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4. Information, Youth, and the Labor Market

Theme 4.1: Potential Cultural Gaps between Youth and Firms

Young people have had limited exposure to work life, and hence to the expectations of employers about adequate behavior in the workplace. This often translates into conflicts between employers and employees and short job tenure.

Many countries have adopted a set of school-to-work programs designed to address this issue (Stern et al. 1997). These include job shadowing (following a competent worker through the work day); mentoring (matching students to an individual in an occupation); cooperative education (combining academic and vocational studies); work in a school-sponsored enterprise; tech prep (a planned program of study with a defined career focus); and internships or apprenticeships.

Neumark and Rothstein (2005) analyzed surveys from the National Longitudinal Survey of Youth (NLSY) data in the US to explore the effectiveness of these programs. They found that internships and apprenticeships, cooperative education (involving a combination of academic and vocational study), and school-sponsored business were the most effective interventions for men in terms of subsequent employment rates. For women, they found that internships or apprenticeships were the only effective measure.

More evidence is needed to understand the effects of these programs and the mechanisms behind them, and to address their shortcomings. For example, Eby et al. (2008) provide a meta-analysis of findings in the psychology literature about the effects of mentoring. They report substantial positive
effects on attitudinal, behavioral, health, relational and emotional outcomes. However, as pointed out by the authors, these results are more correlations than real causal relationships.

Apprenticeship programs typically require young workers not only to find a trainer enterprise but also to stay with that enterprise for the entire length of the apprenticeship. In practice, both requirements are often difficult, with many youths dropping out from the apprenticeship system because of an initial mismatch and increasing tension between the youth and his/her tutor within the firm. As a result, around 20 percent of young people in apprenticeships drop out. Crepón et al. (Ongoing) are currently testing one attempt to close this gap in France. The intervention assigns young people to a mentor who assists the youth in identifying crafts and firms, establishing a good relationships between the young people and their tutors within firms, and setting realistic expectations regarding the youth’s and the firm’s demands and behaviors.

Another model is the Career Academy, which is a type of job shadowing program. Its purpose is to send young people (typically still enrolled in school) on regular visits to firms, where they can observe the firm’s practices and people’s behaviors. It is one of the few such programs that have been evaluated using a randomized controlled trial (Kemple, Poglinco, and Snipes 1999) and, significantly, has been evaluated over a long period. Eight years after random assignment, the program produced sustained earnings gains of 11 percent on average, concentrated among young men. Career Academies also produced an increase in the percentage of young people living independently with children and a spouse or partner.

Summer or part-time employment while youth are still in school may facilitate school-to-work transition by familiarizing students with workplace culture and fostering traits that are conducive to future career success (Schoenhals, Tienda, and Schneider 1998). Longitudinal studies demonstrate the importance of work in fostering personal responsibility and developing autonomy; the latter effect was found to be more pronounced in girls than in boys (Steinberg et al. 1982). Using US longitudinal data on male students, Meyer and Wise (1982) show strong correlations between hours worked during high
school and wages earned in the first four years following high school graduation. The estimated effect of working part-time during high school on annual income was estimated to be potentially as high as 30-35 percent.

Ruhm (1995, 1997) uses data from the National Longitudinal Survey of Youth to assess the impact of part-time employment during school on future economic outcomes. He finds that high school seniors who worked part-time had substantially greater future earnings, fringe benefits, and occupational status. In particular, working ten (20) additional hours per week increased future earnings by 14 percent (22 percent), work hours by 94 (182) hours per week, and total compensation by 8 percent (11 percent). Ruhm’s results indicate that part-time employment during school increased investments in human capital and eased the transition from school to work, especially for students who went straight from high school to the workplace. The Meyer and Wise (1982) and the Ruhm (1995, 1997) studies must be interpreted with caution, however, as they do not adequately control for unobserved heterogeneity and selection into part-time employment.

Hotz et al. (1999) use the same dataset and employ dynamic selection models to test the robustness of Ruhm’s results. They find that the magnitude and significance of the reported benefits of part-time employment to be significantly smaller under their preferred specification. Consequently, they argue that heterogeneity and selection drove up the estimates of the Ruhm (1995; 1997) studies. Light (1999) further builds on Ruhm’s and Hotz et al.’s findings by using the same dataset and applying IV/GLS techniques. She finds significant but small direct effects (on the order of 2-6 percent) of part-time work in 11th and 12th grade on post-graduation labor market success. She also argues that part-time work poses an additional indirect effect on future labor prospects by inducing students to take more vocational classes, which further prepare them for the labor market.

While the majority of the work on part-time employment has been conducted in the United States, two studies find similar trends in other developed countries. Using longitudinal survey data from Australia, Robinson (1999) finds that having a part-time job during secondary school significantly
reduced the length of unemployment following high school graduation. Hakkinen (2006) uses panel data of Finnish university students and finds that employment during university substantially increases earnings in the year following graduation. However, the effect quickly attenuates over time.

In developing countries, work and school compete for youths’ time from childhood onwards. Heady (2003), for example, uses panel data of Ghanaian households and finds that in addition to decreasing school attendance, child labor leaves children with less energy for class and pulls children’s interests away from school. Research regarding the effectiveness of part-time labor in preparing youth for full-time employment in developing countries is sparse, and more work needs to be done on this topic. Interesting research could be undertaken to help address the extent of the cultural gap between the young people and world of work and the ways to close it.

**Theme 4.2: Information Imperfections Regarding Labor Market Entry**

A key strand in the literature on the underemployment of young people is their knowledge of the labor market and their manner of searching for work. Variation in the availability of information among job seekers may account for a large share of the heterogeneity of labor market outcomes. Because of their age and lack of experience, youths may be especially disadvantaged in knowledge of the labor market. In developing countries, both employee- and employer-side information barriers are prevalent. To take one example of the serious consequences of this mismatch, Egypt possesses 1.5 million unemployed youth, while 600,000 job openings in the formal sector sit vacant (AfDB et al. 2012).

The channels through which information travels also affect whether individuals can find jobs. Personal contacts and social networks are one means of collecting information, and they play a major role in the job search process (Mortensen and Vishwanath 1994; see also Ioannides and Loury 2004 for a review of the literature). Social networks operate on several levels, from merely passing on information about a job vacancy to providing a recommendation to an employer. Based on a series of studies that span
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the past three decades and using a variety of data sources from both the US and other countries, Topa (2011) estimates that at least half of all jobs are typically found through informal contacts.

Youths, however, often lack access to beneficial social networks. Granovetter (1973) breaks down social networks into “strong” and “weak” ties, each of which has different implications for the job search. Strong ties, such as those among family and close friends, tend to have many other ties in common, so there may be information overlap. Weak ties act as a bridge, sharing information between two groups which interact less frequently. Weak ties may bring job seekers into contact with individuals who have a higher occupational status, and therefore they tend to be more productive in finding a job than strong ties (Yakubovich 2005). Montgomery (1992) distinguishes two reasons for this differential: weak ties relay job information more frequently than strong ties (Granovetter 1973), and/or job offers that come from weak ties may be drawn from a better distribution (Lin, Ensel, and Vaughn 1981). Since they do not have many professional contacts when they enter the labor market, youths are more likely to use strong ties than weak ties and therefore be less successful in finding a job.

Recent empirical research has attempted to further investigate the relevance of networks for labor market integration. Munshi (2003) and Edin, Fredericksson, and Aslund (2003) find a positive relationship between the number of network members and successful labor market outcomes in the US and Sweden, respectively. Beaman (2012) finds a more heterogeneous relationship between social network size and labor market outcomes: the impact of the size of the network depends on the length of time the other members have been part of the network. Having a greater number of new members in one’s network is associated with a negative relationship between network size and employment outcomes, while having more tenured members in one’s network causes network size to positively affect employment outcomes.

Much of the recent literature has analyzed the role of neighborhood effects in labor market outcomes. Bayer, Ross, and Topa (2008) and Topa (2001) find a positive impact of social interactions among neighbors, and Calvó-Armengol and Jackson (2004) and Topa (2001) show that this effect is even
stronger if more individuals in the neighborhood are currently employed. Being surrounded by social contacts that are also unemployed may make it more difficult to find a job.

Recently, there has been increased research and policy interest in using mentoring programs to facilitate the development of important social networks for youth. In France, an ongoing randomized experiment tries to assess the impact on employment of providing youth with a mentor versus providing youth with information about current job openings, the content of the jobs, and the required skills (Cahuc et al. Ongoing).

More generalized interventions to improve access to labor market information may further help rectify information mismatches between employers and youth. Giving youth greater access to the information regarding the wages, skills, and training needed to succeed in the job search may improve youth integration into the labor market. In developing countries, the spread of cellular phones has provided better information systems to guide job seekers to places with greater job opportunities. Public employment services may facilitate information flow between employers and job seekers – however, public employment services are difficult to find in developing countries, and what few services exist have not reported significant success for youth (AfDB et al. 2012).

In order to improve youth’s labor market integration, we need both more evidence about the effects of networks on the labor market integration, as well as more programs to build networks or integrate youth into existing networks. The analysis of youths’ access to social ties and the implications for employment outcomes would theoretically apply to developing country settings as well. However, the lack of work in this area precludes assessment as to whether the relationship actually holds in practice. More empirical studies of social networks within both urban and rural settings in developing countries would better answer the question of how various facets of social connectedness can be leveraged to benefit youth labor market outcomes.
Theme 4.3: Information Asymmetries and Youth Abilities

One of the main information problems in the labor market is asymmetric information on worker productivity. When there is asymmetric information, low-quality workers exert a negative externality on higher-quality workers. For example, due to the large variation in quality for vocational schools in Egypt—which made it difficult to assess the signal value of vocational school employers were especially hesitant to employ vocational school graduates (van Eekelen, de Luca, and Ismail 2001). The problem of asymmetric information may be especially important for young people because they may have few ways to signal their quality; this is a reason why labor market intermediaries play a so strong role in the functioning of labor markets. Being able to credibly signal one’s own productivity may be a key asset in the success of one’s job search, and producing referrals is one of the possible ways to do so. Therefore, one possible avenue for policy is building a credible system of referral. What follows is a review of evidence about the signal effect of referrals in the labor market.

Pallais (2011) conducted a field experiment in a large online marketplace known as oDesk. She provided randomly chosen young people registered at the online marketplace with jobs, and for a subset of them she provided information about the quality of the work they did. She was then able to measure their occupation rates and their reservation wages, the minimum wages at which workers are willing to work. The results show that having a first work experience is in itself a good signal in the labor market, and that workers signaled as high quality fare better than others, with higher occupation rates and higher reservation wages. Thus, the observed effects are more related to information revelation than skill acquisition, supporting the view that improving signaling is a key labor market intervention.

Employee referrals provide another way to signal productivity, and may be a useful screening mechanism for employers to the extent that current employees refer people of similar aptitude. By relying on employees, employers can also ease the adverse selection problem. Individuals with employed connections will be more familiar with working conditions and routines and perhaps will have more
realistic expectations about employment in a given firm. Recruitment and training costs are reduced and search costs are lowered on both sides.

A study of employers’ treatment of job applicants (Culp and Dunson 1986) suggests that a lack of references is a significant barrier for youths looking for work. From the employer’s point of view, a lack of a track record in the labor market adds to the uncertainty and risk involved in employing young people. Kugler (2003) presents evidence that at a sectoral level, employee-referred workers tend to have higher wages and lower quit rates, suggesting that referrals provide good matches and thus close information gaps between firms and potential employees. Using referral as the only method of recruitment would perhaps not be beneficial to disadvantaged youth, as it reduces the pool of applicants to those who have employed social connections and excludes those who are forced to take more formal approaches due to lack of contacts.

According to Fafchamps and Moradi (2009), employee referral could have three possible benefits: to aid information gathering (employee referral should help the employer with making a judgment on whether a person’s unobservable characteristics will contribute to or reduce productivity); to increase productivity of future employees (the current employee will exert peer pressure or motivate the new recruit to be productive); and to reduce search costs. Using colonial-era military recruitment data from Ghana, Fafchamps, and Moradi do not find evidence that referred employees had more productive unobservable traits and suggest that the motive for using a referral system is lower search costs. Evidence from a field experiment in India (Beaman and Magruder 2010) highlights the notion that employer incentives may not be aligned with network incentives. If the employer incentivizes the current employee appropriately, they will tend to refer a more skilled person for a job; if not, the employee may be more likely to refer a friend or family member, with less focus on ability.

Ability testing and credential systems are two additional methods of revealing information about ability. In ability tests, the skills needed to perform a job are translated into a test, which enables employers to select higher-ability individuals. The organization of formal credential systems would allow
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the relay of information about candidates’ performance to the labor market. We need more ideas about ways to solve the asymmetric information problem for youth in the labor market and more evidence about the effects of these interventions.

**Theme 4.4: Employer Beliefs about Youth Employability**

In the absence of adequate information about young people’s ability, beliefs may play a key role in firm decisions. Firms may assume that young people have low productivity, and this may reduce their demand for young people as employees and, more generally, negatively affect the integration of youth in the labor market.

Managers’ beliefs that workers will perform poorly may actually cause poor performance (a self-fulfilling prophecy). In an ongoing experiment in a large French firm (Pallais and Parienté), the beliefs of managers about the abilities of women and disadvantaged groups are first measured using an implicit association test (IAT). Then, workers are randomly assigned to managers. After three months, objective measures of worker performance are collected, and workers and managers are surveyed about the employment experience. This experiment allows the researchers to answer several questions. First, do women and members of disadvantaged groups perform more poorly if they are assigned to a manager who is biased against them? If so, what is the mechanism though which managers’ beliefs affect worker performance (e.g., do managers assign workers they are biased against to worse tasks or spend less time training them)? Finally, given the importance of managers’ evaluations on workers’ employment trajectories, managers’ evaluations of workers will be compared to objective criteria on workers’ actual performance to test whether managers give workers they are biased against poorer evaluations than are warranted. Running similar experiments in developing countries will help determine whether and the extent to which such biases characterize the workplace for youth there. It is possible that, if developing
countries have fewer formally established workplace rules and regulations regarding fair employee practices, manager bias may be exercised more intensely and more greatly influence youth productivity.

5. Location, Neighborhood, and Mobility

**Theme 5.1: The Role of Location and Spatial Mismatch in Labor Market Integration**

One obvious issue related to integration into the labor market is physical access to areas were employment opportunities exist. The *spatial mismatch hypothesis* attempts to explain minority low-skilled workers’ underemployment by the fact that they are physically disconnected from job opportunities (see Gobillon, Selod, and Zenou 2007 and Ihlanfeldt and Sjoquist 1998 for a comprehensive review). Longer distances to jobs induce bigger costs to become employed. High transportation costs to reach employment areas or employment agencies may exceed the benefits of searching for a job (Holzer, Ihlanfeldt, and Sjoquist 1994). The costs of relocation near job opportunities may also prevent the unemployed from searching actively (Smith and Zenou 2003; Wasmer and Zenou 2006). Getting information on jobs can also be costly, and informational frictions are likely to increase with physical distance (Ihlanfeldt 1997).

A second channel through which location may negatively impact integration is residential discrimination. Living in a deprived area may constitute a bad signal in the labor market. The term *redlining* was coined to describe the practice of excluding people living in certain areas from access to credit. Similarly, employers may be reluctant to hire workers from segregated areas based on the belief that workers living in these areas are, on average, less productive than others. For instance, employers may think that the productivity of workers decreases with distance to jobs (Zenou 2002), because of tiredness or lateness induced by high commuting time.
A bad location is *a priori* detrimental to everyone; however, some groups may be more affected by the mechanisms described above than others. The literature traditionally focuses on blacks in the US and/or on the poor. Youth may also suffer more than other individuals from a bad location since they are also more likely to be at a greater informational distance from job opportunities.

Many programs, especially in the US, have tried to cope with these spatial issues. Three types of policy intervention can be distinguished. The first idea is to move people closer to employment areas. In the US, this has typically meant moving them from (usually black) inner cities to (predominantly white) suburbs. Examples include housing programs such as the Gautreaux initiative in Chicago and the US Department of Housing and Urban Development’s Moving to Opportunity program, which provided vouchers to low-income families to help them move from disadvantaged areas to new neighborhoods. A second possibility is to improve transportation access for people living away from jobs (Holzer, Quigley, and Raphael 2003). In an ongoing study in South Africa, Banerjee and Sequeira are measuring the impact of subsidizing transportation costs on job search activity and employment. The intervention provides unemployed youth residing away from economic centers with transport vouchers to travel to economic centers where there are more job opportunities. A third policy response is to encourage firms to locate near deprived neighborhoods. This is the aim of enterprise zones, where firms benefit from preferential tax treatment in exchange for locating in designated zones.

A number of studies on spatially-based policies have failed to find evidence that they are effective in reducing employment gaps (Hellerstein and Neumark 2011). However, most of this research to date has focused on blacks in the US. More evidence is needed on the effects of all three types of interventions—moving workers, making transportation easier, and moving jobs—in other contexts, specifically on youth. If the results discussed are reflective of policy effects on the general population, it is plausible that they will apply to youth (since youth are, after all, a subset of the general population). However, because a variety of previously mentioned factors set youth apart (larger propensity for risky
behavior, higher future discount rates, greater likelihood of engaging in criminal activity, etc.), the impact of spatially-based policies may be quite different for youth.

In developing countries, migration and seasonal migrations are ways to improve labor market integration. Youth from rural areas may benefit from moving to urban areas where job opportunities tend to be more prevalent. Migrants benefit both the urban areas that host them as well as the rural areas that send them, and the income of rural households could substantially increase from remittances sent by migrant workers. However, credit and childcare constraints prevent workers from moving to areas with greater job vacancies. Migration may be especially difficult for youth, who have had less time to build up savings to finance relocation. For multigenerational households in rural South Africa, for instance, the likelihood of migration and employment for prime-aged workers significantly increases when credit constraints are relaxed (Ardington, Case, and Hosegood 2009; Posel, Fairburn, and Lund 2006). Similarly Bryan, Chowdhury, and Mobarak (2012) find that random assignment of a monetary incentive for migrants in Bangladesh during seasonal famines increased long-term migration. Bryan et al. postulate that the added income made migration possible for households who otherwise would not have been able to support the migrant job seeker. It would be interesting to know more about the ways in which people decide to make such a large move.

Given the importance of credit constraints on migration outcomes, would relocation programs be an effective method of correcting for spatial mismatch in developing countries? On the one hand, relocation programs may help youth more effectively migrate to areas with higher labor demand by covering moving costs and mitigating uncertainty. On the other hand, relocation programs may be more difficult to implement and sustain in developing countries if there exist greater barriers to residential mobility and stringent rules that restrict choice of residence for low-income families. Due to stark differences in living conditions between low-income families in developed countries relative to those in developing countries, it is plausible that relocation programs may have drastically different impacts in developed compared to developing countries.
Theme 5.2: The Role of Social Networks in Access to Jobs

An alternative hypothesis holds that labor market integration may not depend so much on where one lives as whom one lives with. Instead of a spatial mismatch, some studies refer to a social mismatch that could be spatially based. There is a great deal of evidence that neighborhoods have a large effect on a range of outcomes. Crane (1991) proposes that social problems may spread in a neighborhood much like an epidemic. Using French data, Goux and Maurin (2005) find that school performance is highly correlated among children from the same neighborhood.

Using census-tract-based data, O'Regan and Quigley (1996) measure “exposure” as the probability for a member of a group that a randomly picked resident of his or her tract is a member of another given group. They show that exposure to whites increases the probability of employment for black and Hispanic youth, and that exposure to poor people decreases employment probabilities. Similarly, studying the impact of the Gautreaux program, Mendenhall, DeLuca, and Duncan (2006) find that location in a city or suburb did not significantly explain differences in employment outcomes, but that the composition of the neighborhood did.

According to Hellerstein and Neumark (2011), place-based policies “are largely ineffective in increasing employment, likely because spatial mismatch is not the core problem facing urban blacks, and because […] the role of labor market networks was weakened.” Moving blacks toward jobs, or creating jobs where they live, is unlikely to increase employment efficiently if it neglects labor market networks. Therefore, the authors recommend that spatially-based policies also target labor networks.

Some programs have tried to adopt this dual focus to encourage access to jobs. One such program is Jobs-Plus, which attempted to deliver an employment and training program within public housing developments. One of its core components sought to strengthen labor market networks among residents. In a final report, Bloom, Riccio, and Verma (2005) find a positive effect of the program on employment,
although it is difficult to assess the specific impact of the network component of the program, which was called the “community support for work.”

We need more attempts to develop local employment policies--for example, policies aimed at developing local labor networks, policies based on local labor networks, or policies aimed at developing local entrepreneurship. Programs that attempt to develop local labor networks may see greater success than programs that focus on spatial relocation in developing countries, since the former enhances the potential for informal sector development, which employs a larger proportion of the population in developing countries, while the latter involves the removal of youths from the communities in which their social ties are strongest.

To date, few studies have attempted to test the effects of relocation programs or local labor networks in randomized controlled settings. Such studies would be especially valuable in addressing the needs of vulnerable populations, who are disproportionately likely to reside in segregated areas. Youth lack the means and resources to relocate in the absence of a steady job, yet the evidence suggests that residential location also limits youths’ abilities to find steady employment. Use of pilot interventions to determine the most effective methods in combatting such mismatch problems, such as identifying reliable ways to develop strong professional social networks for youth, would provide useful information for future research in both developed and developing countries.

6. Labor Demand for Young People and Contracts

Theme 6.1: Employment Contracts and Labor Demand for Youth

The idea that labor contracts shape firms’ labor demand is an old one. The duration of contracts, as well as the relative costs of hiring workers and the ability to terminate a worker’s contract, affect firms’ choices in the labor market. If firing costs are too high, firms will choose to retain inefficient workers
while perhaps overlooking potentially more productive individuals who are unemployed. Another possible effect is that firms may be reluctant to hire workers without knowledge of their ability to fill the job properly, in anticipation of the difficulty involved in firing them if they prove incompetent. In general, increased firing costs tend to reduce labor market turnover. These effects can be particularly magnified for youth, as asymmetric information, which increases the deterrence effect of stronger employment legislation on employment, is stronger for young people.

For example, the relatively low experience levels of youth can interact with minimum wage laws to reduce demand for younger workers. If young people have less experience and are indeed less productive than other workers, then firms should be willing to offer them lower wages upon their entry into the labor market. However, the distribution of wages, even for those with more experience, is often strongly concentrated around the minimum wage. Although some youth are prepared to work for below the minimum wage to compensate for their lack of experience, the market wage of young people cannot adjust and they are often excluded from the labor market. Many proposed policies offer some wage adjustment, such as different minimum wages for young people or labor tax reductions so as to lower the labor cost while keeping the wage unchanged.

MacLeod (2011) and Kahn (2007) recently surveyed hundreds of studies looking at the effects of employment legislation on employment outcomes for European countries. Most of these follow the Organization for Economic Cooperation and Development’s (OECD) seminal work on the computation of indexes of employment policy legislation and their correlates with employment across countries and time. These studies generally find little relationship between different types of legislation and employment levels, and despite the tremendous work devoted to collecting and synthesizing information about employment legislation, these relationships are not likely to identify causal links between employment legislation and employment outcomes. Other studies have examined the impact of legislative changes that focused on specific segments of the economy. For example, Kugler (1999) examines a 1990 reform in Colombia that lowered dismissal costs in the formal but not the informal sector. She finds an increase in
labor market turnover in the formal sector compared to the informal sector. Similarly, Kugler and Pica (2008) find that Italian reforms of 1990, which increased small firm dismissal costs, reduced hires and fires for small firms relative to larger firms. Other studies examine regional differences within a country. For example, Besley, and Burgess (2004) show that state-level changes in employment protection in a pro-worker direction induced lower output, employment, investment, and productivity in registered or formal manufacturing in India. They also show that output in unregistered or informal manufacturing increased in those states. Magruder (2011) shows that a centralized bargaining system that required that agreements in large unionized firms be extended to nonunionized, smaller firms in South Africa had strong and significant negative effects on employment, mainly concentrated in small firms and start-ups. Autor, Donohue, and Schwab (2004) find the adoption of wrongful-discharge protections by US state courts led to a significant reduction in employment flows, capital deepening, and a rise in labor productivity.

Hiring and firing costs clearly tend to reduce labor market turnover. However, they may also cause firms as well as workers to be more confident that they will appropriate a fair share of the returns to mutual investment in the relationship, for example in training. This effect is largely determined by the nature of the employment contract. Temporary contracts, as they lower the cost of hiring and allow firms a chance to uncover more information about their employees, may favor the employment of young people. The value to youth of obtaining a temporary contract is questionable, however, if the introduction of temporary contracts results in less investment in youth’s human capital, less training, lower wages, and, of course, less job security than a permanent contract would offer. There is evidence that temporary jobs pay less, offer less training, and are less satisfying than regular jobs (Booth, Francesconi, and Frank 2002; Kahn 2007). Furthermore, temporary contracts do not appear to be a pathway to permanent employment; rather, they are used as a substitute for permanent contracts. Conversely, work examining the effects of temporary agency employment on unemployed workers in Denmark, find that temporary agency employment has a positive effect on post-temporary position wages and length of employment,
especially for certain immigrants and low-educated workers (Jahn and Rosholm 2010; Jahn and Rosholm 2012). Further research is necessary to tease out the mechanisms behind these conflicting findings.

Blanchard and Landier (2002) consider some partial employment protection legislation reforms in France that concentrated on relaxing regulation around the use of temporary contracts. They find that without also addressing legislation for permanent contracts, this kind of partial reform had perverse effects: the probability of a fixed-term contract increased, but there was also higher turnover without a shortening of the average unemployment period. Even if employers find what seemed like a good match, they may still rather keep staff on temporary contracts than risk offering a permanent contract with higher firing costs (although this probably depends on the skill level of the job and the tightness of the labor market). There is empirical evidence from Spain (Dolado, Garcia-Serrano, and Jimeno 2002) that partial reforms introduced in the 1980s helped drive the incidence of temporarily employed workers up to over one-third of the workforce, the highest in the EU. High turnover and low conversion of temporary into permanent jobs suggest employers may have been using the temporary employment mechanism as a way to make less costly adjustments to the economic environment, rather than as a means to estimate whether the worker could be a good match for a more permanent position. This high share of temporary contracts persisted into the nineties, when a more balanced reform was enacted.

Another possible avenue for policy is to concentrate reforms on specific demographic groups, such as young people. If there is a negative interaction between high fixed costs of hiring and firing and asymmetric information, and if asymmetric information is larger for certain demographic groups, then the negative effects of employment protection on job flows will be magnified for that group. Policy-induced changes in the structure of contracts can have strong effects on the relative demand for workers from at-risk groups. Kugler, Jimeno, and Hernanz (2005) study the effects of Spanish reforms in 1997 that reduced dismissal costs for permanent jobs for young and senior workers. They find a relative increase in permanent employment for these groups. Acemoglu and Angrist (2001) show that changes in
employment protection reforms concentrated on disabled workers also have large effects on relative employment flows for those workers.

One key issue associated with changes in contracts for specific demographic groups is that they are likely to induce substitution effects. Easing firing and hiring rules for some groups may increase the demand for these groups, but simultaneously reduce the demand for other groups. It is important to account for these potential displacement effects.

Some aspects of contract features and their impact on demand for youth need to be explored in further detail, such as the nature of temporary-contract jobs for youth and their impact on human capital investment: Do they lead to greater integration in the labor market, or does a succession of short-term contracts weaken their attachment and wage/career possibilities? What are the optimal contract features needed to engage youth in the labor market? It is plausible that such labor force dynamics could apply to youth in developing countries, but are there any relevant structural differences between developed and developing countries that would affect the relationship between temporary-contract jobs and youths’ labor market participation?

7. Active Labor Market Policies (ALMPs)

With the intention of reducing unemployment, including youth unemployment, governments around the world have implemented many different active labor market policies (ALMPs). These can be organized under four main categories: employment services, labor market training, wage subsidies, and job creation. There has been a great deal of research effort devoted to evaluating the effects of these policies. Card, Kluve, and Weber (2010) and Betcherman, Olivas, and Dar (2004) provide very useful overviews of the results to date. In general, the evidence is not very supportive for ALMPs. For example, Card, Kluve, and Weber (2010) do not identify any single measure that had a significant effect across the studies surveyed, though they do provide relative rankings of interventions by effectiveness. Overall, subsidized public
sector employment programs are found to have the least favorable estimates; job search assistance programs appear to be effective in the short run, while training either on or off the job provides better results in the medium-to-long run. One clear result from the literature is that programs specifically targeting an age group within the population, such as those under 25 or over 50, are found to be significantly less efficient. Therefore, the overall picture from the existing literature is that ALMPs fail to properly address the needs of young people.

However, the evidence from these evaluations suffers from several problems. First, they have been obtained using nonrandomized methodologies, which may result in biased estimates of program impact. This is especially true of public work programs, which are usually assigned to unemployed individuals who are very detached from the labor market. Second, these studies usually rely on very large administrative files. This has some drawbacks because, as noted by Card, Kluve, and Weber (2010), the outcome variables one can obtain from these files are not always very informative. Frequently these files record only exit from unemployment, without information on the type of exit and the type of resulting contract. Another drawback of these files is that the programs evaluated are classified under very broad and aggregated categories, making it difficult to precisely understand the effect of specific interventions. Moreover, the results that have been found are in many cases probably in fact the average of the effect of many different interventions, some of them having positive effects and others zero or even negative effects. The most relevant issue may be how these policies can be made efficient, instead of whether these policies are efficient.

Across the board there has been little work done to assess the long-term effects of ALMPs; rather, much more is known about short-term effects. The hypothesized “stepping stone” effect is an important one for research. The basic idea behind these programs is that labor experience allows young people to increase their skills, making them productive enough to find jobs by themselves in the future. It would be interesting to know the extent to which the stepping stone effect exists, and whether the implementation of these policies helps reduce the problem of asymmetric information. Research should focus on the
effects of ALMPs, such as employment programs, on the quality of matches and the duration of employment. The discussion below identifies several additional issues that have yet to be sufficiently addressed.

**Theme 7.1: Employment Services**

This broad category covers interventions designed to improve the matching between job seekers and employers. The basic objective is first to shorten unemployment spells, but also to provide young people with a real first job experience. Employment services usually include both assistance in the job search and monitoring of the job seeker’s progress during the search. Providing unemployed and especially young people with a reinforced counseling scheme has been a major direction of public employment policy in developed countries. These services are usually provided by public employment services, but in some circumstances, they may be offered by other labor market intermediaries.

Results in the literature tend to find limited, though usually positive, effects of counseling services. In general, our understanding of the precise effects of these policies has been limited by the fact that usually a broad set of services is evaluated, rather than a precise program intended to have a specific effect or to assist a specific population. The few existing RCTs related to counseling services tend to show positive results. In France, two large random experiments show large effects of counseling services in the short run, but not in the long run. This suggests that counseling services helped the unemployed to find a job, but that the job did not provide them with sufficient labor market experience. One experiment, Behaghel, Crepon, and Gurgand (2009), found that job seekers performed less well when the same counseling program was offered by private providers as opposed to the public sector, holding the incentives in counselor contracts constant. This study also found that when counseling services were provided by private operators, features of the counselors’ contracts strongly shaped job seekers’ performance. In another experiment in France, Crepón, et al (2012), detected potentially large
displacement effects. The potential conclusion from these experiments is that counseling programs can be successful in the short run, but there is a potential to increase their efficacy in the long run. Given the large displacement effects, counseling services may act more like redistributive policies - the population that benefits the most from them would be those more detached from the labor market. However, these results must be confirmed by new experiments.

There are several potential research directions that can increase our knowledge of employment services programs:

*Does providing youth with employment services improve their labor market prospects?*
This issue is especially relevant in developing countries, where frequently no services are provided to young people.

*Can employment services increase the motivation of young job seekers?*
Motivation plays a key role in the intensity and the efficacy of search behavior. Young people who are far removed from the labor market can have very low motivation and little confidence in the advice given to them, including career advice. There are several ongoing experiments in France and Denmark that are testing various ways to foster the motivation of young people.

*Program content: lessons from behavioral economics*

Some lessons can also be drawn from behavioral economics. In a recent paper Babcock et al. (2012) review how findings in the behavioral economic literature can be used to propose new content for counseling services programs. They especially put emphasis on biases and error in setting wage expectations as well as procrastination in searching for work. Individuals may undervalue the benefit of attending counseling programs. Authors suggest policies that increase the instances in which individuals are defaulted to counseling programs. They also suggest easing the access to counseling services and
improving their content with clear individualized and readable information, experimenting with the framing of job opportunities, and using various tools devoted to removing bias from expectations.

Program content: what channels of the job search should counseling focus on?

The standard job search channel in many counseling schemes is through vacancies posted at the Public Employment Service or collected by a private intermediary. Beyond just providing a list of vacancies, reinforced counseling amounts to helping young people choose suitable job offers and apply to them. It may also involve providing young people with information about which sectors are providing jobs and what skills they need. Having the right skills or being on a track to acquire them is the key issue. However, there are also informal search channels, in which just knowing the right people is the key determinant of finding a job. In many developing countries, this is often seen as the only way to find a job. Facilitating job searching through this channel is accomplished primarily by providing young people with mentors. There is currently an experiment underway in France comparing the effects of these two types of search channels.

Program content: what are the effects of counseling versus monitoring?

Frequently, programs are a mix of counseling and monitoring an applicant’s attendance and effort in the job search process. It is important to disentangle the effects of these two aspects of these interventions. Attending regular monitoring appointments is often compulsory and may be accompanied by sanctions (e.g., reduction or termination of unemployment benefit) if a lack of search effort is observed. The threat of sanctions in the event of non-compliance in the job search appears to increase exit rates from unemployment ex-ante (Svarer 2007; Lalive, van Ours, and Zweimuller 2005). However, this increase in exit rates may come at the expense of the quality of the jobs found. Arni, Lalive, and Van Ours (2009) show that the threat or enforcement of sanctions has a positive effect on exit from unemployment, but leads to a reduction in the quality of the position found, both in term of job stability and earnings.
Meetings with caseworkers may also have both a counseling and a monitoring effect. It is during meetings with the unemployed that the caseworker gets information about search effort and gives new directions. Pedersen, Rosholm, and Svarer (2012) use a set of randomized experiments to measure the ex-ante threat effect of the meeting and the ex-post effect. They find large ex-post effects of meetings and large ex-ante threat effects for men.

**How should programs deal with the dropout problem?**

Counseling services may require a commitment from participants over a significant period of time. Due to time inconsistency, financial constraints, or a reduced perception of the value of the counseling scheme, young people often drop out of the program. What incentives can be provided to prevent youth from dropping out of programs? There is currently a program in France that provides young people with cash transfers conditional on their continued participation in their counseling scheme.

**The role of caseworkers**

Although we do not know much about the impact of caseworker skill on their success in counseling young people, the outputs of counseling programs seem to depend strongly on caseworker effort. Behncke, Frolich, and Lechner (2008; 2010) show that caseworkers matter. Outcomes for the unemployed appear to be related to the caseworkers’ beliefs about their role and the characteristics that they may or may not share with the unemployed. This tends to show that the motivation and type of effort put forth by the caseworker affect the efficiency of services.

**Who should provide employment services?**

Existing labor market programs and the intermediaries that they rely on are quite heterogeneous: some programs are operated by the public sector and others by the private sector. Exploring these differences across developing and developed countries will provide greater information regarding who is best equipped to provide employment services across different contexts. In general, there is great variety in the organization and regulation of the market of intermediaries. Identifying the effect of these different arrangements on the success of various interventions is a first-order issue. A related question is how
programs might use the strong sensitivity of private operators to their contract to improve labor market outcomes.

**Theme 7.2: Labor Market Training**

One of the most popular explanations for youth unemployment is skill mismatch: there are skills needed and valued in the labor market, but these are not the skills youth have. Providing young people with the right skills through training is therefore seen as a major policy priority.

Overall, the picture arising from the literature is that training has limited impact. Reviews in Card, Kluve, and Weber (2010) and Betcherman, Olivas, and Dar (2004) show that training has little effect, though some studies in Germany find positive results in the long run (Fitzenberger, Osikominu, and Völter 2007; Lechner, Miquel, and Wunsch 2004). We do not know the reasons for this general failure, partly due to the fact that although there is great heterogeneity among training programs, only the effects of broad categories have been evaluated. Nevertheless, there remains a feeling that training must be a key component of youth labor market integration, given the large gap between the very low skill level of young people and the needs of firms, especially in developing countries.

Some encouraging results have been obtained from the few RCTs that have been conducted on training programs to date. Schochet, Burghardt, and McConnell (2008) carried out an experimental evaluation of Job Corps, a national training program in the US for disadvantaged youths. This appears to be one of the few studies in a developed country with clear positive results. The program was designed to provide general education, social skills, parenting and health education, as well as vocational training. Job placement services were also provided. The training took place in local centers, and participants primarily resided at these centers for the duration of their program. About 70 percent of the control group was enrolled in some other type of non-Job Corps training or schooling. Results showed improved educational attachment: participants spent more time in school or training than they would have had Job Corps not
existed. Employment rates and earnings also increased for youth in the treatment group compared to those in the control group in the initial years after training. Program benefits seemed to fade after the first initial years of training, except for the oldest program participants. Furthermore, while individual outcomes improved, the overall cost-effectiveness of the program may be questionable.

Programs in the developing world that have shown some qualified success also use a balanced combination of measures: a mix of classroom training and on-the-job, internship-style vocational training targeted towards the most disadvantaged youth. A randomized trial in the Dominican Republic found that job training had a positive, albeit unsustained, effect on wages (Card et al. 2011). A more recent randomized trial using a larger sample in Colombia found stronger impacts (Attanasio, Kugler, and Meghir 2009). The program, called “Jóvenes en Acción,” involved three months of classroom training, undertaken by private agencies, followed by three months of vocational training in a private company. The probability of employment rose and wages were, on average, higher for program participants, especially for women. However, we do not know whether this positive effect is due to the vocational training, the internship, or the combination of the two. Training may improve the productivity of young people, but internships may reveal useful information about the quality of a match.

We need to understand why the overall picture about training is so mixed. One possibility is that most studies have looked at training as a broad category, and there is a lot of heterogeneity in training programs. Certain types of training programs may prove more useful for youths’ specific needs than other training programs. A separate but related issue is that youth may lack the means to find the training programs most suitable for their specific needs. Besides answering the question of whether training improves the labor market prospects of young people, research should explore what makes training a more valuable investment for youth.

*How can high-quality training be promoted?*
The quality of training varies considerably, and there is a tradeoff between offering high-quality training to a few people and offering cheap training to a larger set of people. Low-quality training may also be more common since trainers often have poor incentives to provide youths with the right skills. It would be interesting to have experiments where trainers are or are not offered incentives to provide high-quality training.

Apprenticeships are commonly seen as high-quality training. An apprenticeship is a longer-term training arrangement in which young people enter into a contract with a firm and often divide their time between the firm and a training center. The effects of apprenticeships on labor market prospects are not well known, and policymakers may take for granted that they improve the labor market prospects of young people. Apprenticeship programs raise several issues and complications. First, the initial matching of young people to firms may be difficult; youths are very often unable to find a firm willing to offer them an apprenticeship contract. Issues about the contract features, such as the balance of time between the firm and training and the wage level subsidy, likely affect firms’ demand for apprentices. Due to the high demand for and difficulty of finding apprenticeships, many young people fail to find a firm in their sector of choice and end up working in a different sector. This may sidetrack youth into a type of work for which they are not a good long-term match, even if it reduces short-term unemployment. Under such circumstances it is unlikely that there would be a “stepping stone” effect leading to more positive long-term job market outcomes. Therefore, alternative models of long-term vocational training need to be investigated.

Another issue for apprenticeships is the dropout problem. If the relationship between youth apprentices and managers deteriorates, young people may have to find another firm or may drop out of employment altogether. Young people with limited exposure to work life, especially those coming from more disadvantaged backgrounds, may have insufficient knowledge of the expectations of employers and adequate behavior in the workplace. This often translates into conflicts between employers and employees and short job tenure. Here also alternative models of long-term vocational training could be considered.
One attempt to close this gap currently being tested in France is to assign young people to a mentor who is in charge of developing a good relationship between an apprentice and a tutor within the firm, and guiding the youth and the firm concerning the expectations they should have about each other’s demands and behaviors (Crepón et al, Ongoing).

Finally, in countries where the informal economy constitutes a large share of total economic activity, informal apprenticeships may be the only or most effective form of skills training available for youth. However, informally trained youth who are seeking formal sector employment face difficulties in signaling their training to formal employers. Offering a certification for apprenticeships may afford employers a systematic method of recognizing skills acquired during informal training and rectify this information asymmetry (AfDB et al. 2012).

Bruhn and Zia (2011) find mixed effects of a training program on business outcomes in a program conducted in Bosnia and Herzegovina. The program was successful in encouraging young entrepreneurs to make capital investments in businesses: individuals randomly assigned to the treatment group were 11% more likely to undertake new investments. Business practices, loan terms, and investments also improved. Those who had low financial literacy in the beginning of the program exhibited improved financial knowledge, and those with higher financial literacy in the beginning of the program improved their business performance and sales. However, the businesses of individuals randomized into treatment were not more likely to survive than those randomized into control. The authors conclude that business training programs were insufficient to promote business growth in emerging markets, but were nevertheless a necessary component to improving youth business outcomes.

Haan and Serriere (2002) examine a number of training programs focused on informal sector employment in five countries in West and Central Africa. They find that most training programs and vocational institutions fail to focus on the job-relevant technical training that youth desire. Since training programs and vocational institutions are extremely underdeveloped and inaccessible to most youth in Africa, apprenticeships constitute over 90 percent of all training. But low levels of education on both the
teacher’s and the student’s part restrict the ability of the student to obtain the necessary skills and knowledge to obtain employment. If teachers are paid a yearly fee for each apprentice, they have incentive to keep apprentices for as long as possible. Often teachers delay teaching apprentices skills crucial to the trade, and even take proactive measures to prevent apprentices from learning. Restructuring incentive structures for apprenticeships, improving the quality and accessibility of alternative training programs, and offering greater training choices for youth are promising ways to improve the employment prospects of youth in developing countries (Haan and Serriere 2002).

Haan and Serriere (2002) outline some possible ways to improve quality training programs in developing countries. Many interviewed entrepreneurs mention that in addition to technical skills, training programs should teach youth about bookkeeping, management, and marketing. Training programs that develop short courses which focus on technical skills have greater take-up rates and increase household income substantially. In Niger, a post-primary training school increased pass rates on a national exam. In Cameroon, a widespread training program coupled with financial assistance helped 54,000 people find employment. However, the true impacts of the programs are unknown, since these findings were non-experimental and selection bias could have confounded the results (Haan and Serriere 2002).

How should youths be assigned to training?
Assignment to a specific training course is usually made by caseworkers. There is room, however, to test different ways to make these choices, including providing youth with information about skills needed in different sectors and allowing them to upgrade their skills on their own, and providing them with vouchers to finance a training of their choice.

One ongoing experiment tests the idea that young people may efficiently make job placement decisions themselves. Blattman, Fiala, and Martinez (2011) randomly assigned self-organized groups of youth in Northern Uganda to receive cash transfers to use on vocational training or materials to practice a
Overall, groups that received the cash transfer used it to make productive investments: treatment groups received 405 more hours of training and acquired US$300 more in assets. Blattman et al. find a sizable increase in the labor force attachment of those in the treatment group, as well as positive effects on social cohesion within the community. On average, individuals in the treatment group were almost 100 percent more likely to be employed at a skilled job, their earnings were 50 percent higher, and their average hours spent working increased by a third.

*How can demand for training be fostered among young people?*

Evidence shows that the demand for training is very low. In sub-Saharan Africa, youth entrepreneurs in the informal economy have limited information about relevant training programs and are reluctant to enroll since being away from work reduces sales and jeopardizes their business (Haan and Serriere 2002). In developed economies, some evidence suggests that training is seen almost as a disadvantage. For example, Black et al. (2003) show that the threat of training may induce people to exit from unemployment programs. This may also reflect a low perceived value of skills as a way to find a job—actual value of skills notwithstanding—as compared to the perceived value of having a good network.

Demand for training may also increase if credit constraints are relaxed. Hicks et al. (Ongoing) are conducting an evaluation of a randomized voucher program for vocational and technical training institutions in Kenya. The program provides a restricted voucher, which can be used to enroll in a public institution, and an unrestricted voucher, which can be used to enroll in either a private or a public institution. The voucher program increased enrollment and retention rates in vocational schools. Individuals with unrestricted vouchers completed 12 percentage points more coursework than individuals with restricted vouchers, most likely due to the better individual-institution matches that result from the wider range of institution choice and to the high quality of private institutions. The results indicate that
voucher programs can be effective in increasing educational attainment in youth and that unrestricted vouchers lead to better matches between individuals and institutions.

It is probable that individuals underestimate the value of training, and there is room to address the issue of take-up in training programs and have a better understanding of the determinants of the demand. Tools to address demand issues may be worthy of experimentation and evaluation.

**Theme 7.3: Employment Subsidies**

Employment subsidy programs are policies designed to create work opportunities for targeted beneficiaries by subsidizing firms to employ them. The subsidy can have several effects. It can compensate the firm for the potential lower productivity of eligible workers. People with low employability can have access to employment and, in the medium run, benefit from productivity gains either through experience or through training. Wage subsidies are also a way to screen workers and compensate firms for risky choices when hiring among a population on which little information is available. Subsidy programs might enable firms to screen workers, identify the most able, and offer them a more long-term position. Ideally, these interventions would also improve the employability of beneficiaries by the end of the program, which would make beneficiaries more able to find jobs by themselves.

Although results are mixed, the global finding shared by many evaluations of employment subsidy programs is that they help beneficiaries to find a job in the short run. However, the effect vanishes in the long run, and there is little evidence of subsidized jobs being transformed into long-term jobs at the end of the subsidized contract (Card, Kluve, and Weber 2010; Betcherman, Olivas, and Dar 2004).
Katz’s (1998) study of a subsidized employment program in the US finds short-term effects specific to youth. He evaluates the Targeted Jobs Tax Credit (TJTC), a two-year program targeted at vulnerable and disadvantaged workers (among which are disadvantaged youth), which offered a wage subsidy of 50 percent in the first year and 25 percent in the second year. The program increased employment for disadvantaged youth by 7.7 percent.

Randomized experiments studying subsidized employment are scarce, but these also suggest short-run positive impacts, especially when combined with other components, such as training or job search assistance. Galasso, Ravallion, and Salvia (2001) evaluate a randomly assigned wage subsidy scheme targeted to workers in temporary employment in Argentina. The program, called Proempleo, subsidized 50 percent of the first 18 months of wages for workers employed in permanent, regular jobs. The results show that the program helped low-wage workers find regular wage employment. Interestingly, these effects were statistically significant only for women and youth. One striking feature of this study is that, as usual, few firms actually claimed the subsidy, suggesting that there is room for improvement in the implementation of these policies, possibly by reducing administrative costs.

There may be several different reasons for the failure of subsidized employment programs in the medium run, which suggest different solutions:

- Beneficiaries do not reach the skill level necessary to find a job by themselves at the end of the program because the experience accumulated during the subsidized job is not sufficient. Changes in the type and duration of the job may improve the relevance of the experience accumulated.
- Beneficiaries do not accumulate experience because they are not sufficiently motivated by the job. Providing beneficiaries with incentives—for example, through conditional renewal of the contract—is one way to address this problem. Another solution may be to provide beneficiaries with “soft skills” training, with the intention of increasing the perceived social value of being at work.
• Beneficiaries are not able to communicate effectively about their experience and signal themselves convincingly to the labor market after completion of the subsidized job. A possible solution would be to provide participants with referrals and counseling about how to communicate their experiences in their CVs and in interviews.

It is important to note that an increase in the hiring rate of targeted beneficiaries may not necessarily translate into overall gains in employment. Wage subsidies may induce substitution within firms rather than the creation of new jobs. When a subsidy is introduced, it could increase the demand for youth, but at the expense of incumbent workers (Gustman and Steinmeier 1988). Introducing a wage subsidy could, in theory, shift the demand for new hires to young unskilled people without an increase in the total number of new hires, displacing nonsubsidized employees.

Groh et al. (2012) find large displacement effects in a program targeting female community college graduates in Jordan. Before the intervention, only 23 percent of female community college graduates were employed 16 months after graduation, even though at the time of graduation 93 percent expressed the desire to work. The intervention randomly assigned subjects an employment voucher or training in soft skills. Groh et al. find that soft skills training did not significantly affect employment and that the sizable increases in employment from the voucher treatment attenuated four months after the voucher period ended. The temporary increased hiring rate among women in the voucher group did not reflect actual gains in employment, as it was likely due to women in the voucher group displacing women in the control group. Groh et al. conclude that addressing supply-side constraints which prevent the creation of more jobs for college graduates may be more fruitful than skill training or employment subsidy interventions.

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1 The vouchers subsidized employers at minimum wage for 6 months from the hiring date.
Subsidized employment programs may also lead to the hiring of young workers who would have been employed even without the policy, increasing the demand for young unskilled hires only slightly. Because of these two effects, evaluations of the effects of subsidized jobs should randomize at both the firm level and the beneficiary level. For the same reasons, cost-benefit analysis of subsidized programs in the medium and the long run are a first-order issue.

One aspect of subsidy programs in developing countries is the impact of such subsidies on the formalization of jobs. In developing countries with poor institutions and large labor forces, there is a strong incentive to employ workers informally, which implies that some youth may be working but not registered as such in labor market data. Subsidizing wages could incentivize employers to move from the informal to the formal sector, register their employees, and thus increase formal employment. Evidence from two subsidy programs in Turkey appears to confirm this hypothesis (Betcherman, Daysal, and Pages 2010). While these subsidy programs did not create new employment, they did bring workers into the formal labor market.

Another open question is how to practically implement wage subsidies. There are several possibilities. One is through tax reduction, which impacts all participating firms and all of their eligible workers. Another possibility is to identify vacancies suitable for workers in the targeted group (such as young and unskilled workers); usually this is done jointly by caseworkers and the public employment agencies that are responsible for the implementation of the program. The public employment agency then matches targeted workers with these eligible vacancies. A final possibility is to identify eligible workers and then provide them with a voucher that they present to firms in an interview or mention when applying. We have little knowledge about the effects of these policies and the differences between them. One common problem is the small take-up rates: many firms do not claim their tax refund or understand how to use the voucher. Voucher systems seem difficult and administratively costly to implement. In several attempts to implement voucher policies, a very low claim rate of the subsidy has been observed. When administered as tax reductions, the observed claim rate of subsidies has also been low. Tax
deduction methods and vouchers may be even more difficult to implement in developing countries, where large segments of the economy are informal (and hence less sensitive to tax deductions) and where low literacy levels may affect voucher take-up. A recent study which attempts to replicate a wage subsidy voucher program in South Africa by Levinsohn et al (2012) finds that very few firms actually went through the process for redeeming their vouchers. This seems to be for a number of reasons including concerns regarding legitimacy and the administrative burden of claiming the voucher. Allocation of a wage subsidy voucher seems to have no significant effect on labor force participation or earnings but is positively associated with being in wage employment and the length of employment. This positive impact persists two years after voucher allocation. One mechanism through which the impact seems to occur is that individuals in the control group were more likely to turn down job offers initially than those with the wage subsidy voucher.

We need more evidence on the effects of wage subsidies. This evidence should address the displacement effect through randomization at the firm or position level as well as the beneficiary level. It would also be especially useful to have real cost-benefit analysis over the medium run, including the gains from being registered in the formal sector. Ideas and evidence about how to help subsidized jobs turn into real durable insertion in the labor market would also be useful.

Theme 7.4: Public Works Programs

Some countries struggling with extremely high rates of youth unemployment have resorted to direct employment programs. These programs are often politically attractive because they appear to be the only way to have first-order effects on unemployment. By enlisting unemployed youth to work on short-term projects aimed at developing economic and social infrastructure, such as building restoration and the construction of roads and channels, public work projects aim to expand local infrastructure, which would create permanent jobs. However, Kluve (2010) and Betcherman, Olivas, and Dar (2004) conclude that
direct employment programs in the public sector are rarely effective and, in fact, are frequently detrimental to participants’ future employment prospects. Moreover, in some countries these programs are especially costly and attract almost exclusively males due to the nature of the work (see van Eekelen, de Luca, and Ismail 2001 for an example from Egypt). A natural policy implication of this research is that these programs should be discontinued, but political pressures are often such that the programs are difficult to close. Given the political context, can the objectives of direct employment programs be broadened to encompass future employability?

*What is the effect of public works programs when measured with rigorous experimental methods? Are these programs cost-effective?*

Public works programs are a case where addressing selection bias probably requires the use of randomized methods. Eligible participants for public works usually have very low labor market prospects, suggesting that nonexperimental estimates of their impact are likely biased downward. Unfortunately, most of the results to date in the literature have been obtained using less rigorous methods.

One example of a randomized evaluation of a public works program is that of the Community Employment Innovation Project (CEIP) in Canada. CEIP beneficiaries are eligible for three years of work in order to afford them a meaningful longer-term employment experience. Gyarmati et al (2008) found no long-lasting effects from CEIP, but the program was found quite effective in the short-run, a much more promising finding than the usually negative effects found in the nonrandomized literature.

Another point worth noting is that, as these public works programs are often seen as a safety net (in addition to a labor market program), it would be valuable to undertake a comprehensive cost-benefit analysis, including a large set of potentially omitted costs and benefits. It would be especially worthwhile to account for effects on consumption, education, health, crime, and labor supply at the household level.
One such example from a developing country is Attanasio, Meghir, and Vera-Hernandez (2007) which accounts for the impact of the Colombian workfare program *Empleo en Accion* on individuals as well as household earnings. Attanasio, Meghir, and Vera-Hernandez show that participation in the program increased household income by more than the increase in the individual earnings of participants. Therefore, participation in the workfare program generated positive externalities for household members other than the participant. The effects remained significant six months after program completion for participants in small towns, but became insignificant for the rest of the sample.

Imbert and Papp (2011) find that a public works program in rural India increased public employment by 0.3 days per month for prime-aged, low-skilled people living in poorer districts. Wages for casual laborers increased by 4.5 percent in poorer districts and 9 percent in states that implemented the program the most efficiently. The program induced an increase in equilibrium wages in the private sector and generated sizable welfare gains to the poor overall. Effectively, the wages redistributed income from net buyers of labor, richer households, to net suppliers of labor, poorer households.

In Africa, public works programs have found trouble targeting the poorest of the poor. Using data from several community-based public works programs in South Africa, Adato and Haddad (2002) find that even though the programs failed to attract the poorest individuals, they attracted the moderately poor and females despite considerable gender discrimination in project areas. Their study highlights the difficulties of undertaking projects which simultaneously seek to meet community infrastructural needs and employ those who need employment assistance the most. Teklu and Asefa (1999) find that a considerable amount of the non-poor took up employment in public works programs in Kenya and Botswana. They cite the need for more effective screening measures which would screen out the non-poor while avoiding exclusion of the very poor. Such screening mechanisms are important in light of the fact that public works projects do bring about some positive changes: the Botswana and Kenya projects improved income among the poorest individuals and decreased poverty rates among the rural poor.
Andrews et al. (2011) evaluate a recent public works program in Liberia and find that the public works programs employed a considerable amount of females (46 percent overall) and youth (60 percent). Again, while the program saw success in employing the poor, it did not elicit the participation of the most poor, who experience significant social and geographic isolation. Short-term impacts include a 21 percent decline in the poverty gap relative to baseline, reported gains in soft skills, reported increases in savings or investments in education, and benefits to the surrounding community due to the project’s infrastructural improvements. Andrews et al. estimate that it cost 1.96 USD to pay a participant 1 USD; however this estimate fails to account for potential gains in market activity as a result of the infrastructural improvements as well as long-term effects on participants’ future labor market success. Due to how recently the study was conducted, the long-term impacts have yet to be fully realized.

*How can the future labor market prospects of public work beneficiaries be improved?*

Variations on public-sector employment programs should be tested to help us understand why these programs typically do not work in the long-run and how they could be made more effective. For example, one hypothesis could be that the public-sector jobs do not provide valuable labor market experience because they are not interesting, inspiring, or motivating. One could assess this possibility by comparing the effectiveness of these programs across different types of jobs, or by assessing the impact of combining public sector jobs with soft skill training programs aimed at increasing self-esteem and the perceived value of public employment. Another potential hypothesis is that the nature of public sector jobs makes it particularly difficult for participants to signal the experience they have accumulated to potential private-sector employers later on. One could consider combining public sector employment with the production of a credible referral that could be used by participants as they exit the program and start looking for their next job.

*Do public work programs have perverse effects on private sector employment?*
One common criticism of public work programs is that they crowd out private-sector activity. In order for public works programs to reach a large enough scale to be effective, they frequently have to diversify the type of work activity offered, which may involve some activity close to the private sector. In India, Imbert and Papp (2011) find evidence suggesting a one-to-one crowding-out effect of public works programs on private sector work.

Provision, or even the hope of provision, of public work positions may also have disincentive effects on labor supply, though Attanasio, Meghir, and Vera-Hernandez (2007) did not find evidence that Empleo en Accion crowded out the labor effort of family members of program beneficiaries. Research looking at the effects on labor supply in the neighborhood or the family of public work beneficiaries would shed light on this issue. Further studies could also experiment with different provision rates within pre-identified neighborhoods.

In summary, given the political attractiveness of public sector employment, rigorous cost-benefit analysis should be undertaken. Further research should be targeted towards discovering how to make these public sector employment programs more valuable experiences for unemployed youth.

Theme 7.5 Self-Employment and Development of the Informal Sector

A final type of program provides incentives to start businesses or to expand existing small businesses. The emerging literature on the impact of policies for the unemployed directed towards start-ups, entrepreneurship, and self-employment assistance is still light, particularly with regard to youth. Programs

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2 Besley and Coate (1992) present a case for instituting work requirements in government poverty-alleviation programs. They argue that workfare would generate both a screening effect and a deterrent effect. Under the screening effect, workfare can be used to target transfers to only those individuals who truly need the assistance. Such an outcome is particularly desirable since governments do not know individuals' earning-opportunities function—that is, governments cannot identify whether a poor individual is poor because of low human capital or if she chose to reduce her work hours so as to qualify for government assistance.

Besley and Coate formalize an economic model which assumes that high-ability people can work themselves out of poverty and that low-ability people cannot. Government assistance would therefore try to target transfers only to low-ability individuals. Besley and Coate demonstrate that workfare programs decrease incentives for high-ability individuals to mask as low-ability individuals, since entering into a workfare program makes high-ability individuals worse off than they would have if they did not enter into the workforce program. However, workfare programs do not decrease gains to low-ability individuals.
usually combine financial aid to the unemployed, either through direct cash transfers or reduced-rate loans, with mentoring or business training. Caliendo and Kritkos (2010) provides an overview of the evidence in this area, which tends to show increased labor market attachment even in the long run but no effects on earnings.

In many developing countries, the informal sector is a substantial share of the economy. The informal sector is the largest in Sub-Saharan Africa, where it comprised 38.4 percent of total GDP in 2005 (Schneider, Beuhn, and Montenegro 2010). As of 2006, the informal sector in Kenya and South Africa accounted for 82.6 percent and 30.7 percent of all male employment and 92.1 percent and 39.0 percent of all female employment, respectively (UNRISD 2010). Informal sector workers are overwhelmingly low-educated and low-skilled, which contributes to the low productivity of the informal sector. However, that is starting to change, since educated youth are increasingly opting for informal work due to limited employment opportunities in the public sector and the formal private sector. Women usually participate more in the informal sector than men, yet training for informal sector work overwhelmingly favors males (Haan and Serriere 2002).

*How can microfinance programs improve the economic outcomes of youth?*

Microcredit is a very popular intervention related to informal self-employment and business. However, evidence from the few randomized evaluations of microcredit programs has generally found only modest results: one RCT in India (Banerjee et al. 2010) and another in the Philippines (Karlan and Zinman 2010) find little effect. Another evaluation in rural Morocco (Crepon et al. 2011) finds small effects of microcredit on business development and increased self-employment. In Thailand, increased access to loans primarily improved business outcomes for the middle class (Nelson 2011). However, the results suggest that microcredit can have unintended side effects, since increased access to loans also caused children to work longer hours. The increase in child labor persisted even 12 months after the initial loan.
It is unclear whether the same results will apply to youth, given stark differences in microcredit uptake rates and entrepreneurial behavior in youth relative to the adult population. Although youth represent a substantial share of the unemployed population, microfinance institutions (MFIs) are reluctant to loan to youth. First, youth are riskier clients given their lack of experience and the lack of available information regarding their productivity. Youth also represent a small market for MFIs, so the potential gain in profit may not justify the extra costs involved in developing services for youth (e.g., specialized staff with expertise on youth unemployment issues or structuring special credit products appropriate for youth). There is also political opposition to the idea of loaning to adolescents, which risks increasing child labor and encouraging adolescents to drop out of school (Nagarajan 2005).

Akhmisse et al. (2008) evaluate a microfinance program in Morocco that is geared toward offering financial services, financial and business literacy training, and business development support to youth. The authors find that program structure must be significantly altered in order for their services to be appropriate for youth. Youths’ savings decisions and ability to plan for the future are heavily linked to their family environment. Parental influence affects the amount of risk young people take – in Morocco, parents hold stigmas regarding entrepreneurial work and urge their children to wait for the high-paying but scarce jobs in the public sector instead. Working closely with parents along with youth may resolve cultural stigmas against informal work and create environments more conducive towards fostering youths’ entrepreneurial capacity. Closely involving parents may also improve youths’ chances of obtaining credit access, since parents can act as guarantors (Akhmisse et al. 2008).

Akhmisse et al. (2008) also find that young people valued the financial and business literacy training courses as well as the savings services, but that there was still low take-up of the microcredit services. It is currently unclear whether the low take-up rate of microcredit services is due to youths’ (possibly incorrect) perceptions that microcredit will not help, or whether the other offered services are sufficient for youth to progress economically. The authors conclude that savings and asset building may
be more helpful to youth than access to credit. However, it is also the case that current loan terms may not be appropriate for young people. The authors indicate the need for more flexible loan options for youth in order to assess the true impact of credit access on youths’ business outcomes, as current arrangements make it difficult for youth to take advantage of microcredit. For example, microfinance loans typically require that applicants own or rent their own business, but this is not viable for youth, many of whom are just starting their careers (Akhmisse et al. 2008).

Bauchet et al. (2011) review recent RCT microfinance evaluations and find significant heterogeneity in impact among various targeted populations, with substantial benefits to some and significant losses to others. They argue for greater focus on designing different microfinancing options for borrowers based on previous success and background. The RCTs reviewed find that borrowers who already own successful businesses are the most likely to realize significant returns to obtaining microcredit. The propensity to engage in micro-entrepreneurship increases as individuals age and accumulate labor market experience (Narita 2011), so it is unclear whether microcredit will be useful in helping youth, who may lack experience or interest, successfully run their own businesses.

Even if youth are unlikely to start their own micro-enterprise, they may still benefit from microfinance. Bauchet et al. (2011) suggest that microfinance may benefit even those borrowers who are not seeking loans to start a business – if this is the case, then structuring microfinance to adapt to their needs, while still allowing microfinance to be a sustainable business for microlenders, may be a worthwhile avenue for future research. Bauchet et al. (2011) present evidence indicating that while credit products may not increase average income for micro-enterprises, they may increase household consumption, help smooth income shocks, and improve investments in durable goods, home improvements, and education. Poor households have a distinct set of needs (e.g., managing risk, alleviating uneven cash flow, and smoothing consumption) that can be met (at least partially) with
increased credit access, and structuring microloans to address those needs may be welfare-enhancing for youth.

There are plausible ways to restructure traditional microloans that may increase take-up and success rates among youth. Microfinance programs have typically used a group liability scheme, in which applicants must apply in groups and be held jointly responsible for the loans of their group members. Gine and Karlan (2011) find that switching from group to individual liability increased the number of borrowers but did not decrease repayment rates. Their results suggest that the surprisingly low uptake rate of microloans is in part due to the fact that risk-averse individuals are reluctant to cosign for their peers. Since there are steep information asymmetries regarding youths’ abilities, it may be especially difficult for youth to find cosigners. Individual liability loans may more flexibly adapt to the rapidly changing financing needs youth have as they develop and expand their economic pursuits (Nagarajan 2005). It would be interesting to explore whether a group or individual liability arrangement would affect credit access specifically for youth.

Commitment devices, such as a savings account which only makes deposits accessible in the future, have been shown to be effective in increasing household expenditures, savings deposits, and business output (Bauchet et al. 2011). By making money temporarily inaccessible, commitment devices may also facilitate savings behavior by lowering the pressure to share money with friends and family (Brune et al. 2011). Sending inexpensive SMS reminders to save – such as reminding borrowers of the specific purchases they are saving up to make – may also help overcome problems that arise from having high future discount rates (Karlan et al. 2011). As youth have especially high rates of future discounting, possess greater problems with self-control, and may be more susceptible to pressure from peers and family to share their income, the use of commitment devices and savings reminders may considerably improve savings behavior among youth.
Microfinance loans are characterized by short payment periods so as to minimize expected losses from defaults. However, short payment periods constrain borrowers’ ability to use the bulk of their loan on investments, since many borrowers must use part of their loan to meet the required repayments. A randomized evaluation found that giving a grace period of two months increased average micro-enterprise profit by 30%. However, less successful borrowers were more likely to default relative to the control group (Field et al. 2011). Another study demonstrated that switching from weekly to monthly payment periods did not affect repayment rates and cut down on operational costs (Feigenberg, Field, and Pande 2010). Bauchet et al. (2011) suggest that introducing a two-month grace period may improve investments, and that a higher interest rate may be able to make up the losses incurred through any additional defaults. If youth lack experience in running their enterprise, a grace period may be helpful in increasing the amount of initial investment made. However, if youth lack experience managing finances and smoothing funds over time, they may find it harder to make repayments when the length of time between payments is extended.

Given the high potential of employment associated with the informal sector, how can policy foster the development of this sector?

Mechanisms to develop informal-sector businesses may include developing role models, and providing ideas and know-how about various potential self-employment positions. Another possibility is to provide incentives for firms in the formal sector to address demand in the local informal sector. The informal and formal sectors are not independent from one another: the decision to start a business is related to existence of jobs and wages in the formal sector, and labor market rules in the formal sector have effects on the development of the informal sector. Previously mentioned studies in South Africa and India point to labor regulation as a significant factor in explaining employment outcomes in the informal sector: Magruder

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3 However, it is unclear how higher interest would affect demand for microcredit, when take-up of microcredit is already low.
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(2011) finds that centralized bargaining in the formal sector decreased entrepreneurship, while Besley and Burgess (2004) report that more stringent regulation of the formal sector increased output in the informal sector.

Few small and medium enterprises (SMEs) expand into larger businesses even though together they command a sizable share of the economy. Bauchet et al. (2011) point to the need for credit markets to expand to small enterprises, which have outgrown microfinance but do not qualify for traditional business loans. Lack of managerial human capital may limit the ability of SMEs to expand, particularly if it limits access to other resources, such as finance. For youth especially, who are more likely to lack prior business experience, a combination of financial education training and entrepreneurial skill development may increase the productive capacity of microloans. In an ongoing study in Uganda, Fischer, Karlan, and Startz are evaluating an intervention that provides training services to female entrepreneurs. Improvements in business outcomes in treatment groups may suggest that lack of managerial human capital is indeed limiting the growth of SMEs in Uganda. More systematic evidence is needed on the potential of such programs to help SMEs expand into larger businesses.

While many programs provide business training to micro-entrepreneurs, the results have been mixed. Karlan and Valdivia (2011) find no statistically significant effects on business outcomes or employment for microfinance clients in Peru. However, client retention rates and loan repayment rates improved for the microlending program. Similarly, Bruhn and Zia (2011) examine a program designed to encourage young entrepreneurs to make capital investments and find that treated individuals were more likely to undertake new investments, exhibited improved business practices, and experienced more favorable loan terms after the training program. Those who had low financial literacy in the beginning of the program exhibited improved financial knowledge, and those with higher financial literacy in the beginning of the program improved their business performance and sales. However, business training did not change the probability of business survival. The authors conclude that business training programs were insufficient to promote business growth in emerging markets, but were nevertheless a necessary
component to improving business outcomes for youth operating in the informal market. There are currently several ongoing experiments related to business training and business start-ups. One is evaluating a program in France that provides young people from deprived suburbs assistance and counseling in starting firms or projects. A noteworthy feature of this program is its emphasis on the soft skills related to running a project.

The content of the training could significantly affect outcomes. Drexler, Fischer, and Schoar (2011) compared a traditional financial training course to a basic financial training course which focused on teaching entrepreneurs simple rules of thumb. Micro-entrepreneurs randomly selected to receive the latter curriculum were more likely to separate their business and personal cash accounts, more likely to keep records, more likely to calculate revenue, less likely to make reporting mistakes, and earned more revenue when the overall market was unprofitable. Whether these results hold for youth, who may more readily absorb new information and new techniques into their business than older adults, remains an open question.

How can informal housing problems be addressed so as to promote youth employability?

The informal housing sector also potentially affects youth employment in significant ways, but economic research in this area has been sparse. We present on the few relevant studies that are available (taken from the urban planning literature) and infer potential implications for youth employment, with the disclaimer that our speculations cannot be a substitute for rigorous empirical economic analysis. Future research should address gaps in the existing literature, such as: how informal residence status affects youths’ labor outcomes, whether youth disproportionately depend on informal housing, and the impact of poor living situations on educational opportunities and employability.

Informal housing arrangements (e.g., slums, settlements, shanty towns, etc.) often arise out of a desire to locate close to urban centers where greater economic opportunities are available. While informal
occupation decreases segregation and promotes the urban economy, it also increases urban density, creates overcrowding, and shifts costs onto the public sector. Informal settlers have significantly lower levels of literacy and education relative to the rest of the urban population. They often live in substandard conditions, with poor sanitation and other health risks (Karn, Shikura, and Harada 2003). Moreover, because of their political status, informal residents have few means to exercise influence over the socioeconomic processes that entrench inequality (Huchzermeyer 2009; UNECE 2009). Although the effects of these circumstances on youth human capital acquisition and job attainment could be substantial, there is yet to be a full body of economic work on the topic.