Towards a European Labour Market: Combating Long-Term Unemployment and Improving Trade Unions through Increased Migration

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Should we sacrifice social benefits in the name of greater efficiency or accept that the laws of demand and supply lead to a satisfactory labour market? In this paper, Paul Kelly makes a case for regulation within the EU labour market while highlighting the inefficiencies which come with it. He concludes by showing what the EU can learn from the Anglo Saxon model, and in doing so how it can improve equity and reduce levels of long term unemployment.

Introduction

The market for labour is unique. Whilst the normal rules of supply and demand still apply to it, these rules are severely distorted by problems of asymmetric power and information. As a result, economic considerations of efficiency are often forced to yield to social considerations of equity, resulting in labour regulations which distort the operation of the labour market. Nowhere can this be seen more clearly than in the EU's labour market, where "countries have long attached more weight to social protection than to economic efficiency" (Baldwin and Wyplosz, 2012: 215).

Despite this, although the European labour market is unified in terms of its advanced social welfare system, critical differences remain across member states labour markets. Two of the most crucial issues in labour relations throughout the EU remain the role of trade unions in an increasingly integrated Europe, and managing the rising tide of long-term unemployment (LTU). Because these issues are largely tackled by individual member states, there is a lack of awareness of the fact that the most equitable solutions to these issues lie at the EU level. Only by increasing EU integration and migration can member states hope to tackle these problems, as it is this that can increase the efficiency of the European labour market; removing the spectre of LTU and assisting trade unions to act at a

European level.

Thus far, however, the impact of European integration on European employment has been severely limited, due to indirect and direct barriers to migration. Although increased integration through the free movement of goods and capital has boosted employment throughout Europe, it is only when the remaining restrictions on migration are removed that the true benefits of European integration will appear.

The Operation of the European Labour Market and the Necessity of Labour Laws

The operation of the European labour market is similar to the operation of labour markets everywhere, in that it functions through the laws of supply and demand. According to economic theory, if there are no distortions in this market there should be no involuntary unemployment in Europe, even in a recession (Baldwin and Wyplosz, 2012). This is not to say that there would not be unemployment. This unemployment would, however, be voluntary. People would choose not to work because wages would be considered too low, rather than being unable to work because there are no jobs available. If market distortions such as minimum wage laws, limits on dismissals, minimum working conditions and unemployment benefits are introduced, however, this dynamic is interrupted and involuntary unemployment occurs. As this is considered worse than voluntary unemployment, it is argued that there should be as little interference in the labour market as possible.

Even after a brief examination of this argument, however, flaws emerge. Clearly, what might be assumed to be 'voluntary unemployment' can be, in effect, involuntary, as the wages paid for the jobs available may be too low for an individual to survive on. This shows the necessity of minimum wages and other laws regulating labour. Indeed, in the absence of these laws, employers may gain a disproportionate amount of market power over employees in the negotiation of wages. Coupled with the severe information asymmetries that abound in the labour market, this would make it impossible for employees to judicially evaluate different job options. It is for these reasons that these market distortions are permitted both within the European labour market and labour markets everywhere. In the words of Freeman (2004: 35) 'EU labour markets suck compared to the perfect Invisible Hand of economic theory. But so does the US labour market.' In all labour markets, some degree of economic efficiency is sacrificed for social considerations. What is unique about the EU's labour market is the greater weight these considerations are given compared to its peers in the US or elsewhere. Given the diversity of the European labour market, this is one of its few unifying characteristics. In contrast, the challenges posed by trade unions and LTU are tackled in a variety of diverse ways throughout the EU.

The Effect of Trade Unions

Trade unions play a crucial role in EU labour markets as they provide a check on the excessive market power of firms. Despite this, the strength of trade unions varies across Europe. Whilst Nordic, Continental and Mediterranean trade unions exercise a great deal of market power, trade unions within countries which follow the Anglo-Saxon model do not, except within the public sector. Despite this diversity, the EU remains far more unionised than its international counterparts, with union membership twice the size of the US (Booth et al, 2001). This allows EU trade unions to affect the operation of the European labour market far more than their American counterparts affect the US labour market. This is assisted by the fact that EU integration has not produced a goods market which even approaches the ideal type of perfect competition, but is due to the emergence of the oligopolistic competition produced by large multinational firms. In the words of Booth et al (2001: 86), 'more trade should not be confused with more competitive trade.' This has allowed for the continued existence of a market surplus, which firms have shared with unions. Although such a surplus has resulted in a decrease in efficiency in the goods market, trade unions have improved efficiency in the labour market. This can be seen in collective bargaining which has decreased wage negotiation costs and in decreased turnover costs. This has resulted in the empirical finding 'that highly coordinated wage bargaining promotes real wages moderation and low unemployment' (Booth et al, 2001: 152). This effect, however, has only occurred in Continental and Nordic countries, both Anglo-Saxon and Mediterranean countries have failed to harness the efficiency effects trade unions can have on a country's labour market.

A final characteristic of trade unions is their support for increased welfare benefits. Trade unions consistently seek increased welfare benefits so as to improve their power in wage negotiations. , this can lead to LTU as it decreases the incentive to work. This is a problem throughout Europe as, even before the recession, it was recognised that 'European unemployment is mainly a problem of long-term unemployment' (Boeri et al, 2000: 2).

The Effect of LTU

LTU is a severe problem within any labour market as it can produce hysteresis effects which decrease the human capital of the unemployed. This means that they are less valuable to the economy even when they do regain employment. LTU can also cause inflation as, as employers face work shortages, prices rise (Boeri et al, 2000). In addition to this, the long-term unemployed are often considered unemployable and so do not affect wages within the labour market, meaning that involuntary unemployment grows. This further encourages the growth of the black economy, which can exploit workers and harm the efficiency of the economy as a whole. As a result 'long-term unemployment is the worst form of unemployment for those who experience it, and it is also the most inefficient'

(Boeri et al, 2000: 9).

Solutions to this problem must tackle both the supply and demand side of the labour market. From the supply side, as shown by the success of countries following the Nordic model such as Sweden, active labour market policies are essential. These ensure that individuals are offered either training or a job whilst receiving benefits. They also ensure that these benefits can be cut if these offers are refused and that unemployment benefits are not too high so as to harm incentives to work. While countries following the Nordic model have perfected this balance, other European models are still struggling, although there is some significant steps being made within some Continental economies, such as Germany (Kluve et al, 2010: 3).

On the demand side, it is crucial that recruitment subsidies are offered to employers who employ the long-term unemployed, as this can remedy the destructive effects LTU has on human capital and ensures the long-term unemployed re-enter the labour market. An oft-cited solution on the demand side is also to allow for early retirement, thus increasing the amount of vacant jobs the long-term unemployed can compete for. This, however, only decreases the amount of individuals in the labour force which negatively impacts job growth, as it harms innovation by removing the most experienced workers from the labour force, restricting the ability of firms to produce economies of scale, and decreasing the amount of labour they can employ. Empirically, this can be seen in Table 1: countries with faster labour force growth rates have faster employment growth rates (Boeri et al, 2000).

Table 1

Country	Percentage Labour Force Growth 1960-1997	Percentage Employment Growth 1960-1997
Italy	8%	-1%
Sweden	15%	7%
Finland	20%	5%
Belgium	15%	7%
United Kingdom	19%	17%
Greece	20%	18%
Austria	23%	21%
France	30%	19%
Denmark	36%	36%
Ireland	37%	35%
Portugal	45%	38%
Switzerland	44%	40%
Germany	50%	38%
Japan	51%	49%
Netherlands	53%	58%
Norway	59%	58%
Luxembourg	79%	75%
USA	90%	97%
Australia	101%	86%
Iceland	103%	96%
New Zealand	105%	95.5%
Canada	131%	137%

As is evident from this table, this correlation is not spurious. Although it might be assumed the correlation is due to both factors having a common response to economic growth, this thesis is disproved by the fact countries with similar growth rates during this period, such as the USA and the UK, have wildly diverging labour force growth rates, and hence employment growth. Clearly this shows that restricting the growth of the labour force is detrimental for LTU and unemployment in general. This is even clearer when we examine the beneficial effects of migration on growth.

The Effect of Migration and Integration

Integration has hugely affected EU labour markets as it has allowed the free movement of goods and capital, and this has led to greater competition for wages. This is because 'through goods markets, national labour markets indirectly compete against each other' (Baldwin and Wyplosz, 2012: 217). However, although this flattened the demand curve in Europe, wages did not decline as this curve simultaneously shifted up due to an increase in efficiency brought about by the increase in competition. As a result, European integration has increased employment and wages within the EU. Increased intra-EU migration could have similar benefits as it would increase allocative efficiency and could increase the size of the labour force within a given country, both of which promote job growth. These benefits are especially clear, given that 73% of EU migrants are skilled or semi-skilled workers and would thus complement existing workforces (Baldwin and Wyplosz, 2012).

The effect of migration, however, has been severely limited within the EU. Despite the free movement of labour, only 20% of immigration in the EU is intra-EU migration, and most of this is short-term (Guardia and Pichelmann, 2006). This has limited any effect on the EU labour market. This is despite the hugely beneficial consequences of increased migration, with some estimates arguing that a removal of all restrictions worldwide could double world GDP (Hamilton and Whalley, 1984, cited in Hatton, 2007). Clearly, an increase in intra-EU migration would be beneficial for all EU countries, however this has been prevented by a variety of direct and indirect restrictions.

The largest direct barrier to intra-EU migration is a lack of coordination of social policies. Unemployment benefit for EU migrants only lasts for three months in the country they have migrated to, meaning the fear of not being able to find employment within these three months can severely restrict EU migration (Baldwin and Wyplosz, 2012). Even within some EU countries this can also restrict migration, as can be seen in southern Italy, where unemployment benefits for young workers are conditional on remaining in the family home (Boeri et al, 2000). In addition to this, the age when an individual can begin receiving pension benefits varies across the EU. This can provide a disincentive to work in a country with a higher pension age, as an individual will not receive the benefits for the years worked in this country until the higher age is reached. Indirect restrictions such as language barriers, a loss of social networks and a lack of recognition of qualifications in some professions also severely restricts migration.

Conclusion

In conclusion, European labour markets are not exempt from the laws of supply and demand. The effect of excessive welfare benefits, trade unions and LTU can, in part, explain the inefficient operation of the European labour market as they all distort these laws. Despite this, however, welfare benefits and trade union action can be designed so as to improve the efficiency of the labour market and LTU can be resolved if this occurs. Efforts to do this can clearly be seen in countries which follow the Continental and Nordic models, in the form of Active Labour Market policies. In contrast, Anglo-Saxon countries have already gained this efficiency at the price of a decline in equity (Sapir, 2006). Mediterranean countries remain the only markets in Europe which have yet to reform their welfare benefits and trade unions into a manner which can effectively tackle unemployment, especially LTU. In all European regions, however, migration can play a key role in fighting unemployment, but its effect on European labour markets has been blunted by a variety of direct and indirect restrictions on the free movement of labour. A common social policy and language training initiatives could hugely improve this situation and could produce a market which we could truly call a European labour market.

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