Labour market reforms and inequality in Italy

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1. Overview

When we look at the macroeconomic indicators related to the Italian labour market over the last decade, at first glance, we could speak of an economic miracle. Table 1 indicates a significant increase in employment, irrespective of whether we consider jobs (2.5 million) or people (almost 3 million). In this table, we contrast information for the year 1996, immediately after the wave of labour market reforms, which started the following year and the most recent year unaffected by the financial crisis (2007). Most of this change occurred in dependent employment, and drew a corresponding number of the working age population into the workforce. This huge increase in employment was made possible by a slow-down in productivity growth (which increased by half a percentage point per year) accompanied by a stagnation in real wage growth (a yearly increase of 0.7% over the sample period).

Table 1 – Labour market indicators - Italy 1996-2007

	1996 Before the reforms	2007 After the reforms	Absolute difference	% Change
total employment (labour standard units - jobs)	22520	25025	2505	11.12%
dependent employment (labour standard units - jobs)	15494	17899	2405	15.52%
total employment (heads - persons)	20279	23222	2943	14.51%
dependent employment heads - person)	14327	17167	2840	19.82%
unemployed	1542	1035	-507	-32.88%
first job seekers	1004	471	-533	-53.09%
labour force	21799	24257	2458	11.28%
unemployment rate	12%	6%	-5%	-41.67%
first job seekers/labour force	5%	2%	-3%	-60.00%
employment rate (>14)	42%	46%	4	9.52%
GDP deflator (factor costs - index)	93	120	27	29.03%
nominal contractual wage (index)	94	119	25	26.60%
productivity (real value added per employed- index)	95	101	6	6.32%
real wage (index)	96	106	10	10.42%
nominal labour cost (euro)	26682	35275	8592	32.20%
nominal wage (gross - euro)	18531	25810	7279	39.28%
real wage (gross - euro)	20075	22027	1952	9.72%

An increase in employment without wage pressure is a rather exceptional event in standard economic theory. In a competitive framework it is compatible with an infinitely elastic labour supply, as was the case in the fifties of the last century, where the estimated internal migration of more than four million workers from rural areas in Southern regions made possible the take-off of a modern industrial sector in the Northern regions. In a non-competitive framework with union presence, however, expansion in employment is always accompanied by increased wage pressure due to the reduced risk of unemployment. Only when wage and employment are bargained together (in the models of so-called 'efficient bargaining'), risk-adverse workers may require more employment growth than wage increases.

In the sequel, we will consider whether this may represent a potential explanation of the observed evidence. Before doing so, we consider some structural problems characterising the Italian labour market, which remained almost unaffected despite the 'employment miracle'. The first problem concerns the differences in regional patterns of employment and unemployment. Tables 2 and 3 indicate the rise in the employment rate was unevenly distributed over the country. The Central regions

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gained 5 percentage points in their employment rate, followed by the Northern regions. Within each macro-area, the female component reduced its distance from the male counterpart. Even so, the female employment rate in Southern regions is half that of the corresponding male rate and well below the Lisbon target of an overall employment rate of 70% by 2010, with the specific target of an employment rate for women of over 60%.

Table 2 – Employment rate (population aged 15–64)

	North			Centre			South			Italy		
	male	female	total	male	female	total	male	female	total	male	female	total
1996	71.2	45.2	47.3	67.6	39.1	42.8	58.1	23.0	35.7	66.2	38.2	52.2
1997	71.1	45.8	47.4	67.6	39.3	42.8	58.0	23.1	35.6	66.1	38.5	52.3
1998	71.5	46.7	47.7	67.7	40.2	43.0	58.5	24.0	36.1	66.5	39.4	53.0
1999	72.3	48.2	48.4	68.4	41.8	43.7	58.6	24.1	36.0	67.0	40.5	53.7
2000	73.1	49.9	49.2	69.1	43.4	44.4	59.5	24.6	36.5	67.8	41.8	54.8
2001	73.6	51.5	49.8	69.6	45.1	45.1	60.4	26.1	37.3	68.4	43.4	55.9
2002	74.0	52.5	50.3	70.5	46.0	45.8	61.2	27.0	37.9	69.1	44.4	56.7
2003	74.6	53.4	51.0	71.4	46.9	46.8	61.4	27.1	37.8	70.0	45.1	57.5
2004	75.0	54.9	50.8	71.9	50.2	47.3	61.8	30.7	37.4	69.7	45.2	57.4
2005	75.1	55.1	50.7	71.4	50.8	47.2	61.9	30.1	37.0	69.7	45.3	57.5
2006	75.9	56.4	51.4	72.9	51.3	47.8	62.3	31.1	37.4	70.5	46.3	58.4
2007	76.3	56.8	51.6	73.0	51.8	48.1	62.2	31.1	37.3	70.7	46.6	58.7
2008	76.2	57.5	51.7	73.0	52.7	48.3	61.1	31.3	36.9	70.3	47.2	58.7

Source: Labour Force Statistics

Table 3 – Unemployment rate (population aged 15–64)

	North			Centre			South			Italy		
	male	female	total	male	female	total	male	female	total	male	female	total
1996	4.1	10.0	7.0	7.2	14.1	9.6	16.7	29.4	18.5	8.7	15.2	11.2
1997	4.0	9.8	6.8	6.9	14.3	9.5	17.1	30.0	18.9	8.7	15.3	11.3
1998	3.8	9.4	6.6	6.9	13.6	9.3	17.5	30.8	19.6	8.8	15.4	11.3
1999	3.4	8.3	5.9	6.6	13.2	9.0	17.3	31.3	19.6	8.4	14.8	10.9
2000	3.0	7.1	5.1	6.1	11.6	8.1	16.3	30.4	18.8	7.8	13.6	10.1
2001	2.7	5.9	4.4	5.4	10.3	7.3	14.8	28.1	17.3	7.1	12.2	9.1
2002	2.7	5.8	4.3	4.7	9.4	6.5	14.1	26.4	16.3	6.7	11.5	8.6
2003	2.6	5.4	4.0	4.5	9.3	6.9	13.8	25.3	16.1	6.5	11.3	8.4
2004	3.0	5.9	4.3	4.9	8.7	6.5	11.9	20.5	15.0	6.4	10.5	8.0
2005	3.0	5.8	4.2	4.9	8.3	6.4	11.4	19.6	14.3	6.2	10.1	7.7
2006	2.8	5.1	3.8	4.5	8.2	6.1	9.9	16.5	12.2	5.4	8.8	6.8
2007	2.6	4.7	3.5	3.9	7.2	5.3	8.9	14.9	11.0	4.9	7.9	6.1
2008	2.9	5.2	3.9	4.6	8.2	6.1	10.0	15.7	12.0	5.5	8.5	6.7

Source: Labour Force Statistics

It is interesting to note that employment growth continued even in 2008, when the financial crisis unfolded in the final quarter of the year. However, traces of it are still visible in the increase in the unemployment rate, possibly due to an increase in the number of job seekers who were attracted by the brilliant performance previously experienced.

A second feature of the Italian labour market, and one often neglected in official accounts, is its high degree of flexibility. While official accounts tend to depict Italy as a rigid country[1], the indicators of turnover rates suggest a different view. If we look at table 4, we notice that the number of jobs that change holder in a year declined over the decade and remained higher in Southern regions. If we take these rates as evidence of the robustness of the employment relationship (which would also be consistent with turnover rates that are negatively correlated with firm size), we may suspect that the increased employment has increased the robustness of the employment relationship only where the

[1] However, OECD (Organisation for Economic Cooperation and Development) had to correct its official coding of the country over its EPL (employment protection legislation) indicator of rigidity, because of a mistake in the classification of severance payments – see OECD 2004.

labour market was close to full employment and that it has left the rest of the labour market in a fluid state.

Table 4 - Gross turnover rates (hiring+firing/quitting), by firm size and regions - Manufacturing

	total	20-49	50-199	200-499	beyond 500	North-West	North-East	Centre	South
2000	34,6	36,7	39,8	31,1	28,4	25,4	45,7	30,8	37,7
2001	34,8	37,0	37,2	33,0	30,4	25,3	43,0	32,3	42,2
2002	32,2	33,9	33,9	30,7	29,0	24,1	37,7	33,4	40,9
2003	29,9	34,2	30,6	27,4	25,8	23,8	31,5	30,0	34,2
2004	26,1	25,5	27,7	24,8	25,7	20,9	29,2	28,3	37,2
2005	24,0	25,4	24,4	23,2	22,3	18,3	24,7	26,7	35,3
2006	25,8	26,7	27,0	24,3	24,2	20,8	26,2	28,0	37,2
2007	26,4	26,2	28,8	25,3	24,4	22,0	27,1	29,8	37,0
2008	24,0	23,5	25,5	23,1	23,2	20,0	24,8	26,6	34,7

Source: Bank of Italy survey on firms

Last, but not the least, despite huge unemployment differentials, which should be reflected in the expected wages (though attenuated by significant differentials in the cost of living), internal migration is almost absent. This is partially offset by foreign immigration, which concentrates in the Northern regions where the labour market is particularly tight.

The overall picture of the Italian labour market is therefore contradictory. On one side we observe a remarkable performance in terms of employment growth. On the other side geographical differences persist or even widen over the sample period; on the contrary, the gender differential declines all over the country. These are indications that the labour market reforms that occurred in recent decades were able to modify the dynamics of employment generation, without, however, being able to reverse the historical patterns fully.

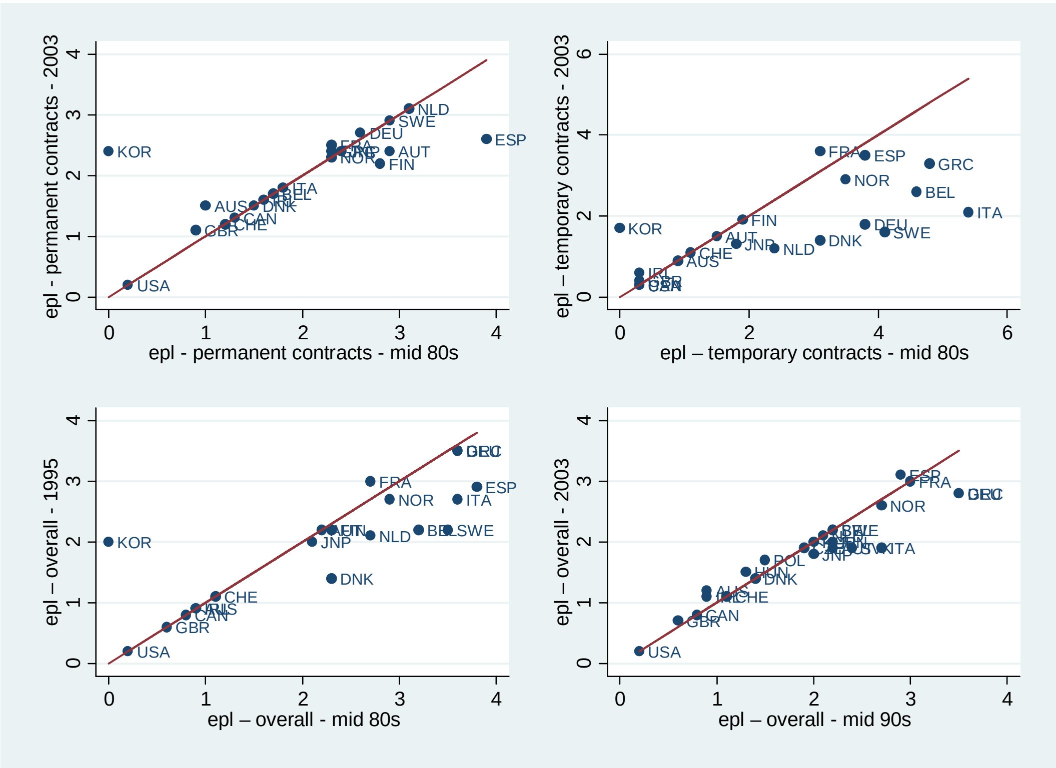
2. Labour market reforms in Italy

Labour market reforms took place in the second half of nineties in two waves of reforms. In July 1993, a social pact was signed between trade unions, employer confederations and the government, in order to introduce a wage freeze for one year and half, followed by a reform of the wage bargaining system, based on a 'two-tier' system (a national contract covering all workers, followed by firm level contracts signed where union power was able to start a bargaining process). The reform of the wage bargaining system officially cancelled the indexation clause (called 'scala mobile'), which had been in place since 1951, to be replaced by an official target in terms of the inflation rate, to be set by the government.
In the aftermath of the ensuing period of wage moderation, in June 1997 the centre-left government partially liberalised the entry wage for first job seekers and widened the number of valid cases for the use of Fixed Term Contracts.[2] In the following period (1998–2001) a series of labour laws introduced temporary work agencies and removed restrictions concerning unskilled workers. This process ended in February 2003, with the introduction of a wide variety of possible employment contracts, from staff leasing to job sharing.[3]
As a consequence of this wave of reforms, Italy can now boast of a very flexible labour market legislation, even if flexibility in theory does not necessarily means flexibility in practice. From the former point of view, Italy is currently classified as being as flexible as Japan (except for collective dismissals – see figure 1).

[2] Law 24/6/1997, n. 196 known as 'Legge Treu', from the name of the then Minister of Labour.
[3] Law 14/2/2003, n. 30 known as 'Legge Biagi', from the name of a government consultant who was killed by a terrorist organisation called Red Brigades.

As in many other countries, this wave of reforms had differential impacts in the labour market, through the introduction of a two-tier system. While the workers with permanent contracts were hardly affected by these reforms, marginal workers with temporary contracts and new entrants were more affected by the new legislation and possibly took advantage of it. Figure 1 plots the OECD (2004) indexes of employment protection legislation over different periods for different contractual situations, the underlying intuition being that, whenever a country lies on the diagonal, there is no change in the policy attitude of that country with respect to labour market legislation. In the top-left panel of figure 1, we clearly see that all countries (except Spain and Korea – Italy is, therefore, in the group) did not, over the sample period 1980–2003, change their policy stance with respect to permanent contract workers. On the contrary, the same countries reduced the degree of protection with respect to workers under temporary contracts (top-right panel), Italy being one of the countries that mainly reduced the degree of protection. Most of this change occurred in the first half of the nineties (bottom-left panel), although a few countries (Italy included) continued to reform even in the second half of the decade (bottom-right panel).

Figure 1 – Waves of labour market liberalisation – OECD countries



Source: data from OECD 2004

What were the consequences of the greater flexibility in the norms? If we look at the share of workers under temporary contracts (see table 5), we do not observe an increasing resort to temporary contracts, which seem to remain restricted to marginal tasks in the industrial sector, and become appealing to small-size firms in the service sector. More interesting is the observation of the recourse to temporary work agencies, which were fully liberalised in 2003 (see table 6). In these circumstances, large firms in the industry sector mostly took advantage of this opportunity, and expanded the share of work carried out under this form of contractual agreement.

Table 5 – Fraction of workers under temporary contracts, by firm size and regions

Industry (excluding constructions)

	total	20-49	50-199	200-499	beyond 500	North-West	North-East	Centre	South
1998	....	....	5,7	5,4	5,4	4,8	6,1	4,5	8,5
1999	....	....	6,1	5,0	5,1	4,9	5,9	4,7	8,1
2000	6,5	8,1	6,6	5,6	5,2	5,3	6,3	5,6	7,3
2001	6,5	8,1	6,2	5,9	5,7	4,7	6,7	6,8	7,4
2002	6,4	7,2	6,5	5,9	6,0	5,2	7,1	6,3	7,4
2003	5,9	6,5	5,9	5,6	5,6	4,6	6,7	6,2	6,7
2004	5,7	6,1	6,5	5,5	4,7	4,8	6,4	5,9	6,2
2005	5,7	7,1	5,6	5,6	4,2	4,1	5,8	5,5	6,3
2006	5,8	6,7	6,1	5,5	4,7	4,5	6,3	5,9	6,0
2007	6,0	6,1	6,5	6,4	5,1	5,6	5,9	6,1	7,0
2008	5,9	6,7	6,4	5,7	4,6	5,1	5,5	5,7	7,0

Private services (excluding finance)

	total	20-49	50-199	200-499	beyond 500	North-West	North-East	Centre	South
2001	8,9	9,4	11,1	7,0	7,7	9,0	10,0	7,3	7,4
2002	9,6	10,0	12,3	7,3	8,1	9,4	10,4	8,6	9,0
2003	9,3	10,1	11,3	10,1	7,3	8,1	11,0	8,0	10,5
2004	10,1	11,3	12,8	9,1	7,9	9,9	9,7	9,2	9,8
2005	10,2	10,2	13,2	7,8	9,0	9,2	11,4	10,0	10,9
2006	10,6	11,3	12,6	10,4	8,7	9,7	10,8	10,8	10,4
2007	10,5	11,1	11,2	11,5	9,2	9,2	11,2	11,2	10,3
2008	10,1	12,6	11,3	9,5	8,0	7,7	11,4	9,7	9,5

Source: Bank of Italy survey on firms

Table 6 – Fraction of workers from temporary work agencies, by firm size and regions

Industry (excluding constructions)

	total	50-199	200-499	beyond 500	North-West	North-East	Centre	South
1999	0,6	0,7	0,6	0,4	0,7	0,6	0,3	0,4
2000	1,1	1,0	1,2	1,2	1,3	1,1	0,8	0,9
2001	1,6	1,3	1,7	2,0	1,8	1,6	1,3	1,4
2002	1,7	1,5	1,9	1,9	1,7	1,9	1,5	1,7
2003	2,0	1,9	2,4	1,9	2,1	2,2	1,6	1,7
2004	2,1	1,8	2,6	2,2	2,4	2,1	1,6	1,9
2005	2,4	1,9	3,2	2,5	2,5	2,5	1,9	2,0
2006	2,9	2,5	3,3	3,0	2,8	3,3	2,4	2,5
2007	3,0	2,6	3,4	3,3	3,2	3,1	2,6	2,8
2008	3,1	2,7	3,8	3,0	3,4	3,1	2,5	2,5

Private services (excluding finance)

	total	50-199	200-499	beyond 500	North-West	North-East	Centre	South
2001	0,7	0,5	0,7	1,0	0,8	0,7	0,7	0,5
2002	0,9	0,5	1,4	1,1	1,1	1,0	0,8	0,6
2003	1,2	1,2	1,4	1,1	1,3	1,3	1,0	1,1
2004	1,1	1,2	1,1	1,0	1,3	0,9	0,9	1,2
2005	1,2	1,4	1,2	1,1	1,4	0,9	1,1	1,4
2006	1,3	1,4	1,0	1,3	1,7	1,0	1,0	1,2
2007	1,2	1,4	0,9	1,2	1,6	1,1	1,0	0,9
2008	1,4	1,5	1,2	1,5	1,7	1,4	1,3	1,1

Source: Bank of Italy survey on firms

By summing the employment shares contained in tables 5 and 6, we reach at a conclusion that the degree of precariousness in the Italian labour market remains limited and involves a share of non-standard workers that does not exceed 10%.[4] This implies that firms recruiting policies were not subverted by the greater availability of the norms. This may be either the result of pre-existing flexibility

[4] For a full discussion of the true size of non-standard employment, using different data sources, see Berton, Richiardi and Sacchi (2009).

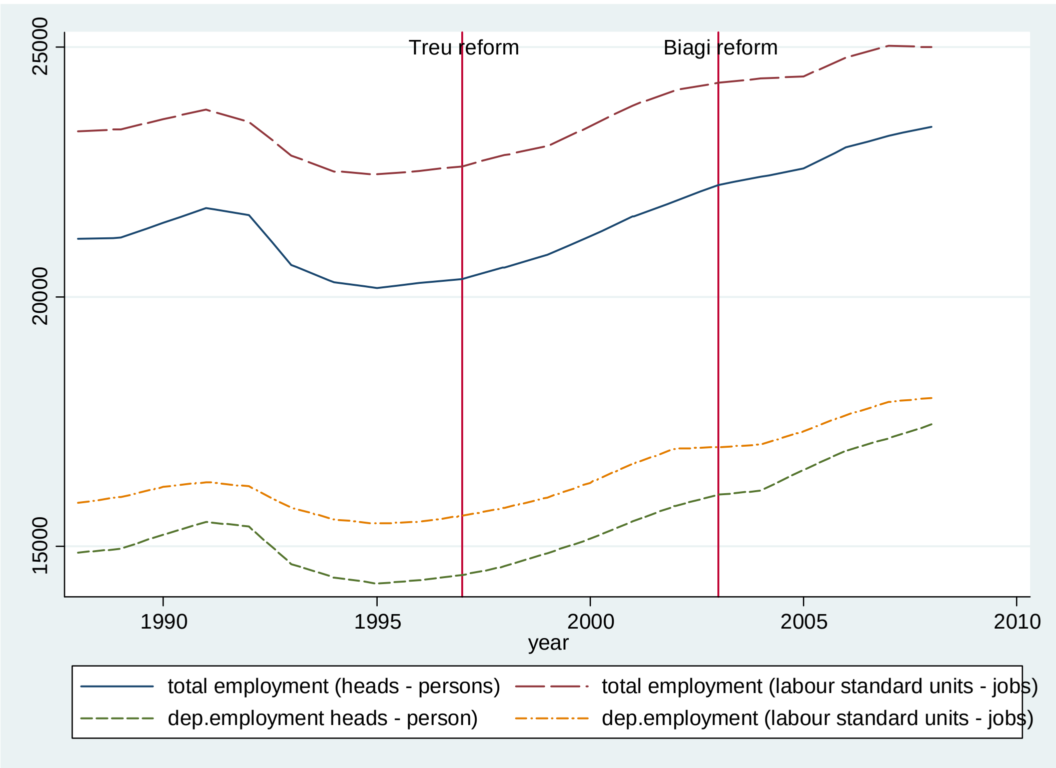
(Italian firms did not use more contractual flexibility because they did not need it), or the undesired effect of a partial reform (Italian firms did not resort to contractual innovation because they were prevented from doing so by union power, which has not been undermined by the new legislative set-up). These two stances have opposing implications: in the former case the implication would be ending the reform process because it has proved ineffective; in the latter case, the reform process should be strengthened, in order to overwhelm the unions and take advantage of fully fledged flexibility in norms.

Where the truth lies is difficult to say. My explanation considers unions as already weak at the beginning of the reform process, as evidenced by the wage dynamics (see next paragraph). They suffered these labour market reforms as partial defeats that they could not avoid, but they would have opposed them had they been able to. Firms were not prevented from expanding the share of non-standard employment contracts; they simply did not want to replace permanent workers with temporary ones. We should not forget the already high turnover rates reported in table 4. When a firm faces the problem of replacing an average of 2 workers out of 5 every year, it does not need additional flexibility to fire more workers: waiting a while would be sufficient to achieve the same result.

3. Employment impact of the reforms

Even if the reforms in labour legislation were unable to change the hiring/firing policies of firms (since we do not observe significant changes in employment composition), there is clear evidence in the data that these reforms were capable of reinforcing employment growth, which had already started (thanks to the wage freeze introduced in 1993 – see figure 2). From the 1995 trough to the 2007 peak, 2.5 million jobs were created (mostly in dependent employment) and more than 3 million people entered employment. However, a large fraction of these jobs was relatively fragile, since almost 800 thousand jobs disappeared in the 2009 crisis.

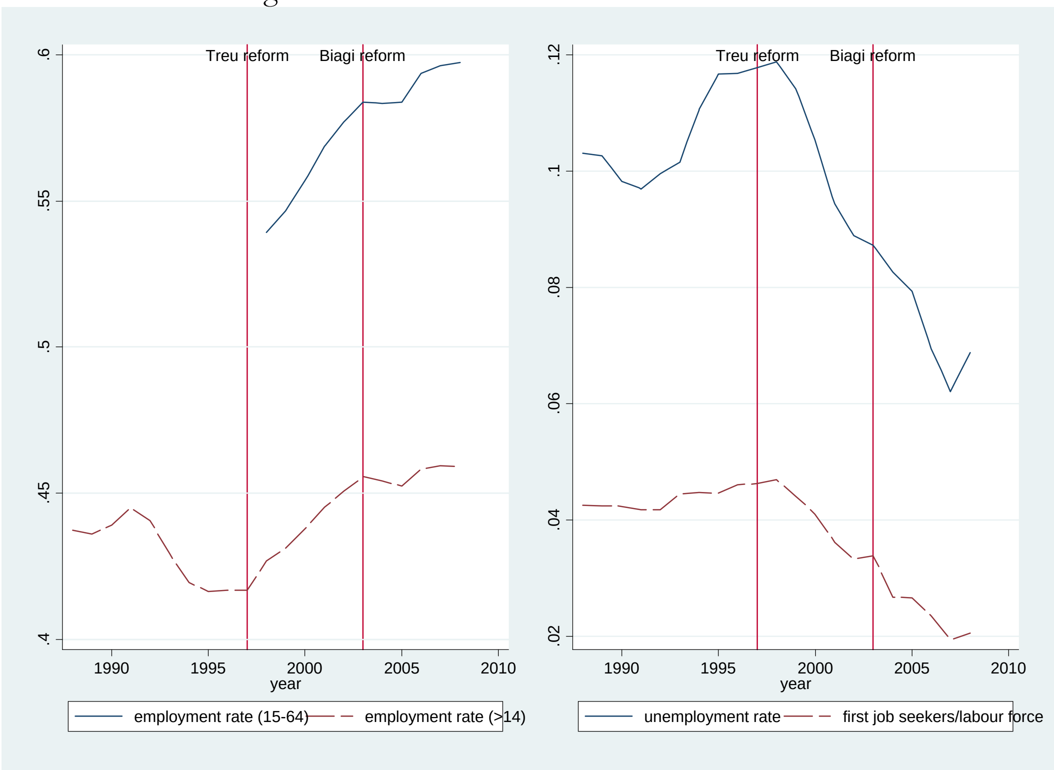
Figure 2 – Employment growth



Source: data from the Appendix to the Relazione del Governatore della Banca d'Italia (various issues).

If more rigorous tests are required, by looking at figure 3 we clearly see that the rise in the employment rate and the decline in the unemployment rate were triggered by the initial 'Treu' reform introduced in 1997, while the second 'Biagi' reform was effective only in continuing the drain of the unemployment pool, by easing the labour market transition of first-job seekers.

Figure 3 – Relevant rates for the labour market



Source: data from the Appendix to the Relazione del Governatore della Banca d'Italia (various issues).

Was a legislative reform sufficient to create new jobs? The answer is clearly negative. We have already seen that the share of those involved in more flexible contractual agreements remains limited, below 10% (see table 7), while dependent employment increased by almost 20%. If we look for an explanation of this pattern of employment growth, we need to pay attention to wage and productivity dynamics (see figure 4).

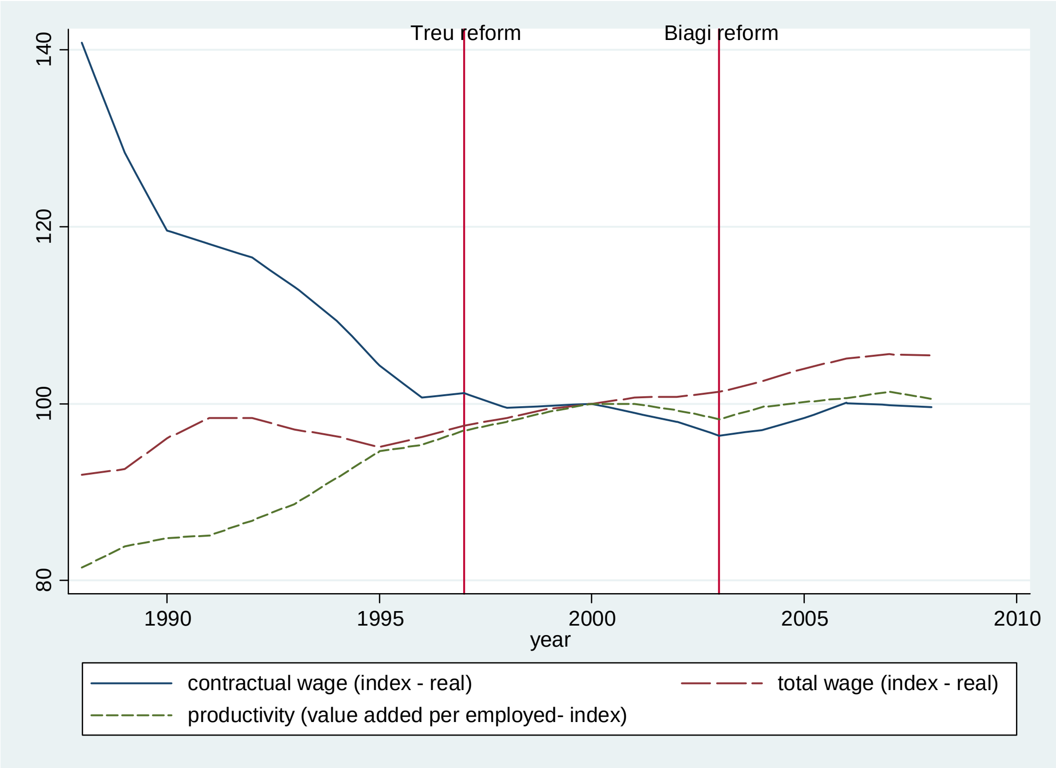
Table 7 – Types of employment – Italy 2008 – aged 15 or more

	Labour market condition					
	Dependent		Freelance (collaboratore a progetto, coordinato e continuativo, occasionale).		Self-employed	
	full time	part time	full time	part time	full time	part time
permanent contract	13086 (55.9%)	2037 (8.7%)			4940 (21.1%)	554 (2.3%)
temporary contract	2323 (9.9%)		465 (1.9%)			

Source: Source: ISTAT 2009. *Rapporto annuale 2008*. Rome. Prospetto 4.1

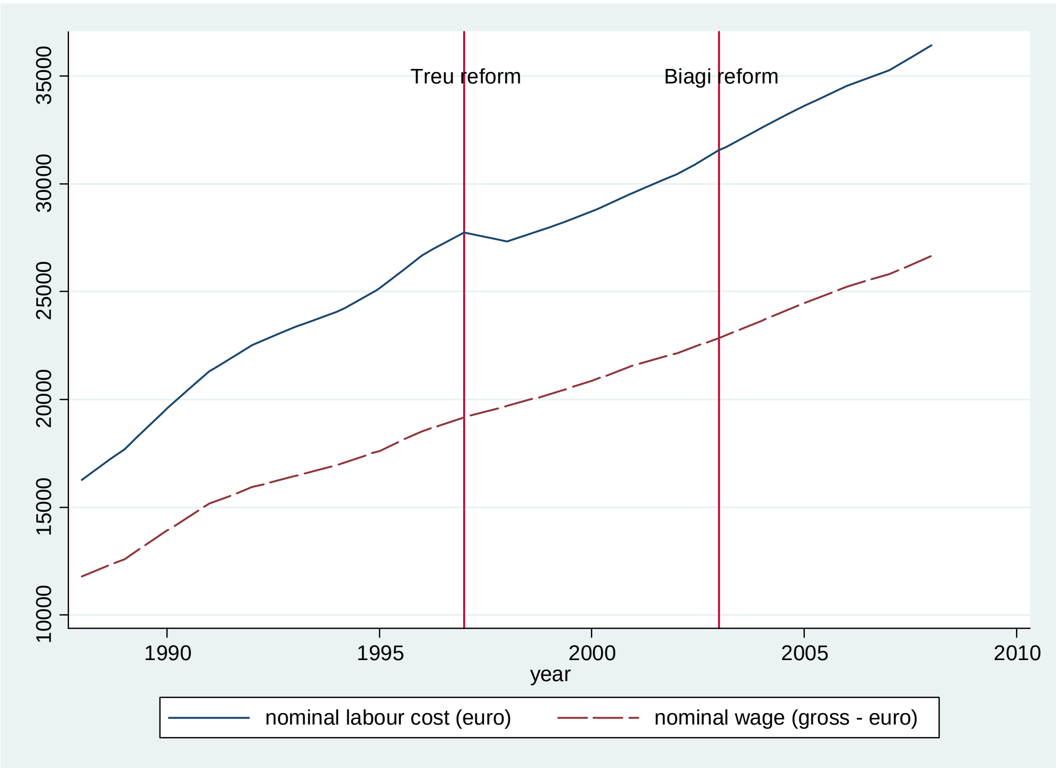
Employment growth appears as the outcome of the productivity slowdown observed since the year 2000, combined with the wage freeze following the 1993 tripartite agreement. As a consequence, labour costs were reduced in real terms (and in 1998 also in nominal terms, thanks to the partial exemption of payroll taxes – see figure 5). Stagnating productivity associated with declining real wages implies a declining labour cost per unit of output, which then explains why it was convenient for firms to hire more workers.

Figure 4 – Productivity and wages



Source: data from the Appendix to the Relazione del Governatore della Banca d'Italia (various issues).

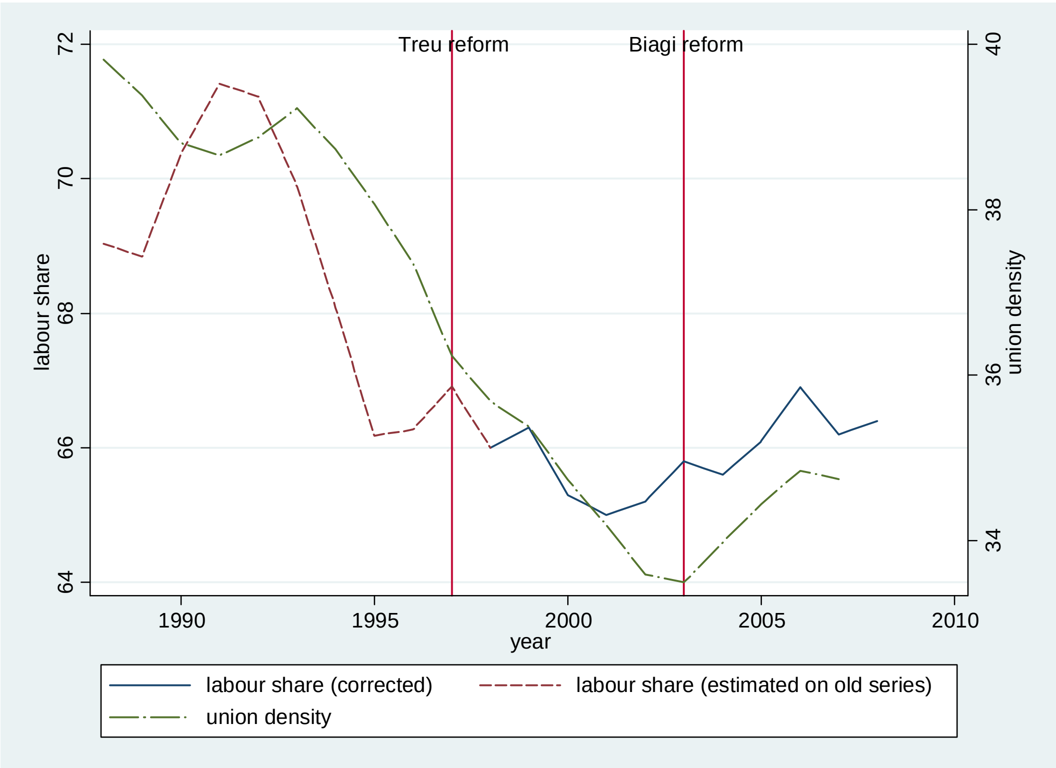
Figure 5 – Nominal labour cost and gross wage, per worker



Source: data from the Appendix to the Relazione del Governatore della Banca d'Italia (various issues).

The macro evidence for this claim is related to the dynamics of the wage share in gross domestic product, which was declining until at least 2001 (or 2002, depending on different data sources). Figure 6 shows an impressive correlation between union membership and labour share over the last two decades. The wage agreement signed in 1993 was effective in freezing the wage pressure, resulting in a decline of the labour share (corrected for self-employment). However, union confederations seem to have paid for their policy, because their membership declined significantly, at least relative to dependent employment. There may be additional reasons for this occurrence, from compositional effects (early retirement of blue-collar workers, entry of women) to increased competition from local/professional unions. However it is widely recognised that Italian unions have lost part of their appeal to potential members, and their lobbying capability.

Figure 6 – Labour share on value added and union density



Source: labour share from the Appendix to the Relazione del Governatore della Banca d'Italia (various issues). Union density from OECD website (http://stats.oecd.org/index.aspx)

From Checchi and García Peñalosa (2009) we also know that a lower labour share contributes to increasing income inequality. These authors argue that labour market institutions play an essential role in explaining the different inequality trends within the OECD, both across countries and over time. These institutions affect simultaneously relative wages, the labour share, the unemployment rate, and hence the distribution of personal income. Union presence in particular has an ambiguous effect because of its two opposing impacts. On the one hand, greater union density increases the unemployment rate and hence income inequality. On the other hand, greater bargaining coordination reduces the wage differential and increases the labour share, both of which tend to make the distribution of income less dispersed. Using a long-term perspective, the model presented in Checchi and García Peñalosa (2009) seems to fit the Italian case (see figure 7). The decline in union power that started in the second half of the 70s was followed by a corresponding decline in the labour share, by an increase in wage differentials (across sectors and/or across qualifications) and by a decline in unemployment. The joint effect of these changes has been an increase in inequality, and as a result Italy is currently among the OECD economies with the highest levels of income inequality (Boeri and Brandolini 2005).

Figure 7 – Inequality indicators

Source: data from Checchi and García Peñalosa (2009)

4. Inequality consequences of the reforms

In the previous paragraph, we saw that exceptional employment growth may be accounted for by a decline in unit labour cost, which has its aggregate counterpart in the decline of the labour share. Given the model predictions summarised in figure 7, we may then expect a positive impact of labour market reforms on earnings and income inequality. Let us provide some evidence in this respect. In table 8, we provide the population weighted distribution of employment in Italy, as inferred from a survey of the Italian population conducted in 2005 by ISFOL, a governmental agency responsible for vocational training. From this table, we observe that women seem to be sorted into dependent and/or temporary employment with reduced working hours.

Table 8 – Contractual agreements by gender – weighed % – Italy 2005

	Males	Females	Total	Males	Females	Total
permanent contract employee	8335438	5827905	14163343	62.42	66.94	64.20
temporary contract employee	639551	711453	1351003	4.79	8.17	6.12
non standard employment	274482	277529	552011	2.06	3.19	2.50
total dependent employment	*9249471*	*6816887*	*16066357*	*69.27*	*78.30*	*72.82*
Among which part-timers	*341249*	*1653916*	*1995165*	*3.69*	*24.26*	*12.42*
high-rank self-employment (entrepreneur, professional, etc)	3704991	1455150	5160141	27.75	16.71	23.39
low-rank self-employment (co.co.co, etc.)	399223	434771	833993	2.99	4.99	3.78
total self-employment	*4104214*	*1889921*	*5994134*	*30.74*	*21.70*	*27.17*
Total	13353684	8706807	22060491	100	100	100

Source: my elaboration from IsfolPlus 2005

When we look at data on earnings[5], we find consistent results: earnings increase with educational attainment by an amount that is consistent with other findings in the related literature. Using

[5] The reliability of sample formation and income self-declarations are discussed in Giammateo 2009.

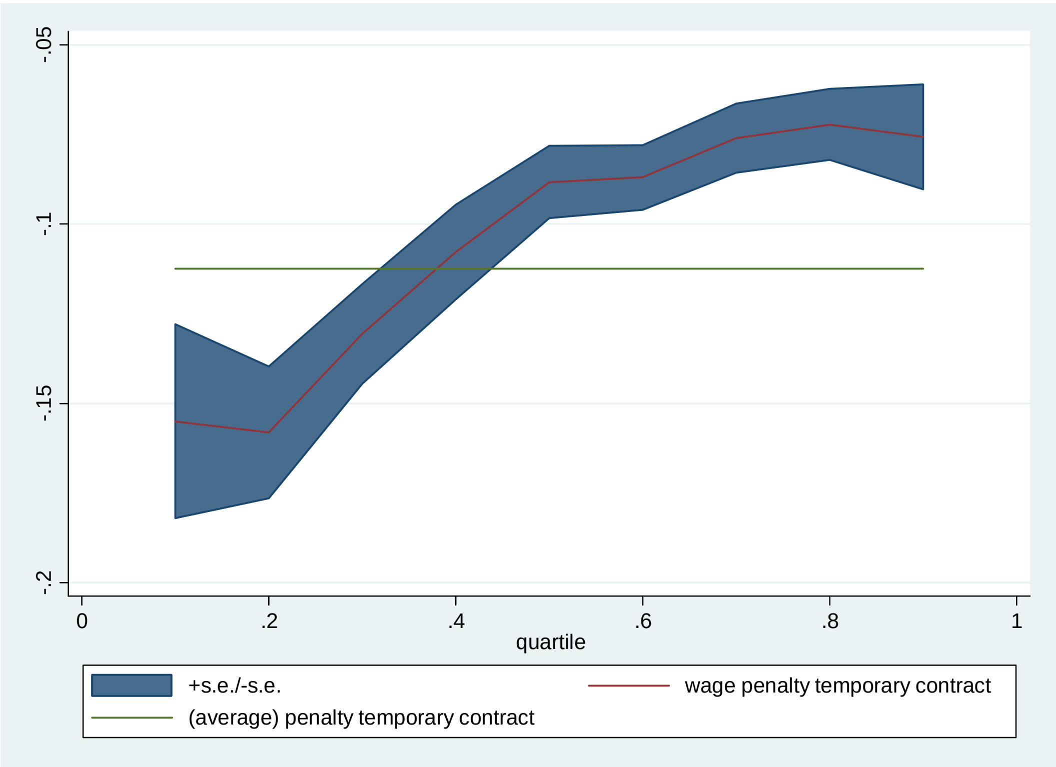
multivariate regression (and controlling for age, cohort, region and ability) we find a return of 15% for completing secondary school (vis à vis completing compulsory education) and of 37% for obtaining a BA degree for men (42% for women) in dependent employment. Interestingly enough, no statistical effect of educational attainment is found in the case of the self-employed. Table 9 provides information about the wage penalty associated with working under a non-standard contract (see also Barbieri and Cutuli 2009). As we can see, there is no consistent pattern of this penalty along the different educational attainments. A more proper way to conduct the same exercise is to use quantile regressions to assess whether the wage penalty is uniform along the entire wage distribution or whether it concentrates somewhere.

Table 9 – Hourly earnings by gender, educational attainment and type of contractual arrangement – weighed - Italy 2005

	Self-employment		Non-standard employment		Dependent employment		Wage penalty for non-standard contract	
educational attainment	male	female	male	female	male	female	male	female
illiterate (nessun titolo)	19.5	3.99	6.38	5.74	8.27	8.3	-22.9%	-30.8%
primary (licenza elementare)	10.6	6.45	9.48	nd	7.94	6.91	+19.4%	nd
lower secondary (licenza media)	9.93	6.38	6.81	5.32	8.12	7.24	-16.1%	-26.5%
upper secondary 3 years	15.2	7.09	3.57	5.84	8.45	8.19	-57.8%	-28.7%
upper secondary 5 years (maturità)	12.8	8.51	6.35	6.81	9.22	8.3	-31.1%	-18.0%
bachelor (laurea)	16	9.57	7.02	8.3	11.5	11.1	-39.1%	-25.0%
postgraduate	12.4	9.46	6.24	9.22	15.4	13.8	-59.4%	-33.3%
Total	*12.2*	*7.57*	*7.02*	*6.81*	*8.61*	*8.19*	*-18.5%*	*-16.8%*

Source: my elaboration from IsfolPlus 2005

Figure 8 – Wage penalty associated to temporary contract – Italy 2006



Source: quantile regression estimated in IsfolPLUS 2006 – controls include gender, age, age², years of education, past results in schools, city size and region of residence

The results of this exercise are reported in figure 8. Given the average penalty of -11% associated with working under a temporary contract, we notice that this penalty mostly affects workers in the two bottom quintiles, while workers in the top quintile are less penalised. Whenever a legislative reform expands the share of workers under temporary contracts then, other things being constant, we can expect an increase in earnings inequality.

There is some micro-data evidence that accounts for such an increase in inequality. Most of the existing literature has focused on whether people under non-standard labour contracts are trapped in a work history consisting of intermittent contracts at low wages. Making use of different datasets (the Survey on Household Income and Wealth-SHIW conducted by the Bank of Italy, the European Community Household Panel–ECHP and the European Union Survey on Income and living conditions-EUSILC, both from Eurostat) Barbieri and Cutuli (2009) find a persistent wage penalty that is a result of the 'deregulation at the margins' of the Italian labour market. They explain this finding by contrasting two alternative explanations: in a world of imperfect information, temporary contracts could represent a screening device that makes it possible to hire the most productive workers; alternatively, in a world of perfect information, temporary contracts at a lower wage represent a better alternative than unemployment for low-productivity workers. Barbieri and Cutuli (2009) find a persistent wage penalty, of the order of 10%, associated with working under a temporary contract, which is halved when individual fixed effects are included. This suggests that increasing labour market flexibility increases wage differentials, partly by sorting individuals according to their unobservable characteristics and partly by changing the equilibrium wage for less qualified occupations. In fact, by using quantile regressions, Barbieri and Cutuli (2009) show that the wage rate associated with temporary contracts is a penalty up to the median and then becomes a premium above it. This indicates that there are at least two types of temporary workers: the 'professionals', who take advantage of temporary contracts to increase their market power by enlarging the set of potential employers; and the 'precarious', who do not succeed in achieving a permanent job because they do not have abilities that are sufficiently demanded in the labour market.

On similar lines, Bellani (2009) shows that the wage penalty associated with temporary contracts among young workers (aged between 15 and 35, thus including apprentices) is also of the order of 10% and became larger in the most recent wave of the survey conducted in 2006. She also applies the Blinder-Oaxaca decomposition and shows that half of the permanent/temporary contract gap can be attributed to discrimination (i.e. the observable characteristics are differentially evaluated, according to the contract). In a dynamic setting using longitudinal samples, Bellani also shows that working under a temporary contract increases the probability of ending up among the low waged, namely those working for a wage rate lower than 2/3 of the median wage.

Different opinions are found in Barbieri and Sestito (2008), who show that working under a temporary contract increases the employment probability with respect to being unemployed. In a similar vein, Bison et al. in Checchi (2009) show that the increased intermittence of work experience associated with a temporary contract is compensated by the shortening of waiting time before entering employment for job seekers (and/or by the reduction of informal work). They evaluate the effect of the Treu reform (1997) with respect to the entire labour force, including the transition in/out of self-employment and conclude that the Italian labour market has taken advantage of this situation by reducing its main dysfunctions, such as long-term unemployment, informal/illegal working and waiting queues.

Finally, in their recent book, Berton, Richiardi and Sacchi (2009) show that most of the people working under non-standard contracts face subsequent long spells of unemployment, during which they are not covered by any welfare provisions (since the current Italian system of unemployment benefits requires a minimum period of contribution and extends for only six months). They focus their attention on the average duration of an employment spell and stress that contractual intermittence may be detrimental to permanent income if it is not accompanied by an increased probability of entering employment (the job-to-job transition of workers employed under non-standard contracts is below 20%).

5. A suggested interpretation

The labour market reforms that set out to increase labour flexibility in Italy did not reach the entire labour force, but only marginal workers. Thus, they reinforced the two-tier nature of the Italian labour market. There are two potential reasons for this outcome: on the one hand, it is possible that the Italian labour market was already sufficiently flexible and did not need additional fluidity (see again the turnover rate reported in table 4 – in addition, we should not forget that approximately 5% of the overall labour input comes from overtime); on the other hand, the reforms were intentionally designed to fragment full-time jobs and therefore could be introduced only where full-time workers could easily be replaced by a plethora of possible contracts. Such jobs (mostly in services) do not require a great deal of training nor do they require mutual investment in the employment relationship.

In a competitive labour framework, as there is in the case of the marginal sectors, the effect of the reform was to increase the elasticity of the (aggregate) labour supply, because households (mostly in their female and youth component) became able to take advantage of interstitial job opportunities. If we combine this with the increased immigration from Eastern Europe and North African countries (estimated to have reached three million people in 2008), we could frame these events as a supply side shock (OECD 2009). The increase in the supply elasticity met the labour demand in an already elastic portion, thus producing an increase in employment without a decline in the real wage (as we recognised in the previous section).

If on the supply side labour market reforms mostly affected the young and women, on the demand side their effect can be traced by the distribution of the marginal workers. Looking at table 10 and taking immigrant workers and/or the female component as proxies for the allocation of marginal workers, we notice that they tend to concentrate in non-qualified jobs, thus reinforcing the idea that flexibility can be introduced only when the employment relationship does not require significant training.

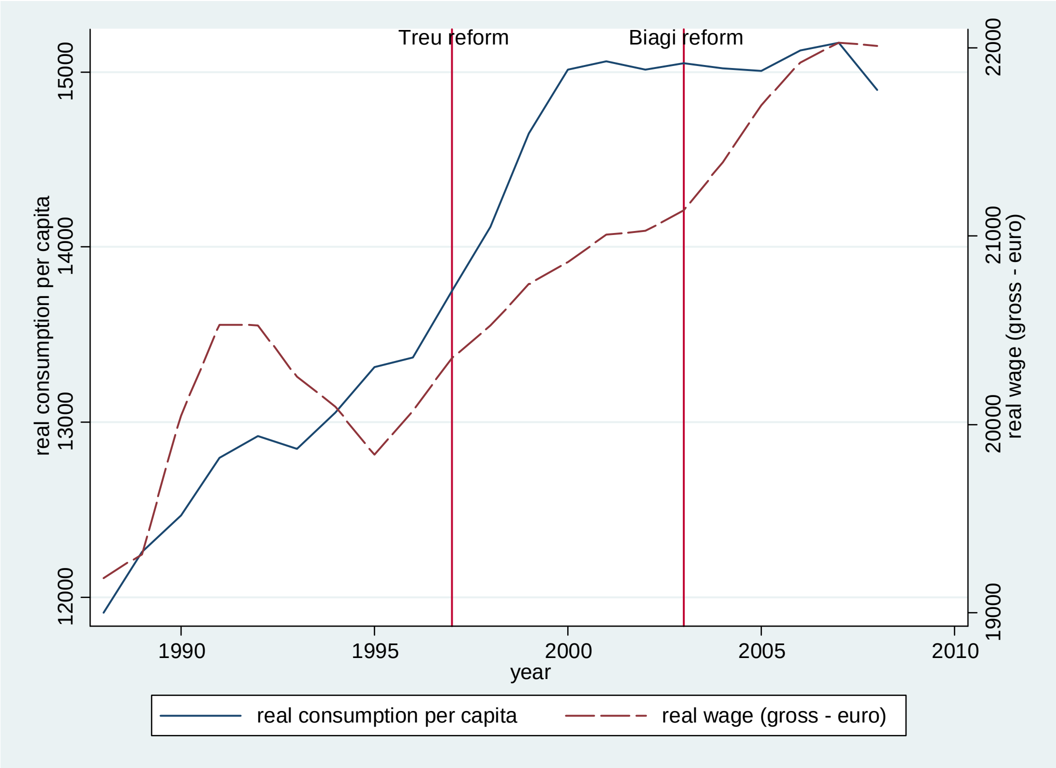
Table 10 – Employment by nationality and gender – Italy 2006

Job characteristics	Foreigners EU25	Foreigners Non EU25	Foreigners Total	Italians	Total	% foreigners On total
Men						
Qualified	50,5	5,4	7,7	35,8	34,1	1,4
White collars	9,7	13,2	13,0	19,8	19,4	4,1
Blue collars	32,0	60,0	58,6	37,3	38,6	9,3
Not qualified	7,8	21,4	20,7	7,1	7,9	16,0
Total	100,0	100,0	100,0	100,0	100,0	6,1
Women						
Qualified	39,2	7,6	11,9	41,8	40,1	1,7
White collars	30,6	26,1	26,7	38,1	37,4	4,0
Blue collars	7,6	19,0	17,4	11,1	11,5	8,6
Not qualified	22,6	47,3	44,0	9,0	11,0	22,6
Total	100,0	100,0	100,0	100,0	100,0	5,7
Total						
Qualified	43,4	6,2	9,3	38,2	36,5	1,5
White collars	22,9	17,8	18,2	27,1	26,6	4,1
Blue collars	16,6	45,3	43,0	26,8	27,8	9,2
Not qualified	17,1	30,7	29,5	7,9	9,1	19,1
Total	100,0	100,0	100,0	100,0	100,0	5,9

Source: ISTAT 2007. *Rapporto annuale 2006*. Rome. Tavola 4.19

The 'honeymoon effect' of employment growth starts to show its limits (Boeri and Garibaldi 2007). The overall perception of families has been of increasing insecurity in the absence of a universal welfare safety net. Flexibilisation at the margin (the costs of which are mostly paid by young generations – think of entry wage combined with pension reforms based on capitalisation) has blocked the transfer of increased income into increased consumption. The transition from jobless growth in the early 90s to what has been termed 'growthless job creation' (Boeri and Garibaldi 2007) is apparent in the dynamics of consumption (see figure 9). Consumption increased steadily in the previous decade and was partly independent of the wage dynamics (which were hardly affected by the 1993 wage freeze agreement) but, starting from the current decade per-capita consumption stagnated, clearly indicating that something in household behaviour had changed.

Figure 9 – Real wages and consumption per capita



Source: data from the Appendix to the Relazione del Governatore della Banca d'Italia (various issues).

Obviously many other factors may have contributed to this outcome. One in particular may be correlated with the process of policy reform. By spreading job opportunities among a larger group of labour market participants, two-tier reforms increase earnings inequality. This does not necessarily imply that household income distribution becomes more unequal, because this depends on the job opportunities distribution within families. However, it is likely that increased income variability translates into a greater perception of insecurity, which induces greater savings in order to achieve consumption smoothing. One should also consider that Italian families may have resisted the decline in income opportunities by decumulating assets during the previous decade, but now they may have reached the limit of desired indebtedness, and therefore may have reverted to a lower consumption pattern.

Labour market reforms have also impacted on union ability to recruit members and to exert wage pressure. While the bulk of union members are likely to be unaffected by these reforms (since most of them are under permanent contracts), the reform affects prospective members, who are likely to develop a perception of being treated unfairly and of being exposed to more frequent spells of unemployment. Disaffection from the unions' values of egalitarianism and solidarity combine with increased wage inequality, which in turn contributes to reduced willingness to join unions (see again figure 6). The decline in union power may account for the faint wage push observed in recent years, despite the decline in unemployment. In other periods in the recent economic history of Italy, an unemployment rate close to the frictional rates would have implied an upturn in bargaining activity, often accompanied by an increase in industrial conflict, in the attempt to seize a fraction of productivity growth. On the contrary, the recent employment growth, accompanied by productivity stagnation, has not spurred any increase in bargaining.

The final question has to do with how long this situation may last. Dissatisfaction with the two-tier reforms, initially applied to pensions and then to labour markets, may produce a policy reversal, as has already occurred in Spain. However, the policy change may also move in the direction of reducing employment protection to permanent contracts only. In such a case, we do not expect a revival of growth, because the presumably increased volatility would compress internal consumption and production even more.

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