What employment policy during a crisis?

By Marion Cochard

After a lull of only a year, unemployment figures started to rise again in April 2011. We are seeing a replay of the dynamics of the 2008 recession: a hiring freeze and the non-renewal of temporary and fixed-term ("CDD") contracts, with redundancies to follow later in the year. The reason, of course, is the current economic downturn, which is hitting while French business margins are still in bad shape after the shock of 2008-2009, particularly in industry. The weakened companies no longer have the strength to cushion the fall as they did four years ago. The French economy is thus expected to slide into recession in the fourth quarter of 2011, and we foresee a fall in activity of 0.2% in 2012. Given that annual growth of 1.1% is needed to kick-off job creation, the resumption of job losses seems inevitable. If we add the existence of a growing workforce to this bleak picture, the number of unemployed will surpass the 3 million threshold by year end.

On the eve of a tense social summit, what are the options for cushioning the impact of the crisis on the labor market? Given the urgency of the situation, the government has two main levers that are responsive and inexpensive: partial unemployment and subsidized jobs in the non-profit sector.

Partial unemployment can cushion the economic hardships faced by business and retain skills in the companies. There is substantial room to expand its use. By way of comparison, in 2009 maximum compensation for partial unemployment was extended to 24 months in Germany, versus 12 months in France. In addition, the greater level of state coverage in Germany partly explains how extensively it is taken up there: partial unemployment affected 1.5 million people at the peak of the crisis, but only 266,000 in France. Nor does this put much of a burden on public finances, as the 610 million euros disbursed by the States on partial unemployment in 2009 were offset by savings on unemployment benefits and the preservation of human capital.

But partial unemployment benefits workers in stable industrial jobs above all, while the brunt of the crisis is being borne by those in precarious employment and young people. These are the sections of the population targeted by subsidized employment. Again, the government has some leeway, because 70,000 subsidized non-profit contracts were eliminated since end 2010 and 300,000 since the early 2000s, and it is also not a very expensive scheme. The creation of 200,000 jobs would for instance cost the state 1 billion euros – contrast this with the shortfall of 4.5 billion euros due to the tax exemption of overtime, which, furthermore, is inconsistent with the logic of partial unemployment. These programs are targeted at those among the unemployed who are most isolated from the labor market – the long-term unemployed and unskilled – and would lower their risk of dropping out of the labor market.

However, even though these tools should be used immediately, they are still just stop-gaps. Partial unemployment remains confined to 80% of industry and designed for short-term use. If today's dire economic situation continues, we know that this approach will only delay layoffs. Similarly, subsidized jobs are not intended to be long-term. These are low-paid part-time jobs intended to deal with reintegration into the labor market, and not a long-term approach.

The biggest challenge is really a correct diagnosis of the current economic situation. By focusing negotiations on the issue of partial unemployment and subsidized jobs, the government seems to be betting on a quick recovery. Yet it is precisely the combined effect of austerity plans throughout

Europe that will weigh on growth in the years to come. Furthermore, the policy of reducing public deficits, which will cost 1.4 percentage point of growth in France in 2012, is expected to continue at least into 2013. It is difficult in these circumstances to expect to pull out of the stagnant situation quickly enough to avoid the looming social catastrophe. Unless there are plans for a new permanent reduction in working hours and the creation of public sector jobs, the best employment policy remains growth. It is thus the issue of macro-economic governance that is posed above all today in France and throughout the euro zone.

Should tax breaks on overtime be reversed?

By Eric Heyer

Among the savings plans announced on 24 August 2011 by French Prime Minister François Fillon figures a change to the system of tax reductions on overtime hours and their exemption from social contributions,[1] a scheme that has been in force in France since 1 October 2007. This provides an opportunity to take another look at some of the main conclusions of the work carried out by the OFCE (French version) on this subject.

1 – An article to be published soon in the *Oxford Review of Economic Policy*[2] explains how the impact of this scheme will differ depending on the position of the economy in the cycle at the time the measure is applied.

- In a favourable economic climate, an increase in working hours prompted by lower labour costs and the elimination of payroll taxes would seem appropriate. The measure is of course not funded (the public deficit deteriorates), and financing it through higher levies would radically change its nature, even though this would not call into question its positive impact on employment and unemployment.
- However, this measure is poorly suited to the kind of economic downturn that the French economy is going through today. In a situation of mass unemployment, an increase of 1% in working hours has a negative impact on employment (-58,000 jobs at 5 years and -87,000 at 10 years). The unemployment rate would increase slightly (0.2 point at 5 years, 0.3 point at 10 years). The measure would have a small impact on growth (0.2 point at 5 years and 0.3 point at 10 years) and is not funded: the deficit would deteriorate by 0.5 point at 5 years (0.4 point at 10 years).

2 – This corroborates the results of a recent study published in *Economie et Statistique*[3]. The authors examined data on 35 sectors of the French economy and estimated that a 1% increase in overtime would destroy about 6,500 jobs in the commercial sector (*i.e.*, 0.04% of commercial jobs), three-quarters of which would be temporary jobs.

Thus, in a context of a severe economic crisis, it seems that an incentive to work longer hours would hurt employment, especially temporary employment.

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[1] The government decided to reintegrate overtime hours into the general schedule of tax reductions while maintaining specific advantages on taxes and social welfare charges. Concretely, this measure will not change anything for employees: net remuneration will not be reduced, and income

tax will not be increased. As for employers, they will continue to benefit from exemptions on charges for declared overtime hours, but will see smaller breaks on charges on low wages. This will take effect next January 1st and, according to the government, will generate 600 million euros in revenue from additional social contributions.

[2] Heyer É. (2011), "The effectiveness of economic policy and position in the cycle: The case of tax reductions on overtime in France", *Oxford Review of Economic Policy*, forthcoming.

[3] Cochard M., G. Cornilleau and É. Heyer (2011): "Les marchés du travail dans la crise", *Economie et Statistiques*, no. 438-440, June.