

The European Youth Guarantee. An Italian Perspective

di Francesco Pastore

The EU Parliament and other EU institutions are considering very seriously the possibility to adopt for all member states a model of management of the labor market that is typical of the Central and Northern European countries. With the obligation of the state to provide young people with a job, training or educational opportunity within three months from the beginning of their unemployment spell, the European Youth Guarantee (EYG) implies a radical change in the way of thinking the labor market in Mediterranean countries in general and in Italy in particular. In the latter, it is entirely up to the individuals and their household to design the best educational attainment level and an effective school-to-work transition strategy for their children. When Public Employment Services (PES) exist, they are very inefficient in Italy. Pro-active schemes cover only a small share of the young people in need and are of very low quality. Much too often a temporary employment contract is the only chance offered to them.

When talking about the EYG, observers often distinguish between macro- and micro-economic factors of youth unemployment and therefore of solutions. Aggregate demand management (or the fight against austerity) is considered to be opposed to structural reforms. Quite often observers contrast one type of policy with the other. Some observers, especially in Central and North-European countries, call for an aggregate demand policy, rather than structural reforms, which are considered to be useless when one needs to deal with a high youth unemployment rate. The EYG does not create new jobs is the argument. Other observers, generally from the right-wing side, argue just the opposite: aggregate demand policy will not work unless there is more flexibility in the labor market and we reduce the cost of labor.

In fact, both arguments own some rights and, especially when the youth unemployment rate is very high like it actually is in Italy, it is clear that interventions on both levels are necessary. When unemployment is so high, in fact, all of its components coexist in reality: Keynesian unemployment, neoclassical unemployment, as well as frictional and mismatch unemployment. Keynesian unemployment is due to insufficient aggregate demand: in the last years, youth unemployment has increased because of the low growth. Without stimulating economic growth, the EYG is bound to fail as a tool to bring full employment. Nonetheless, youth unemployment was already high in the countries where it has increased more, such as the Euro-Mediterranean countries. The reason is that in these countries also other components of youth unemployment are important.

On the one hand, without some fiscal stimulus, the economic outlook will not be favorable to the fight against youth unemployment. Nonetheless, an important point to bear in mind is that not any public spending will do it. Public spending has increased in many Mediterranean countries in the last years, sometimes dramatically increasing the public debt. All Mediterranean countries have experienced a dramatic worsening of the budget constraint on public finances. In Italy, public debt has increased over a few years from 103 to 130 of GDP. And nevertheless, youth unemployment has further escalated. This means that not any public spending is helping youth unemployment. In fact, increasing public debt may be (though it does not always need to be) recessive if it further

increases taxes and if the new taxes weigh eventually on labor incomes, hence depressing the already very low consumption level. With the Maastricht criteria, public deficits soon become recessive for the economy because it is immediately followed by taxes. "Spend and tax" becomes almost instantaneous, not only because of the rational expectations of operators, as some macroeconomists would argue, but also because of the EU constraints on public debt. A discussion on aggregate demand policy cannot escape the problem of where to find the necessary financial resources and therefore either on the instruments to fight tax evasion and elusion or on an in-depth spending review. It is clear that the European Parliament should elaborate criteria to implement an effective spending review both at the EU level and at a country level in order to free public resources for the implementation of the EYG. Labor income earners – the working and middle class – already pay too much in tax and need alternatives to raising taxes on them to support social expenditure. Otherwise, it becomes a vicious circle which will quickly put under threat our democracies, as the last Italian elections suggest.

A possibility could be that Italy is allowed to spend the money of the structural fund and other funds allocated to them and that they currently cannot spend on implementation of the EYG. This money is currently out of reach because of the low absorption capacity and also because the criteria are very hard to fulfill for peripheral countries. Why should the EU Parliament not allow Mediterranean countries to reinforce the PES or to finance proactive labor market schemes? This would be a more effective way of reaching the declared aims of the EU funds than using them in the way they are currently used. They tend to finance a number of small projects that Central and North European countries help renovate the current way of working of the PES, but in Italy and other Mediterranean countries they are almost totally ineffective because they do not have well-functioning institutions.

What criteria should a spending review follow in Italy? To answer this question, it is important to consider that the origin of the crisis lies in the Euro, which has produced many benefits, but also some problems that many countries, especially the Mediterranean countries, have not been fully aware of. The move from a weak to a strong currency, from competitive devaluations to permanent monetary stability has meant a dramatic loss of competitiveness for the manufacturing sector which is the backbone of Italy and the other Mediterranean economies. It is necessary to facilitate the ongoing structural change by providing tools to move resources from the declining low technology to the expanding high technology sectors. The money should be cut from traditional sectors and concentrated on promoting education, research and development and innovation. Industrial policy should be resumed to move resources and jobs from traditional to high tech manufacturing. These measures will not have a direct impact on neoclassical unemployment, which is due to the high cost of labor for firms. The cost of labor is not only the net wage, which goes to workers, but also the wedge, namely the tax on labor, the expenditure on social security and other types of social and health assistance. It is important to reduce this type of costs for firms also because it is going to increase the disposable income of employees. We can fight neoclassical unemployment also by reducing Keynesian unemployment if resources are freed from other, less productive, public spending.

But also structural reforms should be encouraged. Without them, frictional and mismatch unemployment will remain high. Structural reforms will have several positive effects. First, they will reactivate a lot of jobless young people, not only the unemployed, but also the ones completely out of the labor market. In turn, this will increase the number of tax payers and, indirectly, consumption by generating a redistribution of resources from high to low incomes and especially to the unemployed. This is in fact a pre-condition for a really expansionary fiscal policy.

Also before the crisis exploded, Mediterranean countries experienced a dramatically high unemployment rate. One direction for a modern New Deal able to unite the low with the middle class could be that of increasing the public expenditure on developing services which have been excluded from the welfare state in Southern Mediterranean countries. It is not by chance that in Germany about 13% and in the UK about 7% of new jobs are found through public employment

services, whereas in Italy only 3% of workers find their job through the public and private employment services. In fact, in Germany there are only 25 unemployed per staff of the PES, in the UK this number goes up to 30, but in Italy it reaches the remarkable threshold of 500 unemployed. That's an argument that people from Central- and Northern European countries do not consider. For them, the EYG is natural; PES work pretty well and there is a problem of reducing a little bit the expenditure in passive and pro-active schemes. In Italy, youth unemployment is very high because the educational system and the labor market do not provide sufficient guidance to young people. If the EYG could bring up the number of young people who find a job through the PES it would already be a success. And a full understanding of the inefficiencies of the educational and training system of Mediterranean countries strongly suggest that these jobs would be additional, not substitutive to the existing jobs.

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