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Employment Regulation and French Unemployment: Were the French Students Right After All?

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After weeks of massive demonstrations, the French government has backed down in the face of protests led by French students over changes in national labor law. The proposed changes would have allowed employers to fire workers under age 26 without reason, notice, or severance. The hope was that by making it easier to dismiss workers, employers would hire more workers and youth unemployment would fall.

Of course, these conditions, known as "employment at will," are standard for workers of all ages in the United States. Perhaps because we take these employment conditions for granted in the United States, the response in the U.S. media has been scathing. The New York Times Editorial Board has pronounced, for example, that French youth unemployment is "catastrophic" and that the "real threat" of the demonstrations is that the French government "may be dissuaded from attempting the broader social and economic reforms that France requires, both for its own future and for the future of the European Union."

A media consensus has emerged that French youth are stupendously misguided - they have no idea what their own interests are; they have an outdated, childlike dependence on the state for protection from the real world of market forces; and they are often simply lazy and prefer the dole to work. As for French unions, U.S. critics charge that they are merely being opportunistic - trying desperately to stem their descent into irrelevance.

On closer examination, though, maybe there is something to the popular opposition. Large majorities of France opposed the change. Can such a large, highly educated population be so wrong? We suggest that there are three main reasons for American media pundits - and professional economists - to think twice before pronouncing on the ignorance, dependence, laziness, and opportunism of French workers.

The *first* is that the French public probably has a much better grasp of the extent of the youth unemployment problem than is captured in official unemployment statistics. Because large shares of youth are enrolled in school and not employed, the unemployment-to-population measure is a better measure of the magnitude of the unemployment problem than the standard unemployment-to-labor force measure. *Second*, for youth, a larger employment rate should not be the sole criterion of a well-functioning labor market and social system, especially for 16-19 year olds. And *third*, the available economic evidence on the effects of employment protection regulations combined with the available of temporary (fixed contract) jobs for youth, strongly suggests that the proposed change would have little or no effect on either employment opportunities or the unemployment rate for youth. We address each of these points in turn.

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1. How Catastrophic is French Youth Unemployment?

There is no doubt that the official youth unemployment rate in France is very high. At 22 percent, it was substantially above the U.S. rate of 11 percent (and even further above the U.K. rate of 9.9 percent and the Dutch rate of 8.1 percent).¹ But this “catastrophic” French rate reflects the technical definition of unemployment, which is more appropriate for prime-age workers than it is for youth.

The official unemployment rate measures the unemployed (those willing and able to work and currently searching for a job) as a share of the labor force -- the unemployed and the employed. This definition means that, in two countries with the same number of youth and the same number of unemployed youth, the unemployment rate can be hugely different, depending on how many of the young people are employed.² On this score, the difference between the U.S. and France is huge: Row 3 of the table shows that in 2004 only 32.8 percent of French male 15-24 year olds were employed (at least one hour in the survey reference week), compared to 61.9 percent of young U.S. men.

Key Labor Market Indicators for Male Youth for the U.S. and France, 2004

	U.S.	France
1. Unemployment rate (U/U+E)	11.8	20.8
2. Labor Force Participation Rate (U+E/population)	70.2	41.4
3. Employment Population Rate (E/population)	61.9	32.8
4. Unemployment to Population Rate (U/population)	8.3	8.6

Source: statistical annex, OECD Employment Outlook 2005

The fact is that the incidence of unemployment in the total youth population is about the same in the two countries. As the table shows, for male youth the unemployment-to-population rate is 8.3 percent in the United States and 8.6 percent in France. The unemployment-to-population rate for female youth is lower in both countries: 7.4 percent in France and 6.5 percent in the United States.³ *The dramatic difference between France and U.S. is not the relatively large numbers of youth who are unemployed in France, but the relatively small number of employed French youth, especially students.* Using the proper yardstick – relative to the youth population - the magnitude of the youth unemployment problem in France is almost indistinguishable from the situation in the United States.

2. What About Youth Employment Rates?

Compared to other developed OECD countries, France has a low youth employment rate. Because most youth are enrolled in school – and most would agree that in the current world economy more young people enrolled in school and training programs is better than less – the welfare effects of higher youth employment rates, however, is not straightforward. This is surely the case for 16-19 year old full-time students.

In 2003, the vast majority of 15 to 19 year olds in both France (83.8 percent) and the United States (82.9 percent) were enrolled in school. But their employment rates were strikingly different. In the U.S., 23.1 percent were also working (generally part-time), compared to only 1.8 percent of these French teenagers. For those enrolled in school, U.S. teenagers had a much higher unemployment-to-population rate (3.5 vs .8); for those not enrolled, the unemployment-to-population rate was about the same (2.4 for the U.S. and 2.1 for France).⁴

The picture is different for 20-24 year olds. A much higher share of young French adults are still enrolled in education (51.1 in France compared to 35.0 percent in the United States), but the unemployment-to-population rate for those not enrolled is higher in France (9.6 vs 5.9).

Which mix of employment and enrollment is preferable? Clearly we would want as many 15 to 19 year olds as possible to be in school and both countries have succeeded fairly well in achieving this goal. Whether U.S. teenagers – and the future quality of the work force – are better off with students in low-wage, largely part-time work is not so clear. Turning to young adults, France does a much better job of keeping 20 to 24 year olds in school. In 2003, while about one-third of French young adults are not in school and hold jobs, almost half (48.5 percent) of their U.S. counterparts are employed and not in school. Which is better? If French students are taking advantage of their schooling to build skills and capacities, their higher enrollment rates are preferable. But if a large share of French youth are in school only because they can't get jobs and are mainly just biding their time, as some argue, their higher enrollment rate at least partly just masks inadequate job opportunities.

A far better statistic for measuring poor labor market performance and social dysfunction is the share of young adults (ages 20-24) who are neither enrolled in school nor employed. On this criterion, France and the U.S. perform almost identically: in 2000, the share of all young adults not in school and not employed was 14.1% in France and 14.4% in the United States. This compares, for example, to 15.4 percent for the U.K. and just 7 percent for the Netherlands.⁵

Analysis of the productivity levels of French and American workers gives some indirect support to the belief that high youth enrollment rates and low youth employment rates may payoff for France. According to three different sources of hourly labor productivity in the early 2000s, French workers are, on average, about anywhere from 6-16 percent more productive than their American counterparts.⁶

3. Will Dismantling Employment Protection Laws Increase Youth Employment?

It is widely accepted, particularly among economists, that employment protection legislation (EPL) is one of the main reasons for high unemployment, and this helps explain high youth unemployment in France, which, it is claimed, is characterized by some of the strictest employment protection in Europe. According to the OECD, France is the only rich, developed country that has acted to strengthen EPL in recent years. In the view of its critics, EPL will have the greatest effects on the employment opportunities

of “outsiders”, such as youth and women. In fact, the available economic evidence provides little support for the view that scaling back EPL will result in declining unemployment.

The OECD provides the only reliable measure of EPL for comparisons across countries. Their measure combines a score for “regular” employment (the best jobs with the most rights), “temporary” employment (short-term, fixed contract jobs), and collective dismissals.

For regular employment, France gets a score (2.5) - higher than the score for many OECD countries, but about the same or lower than some low unemployment countries including Austria (2.4), the Netherlands (3.1), Norway (2.3), and Sweden (2.9). The U.S., by comparison, gets a score of 0.2. It should be noted that all four of the countries just cited have achieved unemployment rates that are similar to or lower than rates in the United States. But with respect to temporary employment, France stands out with a higher EPL strictness score than any other developed country.

At the same time, France gets a relatively low (less strict) score (2.1) on collective dismissals, which is not only well below “success stories” of the Netherlands (3.0), Austria (3.3), Ireland (2.4) and Denmark (3.9), but is also far below the U.K. and the U.S. (both at 2.9).

In the end, the OECD gives France one of the highest overall EPL strictness scores because they chose (without published explanation) to weight the strictness of temporary and regular employment regulations equally (5/12), despite the fact that only 15 percent of France’s workers are employed in temporary jobs. And France’s relatively low collective dismissal score gets just a 2/12 weight.

The upshot is that, apart from the rules governing temporary employment, France’s employment protection laws are not stricter than many other low unemployment European countries. The OECD’s weighting scheme produces an overall score that certainly oversimplifies and arguably misrepresents the relative strictness of French laws.

In any event, despite numerous studies that have run statistical tests on the EPL-unemployment relationship, there is little evidence that there is any connection.⁷ The OECD’s own assessment of the empirical impact of EPL on unemployment places no blame on EPL for the high unemployment problems facing some European countries including France. According to the OECD’s 1999 evaluation of EPL, “The basic finding appears robust: overall unemployment is not significantly related to EPL strictness.”⁸ The OECD’s conclusion was reaffirmed in 2006 in what is perhaps the most careful test of its kind to date.⁹ The OECD finds stronger evidence that EPL may affect youth unemployment, but even here, their conclusion was that the results should be “considered with caution.”¹⁰

The relatively small effect of EPL on unemployment is not terribly surprising. EPL may make employers less willing to hire new workers -- because it might be difficult to dismiss them later if demand falls or the workers turn out to be a bad fit -- but, the

purpose of EPL is to make it harder for employers to dismiss workers, which helps to keep employment rates higher than they otherwise would be in economic downturns.

In sum, the balance of the statistical evidence to date from cross-country analysis of EPL and other labor-market institutions is that the strictness of EPL has little or no effect on unemployment, with the results for youth are mixed at best. It is also the case that French employers have the option of employing youth under temporary, fixed contracts. While less than 15 percent of all French workers are so employed, young workers account for almost half of all temporary workers (44 percent in 2000), and nearly 35 percent of all employed French youth have temporary contracts.¹¹ These temporary contracts already provide employers with substantial employment “flexibility.”

4. Were the French Students Right?

The widely held view, repeatedly parroted in the U.S. media, that French economic performance is poor and that French employment performance is catastrophic, flies in the face of the evidence. And the conventional wisdom that the French students are wholly misguided in their desire to maintain stronger employment protections than prevail in the United States is mistaken and offers a striking example of the ability of free market ideology to trump the facts.

With substantially higher hourly productivity, the French economy has produced almost as much employment growth as the U.S. since President Bush came into office (3.1 vs 3.5 percent growth between 2000 and 2005).¹² The two countries have almost identical shares of young people in unemployment -- the high youth unemployment rates so often cited in the media give a distorted view of the situation in France because so few French youth enrolled in school are employed. And perhaps most importantly, the shares of French and U.S. youth not employed and not enrolled in school – by far the most important measure of social dysfunction - are nearly identical.

At the same time, the French have far higher shares of the young adult (20-24) population enrolled in school, which on balance must be a good thing. And as American students will be the first to appreciate, French students do not enter the labor market with crushing debt burdens (school tuition in France is negligible compared to the U.S.).

Even the widespread belief that freeing employers to fire younger workers without cause will cause firms to create more jobs and thereby reduce the unemployment rate is not well-supported by economic research. French students and young people may well be correct that employers would only respond to the legal ability to fire workers under the age of 26 simply by substituting younger for older workers, and then by firing them when they approach age 26. The result would perhaps be some more precarious jobs, but probably no more jobs overall, and almost certainly no change in the overall unemployment rate.

We do not underestimate the inadequacy of job opportunities facing French youth. But the withering attack on the French and their welfare state in recent weeks reflects both a greatly exaggerated view of the real magnitude of youth unemployment levels and a

wildly exaggerated belief in the effects of employment protection regulations on unemployment.

At the same time, the proposal, and the harsh criticism of those who dared question its net payoffs, reflects a narrow free market fundamentalism in which serious economic evidence of the beneficent effects of deregulation becomes entirely unnecessary. Who has seen such evidence cited in the scores of commentaries on this issue? Perhaps the French students sensed that free market ideology had trumped the evidence. At least in this regard, the French students *were* right after all.

¹ From the *OECD Employment Outlook 2005*, Statistical Annex.

² A hypothetical example may be helpful. Imagine that two countries both had 100 people between 15 and 24 years old, and both countries had 10 unemployed workers in the same age range. Now imagine that in country A, young people tended to work while they were studying, so that 50 of the young in country A were working. Meanwhile, in country B, college tuition was free so young people had little need to work to pay for college, so only 20 young people were working. The unemployment rate in country A --where young people work a lot-- is 16.6 percent (calculated as 10 unemployed / (10 unemployed + 50 employed)); in country B --where young people tend not to work while they study-- the unemployment rate is twice as high, 33.3 percent (10 unemployed / (10 unemployed + 20 employed). In both countries, the same share of all youth is unemployed --10 percent-- but in the high employment country the official unemployment rate is much higher than in the low employment country.

³ The UPOP rate shown in row 4 of the table is calculated simply by subtracting the employment rate (row 3) from the labor force participation rate (row 2).

⁴ Enrollment and employment statistics are from the OECD's *Education at a Glance 2005*, Table C4.2a. We thank Paul Swaim for referring us to these data.

⁵ *OECD Employment Outlook 2002*, Chapter 1, Table 1.6a).

⁶ With the U.S. indexed at 100, Eurostat puts France at 106 for 2002; OECD has France at 108.5 for 2003; and Groningen puts France at 115.6 for 2004. Eurostat data as reported in Cette (2005), Table 1. OECD data from the OECD Productivity Database, February 14, 2005. Groningen data from analysis of Groningen Growth and Development Centre and The Conference Board, Total Economy Database, January 2005, <http://www.ggdc.net>, downloaded July 5, 2005.

⁷ See Baker et al., "Labor Market Institutions and Unemployment: A Critical Assessment of the Cross-Country Evidence," in David R. Howell, *Fighting Unemployment: The Limits of Free Market Orthodoxy* (Oxford University Press), 2005.

⁸ *OECD Employment Outlook 1999*, Chapter 2, p. 77). In their updated study of the effects of employment protection regulation, the OECD concludes similarly: "evidence of the role played by EPL on aggregate employment and unemployment rates remains mixed in both theoretical and empirical studies..." (*OECD Employment Outlook 2004*, chapter 2, p. 81).

⁹ OECD, *Reassessment of the Jobs Study*, Background Paper #1, 2006.

¹⁰ *OECD Employment Outlook 2004*, Chapter 2, box 2.4, p. 86.

¹¹ *OECD Employment Outlook 2002*, Chapter 3, Tables 3.4 and 3.3 respectively.

¹² OECD employment data, downloaded from OECD.org April 13, 2006.