

EUROPEAN UNEMPLOYMENT REVISITED: SHOCKS, INSTITUTIONS, INTEGRATION

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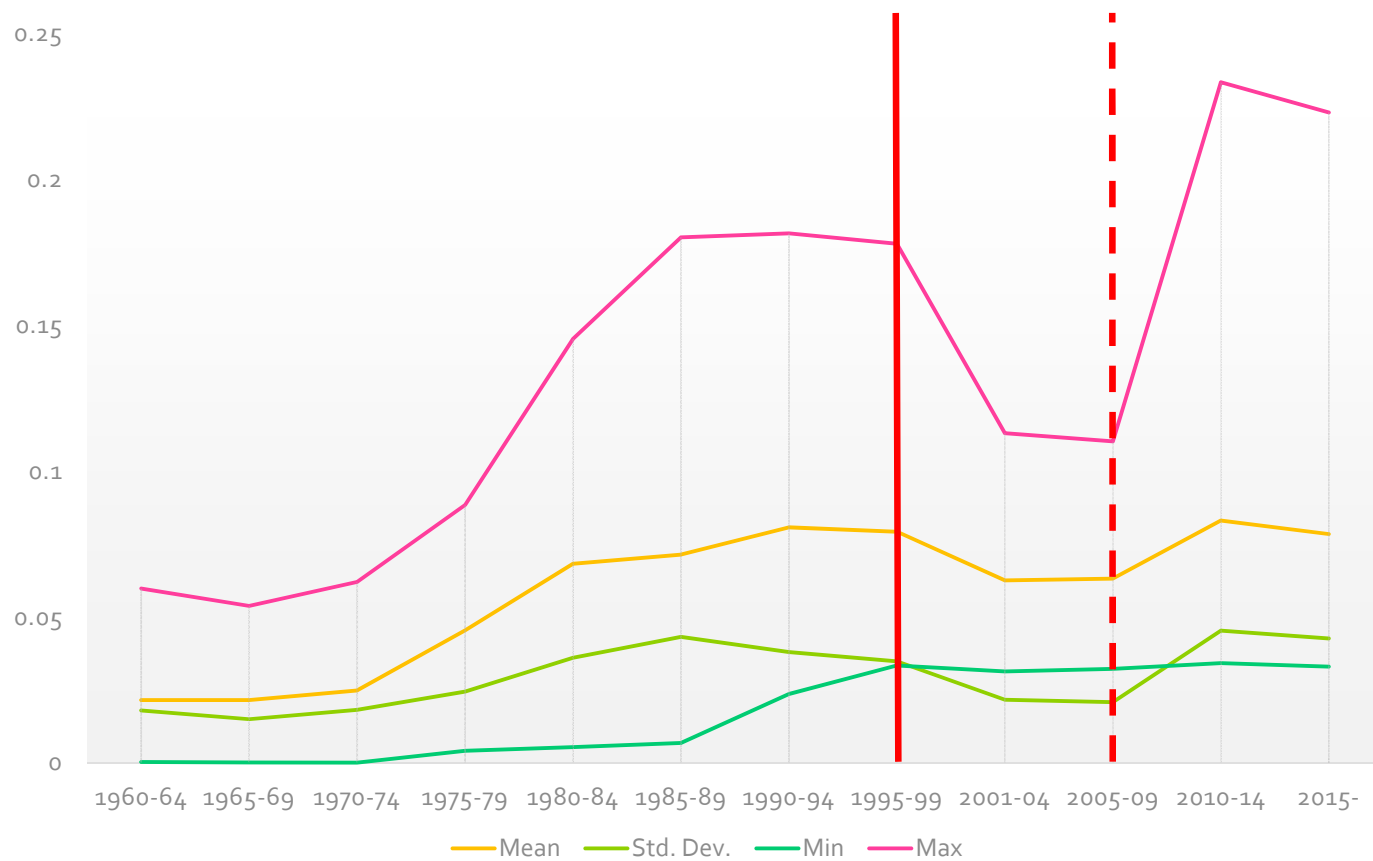
STARTING POINT

- What causes unemployment differences over time, across countries?
- (Besides cyclical fluctuations) Labor Market Institutions (LMIs)
- Since the early 1980s, long literature on the relevance of LMIs. Quite ambitious:
 - Measurement of LMIs
 - LMIs in theory and in practice
 - Scope and interactions among LMIs
 - LMIs are themselves explained by something else
 - LMIs have different effects along the business cycle
 - Similar LMIs seem to perform well in some countries at some moment in time, but not in others.

AN IMPORTANT MILESTONE

- Blanchard and Wolfers (2000): 20 countries in 1960-1995/6
 - A simple and intuitive specification: Reduced set of (mostly time invariant) LMIs interacted with three macro shocks (TFP, r , shifts in labor demand)
 - *“If our account is correct, one can be mildly optimistic about the future of European unemployment....The effects of adverse shocks should go away...more favourable macroeconomics environment and the improvement in institutions should lead to a substantial decline in unemployment”*

UNEMPLOYMENT SINCE BW (2000)



Unemployment declined
1995-2009

...increased since 2010

Big rise in heterogeneity

...also since 2010

MAIN TAKEAWAYS FROM GB'S PAPER

- Blanchard and Wolfers (2000) still works...(same 20 countries for 1960-2015/6)
- ...but need to take into account changes in LMIs and new macro environment (financial integration)
- Three main ideas to explain recent movements in unemployment
 - Intentional unemployment. Unemployment as a side effect of redistributive policies.
 - The inertia in the propagation of shocks
 - The role of international capital movements

INTENTIONAL UNEMPLOYMENT, THE ROLE OF LMIS AND LABOR MARKET REFORMS IN EUROPE SINCE 1995

- **What do labor market institutions do? Three views**
 - Rent-seeking: Redistribution at the expense of efficiency
 - Buffers to limit impact on social interactions and provide collective incentives
 - Remedies for market imperfections: insurance, efficient reallocation, retraining, job-seeking incentives.
- **Design, reforms, and effects of labor market policies shaped by:**
 - Historical factors
 - Political considerations
 - Economic context (structural change, integration, business cycles...)

INTENTIONAL UNEMPLOYMENT, THE ROLE OF LMIS AND LABOR MARKET REFORMS IN EUROPE SINCE 1995

· My view:

- Skepticism about GB's interpretation of LMIs as an "optimal" way of distributing efficiency-equity in a political economy model. Some LMIs does not improve neither efficiency nor equity
- GB: *"It would be strange if economist knew better about institutions than policy-makers and than the citizens who elect them"*.
- The views of policy-makers (in this field, mostly lawyers) vs. economists' views ([a recent Greek experience](#)).
- LMIs-Reforms in Europe since 1995
 - Productivity-enhancing (Boeri and Jimeno, 2015) ?
 - Demand-supporting (IMF, WEO-2016, ch. 3) ?
 - **Cost-reducing and inequality-increasing (WDN evidence)**

INTENTIONAL UNEMPLOYMENT, THE ROLE OF LMIS AND LABOR MARKET REFORMS IN EUROPE SINCE 1995 (EVIDENCE FROM *WAGE DYNAMICS NETWORK*, 2010-2014)

Chart 10: Easier to lay off employees

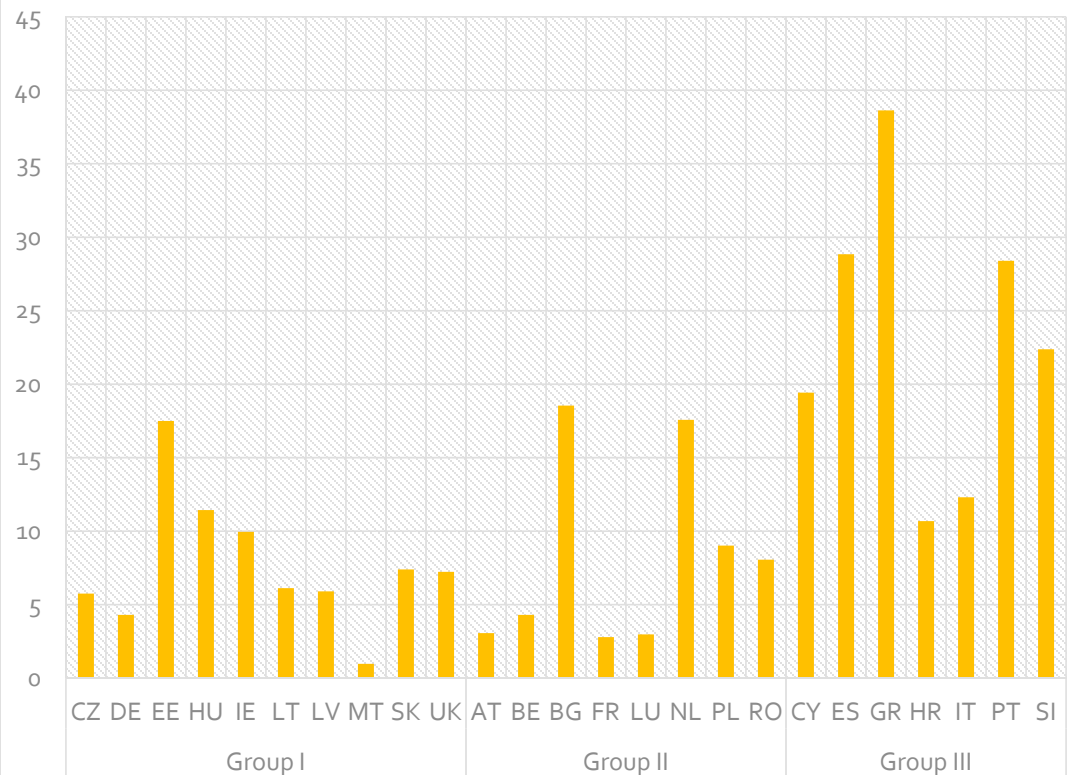
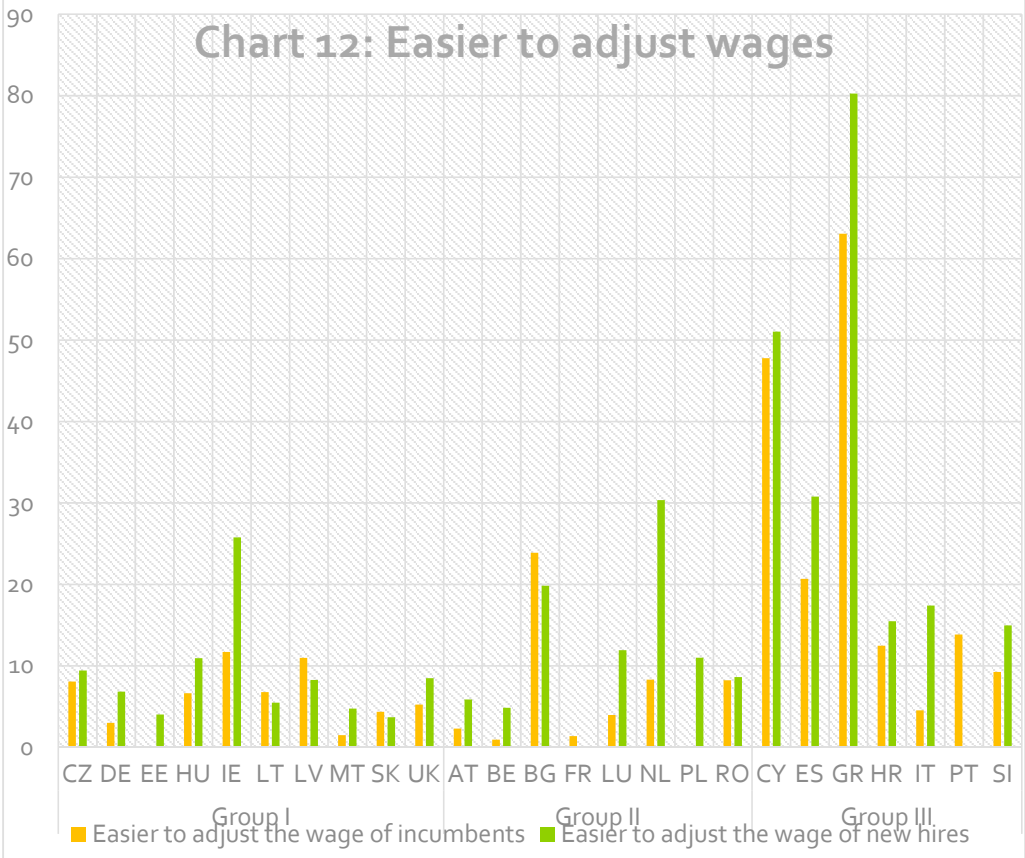


Chart 12: Easier to adjust wages



**SOME COMMENTS:
ON SHOCKS (1995-2016) AND WAGE INERTIA
(EVIDENCE FROM *WAGE DYNAMICS NETWORK*, 2010-2014)**

- GB: Adjustment costs and lags are NOT the same across countries or periods, or differ in ways captured by country effects and institutional indicators.
- Indeed, quite a lot of variation in wage responses to shocks across countries, over time
- Rely (once more) on evidence from the *Wage Dynamics Network*

SOME COMMENTS: ON SHOCKS (1995-2016) AND WAGE INERTIA (EVIDENCE FROM WAGE DYNAMICS NETWORK, 2010-2014)

Percentage of firms having frozen wages
Percentage of firms, employment-weighted values

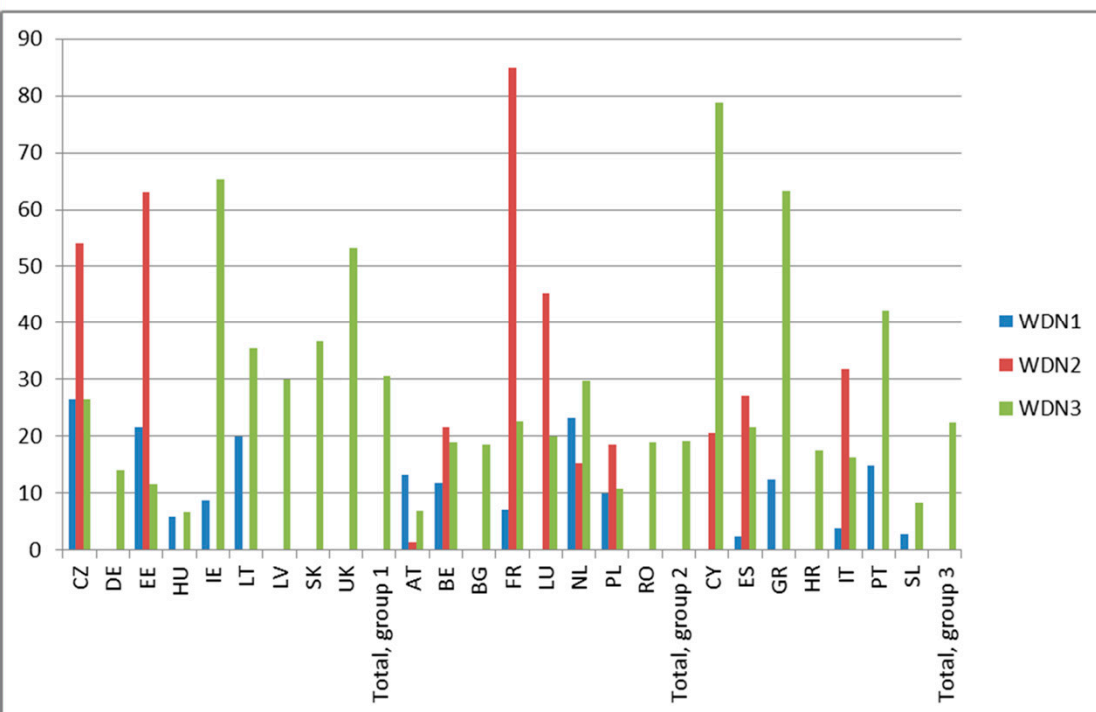


Table 3. Changes in wages and shocks. Probit; marginal effects.

	(1)	(2)	(3)	(4)
	Base wage		Flexible wage component	
Demand shock	0.079*** (5.600)	0.072*** (5.428)	0.137*** (6.832)	0.131*** (6.432)
Dem.shock*Group II	-0.052*** (-2.885)	-0.050*** (-3.009)	-0.021 (-0.760)	-0.031 (-1.133)
Dem.shock*Group III	-0.100*** (-2.997)	-0.106*** (-3.035)	0.016 (0.306)	-0.018 (-0.369)
Access finance		0.048*** (3.248)		0.046** (2.258)
Access fin. * Group II		-0.018 (-0.755)		0.039 (1.110)
Access fin. * Group III		-0.004 (-0.115)		0.098* (1.718)
Observations	17372	17372	17372	17372

Robust z-statistics in parentheses; *** p<0.01, ** p<0.05, * p<0.1. Weighted regressions (wl).

SOME COMMENTS: ON FINANCIAL INTEGRATION

- **GB: Integration favors deregulation in capital-rich countries (Germany, early 2000s), but not everywhere (may imply more regulation in capital-poor countries)**
- **Changes in real interest rates do not represent transitory shocks when capital flows are large... (or under a new macroeconomic regime constrained by low productivity growth and demographic stagnation)**
- **Alternative narratives of the determinants and motivations of labor market reforms since the 2000s:**
 - Adascalitei and Pignatti-Morano (IZA JOLP; 2016): LMIs reforms are positively associated with the unemployment rate, the simultaneous implementation of fiscal consolidation measures, and the presence of a fixed exchange rate regime
 - International pressure under rescue programs and fiscal coordination frameworks (Blanchard, et al., IZA JOLP, 2014)

FINAL REMARKS

- Institutions and shocks still relevant to explain variations of unemployment across countries, over time
- Recent data call for taking into account LMIs reforms and the impact of “new shocks” (financial integration)
- While agree on the empirics and general messages of the paper, I have some disagreements about what LMIs do, and about the drivers of the recent labor market reforms in Europe.

ANNEX. (NOT TO BE SHOWN)



RECOMMENDATIONS EXPERT GROUP FOR THE REVIEW OF GREEK LABOUR MARKET INSTITUTIONS

([HTTP://WWW.IERI.ES/WP-CONTENT/UPLOADS/2016/10/FINAL-REPORT-GREECE-SEPTEMBER-2016.PDF](http://www.ieri.es/wp-content/uploads/2016/10/FINAL-REPORT-GREECE-SEPTEMBER-2016.pdf))

- In the **Memorandum of Understanding** (MoU; dated 19 August 2015) signed with the European Commission, the Greek Government committed to *"launch by October 2015, a consultation process led by a group of independent experts to review a number of existing labour market frameworks, including collective dismissal, industrial action and collective bargaining, taking into account best practices internationally and in Europe."*
- **8 members** (4 appointed by the Greek Government, 4 by the EU/4 labor lawyers, 3 economists, 1 economist/sociologist/industrial relations activist)
- **Guiding principles. Two different views:**
 - European Social Model and ILO-Norms, Subsidiarity, Balance of power between social partners, Balance between efficiency and equity, Growth orientation, Inclusive labour markets, Equal pay, Reliability, Specificity, Integrated approach.
 - Objectives at stake, the balance of trade-offs between them, and the relevant restrictions that condition the feasibility and the effectiveness of the proposed measures to achieve the objectives.