



The demand for job protection Some clues from behavioural economics

Fabio D'Orlando*, Francesco Ferrante

Dipartimento di Scienze Economiche and CreAM - Università di Cassino, Via S. Angelo, Cassino 03043 (Fr), Italy

ARTICLE INFO

Article history:

Received 13 November 2007

Received in revised form 22 August 2008

Accepted 30 August 2008

JEL classification:

D81

E24

D7

D31

J58

Keywords:

Employment protection legislation

Behavioural economics

Loss aversion

Endowment effect

Hedonic adaptation

Redistribution

ABSTRACT

Radical differences in labour market regulations among countries that in other institutional respects are quite similar are still surprisingly frequent. Nonetheless, traditional theoretical analysis meets enormous difficulties in explaining these differences. The scope of our paper is to show that some clues from behavioural economics could be used to better theoretically treat this problem. Our argument is that workers are different, due to the effects of both culture and education. In particular, building on empirical evidence, we argue that *loss aversion* and *hedonic adaptation* are culturally-determined and country-specific aptitudes and that they may help explaining why workers, either employed or unemployed, ask for job protection and are willing to pay the cost of it. The main conclusion of our analysis is that, for poorly educated workers sharing a fatalist view of life, job protection can be more effective than public social expenditure. As a consequence, we suggest that countries with a poorly educated and fatalist workforce will be more prone to offer protection through job protection rather than public social expenditure, which is exactly what the empirical evidence shows.

© 2008 Elsevier Inc. All rights reserved.

1. Introduction

Over the past 15 years or so a general tendency towards deregulation of the labour market has swept most OECD countries, notably the highly-regulated European ones. Nonetheless, radical differences in labour market regulations among countries that in other institutional respects are quite similar are still surprisingly frequent. And deregulation has taken place with differing speed, deepness and resistance and has involved other instruments of social protection, such as unemployment benefits and the pension systems. Traditional theoretical analysis of labour market institutions has run into serious difficulties in explaining these different dynamics. We believe that these difficulties depend on the fact that the traditional approach mainly focus on the pecuniary cost of unemployment, leaving aside psychic costs.

In particular, the empirical evidence indicates that unemployment is one of the most negative outcomes in life, carrying non-pecuniary psychic costs as well as pecuniary ones (Clark and Oswald, 1994; Frey and Stutzer, 2002). Subjects appear incapable of

fully recovering from the loss of well-being determined by unemployment episodes, even if they get full income replacement and even if they find a new job. On more general grounds, in their study on happiness, Di Tella et al. (2007) argue that people can adapt completely to income shocks but that their adaptation to life's events is incomplete.¹

The standard explanations of the demand for job protection largely neglect the non-pecuniary components of the costs of unemployment, thus preventing theoretical analysis from fully grasping the determinants of the phenomenon. We believe that theoretical analysis should include psychic costs among the elements that may induce workers to demand employment protection legislation (EPL) capable of guaranteeing job protection, i.e. keeping workers from being (easily) fired. We also believe that the actual incidence of these psychic costs helps explain international differences in social protection policies and their evolution over time.

To study the role that these psychic costs of unemployment play in determining why workers ask for protection and how they prefer it to be delivered, this paper looks at psychological evidence and some clues from behavioural economics. Indeed, behavioural economics emphasises non-pecuniary costs of labour market

* Corresponding author.

E-mail addresses: fabio.dorlando@unicas.it (F. D'Orlando), f.ferrante@caspur.it (F. Ferrante).

¹ On this point, see also Easterlin (2004).

flexibility which the standard approach to decision-making generally ignores. We focus on the role of some related phenomena examined in economic psychology: *loss-aversion* (Tversky and Kahneman, 1991; Kahneman et al., 1991), the *endowment effect* (Knetsch and Sinden, 1984; Knetsch, 1989; Kahneman et al., 1990, 1991), the *status quo bias* (Samuelson and Zeckhauser, 1988; Kahneman et al., 1991), and *hedonic adaptation* (Clark and Oswald, 1994; Frey and Stutzer, 2002). The inclusion of these phenomena and the analysis of their cultural determinants allows a more robust explanation of the demand for job protection and its relationship with workers' education. In particular, building on Ferrante (2004) and Bè nabou (2000b), we show that workers' educational attainment is a fundamental factor in explaining the demand for job protection and that our interpretative framework helps explain the choice between EPL and social public expenditure (SPE) within Europe. The basic intuition is that education mitigates the adverse effects of fatalism on workers' perception of employment and income opportunities. According to this argument, EPL appears to be more effective to protecting poorly educated workers by re-allocating the non-pecuniary costs of unemployment, than social insurance tools such as unemployment benefits (UBs) or other social programmes (i.e. SPE in general). Hence, we argue that countries with poorly educated workers should be more prone to provide job protection norms than SPE: exactly what empirical evidence shows. The basic conclusion is that flexibility (or inflexibility) is a behavioural attitude of individuals, that is affected primarily by culture and education, and not a normative characteristic of labour markets. But, whereas culture cannot be modelled by politicians and takes a long time to change, education can be affected through appropriate policy measures.

The paper is organized as follows. Section 2 offers some preliminary empirical evidence on how OECD countries provide protection by combining EPL and SPE. Section 3 gives an overview of the standard explanations of the determinants of demand and supply of social protection. Section 4 extends this analysis by focusing on some insights from behavioural economics. Section 5 describes the main policy implications of our analysis and draws the conclusions.

2. Some empirical evidence

2.1. Social protection systems in OECD countries

Governments around the world meet their workers' demand for social protection in different ways. The policy tools, include, social transfers and direct provision of public social services as well as the regulation of product and labour markets. All these tools are intrinsically redistributive, but their effects differ. Whereas social transfers and social public expenditure mainly redistribute income after it is produced, labour and product market regulations, due to their impact on labour demand and supply, substantially lead to *ex-ante* redistributive effects. Moreover, only some are explicitly targeted to workers.

The focus of this paper is on employment protection legislation and social public expenditure, which are the most important instruments of social protection against job risks; hence, we leave aside other labour market institutions and the regulation of product markets. The reason for considering social public expenditure as a whole and not just unemployment benefits as a means of providing social security to workers is that it is a more appropriate measure of the social safety net in the face of income risks due to job loss.

Based on empirical evidence, we can say that two important elements characterize and differentiate social protection systems within OECD: the overall extent of protection and the choice between social expenditure and employment protection.

A reasonable measure of the amount of protection provided through social public expenditure is given by SPE as a percentage of GDP, whereas a measure of the protection offered through labour market regulation is the OECD's index of labour market rigidity. The latter takes account of a large set of factors regarding labour contract regulations (Nicoletti et al., 2000). For neater international comparisons, we also calculated a normalised version of these indexes: NISPE is given by SPE/GDP divided by the sample maximum; NIEPL by the index of labour market rigidity divided by its maximum.²

An overview of the social safety nets enjoyed by workers and their families in the 20 OECD countries examined is given in Table 1.³ As far as social public expenditure is concerned, the rough distinction between continental European countries providing, on average, more social protection than other countries is confirmed with the major exception of the United Kingdom. Similarly, as for job protection legislation, the 20 OECD countries studied can be divided into two main groups in terms of the stringency of job protection: Australia, Canada, Ireland, New Zealand, Switzerland, the United Kingdom and the United States display relatively low levels of regulation, while Austria, Belgium, Denmark, Finland, France, Germany, Italy, the Netherlands, Norway, Sweden, and Spain are characterized by relatively high levels of employment protection.

Figs. 1 and 2 display NIEPL, respectively in the '80s and in the '90s, plotted against the NISPE in the same period, thus providing a more informative picture on different countries' choice between regulation and social benefits. The picture did not change greatly between the two periods, suggesting that North European countries have pursued their high redistributive targets relying more on redistribution of market-generated income through social public expenditure, South European countries more on stringent job security legislation, and central Europe somewhere in the middle. Apart from Japan, all the other countries with medium-low redistributive targets counted more on redistribution of market-generated income through social public expenditure.

Various explanations for these different attitudes to protection of workers have been suggested. The interpretative frameworks are not mutually exclusive and they offer, from their different perspectives, quite a composite picture. Nonetheless, they all rely on a standard framework that neglects some crucial behavioural and psychological elements. Taking these elements into account may give us a better understanding of the determinants of the phenomenon and help explain why some countries rely more on job protection than on public spending to obtain social protection.

Before leaving empirical evidence for theoretical analysis, we should discuss another important empirical pattern, namely the significant explanatory role of education.

2.2. EPL vs. SPE: the role of education

It is reasonable to ask whether, owing to the expected contribution of education to workers' ability to adapt to changes in occupational status, educational levels are a factor explaining the demand for social protection (Bè nabou, 2000b; Ferrante, 2004). A related question is whether education affects the form in which workers wish protection to be delivered. We expect that education should improve workers' behavioural adaptability and thereby reduce the need for job protection.

² Although more recent data are available for some of the variables we have limited the temporal span of the analysis so as to provide comparable data for all the variables.

³ All SPE data in Table 1 and in Figs. 1 and 2 include old cash benefits.

متن کامل مقاله

دریافت فوری ←

ISIArticles

مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات