

(Pseudo-)Comments on:  
“Flexicurity – The Danish Case” by Torben M. Andersen  
“Labour Market Segmentation: Spain and Beyond” by Tito Boeri

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Banco de España and International Monetary Fund, “High-Level Seminar on Labor Market Experiences: Towards More Efficient Labor Markets”, Madrid, 11 May 2010

# 1. Introduction

Rather than discussing Torben's and Tito's presentations on Flexicurity and Dualism, I am going to discuss the Spanish labor market within the frameworks that they use (sorry!)

## Outline:

- ▶ Active Labor Market Policies (ALMP)
- ▶ Unemployment Benefits (UB)
- ▶ Dualism:
  - ▶ Effects
  - ▶ Causes
  - ▶ Proposals
- ▶ Labor reform:
  - ▶ Proposals
  - ▶ Status
  - ▶ Political economy

## 2. Active labor market policies

- ▶ Denmark before ALMP reform (1995):
  - ▶ Generous UB led to long unemployment spells
  - ▶ Low employment protection (EPL) fed flow into unemployment
  - ▶ High unemployment rate (10% in 1994), same as Euro area
- ▶ **Lesson 1:** ALMP reform was crucial, in addition to low EPL and generous UB, for achieving low unemployment
- ▶ **Lesson 2:** We should consider the effects of all labor market institutions jointly, given complementarities among them
- ▶ There is much debate in the literature about whether/which ALMP work (micro vs. macro, short-run vs. long-run,...)
- ▶ I believe ALMP do not work well in Spain, but I leave that discussion for Session 3 of this conference

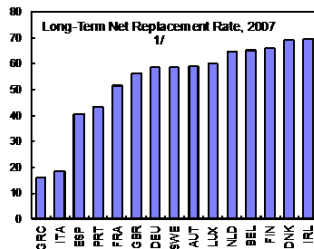
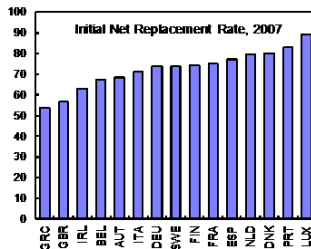
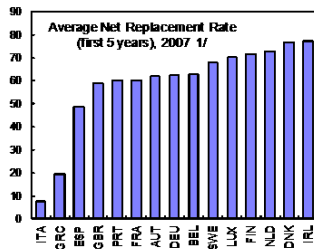
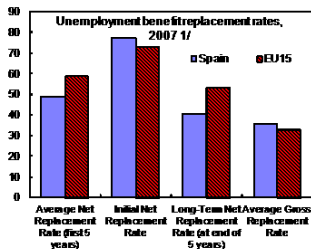
### 3. Unemployment benefits

- ▶ Theory and evidence (e.g. Bassanini-Duval, 2006) show that UB raise unemployment rates, via both replacement rates and benefit duration
- ▶ The same is true for unemployment duration (Bover-Arellano-Bentolila, 2002; Arranz-Muñoz Bullón-Muro, 2009)
- ▶ So, choices along the tradeoff between their welfare-enhancing insurance effects and their negative unemployment effects should determine the optimal level of UB

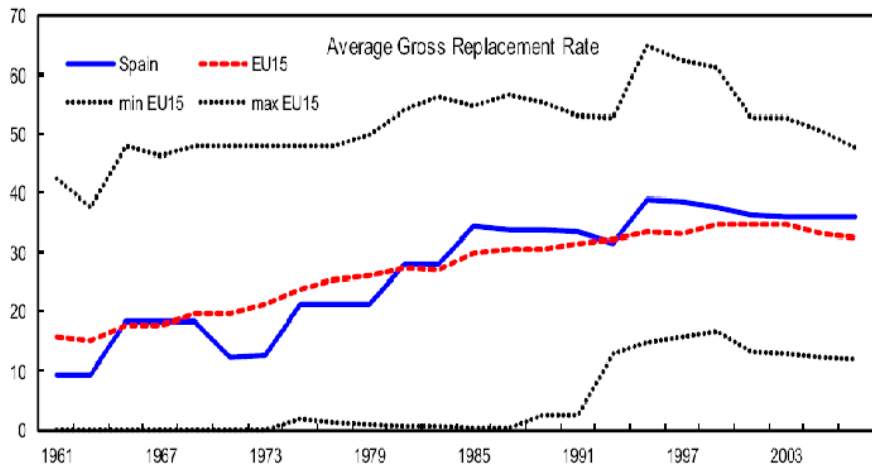
### 3. Unemployment benefits in Spain

From Jaumotte (2010, this conference)

Figure 7. Spain and EU15: Unemployment Benefit Replacement Rates



### 3. Unemployment benefits in Spain



Source: OECD.

1/ Includes social assistance.

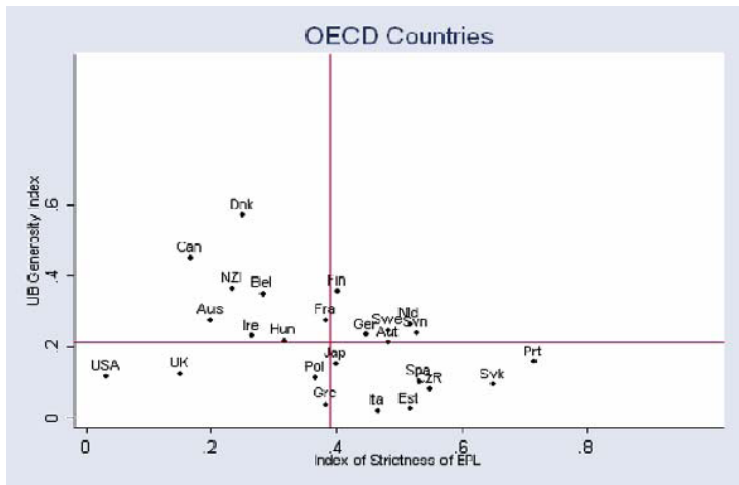
### 3. Unemployment benefits in Spain

UB generosity:

- ▶ Average gross replacement rate is slightly above the EU-15 mean
- ▶ Net benefits appear relatively generous at the beginning of spells but stingy in the medium run
- ▶ Temporary employment (EPL) reduces entitlement to UB. So picture changes once actual coverage is taken into account (another complementarity between labor market institutions):

### 3. The Flexicurity locus

Boeri-Conde Ruiz-Galasso (2007): [Replacement rate  $\times$  UB coverage]  
vs. [Strictness of EPL for regular contracts]



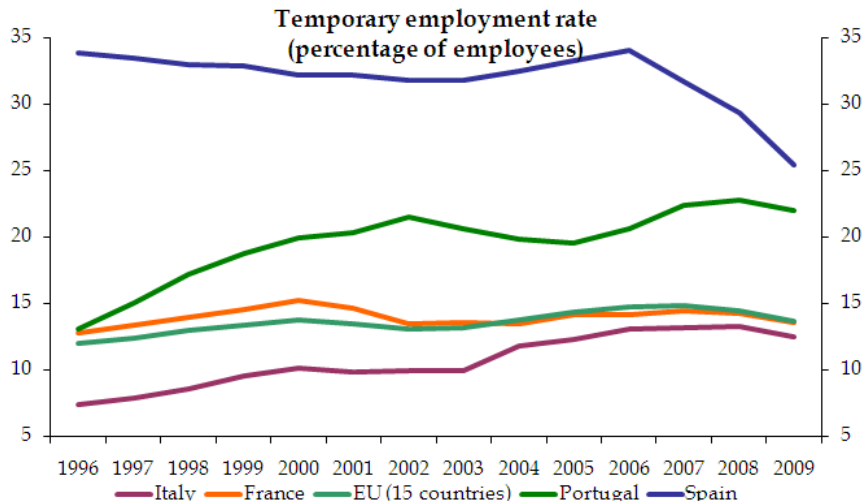


### 3. Unemployment benefits in Spain

Current situation:

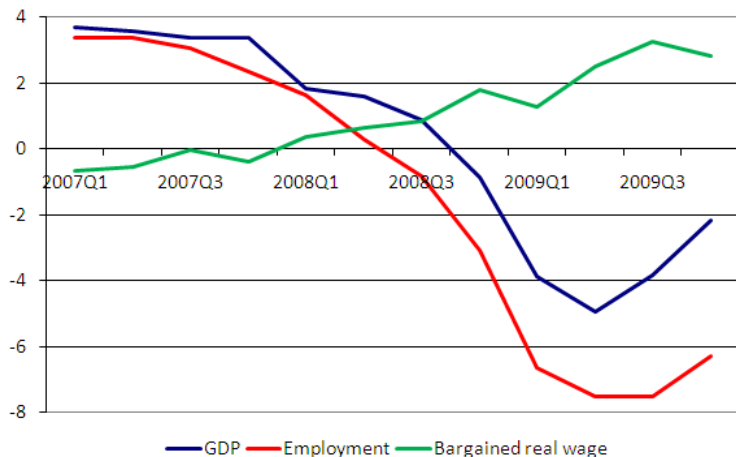
- ▶ UA has been temporarily extended for 6 extra months (€420)
- ▶ UB are not on the negotiating table (last reform: 1992/93)
- ▶ A proposal: *Really* link UB to (improved) activation

### 3. Dualism in Spain: Temporary rate



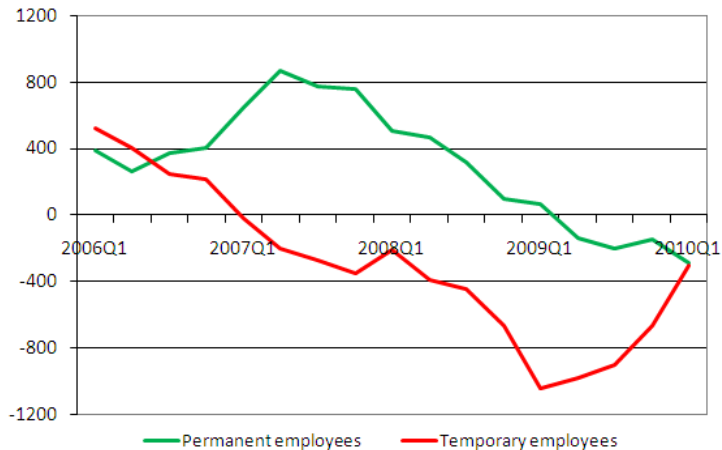
### 3. Dualism in Spain: Effects

Response to the Great Recession (real wages w/ GDP deflator):



### 3. Dualism in Spain: Effects

Disproportionately borne by temporary employees:  
(change on a year before, thousands)

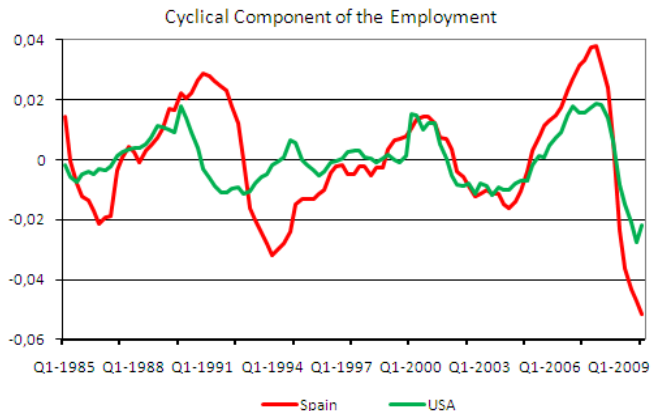


### 3. Dualism in Spain: Effects

- ▶ The Churn (2008):
  - ▶ 16.6 m. contracts  $\Rightarrow$  0.76 contracts/employee
  - ▶ Very short duration: 5 m.  $\leq$  30 days, 2.7 m.  $\leq$  7 days
  - ▶ Very low conversion rate to perm.: 5%; below 8% since 1994
  - ▶ SP 4.8% pers. wrk. age/month, US 5.4%, FR 1.8%
- ▶ Volatility: Highest Okun's law coefficient (employment) in the OECD: 1.67 vs. UK 1.46, US 0.96 (Jaumotte, 2010; also Boeri, 2010)

### 3. Dualism in Spain: Effects

Employment is twice as volatile in Spain as in the US:  
(Standard deviation: SP 18.8%, US 9.4%)



### 3. Dualism in Spain: Effects

- ▶ Individuals: uncertainty, scarring - 15-20% lower wages once in permanent contracts (García Pérez-Rebollo, 2010)
- ▶ Low productivity growth: TFP growth (2005-2008) =  $-0.36\%$ 
  - ▶ Training (Boeri, 2010) and effort (Dolado-Stucchi, 2008), technology adoption based on low-skill labor (Dolado-Jansen-Jimeno, 2009; Bentolila-Dolado-Jimeno, 2009)
- ▶ Interaction with wage setting: Buffer for permanent employees (Bentolila-Dolado, 1994) ( $\Rightarrow$  Session 2 of this conference)
- ▶ So: Competitiveness loss, **the immediate challenge** (Blanchard, 2007)
  - ▶ Unit labor costs vis-à-vis Euro area since 1999:1 (2009): 9.3%, 17.9% in manufacturing
  - ▶ Current Account deficit still 5.4% of GDP

### 3. Dualism in Spain: Causes

- ▶ Industry structure (but employment share in Agriculture, Construction, Real Estate, and Hotels/Restaurants same as in Portugal and Greece, 35%, with lower temp rate)
- ▶ Gap between permanent and temporary firing costs:
  - ▶ Temporary: 0/8 days per year of service (54% of dismissals)
  - ▶ Permanent: 45 days (disciplinary: without going to court) (33% dismissals)
  - ▶ Permanent with 33 days (9% stock) (dismissals at 45 days)
- ▶ Differential unemployment rate increase in Great Recession between France and Spain (similar institutions): 37.5% explained by gap (Bentolila-Cahuc-Dolado-Le Barbanchon, 2010) (see also Costain-Jimeno-Thomas, 2010)
- ▶ Consistent with international evidence in Nunziata-Staffolani (2007) and Jaumotte (2010)



## 4. Labor reform: Proposals

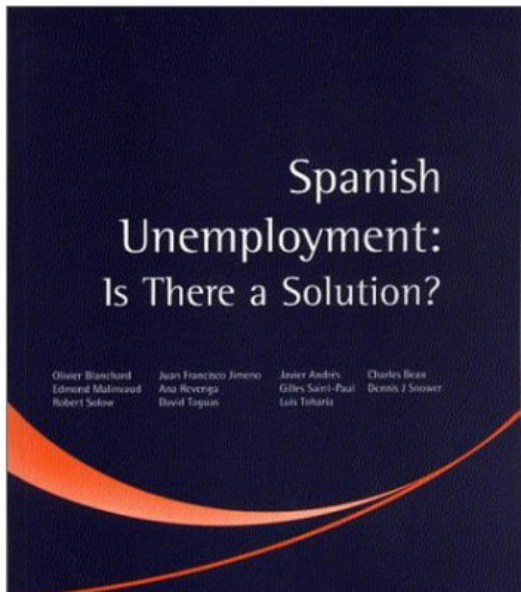
“A Proposal to Restart the Spanish Labor Market” (100 academic economists) (2009):\*

- ▶ Suppress temporary contracts (except for temporary replacement of employees)
- ▶ Single contract with severance pay smoothly increasing with seniority:
  - ▶ Gradual increase in marginal cost (e.g. 2 days per year)
  - ▶ Start above current severance for temporary jobs and end below 45 days (e.g. 12-36 days)
  - ▶ Average severance pay will depend on dismissal probabilities
  - ▶ Job durations increase significantly (García Pérez, 2010)
- ▶ Related to proposals for France (Blanchard-Tirole, 2003; Cahuc-Kramarz, 2004) and Italy (Boeri-Garibaldi, 2008; P. Ichino, 2009)

\*Also contains proposals on UB, ALMP, Collective bargaining regulation

## 4. Labor reform: Proposals

Remember me? (1995)



Olivier Blanchard  
Edmond Malinvaud  
Robert Solow

Juan Francisco Jimeno  
Ana Revenga  
David Tagua

Javier Andrés  
Gilles Saint-Paul  
Luis Tolosa

Charles Bean  
Dennis J. Snower

## 4. Labor reform: What's on the table

[Negotiations between Government, unions, and employers' association]

- ▶ Temporary contracts: Minor tinkering with their uses
- ▶ Permanent contracts: Severance pay for disciplinary reasons set at 33 days, convert part of severance pay into a fund ("Austrian model"), public **subsidy** to severance pay
- ▶ Part-time jobs: **Subsidize** permanent contracts with preset schedule
- ▶ Hiring **subsidies**: focus on youth and over 45 y.o. workers
- ▶ Employment services: Allow private companies to operate
- ▶ Short-time work (*Kurzarbeit*): Partial **income replacement**

Falls short, **costly budgetwise** (11.2% deficit), may be counterproductive (depending on design), could prevent *real* reform

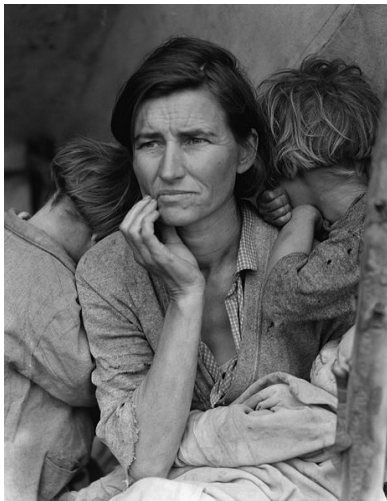
## 4. Labor reform: Political economy

- ▶ Political viability (Saint-Paul, 1993,2002; Dolado-Felgueroso-Jansen, 2010):
  - ▶ Temporary contracts supported by both unions and employers
  - ▶ *Status-quo* bias: Median labor union member is Permanent/Male/55-64 y.o./11-20 yr. tenure/Large firm
  - ▶ Exposure: 99.3% of job losses correspond to non-union members
  - ▶ Reform fatigue: Too many two-tier, incremental reforms (1984, 1992, 1994, 1997, 2002)
- ▶ Persistence of old paradigm...
  - ▶ Protection of the breadwinner's job
  - ▶ Family networks (Algan-Cahuc, 2007, Bentolila-Ichino, 2008)
  - ▶ Low geographical mobility
  - ▶ Low trust, low enforcement (underground economy 20% GDP)

...increasingly under strain from globalization –openness, immigration– & skill-biased technological progress, enhanced by EMU (Bertola, 2010)

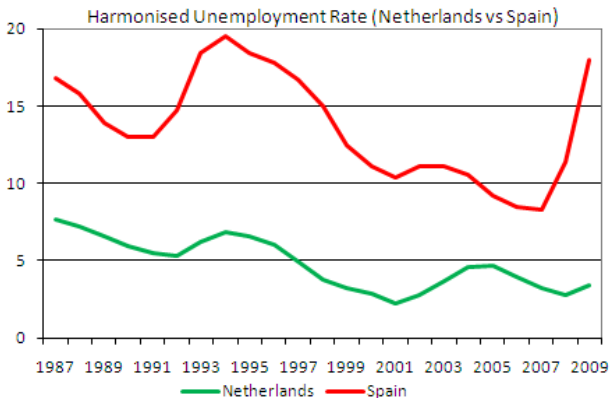
## 5. A grave danger

Very high unemployment for a very long time...



## 5. A grave danger

... but this is not inevitable!



Thank you  
for your attention!