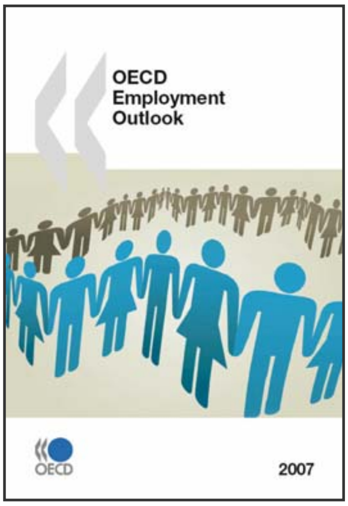


OECD Employment Outlook - 2007 Edition

Summary in English

- The BRICs – Brazil, Russia, India and China – are now important players in the global economy. *Employment Outlook 2007* looks at how this has affected their labour markets and discusses the state of their workforces.
- This edition also looks at how globalisation is affecting workers in OECD countries. While the impact is widely overstated, there is some evidence of growing insecurity in labour markets and widening inequality.
- Also in this edition: How labour market policies affect productivity; The impact of financing social protection on employment; And a look at what OECD countries do to get the unemployed back to work.

The **OECD Employment Outlook** takes an annual look at key issues in employment. In the 2007 edition:

Labour markets in the BRICs

The BRIC economies – Brazil, Russia, India and China – now account for a quarter of global GDP, up from 17% in 1990, and are important economic partners for OECD countries. The BRIC economies' future success will depend in large part on their labour markets. Because of data restraints and the size of the BRICs' informal economies, these markets resist easy examination. Nevertheless, there appear to be a number of definable characteristics and trends:

Rapid growth has driven employment. Collectively, the BRICs created 22 million new jobs each year in the first five years of the millennium, compared with 3.7 million in the OECD area as a whole.

Still, **under-employment** is significant. In Brazil and Russia and China (urban areas), the unemployment rate stands at around 8-9%, and it is somewhat lower in the urban areas in India. There are also high levels of under-employment, particularly among women in Brazil and India, older workers in Russia, and in rural areas in China and India.

Excluding Russia, **informal employment** – i.e. employment that is not officially declared and that makes no contribution to social security – is widespread and growing. In Brazil it accounts for about half of all employment, and about 85% in India.

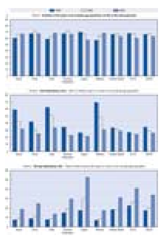
[Fig 1.2] Employment and unemployment rates in the BRICs and OECD areas

Wage inequalities have grown in China and India and remain persistently high in the two other BRICs. This appears to contradict standard trade theory, which suggests that the international integration of economies with high numbers of unskilled workers should lead to an increase in relative wages for such workers.

For the medium term, the BRICs are set to experience significant **population ageing**, which will limit the supply of new workers. Over the next 15 years, labour force growth will slow in India, fall by half in Brazil and effectively stagnate in China. In Russia, the labour force may even contract.

Also over the medium term, **educational attainment** will rise significantly in all the BRICs bar Russia, where levels of educated labour already exceed those of OECD countries. By contrast, education attainment in Brazil, India and China is much lower than in the OECD area. These three countries' rising levels of youth unemployment suggest the quality of education may need to be improved to match labour market requirements.

[Fig 1.7] Population structure in the BRICs and OECD areas

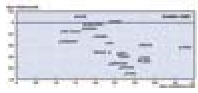


More jobs but less productive?

Growth in GDP per capita is driven by increases in both the proportion of people at work (labour utilisation) and output per worker (labour productivity). In 2006, the Restated OECD Jobs Policy identified a number of alternative labour-market policy packages that increase employment and reduce unemployment. But some argue that only market-driven labour market policies, such as those in the United States or the United Kingdom, can increase labour utilisation and labour productivity at the same time.

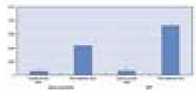
So what impact do labour market policies have on productivity? Strict **employment protection** for existing workers may reduce productivity by restricting the movement of workers into emerging high-productivity industries. In contrast, **minimum wages** seem to increase productivity, although this might be because low-skilled workers find it more difficult to find a job. Generous **unemployment benefits** can increase productivity by helping the unemployed find jobs that match their skills and by encouraging the creation of high-risk, high-productivity jobs. By allowing parents to remain in the workforce, **family-friendly policies** may also boost productivity.

[Fig 2.2] Relationship between growth in labour utilisation and productivity



Policies that promote employment can depress measured productivity, in part by expanding employment opportunities for lower skilled workers. This will bring down average productivity levels but will have no impact on the productivity of existing workers.

[Fig 2.7] The impact of parental leave on productivity



Overall, there is **no strong evidence** to show that policies advocated in the Restated OECD Jobs Strategy undermine productivity growth. Indeed, they are likely to have a positive impact on GDP per capita, while also bringing social benefits, such as increased employment.

OECD workers in the global economy: Increasingly vulnerable?

Globalisation – the freeing up of worldwide trade – has raised people's incomes in the OECD area. For example, OECD countries that see a 10 percentage point increase in trade openness enjoy about a 4% rise in per capita income.

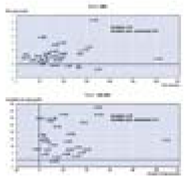
Despite these gains, there is considerable **public ambivalence** about globalisation. While globalisation has helped raise the incomes of many workers, some – particularly the low skilled – have fared less well and there is now genuine public concern that globalisation is squeezing salaries and damaging workers' conditions in OECD countries. How justified are these fears?

There is some evidence that deepening trade over the past few decades has increased both earnings **inequality and insecurity** for OECD workers. But some important caveats need to be kept in mind. Firstly, it is difficult to separate the impact of globalisation from that of technological change or structural reform and, secondly, the impact is not as great as is popularly understood.

The impact of globalisation on workers varies, and is determined in part by their skill levels. While **offshoring** has no real impact on the overall numbers of workers in employment, it can reduce demand for low-skill workers, probably because businesses tend to move the most routine production stages overseas.

More profoundly, globalisation is one of a number of factors – including domestic policy reform and technological change – contributing to **greater flexibility** in both salaries and labour demand, which have both become much more responsive to economic shocks.

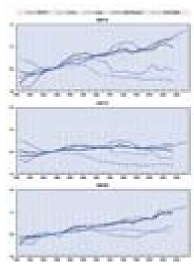
[Fig 3.6] Wage growth and the relationship to trade openness



As an indicator of this change, the **wage elasticity of labour demand** increased from 0.2 to 0.5 (in absolute value) between 1980 and 2002. This translates to a more dynamic labour market which places a premium on being mobile and having the right skills. Indeed, increased foreign competition leads to increased job switching.

On **income inequality**, the share of national income accounted for by workers' wages has fallen, quite sharply in some countries. There is also a growing gap in earnings, but it is largely accounted for by sharp increases in earnings among the top 10% of earners, rather than by falls at the bottom end of the earning range. The extent to which globalisation is contributing to these changes is unclear. However the changes in earnings distribution at least suggest that globalisation is allowing small elites of workers and investors to pull away from everyone else.

[Fig 3.8] Earnings inequality in 10 OECD countries since 1980



In response to all these changes governments need to develop a **package of policies** covering regulatory, employment and social protection issues to support workers in increasingly dynamic labour markets, and must focus especially on developing workers' skills.

Financing social protection: The employment effects

Public spending on social protection – mostly health and pensions – accounts on average for about a quarter of GDP in OECD countries. The scale of this spending and the ways in which it is funded – whether through general taxation, income taxes or employer and employee contributions – can affect labour markets.

The funding of social spending creates a **wedge** between what workers earn in take-home pay and the cost of employing them (as represented by what they pay in income tax and what they and their employers pay in social contributions). In general, the bigger the tax wedge, the bigger the impact on labour markets. However the actual impact is dependent on three main factors:

The tax mix: There are grounds for funding public social protection schemes with a strong collective dimension, such as health, through general taxation. By contrast, social contributions should be used to fund schemes more closely related to labour market status, such as unemployment insurance or pension schemes. Making greater use of general taxation – income tax and consumption taxes, but also possibly environmental and property taxes – can reduce the tax wedge and increase financial incentives to work. However all these options must be considered carefully, and are no substitute for better management of social-spending systems.

Tax progressivity: The tax wedge can have a particularly big impact on low-paid employment, especially where there is a high minimum wage. This may justify reducing the scale of employer contributions. Deadweight losses tend to be substantial, however, and excessive cuts pose a major funding issue.

Finding the right balance between minimum wage, labour taxation and in-work benefits – the three income components of minimum wage earners – is therefore essential. But overall, a move towards more progressive funding sources is advisable.

Links between taxes and benefits: Creating a stronger link between taxes paid and benefits received may help reduce the impact of the tax wedge. For example, employees may accept lower net earnings if they can see clearly that there will be a return later on in terms of raised pensions. However, there are notable limits in this area, related to the strong collective dimension of a number of social schemes, like health. To take another example, employers may improve workforce management if what they pay is related to the firm's history as regards layoffs, early retirement or sickness and disability inflows.

Activating the unemployed: What countries do

Many countries now actively encourage the unemployed to find work by making them more active in job hunting and by improving their employability. There are a number of common elements in these approaches: Early and regular contact for the unemployed with employment counsellors; regular reporting of work availability and efforts to find work; direct referrals to vacant jobs; creation of individual action plans; and referrals to "active labour market programmes" (ALMPs) to counter the jobseeker's loss of motivation and skills .

But how are such strategies **implemented**? The OECD sought to find out by asking member countries to complete a questionnaire on their policies to "activate" the unemployed. While more research needs to be done, it is clear that there is great variation in practices in this area and that countries are using a growing number and variety of instruments.

In most cases, the unemployed must **register** for job placement in order to receive benefits. Registering jobseeker details and assessing their availability for employment enables employment services to make tailor-made interventions. However, in a substantial number of countries, benefits start being paid well before the full process of registration is completed, which may result in a number of possible job matches being missed.

Most countries require the unemployed to **report regularly** on whether they are actively seeking work and are still unemployed. In addition most also require them to attend regular intensive interviews with counsellors. However, there are big variations in the frequency of such reporting and interviewing. There are similar variations in how often jobseekers are referred to vacancies (too rarely, it seems) and in the use of active labour market programmes for the long-term unemployed.

Overall, **monitoring** of the unemployed is increasing. This is likely to encourage more rapid re-employment, but there may be a downside: The unemployed may feel pressured to accept jobs to which they are not suited. While strict job-search monitoring and "work-first" policies are important to fight unemployment persistence, the need for good job matches that make for more stable employment should not be forgotten.

Finally, although **active labour market programmes** have been shown to help long-term unemployed, only a few countries have followed the OECD's recommendation to make attendance in such programmes mandatory. Countries may have good reasons for leaving such decisions to the discretion of job counsellors, but they should still make clear to the unemployed that interventions will become more frequent the longer joblessness continues.