Labor market flexibility: a changing international perspective

Over the past 30 years, labor market flexibility has been viewed as a solution to rising unemployment but also an attack on social standards; policymakers have considered a variety of measures to increase labor market flexibility during this period

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Member nations of the Organization for Economic Cooperation and Development (OECD) have experimented over the past 30 years with a variety of policies to promote flexibility in the labor market. Over this period, the term "labor market flexibility" has taken on a variety of meanings, prompting the observation that "rarely in international discourse has the [term] gone so directly from obscurity to meaninglessness without any intervening period of coherence."[1] This article traces the evolution of labor market flexibility in the context of changing economic conditions.

Labor market flexibility: the early days

In the early and mid-1960's, low unemployment and tight labor markets prompted governments to use a variety of programs to make labor markets more flexible and efficient. (See table 1.)

Some were targeted at strengthening employment services. The United States broadened the functions of the employment service to include identification of current and long-range training needs and to work with training agencies for screening and selecting trainees. A number of countries made efforts to expand the coverage of the employment service. The United Kingdom established professional and executive registers, and Sweden expanded employment services for white-collar workers.

Others were aimed at strengthening worker training programs. Britain established tripartite industrial training boards to strengthen training activities and finance their operation with a levy on all firms. Canada, France, and Sweden expanded adult training programs and the former West Germany started a program for providing support to workers who wished to take training for further advancement.

Several countries also encouraged geographic mobility. Sweden and Norway expanded programs that provided payments to workers who were willing to leave areas of labor surplus and move to areas where jobs were expanding. France introduced a program of grants to encourage geographic mobility.

In 1965, the OECD Council approved a plan that encouraged member countries to adopt active labor market policies that would help their economies to better adapt to economic change. These policies sought to bring jobs to workers in labor surplus areas, help people of all ages to train or retrain for new occupations, or to move to places with better employment opportunities.

The 1974–75 recession, combined with inflationary pressures and soaring unemployment (see table 1), prompted policymakers to turn away from the policies and programs of the 1960's and move toward measures that would maintain, for as long as possible, existing employment levels. Some job preservation measures encouraged employers to introduce programs calling for short-term work in which partial unemployment benefits are paid to workers whose hours have been reduced by their employers to avoid layoffs. Others provided subsidies to employers to keep on the payroll workers who otherwise would have been laid off. Some countries provided support to specific industries such as shipbuilding, steelmaking, and motor vehicle manufacturing, while other nations concentrated on counter-cy-

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Table 1. **Civilian unemployment rate in major industrial countries, third-quarter 1965–93**

[In percent]

Country	Civilian unemployment rate (percent)						
	1965	1970	1975	1980	1985	1990	1993
United States	4.5	4.9	8.5	7.1	7.2	5.5	6.7
Canada	3.6	5.7	6.9	7.5	10.5	8.1	11.4
Japan	1.2	1.2	1.9	2.0	2.6	2.1	2.6
France	1.6	2.5	4.1	6.4	10.4	9.1	11.3
Germany	3	.5	3.4	2.8	7.2	5.0	6.1
Italy	3.5	3.2	3.4	4.4	6.0	7.0	10.6
United Kingdom	2.1	3.1	4.6	7.0	11.2	6.9	10.3
Sweden	1.2	1.5	1.6	2.0	2.8	1.5	9.1
European Union[1]	—	—	—	5.7	10.9	8.4	10.7

[1] Data for European Union is from *Quarterly Labor Force Statistics*, Number 1, 1994. Data refer only to Belgium, France, Germany, Ireland, Italy, the Netherlands, Portugal, Spain, and the United Kingdom.

NOTE: Unemployment rates approximating U.S. concepts. Dashes indicate data are not available.

SOURCE: Bureau of Labor Statistics, *Comparative Labor Force Statistics, 10 Countries, 1959–93, August 1994.*

clical public sector employment programs. Also introduced in this period were measures designed to reduce labor supply by cutting workers' hours or encouraging early retirement.

Over the 1975–83 period in OECD nations in Europe, inflation continued to increase and unemployment more than doubled (from 4.4 percent in 1975 to 9.9 percent in 1983).[2] Policymakers began to focus on six explanations for persistent high unemployment: inadequate economic growth; structural factors such as labor saving technological change; competition from low-wage developing countries; high unemployment compensation payments relative to wages; causal relationship between duration of unemployment and difficulty in finding a job; and inefficient functioning of the labor market.

U.S. model of labor market flexibility

By 1984, many economists had identified "Eurosclerosis," or inefficient and inflexible labor markets as an additional reason for the increasing levels of unemployment in Europe. The U.S. model of labor market flexibility took center stage as the most likely answer to the European unemployment dilemma. The evidence appeared persuasive. Between 1974 and 1984 the U.S. economy created 18 million jobs, while job growth was nil in the major OECD European economies, and had dropped in France, Germany, and the United Kingdom. (See table 2). The unemployment rate in the United States had fallen 2.1 percentage points over the 1982–84 period, from 9.5 percent to 7.4 percent; the rates in OECD nations in Europe had increased 1.3 percentage points, from 8.9 percent to 10.2 percent.[3]

This emphasis on labor market flexibility and its contribution to economic growth and job creation was not a new idea. In the 1960's, active labor market policies sought to promote efficient and flexible labor markets. A 1977 OECD Experts Group headed by former U.S. Council of Economic Advisors Chairman Paul McCracken, urged governments to eliminate restrictions and rigidities in the labor market, such as demand and supply mismatches, rigid wage structures, discrimination against particular social groups, and inadequate training and human capital.[4]

By 1980, attention shifted toward barriers to labor market flexibility that were being created by the expansion of welfare systems in Europe. However, at that time, the OECD stated that "the long-term improvement in social standards is and should be irreversible: what can be done is to attenuate the negative effects of such improvement on the labor market."[5]

By the early 1980's the OECD and others became concerned that social regulations and welfare programs were seriously reducing labor market flexibility and resulting in increased unemployment. Increasingly, commentators and analysts argued that minimum wage legislation distorted factor allocations, that high unemployment benefits reduced work incentives and job protection provisions, and high nonwage labor costs introduced hiring disincentives.

In the OECD's annual reviews beginning in 1984 and focusing on member countries' economic performance and policies, the OECD Secretariat concluded that the "main impediments to better functioning of labor markets arise from specific wage-bargaining institutions, tax and social spending polices, and over-protective leg-

islation. In particular, in many countries the interaction of the income tax and social transfer system, especially unemployment benefits, exacerbated the unemployment problem."[6]

The United States championed this point of view. In October 1984 the U.S. Government developed guidelines for U.S. policy that emphasized the need for the OECD membership to remove barriers to efficient resource allocation. For labor markets, the United States emphasized the importance of eliminating rigidities by removing disincentives to work and by helping workers relocate to find employment. U.S. policymakers targeted the following as interfering with the efficient operation of the labor market: overly-generous unemployment compensation and welfare payments; high marginal tax rates; high nonwage labor costs for employers; government determination of wages; and institutional factors inhibiting the market from working efficiently, such as restrictions on hiring, layoffs, and firing, wage indexation, high minimum wages, worksharing arrangements, and the like.[7]

U.S. Administration officials, including the secretaries of Treasury and Commerce and Chairman of the Council of Economic Advisors, regularly lectured at international meetings that persistent unemployment problems among OECD nations could be solved only by increasing the flexibility in their labor markets. For example, at the 1985 OECD Council Ministerial Meeting, Secretary of the Treasury James A. Baker III warned that the ability of European economies to create jobs will not improve unless policymakers "address fundamental structural rigidities" in the economies of European nations and that it is critical that impediments to hiring and firing of workers be removed "so that firms possess the flexibility and economic incentives to create jobs."[8]

A definition of labor market flexibility

With continued attention focused on labor market flexibility, OECD Secretary-General Jean-Claude Paye established a high-level group of experts with a background in business, labor, and government to review the entire field of labor market flexibility and to report on the available policy options. The group identified six categories of labor market flexibility and made recommendations for each.

- *labor costs*: avoid mechanisms, whether institutional or automatic, that would lead to wage increases greater than productivity increases;
- *conditions of employment*: strike a balance between workers' desire for job security and the needs of economic efficiency;
- *work practices and work patterns*: modify the organization of work to enrich work content and raise levels of skill and to provide increased flexibility in the arrangement of working time;
- *rules and regulations*: apply rules and regulations in a reasonable manner and reassess their direct and indirect impact at regular intervals;
- *mobility*: remove obstacles to mobility such as nontransferable pension arrangements and rigid housing markets;
- *education and training*: improve initial schooling, strengthen retraining programs, and publicize the importance of lifetime learning for a flexible society.[9]

Impact on policy initiatives

By the end of the 1980's, European policymakers were generally reluctant to adopt many of the measures suggested by the OECD and the U.S. government to increase labor market flexibility. The 1989 report by the OECD's Economic Policy Committee noted that at the aggregate level, the evidence was weak that wage flexibility or adaptability of employment had increased generally in the OECD in the 1980's compared with the 1970's.[10]

This reluctance to adopt many of the measures suggested by the OECD and U.S. government was due to weak evidence of the link between increased labor market flexibility and a reduced equilibrium level of unemployment, negative aspects of labor market flexibility, and because reasons other than labor market flexibility were offered to explain the American "job creation miracle."

Impact on unemployment

Although labor market rigidities were routinely cited as causing high unemployment in European nations, the links to the level of unemployment were tenuous. The following briefly examines

Table 2. **Civilian employment in major industrial countries, second quarter, of selected years, 1974–93**
(Millions)

Country	1974	1984	1990	1991	1992	1993
United States	86.8	105.0	117.9	116.9	117.6	119.2
Canada	9.1	10.9	12.6	12.3	12.2	12.4
Japan	52.3	57.1	62.5	63.7	64.4	65.1
France	21.1	21.0	22.1	22.1	22.0	21.9
Germany	26.3	25.9	28.0	28.5	28.7	28.2
Italy	19.4	20.4	21.2	21.4	21.3	20.8
United Kingdom	24.8	23.9	26.6	25.8	25.2	24.6

SOURCE: Labor Force Statistics, 1971–91, *Quarterly Labor Force Statistics*, No. 1, OECD, 1994, pp. 34–35.

the impact of some of the most frequently mentioned rigidities on the unemployment level and job creation and describes the extent to which policymakers responded to the calls to increase labor market flexibility.

Some observers believe that nonwage labor costs, or employers' costs associated with social insurance and other labor taxes, increase unemployment by raising labor costs and forcing employers to rely on overtime work or labor-saving technologies, rather than hiring new workers. Despite the argument that these costs were a major source of labor market rigidity, few efforts were made to reduce these costs during the 1980's. Except for the United Kingdom, which provides several social insurance programs that are financed from general revenues, the other six major industrialized nations that belong to the so-called group of 7, or G-7, showed an increase over that period in nonwage labor costs. (See table 3). This reflected, in part, the recognition by policymakers that to reduce nonwage labor costs, they had to reduce benefits or shift taxes from labor toward other sources such as energy, capital gains, or income. The first option was not politically attractive and little evidence existed that a revenue neutral shift of taxes from labor would reduce the long-term rate of unemployment.

Employment protection measures such as hiring and dismissal procedures were often cited as causes of persistent unemployment in Europe. However, almost no empirical evidence supports the notion that employment protection affects the equilibrium employment level or that labor market adjustment can be improved by weakening such programs. An examination of employment protection measures in Germany, France, and Belgium in the mid–1980's by Katharine Abraham and Susan Houseman found no evidence that changes in such provisions affected the rate of labor market adjustment.[11] Research on employers' responses to the introduction of unfair dismissal legislation in the United Kingdom showed little evidence of reduced hiring.[12]

Cristoph Buechtemann cites a number of sources in arguing that the cost to employers of employment protection legislation is low, and that observers doubt whether employment protection legislation has a genuine impact on firms' dismissal behavior.[13] However, based upon its recent analysis, the OECD concludes that if high unemployment is established, "general legislated protection may add to difficulties, especially for weaker members of the labor force."[14]

A review of employment protection measures in OECD countries over the past decade shows no trend toward deregulation. Deregulation in Germany has been limited to exempting new firms with work councils (boards with elected worker representatives who participate in company decisions) from rules regarding dismissals. In 1986, France eased administrative rules for layoffs. However, the courts have progressively taken over this function and have made it more difficult for employers to dismiss workers. In January 1993, the Socialist government sponsored a new law imposing on employers the obligation to try to find other jobs or "placements" for workers or face having their layoff plans denied. While the opposition at the time opposed the measure, it has not moved to change the law now that it holds power.

Italy, which has the most highly regulated labor market in the European Union, strengthened employment protection in 1990 by extending dismissal regulations to small firms. Ireland also strengthened employment protection in 1991 with the Worker Protection Act, which extended protection to part-time workers. Spain and Portugal continue to have relatively strong protections against dismissal for permanent employees. Courts in the United States and Japan have made it more difficult to dismiss workers. The U.S. Worker Adjustment and Retraining Notification Act, enacted in 1988, requires mandatory advance notice requirements in certain cases of plant closings and mass layoffs. The United Kingdom liberalized some dismissal regulations and made it easier for employers to dismiss workers without the risk of lawsuits.[15]

Unemployment compensation programs that provide high benefits over a long duration provided another explanation for increased European unemployment, particularly long-term unemployment, because individuals are less likely to seek a job if financial incentives to do so are limited. OECD country studies have identified Canada, Denmark, Belgium, and the Netherlands as examples of how extending unemployment benefits appear to have contributed to higher levels of unemployment.

Table 3. **Nonwage labor costs as a percent of hourly compensation costs for production workers in manufacturing, selected years, 1975–92**

Country	1975	1980	1985	1990	1992
United States	16.7	19.1	19.9	20.8	22.6
Canada	9.0	10.6	12.4	13.6	15.0
Japan	10.0	11.4	12.6	13.1	13.1
France	25.7	27.3	29.1	28.6	28.5
Germany	19.4	21.0	22.1	22.4	22.8
Italy	32.8	29.3	29.5	31.9	30.6
United Kingdom	11.5	18.0	15.0	15.1	16.5

SOURCE: *International Comparisons of Hourly Compensation Costs for Production Workers in Manufacturing, 1992*, , Report 844 (Bureau of Labor Statistics, April 1993) p. 11.

However, many empirical studies have shown that the elasticity of unemployment is not very large with respect to replacement rates, which are benefits before taxes as a percentage of previous earnings, and the maximum duration of benefits. In other words, major changes in the replacement rate and duration of benefits would have to be made to bring about significant changes in the unemployment rates. In a study of unemployment insurance in the United States, France, Germany, Sweden, and the United Kingdom, economist Gary Burtless concludes that unemployment compensation "cannot be responsible for higher equilibrium unemployment in Europe, compared with the United States. . . ."[16] However, the OECD concludes that "relatively high unemployment benefit entitlements tend eventually to increase unemployment."[17]

Policymakers in OECD nations in Europe have made no major effort to curtail the level or duration of unemployment benefits. Workers continue to receive generous unemployment benefits for 1 year, 2 years, or in some cases, indefinitely. For example, in 1989, unemployed workers in Belgium received benefits indefinitely, in the Netherlands for 36 months, in France for 30 months, in Spain for 24 months, in Germany and the United Kingdom for 12 months, and in Sweden for 60 weeks. In addition, many countries—Denmark, France, Germany, Ireland, the United Kingdom, Austria, Finland—provide guaranteed income or social welfare payments indefinitely once unemployment insurance has expired.[18] Sweden's nonsocialist government continues to support a system that provides the unemployed with 80 percent of their previous salaries for 300 working days; workers 55 years of age or older receive this benefit for 450 working days.

The minimum wage also has been cited as a cause of high unemployment by pricing low productivity workers out of a job. The OECD concludes that "while the evidence is not conclusive, the balance of evidence suggests that single-rate legal minimum wages do adversely affect the employment prospects of young people trying to get a foothold in the labor market."[19] However, a study of the U.S. labor market by Lawrence Katz and Alan B. Krueger found that a positive relationship exists between movements in the minimum wage and employment in the fast food industry.[20] With regard to the general impact on adult employment, the relationship is even more tenuous.

During the 1980's, the general trend was a reduction in the minimum wage relative to the average wage, with France being the exception. Collectively-bargained minimum wages rose in the Netherlands, despite a freeze in the legal minimum wage over much of the 1980's. Germany does not have a minimum wage set by law, but the minimum wage set by industry rose relative to the pay of highly skilled workers.

Low employment growth and high unemployment in Europe also may have been caused by inflexible employment relationships that prohibit employers from hiring temporary workers. During the 1980's, governments introduced new employment contracts, which may have increased the level of employment as the number of workers on fixed term contracts soared. In France, the number of employees on fixed term contracts rose from 315,000 in 1985 to 611,000 in 1989, a 3.4-percent increase. In Portugal, workers on short-term contracts rose from 403,000 in the fourth quarter of 1983 to 517,000 in the first quarter of 1988, representing 12.0 percent of all employees. In Spain, fixed term contracts registered with the authorities rose from 95,000 in 1981 to 2.07 million in 1985, and to 3.75 million in 1988, or 32 percent of total employment over the period.[21] This trend also was evident in Japan where workers employed by temporary work agencies increased from 87,000 in 1986 to 317,000 in 1989.[22]

Negative aspects of market flexibility

By the end of the 1980's, many commentators and analysts began to point to the negative features of increased labor market flexibility. In referring to U.S. labor market flexibility, the Kreisky Commission on Employment Issues in Europe noted: "Even as the economy has been growing, increasing numbers of Americans have been pushed onto the breadline. The distribution of the benefits of growth has been highly uneven, with little impact on the nation's 20 million hungry citizens. Income disparities in the United States are the widest for 40 years."[23]

Peter Doeringer pointed to the dark side of labor market flexibility in the United States, noting increased joblessness and income loss among displaced workers, disruption of career paths for young adults, career disruption for older workers as a result of early terminations, falling employee commitment, reduced labor productivity resulting from an uncertain job climate, and a large impact on displacements of minorities. Doeringer argues that the enormous amount of workplace turbulence in the United States "has disrupted established labor relations practices and potentially weakened human resource development systems."[24]

The U.S. Department of Labor Commission on Workforce Quality and Labor Market Efficiency, formed in 1989, expressed concern that short-term responses to turbulence in the workplace would undermine work force productivity,

which will affect American competitiveness in the longer term.

Other explanations for U.S. job growth

Factors other than greater labor market flexibility began to emerge as possible explanations for the remarkable U.S. job growth in the 1980's. These included:

Low wage increases. Reflecting small productivity improvements during the period, low wage increases led to the hiring of more workers in the United States, a form of work sharing among low-wage workers.

While Europe concentrated on maintaining the quality of employment, the United States emphasized the importance of increasing the quantity of jobs. Empirical research shows that countries with low wage growth in the 1980's had more employment expansion than countries with high wage growth.

Real hourly earnings of production or nonsupervisory workers on private nonfarm payrolls, which peaked in 1973 at $8.55 per hour and have been headed downward since, were $7.64 by 1989 and $7.39 in 1993.[25] Labor productivity in the business sector increased at an average rate of 0.8 percent between 1979 and 1989, compared with an average growth rate of 2.1 percent in OECD Europe.[26]

Increased supply of labor. A condition that did not exist in Europe enabled the U.S. economy to greatly increase the number of contingent jobs in the 1980's. Many of these were low wage jobs in the service sector. European economies, which had much smaller increases in the supply of labor, could not support the creation of similar jobs. Between 1980 and 1990, U.S. labor force growth increased at an annual rate of 1.6 percent, compared with 0.9 percent in OECD Europe (table 4).

Table 4. **Labor force growth, major industrial countries, selected years, 1970–90**

(Annual average percent growth)

Country	1970–80	1980–90
United States	2.5	1.6
Canada	3.2	1.7
Japan	.9	1.2
France	.9	.4
Germany	.4	.7
Italy	.5	1.6
United Kingdom	.6	.7
OECD Europe	.7	.9

SOURCES: OECD *Employment Outlook*, July 1991 and OECD *Economic Outlook*, 54, December 1993.

Expansionary fiscal policy. In contrast to Europe, the United States expansionary fiscal policy promoted greater job growth, but increased the Federal budget deficit. For example, between 1981 and 1984 the structural (cyclically adjusted) component of the U.S. budget deficit—an indication of the discretionary changes in fiscal policies—grew by 2.5 percent of gross domestic product, while the other major OECD countries reduced their combined deficits by 1.1 percent.[27] During the 1980's, the U.S. budget deficit, as a percent of gross domestic product, increased more than in any of the other major OECD countries.

Labor market flexibility in the 1990's

As governments rejected most efforts to dismantle or modify regulations to increase labor market flexibility, as European unemployment rates began to fall in the latter half of the 1980's (see table 1), and as the U.S. employment level stalled at around 117 million workers in the early 1990's (table 2), policymakers began to reemphasize the active labor market policies of the 1960's.[28] These policies included support for measures such as training, placement and rehabilitation; developing employment-related skills; and helping jobseekers find employment. In addition, policymakers increased their attention to other measures to promote labor market flexibility, such as efforts to link social protection and labor market programs, and increased emphasis on improving the efficiency of labor markets within the firm, or internal flexibility.

Integrating labor market policies

Policymakers began to recognize, partly as a result of the debate over labor market flexibility in the 1980's, the need to link income support measures with labor market policies to promote job search, job motivation, and job readiness.

Several countries introduced programs to forge this link. Australia, New Zealand, the United Kingdom, and Sweden now limit income support to teenagers by requiring them to participate in some form of training, part-time employment, or both. France provides incentives for the unemployed to actively search for work by lowering unemployment benefits more rapidly as the duration of unemployment gets longer. In the spring of 1992, the French government offered each long-term unemployed worker a subsidized private or public sector job, or alternatively, a place in a training program. In addition, France's new minimum income scheme is linked with programs to help recipients find jobs.

The United Kingdom no longer provides benefits to unemployed workers under age 18 because of a government guarantee to provide 16-

and 17-year-olds with some form of training or employment. A new "Community Action Program" initiative is designed to pay the long-term unemployed a small premium over the amount of their weekly unemployment benefits in exchange for public service work and regular job search activity.

In Canada, the training use of unemployment insurance funds was raised from $500 million in 1990 (in Canadian currency) to $2 billion in 1992. In Australia, job search obligations for eligibility to receive unemployment benefits were broadened to require the long-term unemployed to participate in labor market programs such as training or subsidized employment.

Germany introduced stronger incentives recently for workers receiving unemployment compensation to perform seasonal work. In addition, unemployed workers starting their own businesses will be provided funding for 6 months. Suspension periods have been increased from 8 to 12 weeks for unemployed workers who have not accepted a job offer or have refused to participate in training.

The United States also has taken several initiatives to strengthen the link between unemployment insurance and labor market programs. The Worker Profiling and Re-employment Services System changes the focus of the Unemployment Insurance system from passive income support to active efforts at reemployment by identifying workers who are likely to experience long-term unemployment and to provide a package of job search assistance services. In addition, the Self-Employment Assistance Program encourages and enables unemployed workers to create their own jobs by starting their own small businesses using unemployment benefits for that purpose.

Strengthening internal labor markets

In the 1990's, policymakers also recognized the need to strike a balance between the external flexibility (flexibility outside the firm) promoted in the 1980's and the increasing need for functional or internal flexibility (flexibility within the firm) to modify rules for fixing wages, defining jobs, and allocating labor among alternative uses.

The OECD notes that public policy needs to steer a middle course between two risks: that "too high a degree of external labor market flexibility" has an adverse effect on efforts to improve skills, redesign jobs, and redeploy workers within an enterprise. In addition, according to the OECD, "too strong an internalization of the labor market impinges on reallocation of labor throughout the economy, and segments the labor force between those with secure career jobs and those with casual, dead-end jobs."[29]

As countries have been forced by increased world competition and technological change to move away from mass-produced, standardized goods and toward products and services tailored to the needs of particular customers, internal labor market flexibility or functional flexibility has become even more important. The OECD concludes that "functional flexibility"—based on the quality of work required, greater mobility within jobs across tasks, reduction of job boundaries, greater flexibility in job design, and training and retraining—"appears to have clearly outdistanced the Fordist over-emphasis on numerical flexibility and the quantity of labor, controlling the number of hours worked and the organization of working time, regulation of hiring and dismissals, and use of part-time and temporary workers".[30]

The OECD's labor ministers, meeting in 1992, supported a new emphasis on greater internal labor market flexibility by recommending that governments "encourage the private sector to adopt productivity enhancing approaches to work organization, workplace training and greater participation and involvement of workers.[31] In 1993, OECD finance ministers stressed the need to "create skill-based jobs" by making it easier to develop new technology and innovative work practices, including flexibility in work arrangements."

The November 1993 European Commission report, *Growth, Competitiveness and Employment*, stresses the need for both internal and external flexibility and suggests that "the question of labor flexibility needs to be examined from two angles: that of the external labor market, where supply meets demand, and that of the market internal to each business, i.e. the human resources at its disposal which it adjusts according to its needs."[33]

The European Commission concludes that "the more a firm adjusts its manpower resources by making people redundant or by having recourse to fixed-duration contracts, the greater the risk of unemployment and the more prohibitive the external costs become." The Commission states that deregulation of work during the 1980's "has certainly enhanced the external flexibility of the labor market, but has failed to take into account the potential benefits of internal flexibility," which it defines as "improved human resources management in firms."[34] Some argue that the inability of the industrialized countries to adjust to the external shocks of the 1970's and 1980's could have resulted from the failure of employers to adapt their work organizations to changing conditions, which resulted in increasing levels of unemployment.

IN SUM, with the unemployment rate within the European Union increasing from 8.4 percent in 1990 to 10.7 percent in 1993 (see table 1), interest is once again focusing on the European social welfare system as a major impediment to

labor market flexibility and employment growth. In its just released report, the *OECD Jobs Study: Evidence and Explanations*, the OECD recommends a variety of measures to increase labor market flexibility, among them reducing nonwage labor costs, reassessing the role of statutory minimum wages as an instrument for income redistribution, reforming employment security provisions, and reforming unemployment and related benefit systems. These recommendations were praised by the business community while trade unions took strong exception to them, noting that they were potentially divisive.

Labor market flexibility is a concept that defies a simple definition and that will continue to have different meanings for different people. "In England and the rest of Europe, labor market 'flexibility' is code for the freedom of employers to fire workers and reduce wages," was one explanation at a conference in Britain. "But in the United States, labor market flexibility is generally a virtue, one of our great strengths . . . flexibility means empowering employees, flattening hierarchies, and enabling workers to gain additional skills so they can move easily from one job to another—whether to a new position in the same company or new job in a different city. To be sure, in some cases, America's flexibility allows employers to lay off workers or to pay low wages. But that type of flexibility is ultimately foolish, because it succumbs to the diabolical trade-off. It generates additional jobs at the expense of high living standards. The goal must be *both*, which is why in any advanced economy, the links between citizens and the working world must be strong but supple."[35] □

Footnotes

[1] U.S. Secretary of Labor Robert B. Reich, remarks, ILO High Level Meeting on the World Summit for Social Development, Geneva, June 10, 1994.

[2] *Labor Force Statistics* (Paris, OECD) 1971–91.

[3] *Ibid.*

[4] Paul McCracken, et. al, *Towards Full Employment and Price Stability* (Paris, OECD, 1977), pp. 28–29.

[5] *OECD Observer*, Paris, September 1980, pp. 9–10.

[6] *Economies in Transition—Structural Adjustments in OECD Countries*, (Paris, OECD, 1989), p. 16.

[7] "U.S. Government Approach to Structural Adjustment" (unpublished), Washington, Department of State, 1984.

[8] James A. Baker III, U.S. Secretary of the Treasury, remarks, OECD Council Ministerial, Paris, April 12, 1985.

[9] *Labor Market Flexibility*, report by a high-level group of experts to the Secretary-General, OECD, Paris, 1986.

[10] The ILO has produced a series of country monographs on unemployment and labor market flexibility, including *Unemployment and Labor Market Flexibility: the United Kingdom, 1986*; *Unemployment and Labor Market Flexibility: Finland, 1990*; and *Unemployment and Labor Market Flexibility, Austria, 1991*. Reports also were prepared for Italy, the Netherlands, Spain, and Sweden.

[11] Katharine G. Abraham and Susan N. Houseman, "Does Employment Protection Inhibit Labor Market Flexibility? Lessons from Germany, France and Belgium." Paper presented for the NBER/Ford Project, "Social Protection vs. Economic Flexibility: Is There a Tradeoff?" 1993.

[12] Hugh Mosely, "Employment Protection in Europe," *Employment Observatory Policies #44* Berlin, Winter 1993.

[13] Christoph Buechtemann, "Introduction: Employment Security and Labor Markets," in Christoph Buechtemann, ed., *Employment Security and Labor Market Behavior: Interdisciplinary Approaches and International Evidence* (Ithaca, NY, ILR Press), 1993, pp. 33–39.

[14] *The OECD Jobs Study: Evidence and Explanations*, Paris, chapter 6, (forthcoming).

[15] *Labor Market Policies for the 1990's*, (Paris, OECD, 1990), pp. 21–33. *Employment in Europe, 1993*, Commission of the European Communities, Luxembourg, pp. 177-81.

[16] Gary Burtless, "Jobless Pay and High European Unemployment," in Robert Z. Lawrence and Charles L. Schultze, eds., *Barriers to European Growth: A Transatlantic View* (Washington, The Brookings Institution, 1987).

[17] *OECD Employment Outlook*, Paris, 1991, p. 201.

[18] *Ibid.*, p. 201.

[19] *The OECD Jobs Study*, chapter. 5.

[20] Lawrence F. Katz and Alan B. Krueger, *The Effect of Minimum Wages on the Fast Food Industry*, NBER Working Paper No. 3997 (Cambridge, MA, 1992).

[21] *OECD Employment Outlook*, Paris, 1991, p. 51.

[22] *Report of Japan for the OECD Employment/Unemployment Study*, Paris, April 1993.

[23] *A Programme for Full Employment in the 1990s*, Report of the Kreisky Commission on Employment Issues in Europe (Oxford, Pergamon Press, 1989).

[24] Peter Doeringer, "Flexibility and Equity: The American Experience," European and American Labor Markets (Washington, National Planning Association, 1992).

[25] *Economic Report of the President*, 1994.

[26] *OECD Economic Outlook*, Paris, July 1991, p. 49.

[27] *OECD Economic Outlook*, Paris, June 1985, p. 3.

[28] *OECD Economic Surveys*, Paris, 1991–93, and recent press accounts.

[29] *Labor Market Policies for the 1990s*, (OECD, 1990).

[30] *Technology and the Economy: The Key Relationships*, (Paris, OECD, 1992), p. 97.

[31] "Communique of the Meeting of the Employment, Labor and Social Affairs Committee at Ministerial Level" Paris, OECD Press Release, January 16, 1992, p. 5.

[32] "Communique of the Meeting of the Council at Ministerial Level" (Paris, OECD Press Release, January 4, 1993), p. 7.

[33] "Growth, Competitiveness, Employment: White Paper," Commission of the European Communities, Brussels, 1993, p. 17.

[34] "Growth, Competitiveness and Employment," Note for the Council of Ministers (Economic/Finance) on the economic elements of the White Paper, Brussels, 1993 paragraphs 69 and 82.

[35] U.S. Secretary of Labor Robert B. Reich, remarks before the Institute for Public Policy Research, London, June 1994.