



Mutual Learning Programme

DG Employment, Social Affairs and Inclusion

Discussion paper for MLP Expert Workshop on Measures to Address Labour Market Segmentation

**Expert Workshop on "Measures to Address Labour Market
Segmentation"
Ljubljana (Slovenia), 9 November 2015**

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1 Introduction

What do we mean when we talk about labour market segmentation? The term has been used in different ways over the past decades. In this report, I will use it to refer to an increasingly salient divide in European labour markets between secure and insecure jobs. This divide has been institutionalised by the creation and expansion of non-standard forms of employment, most notably temporary employment (such as fixed-term and agency work). For our purpose, it cannot be overemphasised that it does not make much sense to think of segmentation in static terms. A labour market is only segmented if there are significant mobility barriers. A large stock of temporary workers in the labour market is unproblematic if there is high mobility into secure jobs. And indeed, as I will show, many temporary workers make such a successful transition. Segmentation exists, however, if workers feel 'trapped' in unstable and insecure jobs, interrupted by repeated unemployment spells. Addressing segmentation, then, means addressing (lacking) mobility into stable jobs.

To be more specific, we have to be clear about which problems resulting from segmentation we want to address. With some simplification, they can be found in three areas: macro-economic efficiency, workers' well-being, and repercussions for social cohesion and the legitimacy of democracy. Regarding macro-economic effects, there are indications that the growth of temporary employment has hampered productivity growth (because investment in the workforce is discouraged) and that it has failed to increase employment levels (because secure employment is substituted with temporary jobs) (Boeri and Garibaldi 2007; Boeri 2011).

There is also strong evidence that job insecurity and temporary contracts in particular depress workers' health and wellbeing (Benach et al. 2014; De Cuyper et al. 2008; Sverke et al. 2002). The same is, of course, true for unemployment and poverty, experiences that are inevitable if mobility out of insecure jobs is lacking. There are strong indications that the stress caused by such social problems impedes not only health, but also interferes with central aspects of people's lives, including cognitive abilities, family formation and parenting (Mani et al. 2013). What makes segmentation and labour market risk particularly stressful is that many European welfare states are ill-prepared to deal with non-standard workers. Built on the assumptions underlying the post-war employment model, eligibility criteria for social insurance benefits often disadvantage workers with short and interrupted work records (Berton et al. 2012; Clasen and Clegg 2011; Hinrichs and Jessoula 2012).

These links are sufficiently well-established and generally accepted as normatively problematic effects of segmentation. Less often considered are political repercussions in the form of waning trust in European governments and democracies. Throughout Europe, the influence of populist anti-establishment parties has increased (Kriesi 2014). Without condemning these parties per se, they should be taken as a warning sign of growing disenchantment with democracy. Such disenchantment, expressed in alienation or apathy, is certainly a major risk for European societies, given the political challenges ahead of them. And we should seriously consider the possibility that this disenchantment is partly related to the fact that some citizens perceive themselves as losers of economic change - for instance because they feel trapped in a cycle of insecurity and unemployment.

Hence, my premise in this report is that measures to address labour market segmentation should primarily improve non-standard workers' socio-economic situation. But for the sake of social cohesion and democratic legitimacy, they should also break with the 'dualising' reforms of the past and signal more solidarity across labour market divides.

To preview the message I will put forward in this report: the best way to improve the well-being of insecure workers and their integration in politics is to ensure sufficient possibility for upward mobility. This begs, of course, the question how to ensure mobility. As I will show, it is not always easy to answer. Second, and equally important,

we need to make sure that insecure workers' disadvantage is not multiplied through the welfare state, that is, through 'social insurance penalties' related to fragmented employment biographies. Moving to more universal systems can substantively improve the social situation of vulnerable workers and send a strong signal that society does not leave some citizens behind. Third, it is substantively and symbolically important that employers contribute to the social costs of their hiring practices. I will argue in favour of the French prime de précarité (and similar provisions recently implemented in other countries), a severance payment in case employers do not offer a permanent job to temporary workers.

The report is structured as follows. I begin with a background section on patterns of temporary employment in the European Union. It shows that there is considerable segmentation between temporary and permanent job, even if upward transitions happen frequently. In the subsequent section, I review recent attempts of member states to address labour market segmentation on four dimensions: employment protection legislation, active labour market policies, unemployment benefits and working time flexibility. Subsequently, I discuss economic and political challenges to address labour market segmentation. A final section concludes and derives policy recommendations.

2 Background: Labour market segmentation in the European Union

As mentioned before, I will focus on a specific form of segmentation in this report - segmentation between workers with permanent and temporary employment contracts. This is not to deny that other potentially precarious forms of non-standard employment exist: part-time employment, temporary-agency work, and quasi-dependent self-employment. However, as opposed to temporary employment, part-time employment is predominantly voluntary in most European countries.¹ And while temporary agency work and dependent self-employment can be highly precarious, they make up considerably smaller shares of the European workforce.

Figure 1 presents the development of the share of workers with temporary employment contracts in the EU-28 countries. Besides the share among all wage earners, it also presents shares among young (15-29 years) and older workers (55-54 years). First of all, there is considerable variation across member states. Low shares of around six per cent or less are, for instance, observed in Bulgaria, Estonia, Latvia, Lithuania, Romania, and UK. Shares considerably above the EU-28 average of 14 per cent can be found in Croatia, Sweden (both 17 per cent), Cyprus (19), Portugal, the Netherlands (both 21), Spain (24), and Poland (28).

The solid black line in Figure 1 shows very clearly that the young are disproportionately affected by temporary employment. While this is a well-known pattern, a disconcerting finding is that the gap between the young and the general population is growing dramatically in some countries. This is particularly true in Croatia, France, Italy, Netherlands, Poland, Slovenia, and (in most recent years) Spain. Also in Germany, there is a growing share of temporary employment among the young, but the development is difficult to assess against the background of Germany's sizeable apprenticeship system (in which work contracts are usually temporary).

Temporary employment in the age bracket 55-64 is substantially less pronounced compared to the general workforce in virtually all member states. The highest shares are observed for Cyprus, Hungary, Portugal, Spain (all around ten per cent) and Poland (18). Moreover, the development in this group is rather stable. Hence, we can conclude that the problem pressure in terms of segmentation is far stronger among young workers and that it seems advisable to focus on this group.

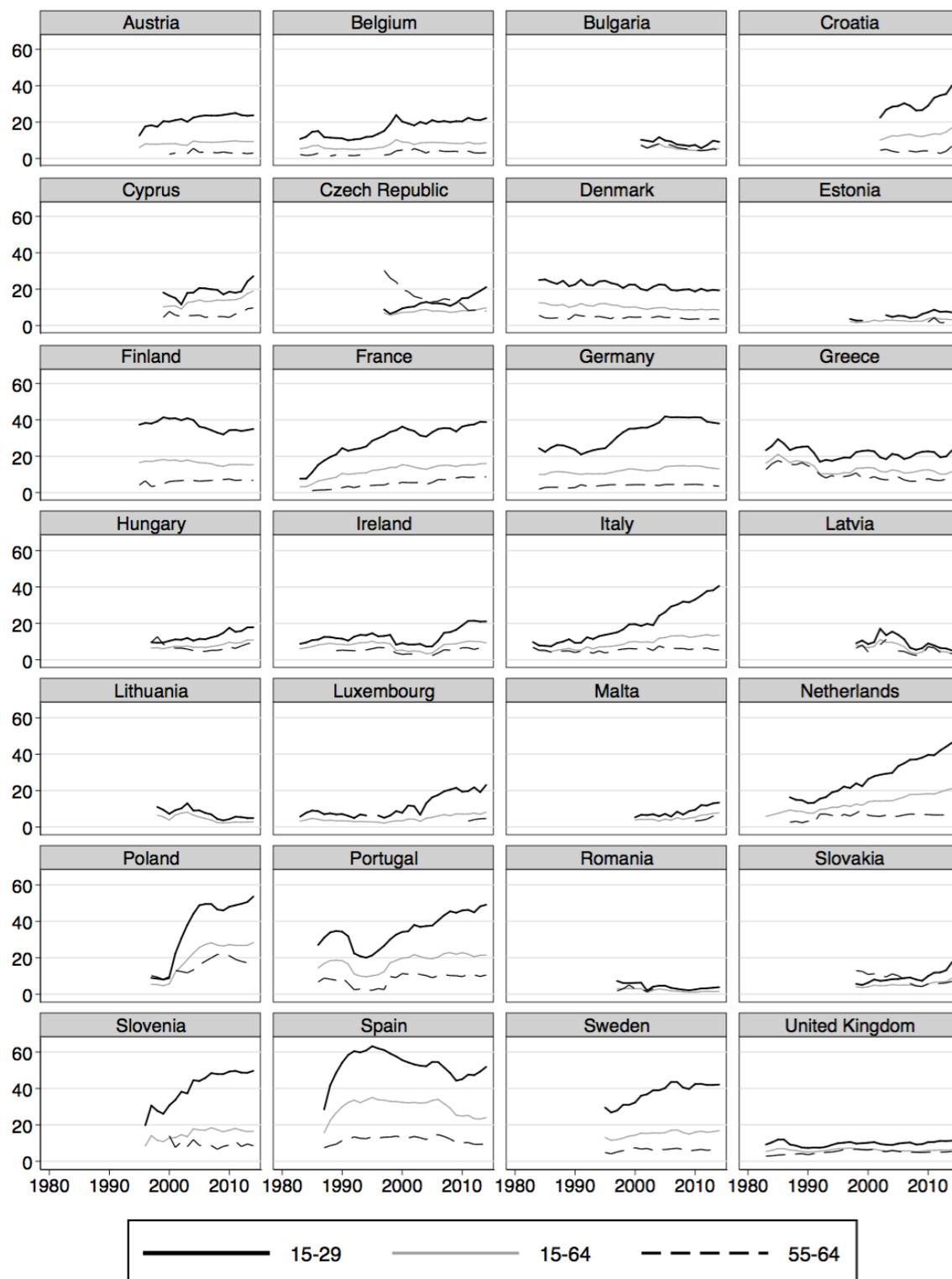
Looking at stocks of temporary workers might be misleading because policy changes affect newly recruited workers only. Figure 2 therefore presents the share of temporary contracts among new employment contracts (less than three months old). Also here we observe a rather strong persistence over the past years and in many member states the use of temporary contracts among newly recruited workers remains pervasive.

A striking pattern in Figures 1 and 2 is that there is *not a single member state that managed to reverse the trend of growing temporary employment among the young*. A partial exception is Spain, but the decline came from an extremely high level and has been reversed in recent years. Hence, the project of "addressing labour market segmentation" cannot build on easily identifiable best-practice cases. One important reason for this lack of success arguably is that many of the most segmented countries face a difficult overall labour market situation. The upper panel in Figure 3 plots against each other unemployment rates and temporary-employment shares among those aged 15-24 (in 2014). With youth unemployment rates above 30 per cent, the Mediterranean countries in particular simply do not have enough jobs to offer young people secure positions in the labour market. This also means that reducing temporary employment cannot be the top priority of policy makers in these countries. There is little doubt that

¹ Only in Greece, Italy, Spain, and Slovakia was the majority of part-time employment involuntary in 2014. Only in Italy and Spain does it account for more than ten per cent of employment (OECD 2015).

the negative socio-economic effects of unemployment are far more severe than those of being in a temporary job.

Figure 1: Shares of temporary in total dependent employment in different age groups, 1983-2014



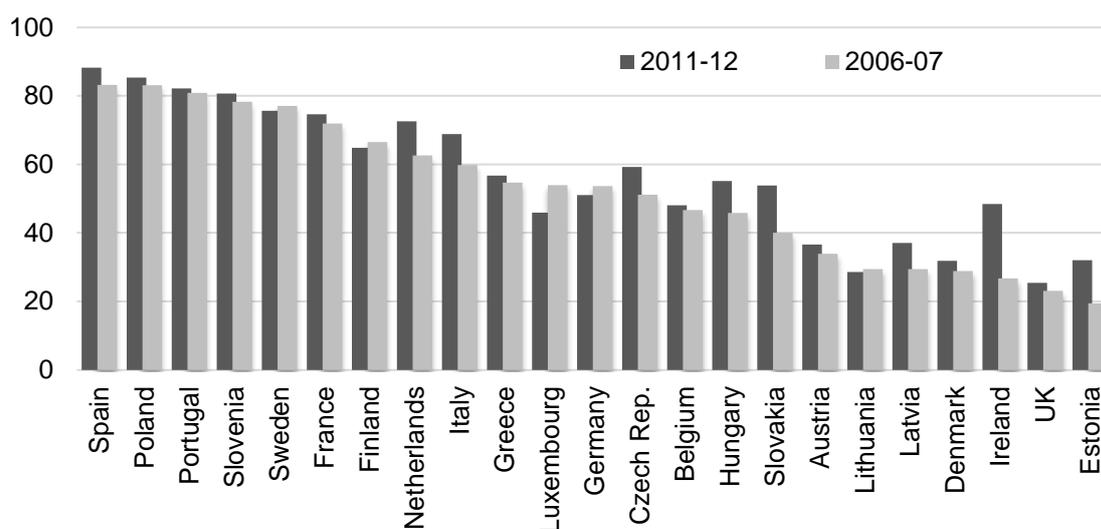
Source: Eurostat (2015)

This point is illustrated best by examining the upward mobility of temporary workers. Comparable data on transition probabilities is difficult to find, but the OECD (2015, p. 188) has recently provided numbers for the long-term probabilities of temporary

workers to obtain a permanent contract. This is an extremely useful indicator. Temporary employment does not produce segmentation, if it is merely a transient experience that leads to stable labour market inclusion. However, if temporary workers stay in insecure positions for a long time, we can conclude that they are 'trapped' in insecure and precarious jobs.

However, there also is a group of countries in which labour market context is less disadvantageous, and temporary employment nonetheless pervasive among the young. This includes Finland, France, Luxemburg, Netherlands, Poland, Slovenia, and Sweden. Austria and Germany could also be included, even if - as mentioned above - their temporary-employment shares are probably inflated by apprentices. Any policy advice will have to reflect the strong variation in overall labour market performance across member states.

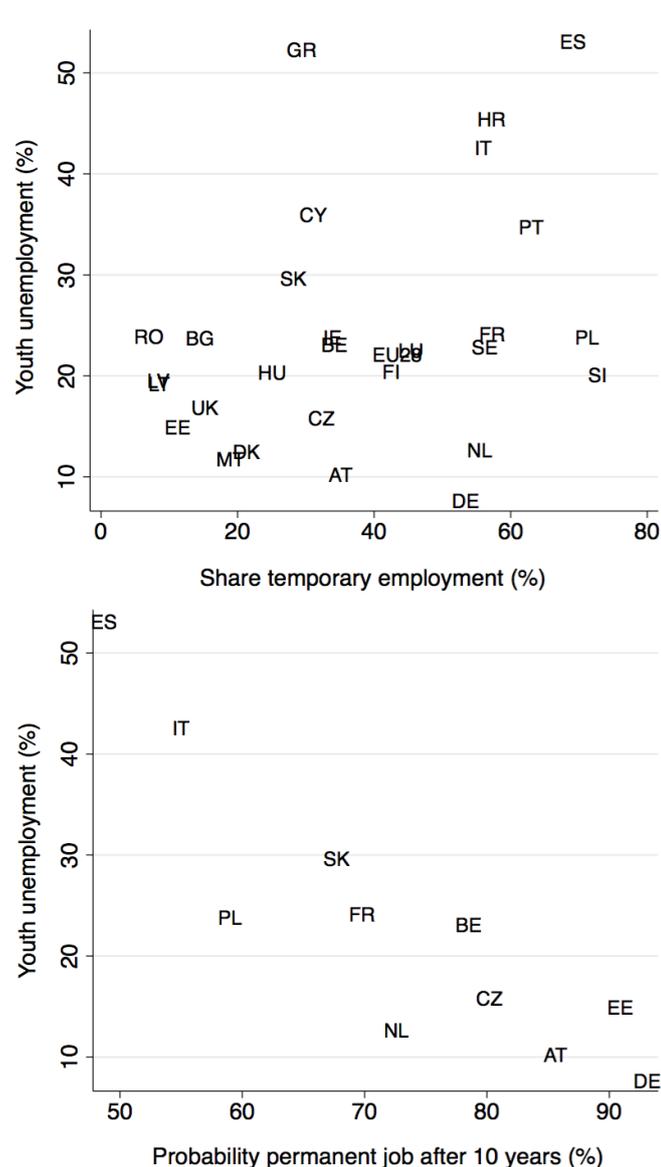
Figure 2: Share of temporary contracts among new employment contracts



Source: OECD (2014, p. 150)

The lower panel in Figure 3 plots against each other youth unemployment rates and the probabilities that temporary workers will obtain a permanent contract over a ten-year period (unfortunately, data is only available for a limited number of European cases). The plot reveals that there is significant variation in transition rates. Whereas virtually all temporary workers move to permanent jobs in Austria, Estonia, and Germany, around half of the workers in Italy and Spain are still in temporary jobs - even after ten years. The plot also reveals that the prospects for upward mobility strongly correlate with general labour market performance. This is not surprising, but it is important to emphasise that labour market segmentation in many European countries is closely related to the macro-economy and insufficient demand for labour.

Figure 3: Youth unemployment, temporary employment and transition probabilities



Source: Youth unemployment and share temporary employment: Eurostat (2015); Probability permanent job after 10 years: OECD (2015, p. 188)

Three conclusions emerge from the analysis:

- 1) Segmentation, measured as shares of temporary employment, is a persistent feature of many, but not all European labour markets. So far, no member state has managed to reverse the trend.
- 2) Segmentation is more severe in member states with high youth unemployment. This concerns the share of temporary employment as well as the prospects of mobility into permanent jobs
- 3) Even if many temporary workers make a successful transition into permanent employment, segmentation does exist. Considerable shares of temporary workers appear to be 'trapped' even in the long run.

Labour market segmentation and political disenchantment

Labour market segmentation is usually seen as a socio-economic problems. However, recent developments suggest that it might as well turn into a political problem. In many member-states political conditions have changed in the aftermath of the crisis. There

seems to be a widespread dissatisfaction with politicians and with how they handle the economy in particular. This is expressed in street protest (e.g. by the Spanish *Indignados*), new or invigorated populist parties (e.g. the Italian *Movimento Cinque Stelle*), and depressed political participation.

Even though it is difficult to show the causal link between segmentation and alienation, disenchantment, or radicalisation, economic grievances do seem to play a role. There is plenty of evidence that the unemployed tend to withdraw from politics (e.g. Anderson 2001, Gallego 2007, Marx and Picot 2013). There also is evidence that the crisis has depressed satisfaction with democracy in those European countries most affected by it (Armingeon and Guthmann 2014). Marx (2015) shows that this trend is a) stronger for temporary workers than for permanent workers and b) more pronounced in the younger democracies of Central and Eastern Europe. He also shows that temporary employment can strongly depress political trust and participation in elections, if workers do not perceive chances for mobility in better jobs.

In sum, research suggests that segmentation may hamper the legitimacy of European democracies by alienating some citizens and by violating norms of what is a fair distribution of social rights. The crisis seems to have exacerbated this process.

3 Measures taken to address labour market segmentation and their impact

How have member states responded to labour market segmentation? In this section, I will present measures taken over the past years in the fields of employment protection legislation, unemployment benefits, active labour market policies, and working-time flexibility. To reduce complexity, I will focus this review on countries with substantive shares of temporary workers and the most significant policy changes.

Employment protection legislation

It is often argued that segmentation results from institutional mobility barriers. Because dismissals are costly in strictly regulated labour markets, employers make use of temporary contracts that allow for 'cheap' adjustment of the workforce. Many policy experts have recommended deregulating employment protection legislation (EPL) for regular contracts, but this has proven difficult for political reasons. Instead, many member states have deregulated the use of temporary contracts - a strategy that has contributed to segmenting the labour market (e.g. Boeri 2011; Kahn 2010).

Thus, there are two possible strategies to address segmentation through EPL reform: deregulating permanent contracts or reregulating temporary contracts. As mentioned above, deregulating permanent contracts has been difficult to implement politically. However, in the aftermath of the Great Recession, some of the most segmented and crisis-ridden countries in Southern Europe have implemented substantial deregulation: France, Italy, Portugal, Greece, Spain, and Slovenia (OECD 2013).

In Portugal, Greece, Spain, and Slovenia post-crisis reforms considerably reduced notice periods and severance pay for (newly hired) permanent workers. In Italy, the recent 'Jobs Act' stipulated that employers do not any longer have to reinstate workers dismissed for invalid economic reasons. While the reforms in Italy, Greece, Portugal, and Spain arguably bring substantive reduction of EPL for permanent workers, reforms in France and the Netherlands were subtler. In France, workers who do not accept collectively agreed wage and working-time adjustments in economic crises can now be dismissed. In the Netherlands, the 2015 Work and Security Act simplified EPL without necessarily lowering it. It clarified in which cases courts or the Public Employment Agency decide on the validity of dismissals. It also introduce a streamlined formula for severance pay, which will considerably reduce the amount in some case, but increase it in others. Hence, the Work and Security Act brings a clarification rather than deregulation of EPL. In the other European countries with high shares of temporary workers (Finland, Poland, and Sweden), no substantial reforms of EPL for permanent workers were undertaken in recent years.

The second possibility to address segmentation through EPL reform is re-regulating temporary contracts. Indeed, there were also some, albeit less far-reaching changes in this direction (OECD 2013; 2014). One trend is to make the use of temporary contracts more expensive for employers, while at the same time offering monetary incentives to allow for transitions into permanent jobs. In Slovenia, the 2013 labour market reform raised employers' unemployment insurance contributions for temporary jobs. If the temporary job is, however, converted into a permanent one, employers are exempted from contributions for a limited time. The social partners in France have agreed on a similar reform. Since May 2013, employers pay increased unemployment insurance contributions depending on the length of the contract. Contributions increase by 3 percentage points, if the contract runs for less than one month, 1.5 if one to three months, and 0.5 for longer contracts. The goal, hence, is to make employers contribute to the costs of extremely flexible hiring practices. Also in France, employers are exempt from contributions for a limited period if they hire younger or older workers on permanent contracts. In Italy, employers since 2012 have to pay a contribution that is 1.4 percentage points higher for temporary than for permanent workers, but get it reimbursed if the job is later converted into a permanent one. In Spain, from 2015 onwards, temporary workers receive a higher severance pay at the end of their contract.

The payment corresponds to the salary of twelve days per year of employment with the firm and is considerably lower than for permanent workers.

Other restrictions of temporary work were implemented in the form of a lower maximum duration. In Slovenia, the 2013 reform limited the time an employer can use temporary contracts for a specific job to two years. In the Netherlands, the maximum duration was limited from three to two years in 2015. However, collectively agreed deviations are still possible, so that it remains to be seen what the reform means in practice.

Some countries made the regulation of temporary contracts more permissive in recent years. Italy has gone furthest in this direction. A recent reform abolished the need to indicate a valid reason for temporary employment. It also extended the maximum duration as well as the possible number of renewals. At the same time firms are, however, not allowed to use temporary contracts for more than 20 percent of the workforce. The maximum duration of temporary contracts was also increased in Greece and Spain.

To sum up: on the face of it, there were some important changes in the field of EPL, an institution that was considered highly path-dependent before the crisis. Overall, there is a trend in some of the most segmented countries to lower dismissal costs for permanent workers in combination with a moderate (and sometimes ambiguous) re-regulation of temporary contracts. Did these changes contribute to reducing segmentation? Given that many of the reforms have only been implemented in the past three to five years, it might still be too early to evaluate their impact on hiring practices with currently available data. However, revisiting Figure 1 casts some doubt on their effectiveness. It shows that the share of temporary contracts has even increased in the countries that deregulated EPL during the crisis. Between 2010 and 2014 the share for workers aged 15-29 increased by roughly seven percentage points in Italy and Spain, three in France and Portugal, and one in Greece. Of course, we do not have a counterfactual situation so that it is difficult to assess the exact influence of the reforms. However, so far there is no discernable contribution to reducing segmentation.

Unemployment benefits

The coverage of temporary workers by unemployment insurance schemes is an important aspect contributing to labour market segmentation. In many countries, the formulas by which benefit generosity and eligibility are calculated tend to disadvantage workers with short employment spells. Moreover, since benefits are often tied to former earnings, the wage penalty of temporary workers translates into worse unemployment protection. The problem is particularly severe in many Southern European countries that lack a universal safety net. Berton et al. (2012) show for instance that in Italy, non-standard employment comes with a significant penalty in social insurance systems.

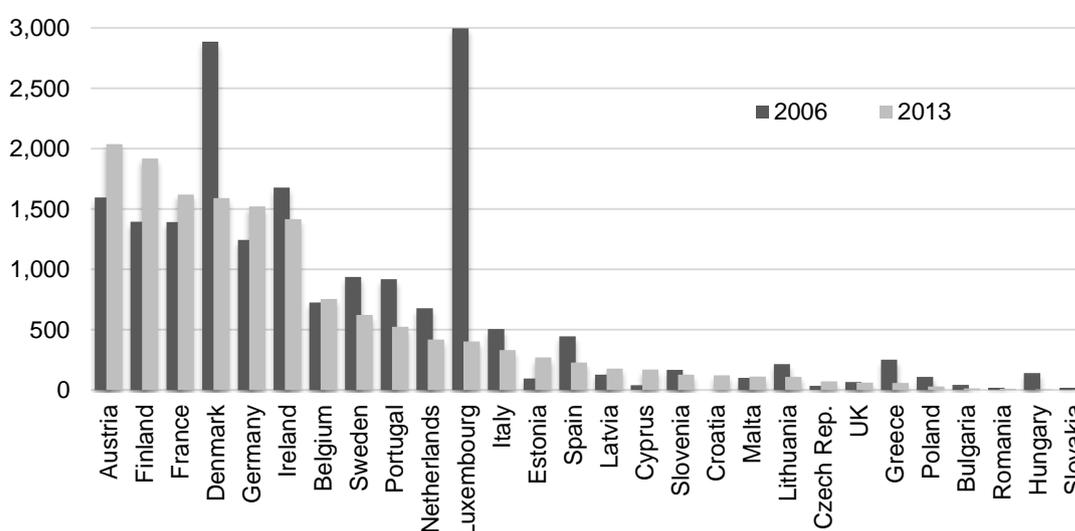
Modernizing the welfare state towards universalism is a difficult task in times of severe budget constraints. A recent step towards more universal benefits was undertaken by the introduction of *Assicurazione Sociale per l'Impiego* (ASPI) in Italy in 2013. ASPI replaces the rather fragmented system of unemployment benefits and makes the system more generous. Interestingly, the reform also introduced *Mini-ASPI*, a special benefit with lower contribution requirements, specifically designed for including workers with short employment spells. While benefit generosity will be the same as for ASPI recipients, duration of *Mini-ASPI* will be lower and conditional on the actual contribution record (Berton et al. 2015). In May 2015, the Italian government replaced ASPI and *Mini-ASPI* with a new scheme (*NASPI*) that uses rather permissive eligibility criteria close to *Mini-ASPI* (13 weeks of contributions in the four years before unemployment). With the goal to better reflect the situation of temporary workers and to extend coverage, the reform is a remarkable step and deserves careful evaluation once fully effective. It has the potential to serve as a model for countries facing similar challenges as Italy.

Active labour market policies

Another possibility to address labour market segmentation is expanding active labour market policies (ALMPs) and human-capital investment in particular. In segmented labour markets, vulnerable workers have a higher risk of becoming unemployed and are therefore more likely to come in contact with public employment services. This, in principle, provides the opportunity to prepare vulnerable workers better for the labour market and to improve future employment outcomes (e.g. job stability or wages). Evaluation studies show that skill-oriented ALMPs are effective in this regard: they improve the chance of being in employment over the long-run and hence clearly contribute to reducing segmentation (Card et al. 2015). Activation policies (e.g. in the forms of sanctions in case of non-compliance) are only effective in the short-run but do not lead to better long-term outcomes. As such, they are unlikely to contribute to reducing segmentation (*ibid.*).

Hence, expanding investment in training the unemployed appears as a plausible strategy to improve long-term labour market integration. To assess which member states followed this route Figure 4 presents ALMP expenditure for the category “Training” per person looking for work in 2006 and 2013, the last available data point. Expenditure is expressed in purchasing power standards, so that small and large economies are comparable. The Figure reveals that there is no general trend towards increased spending on training. Among the more segmented countries, the trend rather seems to go towards less spending per unemployed person. In some of the most segmented countries, this decline comes from a rather low pre-crisis baseline, namely in Greece, Italy, Poland, Spain. Also in the Netherlands, Portugal, and Sweden the numbers point to a marked reduction in training expenditure. Among the countries with moderate-to-high shares of temporary workers, Finland, France and Germany have increased training expenditure. In sum, we cannot identify a clear trend towards more investment and training.

Figure 4: Training expenditure per person looking for work 2006 and 2013 (in purchasing power standards)



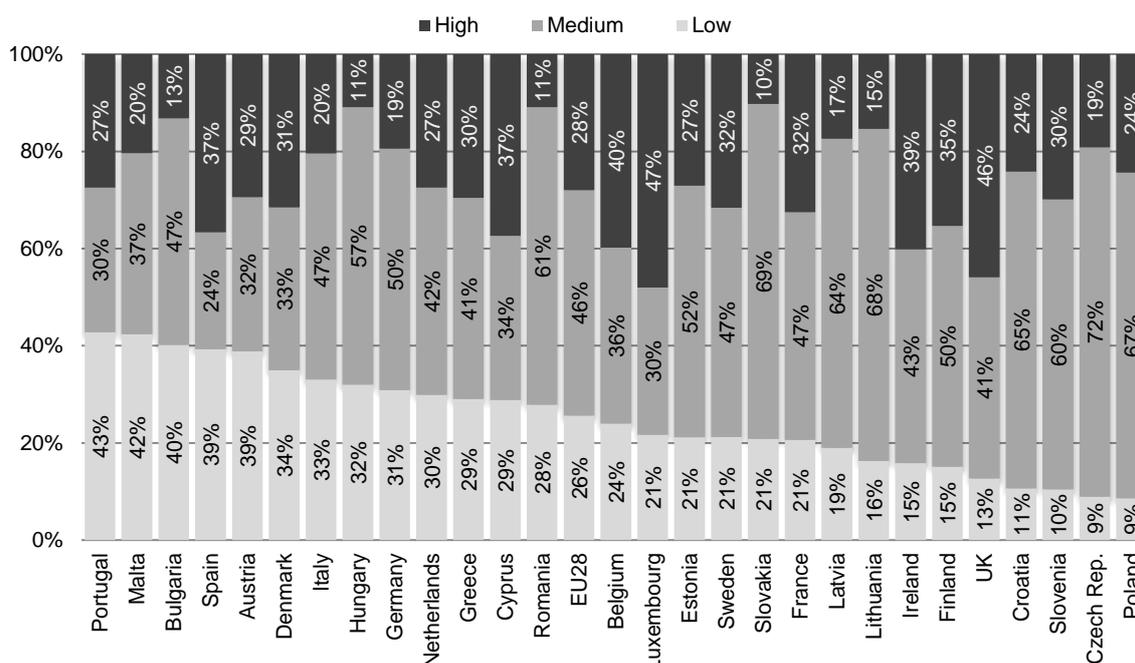
Source: Eurostat (2015)

However, there is one important limitation to the contribution of ALMPs to tackling segmentation. Training the unemployed is most useful for persons with rather low or deteriorated skills, such as in the case of the long-term unemployed. It is more doubtful how effective it is for young people with recent educational experiences and for those who have frequent employment spells in the form of temporary employment. Figure 5 presents a breakdown of the temporary workforce by educational attainment. It shows that workers with low-skills, the prime beneficiaries of training, are in a minority in all

countries (although they account for considerable shares in some segmented labour markets, most notably Portugal and Spain).

Quite to the contrary; in some countries a sizeable share of the temporary workers is highly skilled. Usually between one-fourth and one-third of all temporary workers have a tertiary education. This group is unlikely to benefit from ALMP intervention in the form of additional training. National policy-makers should therefore carefully evaluate mobility patterns of people with different skill background to decide which groups should actually be targeted by training (which is a rather costly policy intervention). In sum, ALMPs can make a considerable contribution to improving long-term labour market integration, but particularly in countries where there are insufficient jobs for skilled workers, they are not a general remedy for segmentation.

Figure 5: Composition of temporary workers by educational attainment, 2014



Source: Eurostat (2015)

Working-time flexibility

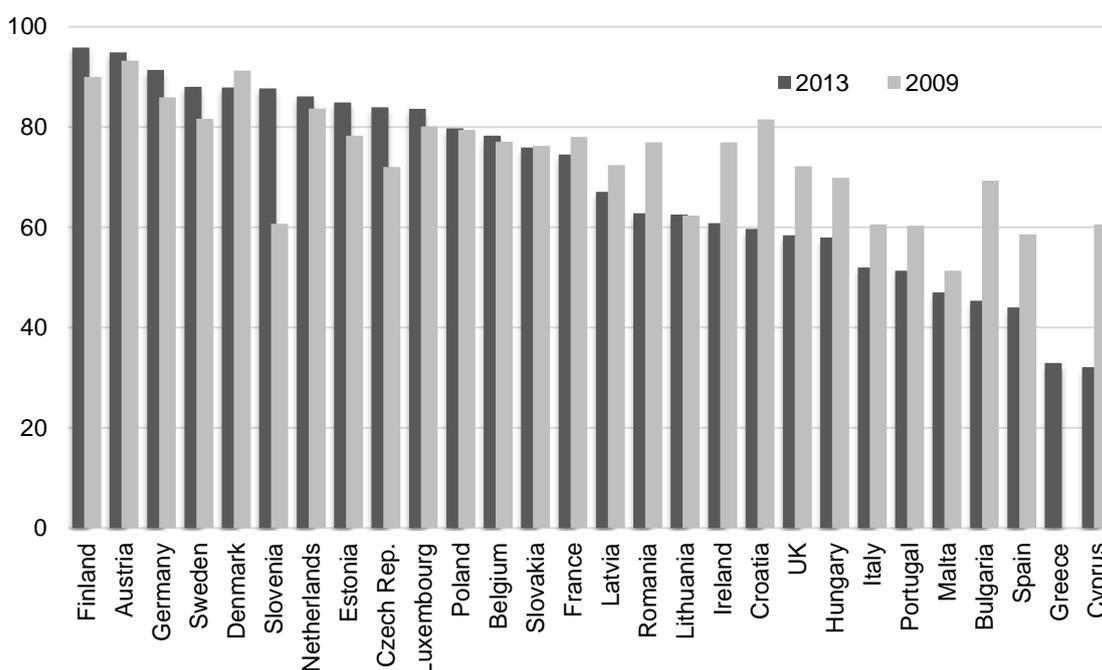
The use of temporary workers reflects employers' need for numerical flexibility. However, adapting staff levels is only one way to achieve it. A functional equivalent to hiring and firing is internal numerical flexibility, for instance in the form of working-time accounts. Such accounts allow accumulating surpluses (or deficits) that is compensated with time off (overtime) later on. As such, working-time accounts help employers to respond to workload fluctuation with using temporary workers. Germany is often cited as an example. In Germany, working-time flexibility has greatly increased in the past decades (Eichhorst and Marx 2011) and played an important role in reducing the impact of the crisis on jobs (in conjunction with government subsidies in the form of a short-time work scheme). It also should be stressed that the availability of working-time flexibility in Germany complements (and possibly limits) the use of temporary employment without making it entirely redundant.

Working-time flexibility is hard to induce through public policy and rather depends on firm-level practices and industrial relations. The feasibility and spread of such practices also greatly depends on the sector and the size of firms. It is therefore better to examine actual firm practices rather than legislation. Figure 6 presents the shares of companies with ten employees or more that allow their workers to accumulate overtime. Admittedly, this is only a crude indicator that says nothing about management's and

workers' discretion in using accumulated hours. But it provides a rough picture of how widespread flexible working time is in the member states.

The results reveal considerable variation in the use of flexible working time (which can, however, be partly related to different composition of national economies by sector and firm size). Interestingly, many countries with high shares of temporary employment rank in the bottom of the distribution and show a recent decline in the use of working-time accounts. This is true for Croatia, Cyprus, Italy, Portugal, and Spain. However, the fact that, for instance, Poland and Sweden combine a wide spread of working time flexibility with very high shares of temporary employment underlines that such flexibility is not a remedy against segmentation per se. More research will be necessary to determine which forms of working-time flexibility exactly provide alternatives to temporary employment.

Figure 6: Percentage of companies that allow employees to use accumulated overtime for days off in 2009 and 2013



Source: Own calculations based on 2009 and 2013 rounds of European Company Survey (European Foundation for the Improvement of Living and Working Conditions 2010; 2015). *Note:* The surveys cover companies with ten or more employees.

A case that stands out is Slovenia. There seems to be a recent surge in the use of working-time accounts. Should this pattern also be visible in finer-grained national datasets, Slovenia would a possible case to examine more closely to derive lessons for policy making.

4 Challenges facing Member States in addressing labour market segmentation

In this section, I will briefly point to the challenges policy-makers face in reducing labour market segmentation. These challenges can be grouped in five categories.

Political preferences: if segmentation is addressed through reducing social rights of 'insiders', it can be difficult to organize democratic majorities for such proposals. EPL is a case in point and it is no surprise that deregulation only took place under severe reform pressure. Also expanding social protection for vulnerable workers could be met with resistance from the majority with lower unemployment risks, because of the considerable costs of such reforms. However, it also should be noted that the political economy literature greatly exaggerates the extent to which public opinion is divided between insiders and outsiders. There is considerable solidarity across the insider-outsider divide (Marx 2015) policy-makers can appeal to.

Macro-economy: as explained above, in some countries there simply seems to be insufficient labour demand to offer secure jobs to the entire workforce. In a context of high unemployment, it is understandable if workers and policy-makers view temporary employment as the lesser of two evils. Unemployment is a persistent problem in some member states. With the acceleration of immigration and technological change, it is far from clear whether this situation can be improved in the near future. What exacerbates the situation is that in the context of the European debt crisis, (political and economic) room for stimulating the economy is very limited. This leads to the next challenge.

Budget constraints: substantially improving the situation of the unemployed and temporary workers costs money: in the form of training for those with insufficient skills, wage subsidies, decent jobs in the public sector, and adequate social protection (against unemployment and in old age). Needless to say, funding such reforms is extremely challenging in times of austerity. Policy-makers will have to look for ways to make employers contribute to the social costs of their hiring practices - without making temporary contracts so expensive that hiring is discouraged.

Evasion and non-compliance: a reasonable assumption to make is that employers will look for legal loopholes to reduce labour costs. Although there is little systematic knowledge, anecdotal evidence from countries such as France, Italy, and Spain also suggests that there is considerable non-compliance with labour law and that labour inspectorates are insufficiently equipped to deal with this situation. Hence, re-regulation of temporary employment might either be ineffective (if compliance is low) or employers respond with relying on other precarious forms of employment. In many member states a trend towards even more unregulated dependent self-employment seems to be under way already. Another risk is that employers respond to stricter regulation with undeclared work, which would imply strong precariousness and loss of tax revenues.

5 Conclusions and points for discussion

The positive message of this report is that member states take segmentation seriously. There are plenty of policy initiatives with the goal to overcome labour market divides. The more pessimistic message is that, so far, there is little success. Temporary employment keeps rising and youth unemployment still is worryingly high. Admittedly, it probably is too early to evaluate some of the very recent reforms. But one should also consider the possibility that the steps taken so far are insufficient to substantially improve the labour market situation.

So which policy options do exist? And how suitable are they against the background of the identified challenges?

Banning or prohibitively regulating temporary contracts might appear as a solution. However, there is clear evidence that temporary employment can serve as a bridge to permanent jobs. And there is little doubt that negative repercussions of temporary employment are dwarfed by the devastating socio-psychological as well as political effects long-term unemployment can have. To the extent that temporary contracts serve as entry points into the labour market for young workers or long-term unemployed, banning them probably does more harm than good.

Another frequently proposed policy solution, that currently enjoys popularity among policy-makers, is the deregulation of permanent contracts. This solution has some symbolic value, because it does away with a labour market institution that leads to a visibly unfair distribution of job security and market risks. That said, it is hard to see how deregulation should address job insecurity. A low-skilled, inexperienced or otherwise vulnerable worker won't be less vulnerable if his or her temporary contract is replaced with a flexible 'permanent' employment contract. If deregulation, however, does not go far enough, incentives to hire on temporary contracts remain. Member states will therefore have to try to find a moderate level of EPL that balances both goals. Recent EPL reforms can be interpreted as steps in this direction.

Similar reservations can be formulated for the frequently proposed single employment contract. Here, the idea is to replace temporary and permanent contracts with a unified legal framework in which dismissal protection is phased-in with tenure. Again, it provides the symbolic advantage of overcoming legal dualism. However, the problem is that such a framework produces thresholds in dismissal costs before which employers prefer to replace a worker with a new one whose protection starts from zero. This effectively means that newly recruited workers still face the same insecurity, at least for some time. In addition, if thresholds are implicit and employer-specific, workers do not even know how long they can stay with the firm and when they make a transition into secure employment. Depending on how the single-employment contract is modelled, it is quite possible that it makes the situation of workers with short tenure even more precarious than it would be on a temporary contract.

A factor that can mitigate effects of temporary contracts is the prospect of making a successful transition into stable employment. On the other hand, temporary contracts are a real social and political problem, if workers see themselves in a 'dead end'. For policymakers, this means that ALMPs should be at the core of any strategy to improve the situation of low-skilled temporary workers who frequently experience unemployment. At least in countries with relatively well-functioning labour markets, governments should make every effort to ensure that lacking or obsolete skills do not 'trap' workers in chains of unemployment and precarious jobs. However, such efforts are somewhat less promising in countries where there are not enough jobs, even for university graduates. The use of subsidies to encourage conversions of temporary into permanent contracts is a plausible alternative that will have to be carefully evaluated over the next years.

Another important concern for policy-makers should be avoiding multiple disadvantages through the welfare state. I would argue that the modernization of unemployment and

pension systems towards more universal schemes would not only improve the socio-economic situation of temporary workers but also increase the legitimacy of the dual employment model. If society compensates temporary workers for their higher risk by offering decent and accessible social security, this could lessen feelings of political marginalization or exclusion. As the fiscal situation in most affected member states does not leave much leeway for social policy expansion, the politics necessary for such changes are complex and probably involve zero-sum conflicts. However, the recent Italian reforms towards more universal unemployment benefits demonstrate that these are not insurmountable hurdles.

However, an important objection to 'fixing' the temporary employment issue with social benefits and labour market policies is that turnover costs are shifted from employers to society. Another way of compensating temporary workers for their risk is granting them 'insecurity bonuses' as is done in France in the form of the *prime de précarité*. In this system, employers have to pay a bonus to the worker (amounting to ten per cent of the total gross wage paid under the contract) if the employment relationship is not continued after the contract has expired. This system ensures that employers contribute to the social costs of their hiring practices and increases incentives to use temporary contracts responsibly. In addition, it might reduce the perception among temporary workers to be disadvantaged on several dimensions (unemployment risk and lower wages). For such a system to be effective, it would be important that, first, the bonus is high enough to substantively affect employers' incentives and workers' material situation (but without totally discouraging hiring). Second, it has to be ensured that there are no legal loopholes that allow circumventing the bonus. Third, and that is a more general point, the equal-pay principle has to be vigorously enforced through monitoring by unions and labour inspectors as well as through severe sanctions in case of non-compliance. Otherwise, employers can cancel out the insecurity bonus by lowering temporary workers' wages – a practice that seems to be widespread already.

An alternative way to provide temporary workers with employer-financed social security are the Austrian *Mitarbeitervorsorgekassen*. In 2003, severance payments were replaced with a system in which employers contribute on a monthly basis to an account for each worker. When the employment relationship is terminated, workers can withdraw the money from their account (instead of a severance payment) or carry it over to their next job and use it as pension savings. An advantage of this model is that also self-employed can be integrated, which is the case in Austria since 2008. Besides providing additional financial security to insecure workers, the system also overcomes stark differences in separation costs.

There is no magical formula to address labour market segmentation. Fiscal, economic, and political circumstances significantly limit room for manoeuvre. Member states should nonetheless continue to carefully modernize labour law and welfare states, even if it is only possible an incremental way. Radical deregulation of permanent contracts or re-regulating of temporary contracts should be avoided. Policy-makers should also resist the temptation of cutting ALMPs and training programmes in particular. Given its favourable long-term consequences, training targeted programmes targeted at the most needy should be an important pillar in any strategy to address segmentation. Member states should continue to experiment with fiscal incentives to convert temporary into permanent contracts, but carefully evaluate the schemes and make their survival conditional upon success. Finally, it will be important to move towards a better social protection of temporary workers. For economic and symbolic reasons, employers will have to make a relevant contribution to this. Austria, France, and Italy exemplify different approaches that could be developed into more broadly applicable strategies to address segmentation.

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