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**The labour market policy in the EU**

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# The labour market policy in the EU<sup>1</sup>

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## Abstract

**Research background:** In the era of demographic changes and need for rationalization of public expenditure, the European Union social policy promotes the activation approach. In addition, there can be noticed a growing importance of increasing the efficiency of public policies.

**Purpose of the article:** The authors are presenting the main theoretical assumptions concerning efficiency as well as classification of methods for measuring of efficiency of labour market policies. Moreover, the EU countries are classified in clusters according to their level of expenditure on different categories of LMP.

**Methodology/methods:** The paper is based on critical analysis of literature as well as analysis of secondary research findings. The cross-country labour market situation in the EU is based on the analysis of the Eurostat data by the k-means method.

**Findings & Value added:** There is a need to work out a complex evaluation of labour market policies in the EU to provide comparative analysis of the EU countries (or groups of countries). It would allow determining the level of development of the country in terms of the efficiency of labour market policies.

The EU countries with the best labour market situation represent diverse levels of LMP expenditure.

**JEL Classification:** J01; J08; J11; J24; J88

**Keywords:** *labour market policy, efficiency, LMP expenditure, clusters of the European Union countries*

## Introduction

The European population is continually subject to aging. In such a demographic situation, maintaining European welfare systems, pension

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schemes and public healthcare is increasingly difficult, while the overall demand for such services is likely to increase. As such, policymakers are concerned about how to ensure long-term sustainability of public finances in the face of a declining share of economically active people (Kumpikaite-Valiuniene, Rollnik-Sadowska, Glinska, 2016). Finding reasonable policy toward for extending efficiency of labour market policy can be treated as the priority of European cohesion orientation. The increasing of efficiency of labour market policy is one of the main objectives of economic policy as it influences the rationalization of usage of public expenditures as well as the improvement of employability of human resources (Marklund, Rollnik-Sadowska 2016).

The purpose of the article is to present the diversification of the EU labour market policy in the context of both theoretical assumptions as well as an analysis of LMP expenditure.

The structure of the paper is as follows: the authors start with an explanation of conducted research method - k-means method.

Subsequently, the theoretical background of labour market policies (LMP) is presented. The second section primarily defines the LMP efficiency and provides classification of measuring methods applied in the European Union.

The final section contains an analysis of the public expenditure on different categories of LMP in the EU. This analysis proves significant diversification among European countries as to the scope of implementation of labour market policy.

## **Research Methods**

The paper was based on critical analysis of literature as well as an analysis of secondary research findings. Moreover, the labour market situation through the EU was based on the analysis of the Eurostat data.

The EU countries were grouped in clusters following k-means method taking into consideration the level of public expenditure on LMP as a share of GDP (regarding 9 categories of LMP). There were selected two years of analysis - 2004 and 2014 to verify if the EU countries made the changes in terms of LMP priorities during that period. In 2004 ten new members entered the EU and 2014 is the year of the most current data in the analyzed area.

Selected method is useful in data presentation for groups of countries with diversified situation like the EU members (Rollnik-Sadowska 2016, pp. 84 - 87).

The K-means method classifies a given data set through a certain number of clusters (assume k clusters) fixed a priori. The main idea is to define k

centroids, one for each cluster (MacQueen, 1967, pp. 281-297). It is the most useful for forming a small number of clusters from a large number of observations. It requires variables that are continuous with no outliers. In the below analysis there were selected the following 3 variables - figure 3 and figure 5 (v1 - public expenditure on LMP services (category 1), v2 - public expenditure on LMP measures (categories 2-7), v3 - public expenditure on LMP supports (categories 8-9)).

### **The efficiency of labour market policy - theoretical approach**

Labour market policy is a subject of public interventions. State allocating public resources for preventing unemployment on the labour market creates supply of public goods, which should be managed efficient and effective. In this context, arises a question about the conceptual scope of the notions of "*efficiency*" and "*effectiveness*".

The overall performance consists of the measurement of efficiency and effectiveness as the degree to which a system achieves programmes and policy goals in terms of outcomes, accessibility, quality and appropriateness (Worthington and Dollery, 2000, pp. 23-52).

In public sector, effectiveness relates the input or the output to the final objectives to be achieved, i.e. the outcome. The outcome is linked to welfare or growth objectives and may be influenced by multiple factors (including outputs and exogenous 'environment' factors). The effectiveness is more difficult to assess than efficiency, since the outcome is influenced by political choice. The distinction between output and outcome is often blurred and output and outcome are used in an interchangeable manner (Afonso, Schuknecht, Tanzi, 2009, p.23).

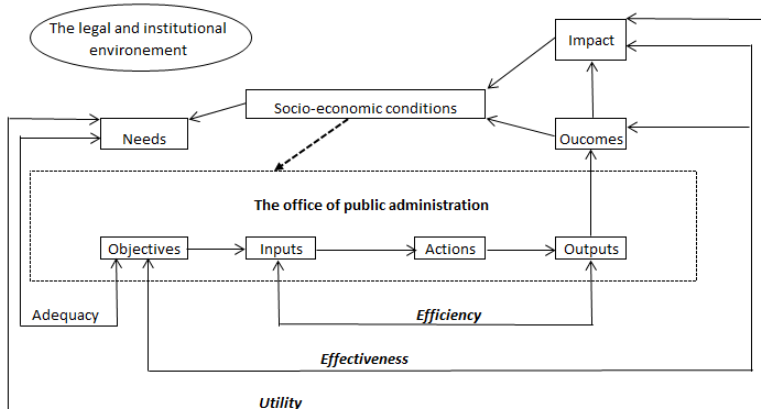
A more precise definition uses the concept of Pareto efficiency. Most economists accept this criterion, according to which the economy produces effectively, when it proves impossible to improve the economic well-being of the individual without worsening the situation of another entity (Stiglitz, 2000, p. 122).

For business organizations the main goal is gaining a profit. The organizations of public sector are non-profit units. This is why it is difficult to use business methods for measurement of its performance. The problem arises because public spending have many objectives and outputs as they often are not sold on the market, causing that prices are not available, and the product cannot be quantified (Balabonienie, Večerskiene, 2015, 314-320).

There can be considered different dimensions of effects of public policy, regardless of the possibility of being by them the subject of a market trans-

action. In the literature utility is emphasized as an important criterion for economic evaluation and economic choice.

**Figure 1.** The relationship between efficiency, effectiveness and utility in the unit of public administration



Source: Pollitt Ch., Bouckaert G. (1999), *Public Management Reform. A Comparative Analysis*, Oxford University Press, UK, p.13.

The above diagram explains the relationship between the "effectiveness", "efficiency" and "utility". Analysis of effectiveness associates expenditures with the results. Evaluation of efficiency obliges to comparing objectives and results. Utility analysis should answer the question of meeting the social needs. The inference should include outside factors and analysis of consumption expenditure by authorities.

Reflections on the efficiency and effectiveness of labour market policy (LMP) require interpretation of this concept. LMP uses instruments aimed at adapting the structure of labour supply to the demand for jobs, focuses on solving short-term and medium-term structural, conjunctural and social problems of the labour market. The statistics of Eurostat distinguished the following groups of labor market instruments: services, measures and supports (Eurostat, 2013, p.13)<sup>6</sup>.

Experience in the implementation of LMP demonstrated higher effectiveness of active policy in comparison with passive. Pissarides (1985) finds that employment subsidies reduce unemployment while unemploy-

<sup>6</sup> Until 2013, the Eurostat methodology distinguished 9 groups of instruments divided onto active and passive support. Services and measures were included to active labor market policies (ALMP).

ment benefits and wage taxes raise it. Many other researchers demonstrate positive effects active labour market programmes, these include Calmfors (Calmfors, 1994), Martin (Martin et al., 2001) Calmfors (Calmfors et al., 2002), Layard (Layard, 2004), Woźniak (Wozniak, 2016). Esping-Andersen notes that the longer the tradition of implementation of ALMP, the higher the level of their effectiveness, and of understanding and social acceptance for this type of action (Esping-Andersen et al., 2001). The foundation of effective implementing LMP is the simultaneous occurrence of certain determinants of the effectiveness. Empirical literature indicates for example, that even moderate benefit sanctions increase the job-finding rates of the unemployed (Cahuc and Zylberberg, 2004; Sengul, 2017). Sanctions also increase the exit rate from unemployment to ALMP for flat-rate labour market support (LMS) recipients (Busk, 2016). However, the circle of conditions is much wider and belong to it such factors as: reducing the threshold level of wage, accepted by the people unemployed, so that they were willing to take lower-paying jobs in relation to their original expectations (Meager, Evans, 1998, pp. 1-102), creation of new workplaces (Calmfors et al., 2002), etc.

The high costs of implementing the instruments of LMP, formulate expectations for evaluation of active forms of counteracting unemployment. Governments pay more attention to the defined results of LMP. However, their assessment in the EU countries, is rather not a subject of systematic evaluation but only the process of monitoring.

The most commonly used is evaluation of net effects at the microeconomic level, assessment of the effectiveness of the entity benefiting from support (Schmid et al. 1996). Estimation the net effect requires to compare economic values obtained in the situation of the unemployed participated in the program, with the actual values of the analogical situation generated in the opposite case, if the unemployed do not take a part in the program. Such counterfactual situation constitutes an appropriate reference plane for the evaluated programme. Evaluation based on counterfactual states is developed on the basis of statistics and econometrics. Statistics approach is represented by works of Rubin (Rubin, 1974, pp. 688-701). Econometric trend has been developed on the basis of Heckman's research (Heckman, Robb, 1985, 239-267).

### **Clustering of the EU countries concerning with LMP expenditure**

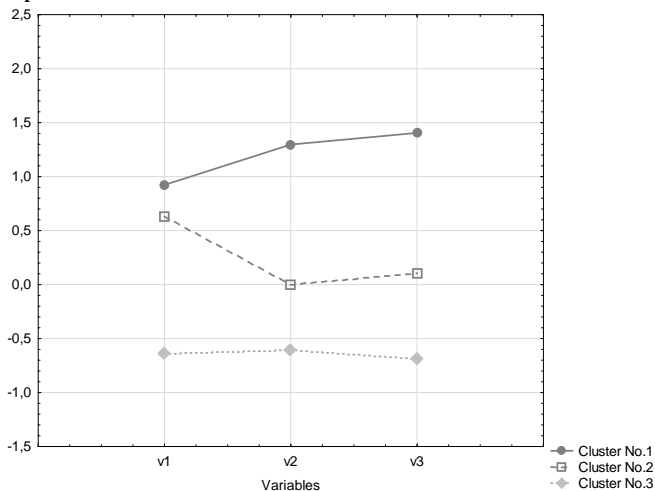
The situation in the EU countries varies in terms of the scope of implementation of labour market policy, which reflects the level of expenditure on different categories of LMP.

The EU countries were grouped into clusters following k-means method. In 2004 the EU countries were grouped into three clusters - figure 2. K - means method allows for profiling the clusters in terms of selected variables. In 2004, the countries grouped in cluster 1 (Belgium, Germany, Finland, France, Sweden, the Netherlands and Denmark) represented the highest public expenditure on LMP (taking into account all categories) measured as the percentage of GDP (figure 2). Those countries are characterized by different labour market models - Scandinavian model in Nordic countries and the Netherlands and corporate one in Germany (Rollnik-Sadowska 2015, pp. 38-51). The year 2004 represented the period of economic stability and those countries disposed financial resources for realisation generous welfare state including LMP.

The countries selected in the second cluster - Ireland, Austria, Spain, Portugal, United Kingdom, represented the average level of LMP expenditure. However, in comparison to the cluster 1 there was only a slight difference of public expenditure on LMP services. That cluster groups western European countries, mainly with liberal social policy model - like Ireland and UK, as well as Mediterranean model countries - Spain and Portugal with low level of rationalisation of social spending.

In 2004 Bulgaria, Czech Republic, Estonia, Greece, Italy, Cyprus, Latvia, Lithuania, Luxembourg, Hungary, Malta, Poland, Romania, Slovenia, Slovakia represented the lowest public expenditure on LMP out of the EU countries.

**Figure 2.** K-means Clustering of the European Union countries according to public expenditure on LMP in 2004





Source: Eurostat data (2017).

In 2014, after the influence of the crisis effects on the labour market the list of countries included in the selected three clusters has been changed (figure 3).

The representatives of the first cluster selected by the k-means method - Denmark, Germany, France, Sweden still demonstrated the highest public expenditure on LMP services and active measures but substantially decreased the spending on passive support, which occurred even lower than in the second cluster. Simultaneously, the first cluster's countries increased the expenditure on LMP services.

The representatives of the second cluster (Belgium, Ireland, Spain, Italy, the Netherlands, Austria, Portugal, Finland) extended the share of all categories of LMP expenditure. However the most significant increase was in terms of passive support (like out-of-work income maintenance and early retirement benefits).

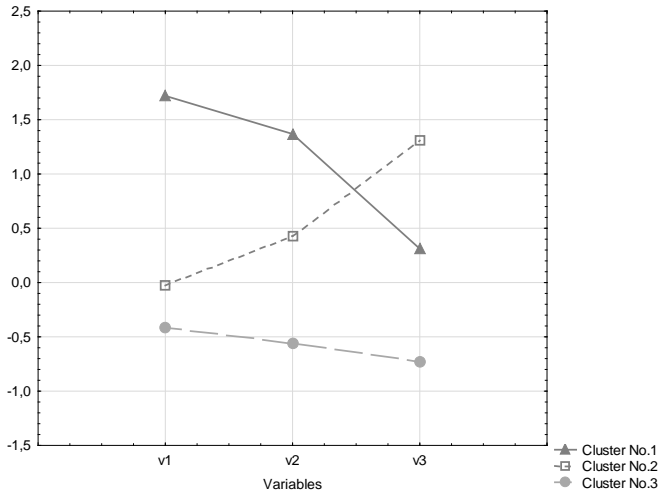
The countries gathered in the third cluster (Bulgaria, Czech Republic, Estonia, Croatia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Romania, Slovenia, Slovakia, Greece, Luxembourg, United Kingdom) maintained relatively the lowest level of all categories of expenditure on LMP in comparison with two other clusters.

It is crucial that in 2014, there is seen wider representation of western countries in the third cluster. Luxembourg in the both analysed years belonged to the third cluster. That country with the highest GDP per capita in PPS in the EU<sup>7</sup>, represents the labour demand surplus, so there is no significant need for public expenditure on LMP and labour supply support. Low expenditure level in Greece on the one hand, it is surprising in light of the difficult situation of Greeks on the labor market and the need of support of the substantial group of the unemployed. On the other hand, it may result from the deficit of budget revenue. In 2014, the third cluster was also joined by the United Kingdom, the country that continuing liberal reforms, has decreased the level of public expenditures, including those on labour market policies (Rollnik-Sadowska, 2013, pp. 80-84).

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<sup>7</sup> In 2015, GDP per capita in PPS in Luxembourg obtained 264 with respect to EU28 = 100 (Eurostat, 2017).

**Figure 3.** K-means Clustering of the European Union countries according to public expenditure on LMP in 2014



Source: Eurostat data (2017).

It has to be mentioned that public expenditure on LMP services is the only category which represents a significant correlation coefficient with employment rate (both in 2004 and 2014). The expenditure on 2-9 categories has occurred not significant in both analyzed years. It can encourage the discussion if the active measures and passive support influence the labour market situation?

### Conclusions

The monitoring of LMP in the EU covers mainly the measurement of effectiveness of ALMP. The European Union has not yet worked out a common evaluation system of LMP efficiency.

The EU LMP data includes statistics on LMP expenditure and participants. Participant data for stocks, entrants, exits and destination of exits are collected. However, there is not yet a standardized publication providing information on destination of exits. The reason is that the data is still incomplete for some countries and there are differences in the observations used.

It occurs that the countries with the best labour market indicators - the highest employment and the lowest unemployment rates (like Germany, Denmark, Estonia, Czech Republic, Luxembourg, the Netherlands, Austria, Sweden, United Kingdom) have been grouped in different clusters with diverse level of LMP expenditure. It encourages the need for future re-

search of determinants of labour market situation in the EU and positioning the role of LMP.

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