passive labour market policies, 2008



Source: performed based on OECD and EUROSTAT data

Generous countries, with high expenses on labour market policies (especially Denmark, Austria and Netherlands), have registered high employment rates and the lowest unemployment rates. However, various Member States, which have assigned a small amount for the expenses on labour market policies, also registered low unemployment rates (especially United Kingdom, Cyprus, Slovenia and Czech Republic). At the same time, in several Member States, the activation to various programmes developed within the framework of active and passive labour market policies is decreasing and the impact of the attendance on outcome indicators is relatively low, pointed out also by the previous correlations.

The specific active and passive labour market policy indicators used by the LAF methodology in order to assess the European labour market performance are classified as: *(i) performance indicators* and *(ii) policy indicators*. These indicators are being analysed according to their significance (table 1).

In order to assess the performance of each specific indicator, the LAF methodology applies a general system based on continuous scores, which consists in standardizing the value of the considered indicator by the mean and the standardized deviation and multiplying it by ten, being described by the following relation:

$$Individual\ score\ for\ each\ indicator = \frac{Indicator\ values - EU15\ average}{Standard\ deviation} * 10$$

The aggregated score for each policy area is determined as a weighted average of the specific individual scores.

The scores range from +30 to -30: a score of 0 implies the indicator in question is the same as the EU15 weighted average, whereas a score of -10 implies the indicator is 1 standard deviation below the EU15 average.

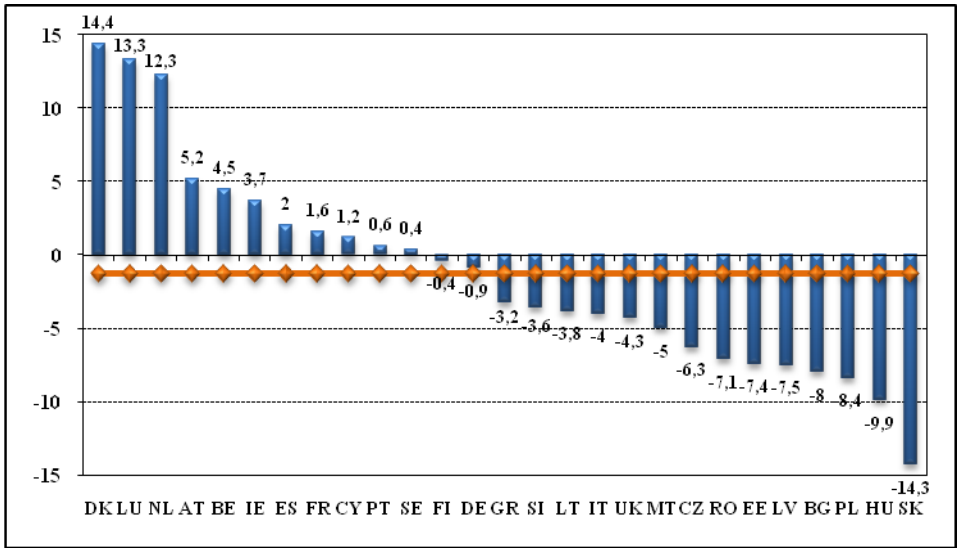
Table 1 Specific active and passive labour market policies indicators used by the LAF Methodology in order to assess the European labour market performance

	Source	Policy/ Performance indicators	Geographical coverage	Time coverage	Significance (high level)
Active LMP expenditure as % of GDP (+)	EMCO	Policy	20 SM	1999 – 2007	Good
Activation: Number of participants in LMP measures divided by the number of persons wanting to work (+)	EMCO	Policy	19 SM	2004 – 2007	Good
Active LMP expenditure per person wanting to work (+)	EMCO	Policy	22 MS	2004 - 2007	Good
Passive LMP expenditures as % of GDP (-)	EMCO	Policy	20 SM	2000 – 2007	Low
Passive LMP expenditures per person wanting to work (-)	EMCO	Policy	25 SM	2004 – 2007	Low
Employment service expenditure per person wanting to work (+)	EMCO	Policy	21 SM	2004 – 2007	Good
Proportion of the unemployed in education and training (+)	EMCO	Policy	20 SM	2000 - 2008	Good
Proportion of the inactive in education and training (+)	EMCO	Policy	24 SM	2000 – 2008	Good
Long-term unemployment rate (-)	EMCO	Performance	27 SM	1999 – 2008	Low
Youth unemployment ratio (-)	EMCO	Performance	27 SM	2000 – 2008	Low
Low-skilled employment rate (%) (+)	LFS	Performance	27 SM	1999 – 2008	Good
Ratio of active to passive LMP expenditures (+)	ECFIN	Policy	18 SM	2000 – 2007	Good
Regular activation in training (+)	EMCO	Policy	22 SM	2006 – 2007	Good

Source: European Commission (2008), „The LIME assessment framework (LAF)", *European Economy*, Occasional Papers no. 41, October 2008; LIME, LAF Methodology, LAF Maquette-ALMPs-12-09

The analysis of these types of indicators according to their statistical relevance allowed the identification of several major indicators, with significant results and effects that can be framed by the LAF methodology, in order to highlight the European labour market performance under the influence of various active and passive labour market measures.

Figure 2 Performance registered after implementing various active and passive labour market policies within the European Union, aggregated scores



Source: own calculation based on LAF Maquette-ALMPs-12-09 (LAF Database)

The implementation of active and passive labour market policies within the European Union has generated different performances for the European labour markets, 11 Member States registering very good and relatively good performances, whereas 16 Member States registered quite low performances. Thus, Denmark registered the highest performance after implementing several active and passive labour market policy measures and programmes (score: 14.4), followed by Luxembourg (13.3) and Netherlands (12.3), while Slovakia (-14.3), Hungary (-9.9) and Poland (-8.4) registered the lowest performance, compared to the EU-15 average.

The EU Member States that have registered very good performances after implementing active and passive labour market policies (with the highest aggregated score) are, in general, countries with flexible labour markets, such as Denmark, Netherlands and Austria. The New Member States of the European Union, countries from Central-Eastern Europe, such as Czech Republic, Estonia, Hungary, Lithuania, Bulgaria, Malta or Slovakia, have registered the lowest overall performance, even though some of these countries had high individual scores for the passive labour market policy indicators (for example, Bulgaria has registered good performances concerning the passive labour market policy expenditures per person wanting to work, passive labour market policies expenditures as a percentage of GDP and the ratio of active to passive labour market policies expenditures).

In Romania, the assessment of specific active and passive labour market indicators through the LAF methodology highlighted an overall negative evolution during 2000 – 2008, the lowest performance being largely due to the negative effects of several indicators, such as the active labour market policies expenditures, employment service expenditure per person wanting to work. The most significant negative effect was generated by the active labour market policies as a percentage of GDP that registered a very low level during the analysed period (0.1% compared to the EU average of 0.4% in 2007).

Romania is placed among the EU member states with the lowest performance after implementing different active and passive labour market policies, especially concerning the active labour market policy expenditures, employment service expenditure per person wanting to work, regular activation in training and the proportion of the unemployed in education and training.

4. Conclusion

The results of the comparative and impact analysis point out the fact that high employment rates within the European Union are in general associated with an increased level of expenses on active and passive labour market policies, but also with a large number of participants to various labour market programmes and with a lower degree of rigidity for labour market institutions.

The impact of specific labour market policies on its performance is very different across EU Member States. Active labour market policies have positive effects on labour market outcomes (especially on the level of employment), but the intensity and effectiveness of these policies vary across countries, according to different types of measures adopted and implemented and to cyclical labour market conditions. Within the analysis, certain types of active labour market programmes have had a positive impact on labour market performance. However, in several cases, these types of programmes have had no impact on improving the employment perspectives of the participants. Employment services are in general the most effective labour market interventions, with a lower cost than certain active labour market programmes.

Passive labour market policies, especially unemployment benefits, generally have an ambiguous impact on the overall labour market performance. On the one hand, these types of policies can increase employment rate, but on the other hand they can discourage the job search.

If we take into consideration the relation between unemployment benefits and other types of labour market policies, the results obtained reveal that the impact of generous unemployment benefits upon the level of unemployment can be mitigated by a higher level of expenses on active labour market policies, especially due to the fact that high expenses on these types of policies are generally associated with labour activation. At the same time, legal norms that intensify labour market rigidity or determine a decrease of labour demand generally have a negative impact on labour market outcomes and performance.

ACKNOWLEDGMENT

This paper is a result of the project POSDRU/88/1.5./S/55287 „Doctoral Programme in Economics at European Knowledge Standards (DOESEC)". This project is co-funded by the European Social Fund through The Sectorial Operational Programme for Human Resources Development 2007-2013, coordinated by The Bucharest Academy of Economic Studies in partnership with West University of Timisoara.

REFERENCES

1. Amuedo-Dorantes C., Serrano-Padial R. (2010), „Labour market flexibility and poverty dynamics", *Labour Economics*, issue 17: pp. 632-642.
2. Arpaia A., Mourre G. (2005), „Labour market institutions and labour market performance: A survey of the literature", European Commission, *Economic Papers*, no. 238, December 2005.
3. Biewen M., Steffes S. (2010), „Unemployment persistence: is there evidence for stigma effects?", Economics Letters, issue 106: pp. 188-198.
4. Bosch M., Maloney W. (2010), „Comparative analysis of labour market dynamics using Markov processes: An application to informality", *Labour Economics*, issue 17: pp. 621-631.

5. Boone J., van Ours J. (2006), „Modelling Financial Incentives to Get the Unemployed Back to Work", *Journal of Institutional and Theoretical Economics (JITE)*, Mohr Siebeck, Tübingen, vol. 127(2), pp. 227-252, June 2006.
6. Boeri T. (2009), „What Happened to European Unemployment?", *De Economist*, issue 157-2: pp. 215-228.
7. Boeri T. (2002), „Let Social Policy Models Compete and Europe Will Win", Paper presented at a Conference hosted by the Kennedy School of Government, Harvard University, April 11–12, 2002.
8. EUROSTAT Database, National Accounts, Population and Social Conditions, Labour Market.
9. European Commission, LIME Assessment Framework Database – LAF Database.
10. Jimeno J., Rodrìguez-Palenzuela D. (2003), „Youth Unemployment in the OECD: Demographic Shifts", *Labour market Institutions and Macroeconomic Shocks*, ENEPRI Working Paper no. 19.
11. Kluve J. (2010), „The effectiveness of European active labour market programs", *Labour Economics*, 10.1016/j.labeco.2010.02.004.
12. Mourre G. (2002), „Did the pattern of aggregate employment growth change in the euro area in the late 1990s?", *Applied Economics*, no. 38, pp. 1783-1807, August 2002.
13. Nickell S. J., Nunziata L., Ochel W. (2005), „Unemployment in the OECD since the 1960s. What do we know", *The Economic Journal*, Vol. 115, pp. 1-27.
14. OECD (2010), Employment Database, Labour market policies and institutions.
15. Phelps E. (1992), „A Review of Unemployment", *Journal of Economic Literature*, Vol. 30, No. 3, pp. 1476-1490.
16. Pries M., Rogerson R. (2009), „Search frictions and labour market participation", *European Economic Review*, issue 53: pp. 568-587.
17. Rovelli R., Bruno R. (2008), „Labour Market Policies, Institutions and Employment Rates in the EU-27", *Institute for the Study of Labour*, IZA Discussion Paper no. 3502, May 2008.
18. Solow R., Stiglitz J. (1968), „Output, Employment and Wages in the Short Run", *The Quarterly Journal of Economics*, Vol. 82, No. 4, pp. 537-560.
19. Venn D. (2009), „Legislation, collective bargaining and enforcement: Updating the OECD employment protection indicators", OECD Social, Employment and Migration Working Papers No. 89.
20. World Bank (2010), Doing Business Database, Employing Workers.