Fixed-term employment and European labor market mobility

Fixed-term contracts are regarded as an instrument for increasing labor market flexibility. However, European countries differ significantly in the prevalence of temporary jobs. A comparison shows that temporary employment promotes labor market mobility to only a limited extent. While it facilitates labor market access in part, it also leads to unstable employment relationships and segmented labor markets with few opportunities for advancement. To create sustainable employment and facilitate transitions into permanent jobs, EU states must combine reforms of employment protection with investment in education and training as well as in active labor market policies.

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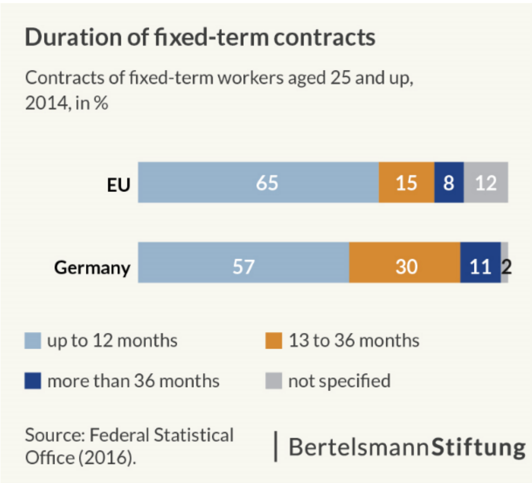
Focus



In contrast to permanent employment relationships, fixed-term labor contracts are of predefined duration. On average, most fixed-term contracts in the EU in 2014 had a maximum duration of one year. In Germany, too, this was the case for 57 percent of contracts. Because trainees are, by definition, temporarily employed, only workers aged 25 and above are considered here.

Labor market mobility and flexibility are highly significant for an economy as a whole. A flexible labor market has a positive effect on the adaptability of a national economy, e.g., during and after a crisis, or when faced with long-term structural changes such as technological change. On the other hand, the mobility of a labor market also directly impacts workers' employment opportunities and their job quality.

Fixed-term contracts are commonly seen as a means of making labor markets more flexible. They are attractive to employers because they allow them to avoid entering into a longer-term contractual relationship with the employee. Thus, production peaks can be covered and risks can be reduced in an insecure business environment. This is particularly relevant when employment protection for workers with permanent contracts is strong and the costs of dismissal are accordingly high. Fixed-term contracts also offer advantages from the employee's perspective. Indeed, many such contracts are entered into in the framework of employee training or development. Moreover, they serve as an extended probationary period, facilitating especially the entry of young people without prior work experience into professional life.

However, temporary jobs are accompanied by relatively high insecurity, as they usually do not guarantee continued employment or a transition into a permanent employment relationship. This is not only a burden to the individual worker, but has negative consequences from an overall economic perspective as well, as the employer and the employee in a fixed-term employment relationship both have less incentive to invest in the development of human capital. Temporary jobs therefore generally offer little further training, few advancement opportunities, and lower wages (Eurofound 2015).

Against this backdrop, the question arises as to what contribution fixed-term employment makes to the mobility of European labor markets. Three basic aspects of mobility figure prominently here:

1. The access function, i.e., the question of whether fixed-term contracts facilitate entry into the labor market

2. The stability of temporary jobs in comparison with permanent employment

3. The stepping-stone function, i.e., the extent to which fixed-term employment serves the transition into permanent employment relationships

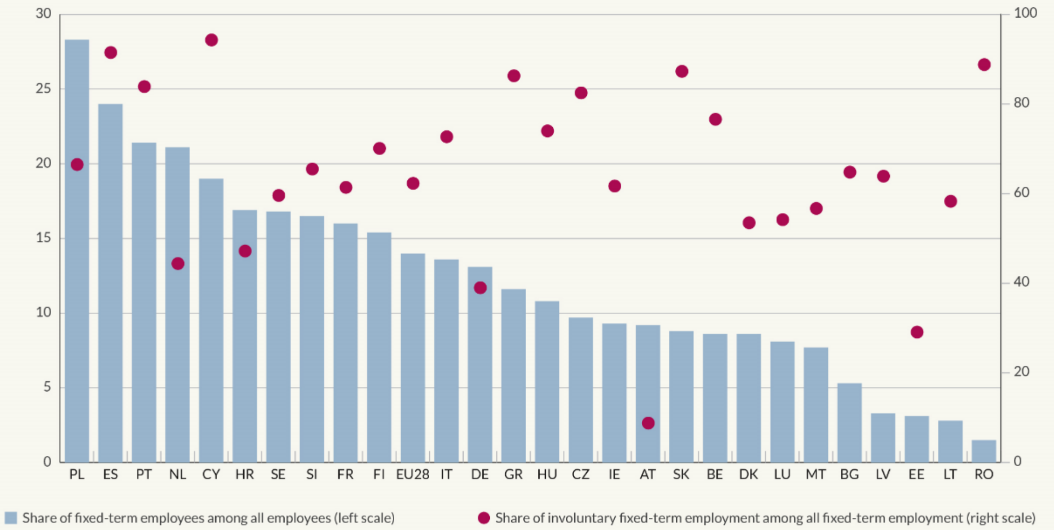
1. Prevalence of fixed-term employment in the EU

In 2014, 14.6 percent of all employment relationships in the EU were of fixed duration. However, in some countries, such as Poland (28.3%) and Spain (24.0%), the share is significantly higher. Above-average rates of fixed-term employment were also observed in Portugal, the Netherlands, Croatia, Sweden, and France (cf. figure 1). In contrast, the proportion of temporary contracts in the Baltic countries and in Romania and Bulgaria is relatively low. Germany, with a share of 13.1 percent, ranks slightly below the European average.

In all countries, temporary jobs play an important role especially among young workers. The share of fixed-term employees among the 15- to 29-year-old age group in most countries is more than twice as high as that among the labor force overall. Across the EU, one in three employees under 30 years of age (32.2%) is temporarily

FIG. 1: **Fixed-term employment and the share of involuntary fixed-term contracts**

Share among all employees aged 15 to 64, 2014, in %



Source: Eurostat Database, Federal Statistical Office (2016).

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employed, while in countries such as Poland, Portugal, and Spain, the rate is roughly one in two (Germany: 38%). The share of fixed-term employees among workers over 50 is only 7 percent in Europe as a whole (Germany: 4%). Thus, over the course of their careers, the great majority of workers succeed in entering into a permanent employment relationship.

Especially in those countries in which temporary jobs are widespread, most fixed-term contracts are involuntary, i.e., the majority of fixed-term employees indicate that they wish for a permanent position. This is the case for 91.5 percent in Spain, 86.3 percent in Greece, and 83.9 percent in Portugal. By contrast, in the Netherlands, only about 44 percent have a fixed-term contract involuntarily, while in Germany the rate is 39 percent and in Austria just 8.8 percent.

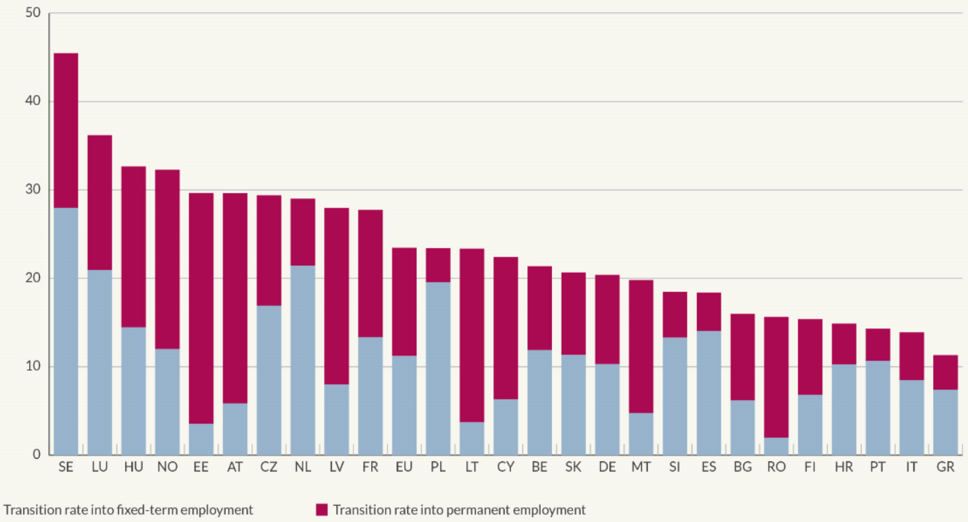
2. Access to employment

Do fixed-term employment contracts facilitate entry into the labor market? Figure 2 shows the annual rates of transition from unemployment into (dependent) employment by contract type in the period from 2011 to 2013 (cf. Bertelsmann Stiftung 2016). In Europe on average, approximately every fourth person who is unemployed in a given year finds a job in the following year. The overall transition rate varies markedly across countries, however. While it is over 45 percent in Sweden, it is less than 15 percent in Greece, Portugal, and Italy, which presumably is attributable in large part to the ongoing employment crisis in the latter countries.

EU-wide, 11 percent of the job seekers took up a temporary position and 12 percent a permanent job. Thus, roughly one in two unemployed persons achieving entry into the labor market does so by way of a fixed-term contract, although the share of tempo-

FIG. 2: **Transition rates out of unemployment by contract type**

2011 to 2013, in %



Source: Bertelsmann Stiftung (2016), calculation based on EU-SILC and SOEP data.

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rary employment as a part of overall employment is significantly lower. This ratio, too, varies strongly between countries. For example, job seekers in Poland are five times more likely to take up a temporary job than a permanent one. Generally, it can be said that in particular in countries with a large share of fixed-term employment, the likelihood of going from unemployment into a temporary position is especially high. This indicates that fixed-term employment indeed facilitates labor market access in these countries.

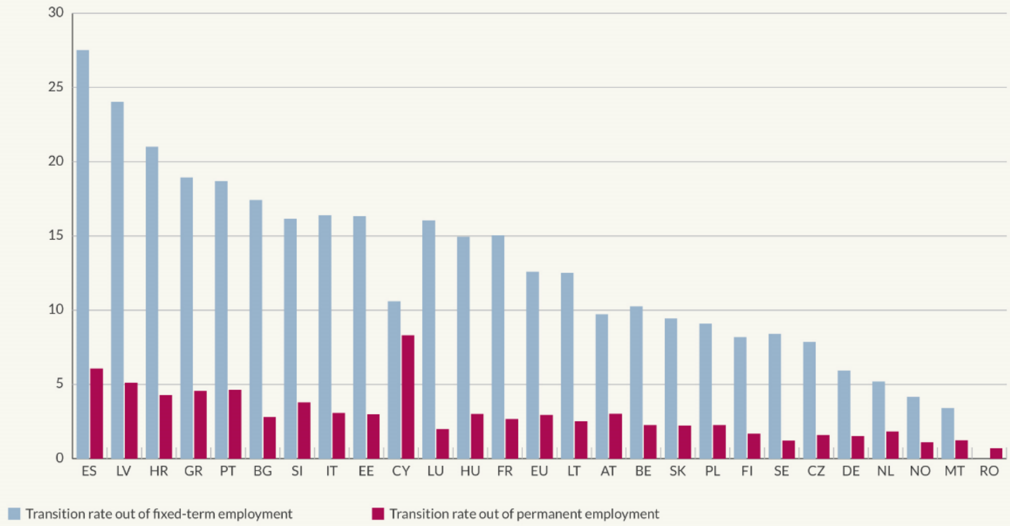
However, this picture is relativized when the fixed-term employment rate is compared with the overall transition rate (temporary and permanent) by country. While job seekers in countries with a high prevalence of temporary employment more frequently take up a temporary job, entry into the labor market (as measured by the transition rate into employment overall) is no easier in these countries than in the countries in which temporary employment only plays a minor role (e.g., Estonia and Lithuania).

3. Employment stability and stepping-stone function

The transition rates in the opposite direction, i.e., from employment into unemployment, offer insight into employment stability or the risk of unemployment faced by employees with fixed-term as opposed to permanent contracts. As figure 3 shows, the transition rates in the Southern European countries and Latvia are the highest, whereas in Norway, Malta, and Romania transition into unemployment is comparatively rare. In all countries, the unemployment risk for fixed-term workers is significantly higher than for the permanently employed: 12.6 percent versus 2.9 percent on average for Europe. The risk of becoming jobless is thus more than four times as high for temporary employees as for employees with permanent contracts.

FIG. 3: **Transition rates into unemployment by contract type**

2011 to 2013, in %



Source: Bertelsmann Stiftung (2016), calculation based on EU-SILC and SOEP data.

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Fixed-term contracts are problematic above all when employees are exposed to high job insecurity, without a realistic chance of gaining a permanent position. The decisive question here is thus whether temporary jobs enable advancement to permanent employment. The EU average shows a transition rate into permanent employment of 33 percent; i.e., one in three fixed-term workers obtains a permanent contract within one year. In France, however, this rate is slightly below 11 percent. Poland, the Netherlands, and the Southern European countries also have low transition rates into permanent employment. Overall, in the countries with an especially high rate of fixed-term employment, mobility between temporary and permanent employment is also very low and the labor market thus strongly segmented.

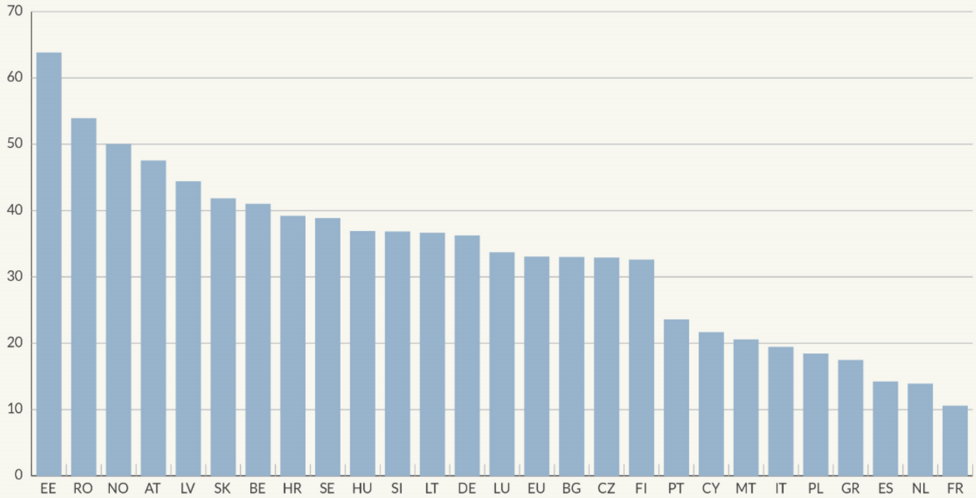
In Germany, the stepping-stone function into permanent employment is slightly above average, at 36 percent. It must be noted, however, that in Germany a relatively high share of the temporarily employed consists of apprentices, who are often subsequently taken on as permanent employees. Even taking this particularity into account, the chance for permanent employment is comparatively high in Germany. Temporary employment thus serves German employers first and foremost as an extended probationary period for the selection of employees who will stay with the company over the long term (Boockmann and Hagen 2008).

4. Balance of security and flexibility

The clear differences between countries with regard to the role of fixed-term employment are closely linked to their respective national labor regulations. In countries with strong employment protection and relatively inflexible labor markets, a tendency toward a higher proportion of temporary

FIG. 4: **Transition rate from fixed-term into permanent employment**

2011 to 2013, in %



Source: Bertelsmann Stiftung (2016), calculation based on EU-SILC and SOEP data.

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employment can be observed. Here, employers have an especially strong incentive to fall back on temporary workers as a "flexibility reserve." Especially in the Southern European countries, the high prevalence of fixed-term contracts can be explained by the fact that, for many years, labor market reforms have in most cases been only partial – i.e., the rules on permanent employment relationships went unchanged, while the creation of temporary jobs was facilitated.

On the whole, flexibilization that relies primarily on the creation of temporary jobs must be judged negatively, even if such a strategy is often easier to implement than comprehensive reforms. While in countries with generally inflexible labor markets, fixed-term employment contracts facilitate the entry of job seekers, the country comparison shows that they do not lead to better employment opportunities for workers overall. At the same time, they are associated with unstable jobs and low opportunities for advancement into permanent employment. Especially in countries with very high rates of temporary employment, the stepping-stone function and the sustainability of the jobs created are weak.

Instead, it is beneficial to combine reasonably low employment protection with measures that increase workers' job security, in particular a well-developed system of unemployment insurance. This also reduces the incentive to resort to temporary employment relationships. The EU Commission has articulated corresponding recommendations, especially the development of the stepping-stone function and the increased creation of permanent jobs with employment protection that increases over the duration of the employment relationship (European Commission 2012).

Since 2008, a number of countries, e.g., Poland and Spain, have relaxed employment protection for workers with permanent contracts so as to reduce the segmentation of the labor market (European Commission 2016). These measures have shown little effect thus far, however, with fixed-term employment still strongly prevalent in these countries. This can be explained by the fact that, with structural labor market reforms, there is a considerable time lag between implementation and impact. The country comparison ultimately shows that the function of fixed-term employment cannot be ascribed entirely to one institution such as employment protection. In countries like Germany, France, and Sweden, it can be observed that a very similar level of employment protection is accompanied by different levels of mobility. The Scandinavian countries, especially, achieve both high transition rates out of unemployment and good advancement opportunities for fixed-term employees. This can be attributed to, among other factors, these countries' high investment in education and training in the framework of Lifelong Learning, as well as to their active labor market policies. A mobile labor market thus requires, not least, high investment in a flexible workforce.

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Policy Brief 2015/05: Brexit – potential economic consequences if the UK exits the EU

If the United Kingdom (UK) exits the EU in 2018, it would reduce that country's exports and make imports more expensive. Depending on the extent of trade policy isolation, the UK's real gross domestic product (GDP) per capita would be between 0.6 and 3.0 percent lower in the year 2030 than if the country remained in the EU. If we take into account the dynamic effects that economic integration has on investment and innovation behavior, the GDP losses could rise to 14 percent. In addition, it will bring unforeseeable political disadvantages for the EU – so from our perspective, we must avoid a Brexit.

Policy Brief 2015/07: Technological change and employment polarization in Germany

The generally positive employment development in the German labor market over the last two decades has been accompanied by a qualitative change in employment structures. While the middle of the job market has stagnated, employment has grown particularly within low-paid and less-skilled jobs, as well as within the high-wage sector. These tendencies toward polarization have been relatively weak; however, there is sign of an increasing labor-market cleavage, particularly with regard to the expansion of atypical employment. These developments can be attributed to the substitution of routine tasks in the course of technological change and globalization, as well as to institutional changes in the German labor market since the early 2000s.

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