SEPTEMBER 2009 Policy Brief

OECD

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

# Helping Workers Weather the Economic Storm



## Introduction

The world economy is in a severe economic downturn with potentially dire consequences for workers and their families. The ultimate dimensions of this crisis are not yet known, but it is already clear that it will be the deepest recession of the post-war era for the OECD area, with the average unemployment rate heading toward an all-time high of nearly 10% at the end of 2010. While the recession appears to be slowing, the recovery is expected to be initially weak; and history shows that unemployment is slow to recede, even once an economic recovery is under way.

High unemployment does not just result in declines of output and income. Joblessness has adverse effects on physical and mental health, crime rates and subjective happiness–including for those who remain employed, but fear losing their job. And if job loss results in a long spell of unemployment, as is particularly likely in a deep recession, this can lead to a loss of valuable skills or demoralisation, reducing the long-term earnings potential of the affected workers and increasing their risk of becoming disconnected from the labour market.

The steep rise in unemployment represents a daunting challenge for employment and social policies, especially at a time when public spending is under pressure on many different fronts. The OECD is closely monitoring the impact of the economic downturn on labour markets, as well as the policy measures that governments are taking to limit its social consequences. This *Policy Brief* summarises the main insights that have emerged, both regarding how workers are faring in the economic crisis and what policy measures governments can take to ensure that workers receive the help they need to weather the storm, while also laying the foundation for a strong recovery and sustained growth. ■

oecd Observer

## How is the crisis affecting labour market outcomes?

Labour-market conditions have deteriorated throughout the OECD area, in some cases at an unprecedented pace. In the period from December 2007 to July 2009, 15.1 million persons joined the ranks of the unemployed in the OECD area, an increase of 50%. The sharpest increase was in Spain, where unemployment climbed 9.7 percentage points, followed by Ireland and the United States, with increases of 7.8 and 4.5 percentage points, respectively. While other countries did not feel the impact of the economic downturn as starkly, unemployment rose in all OECD countries in 2009.

Many OECD countries have responded to the crisis by taking vigorous macroeconomic policy measures, and there are now signs that the recession may be slowing. Nonetheless, the latest OECD projections indicate a further decline in activity in 2009 in the OECD area, with a muted recovery surfacing only in the first half of 2010. Experience has shown that job creation lags output early in a recovery because employers still face a lot of uncertainty about their business prospects and many of their current employees would like to work more hours. If these projections were to materialise, more than 25 million people in the OECD area would join the ranks of the unemployed just in the three years from the beginning of the downturn to the end of 2010, representing an unemployment rate of nearly 10%, a post-war high. The labour market outlook would be even worse if governments had not pursued expansionary monetary and fiscal policy. For example, the fiscal stimulus packages enacted by most countries are projected to raise employment in 2010 by about 1% above the level that would otherwise prevail.

Although rising unemployment is the most visible form of hardship that befalls workers in recessions, employers have also reacted to worsening business conditions by reducing hours for their employees and cutting wages. As a result, underemployment has increased alongside unemployment, and governments may need to channel increased assistance to workers who are still employed, but are not earning enough to support their families adequately. ■

## How does this crisis compare to previous recessions?

Figure 1 compares the relative increase in the unemployment rate from the beginning of the current economic downturn through the end of 2010 (the end point of the most recent OECD projections) with that of four previous recessions. This illustrates that the current downturn is expected to be the most severe in recent decades, with the OECD average unemployment rate projected to increase by nearly 80% between its most recent trough, in the third quarter of 2007, and the end of 2010. The corresponding increases in previous recessions ranged between 20% and 50%.

As compared to their counterparts in past recessions, workers confront this downturn with both advantages and disadvantages. One clear advantage is that the current crisis hit the OECD economy at a time when labour-market conditions were rather favourable. Unemployment rates reached a 27-year low on the eve of this downturn, at an OECD-average level of 5.6%, while over two-thirds of the working-age population were employed, an all-time high. On the downside, the vulnerability of workers to worsening business conditions increased in a number of OECD countries as temporary work has become more common. It is easier for employers to reduce staff in response to deteriorating business conditions by simply not renewing temporary contracts rather than by laying off permanent staff. The over-representation of temporary and other "non-standard" workers among job-losers probably also means that many unemployed workers do not qualify for unemployment benefits. Eligibility rules for these benefits often specify minimum thresholds for earnings or employment continuity that can exclude many temporary and part-time workers. ■

## Who is most affected?

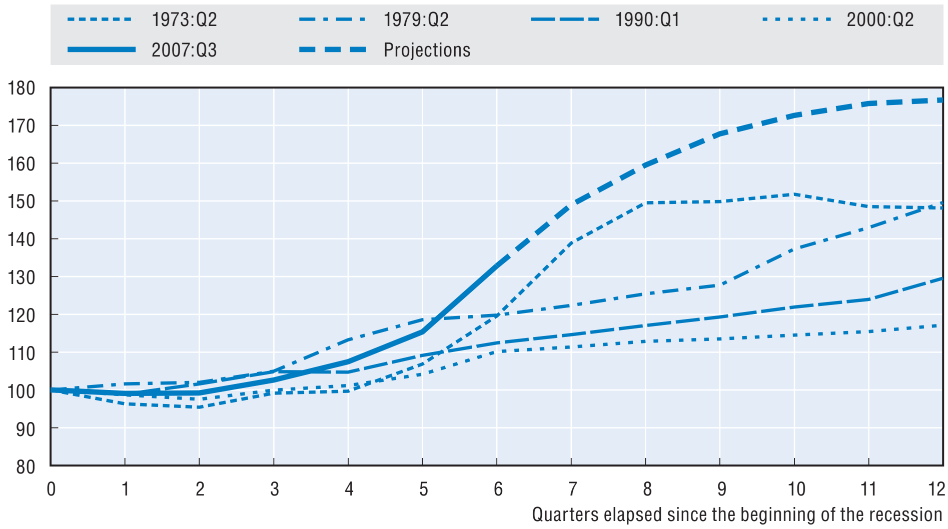
While no workforce group is spared in a deep recession, past economic downturns show that groups that are already relatively disadvantaged in the labour market – youth, low-skilled, immigrants and temporary workers – bear the brunt of falling labour demand. Figure 2 shows that youth and temporary workers are especially vulnerable to cyclical downturns. The vulnerability of disadvantaged groups in a recession results in part from the tendency of employers to lay off low-tenure and less skilled workers first. Once unemployed, disadvantaged job-seekers are also at a greater risk of remaining out of work for a long time, because they are pushed even further to the back of the hiring queue at a time when more workers are competing for fewer job vacancies. To date, the current recession conforms to these patterns.

The problems that workers face in a recession tend to take different forms for different workforce groups. Prime-age workers are better able than youth to remain employed in a recession, but are also more vulnerable to working-time reductions and the associated loss of earnings. Among job-losers, the average duration of unemployment rises for all workforce groups, but this increase is especially marked among youth.

**Figure 1.**

**THE CURRENT CRISIS IS THE WORST IN RECENT DECADES**

**Index base 100 = unemployment rate at the business cycle peak, OECD area, quarterly data**




*Source: OECD Employment Outlook 2009.*

One implication of these complex patterns is that labour-market authorities need to assist greater numbers of job-seekers while also considering their very different employment prospects. Many will be qualified workers who are eligible for unemployment benefit payments but have little recent experience in looking for a job. More disadvantaged job-seekers, such as youth lacking qualifications, tend to be more accustomed to moving between jobs. But they find themselves at a heightened risk of long-term joblessness at a time when employers can be very selective in their hiring decisions. Also, they will often not qualify for unemployment benefits or may receive benefits only for a short period of time. ■

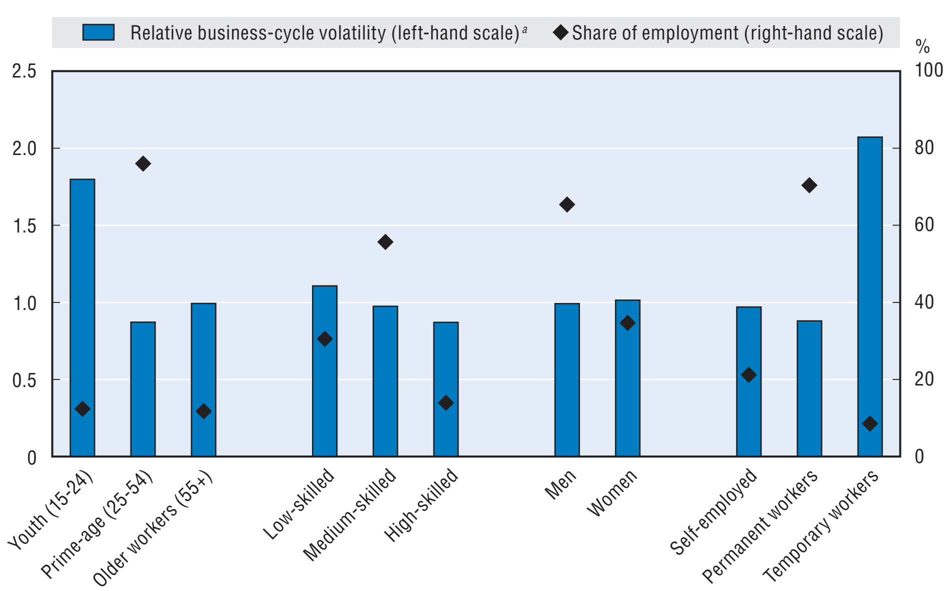
## Are existing safety nets adequate?

The current downturn is severely testing the adequacy of unemployment benefit systems as the primary safety net for job-losers and their families. These benefit systems need to meet three challenges when unemployment surges in a recession. First, governments need to ensure that the necessary administrative and financial capacity is available to meet the increased demand for benefits. Second, prompt action may be needed to fill gaps in the coverage of unemployment benefits that become evident as job losses mount, particularly in countries with substantial proportions of temporary and part-time workers. Finally, the adequacy of income support for the growing group of long-term unemployed becomes a more pressing concern, as unemployment spells lengthen and job-seekers in many countries are confronted with declining benefit payments and expiring entitlements.

**Figure 2.**

**ALREADY DISADVANTAGED GROUPS BEAR THE BRUNT OF FALLING LABOUR DEMAND**

**Index of business-cycle sensitivity for the indicated groups relative to the national averagea**




a. Index based on cyclical variation in total hours worked. A value of 1 for the index indicates an average sensitivity to the business cycle, that is, the same sensitivity as for the total national labour force. Unweighted averages across countries.

*Source : OECD Employment Outlook 2009.*

Where unemployment benefit protection is patchy, governments should make adjustments to ease the negative impact of weakening labour markets on income security, while ensuring that such policy measures do not stifle recovery once economic activity regains momentum. For example, there could be a temporary increase in coverage to non-standard workers. Where unemployment benefit durations are short, temporary extensions to the maximum duration of benefits could help to reduce the number of job-seekers who lose their benefits. But to avoid delaying employment growth after the recession, such extensions need to be temporary, targeted on the most vulnerable, and should not undermine job-search requirements. In response to an OECD questionnaire, 23 of the 29 responding countries reported applying at least one of these measures to shore up income support for the unemployed or for workers with low earnings.

Social assistance and similar minimum-income benefits provide an essential reinforcement to unemployment benefits in a recession, since an increased number of job-losers will either fail to qualify for unemployment benefits or exhaust their unemployment benefit entitlements. In most OECD countries, social assistance and other "last-resort benefits" are not sufficient to lift people out of poverty. Governments should thus carefully monitor whether there are cases of extreme hardship that require an immediate response. These benefits should be *available* and *accessible* to job-losers and other persons who need them, since take-up rates are often low. Most OECD countries have expanded at least one form of social assistance available to job-losers, including temporary measures to help retrenched workers meet mortgage repayments.

While rising joblessness is the main social concern during a severe downturn, there is also likely to be a greater need to assist workers with low earnings. In addition to alleviating hardship suffered from reductions in wages or working hours, income support for low earners can strengthen labour-market attachment during a recession and into the recovery, including for long-term unemployed individuals taking up a new job and new entrants to the labour market. Measures to raise the net incomes of low earners have been taken or announced by more than half of OECD countries, with targeted tax reductions about as common as enhancements to in-work benefits that top-up the earnings of low-income workers. ■

## How can the unemployed be activated when labour demand is weak?

One of the key labour-market policy reforms in recent decades has been the development of activation strategies for unemployed and other benefit recipients. In return for paying benefits and offering effective re-employment services, the government requires recipients to search actively for a new job or participate in measures to improve employability, such as training. The government enforces this requirement with moderate benefit sanctions. Activation strategies have succeeded in moving people off benefit rolls and into work, but much of this success was achieved when labour markets were relatively buoyant. A key question now is how activation procedures need to be adapted in a recession when demand for labour is abnormally low.

It is clear that active labour-market programmes (ALMPs) need to be scaled up in a recession in order to continue to activate the growing number of job-seekers. Historically, spending on active measures has not risen along with the number of unemployed persons in most OECD countries. As a consequence, many job-losers received little or no re-employment assistance during recessions and drifted into long-term unemployment and inactivity. The responses to the OECD questionnaire suggest that governments are being more proactive in this downturn. All 29 responding countries reported expanding ALMP funding, typically by reinforcing multiple types of re-employment services. Nonetheless, it appears that spending in many countries is rising less than proportionately with the rise in unemployment, and this raises concerns about the adequacy of the help available to job-losers. Inadequate funding is less of a concern in Australia, Denmark and Switzerland, where funding for ALMPs automatically increases with the level of unemployment. But strong discretionary action is required in most other countries.

The public employment service (PES) must also decide how the mix of services provided to job-seekers should be adjusted in a recession. The challenge is recognising that some clients will have much-reduced re-employment chances, while making the most of the fact that employers continue to do substantial hiring in a recession. In order to preserve the mutual-obligations ethos of activation regimes, it is essential that the core elements of activation regimes, such as drawing up personal re-employment plans, regular meetings with case managers, and requirements to search actively for jobs, not be allowed to lapse. Nonetheless, to conserve caseworker time and avoid demoralisation, the PES may choose to concentrate job-search assistance on the most employable job-seekers, while easing slightly the requirements intended to demonstrate work availability and active job search for harder-to-place job-seekers. It would then also be necessary to provide increased support in other forms, such as training, targeted hiring subsidies and public-sector job-creation schemes, to the relatively disadvantaged job-seekers. It is important to target these programmes on those most in need and to shrink them back to their normal size as the job market recovers.

In addition to providing additional support to job-seekers, OECD governments have also emphasised measures to reduce the number of layoffs. Three-quarters of the countries reported promoting work-sharing by creating new short-time working schemes or expanding existing schemes, for example by making more employers eligible or expanding the subsidies received by participating employers. Take-up of these programmes has been high in a number of countries, including Germany and the Netherlands. This probably has slowed the rise in unemployment in the early stages of the downturn in these countries. However, experience suggests that it becomes increasingly difficult to sustain short-time working schemes if business-cycle conditions are slow to recover. Attempts to prolong these schemes for extended periods can also become a barrier to needed structural adjustment, since they lock workers into jobs that may no longer be economically viable while making it harder for dynamic firms to attract the workers they need. ■

## What can be done to prepare workers for the recovery?

Inappropriate government responses to high cyclical unemployment can undermine labour supply in the long run, compromising prospects for economic growth. It is thus important that short-term assistance does not compromise labour-market performance after the recession has ended.

For example, early-retirement options were sometimes introduced during past recessions, with the intent of freeing up jobs for young people. Similarly, some OECD governments eased access to disability benefits in recessions, in effect allowing labour-market difficulties to become an additional criterion for accessing these benefits in addition to the usual medical criteria. Both early retirement and easier access to disability benefits proved to be one-way streets: virtually no workers who were offered these benefits returned to the labour force when the economy recovered. These measures are also politically difficult to reverse, amplifying their long-term impact in raising benefit dependency and undermining labour supply. Given the ageing of OECD populations and the resulting pressures on fiscal and welfare systems, it is critical to avoid repeating these types of policy mistakes.

Measures to minimise the number of youth who lack qualifications, such as programmes to prevent dropping out of school, subsidies for apprenticeship contracts for unskilled youth, and second-chance schools, are even more critical in a downturn than when the economy is growing. It is also important to ensure that unemployed, out-of-school youth can access job-search assistance and other appropriate ALMPs.

## For further information

For more information about this *Policy Brief* and OECD work on the jobs crisis, contact:
Paul Swaim, e-mail: paul.swaim@oecd.org, tel.: +33 1 45 24 19 77;
Alexander Hijzen, e-mail: alexander.hijzen@oecd.org, tel.: +33 1 45 24 92 61;
Herwig Immervoll, e-mail: herwig.immervoll@oecd.org, tel.: +33 1 45 24 92 14
or visit *www.oecd.org/els/employment*.

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

## For further reading

OECD (2009), **OECD Employment Outlook 2009**, forthcoming.

OECD (2009), "Maintaining the Activation Stance during the Crisis", background document for the Ministerial Meeting of Labour Ministers, September 2009. Visit *www.oecd.org/employment/ministerial*.

OECD (2009), "Helping Youth Get a Firm Foothold in the Labour Market", background document for the Ministerial Meeting of Labour Ministers, September 2009. Visit *www.oecd.org/employment/ministerial*.

OECD (2009), **OECD Economic Outlook, Volume 2009 Issue 1**, ISBN 978-92-64-05457-8, € 96, 317 pages.

OECD (2006), **OECD Employment Outlook 2006: Boosting Jobs and Incomes**, ISBN 978-92-64-02384-0, € 80, 277 pages.



## Where to contact us?

**OECD HEADQUARTERS**
2, rue André-Pascal
75775 PARIS Cedex 16
Tel.: (33) 01 45 24 81 67
Fax: (33) 01 45 24 19 50
E-mail: sales@oecd.org
Internet: *www.oecd.org*

**GERMANY**
**OECD Berlin Centre**
Schumannstrasse 10
D-10117 BERLIN
Tel.: (49-30) 288 8353
Fax: (49-30) 288 83545
E-mail: berlin.centre@oecd.org
Internet: *www.oecd.org/berlin*

**JAPAN**
**OECD Tokyo Centre**
Nippon Press Center Bldg
2-2-1 Uchisaiwaicho,
Chiyoda-ku
TOKYO 100-0011
Tel.: (81-3) 5532 0021
Fax: (81-3) 5532 0035
E-mail: center@oecdtokyo.org
Internet: *www.oecdtokyo.org*

**MEXICO**
**OECD Mexico Centre**
Av. Presidente Mazaryk 526
Colonia: Polanco
C.P. 11560 MEXICO, D.F.
Tel.: (00.52.55) 9138 6233
Fax: (00.52.55) 5280 0480
E-mail: mexico.contact@oecd.org
Internet: *www.oecd.org/centrodemexico*

**UNITED STATES**
**OECD Washington Center**
2001 L Street N.W., Suite 650
WASHINGTON DC. 20036-4922
Tel.: (1-202) 785 6323
Fax: (1-202) 785 0350
E-mail: washington.contact@oecd.org
Internet: *www.oecdwash.org*
Toll free: (1-800) 456 6323

*The OECD Policy Briefs are prepared by the Public Affairs Division, Public Affairs and Communications Directorate. They are published under the responsibility of the Secretary-General.*

00 2009 1 F 1 P4