

Azure no. 34, Autumn 5769 / 2008

Who Needs Job Security?

By Omer Moav, Ofer Cohen

The benefits of a flexible labor market.

In early November 2006, the union of temporary employees at Israel's Ben-Gurion International Airport declared a strike that left the country's gateway to the world virtually incapacitated. Airport baggage handlers, who had taken over the sorting area and barricaded themselves inside it, refused to load or offload cargo, delaying flights and forcing thousands of furious travelers to wait for hours to pick up their luggage. The pretext for the strike was the Israel Airports Authority's announcement that it intended to fire one hundred twenty *provisional* workers, who had been employed for less than five years. In response, the union declared that its members would not return to work unless the more senior temporary workers were given tenure—that is, immunity from dismissal. The leader of the strike, social activist Dr. Ami Veturi, declared in a press release that “we demand what is necessary for every person in Israel: a decent livelihood, job security, and a respectable life.”¹

The baggage handlers' strike at Ben-Gurion airport, terminated after several days by an injunction of the National Labor Court, ultimately failed to achieve its goal. Nevertheless, the strike demonstrated just how important “job security” is to large sections of the Israeli workforce. A steady job, after all, provides the worker with a livelihood over an extended period of time. No less important, it affords a sense of security and psychological well-being that is monetarily unquantifiable. It is not surprising, therefore, that a survey published in May 2007 by BDI, an Israeli company specializing in business and marketing information, found that Israeli workers, as a rule, prefer job security to higher wages.²

In fact, Israeli employees enjoyed a particularly high level of job security for many years, largely on account of the centralized character of Israel's economy during the early decades of the state. Collective agreements made between Israel's labor federation, the *Histadrut*, and other labor unions with their employers—most notably the government—provided far-reaching protections to a significant segment of the workforce. These agreements and the extension orders that followed them, as well as subsequent Israeli employment legislation, have made the process of firing workers cumbersome, lengthy, and expensive.³ Additionally, the practice of granting tenure to long-term employees has become commonplace in the public sector and is viewed by many workers as a major advantage over private employment. The prospect of immunity from dismissal after only a few years of work compensates for the less-than-glorious salaries offered by government jobs.⁴

To be sure, since the late 1980s, the Israeli economy has undergone sweeping changes, resulting in the decline of organized labor.⁵ Nonetheless, the number of workers benefiting from job security—while steadily declining—remains substantial. Nearly 800,000 workers are employed in the Israeli

public sector, almost a third of the total workforce.⁶ Over 80 percent of these workers are covered by collective agreements that grant them immunity from dismissal. Some workers in the private sector, especially those who are unionized, also enjoy similar arrangements, though on a much smaller scale.⁷

Naturally, the changes that have taken place in the Israeli labor market have been cause for concern among social activists. Faced with the decay of the old, centralized, and inflexible employment model, these activists are struggling relentlessly to preserve workers' traditional employment protections. Many of them continue to identify job security with collective agreements that grant workers the privilege of tenure, and with legislation that restricts an employer's capacity to dismiss his employees.⁸ From the activists' viewpoint, the abolition of these mechanisms is simply malicious, transforming workers into what member of Knesset Shelly Yachimovich of the Labor party called a "poor, desolate, and defenseless population."⁹

Despite the grain of truth in these warnings, which indeed merit some attention, the overall picture of the changing Israeli economy is far more complex. Both empirical and theoretical research shows that, in truth, inflexibility in the labor market causes significant economic and social damage. Not only does it impede economic growth and lower the general standard of living, it also extracts a heavy price from the weaker elements of society, making it increasingly difficult for them to improve their condition. Other countries have already learned this lesson, and some, such as Denmark, have adopted alternative welfare policies that provide workers with income security *without* undermining the flexibility of the labor market. As we will argue in what follows, if Israel wishes to position itself at the forefront of the global economy *and* maintain its moral stature in the process, it must learn from the experience of these countries and act accordingly.

Any discussion of job security—or more precisely, labor-market inflexibility—and its impact on a country's overall economic performance must adopt a wide perspective. That is, it must take into account not only the characteristics of the local economy, but also the position it occupies, or strives to occupy, in the global market. From this panoramic viewpoint, it is evident that the sclerotic disposition of the Israeli labor market saps Israel's social and economic strength.

While the moral and social significance of the changes brought about by globalization can be debated, the new reality they have created—and the unavoidable choice it presents—is beyond doubt: adapt or be left behind. The ever-increasing integration of the world economy on account of the free international exchange of goods, capital, information, and human resources unquestionably leaves many victims in its wake, but it also continuously generates new opportunities. Both multinational corporations and individual entrepreneurs seize these opportunities, for example, to transfer production facilities from developed to developing countries, which offer cheap labor and other economic incentives. For developed industrial economies, this process is painful but necessary. On the one hand, relocation of production centers to the Third World reduces the demand for unskilled labor and consequently raises unemployment—at least temporarily. On the other hand, the

general rise in living standards across the globe is accompanied by a demand for technologically advanced exports, and the skilled labor necessary to produce them. Thus, a country that wishes to reap the fruits of globalization and achieve high growth rates has no choice but to adapt swiftly to the dynamic global economy and utilize its comparative advantages effectively.

However, a country's ability to compete successfully on a global scale depends to a large extent on the flexibility of its labor market. When employers are relatively free to hire and fire their workers, they are capable of responding promptly to economic changes and, as a result, can reallocate resources from less profitable sectors of the economy to other, expanding industries. By contrast, in countries with high dismissal costs and restricted managerial flexibility, it becomes immensely difficult for employers to increase the efficiency of production and incorporate technological innovations.¹⁰ As a result, they may find themselves on the losing side of the intense competition that now typifies international trade.

In addition to hindering the efficiency of production, an inflexible labor market discourages capital investment. Entrepreneurs are thus far from eager to invest heavily in businesses that suffer from a lack of managerial flexibility. As a result, potentially profitable ideas are abandoned because employers fear the prohibitive cost of firing workers should the need arise. Entrepreneurs thus prefer to focus on lower-risk projects, at the expense of efficient resource allocation. Alternatively, they may choose to invest their resources in other countries that offer preferable conditions for setting up and managing a business.¹¹

Advocates of job security claim that tenure increases motivation by providing employees with a sense of partnership in their employers' success.¹² Experience, however, proves otherwise. Workers who know that for all practical purposes they cannot be fired do not appear to feel particularly motivated. The only exception is those cases in which advancement is contingent upon performance. Unfortunately, in workplaces where tenure is granted, opportunities for advancement are limited from the outset, since workers in management positions enjoy tenure arrangements as well and are in no hurry to vacate their positions.¹³

A brief overview of the Israeli public sector reveals the extent to which tenure agreements have become a breeding ground for inefficiency and underemployment. The dynamics of this phenomenon were explained in an article published in *Haaretz* in April 2003:

Managers in the public sector report that a worker's productivity usually rises in the period immediately following tenure approval for an average of one year. During that period the worker feels a sense of commitment to the superior who recommended tenure and strongly identifies with his workplace. After a year to a year and a half, however, the worker's productivity stabilizes and slowly begins to decline. The sense of security which tenure creates instills a certain apathy in the worker. After several years, managers say, tenure becomes the kiss of death.¹⁴

This observation should hardly come as a surprise. Complaints from managers in the public sector

regarding unjustified absences and outrageous work ethics are regularly voiced in the Israeli media. For example, Israel Broadcasting Authority (IBA) chairman Moshe Gavish, originally from the private sector, was shocked by the disorderly workplace at the IBA. In an interview with *The Marker* in July 2007, he said:

This place has technicians who can start working at 5 P.M. and write down that they have been working since 8 A.M. Since this is what has been established in the [collective] salary agreement, they are not writing that for no reason. It is because of these people that whenever I was interviewed... six people [from the IBA] would show up—while two people would come from Channel 2, and one from Channel 10. This was required under labor agreements signed by my predecessors. They established that a reporter in the IBA works four days and doesn't work on Thursday or Friday but receives a salary for those days, which is calculated as overtime to boot. People agreed not to introduce new equipment, because that would render the technicians superfluous.¹⁵

Former director of the Israeli Finance Ministry's Wages and Labor Accords Unit, Yuval Rachlevski, has also strongly denounced the conduct of workers in the public sector: "The public service is riddled with lies and misrepresentations. It is all done in broad daylight, without shame or any qualms over the long, greedy arm picking the public purse."¹⁶ In addition to being a disgrace and a constant source of aggravation for those in need of public services—which is to say, the entire population of Israel—such displays of inefficiency, apathy, indolence, and, at times, even greed have disturbing economic consequences. After all, a decline in worker motivation leads to low productivity and detracts from the quality of public services. Ultimately, this harms the overall production capacity of the economy.

Undeniably, high worker turnover is not without its shortcomings. Reducing the average time that employees spend working in a particular field prevents them from gaining experience and discourages employers from investing in professional training. Nevertheless, the disadvantages of the opposite policy, which allows employees to become careless and incompetent, are far greater than its benefits. This can be seen, for example, in a broad study published last year by economists Andrea Bassanini and Danielle Venn. Analyzing data collected in member states of the Organization for Economic Cooperation and Development (OECD) between 1979 and 2003, the study examined, among other things, the impact of employment protection legislation (EPL) on total productivity levels.¹⁷ Bassanini and Venn found that as worker protections grew stronger and more encompassing, the growth rate of labor productivity decreased.¹⁸

There is no escaping the uncomfortable fact that although an “un-fireable” worker enjoys a sense of security, he or she also tends to become progressively more inept and thus fails to drive the economy forward. In an age of globalization, such cumbersome drawbacks can cost a society dearly, and evidence suggests that those who will pay the highest price are precisely those who cannot afford to.

Elected officials and social activists who campaign for job security argue that it is a social policy that protects the weak and the needy. A closer examination, however, reveals that such a policy usually has the opposite effect: Instead of creating opportunities for employment and financial well-being, it reduces them; and instead of improving the wretched state of the poor, it perpetuates it.

One does not have to be a professional economist in order to understand this problem. Managerial inflexibility reduces production efficiency; as a result, it inevitably cripples the growth of a country’s Gross Domestic Product (GDP), undermining the welfare of society in general. Unfortunately, the underprivileged sectors of society, whose dependence on government largesse is especially great, suffer the heaviest blow. Government entitlement payments constitute a major source of income for these segments of society, which are unable to afford such essential services as education and healthcare on their own. A low level of economic growth reduces government earnings from taxation, thereby limiting the government’s ability to provide a high level of public services. Ultimately, it makes generous entitlements for the needy impossible.

The overall damage to society as a result of stringent and inflexible employment policies is not limited to the problems cited above. In addition to reducing the quality of public services provided to the poor, such policies also deny the underprivileged access to employment. As we noted above, potential employers are less likely to fire employees when the process of dismissal is long, complicated, and costly. The desire to avoid exorbitant compensation costs tends to dissuade managers from employing additional workers, and it deters entrepreneurs from investing in projects that create jobs. Low turnover rates reduce the number of job openings and, consequently, generate fewer opportunities for those seeking employment.¹⁹

It is clear that such a situation benefits only those who are already employed. Weaker groups are

shut out of the job market and often find it difficult to secure an adequate income. Young people, women returning to the workforce after raising children, and immigrants do not benefit from stringent employment protections. In fact, they are actively harmed by them. An interesting example of this was presented by a World Bank study that examined the effects of new severance-pay legislation in Chile. The study demonstrated unequivocally that young people and unskilled laborers were the first to be adversely affected by such legislation. Because their productivity relative to other groups is low, and their earnings are near minimum wage, the heightened cost of dismissal makes it unprofitable to employ them. As a result, they are eventually pushed out of the workforce.²⁰ Adriana Kugler, an economist from the University of Houston who has studied the performance of the labor markets in the United States and Europe over the past decades, stated that

Employment protection generates redistribution from unemployed toward employed, from younger and female workers to middle-age and male workers, and possibly from unskilled toward skilled workers.... This means that the elimination of employment protection regulations may not only be desirable from an efficiency point of view but also from the point of view of generating redistribution toward less protected groups.²¹

This conclusion is supported by many empirical studies, all of which undermine the claims of Israel's social-justice lobby that its efforts in defense of collective agreements and employment tenure are carried out in the name of equality.²² In fact, these regulations only *intensify* the distress and frustration of those who do not benefit from equally effective protections. Even labor-union officials admit that tenure disenfranchises the weaker classes of society. In an interview with the Israeli website Ynet in 2001, Yaakov Zlotnik, former chairman of the Histadrut's Department for Professional Association, said, "the problem is that today, those who are paying the price for the improved conditions of the senior workers are the new workers, who have to wait for years in order to receive tenure and better conditions."²³

Tenure regulations and the high cost of dismissal not only reduce the number of job opportunities, however. They also motivate employers to search for cheaper alternatives. Many times they find what they are looking for in secondary labor markets operated by service providers and temporary employment agencies. These agencies hire workers to perform specific tasks for low wages without social or supplementary benefits. The secondary employment model, which increases flexibility in the short-term labor supply, has become more and more widespread in recent years.²⁴ It is viewed by policymakers as an effective arrangement that improves the rate of economic growth without disrupting the status quo established with permanent workers and the unions that represent them. The problem, however, is that the social costs of this arrangement are far too high.

Indeed, studies show that an ever-increasing reliance on temporary workers can *raise* unemployment rates instead of lowering them. The reason is simple: Employers prefer laying off temporary workers and hiring others in their place rather than paying the high costs of employing them on a permanent basis. In these cases, a high turnover rate does not create new long-term jobs, but only temporary positions. This makes it difficult for job-seekers to find steady employment.²⁵ Moreover, the secondary labor market tends to perpetuate existing social inequalities, since the widespread use of

temporary employment usually reduces investment in workers' training. This, in turn, lowers temporary workers' chances of finding future employment. Finally, in order to make themselves more attractive to potential employers, these workers are forced to accept lower wages. According to data from the Israeli Central Bureau of Statistics, the average monthly salary of contract workers in Israel in 2005 was NIS 4,300—about 60 percent of the average wage of NIS 7,000.²⁶ The primary victims of this form of employment are, once again, the weakest segments of the population—the undereducated, new immigrants, minorities, young people, and women—all of whom are overrepresented in Israel's secondary labor market.²⁷

Unfortunately, the widespread use of contract workers is not limited to the Israeli private sector. Over the past few years, it has become increasingly popular in government offices and the public sector in general. This trend merely adds insult to injury: By making use of subcontractors and temporary employment agencies, the government is granting de facto approval to the mistreatment of temporary workers. As a result, the government is betraying its basic commitment to the well-being of the weaker classes of society and increasing the harm already inflicted upon them by the stringent regulations that protect the public sector's tenured employees.

Ironically, the use of subcontracted labor is an unmistakable byproduct of Israel's extremely inflexible labor market. The well-meaning activism of job security advocates has thus paved the way for the rise of what is essentially a modern slave trade, operating under lawless and immoral conditions. In light of this gloomy reality, the only possible response is a profound restructuring of the Israeli labor market.²⁸ In considering how this might be accomplished, we can learn a great deal from the successes and failures of other countries faced with similar dilemmas.

Although the development of the Israeli economy has been greatly influenced by its unique political, social, and cultural history, there is nothing unique about its problems. They have troubled and continue to trouble many other developed countries. In fact, the majority of Western industrialized economies, especially in Europe, have experienced firsthand the negative consequences of an inflexible labor market.

Of course, these countries do not exercise uniform employment policies. If we were to judge their economies by the level of protection they offer to their workers, we would find Portugal, Italy, Germany, Spain, Sweden, and Greece, with their generous tenure benefits, at one end of the spectrum. At the other end we would find the United States, Britain, Australia, Canada, Switzerland, and New Zealand, which have relatively high turnover rates.²⁹ This division helps to delineate two distinct political and economic models. On the one hand, there is the European welfare state, which attempts to protect workers and the general public from economic hardship by, among other things, regulating labor relations. On the other hand, there is a free-market economy that seeks to increase prosperity by promoting competition and entrepreneurship.

The United States is the quintessential example of an economy of the latter kind, as its employees do not enjoy any extensive income or welfare protection. The extraordinary flexibility of the American labor market stems from a combination of factors. First and foremost, American legislation greatly simplifies the dismissal process: Accepted legal doctrine holds that an employer can fire a worker at any time and for any reason, so long as there is no contract between the parties that explicitly prevents him from doing so.³⁰ Second, American legislation does not require the employer to provide a dismissed employee with severance pay, unless compensation of this kind is included in a written agreement between employer and employee.³¹ Third, the practice of tenure is uncommon in the American labor market, and the average seniority of the American worker is significantly lower than that of his European counterpart.³²

Furthermore, in order to encourage people to work, eligibility for unemployment payments in the United States is limited to twenty-six weeks. In addition, in order to receive them, an unemployed worker needs to meet several requirements: He must, for example, demonstrate that he was not responsible for his dismissal and that he is actively seeking employment. The guidelines for this program are set by the United States Department of Labor and limit the term of eligibility, which different states may shorten but not lengthen. Like the practice in other countries, including Israel, unemployment benefits are not uniform. The actual sum is calculated according to the applicant's salary during the fifty-two weeks prior to filing the request and according to the number of quarters of the business year during which he was fully employed. In this manner, if a worker's income was low in the time period prior to his dismissal, he discovers that the safety net offered by unemployment benefits is not sufficiently generous to replace, even temporarily, a salary earned on the job—motivation enough to find new employment quickly.³³

These practices are largely responsible for the high turnover rate in the American economy, and they are the main cause of the sizable gap between the unemployment rate in the United States, which has fluctuated between 5 and 6 percent over the past few years, and the much higher rates characteristic of European economies.³⁴ In 1992, following decades during which the European countries suffered from an average unemployment rate of 10 percent, the OECD initiated a comprehensive study to investigate the causes of this problem and suggest ways to alleviate it. The study's findings, published two years later, received widespread attention. The report found that unemployment in Europe was a structural phenomenon stemming from difficulties in adapting to globalization. In addition to reforms in the education and welfare systems, its authors recommended restricting the scope of collective agreements and decreasing the level of job protection in order to expand the ability of the labor market to absorb new workers.³⁵

Despite the fact that in recent years European countries have implemented a series of measures designed to reduce unemployment on the continent, the job security reforms that were implemented were only partial and somewhat indecisive. They tended to focus on increasing the availability of part-time and temporary employment opportunities while leaving standard employment arrangements unaltered. The reason for this, at least in some cases, was a general fear of union reaction. An excellent example of this problem is France's failed attempt to reduce its unemployment level—which

in 2006 stood at 23 percent among youths under the age of twenty-five—through the relaxation of some protections against dismissal.³⁶ Early in the same year, French prime minister Dominique de Villepin proposed legislation that would create a new form of association between employer and employee. Called the First Employment Contract, the law allowed employers to hire workers under the age of twenty-six for a two-year trial period during which they would be permitted to dismiss them without having to justify their actions or pay high severance costs. The public outcry against the initiative was dramatic. A coalition of trade unions, leftist organizations, and students protested the law through mass civil disobedience, bringing over a million protesters into the streets. The intense pressure created by the demonstrations had its desired effect: On April 10, 2006, French president Jacques Chirac retracted the law and announced that it would be replaced with “other measures.”³⁷

Several European countries, however, most notably Denmark, have more effectively tackled the problem of an inflexible labor market. Like other welfare states on the continent, Denmark also experienced an extended period of economic hardship, but it has managed to overcome this challenge with astounding success. The testimony of the man who was largely responsible for this accomplishment, former prime minister Paul Nyrup Rasmussen, speaks to the magnitude of the achievement:

When I became prime minister of Denmark in 1993, unemployment had reached a twenty-five-year high of 13 percent, coupled with low economic growth and high public debt. By the time I left power in 2001, employment was at the highest level in Europe at 76.6 percent, and unemployment had fallen below 4 percent.... Despite having no natural resources and no single dominant company, Denmark is now among the most competitive economies in the world.³⁸

Why was Denmark able to succeed where other welfare states have failed? The answer lies in the unique employment model it adopted in the 1990s. The Danish model, termed “flexicurity,” combines a flexible employment policy on the one hand with social security on the other. This combination is achieved through coordination and cooperation between the major players in the Danish economy—parties who, in another country, would be bickering with one another.

It must be stressed that Denmark’s labor market is one of the most organized in the world. Approximately 80 percent of Danish workers are organized into trade unions. Collective agreements regulate working conditions for all public sector employees and for nearly 80 percent of private sector employees. Nevertheless, legislation regulating employment is minimal. Denmark has avoided restrictions on freedom of association between employers and employees. Under such conditions, negotiations over collective agreements can easily become a battleground between competing interests. But the situation in Denmark is unusual. Dialogue between employers and labor unions is founded on mutual understanding and a shared sense of responsibility for the state of the economy. As a result, both parties are committed to avoiding unilateral actions, such as strikes.³⁹ This kind of cooperation enables Denmark to engage in long-term economic planning, control inflation, and limit spending while still safeguarding employment conditions.⁴⁰

According to an understanding reached between Danish employers and labor unions, managers are permitted to dismiss workers quickly and without exceptional expenses. This allows the Danish labor market to be heavily unionized while remaining one of the most flexible in Europe. The average seniority of a Danish employee is one of the lowest on the continent. The Swedish average, for example, is 50 percent higher. While Denmark's high turnover rate results in the dismissal of a relatively high number of employees each year, the relative simplicity of the process also allows for the swift creation of new jobs. This greatly increases the proportion of dismissed workers who are soon rehired elsewhere. In fact, between 25 and 35 percent of the Danish workforce changes its workplace each year.⁴¹

On the surface, the dynamics of the labor market in Denmark resemble those of the United States, but there the resemblance between the two ends. Denmark has not ceased to be a welfare state. It has increased the flexibility of the labor market while simultaneously bolstering the social safety net that grants generous unemployment benefits to the unemployed. Moreover, the state has established employment-training centers that teach unskilled workers—or those seeking professional retraining—the tools they need to be quickly re-employed. In order to avoid weakening the incentive to work—a chronic problem in other European welfare states—Denmark has also shortened the period of eligibility for unemployment benefits, but it has *not* reduced the size of the benefits themselves. Although the cost of this safety net is high and requires correspondingly high taxation levels, Danish employers willingly accept it, because it reinforces their collaboration with the labor unions, ensures their freedom to hire and fire their employees, and enables them to promote their initiatives efficiently.⁴²

In the final analysis, the Danish “flexicurity” model benefits the general public without discriminating against the poor. It supports those who have lost their source of income or lack the ability to support themselves, yet more readily allows for the integration of underprivileged groups into the labor market. This policy is psychologically beneficial as well. Surveys demonstrate that Danish workers feel a greater sense of security in comparison with their counterparts on the continent. A study conducted in 1997, for instance, found that the average proportion of European workers who were apprehensive about their income stood at a massive 70 percent. In contrast, only 43 percent of Danish respondents reported similar anxieties.⁴³ A survey conducted ten years later found that only 5 percent of Danish workers felt insecure about their jobs.⁴⁴

The Danish example demonstrates that “managerial flexibility” and “job security” are not necessarily incompatible. A competitive market economy can adopt dynamic employment regulations that allow for high turnover rates, while simultaneously maintaining the country's humane character and its basic commitment to the welfare of its citizens. Why not attempt the same experiment in the ailing Israeli labor market?

No one disputes the fact that job security, in and of itself, is a worthy cause. Employment fulfills workers' material and spiritual needs: It provides them with the means required for life and enhances their stature in their own eyes and the eyes of their peers. The ability to earn a respectable living is

not a luxury, but a fundamental human right that every just society should recognize and protect.

Security, however, does not have to mean inflexibility. A labor market that has become overly rigid as a result of tenure arrangements, strong labor unions, and the high cost of firing workers creates, at best, an illusion of stability. In reality, it impedes economic development, impairs the general standard of living, and sabotages the ability of the underprivileged to integrate into the workforce. Moreover, it motivates employers to search for alternative hiring models that exploit the distress of the unemployed. In a world of fierce global competition and ever-accelerating technological advances, a lack of managerial flexibility may produce devastating economic and social consequences.

Fortunately, over the last twenty years, the Israeli labor market has become progressively more flexible. This process, however, has been riddled with obstacles and characterized by instability, tension between employers and employees, recurring strikes in the public sector, and the widespread and inappropriate use of contract workers in various industries. Notwithstanding the noteworthy achievements of the Israeli economy, which has seen an average growth rate of 5 percent in the past few years, it continues to suffer from social afflictions that can no longer be ignored. Many Israeli workers live with a persistent and often debilitating sense of uncertainty about their future, while large segments of the population struggle to make ends meet or find themselves unemployed.

This situation requires critical attention. Israel must implement a large-scale reform of its labor market. Such a reform should not permit aggressive free-market competition to dictate the living conditions of workers. On the other hand, it must not shackle the economy and impose centralism and sclerosis. In order to avoid both of these undesirable outcomes, policymakers need to learn from the experience of other countries, most especially from the Danish success story. The concept of job security must be understood in a manner conducive to present economic and social conditions as well as the challenges presented by an era of global competition.

Every future reform in the labor market must take into account that protecting workers does not necessarily mean protecting their employment at a particular workplace. Lawmakers and labor unions must accept shared responsibility for the overall benefit of society and allow entrepreneurs and employers the freedom to replace and mobilize workers in order to invest their resources as efficiently as possible. This will both improve the public welfare and expand the job market. At the same time, the government must fulfill its responsibility for ensuring that its citizens are capable of earning a living. It should be obvious to all that a committed and generous investment in human capital is an economic, social, and moral necessity that no country can afford to ignore.⁴⁵ Should Israel choose to follow the path of reform and devote the necessary effort to obtaining it, it will not only enrich its economic potential, but also increase its moral stature as a society that embodies the highest ideals of solidarity and mutual support.

Omer Moav is a senior fellow at the Shalem Center and a professor of economics at the Hebrew University of Jerusalem and Royal Holloway, University of London. Ofer Cohen is pursuing a master's degree in economics at the Hebrew University of Jerusalem.

Notes

The authors wish to thank Hadas Gabay and Yulia Horn for their generous help in researching this essay.

1. For the Israeli Army Radio report on the strike, see <http://news.msn.co.il/news/Internal/Internal/200611/20061103071959.htm> [Hebrew].

2. The survey, based on the answers of roughly fifteen thousand respondents, has been conducted

annually since 2005 and ranks the fifty best companies to work for in Israel. For the purposes of this survey, a representative sample of two thousand workers are asked to list the criteria that, in their opinion, constitute an attractive workplace. More detailed information can be found at BDI's 2007 "Analysis of Best Companies in Israel to Work For," www.bdicode.co.il/Articles/best%20companies_eng.pdf.

3. Legislation pertaining directly to this procedure includes the 1963 Severance-Pay Law, and the 2001 Pre-notice for Dismissal and Resignation Law. The latter determines the time period required for notification prior to ending a contract.

4. To date, this situation has not changed significantly, as noted by Haim Bior in an article published in *The Marker* over three years ago: "Even today, despite globalization, working for the public sector is attractive, mainly from the standpoint of job security. It is difficult to fire permanent workers in government offices, municipalities, or the Jewish National Fund because of the strong protection barriers placed on these workplaces: collective agreements imposing a myriad of conditions on management when dismissing an employee, and the existence of unions. In terms of salary conditions, the public sector is less attractive: Most workers earn between minimum wage (NIS 3,335 per month) and average wage (NIS 7,400 per month)." Haim Bior, "The Public Sector in Israel: Less Attractive But Still Alive and Kicking," *The Marker*, November 10, 2005 [Hebrew].

5. On this matter see Yinon Cohen, Yitzhak Haberfeld, Guy Mundlak, and Ishak Saporta, "Unpacking Union Density: Membership and Coverage in the Transformation of the Israeli IR System," *Industrial Relations* 42:4 (October 2003), pp. 692-711.

At the annual Tikva Conference, which took place in April 2007 in Tel Aviv, Histadrut Chairman Ofer Eini admitted that the number of Histadrut members has been in continuous decline over the previous two decades. According to Eini, the Histadrut had almost two million members at the beginning of the 1990s, a number which had dropped to only six or seven hundred thousand by 2006. According to data published last year by *The Marker*, 60 or 70 percent of Israeli workers in the early 1990s were union members. This has dropped to 27 percent today. See Haim Bior, "Fighting for the Continuation of Organized Labor," *The Marker*, April 27, 2007 [Hebrew].

6. Data valid for September 2007. See the Bank of Israel Research Department report from November 2007, "Recent Economic Developments 119: April-September 2007," p. 6, www.bankisrael.gov.il/develeng/develeng119/develeng.pdf.

7. Haim Bior, "When the Permanent Becomes Temporary," *The Marker*, April 28, 2003 [Hebrew].

8. See, for example, "Organized Labor Relations and the Teachers' Strike," a blog post by Ishak Saporta from Haoketz ("The Sting"), a social-activist website he co-edits, November 7, 2007, www.haokets.org/article.asp?ArticleID=2429 [Hebrew]. See also Daniel Gutwein, "The Soup-Kitchen Trend," Ynet, September 11, 2007, www.ynet.co.il/articles/0,7340,L-3448692,00.html [Hebrew]; and Guy Davidov, "Dismissal? Only with a Satisfactory Cause," *Haaretz*, August 23, 2005 [Hebrew].

9. For more on this issue, see the website of MK Shelly Yachimovich, www.shelly.org.il/wp/?p=1391

[Hebrew].

10. Hugo Hopenhayn and Richard Rogerson, "Job Turnover and Policy Evaluation: A General Equilibrium Analysis," *Journal of Political Economy* 101:5 (October 1993), pp. 915-938. See also Gilles Saint-Paul, "Is Labor Rigidity Harming Europe's Competitiveness? The Effect of Job Protection on the Pattern of Trade and Welfare," *European Economic Review* 41:3 (April 1997), pp. 499-506; and "Employment Protection, International Specialization, and Innovation," *European Economic Review* 46:2 (February 2002), pp. 375-395.

11. Eric Bartelsman, Andrea Bassanini, John Haltiwanger, Ronald S. Jarmin, and Thorsten Schank, "The Spread of ICT and Productivity Growth: Is Europe Really Lagging Behind in the New Economy?" in Daniel Cohen, Pietro Garibaldi, and Stefano Scarpetta, eds., *The ICT Revolution: Productivity, Differences and the Digital Divide* (Oxford: Oxford, 2004), pp. 1-140.

12. See, for example, Inbal Bar-On's response, "Tenure at the Workplace Serves Capitalism (the Real Type, Not the 'Bibi for the Vulgar Masses' Type)," *Interpretation* online, December 8, 2007, www.interpretation.co.il/10_1013.htm [Hebrew].

In this context, one needs to distinguish between the argument that holds that tenure in the workplace increases workers' motivation, and the argument regarding the "workers' sense of mission." The latter argument is reasonable, since certain employees—social workers or teachers, for example—are indeed motivated by the desire to contribute to society. Arguments that link tenure and positive motivation, by contrast, are not particularly convincing.

13. Andrea Ichino and Regina T. Riphahn, *The Effect of Employment Protection on Worker Effort: A Comparison of Absenteeism During and After Probation*, IZA Discussion Paper no. 385 (Bonn: Institute for the Study of Labor, 2001), <http://ftp.iza.org/dp385.pdf>.

14. Bior, "When the Permanent Becomes Temporary."

15. Yael Walzer, "Reform or [Hand In] a Billion Shekels," *The Marker*, July 13, 2007 [Hebrew].

16. Sari Makover-Belikov, "The Garbage in the Barn Is Cleaner than the Public Domain's Garbage," *Maariv*, July 8, 2005 [Hebrew].

17. In order to determine the degree to which employment protections are binding, OECD economists use the EPL index. The index, which is a rather complicated tool, takes several different factors into account, including protection for permanent workers from dismissal, special requirements for collective dismissals, and temporary employment regulation. For a detailed explanation, see *OECD Employment Outlook 1999: Giving Youth a Better Start* (Paris: OECD, 1999), ch. 2, annex 2.B, pp. 115-118, www.oecd.org/dataoecd/9/46/2079974.pdf.

Total-factor productivity is the measure of an economy's production capacity for a given supply of production factors. This measure is primarily affected by the efficiency of the production process and the level of technological development. An increase in total-factor productivity is therefore of paramount importance to the process of economic growth.

18. Andrea Bassanini and Danielle Venn, *Assessing the Impact of Labor Market Policies on Productivity: A Difference-in-Differences Approach*, OECD Social, Employment and Migration Working Paper no. 54 (Paris: OECD, 2007), www.iza.org/conference_files/MeLaMa_2007/bassanini_a1425.pdf.

19. Most empirical research has not been able to establish a definite correlation between stringent employment protections and unemployment levels. See, for example, *OECD Employment Outlook 2004* (Paris: OECD, 2004) ch. 2, www.oecd.org/dataoecd/8/4/34846656.pdf. The main effect of labor-market stringency is on employment levels, where the data point to a strong negative effect. When the number of available jobs shrinks, a significant proportion of job-seekers simply give up and, as a result, are no longer defined as unemployed.

Unemployment rates are defined as the proportion of jobless persons among labor-force participants, which includes the unemployed plus those in civilian employment. The rate of employment is the number of active workers proportionate to the entire working-age population. As a result, the rates of employment and unemployment do not add up to 100 percent. That is to say, there are individuals of working age who are not part of the workforce and are therefore not included in the employment rate or the unemployment rate.

20. Claudio E. Montenegro and Carmen Pagés, *Who Benefits from Labor Market Regulations? Chile 1960-1998*, Working Paper no. 494 (Washington, D.C.: Inter-American Development Bank, 2003), <http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=788314>.

21. Adriana D. Kugler, "The Effects of Employment Protection in Europe and the USA," *Els Opuscles del CREI* 18 (February 2007), p. 39.

22. See, for example, Olivier Blanchard and Pedro Portugal, "What Hides Behind an Unemployment Rate: Comparing Portuguese and U.S. Labor Markets," *American Economic Review* 91:1 (March 2001), pp. 187-207. Also see Ramón Gómez-Salvador, Julián Messina, and Giovanna Vallanti, "Gross Job Flows and Institutions in Europe," *Labour Economics* 11:4 (August 2004), pp. 469-485; and *OECD Employment Outlook 2004*.

23. Nurit Wurgaft, "Unstable Worker, Available for a Relationship," Ynet, October 1, 2001, www.ynet.co.il/articles/1,7340,L-1160568,00.html [Hebrew].

24. According to the Ministry of Industry, Trade, and Labor, the number of people working for employment contracting agencies in Israel is at present around 115,000, which is about 4.5 percent of the total number of employees in Israel. See Niv Hachlili, "4.5 Percent of Employees Are Contract Workers," *NRG Maariv*, December 11, 2007, www.nrg.co.il/online/16/ART1/669/963.html [Hebrew]. The 2006 report of the Association for Civil Rights in Israel quotes unofficial evaluations estimating the number of contract workers at 10 percent of the total—in contrast to 2 percent in Europe. See Michal Tadjer, *Working Without Dignity: The Violation of Workers' Rights in Israel* (Jerusalem: The Association for Civil Rights in Israel, 2006).

25. This happened, for example, in France. As part of a reform aimed at increasing labor-market flexibility three decades ago, wider use of "temporary contracts" was permitted. These contracts

allowed employers to hire workers for a fixed period of time and then to terminate the contract at low cost. A study conducted by Olivier Blanchard and Augustin Landier demonstrated that this reform failed to achieve its goals: Workers' turnover increased, yet the average period of unemployment was not shortened significantly. Overall, Blanchard and Landier concluded that the temporary contracts only worsened the situation of French workers. See Olivier Blanchard and Augustin Landier, "The Perverse Effects of Partial Labor Market Reform: Fixed-Term Contracts in France," *Economic Journal* 112:480 (June 2002), pp. F214-F244.

26. According to data from the Central Bureau of Statistics published on the Ministry of Industry, Trade, and Labor website, www.moit.gov.il/NR/exeres/FA45C129-00DE-4BB7-BD42-87B7A3A4C07E.htm; also found in Hachlili, "4.5 Percent of Employees Are Contract Workers."

27. Ronit Nadiv, *Employment Through Temporary Employment Agencies, Israel 2000* (Jerusalem: Ministry of Labor, Agency for Human Resource Planning, 2003), pp. 30-34. Also available at www.tamas.gov.il/cmstamat/Rsrc/koach/tichnun_koach_adam/tichnun_pirsumim/pir_skirot/xkablan.pdf [Hebrew].

Regarding the situation in other developed countries, see Lawrence M. Kahn, "The Impact of Employment Protection Mandates on Demographic Temporary Employment Patterns: International Microeconomic Evidence," *Economic Journal* 117:521 (June 2007), pp. F333-F356.

28. An absorption clause in the Temporary Employment Agencies Law came into effect on January 1, 2008, after having been approved by the Knesset in 1996. According to this clause, workers at temporary employment agencies are to be put on the company payroll after nine months of work. Supposedly, this constitutes an improvement in the condition of temporary workers. In practical terms, however, employers can bypass the law in several ways: For example, temporary employment agencies can easily become service-providers, which are not covered by the legislation. Furthermore, implementation of the clause may increase turnover rates among temporary employees, as it gives managers a clear incentive to terminate their employment before the nine-month deadline, leading to a rise in collective dismissals. See Ruth Sinai, "New Law Set to Make Longtime Temps Permanent Staff," *Haaretz*, January 1, 2008.

29. *OECD Employment Outlook 1999*.

30. Mark A. Rothstein, Andria S. Knapp, and Lance Liebman, *Cases and Materials on Employment Law* (New York: Foundation, 1987), p. 738. This doctrine, of course, has certain legal boundaries. Starting in 1941, several state and federal laws were implemented in the United States forbidding dismissal on the basis of discrimination as well as protecting the right of association and activities aimed at exposing corruption in the workplace. Legislators in several states have affixed additional restrictions: (1) An employer may not fire an employee for reasons that violate a state's public policy; (2) employers may not violate the rights of workers which have been established in an implied contract agreement between them; (3) dismissals made in bad faith or involving unfair dealings are prohibited. See Charles J. Muhl, "The Employment-at-Will Doctrine: Three Major Exceptions," *Monthly Labor Review* 124:1 (January 2001), pp. 3-11.

31. See the website of the United States Department of Labor,

www.dol.gov/dol/topic/wages/severancepay.htm.

32. Peter Auer, Janine Berg, and Ibrahim Coulibaly, "Is a Stable Workforce Good for the Economy? Insights into the Tenure-Productivity-Employment Relationship," *International Labour Review* 144:3 (2005), pp. 319-343.

33. See the website of the United States Department of Labor regulations, <http://workforcesecurity.doleta.gov/unemploy/uifactsheet.asp>.

34. Kugler, "The Effects of Employment Protection," pp. 1-6.

35. *The OECD Jobs Study: Facts, Analysis, Strategies* (Paris: OECD, 1994).

36. Ofra Shalev, "International Insecurity," *The Marker*, October 2006, p. 79 [Hebrew].

37. "France to Replace Youth Job Law," BBC News, April 10, 2006, <http://news.bbc.co.uk/2/hi/europe/4895164.stm>.

38. Poul Nyrup Rasmussen, "The Danish Model of 'Flexicurity,'" *The Journal*, Premier Edition (2007), p. 46.

39. There are, of course, exceptions to this rule, such as the large strike of Denmark's private-sector workers during April-May 1998. The strike was declared following the failure of the negotiations between employers and the labor unions that demanded more vacation days, and ended on May 8, following government intervention. See "Parliament Intervenes to End Major Conflict," *European Industrial Relations Observatory* online, www.eurofound.europa.eu/eiro/1998/05/feature/dk9805168f.htm.

40. Soren Kaj Andersen and Mikkel Mailand, *The Danish Flexicurity Model: The Role of the Collective Bargaining System*, Compiled for the Danish Ministry of Employment, University of Copenhagen, September 2005, <http://faos.sociology.ku.dk/dokum/flexicurityska05.pdf>.

41. Thomas Bredgaard, Flemming Larsen, and Per Kongshøj Madsen, *The Flexible Danish Labour Market—A Review*, CARMA Research Papers, no. 1 (Aalborg, Denmark: Center for Labour Market Research, 2005), pp. 9-10, www.socsci.aau.dk/carma/carma-1.pdf.

42. Per Kongshøj Madsen, "The Danish Road to Flexicurity: Where Are We? And How Did We Get There?" in Thomas Bredgaard and Flemming Larsen, eds., *Employment Policy from Different Angles* (Copenhagen: DJØF, 2005), pp. 269-290.

43. *OECD Employment Outlook 1997* (Paris: OECD, 1997), p. 133.

44. "Danes Secure in Global Job Market," *The Copenhagen Post Online*, October 25, 2007, www.cphpost.dk/get/104093.html.

45. Underinvestment in human capital seems to be an inevitable consequence of relatively inflexible labor markets. Government intervention is therefore often required to provide basic education and

professional training. Such intervention can be assisted by private companies and would fulfill the basic needs of employers, the unemployed, and the public purse.