

RIETI-IZA World of Labor Policy Symposium

Reforming Labor Market Institutions to Promote Elderly Employment

Handout



Juan F. JIMENO

Head of the Research Division, the Bank of Spain / Research Fellow, IZA

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Research Institute of Economy, Trade and Industry (RIETI)
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What/How Dismissal Regulation Affects the Elderly Employment and Youth Employment

Juan F. Jimeno
DG Economics, Statistics and Research

RIETI/IZA World of Labor Policy Symposium: Reforming Labor Market Institutions to Promote Elderly Employment

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Warning



The opinions and analyses in this presentation are the responsibility of the author and, therefore, do not necessarily coincide with those of the *Banco de España* or the *Eurosystem*.



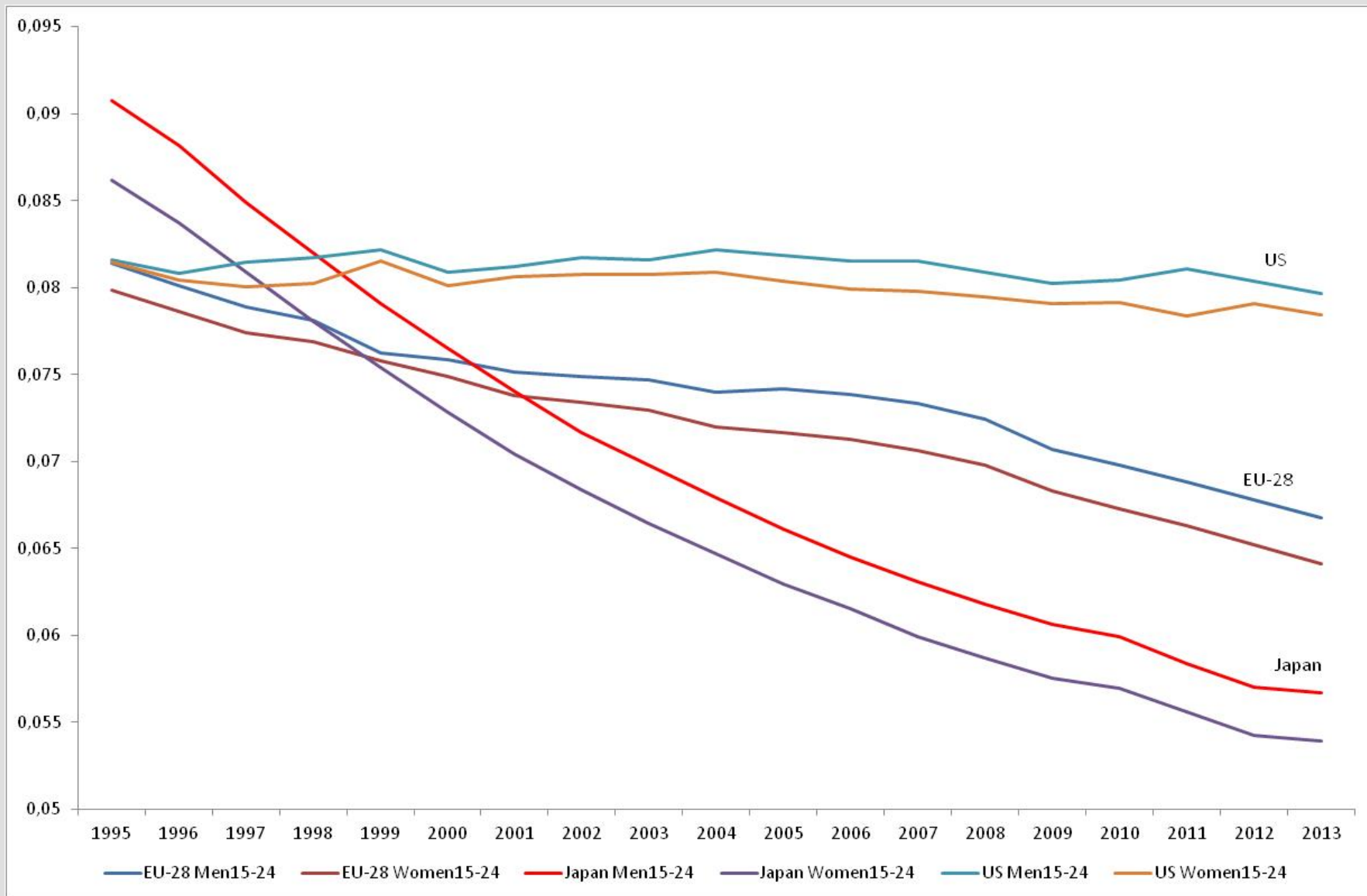
- **Facts**
 - *Demographics*
 - *Employment/unemployment rates of older and young workers*
 - *Worker flows by age in the EU during the Great Recession*

- **Determinants of older workers employment/non-employment**
 - ✓ *Flows from employment to non-employment*
 - ✓ *Flows from non-employment to employment*

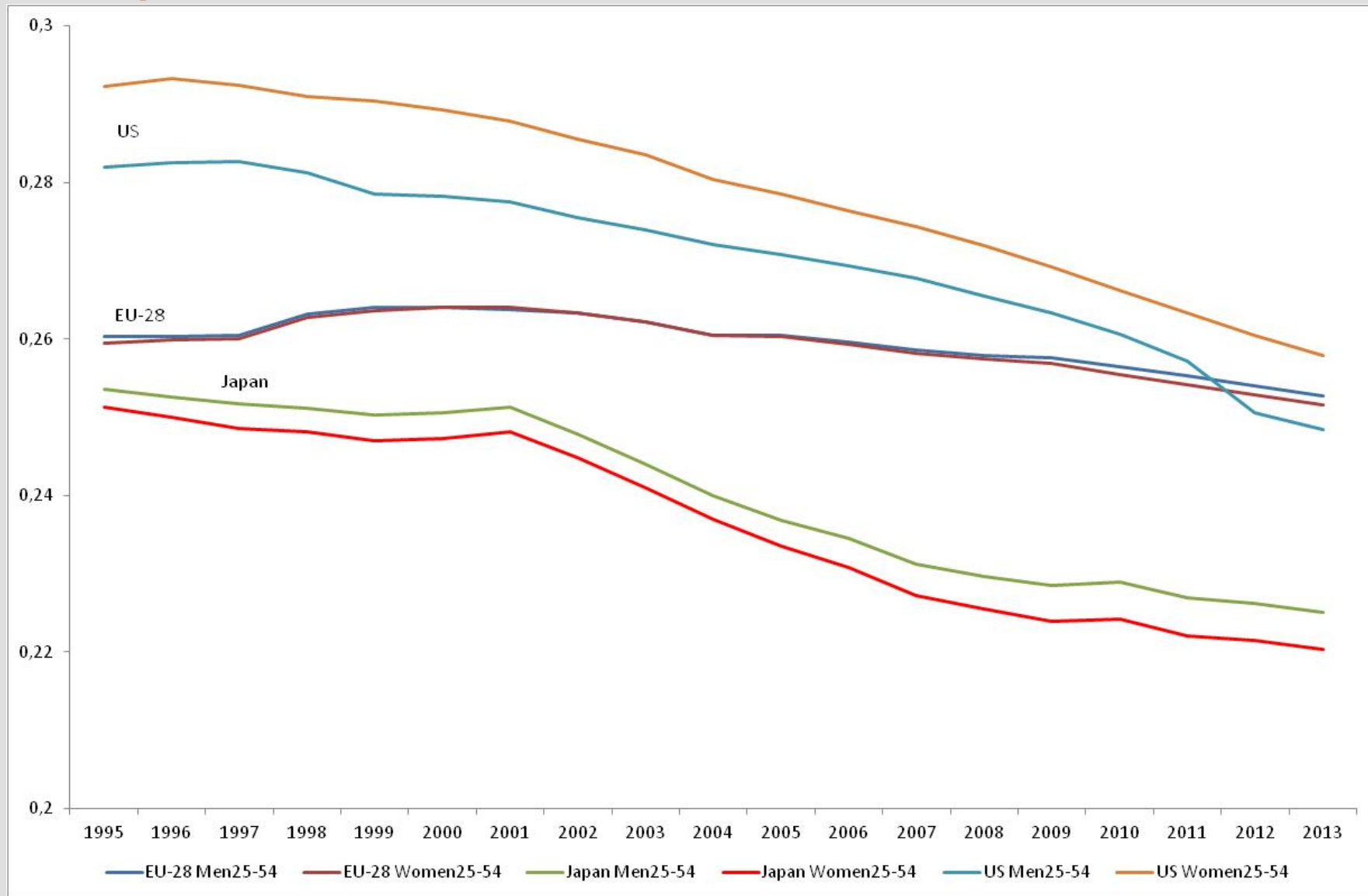
- **Policy responses (focus on older workers)**
 - *Labour market reforms*
 - *Make Employment Protection Legislation more neutral*
 - *Reduce soft-landing schemes towards retirement*
 - *Get wages closer to productivity (reduce seniority-based pay systems)*
 - *Avoid measures inspired by the “lump of labour fallacy”*
 - *Reduce reservation wages of older workers*
 - *Investment in skills*
 - *Pension reforms*

- **Concluding remarks**

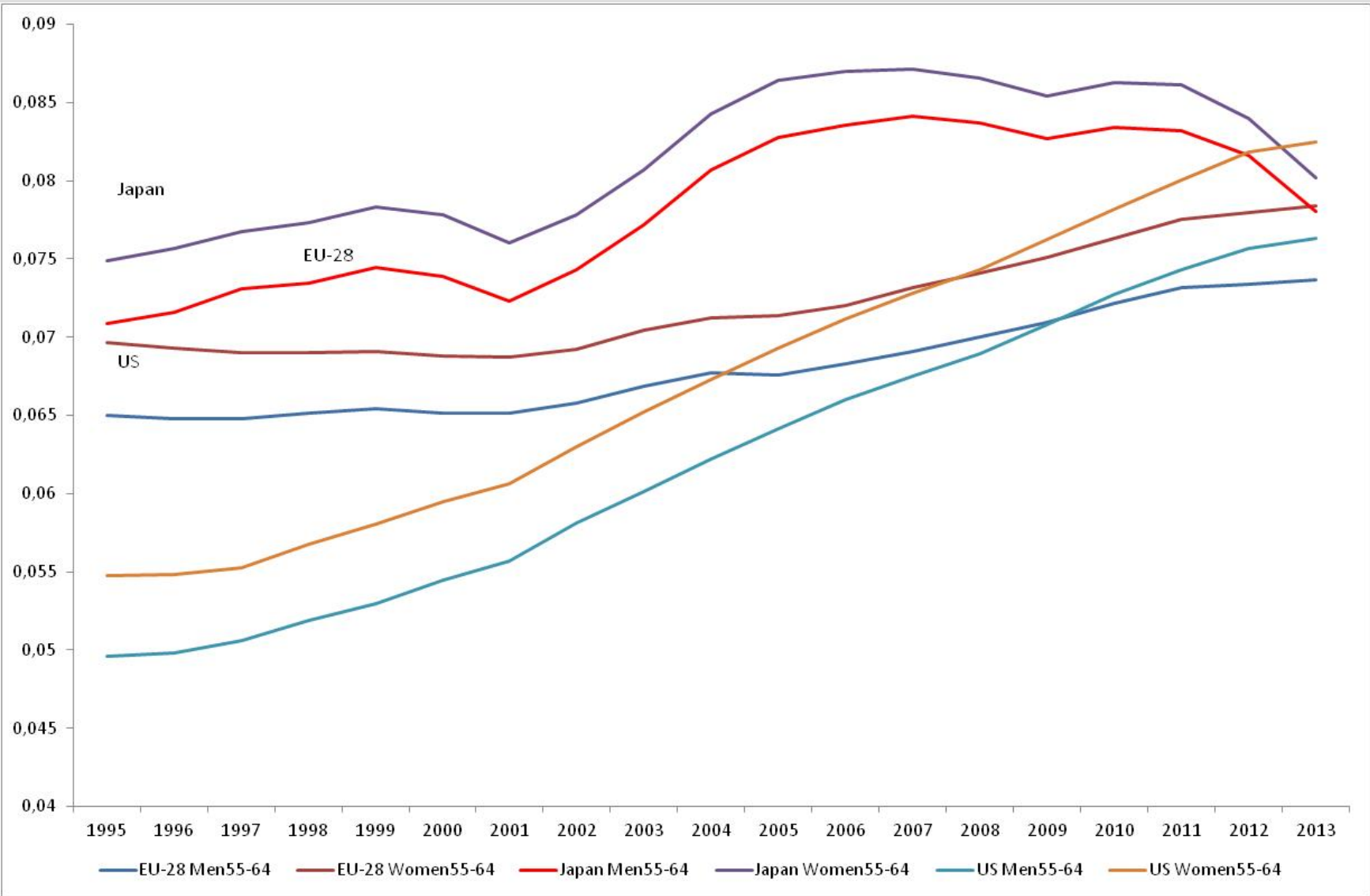
Demographics: Youth Population/Total Population



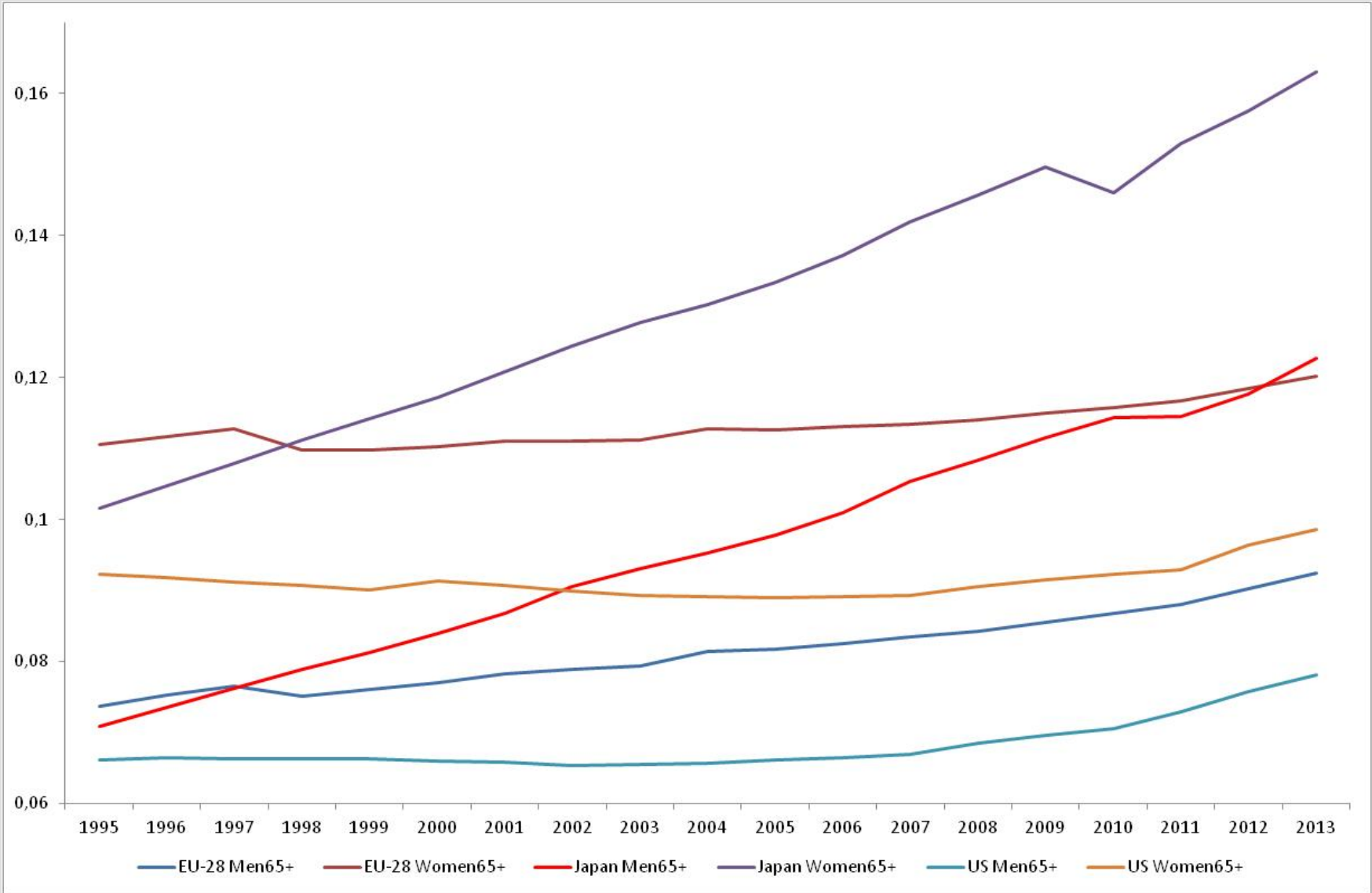
Demographics: Prime-Age Population/Total Population



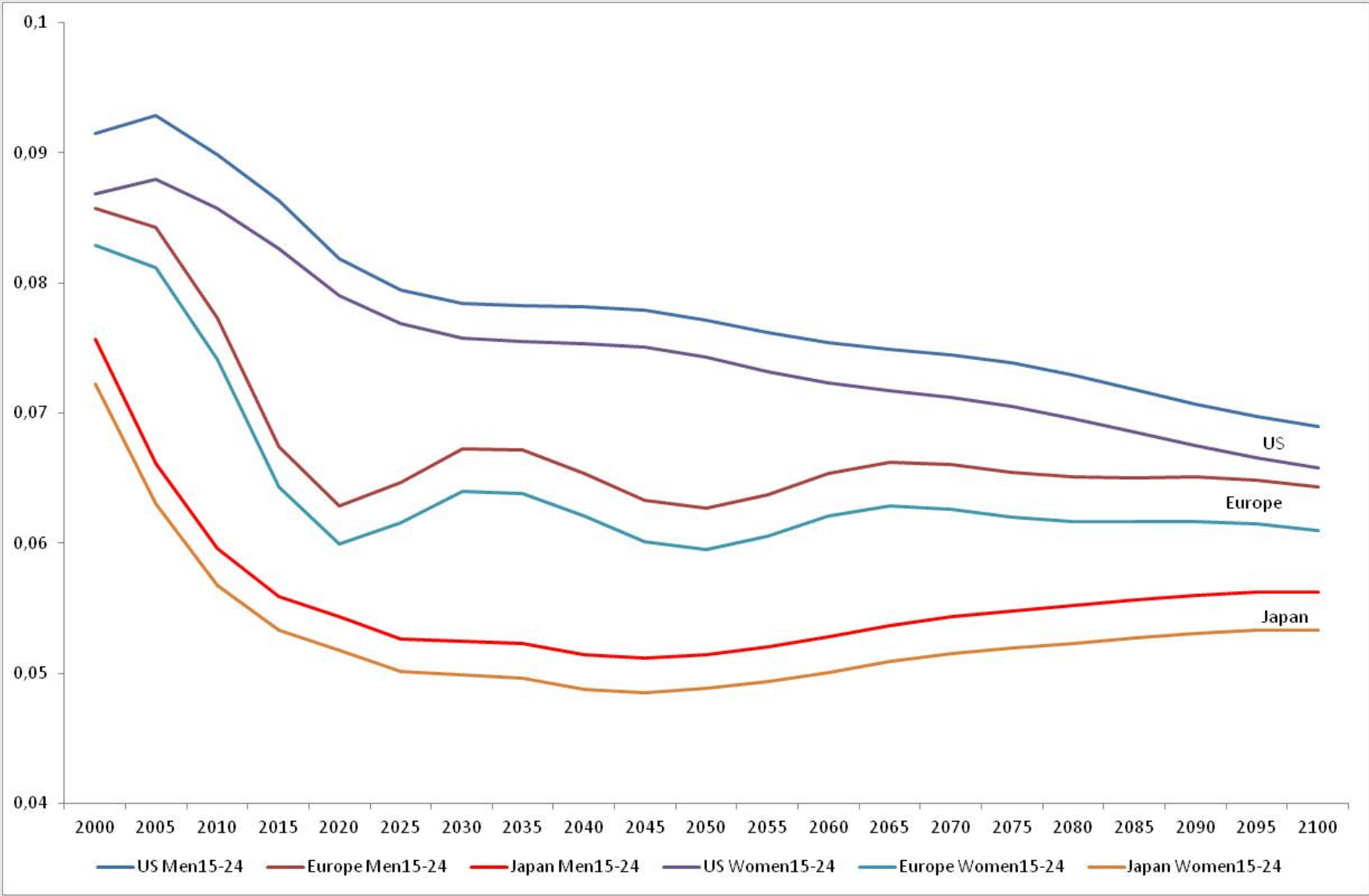
Demographics: Older Population (I) /Total Population



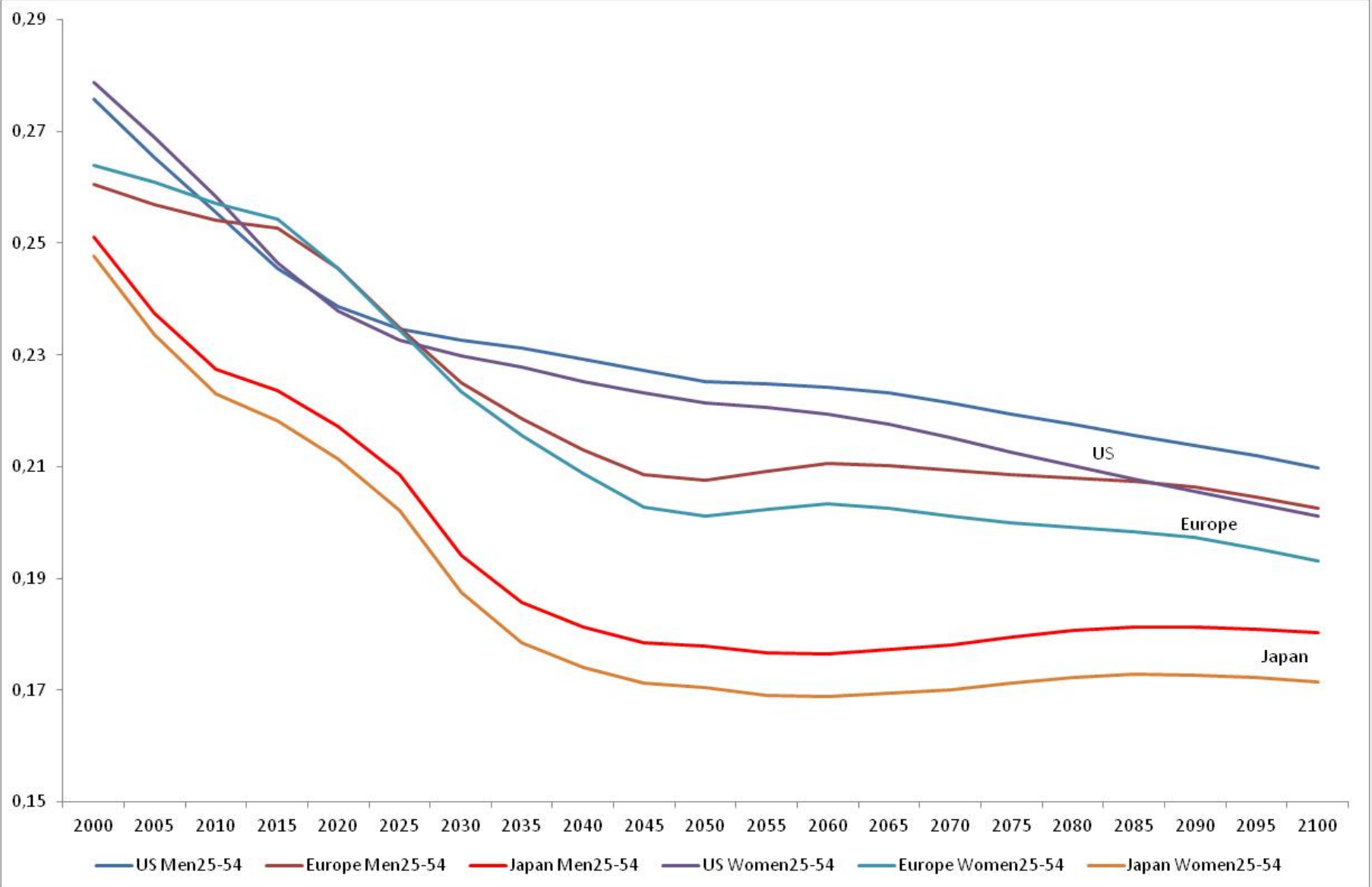
Demographics: Older Population (II) /Total Population



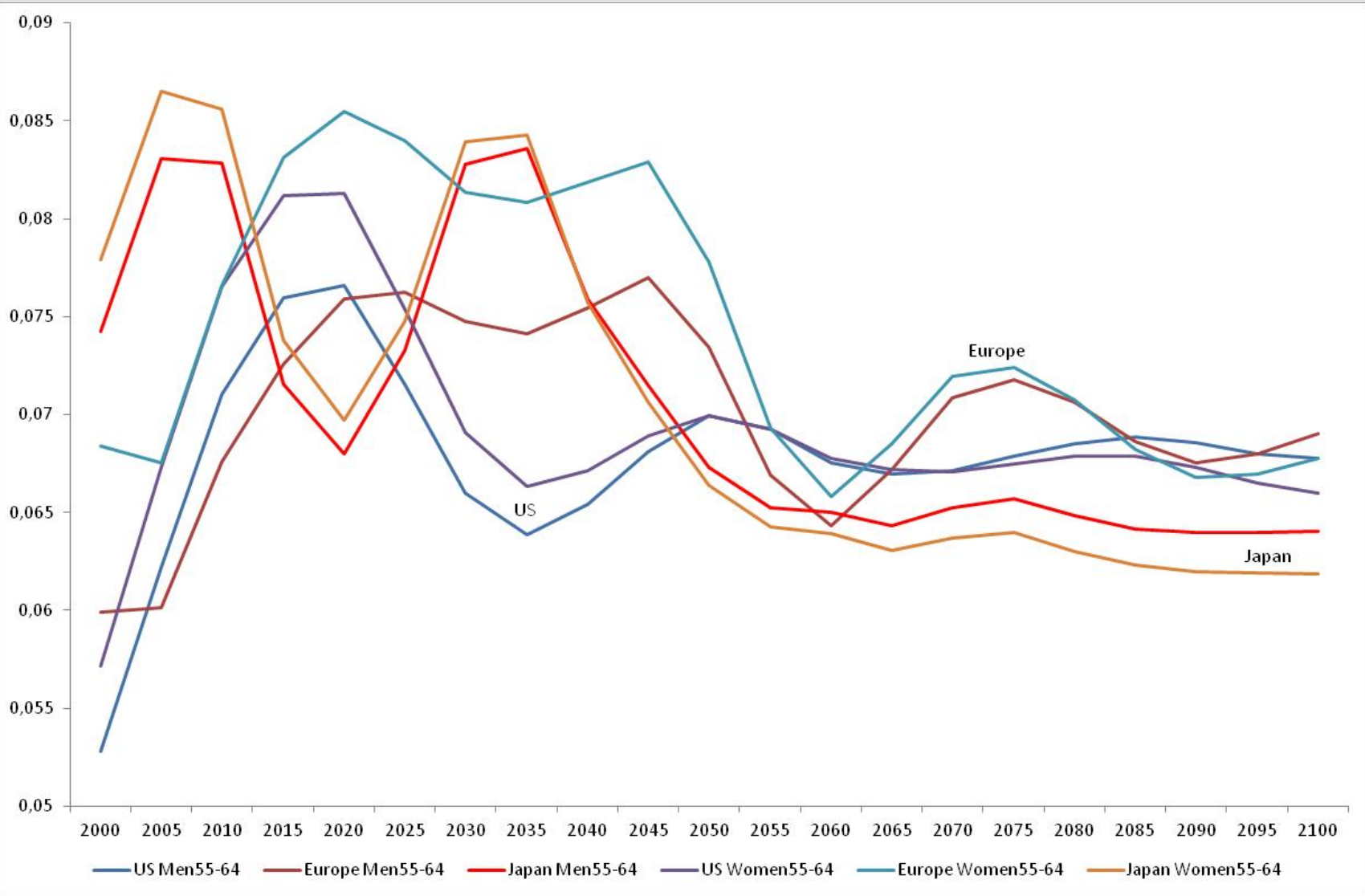
Demographics: Looking ahead-Youth as % Total Pop



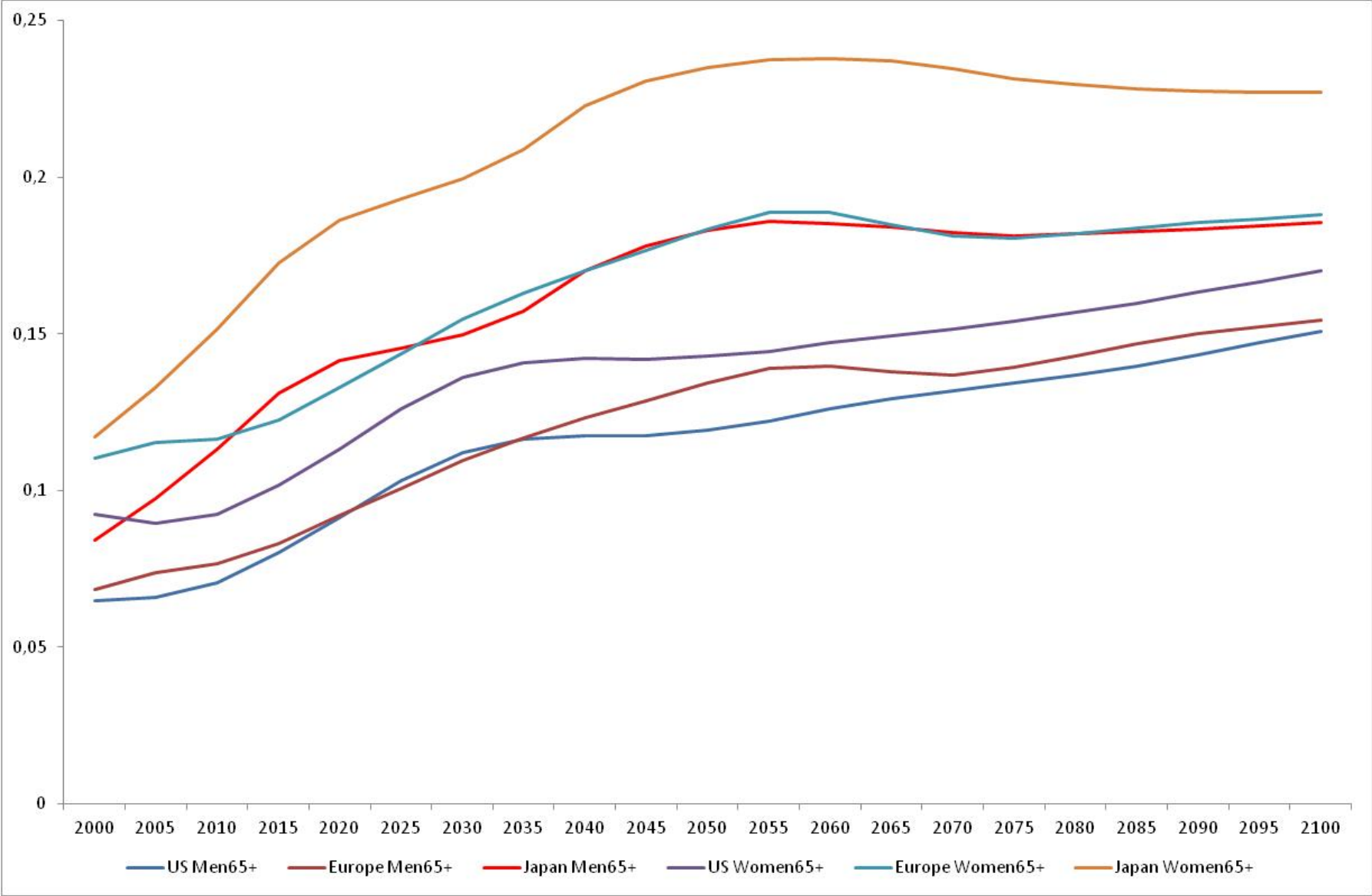
Demographics: Looking ahead-Adults as % Total Pop



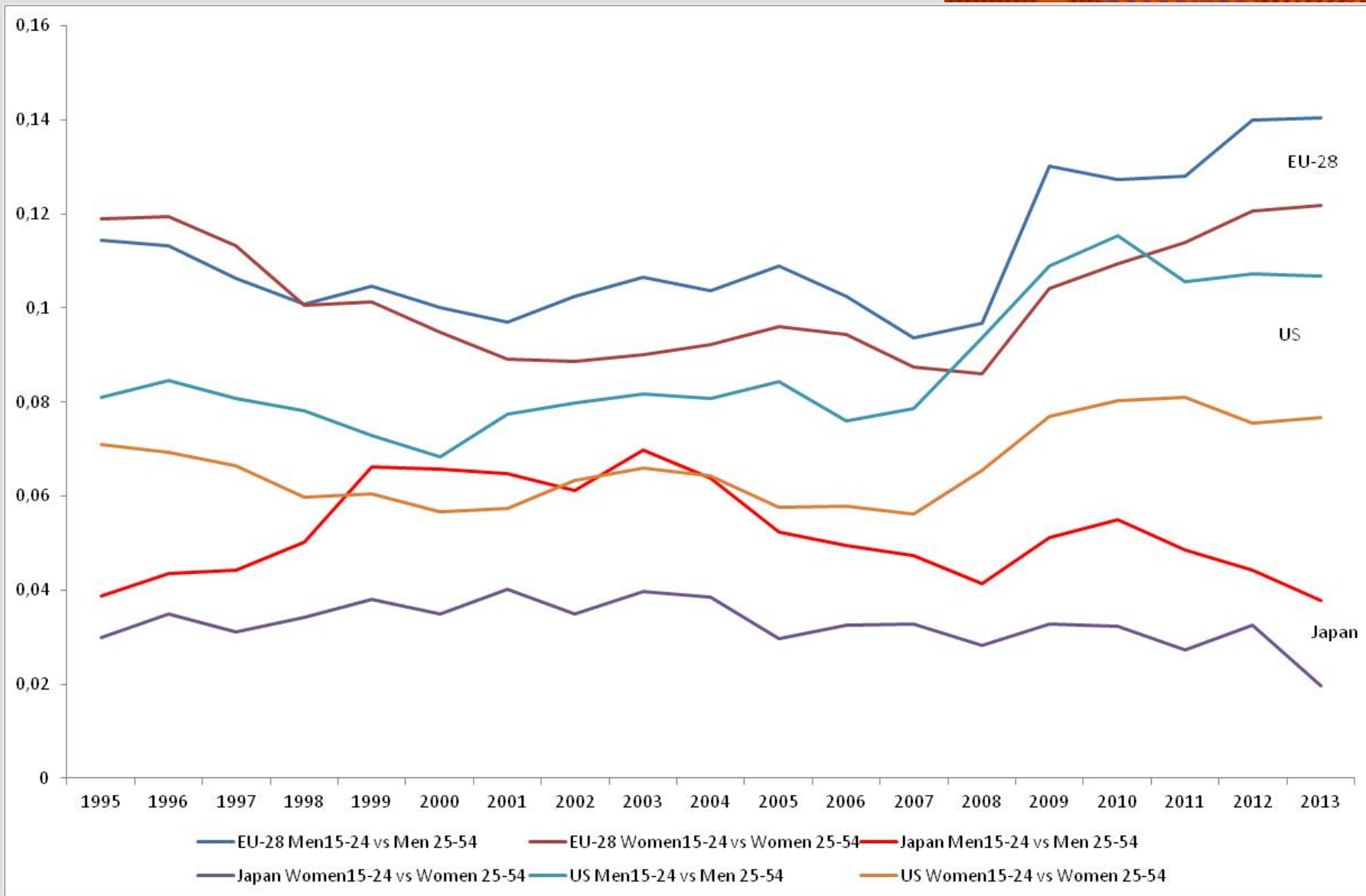
Demographics: Looking ahead- Older Workers as % Total Pop



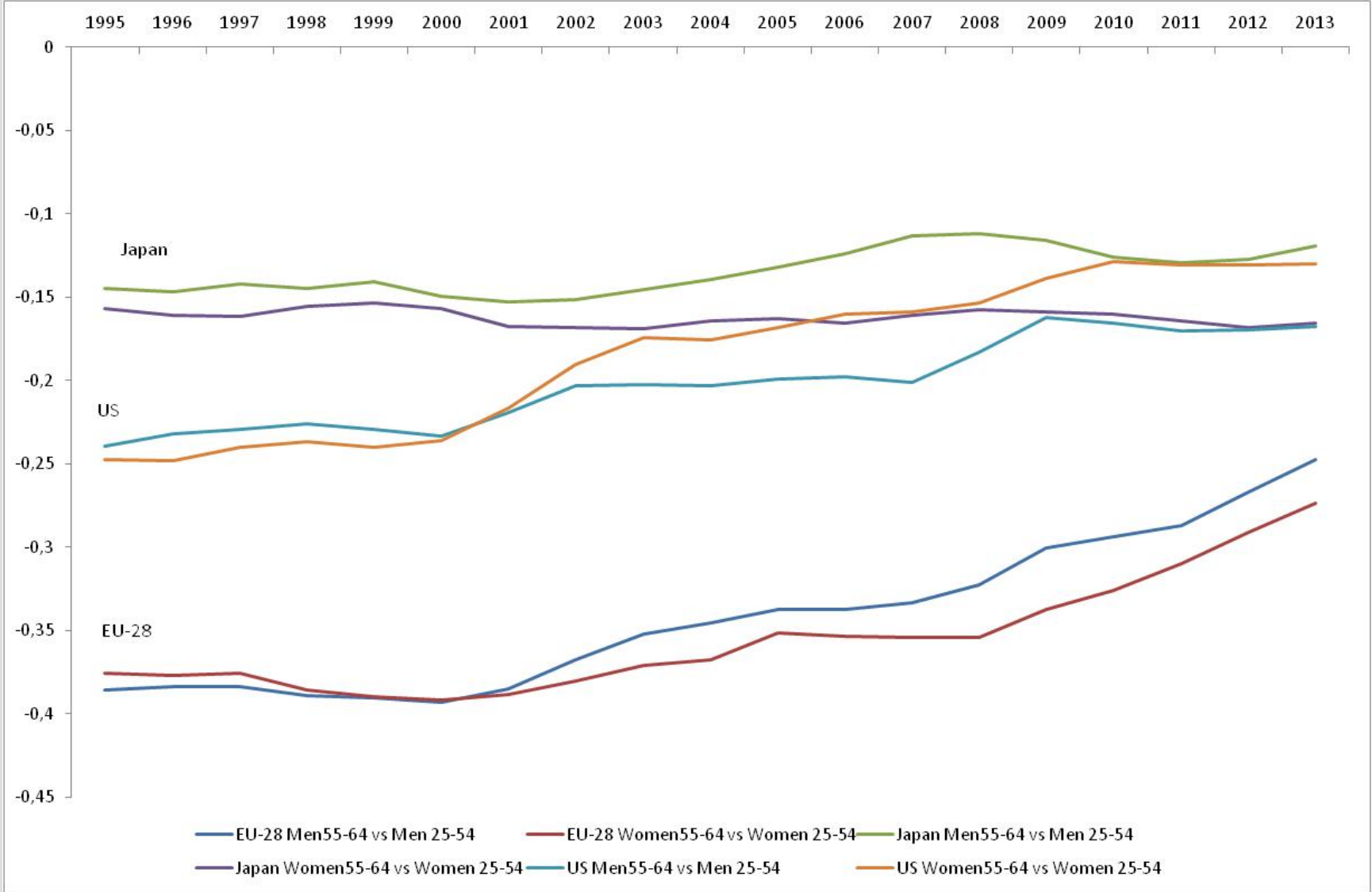
Demographics: Looking ahead- Older Workers as % Total Pop



Youth unemployment rate



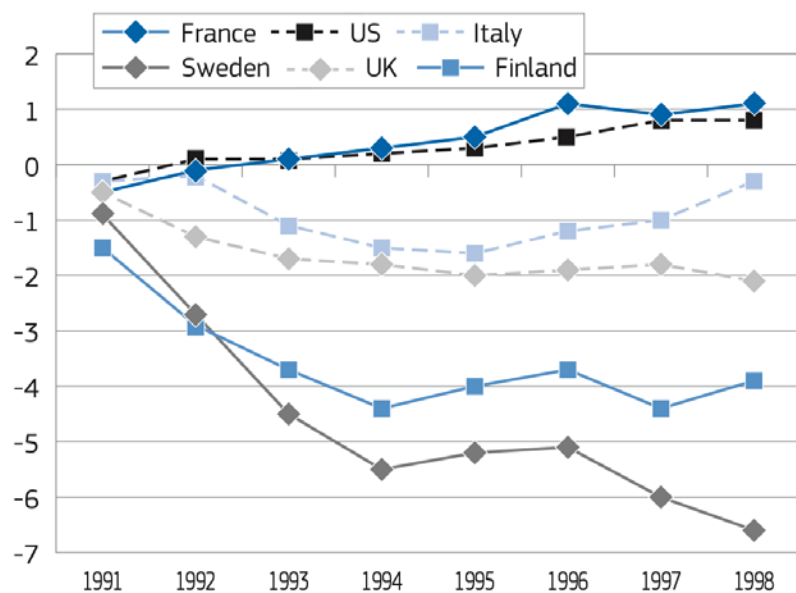
Employment rate (older workers)



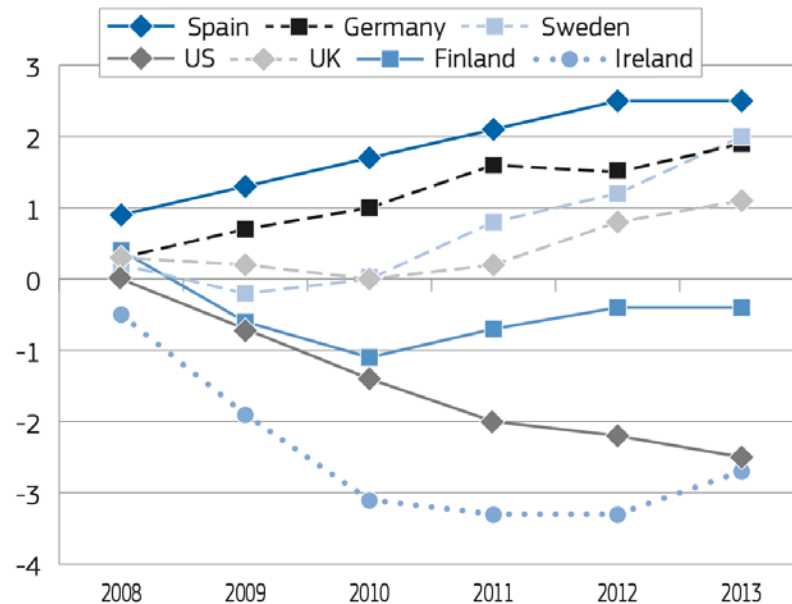
Participation rates in the EU during two crisis



Chart 14: Activity rate (15–64) compared to 1990 and 2007 levels, for selected countries, in pps



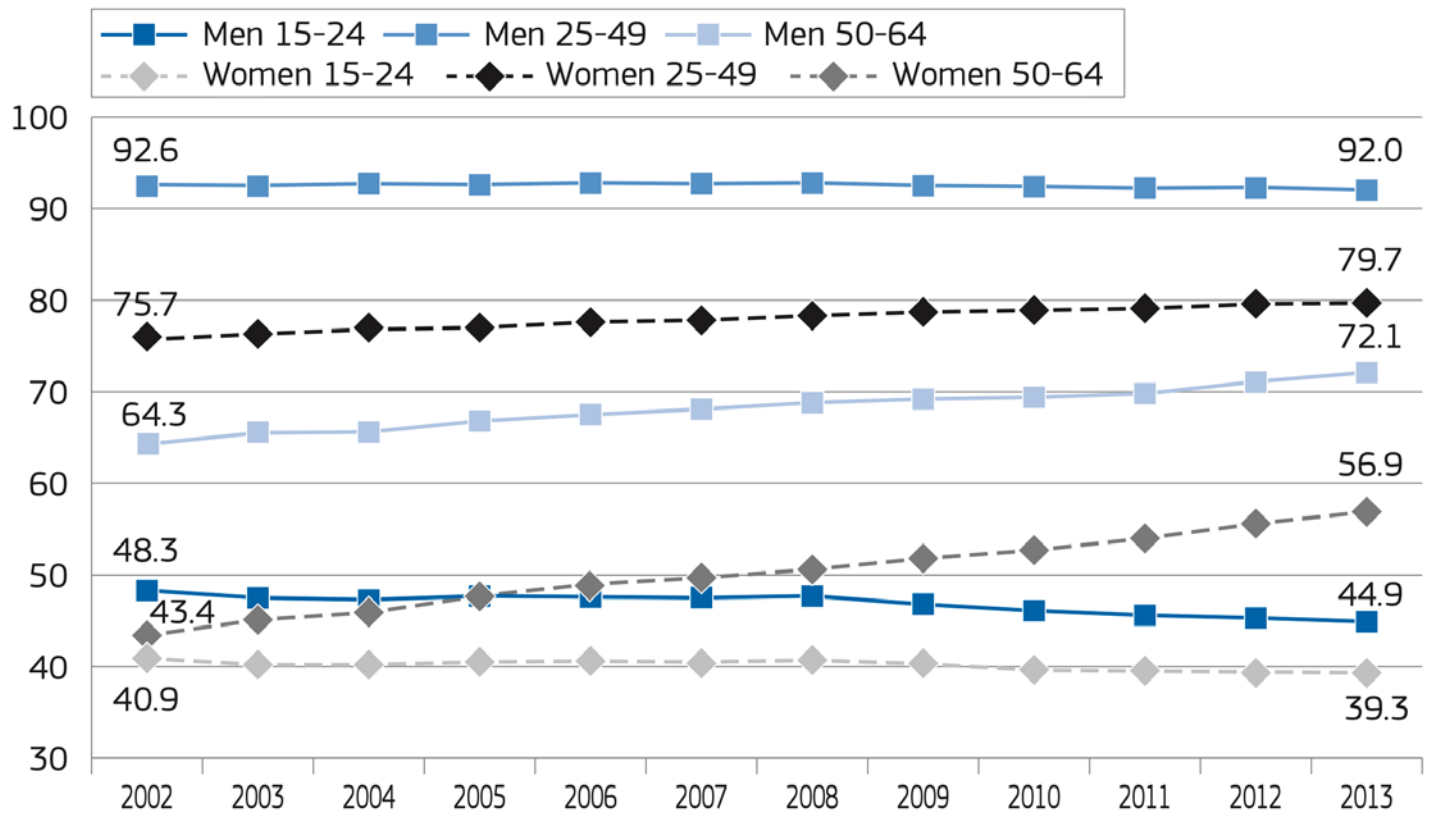
Source: OECD.



Source: Eurostat, EU-LFS and OECD data for the US.

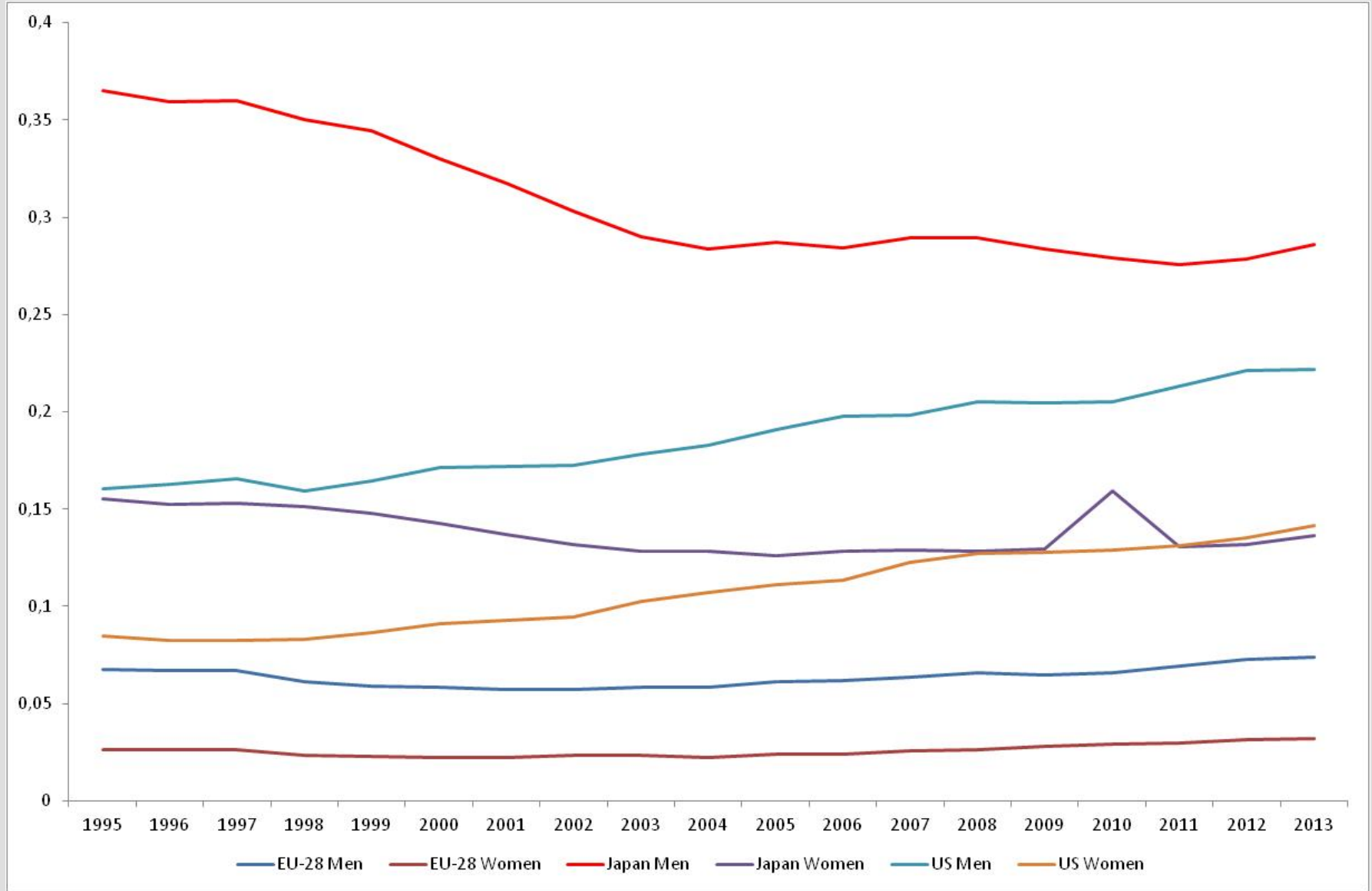


Chart 15: Activity rate by group (age and sex), EU-28, 2002–13 (in %)

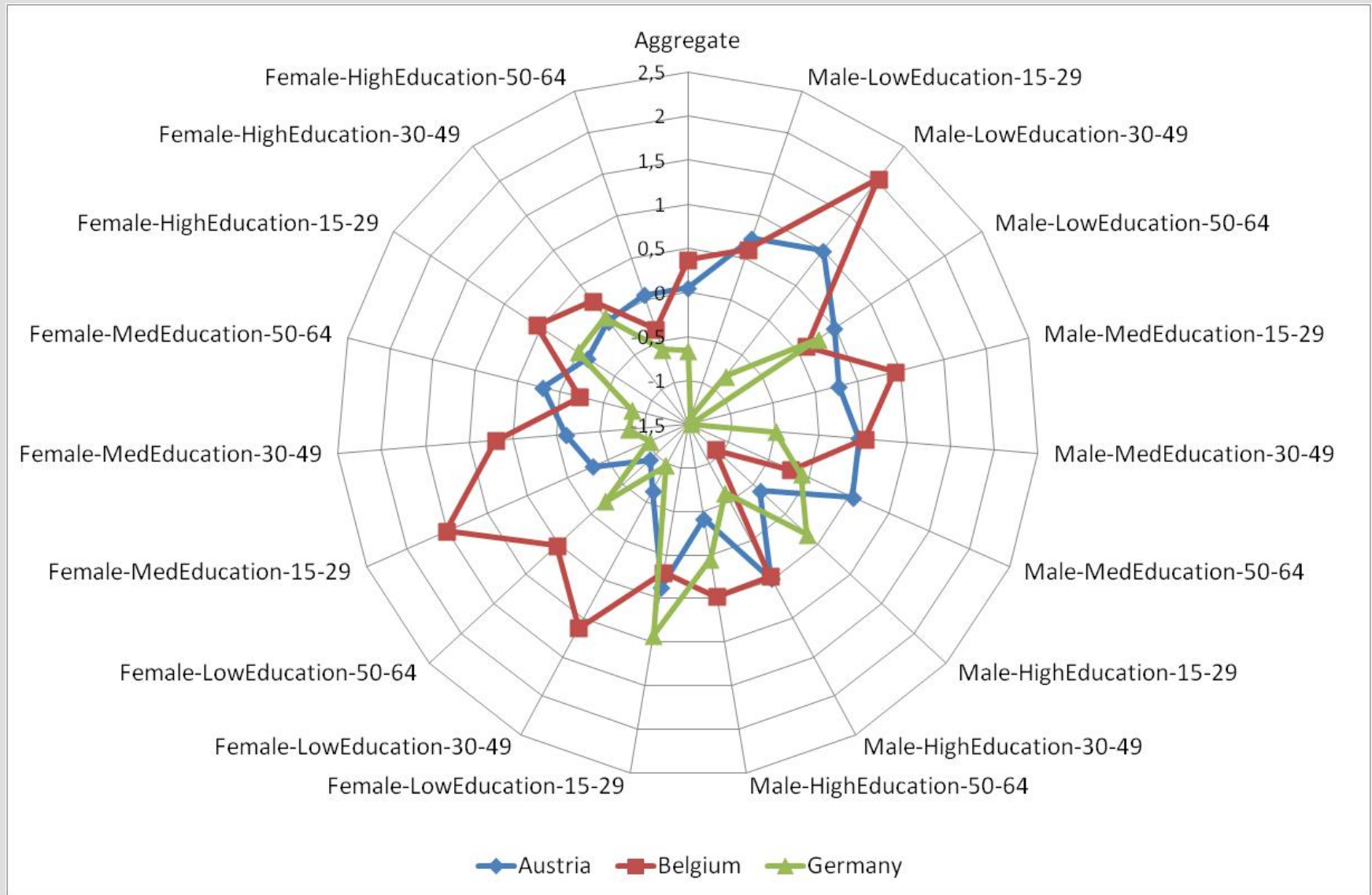


Source: Eurostat, EU-LFS, [lfsi_agan].

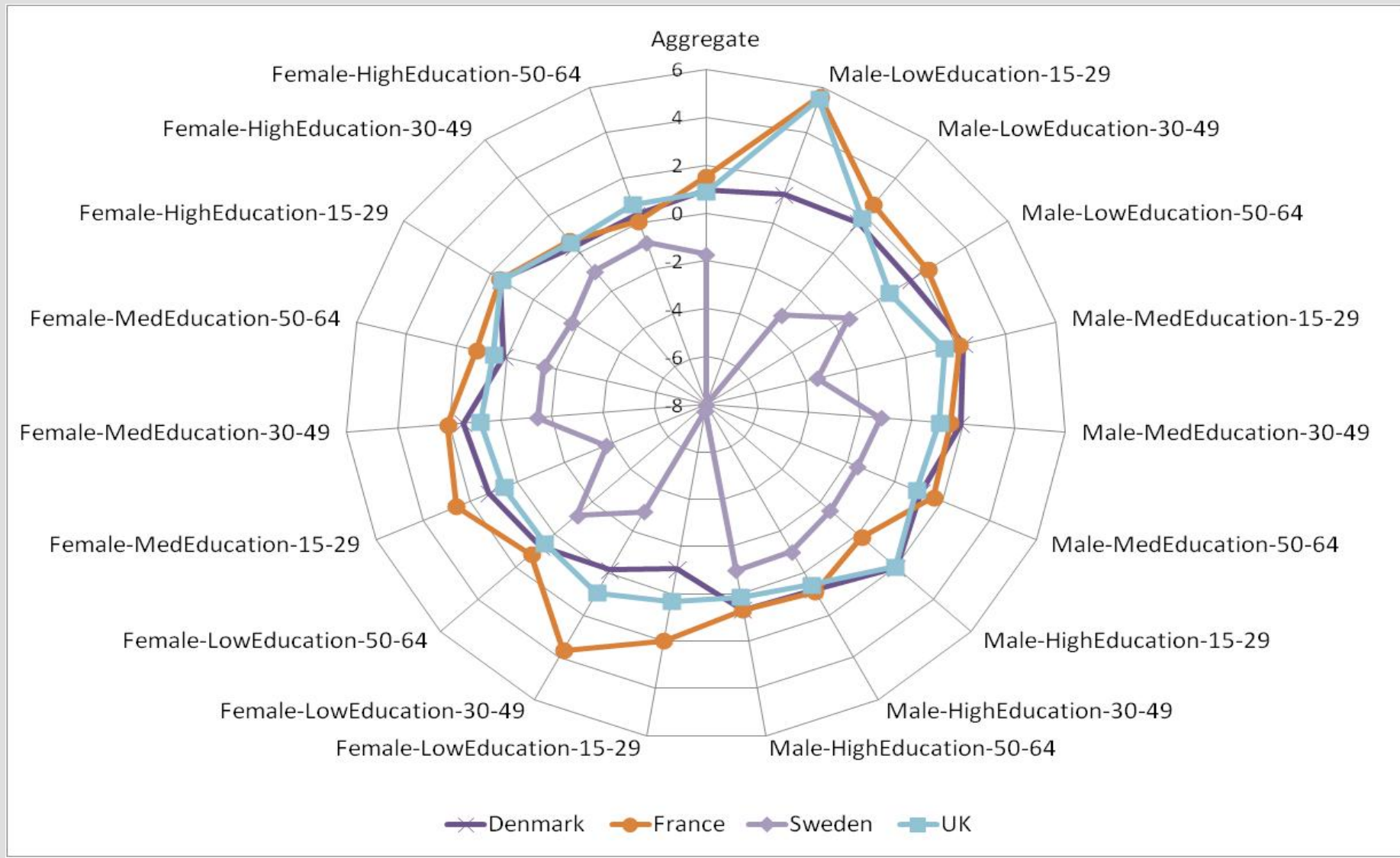
Employment rate (65+)



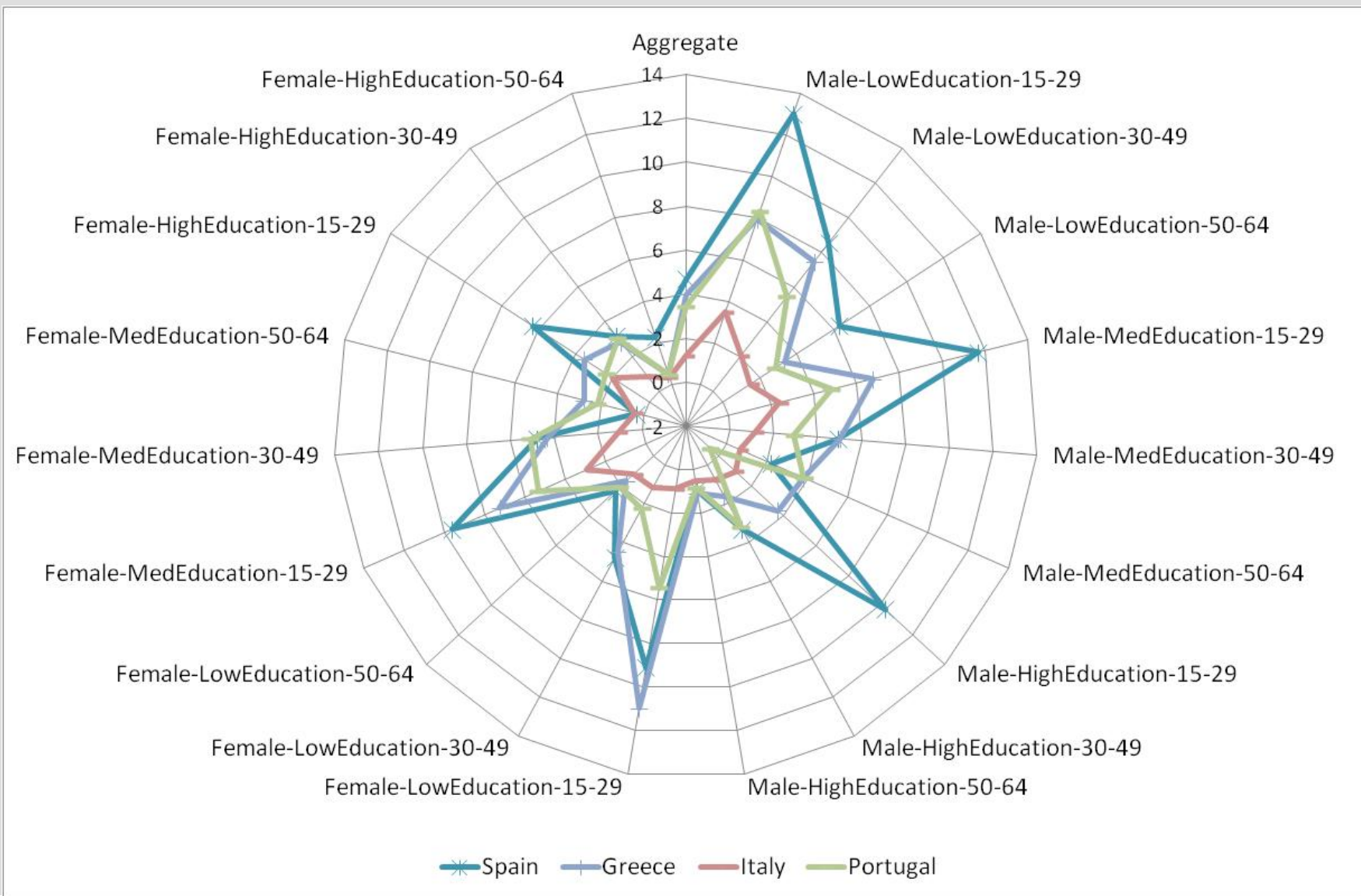
Changes (pp) in the (annual) flows from Employment to Unemployment (2006-2012)



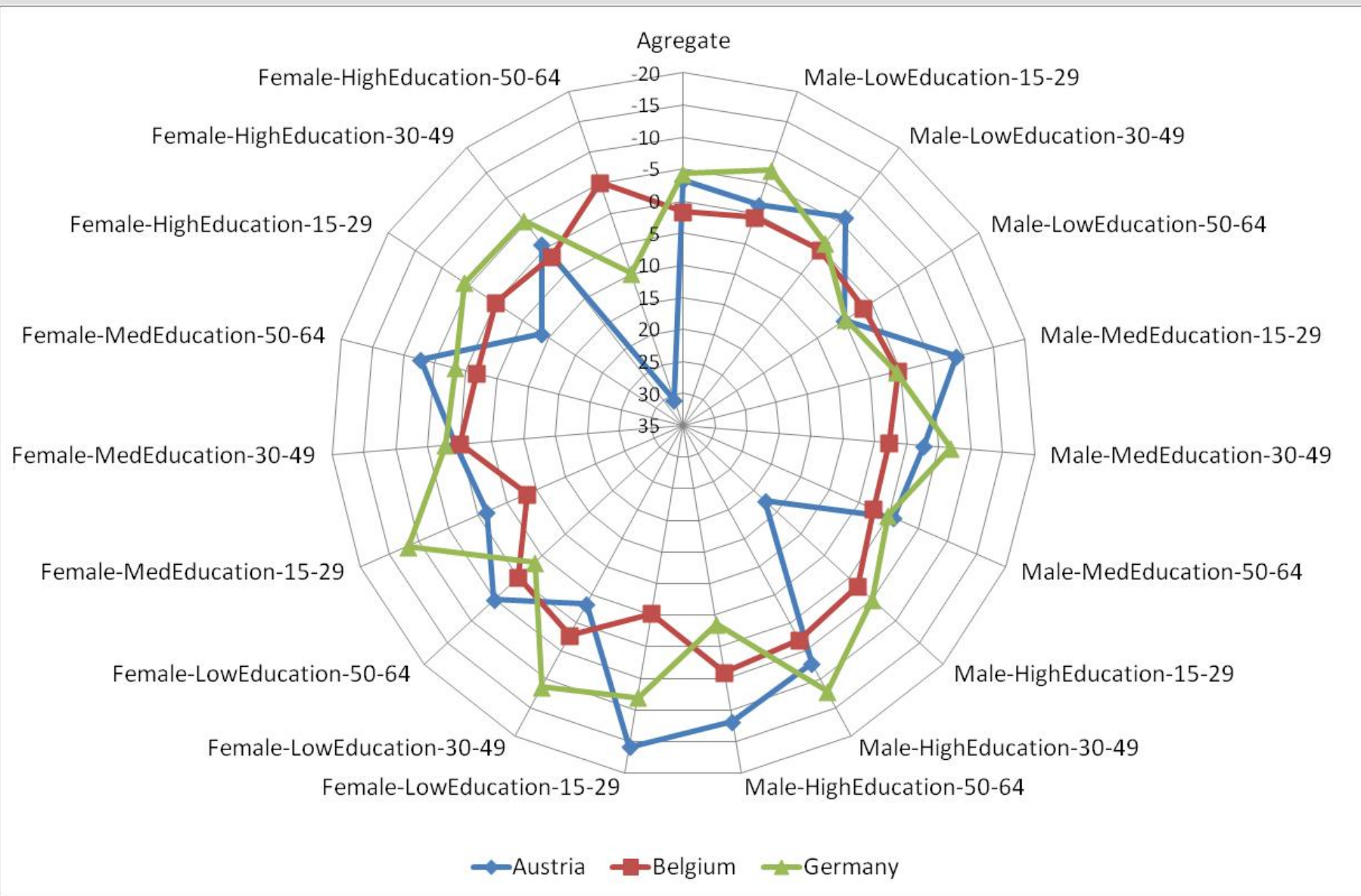
Changes (pp) in the (annual) flows from Employment to Unemployment (2006-2012)



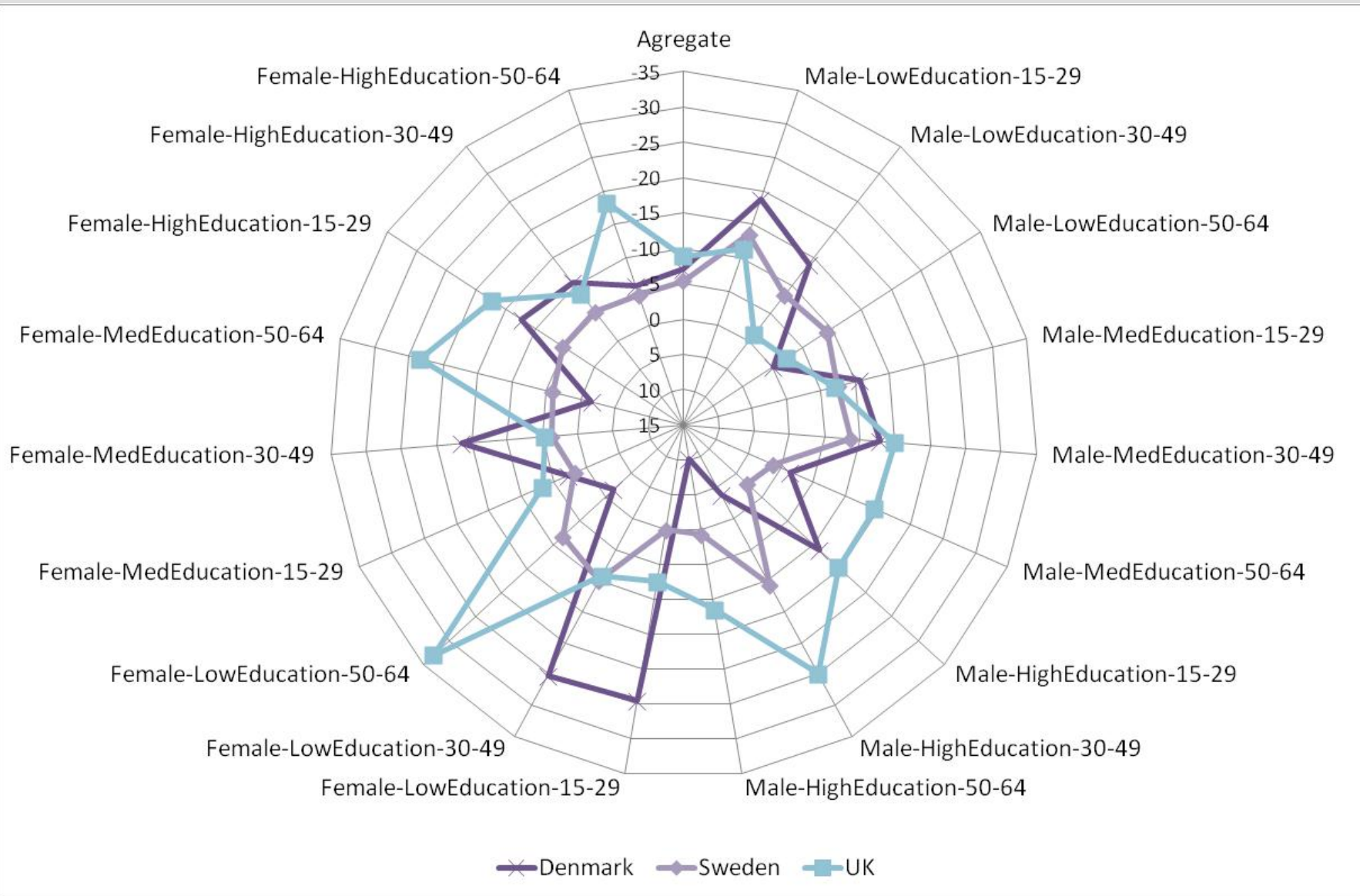
Changes (pp) in the (annual) flows from Employment to Unemployment (2006-2012)



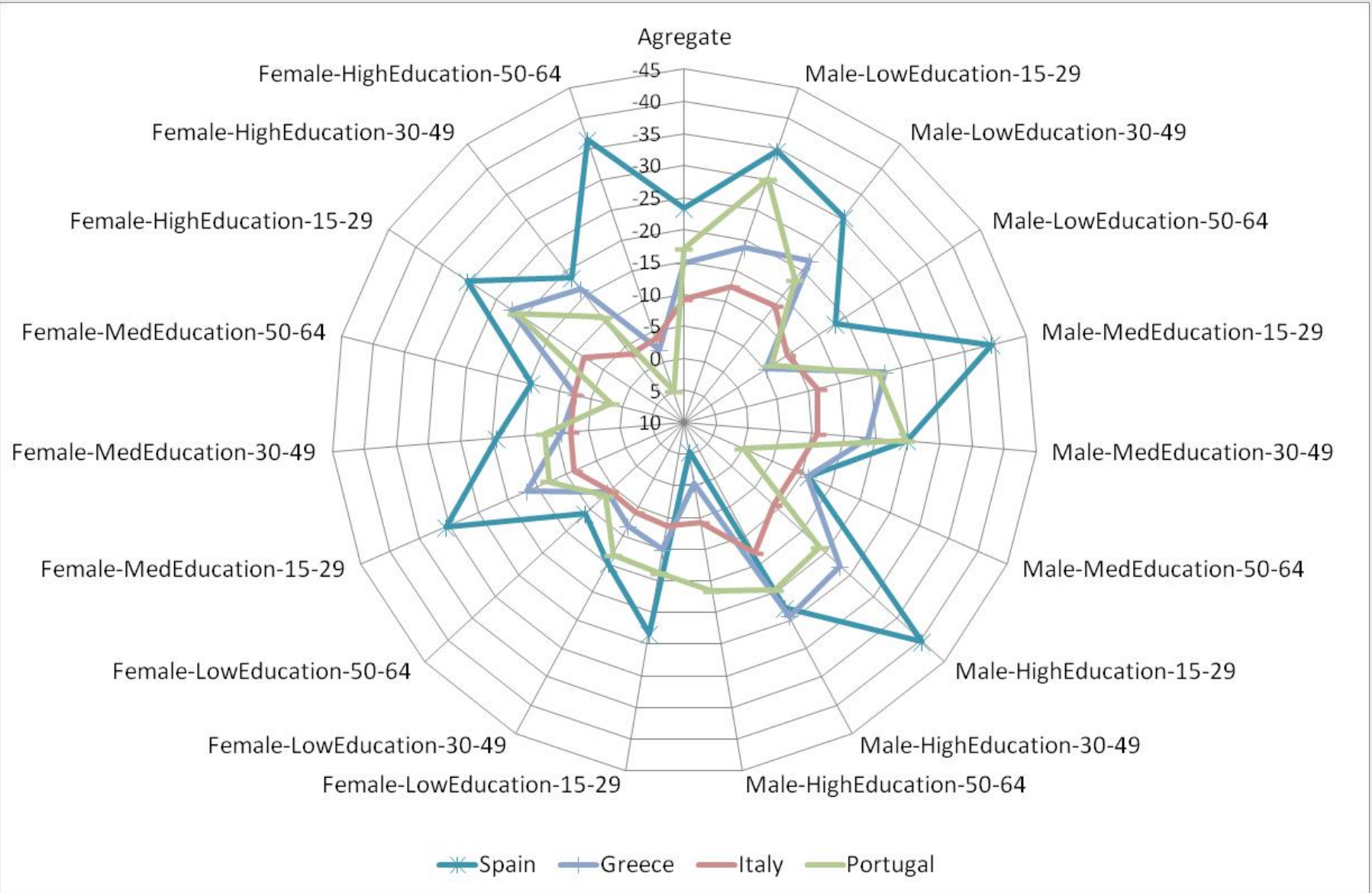
Changes (pp) in the (annual) flows from Unemployment to Employment (2006-2012)



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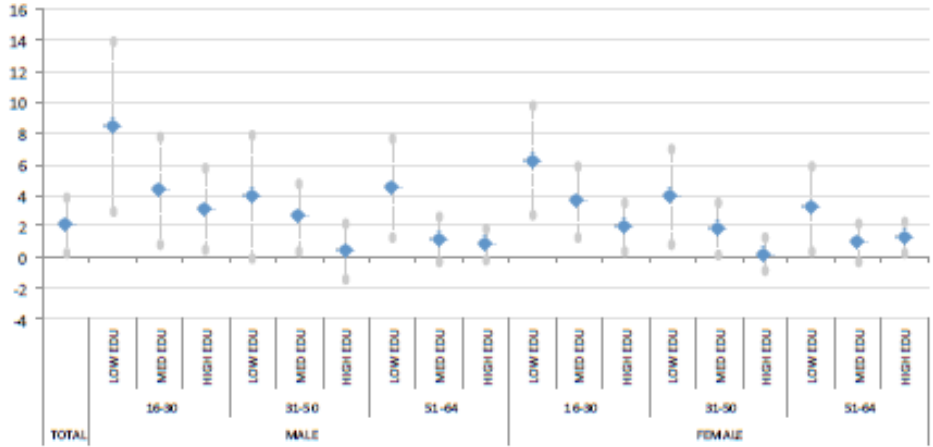




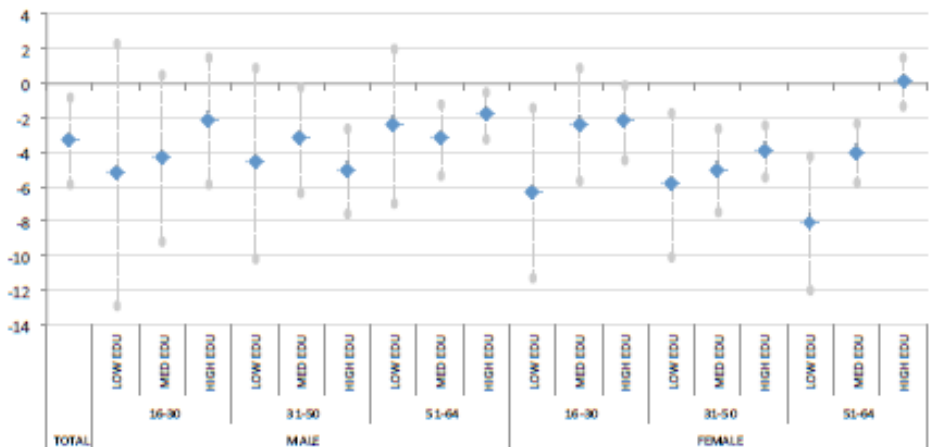
From Employment to Unemployment

$$heu_{ct} = \alpha_0 + \alpha_c + \alpha_1 gdp_{ct} + \alpha_2 Inst_{ct} + \varepsilon_{ct}$$

Employment protection legislation on temporary contracts

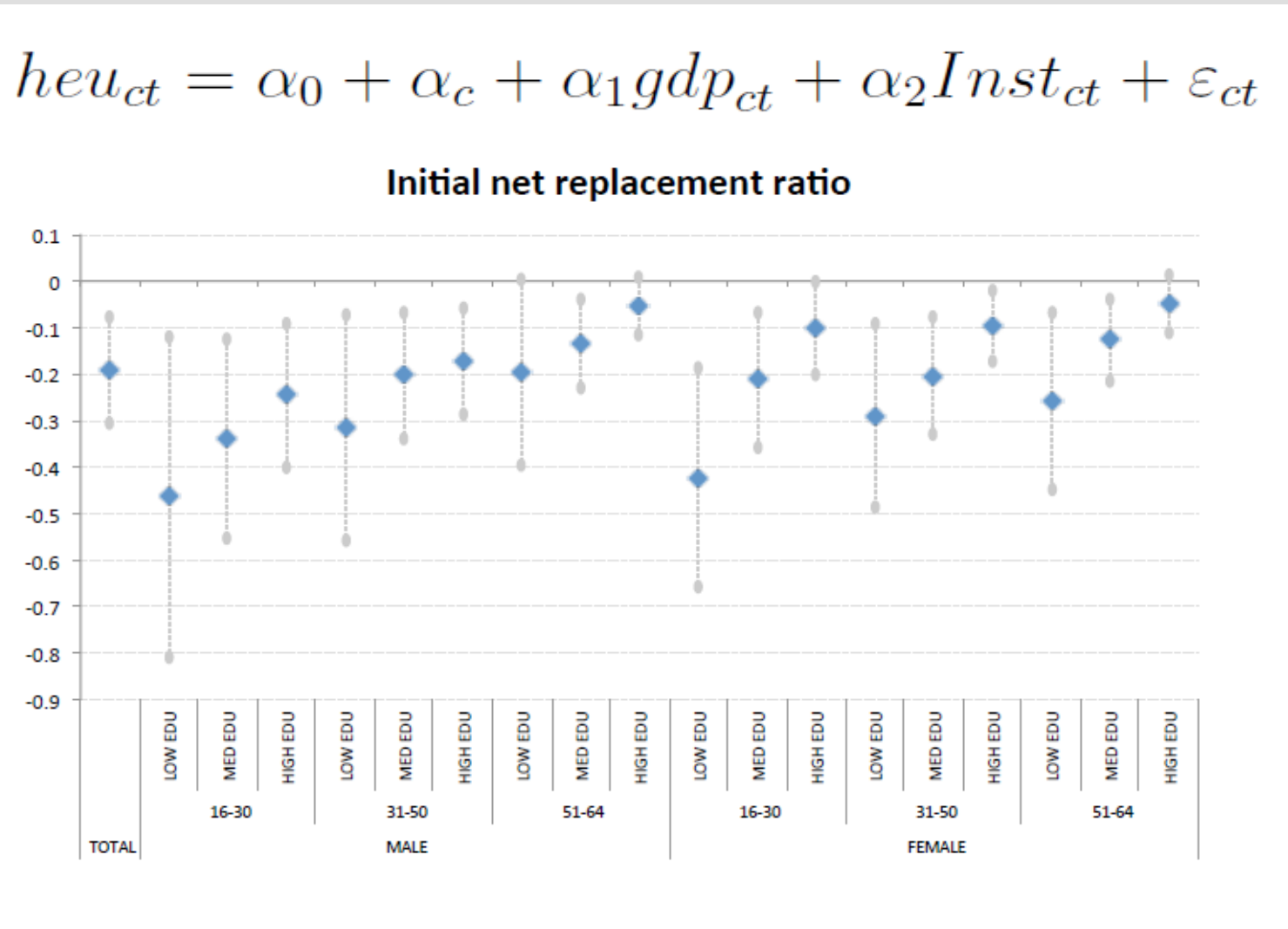


Employment protection legislation on permanent contracts and collective agreements





From Employment to Unemployment

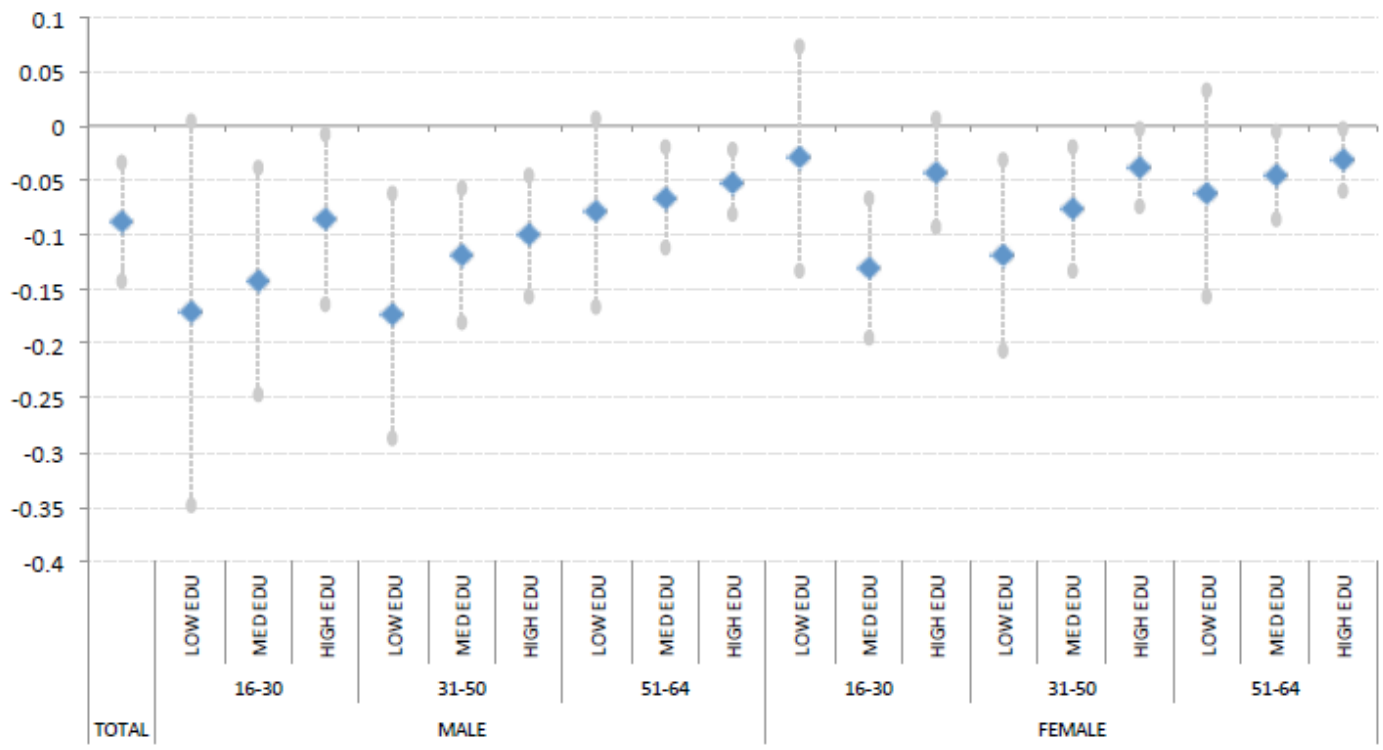




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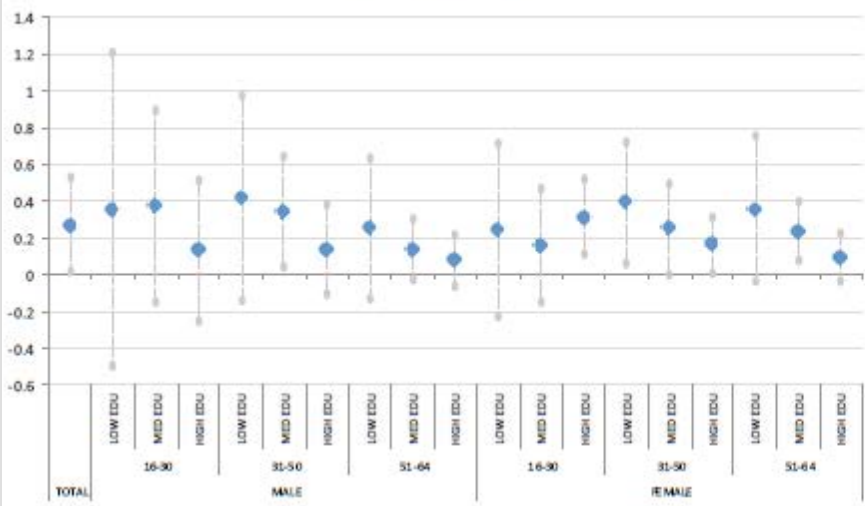
Expenditure in ALMP per unemployed



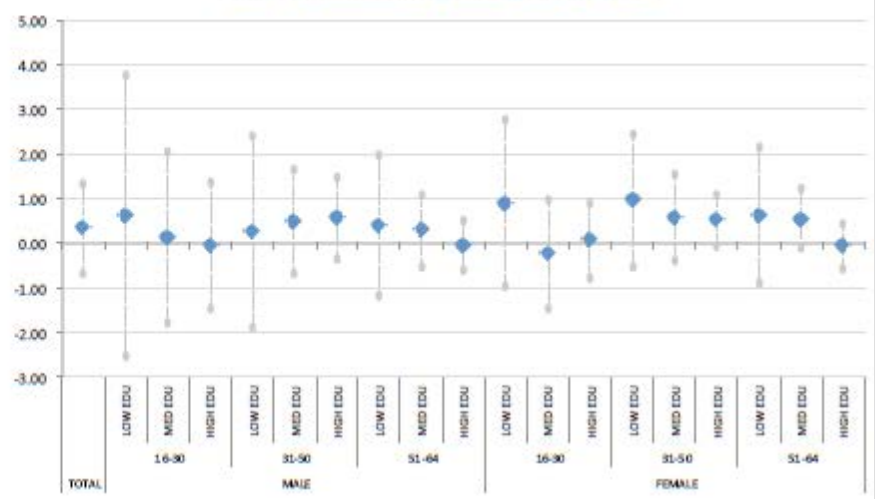
From Employment to Unemployment



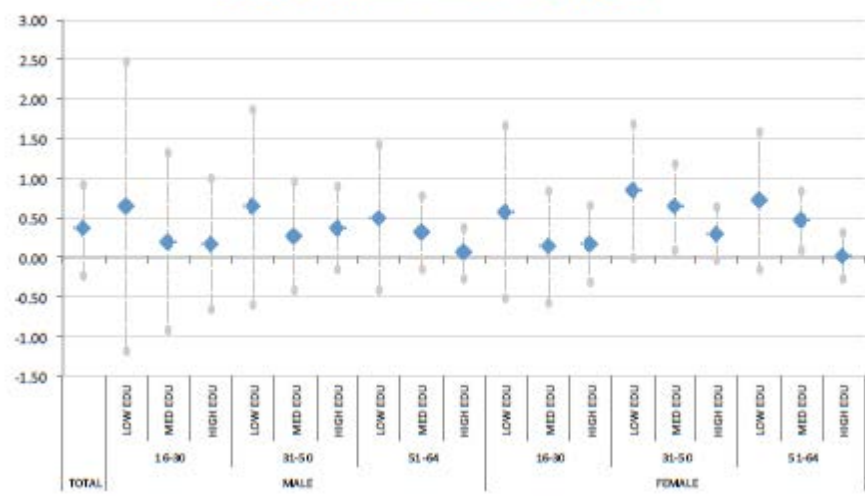
Union density



level at which bargaining takes place



type of coordination of wage setting

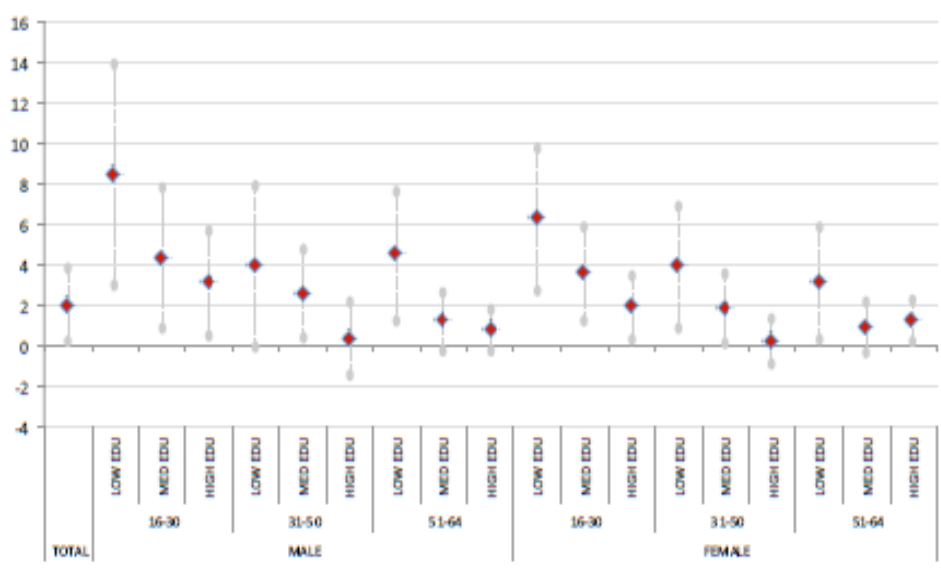




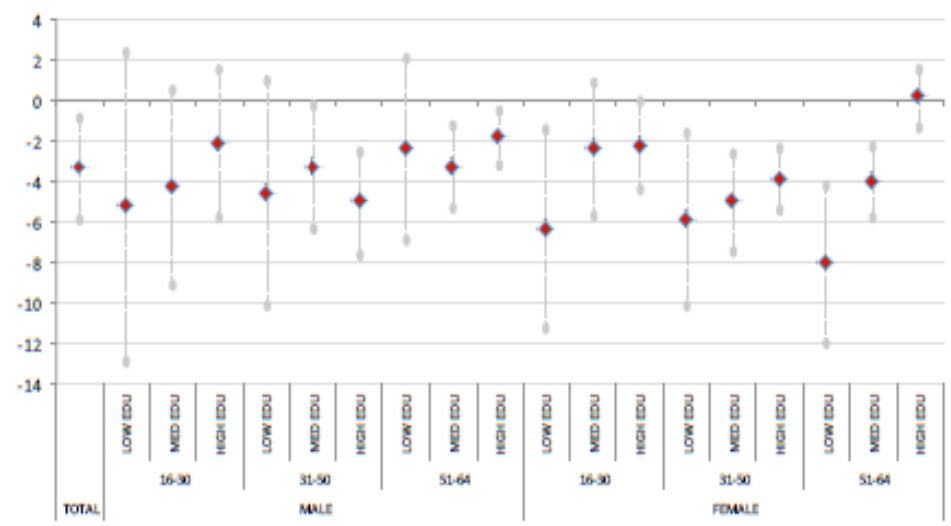
From Unemployment to Employment

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Employment protection legislation on temporary contracts



Employment protection legislation on permanent contracts and collective agreements

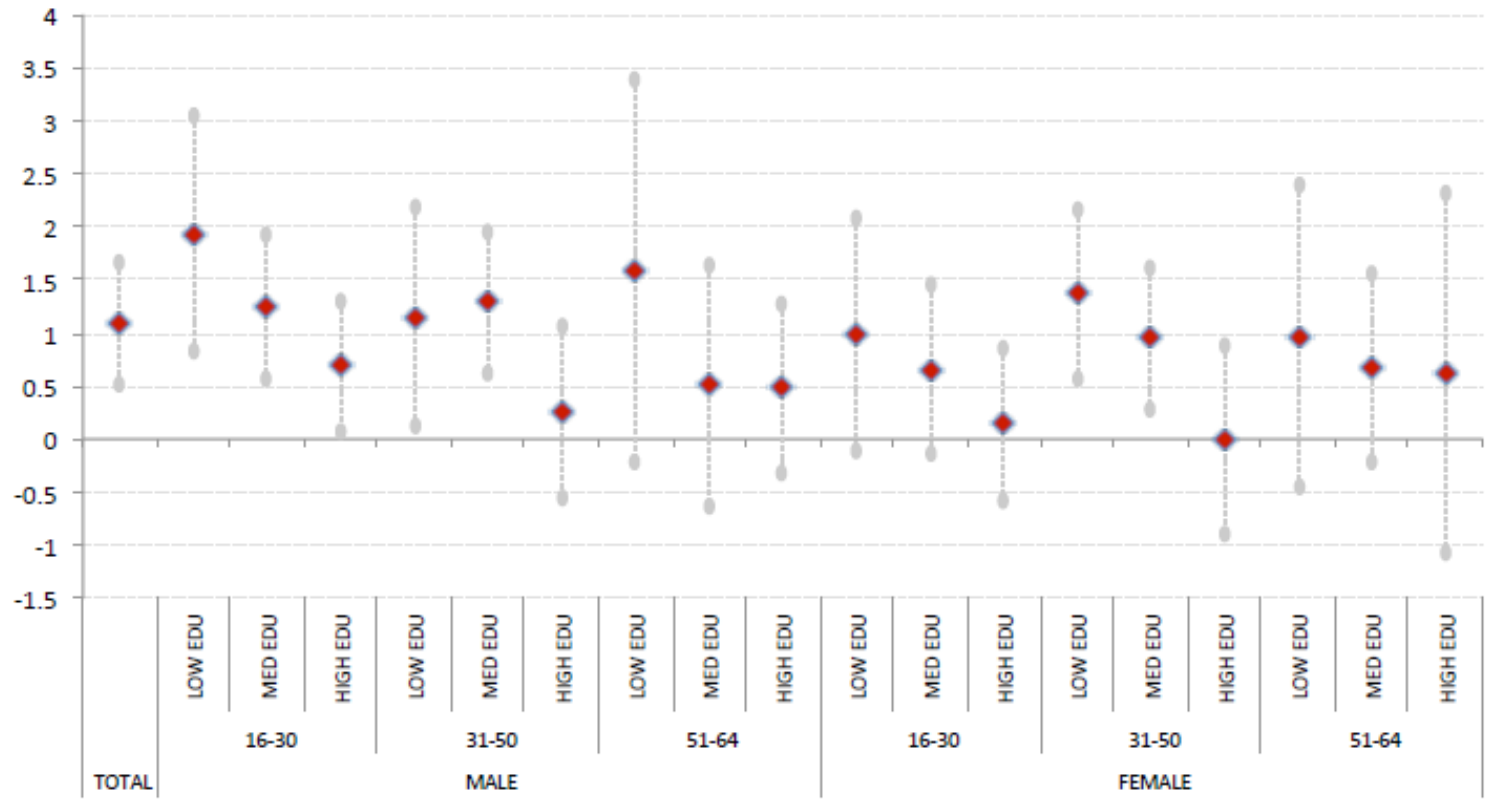




From Unemployment to Employment

$$hue_{ct} = \alpha_0 + \alpha_c + \alpha_1 gdp_{ct} + \alpha_2 Inst_{ct} + \varepsilon_{ct}$$

Initial net replacement ratio

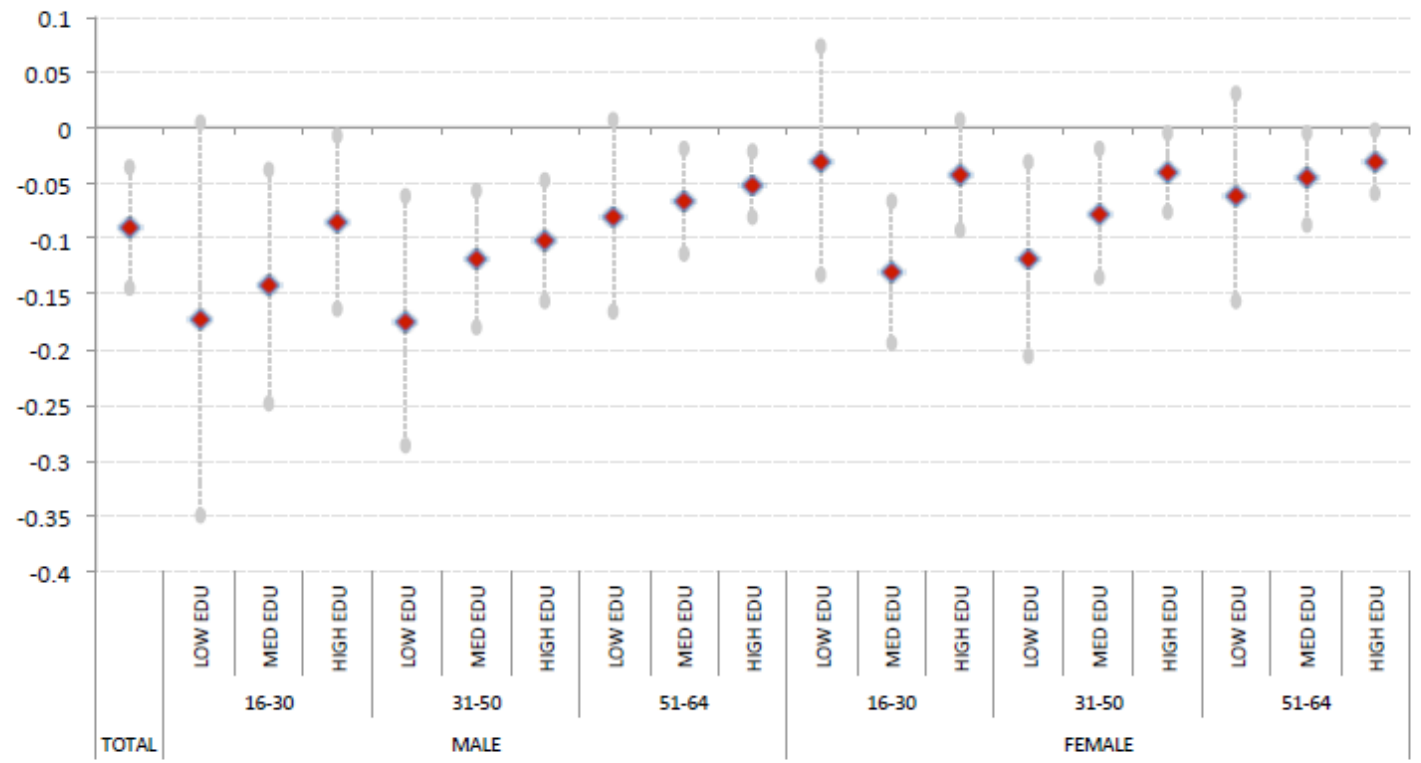




From Unemployment to Employment

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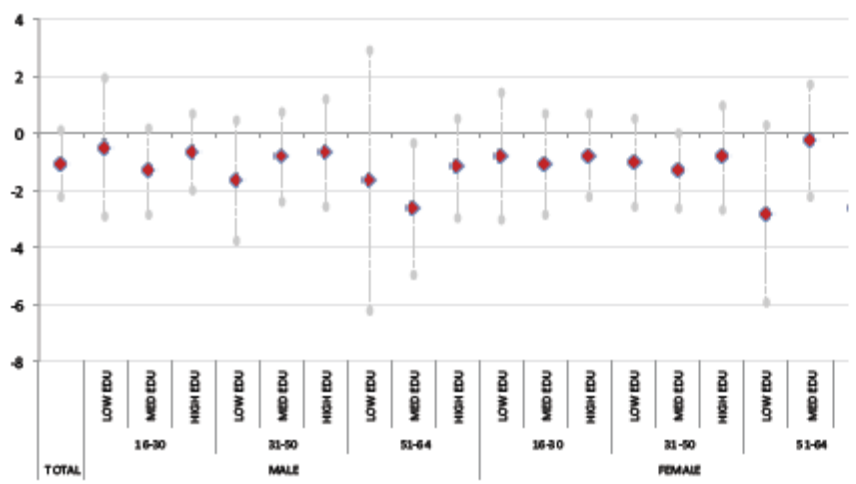
Expenditure in ALMP per unemployed



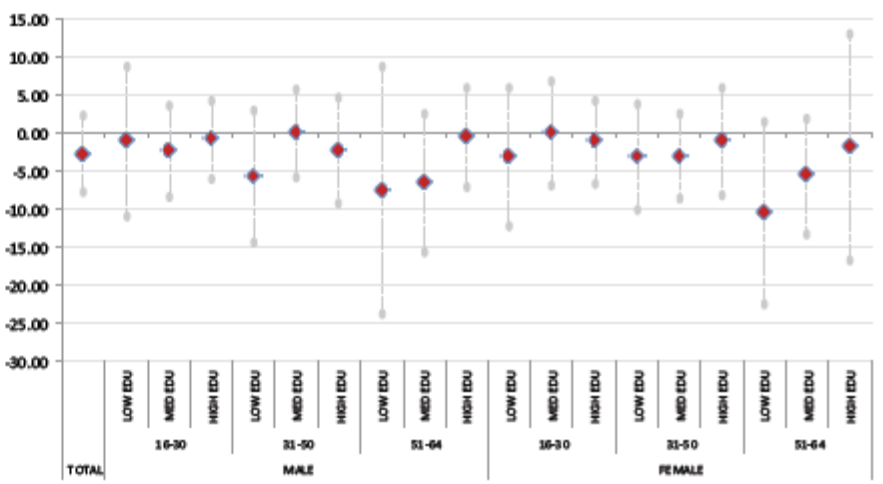
From Unemployment to Employment



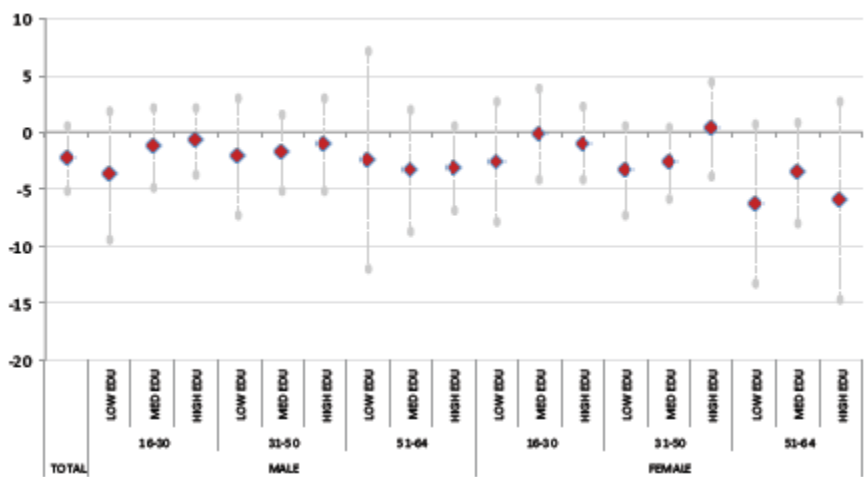
Union density



level at which bargaining takes place



type of coordination of wage setting



Why are firms reluctant to retain older workers?



Flows from employment to non-employment: Driving factors

1. *Labour costs: Wages increase with age*

- ✓ Seniority-based pay systems
- Cohort size effects
- Bargaining power increases with age

Policy responses:

- Reform wage determination
- Get wages closer to productivity

Why are firms reluctant to retain older workers?



Flows from employment to non-employment: Driving factors

2. Productivity: Does it decline with age?

- Physiological fact –Age bias
- Negative externalities ?
- Worsening of employment conditions

Policy responses:

- **Improve employment conditions**
- **Lifelong learning**
- **More flexible work arrangements for older workers**



Flows from employment to non-employment: Driving factors

3. Employment Protection Legislation

- Different provisions by age
- ✓ Alternatives available for older workers but not for younger workers (Soft-landing schemes towards retirement)

Policy responses:

- **EPL: Make firing costs more neutral**
- **Firing costs should not depend on seniority**
- **Protect workers, not jobs**
- **Use unemployment benefits, rather than severance payments, as a compensation for losing jobs**
- **Introduce some “experience-rating” in unemployment benefits, like in the US**



Flows from employment to non-employment: Driving factors

4. “*Social acceptance*”

- ✓ Less “stigma effects”
- ✓ Lump of labour fallacy: “Restricting the supply of older workers increases the employment opportunities of younger workers”
 - Logically unsound
 - None empirical support whatsoever
- Age discrimination: Stereotypes?
 - Evidence of positive effects of anti-discrimination laws in the US (David Neumark)

Policy responses:

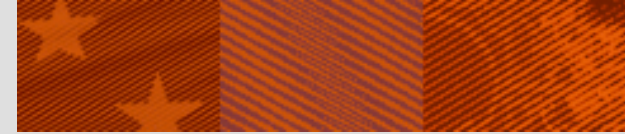
- Banish any idea inspired by the “lump of labour fallacy”
- Forbid age discrimination (specially, collective bargaining agreements ruling on hiring and firing age-related practices)



Flows from non-employment to employment: Driving factors

1. *Skills and the arrival of job offers*

- ***Many dimensions of “skills”:***
 - Education, “General” human capital
 - Experience, “Specific” human capital
 - New organization of work: Versatility, multi-tasking, team work, adaptability...
 - Labour demand is demand for composition of skills embodied in workers
- ***Older workers have a different composition of skills...***
 - Less general human capital
 - More specific human capital (Experience, EPL creates incentives for investment in specific skills)
 - Technological changes bring about changes in the demand of skills (skill-biased technological change)
- ***...and less incentives to invest in training***
 - Less time to extract returns from the investment



Flows from non-employment to employment: Driving factors

2. Non-employed older workers have high reservation wages

- ✓ Less mobile (across sectors, occupations, regions...)
- ✓ Earn non-wage income (benefits)
 - ✓ Soft-landing schemes towards retirement
 - ✓ “Generosity” of pension systems
- ✓ In some cases, return to work imply loosing benefits

Policy responses:

- **Get creative at designing programs to make compatible retirement and (part-time) employment**
- **Do not use pension systems to substitute for unemployment protection at later working ages**
- ✓ **Use pensions for their purpose not to facilitate labour force adjustment**



Flows from non-employment to employment: Driving factors

3. Imperfect substitution between old and younger workers

- ✓ **Changes in the sectoral composition of employment towards activities in which younger workers have a competitive advantage**
- ✓ **Changes in the occupational composition of employment towards activities in which younger workers have a competitive advantage**
- ✓ **But also, shortage of experienced workers in some industries**

Policy responses:

- **Be aware**
- **Get retirees involved in the training of younger workers**



Flows from non-employment to employment: Driving factors

4. Age discrimination: Stereotypes?

- **Evidence of positive effects of anti-discrimination laws in the US (David Neumark)**

Concluding remarks

- **In the EU, better performance of older workers participation/employment rates during the Great Recession than in previous recessions**
- **However, higher employment rates of older workers are absolutely necessary for...**
 - *Maintaining economic growth*
 - *Achieving high overall employment rates*
 - *Sustaining the “Welfare State”*
- **Low employment rates of older workers is the combination of labour demand and labour supply factors...**
 - *EPL, wage costs, and soft-landing schemes raise the flow of older workers from employment to non-employment*
 - *Soft-landing schemes and “generous” pension systems restrict the labour supply of older workers, shutting off the flows of older workers from non-employment to employment*