

The Framework of an Efficient Labour Market



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Objective: To be “Obvious”



- Beat up Straw Men
- Draw Unsurprising Morals
- Discuss a few General Issues
- Illustrate with 2 Specific Initiatives

Is Training & Mobility enough for Labour Market Efficiency?

- Hypothesis: To maximize GDP
 - Put square pegs in square holes & put round pegs in round holes
 - Move when necessary
- All Government has to do is:
 - forecast supply & demand
 - Better Information for Labour Market Matching
 - Provide (Re)training: turn the squares into the well rounded $\nabla \tau_0$

A Subtle Mis-specification: Not Quite so Easy

- Incredible Heterogeneity plus constant change (everywhere)
 - instantly obsolete forecasting
- Macro Context Dominates Outcomes
- Most Change occurs within Firms
 - Reactions of Infra-Marginal Workers are crucial
- Desired Outputs $>$ GDP

Modern Labour markets: Variety + Constant Change

- Jobs in ALL sectors are incredibly varied & constantly changing
 - temporarily square holes & morphing pegs
- People constantly changing in capabilities & skills - endogenously
 - basic rules: “Use it or lose it” “Learn while doing”
- **NO LASTING ALLOCATION OF LABOUR IS POSSIBLE OR DESIRABLE**
- Issue: To design institutions to enable continual & optimal readjustment

Perils of “Central Forecasting” - The “Dodge Report” (1981)

- Makes many good points BUT:
- Central Premiss = high oil prices indefinitely
- Energy Mega-Projects e.g. Cape Breton Coal
- Forecast: demand shift to skilled trades & mining, manufacturing & construction jobs
- Perceived Problem: Excess Supply of highly qualified (especially - University Graduates)
- Actual Event: Oil Price Collapse & Skill Biased Technological Change

Moral: Macro Economic Context is Crucial

- What specific skills are actually needed ?
 - Central forecasting has a poor record
- Market mechanism signals *scarcity*
- Labour market sends few signals when unemployment is high & skills generally in surplus
 - Vacancies & wages - signal to individuals' choices
 - Lost Sales signal firms that training is needed
 - Political pressure signals government & schools to redesign curricula

Are Jobs Scarce or are Workers Scarce ?

- Expert Panel on Skills (2000)
- “No evidence of a generalized shortage of technical skills in Canada”
 - “specific sub-sectors of industry”
 - shortage of “all rounders” with good - Technical + people + management skills
- “shortage of opportunities”
- HWI + occasional surveys
 - current real vacancies are rare (< 1% LF)

Labour Surplus creates inefficiencies

- **Balance** of Supply and Demand affects all labour market Institutions
- Queue of the already qualified implies:
 - atrophy of firm training
 - disincentive to enhancing job quality
 - e.g. family friendly work practices
 - pointless to demand curriculum reform
- Future demand anxiety implies
 - increased risk to worker specialization

Labour Market Change: Internal + External

- Internal Labour Market
 - decisions on wages, allocation of labour, training, vacancies, promotions & work practices made within firms
- External Labour Market
 - hiring wages and mobility of workers between firms
- External Market easier to observe
- BUT most decisions are within firm

Most workers remain in long term jobs

- Predominant Pattern: Initial mobility followed by infrequent job change
- Long Term Jobs imply substantial sunk investments by firms & workers
- “Internal” & “External” change both matter BUT
- Change within firms dominates aggregate productivity growth
 - motivation of infra-marginal workers crucial
 - Expert Panel: shortage of Management Skills

Well-Being γ \$ GDP

- Leisure time, job security, working conditions & job quality are major determinants of well-being, happiness
 - heavily influenced by labour market
- Implications
 - Criteria of “Efficient Labour Market” cannot be narrow
 - Wide Variation in Tastes - but Available Jobs means Available Choices

Efficiency : Necessary Conditions

- Decentralization of Decision Making
 - complex diversity of local changes
- Jobs
 - Demand for Labour is a Derived Demand
 - Strong Aggregate Demand is Crucial
 - Monetary Policy is key
- Understanding of full Incentive Structure for both workers and firms
 - Social Security as risk-sharing

Issue # 1: Risk & Reward



- Economy needs diversified portfolio of specialized skills
- But Individuals reduce risk by choosing generalist training
- Current Trend is to a substantially higher student debt load
- Risk-averse individuals will under-specialize if training fully privatized

Issue # 2: The Skill Base - Who Pays for Higher Education?

- Canadian post secondary system expanded dramatically 1960-75
- High Returns but 25 years of Decline
 - Federal Provincial Turf Wars + Deficit
 - Physical & Human Capital wearing out
- Base Funding is unglamorous & OLD
- Rise & Fall in two Generations ??

Issue # 3: Building Institutions for Continual Social Change



- Internet is already happening
 - HUGE impact on availability of information
- Sectoral Councils - a useful innovation
 - mechanism for “Voice” in shaping continual redesign of curricula
 - forum for labour / management contact & consultation
 - agency for direct service delivery & supervision of accreditation

Issue # 4: Avoiding Gimmicks - Registered Individual Learning Accounts

- Trendy to devolve to individuals risks & rewards of decision making on training
- But 19 year olds tend to be poorly informed
 - informational asymmetry inherent in education
 - problem more severe for disadvantaged groups
 - Vulnerability & Dream Merchants
- politically - cannot exclude for-profit trainers
 - THE MAJOR PROBLEM AREA FOR CANADA STUDENT LOANS

What do we Need for Efficiency?



- JOBS
 - Strong Macro Economic Aggregate Demand
- INSTITUTIONS
 - to identify needs & articulate solutions at industrial level
- POLICY DESIGN
 - to match incentives to social needs
- DOLLARS
 - to pay for needed investments in skills