

# How can Europe promote labour force participation and reduce income inequality?

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In June 2010, the Europe 2020 strategy replaced the Lisbon strategy that had guided European social and employment policy over the previous decade. The Europe 2020 strategy continues the main themes, focused on economic inclusion and territorial cohesion, but also responds to current realities, including the economic downturn and climate change.

To meet the challenges of the Europe 2020 strategy, policymakers must understand which approaches work in what context. With the assistance of initial project funding from the Directorate-General for Employment, Social Policy and Equal Opportunities at the European Commission, RAND Europe assessed two key components of both the Lisbon and Europe 2020 strategies – promoting labour force participation and reducing income inequality – aiming to identify past trends, understand what is driving them, and show how they could inform future policies.

## What did the review of labour force participation show?

The review shows that European policymakers have had to respond to important trends shaping labour markets over the last 30 years – including an increase in educational attainment, a shift towards more service sector employment and white-collar jobs, increasing female labour force participation and demographic changes. During the Lisbon strategy period, the study concludes that upward pressure on wages steadily decreased, employment rates increased and unemployment rates fell. Such improvements in overall employment and growth in the decade to 2007 shifted attention towards specific vulnerable groups – such as the young and old and migrants – whose integration in the labour market could be improved.

The 2008 economic crisis reversed many improvements in employment and growth across Europe. Not surprisingly, vulnerable groups are at particular risk of being in neither employment nor education at times of economic crisis, and they may find it especially difficult to re-enter

## Abstract

A review of progress on labour force participation and income inequality in the Lisbon strategy over the last decade shows the importance of focusing on vulnerable groups – such as the young and old – who are not well integrated into the labour market and are likely to be worse off since the economic crisis starting in 2008. Improving labour force participation will require investment in the education and skills of specific groups at risk. Progress on inequality requires a range of policies and the tackling of specific types of inequality, such as within-group inequality. This study identifies challenges and suggests ideas for policymakers to improve the situation.

the labour market when economic conditions improve. Achieving the targets set in the Europe 2020 strategy will require continued targeting of such groups. Their employment strengthens social inclusion and reduces welfare expenditure.

To target such vulnerable groups successfully, policymakers must understand what keeps them out of the labour market now and whether targeting one group will negatively affect another. Our study focused on how the key trends mentioned above affected labour force participation of younger workers (defined as 16–24 years old) and older ones (55–64 years old). The older group have low labour force participation rates. Increased employment rates would allow them to remain productive and relieve pressure on social security systems. Younger people not in education or work are at great risk of long-term unemployment. Therefore both groups justify the attention of policymakers.

The study finds that, while increased educational attainment and the shift to service sector employment are associated with an overall increase in the probability of young people working compared to the baseline (young people

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RAND Europe  
Westbrook Centre  
Milton Road  
Cambridge CB4 1YG  
United Kingdom  
TEL +44.1223.353.329  
FAX +44.1223.358.845

37, Square de Meeus  
B-1000 Brussels  
Belgium  
TEL +32.2.791.7500  
FAX +32.2.791.7900

Chris van Stolk  
stolk@rand.org

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in full-time education), the same trends also increase the chances of specific groups of young people ending up excluded, not in school and not working. Managing the consequences of the move towards white-collar jobs for older people is another issue. There is an increased probability they will stop working and retire, since their skills may need updating. What works to promote the participation of one group may not harm the other. The study shows no significant trade-offs between increased female participation and the employment of younger and older workers, for example (for an overview of these effects on employment rates, see table below).

### Associations between labour market trends and employment rates of the young and old

Labour market trends	Expected effect on employment rates	
	Young	Old
Demographic change	Negative	Positive
Changes in female participation	None	Positive
Increase in educational attainment	Positive	Positive
Move towards service sector jobs	Negative	Negative
Move towards higher-skilled and white-collar jobs	Positive	Negative

### What did the review of income inequality show?

Sustained income inequality matters to European policymakers as it can limit the opportunities of certain groups. Over the last decade, average income inequality at the pan-European level has changed little. But large variations appear between countries, exacerbated by the 2008 economic crisis. Also, several groups in specific European Member States are still at a significant risk of poverty, including women, older people, single-parent families and jobless households.

The review also shows that, contrasting with the US, Europe has a particular issue with inequality within groups, meaning that groups with the same education, age, gender and sector profiles are showing higher degrees of wage inequality. Within-group inequality is often associated with flexible labour markets, which allow part-time and flexible working arrangements.

Reducing income inequality can have wider effects such as improved perceptions of well-being and better social relations. Lower income equality is not necessarily associated

with lower employment, which means addressing income inequality does not necessarily lead to labour market distortions.

### What can be done to improve the situation?

The aftermath of the economic crisis of 2008 has undone much of the progress on improving employment and growth in Europe over the last 20 years. To achieve its Europe 2020 objectives, Europe needs to address the labour force participation of vulnerable groups and reduce income inequality across groups and regions. Sustained differences in labour force participation and income inequality between Member States may undermine European cohesion and the process of European integration.

The question remains what specific policy responses are available to European policymakers. Here the evidence is more limited. Our review can say something about the general principles of European policy: for instance, for the younger and older populations, it is important – given current trends – to intervene early, to keep the young in employment or school, to upgrade or learn to exploit the skills of older workers across the lifecycle of employment and to promote employment in general. Labour force participation rates in vulnerable groups will also benefit from general improvements in the overall rate of employment. Labour force participation is also a key element in addressing sustained income inequality. To combat within-group inequality, policymakers could provide basic income support and a higher guaranteed minimum income.

These policy principles imply an increased focus in welfare provision on enabling social policy or social investment targeted to specific groups at risk of exclusion from the labour markets or of poverty. Evidence from Nordic countries shows that the increased use of enabling social interventions can effectively mitigate against social risks such as sustained poverty and long-term unemployment. Moreover, as the review highlights, these targeted policies do not need to impact other macroeconomic outcomes or groups.

To make progress at the European level, Member States need to learn from the best performers among them. Action at European level is important to facilitate the exchange of best practice and information on what works, with the aim to seek convergence in how employment and social policy is formulated. This aim is challenging given the limited European mandate in this area, but seems imperative in ensuring a competitive and inclusive Europe in the future. ■

This research brief describes work within RAND Europe documented in MG-1068-RE *Life after Lisbon: Europe's challenges to promote labour force participation and reduce income inequality* by Christian van Stolk, Stijn Hoorens, Philipp-Bastian Brutscher, Priscilla Hunt, Flavia Tsang and Barbara Janta (available at <http://www.rand.org/pubs/monographs/MG1068.html>)

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