

# DUAL LABOUR MARKETS, MINIMUM WAGE AND INEQUALITIES

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This brief is a summary of the „2014 Conference on dual labour markets, minimum wage and inequalities” which took place in Warsaw. It briefly discusses the main causes of labour market duality in the developed countries, consequences of duality and some of the policy implications drawn in the discussions and speeches during the conference.

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Network for  
JOBS AND DEVELOPMENT

# Dual labour markets, minimum wage and inequalities

## 2014 Conference on dual labour markets, minimum wage and inequalities

- This brief contains some of the policy implications drawn in the discussions and speeches during „**2014 Conference on dual labour markets, minimum wage and inequalities**”.
- The conference organised by the **Institute for Structural Research (IBS)** was held in Warsaw on October 8-9, 2014. It focused on labour market duality, i.e. the negative consequences of abusing non-standard forms of employment, employment and distributional effects of minimum wages and income inequalities.
- The agenda of the conference and presentations are available [here](#).
- Short description of speeches and video recordings of presentations and discussions are available [here](#).

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The following speakers have participated in the conference:

- Wolfgang Auer (Ifo Institute)
- Haroon Bhorat (Development Policy Research Unit Cape Town)
- Pietro Garibaldi (University of Torino, Collegio Carlo Alberto)
- Jose Ignacio García Pérez (Universidad Pablo de Olavide)
- Roberta Gatti (World Bank)
- Andrea Garnero (Paris School of Economics, SBS-EM, IZA)
- Peter Goliaš (INEKO)
- Marek Góra (Warsaw School of Economics)
- Krzysztof Hagemejer (Social Policy Office of the Chancellery of the President of Poland)
- Herwig Immervol (OECD)
- Marcel Jansen (Universidad Autónoma de Madrid)
- Piotr Lewandowski (IBS)
- Matteo Morgandi (World Bank)
- Kai-Uwe Müller (DIW)
- Michał Myck (CenEA)
- Jekaterina Navicke (Vilnius University)
- Victoria Osuna Padilla (Universidad Pablo de Olavide)
- Jörg Peschner (European Commission)
- Clemente Pignatti (ILO)
- Jan Rutkowski (The World Bank)
- Wiemer Salverda (AMCIS University of Amsterdam)
- Joanna Tyrowicz (University of Warsaw, GRAPE)
- Michael Weber (The World Bank)

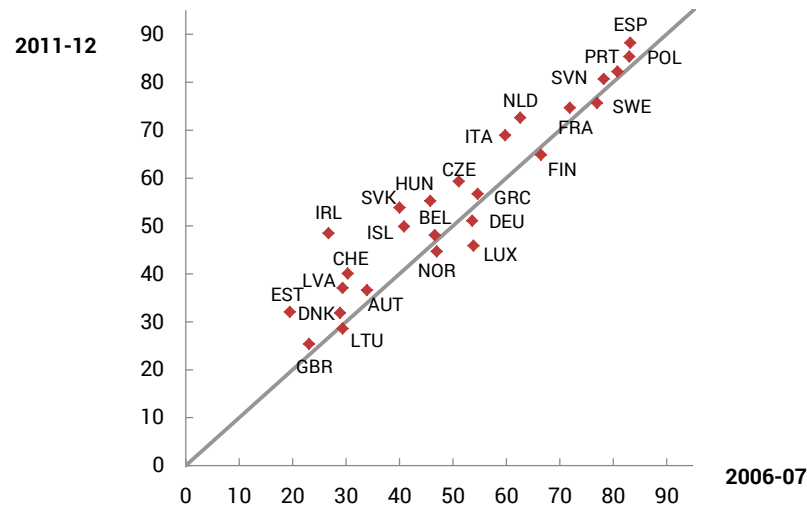
# Duality of labour market in the developed countries

## Duality of European labour markets

The conference was focused on the problem of division of workers into two groups: **privileged** with **standard employment contract** and **unprivileged** with **non-standard, temporary employment**.

- The share of temporary workers among all employees **strongly varies across countries**.
  - In Europe it is the **highest in Poland** (27% in 2013), **Spain and Portugal**, and the lowest in **Romania** (1,5%), **Lithuania and Estonia** (LFS data).
  - The incidence of fixed-term contracts among new hires **has increased** during the Great Recession in most of developed countries.
- To what extent temporary contracts represent a **labour market dysfunction**?
  - There are **professions that require temporary contracts** or specific task contracts.
  - But **temporary jobs often turn out to be persistent** - in most developed countries the **majority** of temporary employees work with fixed term contracts for **over 3 years**.
  - In Spain, Poland and Netherlands **15-20%** of all workers have temporary jobs from **more than 3 years**.

Percentage of fixed-term contracts among new hires



Percentage of temporary workers by duration of temporary contract



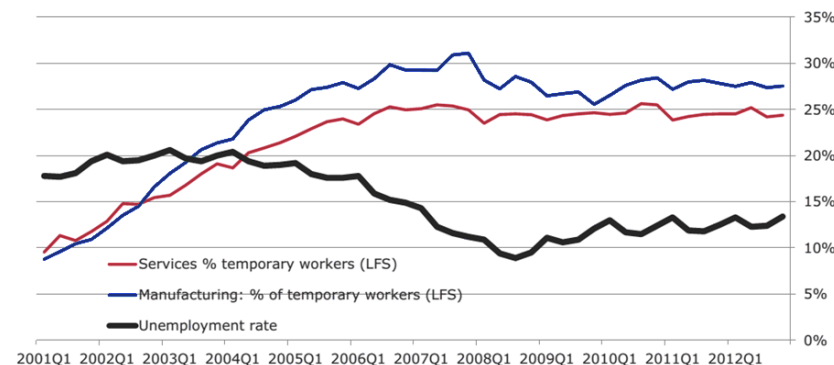
Source: Own calculations based on „OECD Employment Outlook 2014“

# Duality of labour market in the developed countries

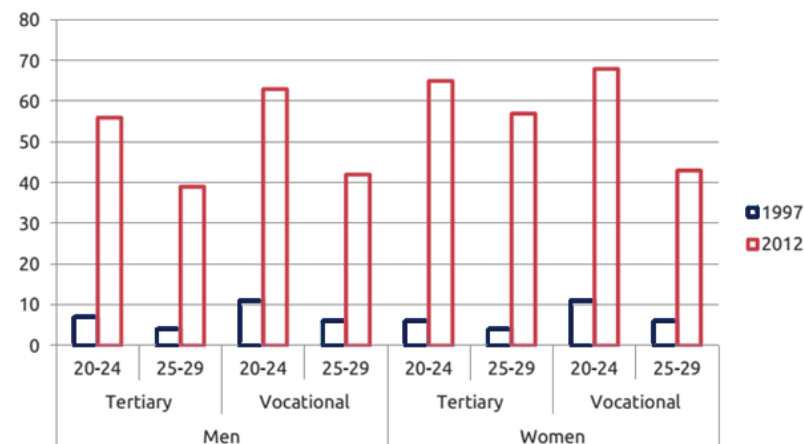
## Temporary employment on Polish labour market

- Since the late 90's the **percentage of temporary workers significantly increased**.
  - The increase was observed in all age groups and among both men and women, irrespective of educational attainment. It was **the strongest among the youth aged 15-24** (13% in 1999 vs. 72% in 2013).
- Temporary contracts in Poland are the most prevalent in **administrative services, arts and accommodation and food service activities** (NACE).
- There is a **heterogeneity among temporary workers**:
  - A significant part of **self-employment** in Poland may result from avoiding regular contracts by employers and **forcing workers to be subcontractors**.
  - Increasingly popular **civil law contracts are much more precarious** than fixed-term employment contracts. In 2012, 1,35 million Poles worked on the basis of the civil law contracts (GUS). In the period 2002-2012 that number increased 2,5 times.
  - Civil law contracts are often concluded in **circumstances which call for an employment contract instead**. Polish National Labour Inspectorate argues that since 2009 the share of such contracts has been growing at the rate of 3 pp annually and in 2012 reached the level of 16% of all contracts which were checked in this respect.

Percentage of temporary workers in services and manufacturing and unemployment rate in Poland



Percentage of temporary workers by gender, age and education



Source: Joanna Tyrowicz on the basis of LFS (first figure) and „Employment in Poland 2012” (IBS) (second figure)

# Duality of labour market in the developed countries

## Why is labour market duality a problem?

- There is a **14% wage penalty for temporary workers** in the EU. Together with instability of employment it can influence the situation of the entire household.
  - The relative **in-work poverty rate** among **temporary workers** in EU is much **higher** than among permanent workers (14,7% vs. 5,5% in 2013). On the other hand, temporary **jobs reduce the risk of poverty relatively to unemployment**, especially for second-earners.
- Temporary jobs involve **lower stability of employment**.
  - In many countries the employment during the crisis had decreased at the expense of temporary contracts.
- Temporary jobs can be **lower-quality jobs**.
  - Besides lower EPL, temporary workers have often **worse** (or even no) **access to benefits**, e.g. holiday and parental leaves, health and pension benefits (see [the table](#) on the next page).
- Instability of employment may have many **consequences to workers and their families**.
  - People with fixed-term contracts face a risk of **long-term deterioration of employment opportunities** and lower remunerations.
  - Temporary employment may also have an **influence on other aspects** of life like fertility.

## Does the fixed-term contract help the youth and low-skilled workers?

Temporary contracts are a popular tool in fighting youth unemployment. However, in Spain, widely available fixed-term contracts at labour market mean higher probability of being temporarily employed in the long-term, fewer total days worked and lower wages. On the other hand, it also result in higher probability of finding a job before the age of 19.

Source: [Jose Ignacio García Pérez, presentation: „Can fixed-term contracts put low skilled youth on a better career path? Evidence from Spain”](#)

## Do the fixed-term contracts reduce fertility?

In recent decades the incidence of temporary contracts in Germany increased significantly. There is some evidence that women starting a career with a fixed-term contract delay giving a birth to their first child. This probably also translates into fewer number of children. For men in Germany the effect of starting career with a fixed-term contract is lower than for women.

Source: [Wolfgang Auer, presentation: „Fertility and health consequences of starting the career with a fixed-term contract”](#)

Contract type	Jobs	
	Typical	Atypical: (unsupervised, deliverable-oriented)
Labor code contracts (open-ended and fixed term)	Match	Mismatch Inefficiency, cost borne by the employer
Civil law contracts (& self-employment)	Mismatch Abuse, cost borne by the employee	Match

Source: [World Bank \(2014\) „Balancing Flexibility and Worker Protection: Understanding Labor Market Duality in Poland”](#)

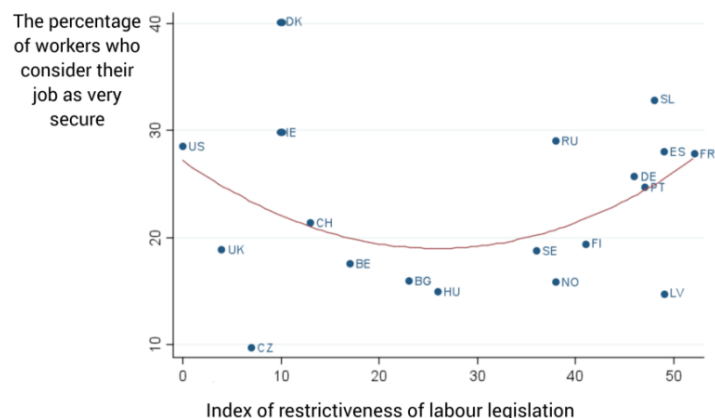
# Causes of labour market duality

## What are the factors contributing to labour market duality?

The gap in the EPL between permanent and non-standard contracts can lead to higher incidence of temporary contracts, especially those which are not covered by all EPL arrangements, like civil law contracts.

- However, countries with high EPL level not necessarily have high share of temporary workers.
- It is probably because the EPL gap is not the only factor influencing incentives to hire people on temporary basis – different rules regarding minimum wage, social security and OHS can also play a role (see differences created by Polish legislation in the table).

Percentage of workers considering their job as secure vs. index of restrictiveness of labour legislation



Source: Marcel Jansen on the basis of „Doing Business” (World Bank, 2005)

Legal and economic characteristics of various types of contracts in Poland (in 2014)

	Labour code contracts (permanent or fixed-term)	Civil law contracts	
		contract of mandate	contract for specific work
Social security benefits:	+	+	-
Maternity/paternity/parental leave and benefit	+	+/- *	-
Health insurance	+	+	+/- ***
Holiday leave	+	-	-
Minimum wage	+	-	-
Regulated working time (40 h/week)	+	-	-
Possibility of trade union membership	+	-	-
Reason for dismissal needs to be stated	+	-	-
Possibility to file with the Labour Court in case of unfair dismissal	+	-	-
Period of notice	+	+/- **	-

\* A woman and, to a certain extent, her partner are entitled to maternity (parental) leave (provided that voluntary sickness insurance contributions are paid, which is only possible if retirement and pension insurance contributions are paid).

\*\* There is no notice period, unless the contract provides otherwise.

\*\*\* Retirement and pension insurance contributions are voluntary.

# Causes of labour market duality

## Do taxes and the minimum wage contribute to the labour market duality?

- **Tax wedge** can be a factor underlying the duality.
  - In Poland the **tax wedge** for a regular employment contract is close to the EU average, but **for a contract for a specific work and a contract of mandate it is much lower.**
  - **Different rules on social security contributions** lead to different tax wedge placed on labour code and civil law contracts (see: [Arak, Lewandowski, Żakowiecki - „Dual labour market in Poland”](#)).
  - The German „**mini-jobs**” are exempted from income taxes and less charged with social contributions than traditional employment. This contributes to their **popularity.**
- **Having sharp teeth is not enough to have a strong bite** (A. Garnero)
  - In the EU countries, **the higher is the minimum wage, the bigger is the share of workers paid below its level.**
  - The **efficiency of the minimum wage** depends on its level, but also on the proportion between workers that are **covered** by it (**insiders**) and those who are not (**outsiders**: „fake” self-employed, workers with civil law contracts, etc.).
  - National statutory minima often mean lower relative minimum wage level but higher coverage than sectoral agreements.

### Does the increase of the minimum wage favour workers with regular contracts?

The influence of minimum wage increase on total employment rate in Poland is limited, although it may be significant for selected groups of workers. Firstly, the effect is slightly higher for women than for men. Secondly, young people are the most affected by the minimum wage increases. Thirdly, temporary workers, as a group relatively easier to dismiss, are much more affected by increases of the minimum wage than permanent workers.

What is more, workers affected by the minimum wage increases, are less likely to have a permanent contract and more likely to work temporarily in the next year than workers earning above the new minimum wage. For all these reasons increases in the minimum wage may influence the structure of employment.

*Source: [Piotr Lewandowski, Agnieszka Kamińska, presentation: „The employment effects of minimum wage in Poland”](#)*

### The results of introducing a minimum wage in South Africa

The minimum wage in South Africa was introduced in early 2000s. There is no significant effect of it found for the retail sector (introduced in 2003), domestic workers (2002), forestry (2006), taxi industry (2005) and security services (2001). Moreover, the minimum wage have positively influenced wages in these sectors. Due to the minimum wage, average hours worked decreased in the taxi industry.

However, introduction of the minimum wage in the agricultural sector in 2003 gave completely different results. Between 2002 and 2003 the employment of the affected group decreased by over 20%. At the same time, to reduce the unit costs of labour, employers reduced part-time employment and increased the average hours worked per worker by 17%.

*Source: [Haroon Borat, presentation: „Exogenous Policy Shocks in an Emerging Economy: The Case of Minimum Wages in South Africa”](#)*

# Potential solutions

## Types of contracts

- **Single contract reform** is potentially an efficient solution to dual labour markets issue. It consists of:
  - In its principle, **employment protection depends on tenure**, not on type of the contract itself;
  - Flexible regulations at signing gradually converge to a stringency of standard employment contract;
  - In no particular moment a firm has to decide whether to keep a worker and increase its protection or replace it with newly hired and less protected person;
  - Some non-standard forms of employment like civil law contracts can be eliminated (as an option).
- One of the ways to decrease the incentive to replace employment contracts with alternative forms, **is to reduce the tax wedge**, in particular **the one imposed on individuals with relatively low earnings** (see: Arak, Lewandowski, Żakowiecki - „Dual labour market in Poland”).
- **Important goal for reforming dual labour market** is to replace the institution of reinstatement with paid compensation, as a consequence of adjudicated unfair dismissal of worker.

- **The biggest challenge** of reforming dual labour market is to overcome the opposition of insiders who benefit from *status quo* and are in majority.

### Reforming non-standard contracts in Slovakia

**Peter Goliaš** of INEKO has described the consequences of 2013's decision of Slovak government to charge non-standard employment contracts (agreements to work – similar to Polish task contracts) with social security contributions. This has led to the following results:

- number of people working on non-standard contracts has dropped by 40%
- number of people on standard employment did not change
- some people, mostly pensioners, deactivated economically
- the unemployment rate has risen very moderately
- number of people moved to shadow economy

These findings are important because they strongly suggest that similar „reform” introduced in Poland might not bring the benefits expected by the government. On October 23<sup>rd</sup> 2014 Polish parliament decided that starting from 2016 all contracts of mandate (main type of precarious non-standard employment contracts in Poland) will be subject to social security contributions based at least on the minimum wage level.

*Source: Peter Goliaš, presentation: „Reforming’ non-standard contracts in Slovakia”*



# Potential solutions

## On the setting of minimum wage

Low-paid workers often live in households with medium levels of total income, so **increasing the minimum wage or lowering its taxation will not reduce inequality**. The minimum wage should not be treated like a redistributive tool, but as a **fair labour standard**.

Setting and adjusting the minimum wage requires **careful balancing act**:

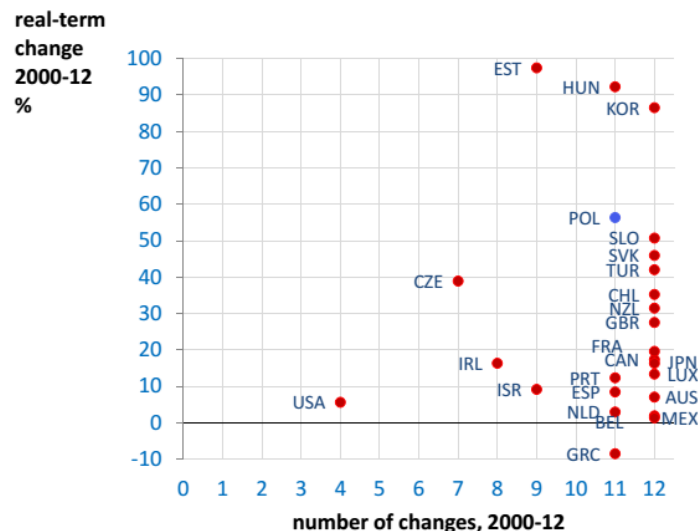
- The wage floors should be adapted to **productivity and earning potential** of the most affected groups (youth and low-skilled persons).
- The impacts of the minimum wage should be **evaluated frequently** with focus on the labour market situation of the most affected groups.
- The level of the minimum wage should be set on the basis of a **simple formula**, and **revisions should be introduced at a pre-determined moment in time**, to lower the uncertainty of employers and employees.
- The minimum wage reforms should be **coordinated with other labour market reforms**, and the reforms of the tax-benefit systems.
- All changes should be **consulted with social partners** and independent technical experts.

### What will be the consequences of introducing a minimum wage in Germany?

The German minimum wage will be set in 2015 at 8.50€ per hour. According to the newest findings of Kai-Uwe Müller and Viktor Steiner (DIW Berlin), such minimum wage will have a substantial impact on the wage distribution. At the same time it will have a very limited effect on available net household income distribution of low wage earners, reduction of means-tested transfers and progressive income taxation. Thus the minimum wage would not be an effective redistributive tool for Germany.

Source: *Kai-Uwe Müller, presentation: „Distributional effects of a minimum wage in a welfare state. The case of Germany”*

### Percentage change and number of changes of the minimum wages in OECD countries (2000-2012)



Source: Herwig Immervoll on the basis of the OECD data



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