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Whither activation policies? Reflections for the future

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Reflections for the Future**

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ABSTRACT

Whither Activation Policies? Reflections for the Future*

Activation policies aimed at getting working-age people off benefits and into work have been embraced by many OECD countries. In a previous paper, I have argued that activation strategies have performed well during the Great Recession and subsequent recovery in some, but not all, of these countries. At the same time it is pertinent to look to the future and to consider what challenges the activation paradigm is likely to face over the coming decades when US and European labour markets have to cope with ageing workforces and immigration, to name but two. In this paper, I set out my views on some of the major challenges facing activation strategies in the future.

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Introduction

What Weishaupt (2011) calls the “activation paradigm” has slowly made inroads in most OECD countries over the past three decades as the dominant approach to tackling the unemployment problem. As such, it built upon and extended an earlier approach to labour market policy which focussed on the role of so-called “active labour market policies” (ALMPs) designed to assist the unemployed to find work. As Weishaupt (2011) notes, the OECD and later the EU Commission played important roles in providing the evidence base for their respective member countries to adopt the activation paradigm and adapt it to their specific histories, institutions and starting points. However, not all countries have bought into the activation paradigm or, even if they pay lip service to it in their policy declarations, have opted to implement its key requirements in a way that is conducive to producing favourable labour market outcomes.

The Great Recession which began in 2008 provided a severe stress test for the activation paradigm as unemployment jumped sharply in many OECD countries and the later Euro crisis gave rise to unprecedented hikes in unemployment in those countries most affected, namely Greece, Ireland, Portugal and Spain. The US economy also experienced a sharp jump in unemployment in 2009-2010, leading to a historically high incidence of long-term unemployment (defined as those out of work for a year or more as a proportion of total unemployment)¹. As a result, the initial stages of the Great Recession witnessed some convergence in labour market performance between the US and Europe. However, the US economy and labour market recovered more quickly than Europe and the unemployment rate in mid-2016 was down to under 5%, half of its post-2008 peak. Nonetheless, the incidence of long-term unemployment remains at almost double its 2007 level: in the first quarter of 2016, it stood at 18.2% compared with 9.7% in the same quarter in 2007.² The European economy and labour market only began to recover in early 2013 and the EU 28 harmonised unemployment rate of 8.6% (seasonally adjusted) in July 2016 is still well above the pre-Great Recession trough of under 7%.

In Martin (2015), I have argued that activation strategies have performed well during the Great Recession and subsequent recovery in some, but not all, countries. Hence, much work remains to ensure that unemployment rates in Europe decline to pre-crisis levels and the US long-term unemployment problem returns to a more normal level.

At the same time it is pertinent to look to the future and to consider what challenges the activation paradigm is likely to face over the coming decades when US and European labour markets have to cope with ageing populations and workforces and immigration, to name but two. In this paper, I set out my views on some of the major challenges facing activation strategies in the future. These views are naturally shaped by my many years of working on this topic at the OECD and extensive reading of the cross-country literature on activation.

The structure of the paper is as follows. First, I trace in a very schematic fashion the roots of the activation paradigm in many European countries. Second, I discuss the different trade-offs which countries have opted to make between the key pillars of an activation strategy and how this has varied over time. Third, I give my assessment of the successes and failures of activation to date. Finally, I present some major challenges facing activation strategies now and into the future.

The roots of activation

Here I can be very brief since this topic is covered exhaustively in Weishaupt (2011). He rightly traces the origins back to the Rehn-Meidner model of Swedish labour market policy which was developed in the 1950s, and later propagated actively among OECD countries in the 1960s and 1970s, especially during the period when Gosta Rehn was Director of the OECD’s Manpower Directorate.

In the Rehn-Meidner model, ALMPs had a crucial role to play in helping to reduce structural unemployment and ensuring that counter-cyclical policy did not run into inflationary bottlenecks. At the beginning, the concept of activation was viewed in a very narrow sense: it meant increasing public resources going into a range of ALMPs as opposed to spending public resources on so-called “passive labour market policies”, namely unemployment insurance (UI), unemployment assistance (UA) and related welfare benefits. The underlying idea was to shift the balance of public spending on labour market policies away from passive spending towards spending on ALMPs and in that way help to reduce structural unemployment.

Following the two oil shocks of the 1970s and the prolonged stagflation of the 1980s and early 1990s, this view of ALMPs still held sway. This can be seen clearly in the OECD’s 1994 Jobs Study. One of the 10 principal recommendations of the Jobs Study was to “Expand and enhance active labour market policies”. The thinking behind this specific recommendation was two-fold: (i) shift the weight of public spending on labour market policies away from unemployment benefits to more active measures which assist reemployment; and (ii) enhance the effectiveness of ALMPs. Another of the 10 recommendations related to “Reform of unemployment and related benefit systems”. The three-fold thrust behind this particular recommendation was: (a) to limit work disincentive effects; (b) reform tax/benefit systems so as to make work pay; and (c) reform benefit conditionality and financing.

However, it is noticeable, with the benefit of hindsight, that there was little or no recognition in the Jobs Study of the need to take account of potentially important interactions between these two specific recommendations³. The same criticism can be made of the early versions of the European Employment Guidelines which were first adopted by the Amsterdam Summit in 1997. They incorporated a guideline entitled “Transition from passive measures to active measures” under one of the four main pillars of the Guidelines, “Improving employability”.

A series of OECD and European Commission country reviews of the implementation of the Jobs Study recommendations and the European Employment Guidelines over the subsequent decade together with academic research has produced a major change in thinking on the appropriate definition of activation and how it should be implemented. A key theoretical paper was Coe and Snower (1997) who highlighted for the first time the potential for complementarities between policies and institutions in the fight against high and persistent unemployment. Since then there have been many empirical studies—see, for example, Bassanini and Duval (2006, 2009)—which have stressed the complementarity or trade-off between ALMPs, unemployment insurance and related welfare benefit systems, employment protection, labour taxes and the structure of collective bargaining.

Thus, by the time that the OECD came to reassess the pertinence of the original Jobs Study recommendations in the mid-2000s, it had adopted a much richer vision of activation encompassing the interactions between UI/UA systems, ALMPs and benefit conditionality and other labour market policies and institutions. This was fully articulated in OECD (2006) and taken on board in the later iterations of the European Employment Guidelines.

While there is no agreed definition of the concept, the OECD currently defines activation strategies as aiming:

“to bring more people into the effective labour force, to counteract the potentially negative effects of unemployment and related benefits on work incentives by enforcing their conditionality on active job search and participation in measures to improve employability, and to manage employment services and other labour market measures so that they effectively promote and assist the return to work”.⁴

Drawing on analytical studies and member country experiences in the 1990s and early 2000s, the OECD and the European Commission encouraged member countries to implement *effective* activation strategies for the unemployed, arguing that the evidence showed that they would help cut unemployment and boost employment. They also argued the case for extending the remit of activation

strategies, suitably modified, to other working-age recipients of a range of inactivity benefits such as disability/long-term sickness, early retirement, and sole-parent or social assistance benefits.

The adoption of effective activation strategies has been a slow and uneven process across OECD countries over the past three decades. The first country to embark on this route was the UK in the late 1980s, and it has continued to develop and refine its activation strategies under successive Conservative and Labour governments.⁵ Somewhat surprisingly given its past history, Sweden did not take the lead among Nordic countries in implementing activation. This palm should go to Norway which began implementing activation measures from the late 1980s on in response to rising concern about the growth in benefit spending⁶. Denmark, which had the most generous benefit system among the Nordics, only began to implement activation measures from the mid-1990s on.⁷ Sweden and Finland lagged behind in introducing activation.

The Clinton welfare reform in the US in 1996 also had a significant impact on the international debate on activation in that it provided an impetus to the move to extend activation to a wide range of welfare recipients of working age, especially sole parents with children. Its focus on workfare as a requirement for benefit receipt and setting time limits for the receipt of welfare benefits was copied by some other OECD countries.

In continental Europe, Switzerland put in place activation measures in the mid-1990s too, but Germany and the Netherlands only moved to do so in the early to mid-2000s. France has been slow to adopt activation and it is only in recent years that its PES has tried to put in place a fully-fledged strategy. Activation strategies have had little content in Southern European countries such as Greece, Italy and Spain. Portugal was an exception here in that it implemented activation measures in the 1990s before relaxing their implementation in the subsequent decade; more recently, it has sought to tighten activation again. Ireland, while playing lip service to activation principles since the mid-1990s, did not in fact begin to implement them until 2012, and still has a way to go on this front. The Central European countries have also been relatively slow to adopt and implement effective activation strategies. All in all, it is hard to conclude that the activation paradigm has swept the field in OECD countries to date.

The trade-offs/complementarities facing countries over activation

Benefit conditionality

One fundamental dilemma that lies at the heart of any activation strategy is how best to ensure that the unemployed and other working-age recipients of welfare benefits can be encouraged to search actively for work and/or take steps to improve their employability while at the same time their consumption of goods and leisure is being subsidised via the tax/benefit system. The unemployed and other working-age recipients of unemployment benefits and their dependents receive income support which varies greatly in terms of its generosity across countries, over time and in terms of family circumstances and past employment histories. One commonly-used summary measure of this benefit generosity is the so-called *net replacement rate*, i.e. the proportion of net income in work that is maintained after job loss. The OECD calculates regularly a wide range of net replacement rates for many different household types and under different assumptions about past employment and earnings histories. These data, published as part of the OECD's Benefits and Wages series, reveal large disparities in benefit generosity across countries and over time, but also between different families within countries⁸. In some cases, net replacement rates are of the order of 70-80% or more, while in other cases and countries they can be as low as 40-50% or less.

All other things being equal, there is a large body of cross-country evidence showing that high replacement rates lead to longer durations of unemployment spells. One obvious route to offset this moral hazard effect is to cut net replacement rates significantly. However, many countries have been unwilling to go down this route because of both equity and efficiency concerns – the latter related to

the fact that the availability of income support can enable the unemployed to search longer for a job that better matches their potential productivity. An activation strategy that *obliges* the unemployed to search actively for work and/or engage with an ALMP to enhance their employability can help offset the work disincentive effect of income support, with the obligation being backed by the threat of a benefit sanction. Nonetheless, the post-2008 period has seen cuts in benefit levels and/or shortening of the duration of benefit receipt in some European countries, e.g. Denmark, Finland, Ireland, Italy (since 2015), the Netherlands and Switzerland.

Obviously, those countries with relatively low replacement rates have less incentive to invest in activation; this is the case in some Central and Eastern European countries and Japan. But in other countries with larger replacement rates, there has not always been the same willingness to use the “threat effect” of a benefit sanction in order to maintain work incentives. The UK and some of the Nordics excluding Finland, Switzerland and the Netherlands have been at the forefront of relying upon threat effects as a way to help ensure that activation is effective. Germany moved in this direction via the Hartz reforms of 2003-2005. France and the French-speaking region of Wallonia in Belgium have been much more reluctant to embark on this route until very recently, as was Ireland.⁹ The Southern European countries have also been extremely reluctant to enforce job-search and employability conditions on the unemployed, paying at best lip-service to the concept of activation. For example, the Italian country note in De Geus *et al.* (2016) highlights that benefit conditionality was first introduced into Italian law in 2003, but was never enforced because the various actors could not agree on how it should be applied!

The eligibility criteria for receipt of unemployment benefits cover not only job-search requirements or the need to participate in ALMPs; they also include a definition of a “suitable job offer” which cannot be refused. All these criteria are subject to the threat of a benefit sanction being imposed if they are not respected. OECD has recently collected qualitative data on these eligibility criteria and used them to compute a composite indicator of the strictness of eligibility criteria for 40 OECD and EU countries for 2014.¹⁰ These data reveal significant cross-country variation in the composite indicator and its main components. However, the indicator is subject to an important caveat: it captures the rules of benefit systems, as set out in law or administrative regulations, but it sheds little light on how these rules are implemented in practice with the sole exceptions of job-search monitoring and documentation requirements which are typically not spelt out in detail in legislation. The OECD activation reviews show that implementation of the criteria varies greatly across countries and over time, and this has a significant impact on the effectiveness of national activation strategies.

Employment protection

Employment protection refers to the legal regulations and collectively-bargained provisions governing the hiring and firing of workers. For many years, the OECD has been calculating indicators of the strictness of employment protection legislation (EPL) for its member countries. Extensive empirical research shows that strict EPL has an impact on the composition of employment and unemployment, labour reallocation and productivity. EPL is also an important determinant of *labour market dualism*, i.e. the degree to which employment is split between workers on permanent contracts who benefit from strong protection against dismissal and workers on temporary contracts who enjoy much less protection.

How does EPL relate to effective activation or the lack thereof? Those countries that have less strict EPL and smaller gaps between EPL for permanent as compared with temporary workers have found it easier to implement activation strategies because, all other things equal, they tend to have more labour reallocation, therefore greater rates of job creation and destruction. For example, both the UK and Denmark, two leaders in applying activation strategies in the EU, have relatively less strict EPL than France or the Southern European countries, highlighting a potential complementarity here. However, Ireland has relatively lax EPL, but, as noted above, has not tried to implement activation effectively until very recently. Germany, on the other hand, has relatively strict EPL for permanent workers but

has been able to implement activation effectively since 2005. On balance, it seems that it is possible to implement effective activation in both strict EPL and less-strict EPL environments.

The state of the business cycle

Another potential trade-off around activation concerns the business cycle. Critics of activation often claim that it is a “fair-weather” instrument: it can work only when labour demand is buoyant, making it easy to impose benefit conditionality. When labour demand is depressed, they claim it makes little sense to activate job seekers since all it will achieve is to reshuffle the queue of the unemployed without any overall impact on the unemployment rate or the incidence of long-term unemployment..

But this negative view of activation ignores the evidence that countries which have been successful in implementing activation have weathered the recent storm of the Great Recession relatively well. Countries as diverse as Australia, Austria, Germany, Japan, Switzerland and the United Kingdom have all experienced more moderate increases in unemployment post-2008 than would have been expected on the basis of previous cyclical patterns. This suggests that effective activation strategies can help make labour markets more resilient to adverse demand shocks.

But it is one thing to argue that effective activation can work in bad times as well as good times; it is another to argue that the mix of policies underlying an effective activation strategy does not need adjusting to the state of labour demand. For example, when labour demand is depressed, should the emphasis on benefit conditionality be weakened and more resources devoted to ALMPs? This question is often posed in terms of a shift from a so-called “work-first” approach to a “train-first” approach. The rationale for such a shift in the activation mix is that the opportunity costs of investing in training for the unemployed, especially those at high risk of long-term unemployment, fall during a steep downturn as the exit rates from unemployment to a job decline. There is some limited econometric evidence from the Nordic countries that suggests it is worthwhile to shift the stance of activation policies towards greater investment in long-duration training during a steep downturn¹¹. But it is not easy to accept this argument uncritically. Investment in training tends to be more costly for the public purse than spending on other ALMPs and it is not easy to expand the supply of cost-effective training quickly in response to a cyclical downturn¹².

Nor is it always clear that a “work-first” approach is less effective in a period of high unemployment. Michaelides and Mueser (2015) provide experimental evidence from a reemployment programme which was implemented by the US state of Nevada during the Great Recession. This experiment required a random sample of new UI claimants to attend a one-to-one meeting with a caseworker in the first three weeks of their UI claim as a condition of remaining eligible for benefits. The purpose of the meeting was to determine whether the claimant was in fact eligible for benefits and actively seeking work. Claimants who either failed to attend the interview or failed the eligibility test were immediately disqualified from benefits. The results showed a significant cut in the average duration of unemployment and in public spending on benefits. Importantly, the programme increased significantly the exit rate from UI receipt to employment. In another study, Martins and Pessoa e Costa (2014) evaluated a large activation programme which was introduced in Portugal in 2012 when the unemployment rate hovered around 16%. Their results showed that, despite the depressed state of labour demand, the activation programme doubled the monthly exit rate to a job.

The bottom line on activation to date

In Martin (2015), I reviewed the cross-country macroeconomic evidence on the effectiveness of ALMPs in reducing unemployment. While acknowledging that this literature is plagued by endogeneity issues, I nonetheless concluded that the vast majority of studies pointed to public spending on ALMPs having helped to cut unemployment rates. I also reviewed the evidence from seven OECD country case studies of activation strategies¹³. Five of these countries in my view had implemented activation strategies successfully, though with very different institutions, and different balances between income

support, benefit conditionality and the public spending effort on ALMPs: Australia, Japan, Norway, Switzerland and the UK¹⁴.

I concluded that Ireland, at least until very recently, and Finland over the past decade had failed to implement their activation strategies successfully. The Irish government has recognised this failure and over the past three years has taken vigorous efforts to design and implement an effective activation strategy. While the Irish unemployment rate has dropped from its post-Great Recession peak of 15.2% in 2011 to 8.3% in July 2016 (seasonally adjusted), it is a bit early yet to conclude that the new activation strategy – called Pathways to Work – has been instrumental in this strong labour market recovery. A rigorous evaluation has just been launched to answer this important question.

The combination of fairly generous replacement rates, slow tapering of these rates over the duration of an unemployment spell, late activation of the unemployed and much less emphasis on public spending on ALMPs as opposed to UI benefits in Finland as compared with its Nordic neighbours helps explain why activation has been relatively ineffective in that country over the past decade.¹⁵ Indeed, the Finnish government has acknowledged this weakness and announced steps at the beginning of 2016 to make its activation strategy more effective; these include some cutbacks to replacement rates. However, the OECD has been pushing Finland for quite some years to make its activation strategy more effective so it remains to be seen how successful the latest reform efforts will prove to be.

Among the larger EU countries, activation still remains a bit of a dirty word in the French political debate though some steps have been taken under both the Sarkozy and Hollande presidencies to introduce key elements of an activation strategy such as more benefit conditionality and greater emphasis on case management and early intervention. But at the same time it has proved extremely difficult to reduce the high degree of labour market duality between permanent and temporary contracts in France, notwithstanding a timid reform of labour law in 2016. Thus, a large question mark hangs over activation in France. The Renzi government in Italy has taken vigorous steps to reform EPL and activation in Italy since early 2015. The difficulty here lies more in designing the institutions needed to implement an effective activation strategy and ensuring that they deliver on their objectives. Given the weaknesses in labour market institutions and policies in Italy to date, namely the decentralisation of the responsibility for the delivery of many activation measures to the regions who are ill-equipped for this task, this will be a major challenge.

The other large Southern European country, Spain, is in an even worse position than Italy with respect to activation. The regions and communities in Spain have responsibility for the delivery of ALMPs while the central government is responsible for the UI system. They have been consistently unable to coordinate their efforts to design and implement an effective activation strategy despite many statements to the contrary. I am very doubtful that this situation will improve in the short-term given the institutional and political obstacles in Spain.

Future challenges

Extending activation to recipients of other welfare benefits

Activation was originally targeted to recipients of unemployment benefits. But the target group for activation has been widened over time to encompass other working-age benefit recipients who are less closely linked to the labour force than the unemployed. Social assistance beneficiaries, especially sole parents with young children, were one of the first of such groups to be targeted for activation; the Clinton welfare reform was partly instrumental in this shift. In addition, many countries have witnessed a trend increase in in long-term sickness/disability benefit rolls among the working-age population. One factor behind this was the tightening of activation requirements on the unemployed, especially the long-term unemployed, which led many claimants to be reclassified as disabled and thereby exempt from benefit conditionality. This phenomenon of significant growth in the numbers of working-age

recipients on disability benefit rolls has been particularly marked in Australia, the Netherlands, the Nordics, the UK and more recently, the US.

In response to this worrying trend, these countries have sought to adapt and extend activation approaches to the needs of those who are less connected to the labour market. Activation, as the OECD country reviews have revealed, works best for those benefit recipients who are relatively job-ready. Activation can also be relatively successful for lone parents with young children so long as the supports provided can help deal with child-care issues and the addition of in-work benefits makes work pay. At the same time, Avram *et al.* (2016) show that, while recent attempts in the UK to impose job-search requirements on sole parents with young children helped many of them to find work, some claimants who had weak attachment to the labour market were shifted to disability benefits.

The Netherlands and the UK have managed to reduce the numbers of disability benefit recipients over the past decade, essentially by cutting down on the inflows to the benefit rolls by tightening up the gate-keeping controls including targeted activation for the unemployed with health problems before they are granted disability status. The Netherlands has also raised the cost of laying off workers with health problems by making employers bear more of the cost of disability benefits. However, the record to date shows that activation policies are less successful in helping recipients of long-term sickness/disability benefits to find work – the OECD activation reviews of Australia, Norway, Switzerland and the UK testify to this relative failure. In addition, other OECD reviews have highlighted the fact that a large share of the inflows to long-term sickness/disability benefits are accounted for by people with mental ill-health -- employers are extremely reluctant to engage with such people.

There is another political economy issue which comes to the fore when activation approaches are extended to recipients of disability benefits: is there general public support for such a move? The evidence shows that public opinion is usually favourable to activation policies targeted to the unemployed. However, there is much less public support for extending benefit conditionality and activation approaches to people with health problems. The disabled, in particular, have very active lobby groups in all countries and these lobbies are very reticent about activation. The UK provides a very clear example of such reticence. Since 2008, the attempt to activate disability benefit recipients has been a continual source of public concern, often focalising around the use (or abuse as the lobbies tend to argue) of the work-capability assessment in order to shift people off disability benefit and on to unemployment benefit. Several attempts have been made to refine the work-capability assessment tool to remedy deficiencies but assessments are often challenged and overturned on appeal. Nor is this problem of lack of public support for activating people with health problems confined to the UK, such reticence also exists in other countries too, e.g. Australia, the Netherlands, Norway and Switzerland. Given the large numbers of working-age people on such benefits and the relatively low exit rates from such benefits to work, it has to be a very high priority to determine how activation strategies can be made more effective for people with health-related issues who have some work capacity and who want to work. What mix of rehabilitation, benefit conditionality and workplace supports could work better for such people than the current one? How can one achieve the necessary coordination between the health care sector, the PES and private employment service providers, rehabilitation services and employers so as to boost the employment and career prospects for the disabled with some work capacity? How can the authorities convince the public that it is legitimate to apply activation to people with health problems? There are no easy answers to these questions. But given the scale of the challenge, it will be vital for countries to invest more in redesigning activation strategies which work for those with health-related issues and convincing the public that it is reasonable to encourage many of these people to seek work.

Supporting career progression

A common criticism of activation strategies is that, while they do assist people to move off benefits and into work, they do not help them to progress up the career ladder. There is much evaluation evidence showing that many benefit recipients are activated to take low-wage jobs which do not offer great career prospects and which may not lift them and their families permanently out of poverty. The poverty trap can be exacerbated by in-work benefits such as the EITC in the US which can impose high marginal effective tax rates (METRs) which discourage recipients from working longer and investing in training to raise their skills. So the aim of an effective activation regime should be not only to get people off benefits and into work, but also to help them access “quality” jobs.

This is much easier said than done. The traditional response has been to invest in further education and training schemes for the unemployed. The problem is that these schemes tend to be more costly than other ALMPs and the evaluation evidence on their effectiveness has been mixed. Most evaluations show negative returns to training programmes in the short-run. However, the few evaluations which track the outcomes of training programmes over longer periods up to a decade tend to show more positive outcomes for participants and the public purse.¹⁶

Given the concerns that training investments might not pay off, another tack has been for the PES to offer continued support to clients even after they have exited benefits into a job with the aim of ensuring that they can stay in the job and enjoy some career progression. Such employment retention and advancement programmes deliver in-work services such as counselling or help with training, usually combined with financial incentives. This approach sounds quite promising but there are at least two major difficulties with it. First, only two OECD countries (the UK and the US) have experimented with such schemes so there is a real dearth of international evidence with which to assess the effectiveness of such schemes against their stated objectives. Second, the evaluations of the existing US and UK schemes suggest that most of them did not work.¹⁷ However, it may be better to have a more limited objective for the PES: it should aim to assist clients to find full-time work rather than part-time, and leave career progression to investments in training and upskilling by workers and their employers.

A related issue arises when income from work is combined with partial receipt of unemployment benefits or in-work benefits. As noted above, this can give rise to high METRs serving to lock people, often second earners in a household, into low-paid and/or part-time jobs. This raises the difficult question of how to apply “in-work” benefit conditionality to such workers with the aim of shifting them from a part-time to a full-time job. It is not obvious how to design and implement an effective system of “in-work” conditionality. The UK is currently grappling with this challenge as part of its introduction of Universal Credit.¹⁸

A third route to promote career progression is to reward private providers of reemployment services who place their clients into sustainable jobs by paying outcome fees linked directly to the durability of the job and the degree of earnings progression. But there is very little rigorous evaluation evidence on whether such financial incentives to private providers work or not.

Given the concern that activation often pushes people off benefits into low-productivity jobs with little or no career progression potential, more rigorous evaluations are needed to establish what education and training investments can pay off for which client groups and over what time horizon. In addition, more experimentation is needed to see if revamped employment retention and advancement programmes can be developed which pay off in terms of career progression and/or private providers can be incentivised to produce such outcomes for their clients in a cost-effective manner.

Contracting with private providers of reemployment services

One notable trend over the past decade or more has been the growing role assigned to private providers of reemployment services, both for-profit and non-profit, operating alongside the PES or in some cases

taking over what was traditionally a PES monopoly. Indeed, Australia took the drastic step almost 20 years ago of abolishing its PES and replacing it with full outsourcing of employment services to private providers who service a wide range of jobseekers under pay-for-performance contracts drawn up by the Employment Department. While no other OECD country has followed the Australian route of abolishing the PES, several have assigned major roles to private providers to assist the long-term unemployed or other at-risk groups, e.g. the Netherlands, UK and Ireland, while many others have subcontracted private providers to supplement the efforts of the PES.

Since this trend towards expanding the role of private providers seems likely to persist, there are questions as to the optimal design and monitoring of contracts in order to secure the desired outcomes for the clients at an acceptable cost to the public purse. Different countries have opted for different solutions on this front and it is unclear yet what common lessons can be drawn. The Australian example, which is now in its fifth contract round, shows that it is important to learn from each contract round and to vary the terms of the succeeding contracts in ways that will improve outcomes. In particular, the Australian example shows how important it is to develop indicators to rank the performance of the private providers. Its Star Rating system is used to drive poor performers out of the market in the next contract round or to reduce the size of their client flow while expanding the market share of above-average performers¹⁹. This issue has proved to be an Achilles Heel for the UK Work Programme. When the private providers in particular regions failed to meet the minimum targets in their contracts, the targets were revised downwards so as to keep them in business.

Another important issue associated with creating a quasi-market in employment services concerns the optimal design of the remuneration system for the private providers. How can one minimise so-called “parking of the hardest-to-place” clients by the private providers and how can one motivate them to achieve good placements into sustainable jobs for the most disadvantaged clients? Here, we note a significant difference in the approaches followed in Australia and the UK. In the former case, two thirds of the money is tied up in service fees and the Employment Pathway Account (a fund which is earmarked for the purchase of specific employment services for the jobseeker) while only one third is tied directly to job outcomes. The UK Work Programme began with small initial service fees which were later abolished so that provider income currently depends solely on job outcomes and sustainability in work fees. The Irish JobPath model of contracting for the long-term unemployed falls somewhere in-between the Australian and UK models in terms of remunerating the private providers for outcomes. It is unclear which of these two provider payment models is optimal and under what conditions.

The potential of e-services

The final challenge concerns the potential role of e-services in the market for employment services: will they prove to be a help or a hindrance for effective activation? The internet has great potential to impact the recruitment market since the cost of job search and recruiting workers online is very low compared with the traditional recruitment channels including the PES. . At the same time, the PES, like most public agencies, is under pressure to cut its costs and deliver its services more effectively. One possible avenue for such cost-saving is via greater reliance on e-services to help place more of its clients into jobs.. This is not just a theoretical possibility. Currently, 90% of unemployment benefit recipients in the Netherlands are being treated via e-services and only 10% of clients – those profiled as being at the highest risk of long-term unemployment – are receiving face-to-face treatment. The Finnish PES also intends to move in a similar direction in order to cut costs and target its resources more to the most disadvantaged job seekers. Private employment service providers have a strong incentive to rely more heavily on e-services as a way of cutting costs and boosting their profits.

We do not know how effective such e-services are nor which clients they might work for best, if they work at all. Until recently, Kuhn (2014) highlights that there was little empirical evidence that the internet was having a significant effect on job search or recruitment outcomes. However, more recent US studies suggest that the picture is changing and workers and firms are beginning to find ways of using the internet more effectively to make job matches. But these studies relate only to the United

States and they do not focus specifically on how the internet and social networking sites have impacted on the core business of the PES.

There is also the concern that recent rigorous evaluations from Denmark and Switzerland show that PES case workers and the approaches they use to activate their clients matter for the return to work²⁰. This suggests that personalised counselling and monitoring of job-search and employability actions are important building blocks of effective activation which require face-to-face contacts with clients and which cannot be substituted for by e-services. However, digitisation is proceeding at a very rapid pace and it can facilitate face-to-face contacts remotely between case workers and their clients (e.g. via Skype). So the jury is out on whether on-line services can be a substitute or a complement to personal interactions between case workers and their clients.

Client satisfaction surveys in the Netherlands showed significant dissatisfaction with the new digital services and the Dutch are currently evaluating whether it would be more effective to increase the reliance on direct contact with case workers in order to speed up the return to work.

Since the impact of digitisation on the job market is likely to increase still further, and the PES in many countries is seeking to explore ways in which e-services can contain their costs and assist the activation approach, this is an area where more innovations will appear in the future and it will be vital to evaluate them rigorously in order to establish which e-services work and for what groups.

Concluding remarks

The concept of activating benefit recipients into work has become an important building block in OECD and EU countries' strategies to fight high unemployment. The concept has evolved over time in the light of both theoretical understanding of the interactions between benefit systems, labour market institutions and active labour market policies and detailed reviews of different countries' experiences. Activation regimes differ greatly in their scope and intensity across EU and OECD countries, reflecting their different starting points, histories, institutional settings and cultures. They all involve different combinations of eligibility criteria for benefit receipt including job-search monitoring, benefit conditionality and referral to ALMPs.

The evidence suggests that effective activation regimes work in the sense of assisting the unemployed to get off benefits and into work; the evidence also suggests that activation has been less successful in terms of promoting career progression in work. The mix of policies which determines whether the activation strategy is effective or not varies across countries. But the evidence also shows that some countries have played lip service to activation principles or failed to implement them effectively; in these cases the outcomes were disappointing. There is also evidence that it is not easy to maintain an effective activation regime over time: governments change and may be less committed to activation than their predecessors or relax the regime inappropriately when the labour market is buoyant. There is also the fact that activation regimes have proved to be most effective for UI benefit recipients and also for recipients of sole-parent benefits when assistance is provided for child care. However, the record of activating recipients of disability benefits into work is much less successful in all countries that have tried to go down this route.

Activation strategies have to adapt to existing and upcoming challenges if they are to continue to be worthwhile public investments. This paper has highlighted four such challenges. Innovative responses and rigorous evaluations will be required to enable countries to surmount these challenges.

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Endnotes

¹ The huge jump in long-term unemployment in the United States undoubtedly reflects the very large extensions to UI benefits agreed in the aftermath of the Great Recession. Since the extensions were abolished at the end of 2013, the incidence of long-term unemployment has fallen back significantly.

² Data are not seasonally adjusted but are smoothed using a three-quarter moving average.

³ For the record, it should be noted that David Grubb, in a private correspondence with me, disagrees on this interpretation of the 1994 Jobs Study. He argues that OECD (1994, Chapter 8) devoted a lot of attention to benefit conditionality in its discussion of the impact of benefit systems on the labour market. While I agree with him on this, it is my contention that it took almost a decade for this analysis, backed up by detailed country studies and academic research, to have a significant impact on OECD policy recommendations when the Jobs Study was reassessed in 2006.

⁴ OECD (2013a, p.132). It is worth noting that Weishaupt (2011, p. 33) adopts a somewhat different definition of an activation paradigm which he states: “rests on three pillars: (a) activating labour market policies, including *early interventions*, *case management*, and *conditional benefits*; (b) a modern, customer and results-oriented PES, governed in a *managerial style*; and (c) a more inclusive, employment-promoting welfare state, that mobilises also women, older workers, and otherwise “inactive” persons (emphasis in the original). His second pillar, a modern PES, is omitted from the OECD definition in recognition of the fact that some OECD countries have greatly expanded the role of private, for-profit or not-for-profit, employment service providers in the market for reemployment services, operating normally alongside the PES. One OECD country, Australia, even abolished its PES in the mid-1990s and now only relies on private providers operating under performance-related contracts. For details, see Martin (2015). Nonetheless, OECD (2015, Chapter 3) assigns a prominent role to the PES as a key actor in activation in most OECD countries.

⁵ For details, see the country note in De Geus *et al.* (2016).

⁶ See Johansson and Hvinden (2008) for details.

⁷ See the country note on Denmark in De Geus *et al.* (2016).

⁸ For details on the OECD tax-benefit models, see www.oecd.org/social/benefits-and-wages.htm

⁹ In Belgium, the province of Flanders has been much more pro-active than Wallonia in enforcing obligations on jobseekers.

¹⁰ For details, see Langenbucher (2015).

¹¹ See Forslund *et al.* (2011) and Norlund (2009).

¹² There is also the non-negligible hurdle to overcome that many countries lack adequate performance management systems to benchmark the quality of training provided to the unemployed by either public or private training providers.

¹³ See Duell *et al.* (2009a, 2009b) for the reports on Finland and Norway; Duell *et al.* (2010a, 2010b) for the reports on Switzerland and Japan; Grubb *et al.* (2009) for the report on Ireland ; OECD (2012) for the report on Australia ; and OECD (2014) for the UK report.

¹⁴ As an aside, it is noteworthy that the UK tightened the strictness of eligibility criteria for benefit receipt between 2011 and 2014. Among these changes, the sanctions regime was made tougher – see Langenbucher (2015). The UK unemployment rate peaked in mid-2011 and has declined steadily since then. At the same time, OECD (2014) notes that the UK expanded significantly the frontline staff in its PES to cope with the post-2008 hike in unemployment. These changes to the activation regime may have contributed to the sharp fall in unemployment over the past five years.

¹⁵ See OECD (2016a, Figure 14) for evidence to this effect. OECD (2016b, Statistical Annex Table Q) shows that in 2014 the ratios of ALMP spending to spending on UI (both expressed as a per cent of GDP) were: 0.59 (Finland); 1.35 (Denmark, Norway); and 1.24 (Sweden).

¹⁶ For a review of the evaluation evidence, see OECD (2015, Box 3.7).

¹⁷ See OECD (2015, Chapter 3, Box 3.6) for a review of the US evaluations. Hendra *et al.* (2015) provide a detailed review of the experimental evaluation of the UK’s Employment Retention and Advancement programme.

¹⁸ See OECD (2014) for a discussion of in-work benefit conditionality and the METR in the context of the introduction of Universal Credit.

¹⁹ The use of Star Ratings as a means of raising the average performance of the private providers marks a sharp contrast between the Australian and Dutch experiences with activation relying upon private providers. The latter devolved responsibility for the provision of most activation services to the most at-risk groups to the municipalities to subcontract with private providers. But no nationwide system to benchmark provider performance was put in place alongside this shift in delivery of the services. This is one important explanation why the Dutch experience with subcontracting private providers of employment services has been much less successful than the Australian experience.

²⁰ See Behncke *et al.* (2008, 2010) for the Swiss evidence; see Van den Berg *et al.* (2012) for the Danish evidence.