

## **Active Labour Market Policy in Ireland**

*Ronan Clarke – Senior Sophister*

*As with any policy recommendation, there is likely to be a gulf between economic theory and government practices. When it comes to labour market policy the consequences of failure are devastating chronic long-term unemployment. Ronan Clarke examines the theory behind Active Labour Market Policy and how it has been applied in Ireland.*

### **Introduction**

Designing an appropriate policy response to unemployment is an ongoing and seemingly intractable problem for many governments. There is much at stake both for economies and for individuals in designing effective labour market policies. Measures designed to combat unemployment or its effects may even introduce inefficiencies that serve to increase joblessness. The recent dramatic growth in employment in Ireland poses new difficulties for policy-makers and it is necessary to ask if the existing policy framework is appropriate given current conditions.

In this essay we discuss the use of active labour market policies in Ireland. We begin by examining issues regarding active labour market policies in general, including its origins and evidence on its effectiveness internationally. We then consider its use in Ireland and review the available evidence on particular schemes. We conclude that, while evaluation and precise targeting are considered essential to the effective use of active labour market policy, there is little evidence that these are being prioritised in Ireland.

### **Active Labour Market Policies - Background and Evaluation**

Active labour market policy (ALMP)<sup>1</sup> refers to a broad range of measures which are designed to improve the skills and competencies of workers and support the search process in the labour market. Passive measures, by contrast, merely provide financial supports for unemployed workers. There is a high degree of heterogeneity in the conception, design and implementation of ALMPs generally.<sup>2</sup> Measures

---

<sup>1</sup> The literature refers variously to ‘active labour market policy’ and ‘active labour market programme(s)’; hereafter, the term ALMP will be used generically.

<sup>2</sup> OECD (1993)

## ACTIVE LABOUR MARKET POLICY IN IRELAND

include training and education programmes, the provision of job placement services, direct job creation schemes and subsidies to employment in the private sector.

While ALMP strategy was originally devised in Sweden in the 1940s<sup>3</sup> to address an inflationary problem associated with full employment, it was later adopted as a means of reallocating labour supply in response to widespread unemployment in the industrial economies. The OECD introduced policy recommendations in 1990 advocating a shift in labour market expenditures to “*active measures which mobilise labour supply, improve the quality of the labour force, and strengthen the search process...*”<sup>4</sup> According to O’Connell and McGinnity, ALMPs had, by the mid-1990s, become “*the principal state response to mass unemployment throughout the industrial societies*”<sup>5</sup>.

By 1995 the average expenditure of OECD countries on ALMPs was almost one per cent of GDP (see Table 1). This level of expenditure of public funds is, arguably, only justified if the programmes being funded are effective in terms of tackling unemployment and delivering wider economic benefits. This highlights the central importance of evaluation of ALMPs and the OECD has recommended that an evaluation culture should become “*part of the normal policy infrastructure*”<sup>6</sup>.

Table 1: Social Expenditure, 1995 - percentages of GDP

	Unemployment Benefits	Active Labour Market Programmes
Ireland	2.8	1.7
UK	1.3	0.5
US	0.3	0.2
OECD average	1.6	0.8
EU (15) average	2.2	1.1

Source: OECD (1998)

<sup>3</sup> Schmid (1996) credits two Swedish economists, Günter Rehn (1948) and Rudolph Meidner (1948) with first writing about AMLP.

<sup>4</sup> OECD (1993)

<sup>5</sup> O’Connell & McGinnity (1997)

<sup>6</sup> OECD (1998)

Evaluations of labour market schemes may take either of two approaches. The microeconomic approach examines the labour market outcomes of programme participants, such as employment and wages, while the macroeconomic approach focuses on changes in aggregate indicators such as the unemployment rate. In either case there are a range of complex issues to be considered and the OECD believes that “*even with the best application of available data and methods, evaluations are likely to remain partial and incomplete*”<sup>7</sup>.

Three problems in particular affect the impact of ALMP and pose substantial difficulties for designing and assessing effective programmes. Deadweight refers to a situation whereby the outcome of a scheme, in terms of additional employment, would have happened anyway in the absence of intervention. Given the implication that valuable resources are being used to no effect, programme designers should set out to minimise its impact, and evaluation studies should attempt to accurately identify the extent to which deadweight is present. Substitution refers to the possibility that recruitment through an active labour scheme is merely replacing labour recruited on the open labour market. Again this may be inevitable and the occurrence of this should be minimised where possible. Finally, displacement refers to a situation whereby firms participating in employment schemes are using subsidies to increase competitiveness and thus displace business elsewhere in the economy.

Some studies of wage subsidy schemes carried out in the US and Europe have shown combined deadweight and substitution effects to the order of 70 to 90 per cent of the gross number of jobs created.<sup>8</sup> The crucial point from an evaluation point of view is that where these inefficiencies are significant, the effectiveness of a particular scheme may be overstated. From a policy point of view, however, it may be the case that these effects can be tolerated if overall there is a benefit to the most disadvantaged in the labour market. The effect would therefore be to move more disadvantaged groups up the labour market ‘queue’ at the expense of less disadvantaged groups.

International evidence on the effectiveness of ALMP is, according to O’Connell and McGinnity<sup>9</sup>, “*generally inconclusive, but frequently pessimistic*”. The OECD<sup>10</sup> has

---

<sup>7</sup> OECD (1993)

<sup>8</sup> Bellman & Jackman (1996)

<sup>9</sup> O’Connell & McGinnity (1997)

<sup>10</sup> OECD (1993)

## ACTIVE LABOUR MARKET POLICY IN IRELAND

conducted a comprehensive review of international evidence and concludes that there is little aggregate employment effect from ALMP. However, O'Connell<sup>11</sup> points out that micro-level studies, which generally find limited effectiveness, show that the effects on employment prospects and earnings differ across types of programme and target groups, suggesting that the key to effectiveness may lie in appropriate design. In particular, if programmes have little or no impact on the level of unemployment and are instead redistributing labour market opportunities, then it is crucial that those individuals most in need of help are precisely targeted.

This prompts the question of what type of scheme is most likely to work. O'Connell and McGinnity<sup>12</sup> identify a particular programme's degree of market orientation as a critical factor in effectiveness. They claim that participants on schemes such as private sector employment subsidies, which place participants in 'real' work situations, "*fare consistently and significantly better*"<sup>13</sup> when it comes to post-programme employment prospects. The OECD maintains that, generally speaking, "*positive programme outcomes appear most likely when the targeting is relatively precise and programme activities are designed to meet the needs of individuals, rather than jobless people in general*".<sup>14</sup>

### ALMP in Ireland

By any measure, ALMP is clearly a major tool of government labour market policy in Ireland. For instance, 12 per cent of the labour force participated in some form of ALMP in 1995 (see Table 2). At 1.7 per cent of GDP, Ireland's expenditure on ALMP in 1996 was behind only Denmark, Finland and Sweden among OECD countries.<sup>15</sup> While ALMP was originally introduced against a background of mass unemployment in the early 1980s, the 1990s saw dramatic improvements in both the unemployment rate and the level of long-term unemployment. Therefore, it must be asked if such a high commitment of resources to ALMP continues to be justified, and whether the programmes on offer are likely to be appropriate.

---

<sup>11</sup> O'Connell (1999)

<sup>12</sup> O'Connell and McGinnity (1997)

<sup>13</sup> *ibid*

<sup>14</sup> OECD (1993)

<sup>15</sup> OECD (1998)

Table 2: Participant Flows into ALMPs as Percentage of Labour Force

	Ireland		OECD			EU
	1991	1994	1995	1996	1996	
Labour market training	4.5	4.7	4.8	4.1	3.2	4.0
Youth measures	1.5	1.4	1.4	1.3	1.1	1.4
Subsidised employment	1.6	5.2	5.6	5.7	2.2	2.6
- Subsidies to private sector employment	0.2	1.4	1.8	1.9	0.7	0.8
- Subsidies to self-employment	0.1	0.1	0.1	0.1	0.1	0.2
- Direct job creation	1.3	3.6	3.8	3.7	1.3	1.6
Measures for the disabled	0.2	0.2	0.1	0.1	0.4	0.5
Total	7.8	11.5	11.9	11.3	6.9	8.5

Source: OECD (1998)

The high commitment of resources to ALMP over the past two decades has led to a proliferation of programmes on offer. In 1998 there were over 30 active labour market programmes in Ireland, and according to the OECD this has led to “*similar programmes being offered to the same client group, increasing administrative and information costs*”.<sup>16</sup> Perhaps more worrying is the OECD’s belief that the evaluation process is “*not well entrenched*”<sup>17</sup> in Ireland. In the absence of administrative focus and lack of evaluation, it is likely to be extremely difficult to deliver the precise targeting of individuals discussed above.

The introduction of the Community Employment (CE) scheme in 1992 represented a significant shift in the balance of programmes in favour of direct employment and this has persisted. The scheme offers jobs in the social and community sector to the unemployed. However, as the CE is not precisely targeted, O’Connell and McGinnity see this development as prioritising high volume programmes at the expense of quality and effectiveness and deem it a “*step in the wrong direction*”.<sup>18</sup>

<sup>16</sup> OECD (1998)

<sup>17</sup> *ibid*

<sup>18</sup> O’Connell and McGinnity (1997)

## ACTIVE LABOUR MARKET POLICY IN IRELAND

Although the CE remains the largest scheme in Ireland by participants, it would also seem to be the least effective in terms of progression to employment and O'Connell and McGinnity found that it had "*no discernible impact on subsequent employment prospects*"<sup>19</sup> of participants.

A more innovative approach to employment schemes was taken with the introduction of the Back to Work Allowance Scheme (BTWAS) in 1993. This allows the long-term unemployed to take up employment or self-employment whilst retaining some of their unemployment payments and secondary benefits for a limited period. Unlike traditional private sector employment schemes, employers receive no direct subsidy. The rationale for the BTWAS was to address the needs of the long-term unemployed who proved impervious to both employment growth and the existing package of labour market measures in the early 1990s.<sup>20</sup>

The existence of an unemployment trap was suggested by the fact that, for a substantial number of the unemployed, income out of work represented a high proportion of potential income in work. Callan and Nolan estimate that the percentage of unemployed facing replacement ratios of 70 per cent or higher increased from 36.4 per cent to 37.3 per cent between 1987 and 1994.<sup>21</sup> However, there is evidence that replacement ratios have declined in recent times for a number of reasons such as taxation reforms, and combined with the decline in long-term unemployment, it would seem that the original rationale for the BTWAS may be less relevant today.

The empirical evidence regarding such employment subsidy schemes is generally not encouraging. The OECD review of international evaluation studies found that, in addition to high levels of substitution and displacement, deadweight costs for employment subsidy schemes "*often correspond to well over half of the total participation*"<sup>22</sup>. Consequently, it finds, "*it may be most difficult to defend subsidy programmes with relatively broad targeting*"<sup>23</sup>. The BTWAS, however, is offered to anyone over 23 years in receipt of unemployment assistance for a minimum of 12

---

<sup>19</sup> O'Connell (1999)

<sup>20</sup> WRC (1997)

<sup>21</sup> Callan & Nolan (1999), p.46; estimation of replacement ratios is based on unemployment payments alone and does not include secondary benefits.

<sup>22</sup> OECD (1993)

<sup>23</sup> *ibid*

months, and there is evidence that it is catering for the better educated and more occupationally qualified among the long-term unemployed.

A government-commissioned evaluation of the BTWAS, carried out by WRC consultants<sup>24</sup> in 1997, found that programme entrants were relatively less educationally disadvantaged than the pool of long-term unemployed from which they were drawn, as well as the unemployed as a whole. For instance, 11.3 per cent of participants had third-level education compared to 4.7 per cent of the unemployed, and 3.1 per cent of the long-term unemployed.<sup>25</sup> In addition, the survey responses received by WRC appear to support the OECD assertion regarding the extent of deadweight in such schemes. For instance, the study reported 42 per cent of participants as saying that they would have taken up employment or self-employment in the absence of the scheme.<sup>26</sup>

The evidence suggests that the two schemes discussed here fail both in terms of creating additional employment and targeting existing employment opportunities at those most in need among the unemployed. As the dramatic improvement in labour market conditions in recent years somewhat negates the goal of employment creation, it is difficult to see how continuing to commit the same level of resources to the CE scheme can be justified. On the other hand, targeting of employment measures has become if anything more crucial. It is reasonable to assume that those who remain long-term unemployed in the context of a booming employment market are especially in need of intervention. Therefore, to the extent that in the past programmes were inappropriately designed in this regard, they are likely to be even more so now.

### Conclusion

Governments everywhere continue to commit substantial resources to active labour market policy, and this is especially true in Ireland. However, it is far from clear that this policy approach can be relied upon to deliver positive results. In terms of its ability to create additional employment, the international evidence is generally pessimistic. However, the use of ALMP may still be justified as a means of redistributing existing employment opportunities among the unemployed. In order

---

<sup>24</sup> WRC (1997)

<sup>25</sup> WRC (1997)

<sup>26</sup> WRC (1997)

## ACTIVE LABOUR MARKET POLICY IN IRELAND

for this to be effective, however, programmes must be designed to effectively target particular groups and a culture of evaluation should be encouraged so as to ensure targets are being met.

In Ireland both the number of programmes on offer and the number of participants are large by international standards. Generally speaking, a lack of focus has resulted and planning and evaluation have not been prioritised. In the case of two of the larger schemes, the BTWAS and Community Employment, the lack of targeting is particularly evident as well as a failure to minimise the impact of deadweight. The buoyant labour market conditions currently prevailing in Ireland are good news for workers and policy-makers alike. However the need for careful planning and evaluation of the spending of large amounts of public funds on ALMP has not diminished.

### Bibliography

**Bellmann, L. & R. Jackman** (1996) "Aggregate Impact Analysis" in Schmid, G., O'Reilly, J. & K. Schömann (eds.) *International Handbook of Labour Market Policy and Evaluation*. Cheltenham: Edward Elgar.

**Callan, T. & B. Nolan** (1999) *Tax and Welfare Changes, Poverty and Work Incentives in Ireland 1987-1994*. ESRI Policy Research Series No. 34. Economic and Social Research Institute: Dublin

**Kearney, C. (ed.), Callan, T., Duffy, D., Durkan, J., Lane, P., McCarthy, T., Nestor, R., Nolan, B. & J. Walsh** (1999) *Budget Perspectives: Proceedings of a Conference Held on 27 September 1999*. Economic and Social Research Institute: Dublin

**Nicaise, I., Bollens, J., Dawes, L., Laghaei, S., Thaulow, I., Verdié, M. & A. Wagner** (1995), *Labour Market Programmes for the Poor in Europe: Pitfalls, Dilemmas and How to Avoid Them*. Aldershot: Avebury.

**O'Connell, P. J.** (1999) *Are They Working? Market Orientation and the Effectiveness of Active Labour Market Programmes in Ireland*. ESRI Working Paper No. 105. Economic and Social Research Institute: Dublin

**O'Connell, P. J. & F. McGinnity** (1997) *Working Schemes? Active Labour Market Policy in Ireland*. Aldershot: Ashgate.



**OECD** (1993) “Active Labour Market Policies: Assessing Macroeconomic and Microeconomic Effects” in *Employment Outlook*, June. Organisation for Economic Co-Operation and Development: Paris

**OECD** (1996) “Making Work Pay” in *Employment Outlook*, July. Organisation for Economic Co-Operation and Development: Paris

**OECD** (1998) *The Public Employment Service: Greece, Ireland, Portugal*. Organisation for Economic Co-Operation and Development: Paris

**OECD** (1999a) *OECD Economic Surveys 1998-99: Ireland*. Organisation for Economic Co-Operation and Development: Paris.

**OECD** (1999b) *Employment Outlook*, June. Organisation for Economic Co-Operation and Development: Paris.

**Schmid, G.** (1996) “New Public Management of Further Training” in Schmid, G., O’Reilly, J. & K. Schömann (eds.) *International Handbook of Labour Market Policy and Evaluation*. Cheltenham: Edward Elgar.

**Snower, D. J.** (1997) “The Simple Economics of Benefits Transfers” in Snower, D. J. & G. de la Dehesa (eds.) *Unemployment Policy: Government Options for the Labour Market*. Centre for Economic Policy Research. Cambridge University Press: Cambridge.

**WRC Social and Economic Consultants** (1997) *Developing Active Welfare Policy: An Evaluation of the Back to Work Allowance Scheme*. Department of Social, Community and Family Affairs: Dublin.