ECONOMIC IMPLICATION OF LABOUR MARKET ORGANISATION [104]

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Abstract: *Labour is an essential and specific resource to a firm. The framework for any labour contract is set by the individual country's regulation, i.e. its labour market institutional mechanism design. Our research problem is concentrated onto the objection of a growing discrepancy between firms' needs and employment contracts as they are actually implemented under current regulation. The foremost economic question at hand is whether the labour market and firm's regulatory institutional mechanism design is commensurate with the specific firm's needs and the needs of the economy of that particular country. During the 20th century, employment regulation was mostly tightened under the excuse of greater worker protection consequently reducing the freedom of contract between employers and employees. Firms needed and asked for exactly the opposite: more flexible employment contracts. Employment regulation is an essential part of the legal business framework since it governs employment relationships and sets the span of contract flexibility, thereby influencing international competitiveness of a firm and the economy as well. We conjecture the less flexible working arrangements are the less beneficial is the employment environment as firms are more procrastinated by regulation. We investigate regulatory practices of selected European Union countries (Austria, Croatia, Finland, and Ireland) regarding labour market issues and its consequences. Labour market flexibility is a composite indicator of selected factors conjectured to ultimately influence the economic performance of nations. Our aim is to identify factors influencing labour market flexibility and the selected output variables such as employment, productivity, and others.*

Key words: labour economics, employment regulation, labour flexibility, labour market organisation.

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1. INTRODUCTION

Labour market regulation in general, and employment regulation in particular is the most essential part of the legal business framework since it governs employment relationships within a firm and influences the international competitiveness of a single firm and thus also the economy. "In a global economy – one would expect the location to diminish in importance. But the opposite is true." [1] In human capital driven economies, labour remains the only flexible

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production factor. And again, "competitive advantage lies in knowledge, relationships, and motivation." [1]

Our research problem is mainly concentrated on the growing discrepancy between firms' needs for human capital and their ability to engage into mutually beneficial free contractual arrangements. As regulations procrastinate contractual freedoms of firms and labour there is growing evidence that such regulatory evolution has detrimental consequences for entire economies. An economy is a sum total of the productive power found on a certain territory. By definition, firms are organisational units free of institutional inflexibilities that reduce transaction costs.[2][3][4][5] Firms need exactly the opposite: more flexible employment contracts, i.e. less institutional constraints. Firms compensate institutional inflexibility with organisational flexibility, i.e. long-term flexible employment contracts. The more institutionally constrained firms are, the less similarity they bear to an organisational hierarchy and more to an institutional network. Society needs institutions to protect its individuals from the leviathan of its more powerful units. But institutions impose transaction costs. Firms are organisational units with loose institutional regulations reducing transaction costs between cooperating individuals thereby reducing production costs. Institutional networks are more flexible at starting and protecting new ideas, but are less efficient in producing final results. Thus, an institutionally protected network is probably a preferred organisational structure for a university or a research centre needing the protection of individual creativities but not for an internationally competing firm searching for the most efficient production process. Firms are thus also defined by their technologies, i.e. cost structures, whereby the more efficient survive, and the less competitive die out in a Schumpeterian "catallactic" process.

Labour market and employment regulation is an institutional mechanism design set by the regulator of an individual country giving the country a distinctive entrepreneurial and cultural stamp. We investigate the grade of regulatory labour flexibility in selected European Union member states, the consequences of their regulatory practices and a comparison with previous theoretical assumptions. Paper's aim is to qualitatively identify relevant factors influencing labour flexibility. We shall try to falsify the positive causal relationship between some of these factors and the selected output variables such as employment, productivity or GDP per capita.

2. THE THEORY OF THE FIRM IN AN INTERNATIONAL ENVIRONMENT

A firm, besides as an organisational hierarchy may also be simplified into a technological production function. Technology determinates the effectiveness of the firm, and the expected effectiveness is the determinant of the firm's course of action, i.e. its conduct on the market.[6]

Diverse technologies require different organisational structures that may not be effectively standardised into single labour legislation. Firms compete on an international market according to competitiveness rules set by their local legislators. Inadequate labour legislation may cause severe disadvantages for an industry or an entire economy. Cost structures are an important behavioural determinants for firms. Irreversible costs in form of sunk fixed costs are major risk determinants for firms.[7] Labour consists of one of the last few flexible resources. Labour flexibility is determined by two major groups of factors: the intrinsic qualities of human capital, and the institutional framework of a particular market. Institutional factors comprise laws, bylaws, rules and regulations, as well as customs and practices including the results of collective bargaining. Statutory acts were meant to promote the well-being of the workers and set a bar on minimum working conditions. Similarly to minimum wage laws, statutory regulation promotes the wellbeing of the ones whose productivity justifies the threshold, but prohibits the ones below the productivity threshold to enter the market. Although the motives for labour legislation were to better the lives of the workers, the unwanted consequence was to reduce the flexibility of the labour market and to decrease the number of available jobs, as producers settled in countries with more flexible labour legislation. The free flow of capital, together with the free flow of goods together with a partially free flow of labour, will induce a Tiebout kind of competitive migration of investment and labour into more flexible countries. As economies open up to international trade, institutional regulation becomes an important competitive advantage for a firm.[1] The decision where to settle is, besides the technological decision, the most important decision a firm must make. The more liberal the institutional framework, the more organisational freedom a firm has at its disposal, reducing its internal transaction costs. Lower the transaction costs, lower the overall costs, and higher the flexibility, adaptability, and competitiveness of the firm on the market, through constant product and process innovation. Investments into research and development are ex ante decisions based on expected ex post profitability. The expected profitability is a risky factor dependent on total irreversible costs. Thus, more irreversible costs, more risky the investment, and lower the expected profit. According to Williamson [8][9][10] human factors influence transaction costs across firms, and thus influence their competitiveness.

3. THE ANALYSIS OF EMPLOYMENT REGULATIONS IN SELECTED COUNTRIES

In order to compare theoretical assumptions with real world data, we selected four EU countries for an empirical analysis. Beside Croatia, which is our home country, we selected Austria as the nearest country sharing many institutional solutions, but much more developed by most economic indicators. Furthermore, we selected Ireland and Finland as having opposite employment policies, with Finland having a well developed welfare system, and the rapidly growing Ireland, well known for the lack of regulation in the employment area. All three foreign countries in our analysis are targets for Croatian and SEE outmigration. As a paradox, the common opinion of the Croatian public discourse is that employees in private business entities are vastly under-protected. Therefore, comparison with departing workers' target countries seemed reasonable, as one would expect that under protected and unhappy employees would migrate in a direction of countries with better employee protections.

The next four tables (Table 1-5) sublimate the data expected to be of importance for shaping the flexibility of firms and the stability and the job security of employees.

The analysis shows noticeable cross-country differences among selected countries that are all EU members and that are sharing many cultural and historical features, the similar economic environment and joint legislative within EU Framework. However, labour legislation is largely devolved to the member states. Consequently, different policies have evolved across the EU.

	UNEMPLOYMENT % (2016, ACTIVE POPULATION)			LONG-TERM UNEMPLOYMENT % (2016, BETWEEN 20-64)			YOUTH UNEMPLOYMENT % (2016)
COUNTRY	**Total**	**Males**	**Females**	**Total**	**Males**	**Females**	**Total**
IRELAND	7.9	9.1	6.5	4.3	5.5	2.8	9.1
CROATIA	13.4	12.7	14.2	6.6	6.8	6.5	25.4

AUSTRIA	6.0	6.5	5.6	1.9	2.2	1.6	9.4
FINNLAND	8.8	9.0	8.6	2.4	2.7	2.1	16.5

Table 1: Unemployment rates in selected countries (Eurostat) [11]

Looking just at the workweek duration (Table 5), Austria is less flexible than other countries because employers have to adapt their personnel requirements into smaller available periods of a week and in some situations wait for the weekend to pass to finish the job.

	CRO	IRE	AT	FIN
Equal reward for work of equal value	YES			
Ban on discrimination based gender in hiring	NO	YES	NO	YES
Financial aid during maternity leave	YES			
Length of paid maternity leave (days)	208	182	112	105
Full salary during maternity leave	YES	NO	YES	NO
Duration of employment before eligibility for unemployment compensation (months)	9	24	12	6
Minimum salary	400 €	1.484 €	1.000 €	not prescribed
Average salary	735 €	2.129 €	2.124 €	2.300 €

Table 2: Some aspects of employment quality (authors calculations based on the Doing Business Database) [12]

Similarly, just for argument sake, we assume comparable labour productivity, Finnish firms have their workers 2.5 working hours per week less and might need more employees to cover the same needs. There is an even bigger discrepancy when taking into account night work premiums from 0 (no obligation of an extra pay) in Ireland to 67% in Austria. Croatia with 10%, and Finland with 15 are rather moderate compared to Austria. Therefore, it is to expect the Austrian firms to be reluctant to use night shifts on tight schedules.

	CRO	IRE	AT	FIN
Maximum work probation	6	12	1	6
Dismissal due to redundancy	YES			
Third party notification if one worker is dismissed	YES	NO	YES	YES

Third party notification if nine workers are dismissed	YES			
Third party approval if nine workers are dismissed	NO			
Obligation to retrain or reassign before dismissal for redundancy	NO	NO	NO	YES
Priority rules for dismissals for redundancy	YES	NO	YES	NO
Priority rules for reemployment	YES	NO	YES	YES

Table 3: Rules over probation and redundancy (authors calculations based on Doing Business Database) [12]

The same goes for high premiums (100%) that Finnish and Austrian workers will receive if they have to work during their rest day. A premium of 35% in Croatia might look rather moderate, but then again Ireland laws do not recognise any premium at all. Overtime compensation is also not prescribed by Ireland's laws, while other three countries are in line with the 50% premium. Ireland also has 30-35% less paid public holydays than the rest of the group and the probation period is twice as long as in Finland or Croatia.

	CRO	**IRE**	**AT**	**FIN**
More than 1 year of tenure				
Notice period before layoff (weeks)	4.3	1	2	4.3
Severance pay (salaries)	0	0	0	0
More than 5 years of tenure				
Notice period before layoff (weeks)	8.7	4	2	8.7
Severance pay (salaries)	7.2	11	0	0
More than 10 years of tenure				
Notice period before redundancy layoff (weeks)	10.7	6	2	17.3
Severance pay (salaries)	14.4	21	0	0
Average notice period (weeks)	7.9	3.7	2	10.1
Average severance pay (salaries)	7.2	10.7	0	0

Table 4: Notice periods before layoff and severance pays (calculations based on Doing Business Database) [13]

Austrian regulations, although most restrictive between labour laws in most analysed indicators among selected countries, are not regulating severance pay (Table 4). It might seem like it is noticeable break to Austrian firms when dealing with layoff situation and workers redundancies but additional analysis showed that in Austria, as in Finland, workers in most industries are joint in the powerful labour syndicates. Power of syndicates is widely known source of constraints to labour flexibility, and should be taken into analysis. However, Germanic and Scandinavian countries have numerous syndicates that are additionally regulating labour differently in many industries, but due to their heterogeneity, their industry specific constraints cannot be fitted in cross-country analysis.

The major setback in labour flexibility in Ireland is the paid maternity leave (Table 2). It is the second longest (after Croatia) but in all other selected countries, it is the state expense, while in Ireland it is paid by the employer. Biggest comparable flexibility setback in Finland is the obligatory retraining or reassignment of an employee before redundancy. From a firms' standpoint, retraining or reassignment requires additional time and resources, while others, already trained workers for that job, cannot be hired because of priority rules prescribed by law.[11] Croatia and Austria are less flexible than the other two countries with priority rules for redundancies.

	CRO	IRE	AT	FIN
Workweek (days)	6	6	5.5	6
Workweek (hours)	40	39	40	37.5
Lunch break (min)	30	30	30	60
Night work premium (%)	10	0	67	15
Sunday/rest day work premium (%)	35	0	100	100
Overtime premium (%)	50	0	50	50
Night work restrictions	Yes	No	Yes	No
Obligatory rest day (%)	Yes	No	No	No
Paid public holydays (annually)	14	9	13	13
Permitted number of overtimes (weekly)	10	-	5	8
Paid annual leave (average no. of days)	20	20	25	30

Table 5: Data on working hours (authors: calculations based on Doing Business Database) [12]

4. DISCUSSION

As pointed by Wallis [14], organizations are primarily driven by relationships, not by rules. Rules are emerging when there is a failure with relationship. Wallis's deep thought looks even truer when analysis shows that Croatia, country that finally got out of long economic depression and has heavily regulated labour rights, is losing citizens so fast that one of our leading demographers is describing it with a phrase "the state of emergency".[15] Ironically, one of the most frequently mentioned destinations for departed workers is Ireland [16], the country that, according to presented and analysed data, offers significantly less legal protection to its workers. It would pretentious and inaccurate to draw a conclusion that Croatia is emitting, and Ireland recipient country for labour migration because latter is allowing its firms to be flexible i.e., does not choke its economy with the ropes of over-regulation. Besides that labour regulation is only one of many factor that influences economic growth, another country in our selection, Austria, has many similarities in regulation with Croatia and it is still very successful by most economic indicators. However, if we once again reflect on Wallis's premise, in wealthier countries that have a reputation for being well arranged, workers seem to find stability regardless of the level of formal labour regulations. In Croatia, regardless of the existence of regulations that should protect their rights, because of poor economic environment, inflexibility, well known southern creativity to bypass regulation etc., workers in private sector often feel very unprotected and uncertain about their future. Therefore, it can be questioned whether regulation (not only the one affecting the labour) is the constraining factor in firms' attempts to better their business results. The markets have their dynamics, technology is rapidly developing what creates pressure towards additional investments in inflexible factors and even labour is not so flexible factor as it may seems.

5. CONCLUSION

We tried to identify and analyse factors influencing labour market flexibility in selected countries: Croatia, Ireland, Austria, and Finland. Labour is a specific resource to firms. As it cannot be owned, the closest form of control of human capital are incomplete labour contracts. The more flexible the labour as a resource, the greater the manoeuvring space for a firm to stay competitive on the market. We identified 28 factors in 4 selected countries influencing labour flexibility. The analysis led to following conclusions: the Irish labour market is the most flexible and Ireland's macroeconomic indicators show dynamically the best results. The Croatian and Austrian labour markets are the most inflexible, with moderate economic growth and somewhat differing macroeconomic indicators. Finland is located in between the analysed countries. It may be concluded that Croatia and Austria have the least flexible labour markets with the lowest economic growth among the analysed countries and with moderate macroeconomic indicators.

Labour market and job flexibility are actually helping workers by promoting flexible and dynamic economic environments. Higher economic activity secures jobs by increasing its demand. The best evidence of this is Ireland which is achieving an expansion of economic growth and simultaneously a widening of available jobs.

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