



I Z A

# COMPACT

## CONSIDERING THE FUTURE OF LABOR

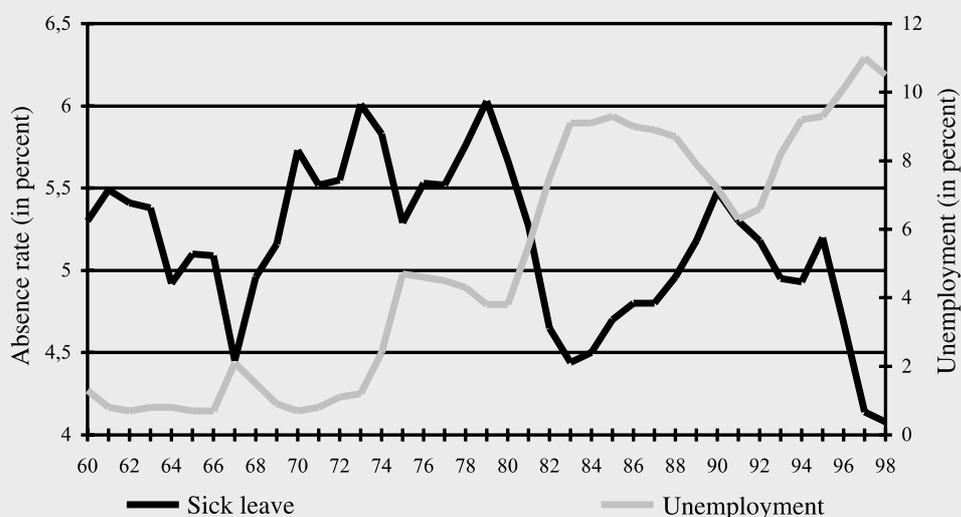
### Absenteeism in Germany – What Role Does Unemployment Play?

Ever since the introduction of sick pay for workers, there have been discussions concerning the number of working days lost through absenteeism. After the German government revised the legal provisions concerning sick pay in 1996 and 1999, absenteeism and its causes have secured a prominent place in public debate. Many people believe that guaranteed sick pay is widely abused. The observation that absences from work decrease strongly during times of recession seems to support this assumption. There is another reason for why the amount of sick pay is the topic of heated discussion: the continued payment of wages constitutes a part of employers' contributions, which are often viewed as the primary cause of high unemployment. A new IZA study investigates the correlation between unemployment and absenteeism (for a detailed account see: *Thalmaier, Anja, Bestimmungsgründe von Fehlzeiten: Welche Rolle spielt die Arbeitslosigkeit?*, IZA Discussion Paper No. 62).

#### The Development of Absenteeism

Over the last four decades, absenteeism in Germany has been subject to cyclical fluctuations. The first major increase, which occurred in the late 1970s, can be attributed mainly to the "Continued Wage Payment Act" of 1969. This law regulated the continued payment of wages to blue-collar workers and brought it into line with the relevant provisions for white-collar workers. All workers were then entitled to their regular wage payments for the first six weeks of work absence. Nonetheless, differences between blue-collar and white-collar workers remained, e.g. regarding the obligation to present a physician's certificate. Since the late 1970s, the absence rate has declined but continues to fluctuate cyclically. After an all-time high of 6.0 percent in 1979, aggregate work absence has fallen to only 4.1 percent for 1998. The rate rose to 5.5 percent in 1990 and peaked again in 1995.

#### Absence Rate and Unemployment in West Germany, 1960-1998



Source: Institut für Arbeitsmarkt- und Berufsforschung (IAB); Statistisches Bundesamt  
"Sick leave" represents workers who are absent from work as a percentage of the total workforce.

A potential cause of the 1995 increase is the standardization of legal provisions in 1994. Blue-collar workers – like their white-collar colleagues – were no longer required to present a doctor's certificate until the third consecutive day of absence. The year 1996 marked the first time in the history of sick pay in Germany that benefits were actually reduced: legislation cut the continued wage payment from 100 to 80 percent of regular wages. This only affected the legal entitlement, however, and not any agreements reached in collective wage negotiations.

In general, there is an inverse relation between the cyclical fluctuation of the absence rate and the trend of unemployment. For example, sick leave fell to a level of 4.5 percent in 1967 when Germany went into its first post-war recession. In the same year, unemployment reached 2.1 percent – a record high in those days. The oil crises in 1975 and 1983 again coincided with a low level of work absence (5.2 and 4.4 percent, respectively), while unem-

ployment peaked at 4.7 and 9.1 percent. The recession year of 1993 also led to a decline in absenteeism. After a short increase in 1995, the level continued to drop to a historic low of 4.1 percent in 1998. Unemployment, on the other hand, remains today above the record level of 10 percent.

#### Legal Provisions Versus Collective Wage Agreements Concerning Sick Pay

Since reliable data is not available, it is hard to tell exactly how many workers were directly affected by the 1996 legislation. It is safe to assume, however, that only about 20 percent of workers faced a reduction in the amount of sick pay they would receive. Without judicial review, it was often difficult to determine whether collective wage agreements contained independent provisions about sick pay, or whether they simply drew on the relevant legislation. The new law kept labor courts busy as it intruded in an area largely regulated through collected bargaining.

In response to the legislation, unions used their leverage in the wage negotiations of 1996 and 1997 to ensure full sick pay for over 15 million employees – either by continuing the old practice or by designing new agreements. In light of this, the impact of the legally mandated reduction of sick pay was probably rather weak. By the same logic, the most recent law (enacted in 1999), which raised sick pay again, is unlikely to lead to a noticeable increase in absenteeism.

The legislation of 1996 and 1999 has shown, however, that the government

can both help firms to cut costs and make the law more compatible with incentives independent of reduced sick pay. The 1999 amendment allows wage agreements to alter the basis of assessment for sick pay. One of the implications of this is that regular overtime does not have to be taken into account in determining sick pay. As a further consequence of the 1996 amendment, firms may pay their employees premiums based on the number of sick days. This serves as an incentive for workers to refrain from absenteeism. The new legislation therefore allows firms to cut costs with-

out endangering the socially desirable – and certainly necessary – financial security of workers in case of illness.

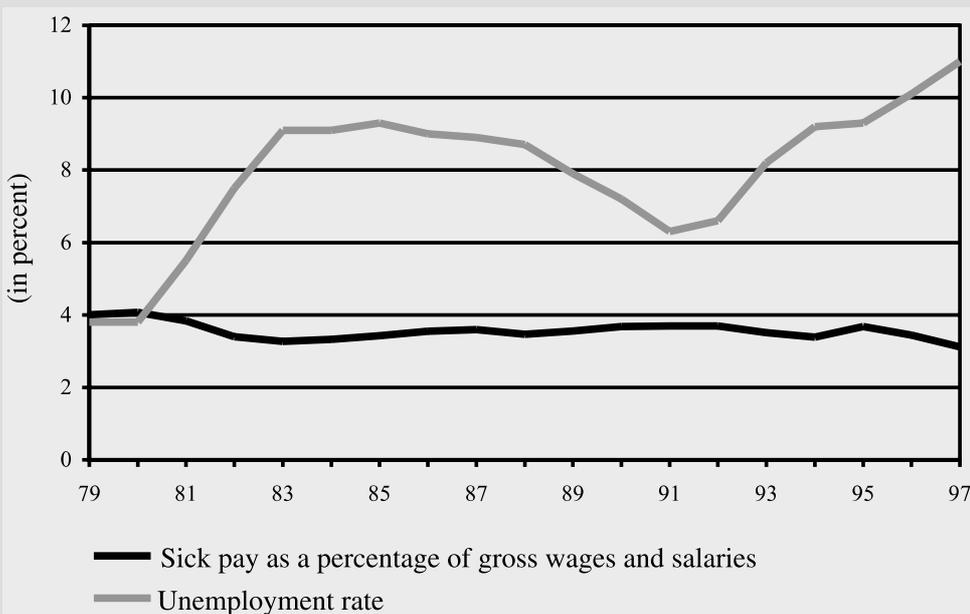
### The Cost of Sick Pay

Firms have to carry considerable financial burden due to mandatory sick pay. In 1997, these employer costs amounted to DM 40.53 billion in West Germany alone. Although sick pay as a percentage of gross wages and salaries has remained almost constant, unemployment has continued to rise.

This observation gives us reason to doubt a causal relationship between sick pay and high rates of unemployment. An examination of employer costs for sick pay as a percentage of total labor costs supports this assumption. In 1996, sick pay represented a mere 2.28 percent of firms' total labor costs. As a share of employers' contribution, sick pay amounted to only 5.11 percent. In contrast, vacation premiums and other extra pay like the Christmas bonus – at 17.56 and 17.03 percent, respectively – constituted a much larger component of employers' contribution.

Cutting sick pay from 100 to 80 percent would reduce direct labor costs by a mere 0.45 percent – even under the assumption that all collective bargaining agreements include this provision. In other words, a reduction of sick pay does not generally lead to a noticeable decline in employee benefit costs. The political and public debates over this subject therefore do not serve a purpose.

### Sick Pay and Unemployment in West Germany, 1979-1997



Source: Bundesministerium für Arbeit und Sozialordnung; Statistisches Bundesamt

### Labor Costs Per Full-Time Worker in the German Manufacturing Industry, 1996

	Amount (in DM)	Percentage of Labor costs	Employers' contribution
<b>Total labor costs (year)</b>	81,742.00	-	-
Labor costs per hour worked	50.86	-	-
<i>including:</i>			
Compensation for actual work	45,298.00	55.42	-
Total employers' contribution	36,444.00	44.58	-
<i>including:</i>			
Legally required employers' contribution	17,078.00	20.89	46.86
Paid time off	10,920.00	13.36	29.96
<i>including:</i>			
Vacation bonus	6,401.00	7.83	17.56
Legally required sick pay	1,866.00	2.28	5.11
Supplemental sick pay	82.00	0.10	0.23
Legally required employers' contribution to Social Security	12,723.00	15.56	34.91
Premiums (e.g. Christmas bonus)	6,205.00	7.59	17.03

<sup>1</sup> Annual wages and salaries minus premiums, paid leave, and social components (e. g. benefits for married couples and families with children)  
Source: Statistisches Bundesamt; own calculations.

### Theoretical Considerations

Using efficiency wage theory, we can analyze sick days as a component of labor productivity interpreting them as an extreme form of shirking. This assumption is based on the fact that the distribution of information between employer and employee is asymmetric - only the worker knows his own state of health. As the employee may be tempted to lie about his health, there is a certain "moral hazard" involved. Designing an incentive system to prevent workers from shirking is therefore very important and the existence of involuntary unemployment makes such incentives very effective. According to this theory, employers can use unemployment to discipline their employees and to ensure that they put in enough days at work. By the same logic, workers laid off for shirking will find it hard to get a new job. The benefits from frequent days off are thus limited. If absenteeism serves as an indicator of the employee's work effort, then we can use the connection between sick days and unemployment to examine the effectiveness of involuntary unemployment as a means to discipline employees.

### Empirical Analysis

The analysis of the average number of absences from work - based on data provided by the German Socio-Economic Panel (SOEP) for the period from 1985 to 1996 - shows large occupational differences. Blue-collar workers, whose working conditions are often more strenuous and detrimental to health, have the highest number of sick days. On average, they miss 16.27 working days per year, followed by civil

servants (10.60 days). White-collar workers have the lowest number of absences (12.95 days) in the period under study. The average of sick days amounts to 12.95. Since the percentage of blue-collar workers in the workforce continues to decline due to structural change, the already existing downward trend in total sick days is likely to be reinforced. Another striking observation is that women are much more often absent from work than men. While female blue-collar workers average 18.69 sick days per year, the corresponding numbers are 12.25 for female civil servants and 11.85 for female white-collar workers.

Compared to workers in the manufacturing and processing industries, who show a high number of absences, employees in the service sector take much fewer sick days. While steelworkers miss on average 15.75 working days and workers in the chemical industry take 12.96 sick days per year, the annual absences of bank employees amount to only 9.38 days. In the wholesale business, sick days average 8.79 per year. We can conclude from this observation that sick days will continue to decline in the future as most of the newly created jobs are in the service sector.

The findings of the IZA study stress the theory that unemployment has a tremendous impact on absenteeism: whenever unemployment goes up, the number of absences from work due to illness drops significantly. This applies to blue-collar and white-collar workers alike. For civil servants, however, there is no inverse relation between sick days and unemployment because they do

not run the risk of losing their jobs. Moreover, empirical analysis of the causes of absenteeism shows that employment in large companies or the public sector brings about a significant increase in the number of sick days. For female workers, the number of working hours has a positive influence on absenteeism: women with part-time jobs take fewer sick days. Older employees average more absences than their younger colleagues. The wage level, however, seems to have no major impact on the number of sick days.

### Conclusions

The IZA study concludes that the national average of sick days will remain on a relatively low level in the future. This is partly due to persistent unemployment. In addition, further deregulation of public enterprises will have a dampening effect on absenteeism. A continuing increase in part-time job opportunities could yield the same effect. In light of these circumstances, decision-makers in politics and wage negotiation rounds should judge the function of continued wage payments realistically in their search for cost-cutting measures to stimulate employment. This much is certain: reduced sick pay fails to bring employers' contribution down by even as little as one percent.



## Youth Unemployment – How To Encourage Work

### Facts About Youth Unemployment

In many European and OECD countries, youth unemployment has reached dramatic dimensions. Relief is currently not in sight. An analysis of data on international unemployment from the year 1996 onwards shows that youth unemployment is on average nearly twice as high as total unemployment in EU and OECD countries. The labor market situation of under 25-year-olds is the most worrying.

Cross-country differences in this aspect are quite significant. While the unemployment rates among young people, adults, and the total workforce are on approximately the same level in Germany, youth unemployment in countries like Belgium, Finland, France, Greece, Italy, Poland, Sweden, and Spain has reached an alarming magnitude. The numbers - as compared to unemployment among the over 25-year-olds - are twice to four times higher.

It comes as no surprise that unemployment among young people without higher education is particularly high in these countries. Although the probability to become unemployed decreases with a rising level of education, qualification alone is no guarantee of a job. In an international comparison, countries with a solid educational system, such as Germany, Denmark, or Austria, suffer less from youth unemployment. This fact, however, should not distract from the immediate necessity of under-

taking effective policy measures to improve the situation on the labor market.

### **Youth Unemployment – Partly a Result of Immigration?**

During an IZA lunchtime meeting on youth unemployment in Bonn, Germany, on June 17, 1999 IZA Fellow *Rudolf Winter-Ebmer* (University of Linz, Austria and CEPR) dismissed theoretical explanations that oversimplify the problem of youth unemployment by attributing it, for instance, to immigration. Empirical analysis of the Austrian case reveals that a connection between both phenomena is practically non-existent. Exceptions are the construction industry and the hotel and restaurant industry, where the unemployment risk increases with the influx of foreign workers. "When employment of foreign workers rises one percent, unemployment risk increases by only one quarter of one percent. Among women and white-collar workers, competition does not lead to displacement of young domestic workers at all. The average duration of unemployment for young workers in Austria is about ninety days. It would be one week longer if employment of foreign workers were to go up one percent. The scapegoat theory has once again turned out to be wrong", *Rudolf Winter-Ebmer* concluded.

### **Policy Advice to Tackle Youth Unemployment: Job Subsidies**

Even in countries like Germany, where it does not exceed the average rate of total unemployment, youth unemployment is a serious problem, mainly because it brings about the danger of long-term unemployment. The young unskilled among young unemployed workers are particularly likely to be out of work again at a later stage in their lives. It is therefore necessary to devise adequate training programs to cope with this problem, but it is even more important for us to turn away from our current system of financing unemployment, which fails to encourage young people in particular to show individual initiative and ambition. In the words of IZA Fellow *Dennis J. Snower* (Birkbeck College, London and CEPR), this system of financial redistribution undermines the vitality of the market economy, and eliminates incentives to seek work: "The German system of unemployment benefits prevents active job

search and aggravates the very problems it was designed to reduce. The government has to stop giving money to the unemployed – it has to start offering them targeted job incentives."

The renowned British labor market expert recommends the introduction of a voucher system. Firms could cash in vouchers, which are supposed to replace unemployment benefits altogether, for a time-limited wage subsidy from the government. The value of the voucher would increase with the duration of unemployment and with training undergone in order to make the long-term unemployed more attractive to employers. Companies could funnel the additional funds derived from the vouchers into further training, which would enable them to save and create jobs. Drawing on the resources that previously went into unemployment benefits, this method is designed to be cost-neutral. "Germany would be well advised to subsidize jobs consistently. The voucher system would be a courageous solution", said *Dennis Snower*.

IZA Director *Klaus F. Zimmermann* also calls for targeted support of active job search. "Our system of financing unemployment instead of work has put us on the wrong track. Especially with the burdensome legacy of its predecessors in mind, this administration has every reason to follow a straight course in labor market policy. It is certainly easier to trot along the beaten track, but this will only lead to a dead end. The voucher model, on the other hand, would be a significant step in a more sensible direction of economic and social policy."

**A special issue of the "Journal of Population Economics" examines the topic of youth unemployment from various angles:**

## **Journal of Population Economics**

Special issue  
**Youth Labor Market**  
(Volume 12, Number 2)

Klaus F. Zimmermann  
**Editorial**

J. Michael Orszag/  
Dennis Snower  
**Youth unemployment and  
government policy**

Diane J. Macunovic  
**The fortunes of one's birth:  
Relative cohort size and the  
youth labor market in the  
United States**

Gerard J. van den Berg/  
Jan C. van Ours  
**Duration dependence and  
heterogeneity in French youth  
unemployment durations**

Patricia Rice  
**The impact of local labour  
markets on investment in  
further education: Evidence  
from the England and Wales  
youth cohort studies**

Alan Barrett/Tim Callan/  
Brian Nolan  
**Returns to education in the  
Irish youth labor market**

Rudolf Winter-Ebmer/  
Josef Zweimüller  
**Do immigrants displace  
young native workers?  
The Austrian experience**

## "Impulse für Arbeit" – IZA Meets Another Demand

In August 1999, a new employment initiative was established whose participants alone warrant a closer look. Among the founders are the VEBA AG, one of Germany's largest employers, represented by its chairman and CEO, Ulrich Hartmann; the suffragan bishop of the Diocese of Essen, *Franz Grave*; and the president of the Evangelical Church of the Rhineland, *Manfred Kock*. IZA is responsible for the management of this important project as well as for scientific advice and has already presented a research report on "Causes of and Strategies against Unemployment". (A German version of this research report is available at IZA's homepage). IZA-Director Klaus F. Zimmermann chairs a commission of high-ranking experts from universities, business and society.

The objective of "Impulse für Arbeit" ("Impulses for Employment") is to formulate specific policy recommendations and to develop projects that help reduce unemployment on the local and regional levels with the cooperation of adequate partners. "Impulse für Arbeit" will concentrate on the microeconomic level and the major problem group of the German labor market – the unskilled workers.

There are a number of initiatives in Germany that demonstrate the willingness to tackle the unemployment problem. But in many cases, the projects fail to focus on the relevant target groups. Instead they often favor groups that do not need immediate support. Many of the programs also lack scientific evaluation. As a consequence, the actual impact on employment that can be attributed to public or private initiatives often remains unclear. Nonetheless, "Impulse für Arbeit" – as well as working on the implementation of new models – will also examine the feasibility of existing projects.

When "Impulse für Arbeit" was presented to the public, VEBA human resources manager *Manfred Krüper* took the opportunity to stress the social responsibility of the business community. Employers should not limit their efforts to pointing out the failure of labor market policy and the need for reforms, but they should actively support the creation of new jobs. Both *Franz Grave* of the Catholic Church and *Manfred Kock* of the Protestant Church emphasized the churches' multifaceted commitment to encouraging

employment, which they intend to continue by participating in "Impulse für Arbeit".

IZA-Director *Klaus F. Zimmermann* pointed out the urgent need of targeted measures for the alarmingly large number of unskilled workers among the jobless. One fourth of all unskilled workers in West Germany – and as much as one half in the east – is out of work (see figure). Their jobs in the industrial sector have fallen victim to structural change and technological progress, and the emerging market for services has not yet produced enough new jobs to offset these losses. "Labor market policy needs active support at the local level by firms or private initiatives in order to create on-the-spot job opportunities for the less qualified. Our initiative is prepared to meet this chal-

lenge. It will not center on maximizing the number of job referrals but rather on hitting the relevant target group", Zimmermann explained.

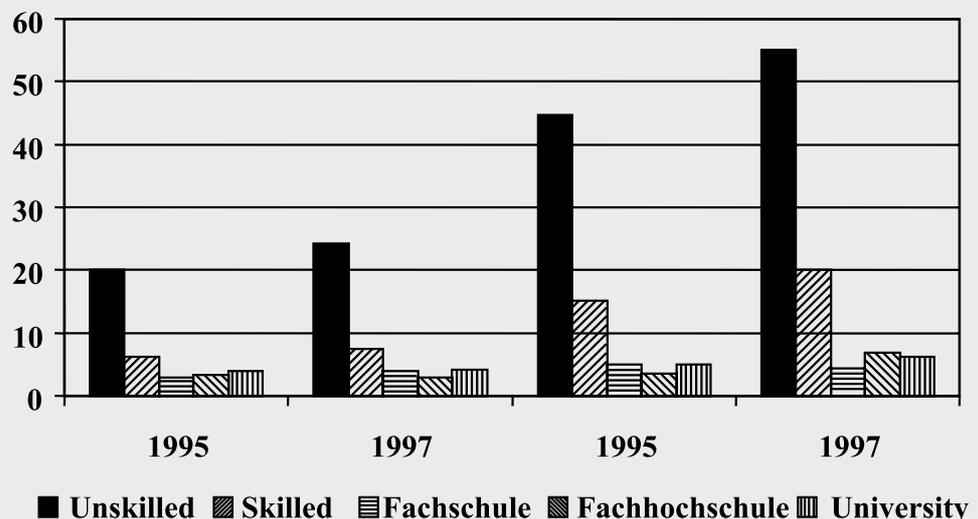
The projects envisaged by "Impulse für Arbeit" will include the following fields of activity: information on job search, strengthening of individual initiative, education and training, encouragement of risk-taking, and increasing the flexibility of employers and employees. The commission will act as a "think tank", but, in coordination with VEBA, it will also seek the cooperation of selected partners to put the ideas into practice,

"Impulse für Arbeit" has its own internet homepage (see [www.impulse-fuer-arbeit.de](http://www.impulse-fuer-arbeit.de)). It is designed mainly for the exchange of ideas.



Klaus F. Zimmermann, Manfred Krüper, Manfred Kock, Franz Grave

### Unemployment by Qualification and Educational Level in Germany (in percent)



■ Unskilled ■ Skilled ■ Fachschule ■ Fachhochschule ■ University

## European Symposium in Labor Economics 1999

The European Summer Symposium in Labor Economics (ESSLE 1999) was the first occasion for IZA to provide a forum for the lively exchange of ideas and experience among leading labor market experts. At the same time, this event gave up-and-coming European academics the opportunity to present their research findings. The labour group of the London-based "Centre for Economic Policy Research" (CEPR) is the core of this annual event. IZA director *Klaus F. Zimmermann* is also Co-Director of the CEPR research program in labor economics. IZA Fellow *Juan Dolado* is the other Co-Director.

The announcement of the symposium was met with such great response that a strict selection of participants was necessary. On September 13-19, 1999 forty researchers were able to discuss recent research findings in a relaxed atmosphere and to establish contacts for future cooperation. The management center of the Deutsche Post (German Postal Service) in the Bavarian town of Buch at the lake of Ammersee offered excellent working conditions. IZA was able to engage some of the most renowned experts in the field of labor economics to give presentations.

### The Efficiency of Labor Market Programs and Their Evaluation

The symposium began with a lecture by IZA Fellow *James J. Heckman* (University of Chicago, USA) on the effects of labor market programs and the problems of evaluating these programs.



James J. Heckman

Government initiatives to integrate the unemployed receive much public attention, especially regarding the use of funds provided by the tax-payer. Scientific evaluation of programs that have been put into practice often causes widespread disillusionment, however. This applies to training projects as well as to direct job subsidies and other measures. It is highly disputed whether

labor market intervention can be rendered more effective by narrowing down the targets. Although the government makes vast sums of money available, the current practice frequently shows that the indiscriminate distribution of funds is largely inefficient.

*James J. Heckman* gave a detailed explanation of the methodical problems of evaluating labor market programs. The United States has far more experience in this matter than Europe. This can be attributed partly to the fact that Americans are less hesitant to conduct so-called "social experiments". Heckman criticized that too much attention in the past has been paid to adjusting evaluation methods to existing selection problems instead of investing in the retrieval of more useful data.

### Social Security and Access to Retirement Benefits

*David Wise* (Harvard University, USA) gave a presentation on social security systems and their impact on access to retirement benefits.



David Wise

In most countries pension funding is still based on intergenerational contracts. Since most industrial countries witness an aging population, the problems of this concept are well-known: an increasingly small workforce has to finance pensions for a growing number of retirees. As a consequence, politicians in several countries have initiated reforms of a more or less fundamental nature. It is quite ironic, *Wise* contended, that the traditional social security system usually creates the very problems it will have to deal with later.

*David Wise* focused on incentives that influence the time at which retirement benefits are accessed. While some countries have strict regulations con-

cerning retirement age, others are more flexible in this respect. Empirical studies show that workers are surprisingly susceptible to incentives which encourage them to retire earlier. Politicians often underestimate the influence of other social security benefits on the time of retirement. But these benefits are sometimes used intentionally to lower the retirement age. In many countries, financing early retirement through unemployment benefits seems to be widely accepted as common practice.

### Growing Importance of School Education

*Orley Ashenfelter* (Princeton University, USA) lectured on the relationship between school education and labor income.



Orley Ashenfelter

Workers with a higher level of education earn a higher income on average, provided that their jobs correspond to their skills. Although this is not necessarily always the case, the underlying causal relationship is nowadays accepted as empirically proven. According to *Ashenfelter*, school education as the foundation of professional training will undoubtedly play an even more significant role in the future. It is therefore necessary to provide equal opportunities unless income differences are to become a foregone conclusion. *Ashenfelter* pointed out that various methods have already been tested. A viable policy could include the creation of supplementary education opportunities or direct financial support (in the form of government grants) for the education of children from low-income families. *Ashenfelter* also attended to the question of how to raise the general standard of education in order to achieve a higher income level in the long run. Although some approaches have been pursued, there is still little empirical evidence of their effectiveness.

## European Summer Symposium in Labour Economics

A CEPR-IZA Conference

### Tuesday 14 September:

- 09.30 - 11.30 1. Morning Session I** *Chair: Klaus F. Zimmermann*  
**Evaluation of Labour Market Programmes**  
 James Heckman (University of Chicago and IZA)
- 15.30 - 17.00 2. Parallel Session A** *Chair: Lars Ljungqvist*  
**Wages, Experience and Seniority**  
 Christian Dustmann (Institute for Fiscal Studies, University College London, CEPR and IZA)  
 Costas Meghir (Institute for Fiscal Studies, University College London and CEPR)
- 17.00 - 18.30 Household Characteristics, Ability and Education: Evidence from a Dynamic Expected Utility Model**  
 Christian Belzil (Concordia University and IZA)  
 Jörgen Hansen (IZA)
- 15.30 - 17.00 3. Parallel Session B** *Chair: Gerard Pfann*  
**Does Shorter Schooling Hurt Student Performance and Earnings?**  
 Jörn-Steffen Pischke (MIT, CEPR and IZA)
- 17.00 - 18.30 Transitions from School to Work: Search Time and Job Duration**  
 Espen Bratberg (University of Bergen)  
 Øivind Anti Nilsen (University of Bergen and IZA)
- 20.00 - 21.30 4. Parallel Session C** *Chair: Pietro Garibaldi*  
**The Evolution of Earnings Inequality in Italy and the Escalator Cause**  
 Marco Manacorda (Centre for Labor Economics, University of California, Berkeley)
- 20.00 - 21.30 5. Parallel Session D** *Chair: Gil Epstein*  
**Immigrant Labor and Workplace Safety**  
 Thomas Bauer (IZA and CEPR)  
 Andreas Million (University of Munich),  
 Ralph Rotte (University of Munich and IZA),  
 Klaus F. Zimmermann (IZA, Bonn University and CEPR)

### Wednesday 15 September:

- 09.30 - 11.30 6. Morning Session II** *Chair: Juan J. Dolado*  
**Social Security Programs and Retirement Around the World**  
 David Wise (NBER and Harvard University)
- 15.30 - 17.00 7. Parallel Session A** *Chair: Michael Burda*  
**Squandering European Labor: Social Safety Nets and Economic Turbulence**  
 Lars Ljungqvist (Stockholm School of Economics, CEPR and IZA)
- 17.00 - 18.30 Modelling Financial Incentives to Get Unemployed into Work**  
 Jan Boone (CentER, Tilburg University, and CPB)  
 Jan van Ours (CentER, Tilburg University, CEPR and IZA)
- 15.30 - 17.00 8. Parallel Session B** *Chair: Barbara Petrongolo*  
**On the Neutrality of Severance Payments in the Theory of Search Unemployment**  
 Pietro Garibaldi (International Monetary Fund and CEPR)  
 Gianluca Violante (University College London and CEPR)
- 17.00 - 18.30 Job Protection, Minimum Wage and Unemployment**  
 Pierre Cahuc (University of Paris I, CEPREMAP, CREST-INSEE, Institut Universitaire de France and IZA)  
 André Zylberberg (CNRS and University of Paris I)
- 20.00 - 21.30 9. Parallel Session C** *Chair: Marco Francesconi*  
**General Training and Human-Capital Externalities**  
 Alison Booth (University of Essex, CEPR and IZA)
- 20.00 - 21.30 10. Parallel Session D** *Chair: Javier Ortega*  
**The Endogenous Determination of the Minimum Wage**  
 Gil Epstein (Bar-Ilan University, CEPR and IZA)  
 Shmuel Nitzan (Bar-Ilan University)

### Thursday 16 September:

- 09.30 - 11.30 11. Morning Session III** *Chair: Costas Meghir*  
**The Payoff to Education**  
 Orley Ashenfelter (Princeton University)
- 20.00 - 21.30 12. Parallel Session A** *Chair: Pietro Garibaldi*  
**Screening vs. Training in General Equilibrium Search Models**  
 Etienne Wasmer (ECARE, University of Bruxelles, CEPR and IZA)
- 20.00 - 21.30 13. Parallel Session B** *Chair: Christian Dustmann*  
**Corporate Downsizing and Efficient Quitting**  
 Gerard Pfann (Maastricht University, CEPR and IZA)

### Friday 17 September:

- 09.30 - 11.30 14. Morning Session IV** *Chair: Alison Booth*  
**The Future of Personnel Economics**  
 Edward Lazear (Stanford University)
- 15.30 - 17.00 15. Parallel Session A** *Chair: Jennifer Hunt*  
**Money for Nothing and Your Chips for Free? The Anatomy of the PC Wage Differential**  
 John Haiksen-DeNew (DIW and IZA)  
 Christoph M. Schmidt (University of Heidelberg, CEPR and IZA)
- 17.00 - 18.30 Labor Market Assimilation and the Self-Employment Decision of Immigrant Entrepreneurs**  
 Magnus Lofstrom (IZA)
- 15.30 - 17.00 16. Parallel Session B** *Chair: Thomas Bauer*  
**Group Interactions and Individual Background: Explaining Regional Shirking Differentials in a Large Italian Bank**  
 Andrea Ichino (European University Institute, IGIER, CEPR and IZA)  
 Giovanni Maggi (Princeton University and NBER)
- 17.00 - 18.30 Absenteeism and Employment Probation**  
 Regina Riphahn (University of Munich, CEPR and IZA),  
 Anja Thalmaier (IZA)
- 20.00 - 21.30 17. Parallel Session C** *Chair: Jörn-Steffen Pischke*  
**Employment and the Distributional Effects of Restricting Working Time**  
 Ramon Marimon (European University Institute, University Pompeu Fabra, Barcelona, NBER and CEPR)  
 Fabrizio Zilibotti (Institute for International Economic Studies, Stockholm, University Pompeu Fabra, Barcelona and CEPR)

**20.00 - 21.30 18. Parallel Session D** *Chair: Jan van Ours*  
 Re-employment Probabilities and Returns to Matching  
 Barbara Petrongolo (University Carlos III, Madrid, London School of Economics and CEPR)

**Saturday 18 September:**

**09.30 - 11.30 19. Morning Session V** *Chair: Zvi Eckstein*  
**The Evolution of Labour Markets in Transitional Economies,**  
 Jan Svejnar (WDI, University of Michigan, CERGE-EI, Prague and CEPR)

**15.30 - 17.00 20. Parallel Session A** *Chair: John Haisken-DeNew*  
**Post-Unification Wage Growth in East Germany**  
 Jennifer Hunt (Yale University, CEPR, and IZA)

**17.00 - 18.30 Estimating Wage Losses of Displaced Workers in Germany**  
 Michael Burda (Humboldt-University of Berlin, CEPR and IZA)  
 Antje Mertens (Max Planck Institute and Humboldt-University of Berlin)

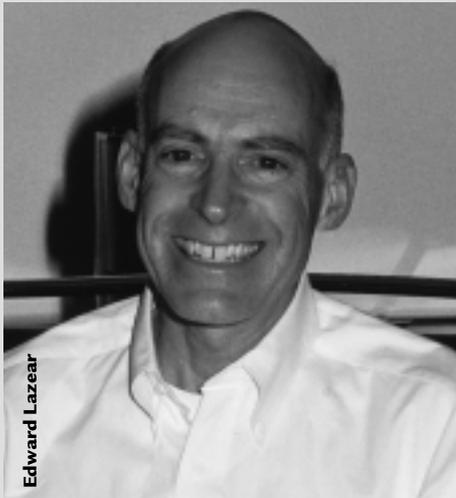
**15.30 - 17.00 21. Parallel Session B** *Chair: Oivind Anti Nilsen*  
**Identifying the Effect of Unemployment on Crime**  
 Steven Raphael (University of California)  
 Rudolf Winter-Ebmer (University of Linz,  
 Vienna Institute for Economic Policy Research, CEPR and IZA)

**17.00 - 18.30 Demand Uncertainty, Mismatch and (Un)Employment - A Microeconomic Approach**  
 Mohamed Jellal (CES, University of Rabat)  
 Jacques-François Thisse (CORE, Université Catholique de Louvain, CERAS, Ecole Nationale des Ponts et Chaussées and CEPR)  
 Yves Zenou (CERAS, Ecole Nationale des Ponts et Chaussées, GAINS, Université du Maine, CEPR and IZA)

**Organizers:** Juan J. Dolado (Universidad Carlos III, Madrid, CEPR and IZA)  
 Klaus F. Zimmermann (IZA, Bonn University and CEPR)

## The Future of Personnel Economics

One of the leading experts in personnel economics, *Edward Lazear* (Stanford University, USA), gave a presentation on the future of this relatively young field.



Edward Lazear

It applies microeconomic instruments to all areas inside a company that are relevant to personnel questions. Although related to human resource management (as taught in business administration courses), the approach to this important issue is fundamentally different. Personnel economics centers on the assumption that individuals act rationally and that their behavior is influenced by interaction with others rather than by outside forces. It also assumes a state of equilibrium and efficiency. According to Edward Lazear, this combination enables personnel economists to produce structured and precise answers.

The goal is to develop an understanding of the behavior of individuals inside a company and eventually to arrive at practical concepts. Various empirical studies already support the theoretical models. Edward Lazear pointed out that personnel economics still contains many interesting, unanswered questions and is thus a area for vast future research.

## The Development of Labor Markets in Transition Countries

The transformation of Eastern European labor markets was the central topic of a lecture by *Jan Svejnar* (University of Michigan, USA and CEPR).



Jan Svejnar

In the decade after the fall of the Iron Curtain, the former Socialist countries have moved with varying success towards a market economy.

Unemployment in many transition countries has climbed to double digits,

notwithstanding a strong decrease in workforce participation, extreme currency devaluation, cuts in the once enormous unemployment benefits, and great efforts to shape an active labor market policy. A variety of more detailed observations document the transition to market economies. As Jan Svejnar explained, the wage level, for instance, now depends strongly on the company's success. In addition, rapid increases in returns to human capital has contributed to larger income variations at a macroeconomic level. Another remarkable observation is that the creation of an adequate economic framework under the new regime has exerted very little influence on individual behavior. More generous unemployment benefits, for example, did not necessarily bring about longer periods of unemployment.

## A Successful Event

Many further discussions and lectures on labor market topics rounded off the European Summer Symposium in Labor Economics. Throughout the course of the event, the participants had the opportunity to exchange ideas in smaller groups. The concept of the ESSLE was without doubt a full success. Unlike the larger economic conferences, where labor economics, as one field of many, usually receives less room for the presentation of research findings, the ESSLE was a fertile ground for extensive discussion of topics in labor economics. The management center of the Deutsche Post AG offered the perfect environment and will again be the location for ESSLE over the next years.

# CURRENT RESEARCH

## Migration: The Controversies and the Evidence – A New Study on the Substitutability Between Trade and Migration

This just out anthology takes a critical look at the current divide over immigration policies. It hopes to shed new light on the debate by bringing together papers that investigate the link between trade and factor mobility, particularly labor migration, from theoretical and empirical perspectives. It examines the

substitutability between trade and migration, the impact of regional integration on the location of economic activity, the role of public goods provisions, and the political economy of migration. Several papers quantify the link between trade, trade policies, migration, and income distribution in sending and receiving nations using econometric methods and general equilibrium simulations. Case studies of past and present migration episodes

are also presented: the impact of NAFTA on migratory pressure and wage gaps; the trade-migration links between Eastern and Western Europe; and the historical experience with migration flows in the nineteenth century. The editors are Riccardo Faini (University of Brescia, Centro Studi Luca d'Angliano, and CEPR), Jaime de Melo (University of Geneva and CEPR) and Klaus F. Zimmermann (IZA, Bonn University and CEPR)

## Migration

### The Controversies and the Evidence

Edited by Riccardo Faini, Jaime de Melo, Klaus F. Zimmermann

#### Contents

#### Trade and migration: an introduction

*Riccardo Faini/Jaime de Melo/Klaus F. Zimmermann*

#### Part One: Insights from Theory

#### Trade liberalisation and factor mobility: an overview

*Antony J. Venables*

Discussion: André Sapir

#### Regional integration, trade and migration are demand linkages relevant in Europe?

*Rodney D. Ludema/Ian Wooton*

Discussion: Giorgio Basevi

#### Beyond international factor movements: cultural preferences, endogenous policies and the migration of people: an overview

*Arye L. Hillman/Avi Weiss*

Discussion: Francesco Daveri

#### Trade liberalisation and public-good provision: migration-promoting or migration-detering?

*Konstantine Gatsios/Panos Hatzipanayotou/Michael S. Michael*

Discussion: Ignazio Musu

#### Part Two: Quantifying the Links between Trade and Migration

#### Trade and migration: a production-theory approach

*Ulrich Kohli*

Discussion: Marzio Galeotti

#### Migration, dual labour markets and social welfare in a small open economy

*Tobias Müller*

Discussion: Rudolf Winter-Ebmer

#### Globalisation and migratory pressures from developing countries: a simulation analysis

*Riccardo Faini/Jean-Marie Grether/Jaime de Melo*

Discussion: Alessandra Venturini

#### Part Three: Historical and Contemporary Evidence

#### Were trade and factor mobility substitutes in history?

*William J. Collins/Kevin O'Rourke/Jeffrey G. Williamson*

Discussion: Gianni Toniolo

#### Liberalisation and incentives for labour migration: theory with applications to NAFTA

*James R. Markusen/Steven Zahniser*

Discussion: Pasquale M. Sgro

#### East-West trade and migration: the Austro-German case

*Rudolf Winter-Ebmer/Klaus F. Zimmermann*

Discussion: Marina Schenkel



### New IZA Report on Job Creation for Unskilled Labor

IZA just completed a study on the question of promoting a low-wage sector. The report, by order of the German Ministry of Labor, analyzes different models and estimates the costs incurred as well as the number of potentially created jobs (see also page 14 of this issue). The study is available in German language at [www.iza.org](http://www.iza.org).



### IZA Report: "Causes and Ways to Fight Unemployment"

In time for the start of the employment initiative entitled "Impulse für Arbeit", IZA has presented a report on the situation of the German labor market and the specific problems in the field of unskilled labor (see also page 5 of this issue). The complete text can be downloaded at [www.iza.org](http://www.iza.org).



### Journal of Population Economics: A Decade of Success

A recent article in "Population and Development Review" (Hendrik P. van Dalen/Kène Henkens, How Influential are Demography Journals?, in: Population and Development Review 25, 1999, pp. 229-251) investigates the importance of demographic journals. It is based on statistics provided by the

Institute for Scientific Information (ISI), such as the well-known Social Science Citation Index (SSCI). The Journal of Population Economics, which first appeared in 1988 and had been in circulation for only eight years in the data set at the time of the analysis, was by far the youngest of the sixteen scientific journals under study. Twelve of its competitors had already been on the market for over twenty years. Since the study mainly examines how often each journal is quoted in other publications, the long-established journals naturally

have a greater competitive advantage. This situation notwithstanding, the Journal of Population Economics, headquartered at IZA, has been enormously successful.

The statistics warrant a surprisingly favorable evaluation. The number of articles from the Journal of Population Economics cited in other publications within the first two years (or five years, respectively) of its existence is far above the average of all journals under study. The analysis also shows that the

strength of the Journal of Population Economics lies in its capability to publish highly relevant articles about issues of ongoing scientific debates. In addition, the Journal of Population Economics is quoted much more frequently in economic journals than in demographic publications. This fact demonstrates that the Journal has already taken its envisioned role as a link between demography and economics, thus preparing the way for demographic questions and research findings to enter the world of economics.

## SHORT REPORTS

### +++ Third European Summer School in Labor Economics: May 29 – June 4, 2000

#### +++ Call for Papers +++

In the year 2000, the Third European Summer School in Labor Economics will take place from May 29 – June 4 at the lake of Ammersee near Munich in Bavaria, Germany. Once again IZA has been able to engage renowned labor market experts to give lectures on a frontier research agenda research findings and to discuss labor market topics with a larger number of Ph.D. students, who also present their own research ideas during the course of the week. The lecturers are: *Dan Hamermesh* (University of Texas at Austin, USA) on "Labor demand," and *Gerard van den Berg* (Free University of Amsterdam, The Netherlands and CEPR); on "Search models and duration models in labor economics". Submissions of students who want to participate should reach IZA not later than December 31, 1999. All applicants must submit a CV, a letter of support from a Ph.D. supervisor, and an abstract of a potential presentation of own research results. Only applications from Ph.D. students from European universities will be considered. Submissions by fax or email to Dr. Thomas Bauer (fax: +49-228-3894-210; email: [bauer@iza.org](mailto:bauer@iza.org)) are recommended. Details on the previous European Summer Schools in Labor Economics and the application procedure are available on the IZA homepage.



### +++ ESPE 2000 at IZA +++ Call for Papers +++

The Fourteenth Annual Conference of the European Society for Population Economics (ESPE) will take place at IZA, June 15-17, 2000. The purpose of the conference is the exchange of research in the allied fields of labor eco-

nomics, household economics, public economics, demography, statistics, and economic history. Abstracts of papers for presentation at this conference should be submitted, together with a draft of a completed paper if available, by February 1, 2000. The preliminary program will be mailed to those who submit papers and to other ESPE members on March 15, 2000. Waivers of the conference fee will be provided for ten graduate students. For more details on ESPE 2000 see [www.iza.org](http://www.iza.org).



### +++ IZA Workshop: "Absenteeism and Economic Incentives – Comparisons Across Countries" +++

On November 6, 1999, IZA hosted an international workshop considering the driving forces behind absenteeism. The workshop brought together academics from a variety of countries, who presented the most recent research results from within their different institutional settings. This will promote the formulation of policy recommendations. For the program see [www.iza.org](http://www.iza.org).



### +++ IZA Workshop: "The Economics of Child Care" +++

The objective of this meeting, which took place at IZA on November 15-16, 1999, was to ignite discussion of what factors are important in the provision of effective and efficient child care. On an international level, child care has featured prominently on the agenda of political parties in recent years. In contrast, economists have rarely discussed this topic until now. The workshop collected the most important European and American research results. For more details visit IZA's homepage.

### +++ IZA Workshop: "Evaluation of Labour Market Projects" +++

An IZA expert meeting on the evaluation of labor market projects will take place in Berlin on November 29-30, 1999. Further details are available on the IZA homepage.



### +++ "Labour Demand, Education and the Dynamics of Social Exclusion" – CEPR Workshop in Israel +++

"Labour Demand, Education and the Dynamics of Social Exclusion" is the subject of a CEPR workshop, hosted by the Department of Economics, Bar-Ilan University, Israel, on November 21-22, 1999. IZA will be represented by various researchers. IZA Director *Klaus F. Zimmermann* and IZA Fellow *Shoshana Neuman* (Bar-Ilan University and CEPR) are responsible for organizing the event. More details can be found at [www.iza.org](http://www.iza.org).



### +++ Successful CEPR-IZA Conference in Dublin: "Marginal Labour Markets in Metropolitan Areas" +++

Hosted by the Economic and Social Research Institute (ESRI), a CEPR Conference on "Marginal Labour Markets in Metropolitan Areas" took place in Dublin, Ireland, on October 10-12, 1999. Some of IZA's Research Associates and Research Fellows have participated. Organizers were IZA Fellow *Alan Barrett* (ESRI and CEPR) and IZA Director *Klaus F. Zimmermann*. For the program see p. 11.



### +++ Successful IZA Workshop: "Working Time Reduction: A European Perspective" +++

During an IZA workshop on working time reduction in Berlin, October 27, 1999, *Thomas Bauer* (IZA and CEPR) lectured on

## Marginal Labour Markets in Metropolitan Areas

Hosted by the Economic and Social Research Institute. Dublin, 10/12 October 1999

### Sunday 10 October:

#### Morning Session:

##### Immigrants (1)

Chair: Alan Barrett

09.00 - 10.15

##### Natives and Migrants in the London Labour Market 1929-31

Timothy Hatton (University of Essex, CEPR and IZA) and Roy Bailey (University of Essex)

Discussant: Per-Anders Edin (Uppsala University and CEPR)

10.15 - 11.30

Chair: Alan Barrett

##### Immigrant Earnings: Language Skill, Linguistic Concentrations and the Business Cycle

Barry R. Chiswick (University of Illinois, Chicago and IZA) and Paul W. Miller (University of Western Australia)

Discussant: Christian Dustmann (University College London, CEPR and IZA)

12.00 - 13.15

Chair: Alan Barrett

##### Labor Market Assimilation and the Self-Employment Decisions of Immigrant Entrepreneurs

Magnus Lofstrom (IZA)

Discussant: Shoshana Neuman (Bar-Ilan University, Ramat-Gan, CEPR and IZA)

#### Afternoon Session:

##### Neighbourhood Effects

Chair: Timothy Hatton

14.30 - 15.45

##### Settlement Policies, Ethnic Enclaves, and the Economic Success of Immigrants

Olof Åslund (Uppsala University), Per-Anders Edin (Uppsala University and CEPR) and Peter Fredriksson (Uppsala University)

Discussant: Olive Sweetman (National University of Ireland, Maynooth)

16.15 - 17.30

Chair: Timothy Hatton

##### Residential Location and Youth Unemployment: The Economic Geography of School-to-Work Transitions

Regina T. Riphahn (University of Munich, CEPR and IZA)

Discussant: Alessandra Venturini (University of Padova and IZA)

### Monday 11 October:

#### Morning Session:

##### Cities

Chair: Alan Barrett

09.00 - 10.15

##### Why Do Poor People Live in Cities?

Edward Glaeser (Harvard University)

Discussant: Yves Zenou (Université Panthéon-Assass, Paris, CEPR and IZA)

10.15 - 11.30

Chair: Alan Barrett

##### The Impact of the Indonesian Economic Crises on Urban Employment

Kathleen Beagle (RAND, California) Elizabeth Frankenberg (RAND, California), James P. Smith (RAND, California) and

Duncan Thomas (RAND, California and UCLA)

Discussant: Thomas Bauer (IZA and CEPR)

12.00 - 13.15

Chair: Regina Riphahn

##### The Amsterdam Labour Market: A Problem Posed

Joop Hartog (University of Amsterdam and IZA) and Aslan Zorlu (University of Amsterdam)

Discussant: Kostas Mavromaras (University of Newcastle and IZA)

#### Afternoon Session:

##### Theory of Marginalization

Chair: Amanda Gosling

14.30 - 15.45

##### Endogenous Marginalisation of Immigrants

Gil S. Epstein (Bar-Ilan University, Ramat-Gan, CEPR and IZA)

Discussant: Peter Frederiksson (Uppsala University)

16.15 - 17.30

Chair: Amanda Gosling

##### A Theory of Prostitution: The Madonna-Whore Dichotomy Revisited

Lena Edlund (Stockholm School of Economics and Columbia University) and Evelyn Korn (University of Tübingen)

Discussant: Robert E. Wright (University of Stirling, CEPR and IZA)

### Tuesday 12 October:

#### Morning Session:

##### Marginalized Groups

Chair: Thomas Bauer

09.00 - 10.15

##### The Impact of National Policy and Occupational Mobility on the Sub-Minimum Wage Employment of Latina Women in the United States

Deborah A. Cobb-Clark (Australian National University, Canberra) and Sherrie A. Kossoudji (University of Michigan)

Discussant: Amanda Gosling (University of Essex and CEPR)

10.15 - 11.30

##### Urban Housing and the Role of 'Underclass' Processes: The Case of Ireland

Brian Nolan (Economic and Social Research Institute, Dublin) and Chris Whelan (Economic and Social Research Institute, Dublin)

Discussant: Jan C. van Ours (CentER, Tilburg University, CEPR and IZA)

12.00 - 13.15

Chair: Thomas Bauer

##### Enclaves, Neighbourhood Effects and Economic Activity: Ethnic Minorities in England and Wales

Kenneth Clark (University of Manchester) and Stephen Drinkwater (University of Surrey)

Discussant: Colm Harmon (University College Dublin and CEPR)

#### Afternoon Session:

##### Immigrants (2)

Chair: Alan Barrett

14.30 - 15.45

##### The English Language Fluency and Occupational Success of Ethnic Minority Immigrant Men Living in English Metropolitan Areas

Michael A. Shields (University of Leicester and IZA) and Stephen Wheatley Price (University of Leicester)

Discussant: Donal O'Neill (National University of Ireland, Maynooth)

#### Organizers:

Alan M. Barrett (Economic and Social Research Institute, Dublin, CEPR and IZA)

Klaus F. Zimmermann (IZA, Bonn University and CEPR)

"Overtime Reduction and Unemployment". *Francis Kramarz* (CREST, France, CEPR and IZA) gave a presentation on "The French Experience of Working Time Reduction". *Rob Euwals* (IZA) lectured on "The Myth of Worksharing - A Case Study for the Netherlands". IZA Director *Klaus F. Zimmermann* led the discussion.



**+++ Dennis J. Snower is New IZA Research Director for its "Welfare State and Labor Market" Program +++**

The renowned English labor economist *Dennis J. Snower* has taken leadership of the IZA research program entitled "Welfare State and Labor Market". Since 1989, he has been Professor of Economics at Birkbeck College, University of London. Teaching and research assignments have taken him around the world to institutions including Columbia University, the University of Stockholm, the University of Jerusalem, the International Monetary Fund, the European University Institute, and Dartmouth College. Prior to these posts, he had been assistant professor at the University of Maryland and the Vienna Institute of Advanced Studies. In 1975, he received a Ph.D. for his dissertation on "Dynamic Forces of Advanced Capitalist Economies". His most recent publications include *Unemployment Policy: Government Options for the Labour Market* (edited with Guillermo de la Dehaza), Cambridge 1997; *Economic Policies and Unemployment Dynamics in Europe* (edited with Brian Henry), Washington 1996; and *Acquiring Skills: Market Failures, their Symptoms and Policy Responses*, Cambridge 1996. His scientific essays were published in journals such as the *American Economic Review*, *Journal of Political Economy*, *European Economic Review*, *Oxford Economic Papers*, *Economic Journal* and the *Journal of Population Economics*. Dennis J. Snower has been Fellow of the Royal Society of Arts since 1993 and IZA Fellow since 1998.



Dennis J. Snower

The new IZA research director describes the objective of the IZA research program that is now under his guidance: "The welfare state is under scrutiny all over Europe. It has to set the right incentives to create employment. Periods of unemployment need to be shortened and used for acquiring or improving skills. The goal of welfare state policy should not be drastic cuts in the welfare system, but much rather a bundle of positive incentives".



**+++ New IZA Staff Members +++**

In July 1999, *Jörgen Hansen* joined the IZA team as a research associate. He received his Ph.D. in Economics from the University of Gothenburg, Sweden, in 1997. Part of his graduate training he spent at Stanford University and the University of Michigan at Ann Arbor. Before *Jörgen Hansen* joined IZA, he spent two years in Montreal (at the University of Montreal and Concordia University) as a visiting scholar. His research interests include returns to education, labor supply, discrimination, and welfare dependency.



Jörgen Hansen

Also in July, *Magnus Lofstrom* became a new IZA research associate.

He received his doctorate from the University of California, San Diego, in June 1999 for his dissertation entitled "Three Essays on the Role of Skills and Education in Immigration and Self-Employment". Additional research projects he has been involved with include studies analyzing the role of immigrant labor in the U.S. and Japanese economies, the effects of welfare reform on unemployment, and the effects of immigration on schooling. His research interests at IZA include migration, self-employment, education, and earnings inequality.



Magnus Lofstrom

*Simone Fuchs* joined the IZA as a team assistant in June 1999. She works for the *Journal of Population Economics* and takes responsibility for management issues like the organization of different research events. In addition, she has taken over some duties at the IZA secretary.



Simone Fuchs



**+++ IZA Research Affiliates on Assignments Abroad +++**

Starting this fall, several IZA Research Affiliates spend ten months abroad working in foreign research institutions. Their assignments are part of the "European Doctoral Program in Quantitative Economics" at the University of Bonn. *René Fahr* stays at the London School of Economics, *Lieselotte Locher* at the University of Tel Aviv, *Uwe Sunde* at Pompeu Fabra University in Barcelona, and *Wendelin Schnedler* at the Centre de Recherche en Economie et Statistique (CREST) in Paris. IZA provides financial support to *Wendelin Schnedler*, whose research will be part of the CEPR-IZA project entitled "Labor Demand, Education and the Dynamics of Social Exclusion". The other IZA affiliates receive grants from the German Academic Exchange Service (DAAD). IZA and the University of Bonn cooperate closely in supporting these projects.

### IZA VISITORS PROGRAM

A number of renowned economists visited IZA from July to October 1999 to exchange research findings and discuss problems of international labor market policy, including:

- |   |   |
|---|---|
| - <i>Christoph M. Schmidt</i><br>University of Heidelberg, Germany            | - <i>Zvi Eckstein</i><br>University of Tel Aviv, Israel             |
| - <i>Josef Zweimüller</i><br>University of Zurich, Switzerland                | - <i>Stephen Nickell</i><br>London School of Economics, UK          |
| - <i>Wolfgang Schwerdt</i><br>University of Paris, France                     | - <i>Joop Hartog</i><br>University of Amsterdam, The Netherlands    |
| - <i>Dennis Snower</i><br>Birkbeck College, London, UK                        | - <i>Lars-Hendrik Röller</i><br>Humboldt-University Berlin, Germany |
| - <i>Regina Riphahn</i><br>University of Munich, Germany                      | - <i>Nina Smith</i><br>Aarhus School of Economics, Denmark          |
| - <i>Jan C. van Ours</i><br>University of Tilburg, The Netherlands            | - <i>Giorgio Brunello</i><br>University of Padua, Italy             |
| - <i>Ira N. Gang</i><br>Rutgers University, USA                               | - <i>Kurt Brannas</i><br>University of Umea, Sweden                 |
| - <i>Gil Epstein</i><br>Bar-Ilan University, Israel                           | - <i>Harmen Lehment</i><br>University of Kiel, Germany              |
| - <i>Kevin J. Murphy</i><br>University of Southern California, USA            | - <i>Richard Freeman</i><br>Harvard University, USA                 |
| - <i>Guisepe Bertola</i><br>European University Institute, Italy              | - <i>Stefan Bender</i><br>IAB, Nuremberg, Germany                   |
| - <i>Arie Kapteyn</i><br>University of Tilburg, The Netherlands               | - <i>John Haisken-DeNew</i><br>DIW, Berlin, Germany                 |
| - <i>Don J. DeVoretz</i><br>Simon Fraser University, Canada                   | - <i>Alison Booth</i><br>University of Essex, UK                    |
| - <i>Christiane Werner</i><br>Simon Fraser University, Canada                 | - <i>John M. Abowd</i><br>Cornell University, Ithaca N. Y., USA     |
| - <i>Gerard van den Berg</i><br>Free University of Amsterdam, The Netherlands |   |



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A complete list of IZA Discussion Papers is available on our homepage at [www.iza.org](http://www.iza.org). Most papers are downloadable.

# O P I N I O N

## The Low-Wage Sector – Worth a Try!



Globalization has altered the economic framework for labor and has intensified communication, information, trade, and capital transfers. This process has aggravated the labor market position of less-skilled workers, especially in Europe, where they are now facing unemployment of dramatic proportions.

– Trying to moderate productivity growth by slowing down technological progress would be ill-advised, however. We should instead trust that a policy of encouraging the acceptance of information technology will quickly open new markets and create employment. Policy-makers and companies should review their modernization strategies and analyze whether they are in fact creating new employment opportunities for less-skilled workers.

– A "qualification offensive" by both the government and the private sector could eliminate productivity deficits of less-qualified workers – within the limits of trainability, of course. This, however, would only bring relief in the medium run. It is furthermore questionable whether the market for further

training is already flexible enough to master new challenges. A successful fight against unemployment does not depend on high-tech training but on a principal strategy for qualifying workers to perform simple tasks.

– A stronger demand for goods and services that are produced by less-skilled workers may bring about an increase in product prices (relative to those of other goods and services) and, consequently, a higher labor demand. But the government would have to cooperate, for instance, by systematically chipping away at regulatory restrictions in the service sector.

– A reduction of direct or indirect wage costs could lower the gross wages paid by firms. This would not only require an agreement on wage cuts in the low-wage sector but also drastic cuts in government spending that could affect, for example, retirement benefits. The generally high wage level is not what causes the current problems. Nonetheless, even in Germany simple tasks have to become cheaper, and the wage gap between low-income and high-income jobs has to be widened for at least a while.

So is the creation of a low-wage sector, as discussed in the German "Alliance for Jobs" talks, the right concept? Many of the proposed models suggest that Social Security contributions should be provided here, entirely or in part, by the government. This would allow labor market intervention from two sides: As firms profit from falling gross wage costs, they will demand more labor. Workers may earn higher incomes, which would make alternative transfer payments less attractive and encourage unemployed workers to accept a job.

Tempting though this may seem, it would be wrong to rely on subsidies in the low-wage sector to boost a larger

supply of labor. An increased labor supply would only generate more employment if wages were allowed to drop under the pressure of competition. In reality, this is unlikely to happen in Germany. It is therefore important to concentrate on the demand side.

In a recent report, IZA evaluated one of the proposals put forward in the German "Alliance for Jobs" talks. The model in question is based on subsidies for employer contributions to Social Security. According to the study, the net burden imposed on public budgets would amount to DM 14.2 billion, while the net credit to Social Security would be DM 12.6 billion. This could help create up to 400,000 new jobs. The tax-payer would have to carry net costs of barely DM 4,000 per new job per year. Sounds like a pretty good deal! A model experiment could clarify whether this approach would at least ignite the initial spark for change in the labor market.

But there is ample reason to doubt that expensive long-term subsidies or a stabilizing low-wage sector will continue to be prudent policy options in the long run. Eventually, it will be up to the market to create demand opportunities and to assess qualifications. Assuming an increase in the demand for goods produced by workers who are now considered unskilled or less-qualified, worker's wages could also rise. This would be the ideal way to approach unemployment problem. The State could play an activating role by granting targeted business start-up loans for less-qualified workers, by lowering consumption taxes for goods from the low-wage sector, or by spurring government demand in this sector.

*K. F. Zimmermann*



IZA

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zur Zukunft  
der Arbeit

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