Labour market flows: Accounting for the public sector

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Idriss Fontaine[5], Ismael Galvez-Iniesta[4], Pedro Gomes[1,3] and Diego Vila-Martin[2]

[1]Birkbeck, University of London, [2]University of Amsterdam, [3]Centre For Macroeconomics,
[4]Universidad Carlos III de Madrid, [5]Universite de La Reunion

In developed economies, 10 to 35 percent of all workers are employed by the government. Government hire workers to produce goods and services. However, governments face different constraints than private-sector firms and are not driven by profit maximization. Hence, government employment and wage policies are driven by other objectives including: attaining budgetary targets, implementing macroeconomic stabilization, redistributing resources or satisfying interest groups for electoral gains. As a consequence, public-sector labour markets might behave differently from their private-sector counterparts.

We establish a number of key facts about the French, Spanish, UK and US labour market over the past 15 years, focussing on the role played by the public sector. We chose these four countries because they are large countries with sizable public sectors, and have been recently facing pressure to reform their public sectors. Furthermore, because they have different labour market institutions, public-sector hiring procedures and wage policies and various weights on different industries, facts that are found to be common across the four countries should be seen as intrinsic characteristics of the public sector. While we do not attempt to explain these facts, we believe that they are an important first step to foster theoretical research on the topic. They can help economists understand the characteristics of the public sector and its policies. We show that public-sector labour markets do indeed behave differently than the private sector.

We provide evidence on the size of stocks and the worker flows between public and private employment, unemployment and inactivity, and how they very over the business cycle. In France and the UK, the public sector represents 21 and 23 percent of total employment, respectively. Spain and the US have smaller public sectors, representing 16 percent of total employment. There is 30 to 50 percent less worker turnover in the public sector relative to the private sector. In each quarter (month in the US), the probability of a worker losing his job is 2-3 times higher in the private sector. In each quarter (month in the US), 20 percent of unemployed workers find a job in the private sector, but only two to three percent find a public-sector job. There are few direct transitions between the public and private sectors: 60 to 85 percent of the new hires in the public sector come from non-employment.

The government hires mostly women, college graduates and older workers, which create asymmetric exposures to public-sector policies for different workers. The public sector accounts for

20 to 30 percent of total employment of women; 20 to 40 percent of employment of college graduates; and 20 to 25 percent of employment of older worker. The public sector hires few young workers or workers with only a primary education.

In the last decade in European countries, public-sector employment was a key fiscal policy variable. Following budgetary constraints, many countries imposed measures such as hiring freezes layoffs of public-sector workers, as well as wage cuts or freezes that affected the retention of these workers. We quantify how government hiring and separations have contributed to unemployment fluctuations. We find a relative split of 80-20 percent of the contribution of private- and public-sector employment to fluctuations in the unemployment rate in UK, 85-15 in France and of 90-10 percent in Spain and the US. We also show that since 2008, holding private-sector behaviour constant, public-sector employment policies contributed to higher unemployment rate in France and UK between 2010 and 2015, by 1.1 and 0.9 respectively. On the other hand, they contributed to lower unemployment rate in Spain and US by 1.3 and 0.8 percentage points.

We document that jobs are safer in the public sector. The argument that public-sector jobs are safer is often used in policy discussions surrounding public-sector pay. However, while there are several papers estimating the wage differentials across sectors, there are no estimates of the value of the job-security. We use a simple back-of-the-envelope calculation to find the percentage of their wage that private-sector workers would be willing to forgo to have the same job-separation probability as in the public sector. In our preferred scenario, workers would pay 0.5 to 2.9 percent of their wage for the job security of the public sector. This is equivalent to between 0.4 to 0.7 percent of total government spending in France and between 0.2 to 0.4 percent in the UK, Spain and the US.