

What are the effects of active labour market policy? An introduction

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Government spending on active labour market programmes (ALMP) has been on the rise in most OECD countries over the past two decades. In the year 2000, a typical OECD country spent 0.8 per cent of GDP on ALMP. Sweden has consistently belonged to the group of countries with an above average spending on ALMP, and its spending peaked during the severe recession of the 1990s. In 1993, ALMP comprised 3 per cent of GDP and encompassed 4 per cent of the labour force; by the year 2000, spending had declined to 1.4 per cent of GDP.

Active labour market programmes appear in many guises. There are at least three broad ingredients. *Public employment services* aim at improving the matching between vacancies and job seekers. *Labour market training* involves spending on vocational training and is targeted at the unemployed or at employed workers at risk of becoming unemployed. *Subsidised employment* includes a variety of measures to raise employment, typically targeted at unemployed workers.

The growing practical interest in ALMP has nurtured an expanding industry of evaluation research. Although Sweden has been a pioneer when it comes to launching large-scale labour market programmes, other countries have pioneered a thorough evaluation of the programmes. The most noticeable contributions in this field originate from the US, where spending on ALMP has consistently been way below the OECD average. In recent years, however, there have been signs that Sweden is catching up in this area. New policy initiatives have brought evaluation to the fore and new data sets have facilitated microeconomic studies of ALMP.

What do we know, then, about the effects of these programmes? The purpose of this issue of *Swedish Economic Policy Review* is to shed light on this question. The issue includes seven papers presented at a

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one-day conference on October 8, 2001 in Stockholm, organised by the Economic Council in cooperation with the Institute for Labour Market Policy Evaluation (IFAU). In addition to the presentation of results from new research, the aim of the conference was to offer an overview of recent experiences of ALMP in Sweden and elsewhere.

In the first paper, *John Martin* and *David Grubb* summarise recent research concerning what works among active policies and for whom. The review draws on the recent literature on the evaluation of active labour market programmes as well as country reviews and studies conducted by the OECD on the interactions between active and passive labour market policies and the role of the public employment service. At first sight, the evaluation results on the impact of many active labour market programmes are not very encouraging. But the authors notice that there are some success stories: job-search assistance, wage subsidies in the private sector, and labour market training do work for some target groups, even if the impact is not large. Active labour market policies are not a magic bullet to solve the unemployment problem on their own, however. Activation policies that combine high-quality assistance in finding work with pressure on unemployed people to accept it can be effective, but more rapid returns to work sometimes come at the cost of accepting lower re-employment earnings.

The following four papers deal with the Swedish experience of practising ALMP. The paper by *Lars Calmfors*, *Anders Forslund* and *Maria Hemström* presents a comprehensive survey and assessment of the evaluation literature pertaining to Sweden. There are six main conclusions: (i) there is hardly any evidence of a positive effect on matching efficiency; (ii) there are indications of positive effects on labour force participation; (iii) subsidised employment seems to cause displacement of regular employment, whereas this appears not to be the case for labour market training; (iv) it is unclear whether ALMP raise the aggregate wage pressure in the economy; (v) in the 1990s, training programmes do not appear to have enhanced the employment probabilities of participants, whereas some forms of subsidised employment seem to have had such effects; and (vi) youth programmes seem to have caused substantial displacement effects at the same time as the gains for participants appear uncertain. The authors' overall policy conclusion is that the use of ALMP on the scale experienced in Sweden in the 1990s is not an efficient means of employ-

ment policy. To be effective, ALMP should be used on a smaller scale.

Barbara Sianesi has written the second paper on Swedish ALMP. She focuses on the *relative* performance of various programmes and asks which programmes work best. The effectiveness of the programmes is assessed in terms of their impact on individual employment probabilities and the duration of unemployment benefit receipt. The evidence as to the overall effectiveness of the programmes is rather mixed, with individuals joining a programme subsequently enjoying higher employment rates, but also a higher probability of drawing unemployment benefits over time than if they had searched longer in open unemployment. The comparison of the relative performance involves six programmes applied in the 1990s: labour market training, workplace introduction, work experience placement, relief work, trainee replacement and employment subsidies. The best results by far are found for employment subsidies, followed by trainee replacement schemes.

The paper by *Katarina Richardson* and *Gerard van den Berg* presents new results regarding the impact of Swedish labour market training, the most expensive type of active labour market programme in Sweden. The number of evaluation studies of training has been rather small, however. Most of the earlier studies have analysed the impact on participants' earnings and used data from the early 1980s. Richardson and van den Berg focus on the impact on the duration of unemployment by using longitudinal administrative data containing the population of unemployed in the period 1993-2000. The results indicate a significantly positive effect on exit to work after the programme. The magnitude of the effect is very large shortly after finishing the course but it then diminishes. A noteworthy finding is that the net effect of participation in the programme on the mean unemployment duration is close to zero when the time spent in the programme is taken into account.

Kerstin Johansson has written the fourth paper on Swedish labour market policies. She investigates the impact of ALMP on labour force participation rates by making use of regionally disaggregated data (panel data for Swedish municipalities for the period 1986-1998). The key finding is that ALMP do seem to increase participation rates. Taken at face value, the estimated effect is substantial. As Johansson notes, the programmes have been used to qualify unemployed for new periods of unemployment benefits, a fact that should be kept in

mind when interpreting the results. The effect on the effective labour force may be less than estimated if participation in programmes in part serves to qualify for benefits.

The paper by *Richard Blundell* and *Costas Meghir* provides a review of recent British experiences of alternative programmes designed to enhance employment among low-skilled and low-income people. The New Deal for Young People is an example of a labour market programme that is individually based, not means-tested and of limited duration. The Working Families Tax Credits is an example of earned income tax credits—“in-work” benefits—that are based on family income, means-tested and of indefinite duration. The paper’s evaluation of the New Deal exploits quasi-experimental features of the programme to identify the effects on exit rates to employment. The results suggest that the policy had a positive effect on the transition rates to unsubsidised employment. The evaluation of the in-work benefits is mainly based on ex ante simulations of estimated labour supply models and indicates a modest positive effect on employment among the target groups, i.e. low-income families. These findings are broadly similar to results found in related studies based on data for the US.

Pedro Manuel Carneiro, *Karsten Hansen* and *James Heckman* have written the final paper in this issue. The paper summarises their recent research on evaluating the distributional consequences of social programmes. This research extends the economic policy evaluation literature beyond estimating mean impacts to estimate *distributions* of outcomes generated by different policies. The approach thus enables analysts to evaluate the distributional effects of social programmes. The methods determine which people are affected by a given policy and what their gains are. The authors apply the methods to analyse two proposed policy reforms in US education.

All in all, the collection of papers in this issue of *Swedish Economic Policy Review* provides some good news for proponents of ALMP but also arguments for sceptics. Some programmes appear to work as intended, especially if there is pressure on the unemployed to accept them. The Swedish evidence is rather mixed, however. It seems plausible that ALMP have had positive effects on labour force participation, although it is unclear to what extent this reflects active job search as opposed to “benefit seeking”. The effects of labour market training and youth programmes on individual employment performance do not seem impressive and may not pass cost benefit tests.

ALMP as practised in Sweden over the past couple of decades have seen a large number of policy packages. To some extent, the plethora of programmes reflects re-labelling rather than substantive changes. Be that as it may, it is nevertheless striking how keen governments (of different political colours) have been to innovate on a large scale and how largely unconcerned they have been to view programme evaluation as an integral part of programme design. The one and only randomised experiment in this area took place almost thirty years ago! It is perhaps understandable that programme evaluation issues become of second-order importance in an exceptionally deep recession, as that experienced by Sweden in the early 1990s. In more normal macroeconomic conditions, however, there is little excuse for ignoring evaluation issues when designing active labour market programmes.

