

Fixed-term Contracts and the Duration Distribution of Unemployment*

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Abstract

In the mid-1980s, many European countries introduced fixed-term contracts. This paper studies the possible implications of such reforms for the duration distribution of unemployment. I estimate a parametric duration model using cross-sectional data drawn from the Spanish Labor Force Survey from 1980 to 1994 to analyze the probability of leaving unemployment before and after the introduction of fixed-term contracts. I find that the difference in the probability of leaving unemployment between the short and long term unemployed increased after this reform. This difference increased more among those population groups more affected by the reform. Semi-parametric estimation of the model also shows that for long spells, the probability of leaving unemployment decreased between the mid-1980s and the early 1990s.

Keywords: cross-sectional data, duration model, turnover.

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1. Introduction

In the mid-1980s, many European countries introduced fixed-term contracts in order to fight the high and persistent levels of unemployment that they had suffered since the mid-1970s. Prior to the mid-1980s, European labor markets had typically been characterized by a wide use of permanent contracts with high regulated firing costs. The idea behind this policy was to increase flexibility in the labor market by allowing employers the option of hiring workers under shorter contracts with negligible firing costs.¹

Since their introduction, fixed-term contracts have been widely used, and an increasing number of new jobs are fixed-term (see OECD, 1993). European labor markets have become more dynamic in terms of worker turnover rates, but, contrary to expectation, the unemployment rate has remained largely unchanged (see table 1). The consequences of the introduction of fixed-term contracts have generated interest and concern among both academics and policy-makers (see Booth et al., 2002, and OECD, 2002). Much of the existing research on fixed-term contracts (or temporary contracts, TCs)² has focused on their effectiveness in reducing unemployment. There is a wide consensus among economists that the introduction of such contracts does not necessarily increase employment despite the emergence of a dual labor market among employed workers.³ In this paper, I study the possible effect of TCs, through increased labor market flows, on the duration distribution of unemployment. In particular, I study the possibility that the pool of unemployed workers becomes segmented.

Along with the high rates of unemployment, another worrisome feature of European labor markets is the high proportion of unemployed workers who have been unemployed for a long

¹See Grubb and Wells (1993) and OECD (1999) for a detailed description of fixed-term contract regulations in Europe.

²The terms fixed-term contract and temporary contract (TC) will be used interchangeably throughout this paper.

³See, among others, Aguirregabiria and Alonso-Borrego (1999), Alonso-Borrego et al. (1999), Bentolila and Dolado (1994), Güell (2000) and Saint-Paul (1996).

period of time (see Machin and Manning, 1999). In Europe, on average, between 1983 and 1994, 48 percent of the unemployed had been in unemployment for more than 12 months (the long-term unemployed, LTU), while in the US this proportion was only 9 percent (see table 1). Therefore, it is important to investigate whether the introduction of TCs has improved the functioning of the labor market for the LTU.

In this paper, I provide some theoretical considerations of the effects of introducing TCs on the duration distribution of unemployment, and I then present an application to Spain, a particularly striking case. More precisely, I analyze the effects of TCs on the incidence of LTU, on the duration dependence of unemployment and on the outflow rate of the LTU workers.

In the mid-1980s, the Spanish unemployment rate was close to 20 percent, the highest of the OECD countries. In 1984, Spain introduced a temporary contract policy that was far more liberal than that of other European countries. In particular, while in some countries TCs were restricted to particular types of workers or sectors, there were no such restrictions in Spain. Before the reform, TCs were only allowed for seasonal jobs. One key feature of the reform was that it allowed the use of TCs for jobs that are not necessarily seasonal. In fact, all workers in all occupations and sectors could be hired under a TC. Concerns that the extremely high levels of labor market regulation were responsible for Spain's high unemployment rate motivated this sweeping reform (see OECD, 1994). Figure 1 shows the evolution of the unemployment rate as well as the increase of the share of TCs from 1980 to 1996. The higher share of TCs in total employment after the reform can be mainly attributed to their widespread use in non-seasonal jobs (see Güell and Petrongolo, 2006).

A decade after the introduction of fixed-term contracts, the unemployment rate in Spain had returned to pre-reform levels. Moreover, the share of fixed-term employees had become the highest in Europe, around 33 percent, while the European average was 11 percent (see

table 1). As a consequence, in 1994, a second reform that restricted the use of TCs was implemented. Therefore, the Spanish experience between 1980 and 1994 appears to be particularly useful for studying the effects of these types of policies.⁴

Although the effects of TCs on unemployment have been unsatisfactory, there have been other changes in other dimensions of the labor market that can reasonably be attributed to these flexibility measures. First, the share of employed workers becoming unemployed (the inflow rate into unemployment) as well as the share of unemployed workers becoming employed (the outflow rate from unemployment) have increased substantially over this period (see figures 2 and 3, respectively). TCs have played an important role in this increase in turnover during this period. After the 1984 reform, on average, as many as 94 percent of all newly registered contracts have been TCs (see figure 4) while previously it was around 20 percent.⁵ Bover et al. (2002) and García-Pérez (1997) also find that TCs increase the employment chances of the unemployed in Spain. As for the inflows back to unemployment, on average, between 1987 and 1994, as many as 75 percent of these workers were separated from their jobs because their fixed-term contract came to an end.⁶ Another supporting fact is that, on average, the renewal rate of TCs into permanent ones has been very low, around 8 percent, which implies a large flow from non-renewed workers into unemployment.⁷ Finally, García-Serrano (1998) studies the role of TCs in worker turnover in Spain and concludes that these contracts account for the largest portion of the hiring and separations rates.

The increase in outflows from unemployment implied a second important change in the Spanish labor market relating to the long-term unemployment rates, which is also among the highest in Europe (see table 1). The incidence of LTU typically displays anti-clockwise

⁴Clearly, it is also possible that during this period there were some underlying structural changes in the Spanish economy, such as sectorial shocks. However, in terms of legal changes, the introduction of TCs was the main reform in the labor market during this period. In any case, as will be explained later, the important fact is that, in the labor market, these other possible changes materialized through temporary contracts.

⁵See Figure 1 in Bover et al. (2002).

⁶The inflow is measured by the unemployed who have duration less than 1 month.

⁷See Güell and Petrongolo (2006).

loops over the business cycle (see Machin and Manning, 1999). As can be seen in figure 5, for a given unemployment rate, the incidence of LTU in Spain in the early 1990s is lower than in the mid-1980s. Comparing periods which are at the same point in the cycle, say from 1983 to 1985 and from 1992 to 1994, there has been a shift in the unemployment rate-LTU relationship. In fact, this seems to be a common feature in several European countries (see table 1). As mentioned in Machin and Manning (1999), when the outflow rate increases at any duration of unemployment, the incidence of LTU tends to decline. Therefore, the lower incidence of LTU can also be attributed to the increased outflows that have occurred since the introduction of TCs.

Previous studies that estimate the probability of leaving unemployment in Spain find that there is a very strong duration dependence.⁸ In other words, *ceteris paribus*, unemployed workers with shorter unemployment spells have higher probabilities of leaving unemployment than those with longer spells. But an important question that remains is whether the introduction of TCs has changed the duration distribution of unemployment through changes in duration dependence. The aim of this paper is to analyze the changes in the probability of leaving unemployment for the short term unemployed relative to the LTU before and after the introduction of TCs in Spain.

As with many other countries, panel data are not always available. Panel data from the Spanish Labor Force Survey are only available after 1987. Therefore, to analyze the changes in duration dependence before and after the introduction of TCs, I use cross-sectional data drawn from the same survey for the years 1980 to 1994. I exploit these data following the parametric duration model suggested by Nickell (1979a).⁹ In order to further study the changes in the probability of leaving unemployment among the LTU, I estimate a semi-parametric version of Nickell's model and discuss the conditions under which such a model

⁸See, for instance, Alba (1999), Bover et al. (2002), García-Pérez (1997), Jenkins and García-Serrano (2000) and Machin and Manning (1999).

⁹Andrés et al. (1989) also estimate this model using a 1985 data set from the Spanish Ministry of Finance.

can be estimated.

The remainder of this paper is organized as follows. Section 2 provides some intuition of the effect of the introduction of TCs on the duration distribution of unemployment. Section 3 describes the data. Section 4 presents a duration model of the transition from unemployment to employment. Section 5 presents the empirical results, and section 6 concludes.

2. Some Intuition

In this section, I consider the different hiring rules used by firms and their implications for the duration distribution of unemployment. I assume that once TCs are introduced, unemployed workers are always hired under a TC. This is driven by firms' choices rather than workers' preferences for temporary jobs.¹⁰ When hiring, firms can either choose randomly among the pool of unemployed workers or, alternatively, they can rank applicants by their spells of unemployment, hiring first those workers with the shortest duration of unemployment (see Blanchard, 1991, and Blanchard and Diamond, 1994).

The introduction of TCs increases outflows from unemployment to employment since they are less costly than permanent contracts. As Machin and Manning (1999) show, when the outflow rate increases at *any* duration of unemployment, the incidence of LTU tends to decline. This implies that, independently of the hiring rule adopted by firms, the share of LTU will be reduced after the introduction of TCs (as figure 5 shows). The intuition behind this result is that, even if TCs do not increase (directly) the outflow rate of the LTU, as long as other unemployed workers with shorter spells become employed, then there is less build-up into longer spells.

However, the different hiring rules adopted by firms can have different effects on the duration dependence of unemployment. As Blanchard and Diamond (1994) show, if firms rank

¹⁰As mentioned, since the introduction of TCs, almost all new contracts are of this type. Moreover, on average, from 1987 to 1994, as many as 89 percent of temporary workers reported that they were holding a TC because they could not find a permanent one.

unemployed workers and hire those with the shortest spells of unemployment, then the exit rate from unemployment is a decreasing function of duration. Moreover to the extent that firms do not hire randomly, it is quite possible that duration dependence of unemployment might have increased after the introduction of TCs (despite the lower incidence of LTU). It is important to note that the introduction of TCs is characterized by an increase in both inflows and outflows between unemployment and employment.

Assume that all unemployed workers are homogeneous and that only duration of unemployment affects workers' probability of leaving unemployment. In this case, the short-term unemployed (STU) exit first after the introduction of TCs. Contrary to the situation prior to the introduction of TCs, their employment spell under TCs is shorter and, at the end of their TC, they go back to unemployment. Once in unemployment, they are again the unemployed with the shortest spell and thus with the highest re-employment probability. In other words, what matters is the relative position with respect to the other unemployed. The higher flows in the labour market make the STU accumulate much less unemployment duration than the other unemployed. Therefore, the introduction of TCs could cause that the LTU, even if fewer in number, to experience higher persistence in unemployment.

This is in sharp contrast with the situation in which only permanent contracts were allowed. The STU would also be the first ones to leave unemployment. However, the fact flows back to unemployment are less frequent implies that the LTU would move up faster in their ranking position, increasing their chances to leave unemployment whenever a new offer would arrive. Lower inflows into unemployment make all the unemployed stay relatively in the same position.

Unemployed workers may also differ in key individual characteristics that make some more likely to be re-employed (for instance, gender, age or education).¹¹ An analogous ranking

¹¹Given that since the introduction of TCs, 94 percent of new contracts are TCs, I assume that the probability of being reemployed is the same as the probability of being reemployed with a TC.

model based on characteristics interacted with unemployment duration applies. Similar dynamics to the ones explained above arise. After the introduction of TCs, workers with ‘better’ characteristics enjoy higher exit rates than workers without them. And, as long as they maintain these characteristics, they continue to have a higher re-employment probability when they return to unemployment after their TC finishes. Similar arguments apply to unobserved characteristics.

In practice, the probability of leaving unemployment is a function of duration, observable and unobservable characteristics. Therefore the mechanisms explained above interact with one another and they reinforce themselves. That is, the introduction of TCs can imply relatively lower exit rates for the unemployed workers who not only have longer spells of unemployment, but also lack some key characteristics (both observable and unobservable).

To conclude this section, to the extent that firms do not hire randomly, TCs will tend to always be enjoyed by the same group of unemployed workers. This implies that the duration dependence of unemployment will increase. The introduction of TCs can generate a segmented unemployment pool. That is, some unemployed workers will be constantly churning from unemployment to employment under TCs, while the other unemployed workers will not exit unemployment, experiencing longer durations of unemployment.

In accordance to the discussion of this section, in section (4) I analyze empirically the changes in duration dependence before and after the introduction of TCs. I will consider a model in which the probability of leaving unemployment depends on unemployment duration, individual characteristics and unobserved heterogeneity.

3. The Data

I use the Spanish Labor Force Survey (*Encuesta de la Población Activa*, EPA), which is carried out quarterly on a sample of some 60,000 households.¹² It is designed to be repre-

¹²For a more detailed description, see http://www.ine.es/en/daco/daco43/notaepa_en.htm

sentative of the total Spanish population and contains very detailed information about the labor force status of individuals.

My sample contains data from the second quarters of each year from 1980 to 1994. The time span of the sample is an important feature of the data because it will allow me to analyze the probability of leaving unemployment before and after the introduction of TCs. As mentioned, all workers were eligible for the TCs introduced in 1984 and therefore there is no control group. However, as explained above, TCs played an important role in changing the labor market flows and, therefore, it is reasonable to expect that most of the changes in the duration distribution of unemployment over this period are related to the introduction of TCs.

In the absence of a control group, I can devise a quasi experimental setting. It is likely that some unemployed workers were more affected by this reform than others, and thus it is possible to analyze the difference in the change in duration dependence between the more affected groups and those less affected. Since prior to the 1984 reform there were already seasonal TCs, it is likely that those sectors characterized by a more seasonal activity were less affected by the reform. Similarly, since lower skilled workers tend to work in these sectors,¹³ it is likely that these workers were less affected by the reform. The EPA contains information on the type of contract starting in 1987. So it is possible to analyze the evolution of TCs from 1987 and 1994 and assume that the level in 1987 is close to the pre-reform level of TCs.¹⁴ Columns (1) and (2) of Table 2 report the share of TCs among non-seasonal and seasonal sectors, respectively.¹⁵ As expected, the share of TCs was lower in 1987 for non-seasonal sectors than for seasonal sectors. Also, in 1994, this was still the case. However, over the period analyzed, the share of TCs increased much more for non-seasonal sectors than

¹³Columns 10 and 11 in Table 3 suggest that this is the case.

¹⁴This assumption does not seem too restrictive since the share of TCs has been increasing monotonically for the whole period (see figure 1 and table 2).

¹⁵Unemployed workers in the EPA report the sector in which they worked in their previous job.

for seasonal sectors. A similar pattern can be found when comparing skilled and unskilled workers (columns (3) and (4)). The share of TCs is lower for skilled workers throughout the period, but it increased more for these workers than for the unskilled workers. Given this, I will also estimate the probability of leaving unemployment allowing for the duration dependence parameter to vary between these different groups before and after the reform.

As will be discussed, one main assumption of the econometric model is that the composition of the flow into unemployment is fixed over some period of time prior to any particular year analyzed. For this reason, I have excluded women from my sample since this assumption may be too strong for them.¹⁶ Thus, my sample includes all men who are unemployed and who report how long they have been searching for a job.¹⁷ I exclude men aged 65 or older because transitions to non-employment are more likely for this group. Since I want to focus on the effects of TCs on the *existing* distribution of unemployment, I will also exclude first-job seekers. This leaves me with a sample of 80,790 unemployed male workers.

One advantage of the cross-sectional EPA (relative to the currently available panel EPA¹⁸) is that it contains information on the region of residence as well as some household characteristics. However, until 1987 there was no information on unemployment benefits or on the reason for previous job loss. In order to fully exploit all the relevant information contained in the data, my analysis will be carried out in two parts. First, I use all the years of the sample, from 1980 to 1994. The analysis is undertaken with those variables common to all sample years. This first part of the analysis thus exploits information for a very long time period at the expense of some relevant variables only available in the most recent years. These additional variables will be exploited in the second part of the analysis for those years for which they are available, from 1987 to 1994.

¹⁶If anything, this should underestimate the effects of fixed-term contracts since the incidence of these contracts is higher for females than for males.

¹⁷A formal test of this stationarity assumption for this sample is undertaken in section 4.

¹⁸See Bover et al. (2002).

All the unemployed people in the sample are asked how long they have been looking for a job. This search time will be used as the individual's uncompleted duration of unemployment.¹⁹ Explanatory variables available for the whole sample period include personal characteristics of the individual such as age, education and marital status, as well as some household characteristics such as the number of children and the number of working adults in the household. Finally, the local unemployment rate is also included to capture business cycle effects.²⁰ This quarterly regional unemployment rate will be the only time-varying regressor. For the second part of the analysis, two more variables are available: a dummy variable that indicates if the worker receives unemployment benefits (UI); and a dummy variable indicating whether the reason for separation from the previous job was the ending of a TC (EndTC).

The workers statute of 1980 sets the basic framework for the current Spanish unemployment benefit system, which is very similar to that of most European countries. There are two types of benefits. First, the unemployment insurance system that pays benefits to dismissed workers that have previous work experience. Workers get paid a share of their previous wage, which gets reduced along the duration of unemployment. Total benefit duration is also related to the previous accumulated work experience with a maximum of two years. Second, the unemployment assistance system provides benefits for those unemployed workers with low household income that have either exhausted their unemployment insurance or that were not eligible for this when they became unemployed.²¹ Holding unemployment insurance

¹⁹In steady state, the average uncompleted duration of unemployment is proportional to the average completed duration of unemployment (see Layard et al., 1991).

²⁰Unemployment rate at the regional level includes 50 provinces within Spain. The annual growth rate of GDP will also be considered.

²¹During the period of study there were two modest reforms that increased the generosity of unemployment insurance in 1984 and of the unemployment assistance system in 1989. These reforms could have reduced the probability of job acceptance. However, as figure 3 shows, the outflow rate increased for the whole period, which indicates that the effect of TCs was much more important. Finally, in 1992 there was a more important reform that reduced the generosity of the unemployment insurance. The motivation for this reform was the increased inflows and outflows from unemployment through TCs, which generated an important deficit in the Spanish unemployment benefit system. This reform could have also contributed to increase the probability

could contribute to the emergence of duration dependence and therefore this variable will be included in the second part of the analysis.

Before the reform, workers who were unemployed because their TC ended could only be those who had held a seasonal TC. Therefore, it is likely that the reform generated an exogenous increase in the number of workers who lost their job due to the expiration of a (non-seasonal) TC. Although the variable that indicates the reason for job loss was not available before 1987, it is a potential source of identification of the change in duration dependence after the introduction of TCs.²² This variable is very important for my purpose since it can potentially capture all the unemployed workers that enjoy the greater employment chances provided by this type of contract. Separate estimation of the model will be done for these workers.

Table 3 reports average sample values for the whole sample (column 1) as well as for each subsample for which a different model will be allowed. Column 2 corresponds to the sample for the years *before* the reform. Columns 3 to 5 correspond to different samples for the years *after* the reform.²³ First, the whole period after the reform (column 3); column 4 only considers the years 1992 to 1994, which correspond to the years which are at comparable points of the business cycle as the years before the reform (see figure 5). Column 5 reports the values for the years from 1987 to 1994, for which more variables are available. Columns 6 to 13 correspond to different population groups. First, for the years 1987 to 1994, the unemployed who ended a TC (column 6), those who were separated for other reasons (column 7), those who ended a non-seasonal TC (column 8), those who ended a seasonal TC (column 9). Second, for all the sample years, columns (10) to (13) correspond to the different groups

of leaving unemployment. However, its effect would be present at most in the last two years my sample.

²²This variable distinguishes between the end of a seasonal TC and a non-seasonal TC. Between 1987 and 1994, the number of people who have finished a seasonal TC have remained constant; while the number of people who have finished a non-seasonal TC has increased substantially: from 13 percent of the unemployed in 1987 to 26 percent in 1994.

²³Separating the period after the reform into two periods according to the importance of TCs in the economy implies similar qualitative results to the ones found here. Results available upon request.

defined in table 2. Finally, the (uncompleted) duration of unemployment for the different sub-samples is also reported. As mentioned, this should be compared carefully for sample years corresponding to different points of the cycle.

As will be discussed in the next section, in order to estimate the method proposed by Nickell (1979a), it is necessary to complement these cross-sectional data with historical time series of the inflows into unemployment. Unfortunately, the EPA does not offer a long time series on inflows into unemployment.²⁴ I use the monthly registered data on unemployed and new contracts that are available since 1978.²⁵ These data, from the Spanish Employment Office (INEM), allow me to construct monthly (male) inflows into unemployment. Since only those unemployed who have worked before can claim unemployment insurance, first-job seekers generally do not register at the Employment Office. This reinforces the decision to exclude this group from my analysis.

4. Econometric Specification

My sample has only cross-sectional data on uncompleted spells of unemployment. I will estimate the hazard rate of leaving unemployment following the method proposed by Nickell (1979a). The main requirement for implementing this method is historical data on the inflows into unemployment. The intuition behind this duration model is that the cross-sectional data represent the unemployed who have “survived” with different durations at time t , while the inflow data represent the population “at risk” at different points in time. Generally, these data are easily available at the aggregate level. As Nickell shows, assuming

²⁴The inflow rate could be obtained from those unemployed that report spells of less than 1 month, although the “heaping” problem particularly affects this category (people approximate to 1 month). Moreover, the EPA questionnaires have changed three times regarding the unemployment search time (see table A in the Appendix for details). This implies that after 1987, this duration category is even more underrepresented (since the answer “less than 1 month” is not allowed explicitly). Therefore there is a rupture in the series after 1987 due to the change in the questionnaire.

²⁵Another advantage of these data is their monthly frequency. This feature is very important for the semi-parametric estimation of the model.

that the composition of the flow into unemployment is fixed over time, the model can be estimated. As it will be discussed later, the frequency of these inflow data is an important issue to be considered in order to estimate such model, especially semi-parametrically.

Suppose that the probability of leaving unemployment from time t to time $t + 1$ for an unemployed individual i , conditional on having entered unemployment at time $t - s$ and on being unemployed at t is given by

$$h_i(t, s) = h(x_i(t_i, s), \theta_i, t, s) \quad (4.1)$$

where t_i is the date in which the interview took place (in my case, the second quarter of every different year considered); x_i are the relevant characteristics of the individual i , which include the individual's regional unemployment rate during all the spell of unemployment; and θ_i is a random variable independent x_i and t that captures the effect of possibly omitted regressors such as individual's unobserved characteristics.

I have specified h to depend on t . More precisely, I allow the hazard function to be different for different time periods. For example, the hazard for the years before the reform can be different from the hazard for the years after the reform. However, within a sub-period, h does not depend on t . That is, for example, the same function is assumed for the different years prior to the reform (as in Nickell, 1979a).

To write the likelihood, it is necessary to derive the probability for an individual of being unemployed at time t . First, let $S_i(t, v)$ be the probability individual i of being (remained) unemployed at time t conditional on having entered unemployed at time $t - v$. Therefore

$$S_i(t, v) = \prod_{\tau=1}^v (1 - h(x_i(t, \tau), \theta_i, t, \tau)), \text{ for } v \geq 1 \quad (4.2)$$

Suppose that the probability of an individual i of having entered unemployment at time τ is given by $u_i(\tau)$. Then the probability of being unemployed at time t , $U_i(t)$, is given by

$$U_i(t) = \sum_{\tau=0}^{\infty} u_i(t - \tau) S_i(t, \tau) \quad (4.3)$$

It is then possible to write the likelihood for an unemployed individual in my sample, that is the probability of having entered unemployment at time $t - v$ conditional on being unemployed at time t , as

$$L_i = \frac{u_i(t_i - v)S_i(t_i, v)}{\sum_{v=0}^{\infty} u_i(t_i - v)S_i(t_i, v)} \quad (4.4)$$

For early years of the sample, the duration of unemployment is presented in the form of bands (see the Appendix, table A, first column). That is, given the date of the interview, t_i , the individual could have entered unemployment at any time between $t_i - a_i$ and $t_i - b_i$. Therefore given my data, the likelihood becomes²⁶

$$L_i = \frac{\sum_{v=a_i}^{b_i} u_i(t_i - v)S_i(t_i, v)}{\sum_{v=0}^{\infty} u_i(t_i - v)S_i(t_i, v)} \quad (4.5)$$

Obtaining prior estimates of u_i , say \hat{u}_i , I can then write down the likelihood for my unemployed sample of individuals, $i = 1, \dots, I$ as

$$L = \prod_{i=1}^I \left(\frac{\sum_{v=a_i}^{b_i} \hat{u}_i(t_i - v)S_i(t_i, v)}{\sum_{v=0}^{\infty} \hat{u}_i(t_i - v)S_i(t_i, v)} \right) \quad (4.6)$$

There is one last thing to be specified in order to compute this likelihood function. This has to do with the infinite sum in the denominator. I will assume that for long enough durations, the conditional probability specified in (4.1) does not depend on duration and that the estimated probability of having entered unemployment is a constant. In particular, I make these assumptions for durations greater than 36 months.²⁷ The corresponding \hat{u} is the average over the calendar year corresponding to 36 months of duration of unemployment for every individual ($u_{i,36}$). Finally, the likelihood to be maximized is as follows

$$L = \prod_{i=1}^I \left(\frac{\sum_{v=a_i}^{b_i} \hat{u}_i(t_i - v)S_i(t_i, v)}{\sum_{v=0}^{36} \hat{u}_i(t_i - v)S_i(t_i, v) + \frac{u_{i,36}}{h_i(36)}S_i(t_i, 36)} \right) \quad (4.7)$$

²⁶Aggregating the data after 1987 into the same duration groups as the earlier period gives the same qualitative results as those obtained here (results available upon request).

²⁷Between 1987 and 1994, on average, only 7 percent of the unemployed had a duration greater than 3 years.

The probability of individual i , with current characteristics x_{ci} , having entered unemployment at time τ is defined by

$$u_i(\tau) = k(x(x_{ci}, \tau), \tau) \frac{\text{aggregate flow into unemployment in month } \tau}{\text{aggregate employment in month } (\tau - 1)} \quad (4.8)$$

where $k(x(\cdot), \tau)$ is the proportion of the inflow into unemployment at time τ with characteristics x . Assuming that k is independent of time, this probability can be estimated by

$$\hat{u}_i(\tau) = \text{constant} \times \left(\frac{\text{aggregate flow into unemployment in month } \tau}{\text{aggregate employment in month } (\tau - 1)} \right) \quad (4.9)$$

where the constant (which can depend on x_{ci}) cancels out in the likelihood function.

Estimation of (4.7) using cross-sectional data from time t requires this stationarity assumption for the period t to $t - 36$, that is, during the 3 years prior to a given cross-section. There are two ways by which $k(x(\cdot, \tau), \tau)$ is affected over time. First, to assume that $k(x(\cdot, \tau), \cdot)$ is constant is to assume that any changes in relevant characteristics over time are small. This corresponds to the standard assumption of time unvarying regressors. Second, assuming that $k(x(\cdot), \tau)$ is constant also means that there are small changes in the proportions of individuals with particular characteristics in the inflow into unemployment. This point is more difficult to test, mainly because the inflow data from the Spanish Employment Office are not available for the different relevant characteristics. The only disaggregation is by gender.²⁸ The solution adopted regarding this issue has been to choose a sample of individuals for whom this assumption is more plausible. I concentrate my analysis on men who have worked before and have the highest attachment in the labor market. A feature of this sample is that it excludes inflows from inactivity to unemployment which are more affected by the business cycle.²⁹

²⁸Nickell (1979a and 1979b) points out the same problem for the UK.

²⁹See van den Berg and van der Klaauw (2001) for a model in which micro and macro data are combined and the business cycle is allowed to affect the composition of inflow into unemployment.

However, it is possible to test this stationarity assumption after 1987 using the EPA cross-sectional data. After this year, the survey contains information on job tenure of employed workers. This allows me to construct individual inflow rates in a given cross-section by using the sample of employed workers with tenure greater than one month (that is, the pool of employed workers that were employed in the previous period and that constitute the population at risk that can become unemployed) as well as the sample of individuals who entered unemployment during this month. I separately regress the inflow rate on all the observable individual characteristics interacted with year dummies for the three year periods which corresponds to the period for which this assumption is made, and test whether the coefficients on the interaction terms are jointly zero.³⁰ Table C in the Appendix reports the value of the χ^2 test and the associated p-value in brackets for the hypothesis that the composition of inflows within the three year window by each observable characteristic is constant. Column (7) in this table reports the results corresponding to the stationarity assumption for the whole period 1987–1994. Overall the results in this table indicate the stationarity assumption cannot be rejected at the conventional significance levels for the sample of individuals chosen for the period 1987–1994.

I will first specify $h(t, s)$ following a proportional hazard model where the underlying baseline is a Weibull distribution, which is the simplest specification in which it is possible to capture the impact of the average exit rate and duration dependence (see Machin and Manning, 1999).³¹ That is,

$$h_i(t, s) = 1 - \exp\left(\int_s^{s+1} \lambda(u) du\right), \text{ where } \lambda(s) = -\exp(x'_i(s)\beta)\theta_i\lambda_0(s) \quad (4.10)$$

³⁰The variables UI and endTC cannot be calculated in an exact way for employed workers.

³¹The results obtained there are qualitatively the same as those obtained with a logit distribution specification (results available upon request).

and

$$\lambda_0(s) = \alpha s^{\alpha-1} \quad (4.11)$$

Regarding unobserved heterogeneity, I will first consider the case in which there is no unobserved heterogeneity (i.e., $\theta_i = 1$). Then I will consider the case in which θ_i is characterized by a discrete distribution with two points of support, namely θ_1 and θ_2 , with associated probabilities ϕ and $1 - \phi$, respectively.³²

In order to further investigate the changes in the relative probability of leaving unemployment of the LTU, I re-estimate the model allowing a more flexible baseline hazard. The parametric estimation only allows me to analyze this question partially since the baseline hazard (see (4.11)) monotonically decreases with duration, so changes in the duration dependence parameter (α) will imply shifts of the whole base-line function.

Given the grouping of the duration data, a piecewise constant baseline hazard will be estimated.³³ Since I want to focus on changes in the probability of leaving unemployment for the LTU, I estimate three different steps which capture the very short-term unemployed (less than 6 months), a middle group (6 to 11 months) and the LTU (12 months or more).

It is important to note how the frequency of the inflow data plays a role in the estimation. In order to estimate the model, it is crucial that each duration group (the population that has survived and that we observe at time t in the cross-section with duration s) can be matched unequivocally with its population at risk, namely the inflow at time $t - s$. If this condition did not hold (for instance, if the inflow at $t - s$ could be attached to more than one survival group) an identification problem would arise, since a given inflow point could correspond to more than one duration group. In this case, it would not be possible to estimate a separated step for such a group. Let s_i be the frequency of the inflow data. That is, we observe the

³²As Nickell (1979a) shows, in this case, $S_i(t, v) = \phi \prod_{\tau=1}^v (1 - h(x_i(t, \tau), \theta_1, t, \tau)) + (1 - \phi) \prod_{\tau=1}^v (1 - h(x_i(t, \tau), \theta_2, t, \tau))$.

³³For comparison reasons, the same steps will be estimated for the years after 1987.

inflow data at period t , $t - s_i$, $t - 2s_i$, etc. In the cross-section each duration group has duration s (which depends on how the durations are aggregated). It is then crucial that $s_i \leq s$, so that a different step can be estimated for each duration group.

When the inflow is less frequent than the duration groups, then the step-wise assumptions (or even the parametric) will not suffice to estimate such a model. Further assumptions could be made to recover, for instance, monthly inflows from quarterly inflows. However, this would seem to be less appropriate in the semi-parametric case. As mentioned earlier, the inflow data is monthly. The duration groups of the cross-sectional data vary over time. Before 1987, the grouping of the data is quarterly (except for the first group), then 6 months and then yearly. After 1987, the grouping is monthly (if duration is less than 2 years) and then yearly. Therefore, there is no identification problem.

5. Empirical Results

I now estimate the hazard of leaving unemployment as modeled in the previous section. First, I estimate the Weibull base-line hazard specified in (4.11). Column (1) in table 4 reports the estimates for the whole sample, 1980—1994. Every variable is interacted with a post-reform dummy ($d8594$). The duration dependence parameter is statistically different before and after the reform. Figure 6 plots the hazard of leaving unemployment for the reference category estimated by this regression for the years before and after the reform. As can be seen, in the years after the reform the duration dependence of unemployment is much higher than before. For durations of less than 5 months, the probability of leaving unemployment is much higher than before. But the reverse is true for durations of 6 months or more.

The effects of the individual characteristics on the probability of exiting unemployment are fairly standard and consistent with previous studies (see Alba, 1999, and Bover et al., 2002). The re-employment probability decreases with age. Being married substantially

increases the probability of finding a job. This has to do with lower reservation wages of these individuals given their household responsibilities, and for the same reason their attachment to the labor market is strong. Similarly, the effect of the number of children is positive, but small. Also, the effect of the number of working adults in the household is negative, but again, not very large. The estimated coefficients on education (secondary education or more) are negative for the pre-reform years, but positive afterwards. The latter accords with existing results, such as Bover et al. (2002) who find that secondary education has no significant effect while a university degree has a positive effect on the re-employment probabilities for the period 1987–94 during the first three months of unemployment. The former may be partially explained by the fact that most workers in the pre-reform period had just a secondary degree.³⁴ Finally, the effect of the business cycle indicator (the local unemployment rate) is always negative. Columns (2) to (4) report the estimates the same model as in column (1) but with different business cycle indicators. As can be seen results are robust to the different specifications.³⁵

While the period before the reform (from 1980 to 1984) is a recession, in the period after the reform there are some years of expansion (from 1985 to 1991) and some years of recession (from 1992 to 1994). As mentioned before, LTU typically displays anti-clockwise loops over the cycle implying that the incidence of LTU is generally higher in an expansion than in a recession (see Machin and Manning, 1999). This can imply higher duration dependence in expansion years. Given this, I re-estimate the model allowing for an interaction term of the duration dependence parameter with the quarterly change in the unemployment rate (in logs). Column (5) of table 4 reports these estimates. As expected, since duration dependence increases when the unemployment raises, the coefficient of this interaction term is positive

³⁴These findings are consistent with the higher incidence of LTU among higher educated unemployed individuals (Machin and Manning, 1999).

³⁵The effect of the business cycle is smaller when measured in terms of GDP growth since this is a national-wide variable and it has less variation than the regional unemployment rate.

and significant. For the period before the reform, the unemployment is rising for all the years and the average change in the unemployment rate is 0.024. For the post-reform period, there is an expansion and a recession and the average change in unemployment rate is -0.004. Given the new estimated coefficient, this implies that the business cycle contributes to a lower duration dependence in the pre-reform period (higher α by 0.05) and to a higher duration dependence in the post-reform period (lower α by 0.01). In this estimation, the coefficient on the post-reform dummy interacted with α is now the change in duration dependence after the reform net of the business cycle effects. As expected, it is smaller than that in column (1), but the difference is very small. This suggests that duration dependence is larger in the post-reform period even after taking into account business cycle effects.

In table 5, I report the estimates of the probability of leaving unemployment for the post-reform period with each variable interacted with a recession dummy (which takes value 1 for the recession years, i.e. 1992 to 1994). As expected, I find that duration dependence is lower during recessions. However, comparing the estimated parameter of the duration dependence for the recession years, it is still lower than in the pre-reform period (see table 11, column 4).³⁶

A further check of the increase of duration dependence after the introduction of TCs, despite the fact there are some expansion years in the post-reform period, is to compare the years 1983 and 1992, which are the most comparable in terms of unemployment rates (see figure 5). Table 6 reports these estimates. The change in duration dependence after the reform is somehow smaller than for the whole sample period, indicating the effect of the business cycle, but it is still significant.

As mentioned above, it is important to allow for unobserved heterogeneity in the model.

Table 7 reports the estimates of the model for the case of a discrete-distribution unobserved

³⁶Testing that the duration dependence parameter in these recession years is the same as in the pre-reform period (that is, $\alpha = 0.849$) gives the test statistic $z = 13.51$. Therefore, the null hypothesis is rejected at standard levels of significance.

heterogeneity. As expected, the inclusion of more parameters to be estimated increases the value of the duration dependence parameter. The main result regarding the increase in duration dependence after the reform is smaller than in previous specifications but it is still sizeable and significant.³⁷ These estimates also provide some evidence that, in terms of unobserved characteristics, the difference in the probability of leaving unemployment between the workers type θ_1 and type θ_2 increased after the reform.

As table 2 shows, even if there is no control group, some unemployed workers were more affected by this reform than others. Given this, I re-estimate the model allowing for the duration dependence parameter to vary between workers in different sectors and skills before and after the reform.³⁸ According to the theoretical considerations discussed above, duration dependence of those groups more affected by the reform (that is, non-seasonal and skilled workers, respectively) should have changed more after the reform than for those groups less affected. At the same time, since the level of TCs for the more affected groups is lower both before and after the reform, the level of duration dependence should also be lower in the two periods for these groups.

Table 8 displays these estimates. As in the rest of the paper, the duration dependence parameter is interacted with a post-reform dummy (*d8594*). Moreover, it is also interacted with a *more_affected_group* dummy (which takes value 1 for the different groups discussed above). Finally, the duration dependence parameter is interacted with the post-reform and the *more_affected_group* dummy. The coefficient on this last variable indicates the differential change in duration dependence after the reform for the more and less affected groups. As expected, it is always negative for the different groups analyzed suggesting that dura-

³⁷Bover et al. (2002) as well as Canziani and Petrongolo (2001), using the panel version of the same data set, find that their results do not change qualitatively after controlling for unobserved heterogeneity.

³⁸Sector refers to sector in the previous job. The prediction is thus that to the extent that workers get reemployed in the same sector as in their previous job, those unemployed in non-seasonal sectors should be more affected by the reform. Given the reduction in the agriculture sector, it has been excluded from the analysis. This corresponds to only 5 per cent of the sample. Results in Table 4 remain unchanged if agriculture is excluded.

tion dependence increased more for the more affected groups after the reform. Also, the coefficient of the duration dependence parameter interacted with the *more_affected_group* dummy is always positive which indicates that duration dependence was lower for these groups prior to the reform. Finally, the sum of the coefficients on $\alpha \times \text{more_affected_group}$ and $\alpha \times d8594 \times \text{more_affected_group}$ is always positive which indicates that duration dependence is also lower for the more affected groups after the reform. Overall these results give further support to the idea that the introduction of TCs can increase the duration dependence of unemployment.

The number of variables available in the Spanish Labor Force Survey has increased over time. Therefore, I estimate a second set of regressions in which more variables are included for the period 1987—1994. The inclusion of more variables can affect the estimated duration dependence parameter. Therefore, it is important to check whether the above result is affected by the exclusion of these variables. Table 9 displays the results of the estimations without the UI dummy and the end-of-temporary-contract dummy; the estimations including only one of the two variables; and the estimation including both variables. As expected, the parameter of duration dependence increases with the different specifications. However, it is always lower than in the pre-reform period.³⁹ It is interesting to note that since UI is based on previous work experience and the introduction of TCs implied shorter job tenures, it was potentially more difficult to obtain UI in the post-reform period. This would imply, *ceteris paribus*, lower duration dependence in the post-reform period due to an interaction effect between TC and UI. However, results in table 9 suggest that the direct mechanism of TCs suggested in this paper is stronger and overall duration dependence increases after the introduction of TCs.

³⁹Regressions from table 9 (columns 2 to 4) are not strictly comparable to that in table 4 (column 1) since the latter has fewer explanatory variables. However, since the exclusion of additional explanatory variables generates an underestimate of α in the pre-reform period (table 4), its comparison with the estimated α in table 9 is more restrictive than it should be.

The effects of the variables also included in the previous regressions remain very similar. As can be seen, the effect of UI is positive. At first glance, this result may be surprising if one has in mind the standard *disincentive effect* from job search theory (see Mortensen, 1970 and 1977).⁴⁰ There are several possible reasons for this result. First, the UI variable is only an indicator of whether the unemployed person is receiving benefits when being interviewed. There is wide consensus that the effects of unemployment benefit levels are far from robust, being in general not very significant and of small size, and that other dimensions of unemployment compensation may be more important, such as duration of benefits (see Atkinson and Micklewright (1991) for a review).⁴¹

Secondly, Alba (1999) and Bover et al. (2002) find that the effect of receiving unemployment benefits is significant and quite sizeable, but that this effect is reduced over the spell of unemployment. In other words, that the correlation between unemployment duration and UI is smaller as duration increases. Table B in the Appendix reports this correlation for different duration categories. Indeed, this correlation is higher at shorter durations, suggesting that the disincentive effect is present there. However, for longer durations, the correlation not only becomes smaller but it actually becomes negative. Wadsworth (1990) and Schmitt and Wadsworth (1993) exploit the idea that UI facilitate search by providing income with which to finance job search efforts (*the job offers effect*). These studies compare the search behavior of benefit claimants and non-claimants. They find that non-claimants search harder during the initial stages of unemployment when benefits may provide a temporary leisure subsidy to benefit claimants. As unemployment duration lengthens, search activities fall for both groups, but benefit recipients are able to maintain a higher level of search effort and

⁴⁰However, Toharia (1997) reviews different studies on the disincentive effects of UI in Spain and concludes that, on the whole, the studies available are not conclusive.

⁴¹Moreover, in cross-sectional data, the fraction of UI recipients can be underestimated for two reasons. First, some unemployed can be interviewed once their UI has already expired and they can report they are not recipients of UI. Second, in Spain, it is often the case that the unemployed start receiving benefits with some delay due to administrative reasons, so they may not report receiving UI if interviewed early in their spell.

therefore have a relatively higher probability of receiving a job offer. This *job offers* effect seems to be very strong in my data. A possible reason why the cited works on Spain may differ on the effect of UI is the treatment given to the unemployment duration variable.⁴²

The other new variable included in this second part of the analysis is a dummy that equals 1 if the reason for separation from the previous job was the ending of a TC. As can be seen in table 9, the estimated coefficient on this variable is positive and significant. This result accords with the idea that TCs have isolated some of the unemployed, making them more employable than the other unemployed. I investigate this issue further by estimating a model in which every variable is interacted with this dummy (see column 1 in table 10). As can be seen, those jobless workers who are unemployed because their TC came to an end have less duration dependence than the other unemployed (this includes voluntary quits, redundancy, retirement, illness, etc.). Canziani and Petrongolo (2001) estimate a semi-parametric duration model using the panel version of the Spanish Labor Force Survey data for the years 1987–1996 and also find that those jobless workers whose TC ended have higher re-employment probabilities. Jenkins and García-Serrano (2000) using data from the national unemployment benefit administration database find that those who entered UI from a TC have much higher re-employment probabilities than those whose contract was a permanent one.

I re-estimate the model for all those workers who are unemployed because their TC came to an end (column 2 of table 10). Among these workers, it is possible to further distinguish if the TC was a seasonal one or not. I find that those workers that are unemployed because their non-seasonal TC expired have lower duration dependence than workers that had a seasonal TC. This result is in line with the result that unemployed from non-seasonal sectors have lower duration dependence in the post-reform period (see table 8).

⁴²Alba (1999) excludes from his sample unemployed people of more than 36 months. Bover et al. (2002) treat durations of more than 14 months as censored at 14 months.

Table 11, columns 5 and 6, report the duration dependence estimates for those unemployed for whom the reason for separation from their last job was the ending of a TC and for those for whom there was another reason. Figure 7 plots the hazard of leaving unemployment for these two groups of unemployed workers from these regressions. Unemployed workers who came from a TC have greater probability of leaving unemployment at any duration than the others. Secondly, the hazard for those who became jobless because of the ending of a TC is flatter than for the other groups of individuals. That is, although there is negative duration dependence, it is much smaller than for those individuals that lost their jobs for other reasons. These results also suggest that TCs have increased the employment chances for a group of the unemployed that churns from employment to unemployment frequently. The remaining unemployed have lower probability of re-employment, and this probability is worse at longer durations.

It is interesting to note that education has an insignificant effect on those who ended a TC, while it has a positive significant effect for those who became jobless for reasons other than the ending of a TC. One possible explanation is that since people who became unemployed because of the ending of a TC have greater probability of leaving unemployment, they are more attached to the labor market and therefore having a university degree or not does not substantially affect the probability of finding a job. Instead, people that became jobless for other reasons are less attached to the labor market and therefore having a university degree can improve their probability of becoming employed.

Returning to the effects of UI, the coefficients for both groups appear to be positive although larger for those who became unemployed for reasons other than ending a TC. This is consistent with the aforementioned effect of unemployment insurance on the duration of unemployment because the unemployed workers who became unemployed for other reasons experience longer durations of unemployment.

All the results discussed above indicate that the distribution of the duration of unemployment has become more unequal in the early 1990s compared to the mid-1980s. A possible explanation for this fact is the introduction of TCs. As mentioned above, these contracts have generated an increase in the average outflow rate. To the extent that the higher employment chances created by these contracts have not been shared equally among all the unemployed, then the outflow rate from unemployment for those who have not benefited from TCs will not have increased. The above results suggest that the re-employment probability of the latter have been reduced. To further investigate this, I re-estimate the above model allowing for a more flexible base-line hazard.

Table 12 report the estimates for the whole sample where every variable is interacted with a post-reform dummy ($d8594$). This regression is similar to the one reported in Table 4, except that three different steps of the baseline hazard are allowed. Figure 8 plots the hazard of leaving unemployment for the reference category estimated by this regression for the years before and after the reform. As can be seen, in the years after the reform the last step of the baseline, which corresponds to the LTU, is lower than in the years before the reform. This result is consistent with the results of the previous parametric estimations. That is, conditional on being long-term unemployed, the probability of leaving unemployment after the reform are lower than before.

6. Conclusion

In this paper I have analyzed the effects of the introduction of fixed-term contracts on the duration distribution of unemployment in Spain. The motivation was, on the one hand, to study whether this policy impacted different dimensions of the labor market, given the failure to reduce unemployment. On the other hand, since the introduction of temporary contracts has made the labor market more dynamic, an additional motivation was to study the impact of the increase in inflows and outflows from unemployment to employment on

the duration distribution of the unemployment.

To answer these questions, I have exploited cross-sectional data available over a very long time period (from 1980 to 1994) that allowed me to analyze the probability of leaving unemployment before and after the introduction of fixed-term contracts in Spain. In particular, I have explored the possibility that fixed-term contracts implied longer duration of unemployment for the long-term unemployed even while it lowered the incidence of LTU due to increased (average) outflow rate. I have found evidence of this effect. In particular, the relative probability of leaving unemployment for the short term unemployed versus the long term unemployed increased significantly from the mid 1980s to the early 1990s. I also find that duration dependence increased relatively more for those population groups that were more affected by the reform than for those who were less affected by the reform.

It seems plausible that these changes have been driven by the introduction of TCs, since this was the major institutional change in the time period studied. Clearly, it is possible that during the period of time analyzed there were also some underlying structural changes in the Spanish economy. As discussed, the important fact is that, in the labor market, these other possible changes materialized through temporary contracts.

It is often argued that a high proportion of LTU is a possible cause of high unemployment itself. Although this causality cannot be conclusively inferred (see Machin and Manning, 1999), in the case of Spain it is possible that the limited success of flexibility measures in reducing unemployment could be linked to the fact that TCs have not helped to reduce the duration dependence in unemployment.

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Table 1: Unemployment rate, incidence of LTU and share of TCs for several countries

		1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Denmark	urate	9.0	8.5	7.1	5.4	5.4	6.1	7.3	7.7	8.4	9.2	10.1	8.2
	LTU	33.0	-	39.3	32.9	30.6	28.7	25.9	33.7	31.2	27.0	-	32.1
	TCs	-	12.5	12.3	-	11.2	11.5	10.0	10.8	11.9	11.0	10.7	12.0
France	urate	8.1	9.7	10.1	10.2	10.4	9.8	9.3	8.9	9.5	10.4	11.7	12.3
	LTU	42.2	-	46.8	47.8	45.5	44.8	43.9	38.3	37.3	36.1	34.2	38.3
	TCs	3.3	-	4.7	-	7.1	7.8	8.5	10.5	10.2	10.5	10.9	11.0
Germany	urate	6.9	7.1	7.2	6.5	6.3	6.2	5.6	4.8	5.6	6.6	7.9	8.4
	LTU	39.3	-	47.9	48.9	48.2	46.7	49.0	46.3	45.5	33.5	-	44.3
	TCs	10.0	-	10.0	-	11.6	11.4	11.0	10.5	10.1	10.5	10.3	10.3
Ireland	urate	14.0	15.5	16.8	16.8	16.6	16.1	14.7	13.4	14.8	15.4	15.6	14.3
	LTU	36.9	-	64.7	65.2	66.4	66.0	67.3	67.2	60.3	-	-	64.3
	TCs	6.2	-	7.3	-	8.6	9.1	8.6	8.5	8.3	8.7	9.4	9.5
Italy	urate	7.7	8.1	8.5	9.2	9.9	10.0	10.0	9.1	8.8	9.0	10.3	11.4
	LTU	57.7	-	65.8	66.1	66.4	69.0	70.4	71.1	67.1	58.2	-	61.5
	TCs	6.6	-	4.8	-	5.4	5.8	6.3	5.2	5.4	7.5	6.0	7.3
Portugal	urate	7.8	8.5	8.7	8.4	6.9	5.5	4.9	4.6	4.0	4.2	5.7	7.0
	LTU	-	-	56.0	56.0	56.6	51.2	48.3	48.1	38.3	30.9	-	43.4
	TCs	-	-	-	14.4	16.9	18.5	18.7	18.3	16.4	11.0	9.8	9.4
Spain	urate	17.5	20.3	21.7	21.0	20.1	19.1	16.9	16.2	16.4	18.5	22.8	24.1
	LTU	52.4	-	56.7	57.6	62.0	61.5	58.5	54.0	51.1	47.4	50.1	56.1
	TCs	-	-	-	-	15.6	22.4	26.6	29.8	32.2	33.5	32.2	33.7
UK	urate	11.1	11.1	11.5	11.5	10.6	8.7	7.3	7.1	8.8	10.1	10.5	9.6
	LTU	47.0	-	47.0	45.9	45.9	44.7	40.8	36.0	28.1	35.4	-	45.4
	TCs	5.5	-	7.0	-	6.3	6.0	5.4	5.2	5.3	5.5	5.9	6.5
US	urate	9.6	7.5	7.2	7.0	6.2	5.5	5.3	5.5	6.7	7.4	6.8	6.1
	LTU	13.3	-	9.5	8.7	8.1	7.4	5.7	5.6	6.3	11.2	11.7	12.2

Notes: (1) *urate* is the unemployment rate; *LTU* is the share of unemployed with spells ≥ 12 months and *TCs* is the share of workers under a temporary contract among employed; (2) Since 1991, data on Germany and EU include the new German Länder; (3) Source: OECD (1993, 1996 and 1999).

Table 2: Evolution of Share of Fixed-Term Contracts,
by Population Groups

	Sectors ¹		Education ²		All
	Non-Seasonal (1)	Seasonal (2)	Skilled (3)	Unskilled (4)	
1987	10.47	33.76	14.71	23.41	15.59
1988	15.74	44.38	21.01	30.21	21.94
1989	19.26	50.60	25.56	31.18	26.11
1990	21.41	54.12	27.89	35.97	28.64
1991	22.50	56.13	29.28	37.23	29.97
1992	24.27	59.01	30.98	39.41	31.66
1993	23.52	57.39	29.97	35.61	30.38
1994	25.12	58.76	31.34	39.02	31.84
Growth rate	139.92	74.07	113.05	66.68	104.17

Notes: ¹Non-Seasonal includes manufacturing and services, Seasonal includes construction; ²Skilled includes primary education and above, Unskilled is below primary education; Source: EPA.

Table 3: Sample characteristics

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
	1980-94	1980-84	1985-94	1992-94	1987-94	EndTC ¹		EndTCNonSeasonal ²		NonSeasonalSector ³		Skilled ³	
						yes	no	yes	no	yes	no	yes	no
Age	35.738 (13.440)	35.010 (13.267)	36.041 (13.502)	36.667 (14.141)	35.926 (13.603)	34.632 (13.490)	36.317 (13.378)	32.965 (11.918)	33.869 (12.988)	33.417 (12.535)	36.659 (12.657)	32.931 (12.145)	45.664 (11.750)
Married	0.527 (0.499)	0.551 (0.497)	0.517 (0.499)	0.492 (0.499)	0.497 (0.500)	0.452 (0.498)	0.566 (0.495)	0.428 (0.494)	0.472 (0.499)	0.473 (0.499)	0.600 (0.489)	0.469 (0.499)	0.761 (0.426)
Second. or univ. ed.	0.326 (0.469)	0.197 (0.398)	0.379 (0.485)	0.476 (0.499)	0.417 (0.493)	0.435 (0.496)	0.268 (0.443)	0.483 (0.499)	0.339 (0.473)	0.446 (0.497)	0.206 (0.405)		
N. of kids	1.003 (1.253)	1.219 (1.416)	0.914 (1.168)	0.808 (1.047)	0.865 (1.124)	0.881 (1.133)	1.068 (1.307)	0.818 (1.094)	0.968 (1.195)	0.895 (1.163)	1.150 (1.327)	0.945 (1.181)	1.230 (1.513)
N. of working adults	0.718 (0.886)	0.699 (0.872)	0.728 (0.891)	0.751 (0.884)	0.762 (0.906)	0.766 (0.911)	0.694 (0.871)	0.810 (0.922)	0.655 (0.878)	0.795 (0.905)	0.658 (0.868)	0.754 (0.897)	0.534 (0.804)
UI				0.463 (0.499)	0.430 (0.495)	0.441 (0.496)	0.216 (0.411)	0.439 (0.496)	0.436 (0.495)				
EndTC				0.713 (0.452)	0.629 (0.483)	1.000 (0.000)	0.000 (0.000)	1.000 (0.000)	1.000 (0.000)				
Log local unemployment	2.692 (0.484)	2.423 (0.512)	2.803 (0.425)	2.691 (0.443)	2.781 (0.441)	2.800 (0.447)	2.747 (0.428)	2.691 (0.427)	3.010 (0.410)	2.628 (0.475)	2.640 (0.501)	2.660 (0.484)	2.833 (0.459)
Log GDP growth rate	2.356 (0.400)	2.489 (0.396)	2.299 (0.343)	1.965 (0.297)	2.215 (0.329)	2.187 (0.337)	2.262 (0.310)	2.170 (0.325)	2.281 (0.340)	2.361 (0.365)	2.375 (0.377)	2.364 (0.364)	2.404 (0.338)
Duration of unemployment ⁴	14.492 (12.887)	12.724 (11.676)	15.227 (13.227)	13.657 (12.333)	15.026 (13.286)	11.897 (11.603)	20.347 (14.241)	10.685 (10.029)	9.245 (10.140)	13.469 (11.641)	12.503 (11.411)	13.582 (12.582)	13.475 (12.628)
Total No. of spells	80,790	23,720	57,070	18,991	44,053	27,740	16,313	18,364	9,376	39,368	24,243	66,135	14,655

¹Equals 1 if reason job loss was the ending of a TC and zero if other reasons; ²Equals 1 if reason job loss was the ending of a non-seasonal TC and zero if it was the ending of a seasonal TC; ³As in Table 2; ⁴Uncompleted duration of unemployment. Reported duration for years after 1987 has been grouped as in previous years.

Note: (1) Standard deviations in brackets; (2) Source: EPA.

Table 4: Maximum likelihood estimates of the probability of leaving unemployment, Weibull specification: full sample, 1980-1994

	(1)	(2)	(3)	(4)	(5)
	Coef.	Coef.	Coef.	Coef.	Coef.
α	0.841	0.822	0.834	0.841	0.843
	(0.023)	(0.023)	(0.023)	(0.023)	(0.027)
$\alpha \times d8594$	-0.346	-0.327	-0.304	-0.305	-0.317
	(0.026)	(0.025)	(0.026)	(0.026)	(0.030)
$\alpha \times \Delta \log \text{ local unemployment rate}$					0.222
					(0.008)
constant	-0.865	-0.709	-1.168	-1.138	-0.837
	(0.104)	(0.104)	(0.105)	(0.106)	(0.118)
constant $\times d8594$	0.952	0.734	1.184	1.155	1.054
	(0.124)	(0.124)	(0.119)	(0.120)	(0.141)
age	-0.011	-0.012	-0.010	-0.010	-0.012
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
age $\times d8594$	0.002	0.003	-0.007	-0.007	-0.005
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
married	0.197	0.193	0.226	0.225	0.235
	(0.026)	(0.026)	(0.026)	(0.026)	(0.031)
married $\times d8594$	-0.215	-0.210	-0.061	-0.060	-0.036
	(0.029)	(0.029)	(0.031)	(0.031)	(0.037)
second. or univ. ed.	-0.094	-0.104	-0.084	-0.084	-0.085
	(0.027)	(0.026)	(0.026)	(0.026)	(0.031)
second. or univ. ed. $\times d8594$	0.151	0.164	0.054	0.053	0.062
	(0.029)	(0.029)	(0.030)	(0.030)	(0.035)
n. of kids	0.021	0.020	0.007	0.008	0.010
	(0.007)	(0.007)	(0.007)	(0.007)	(0.010)
n. of kids $\times d8594$	0.026	0.026	0.007	0.007	0.003
	(0.009)	(0.009)	(0.009)	(0.009)	(0.011)
n. of working adults	-0.042	-0.045	-0.012	-0.012	-0.047
	(0.012)	(0.012)	(0.012)	(0.012)	(0.014)
n. of working adults $\times d8594$	0.018	0.022	0.004	0.005	0.045
	(0.014)	(0.014)	(0.014)	(0.014)	(0.017)
<i>business_cycle_indicator</i> *	-0.304	-0.323	-0.192	-0.211	-0.303
	(0.021)	(0.022)	(0.023)	(0.024)	(0.024)
<i>business_cycle_indicator</i> $\times d8594$	0.081	0.123	-0.003	0.001	0.079
	(0.025)	(0.026)	(0.027)	(0.028)	(0.029)
mean log-likelihood	-2.402	-2.403	-2.404	-2.403	-2.388
No. of obs.	80,790	80,790	80,790	80,790	80,790

*Corresponds to: log local unemployment rate (COLUMNS 1 and 5); lagged local unemployment rate (COLUMN 2), log GDP growth rate (COLUMN 3); log lagged GDP growth rate (COLUMN 4);

Note: (1) Standard errors in parenthesis; (2) The variable *d8594* is equal to 1 for the years 1985 to 1994 and zero otherwise; (3) Source: EPA.

Table 5: Maximum likelihood estimates of the probability of leaving unemployment, Weibull specification: post reform sample, 1985-1994

	Coefficient
α	0.402 (0.010)
$\alpha \times d9294$	0.257 (0.017)
constant	0.428 (0.061)
constant $\times d9294$	-1.128 (0.101)
age	-0.017 (0.001)
age $\times d9294$	0.013 (0.001)
married	0.156 (0.014)
married $\times d9294$	-0.254 (0.021)
second. or univ. ed.	-0.070 (0.012)
second. or univ. ed. $\times d9294$	0.143 (0.019)
n. of kids	0.011 (0.005)
n. of kids $\times d9294$	0.081 (0.008)
n. of working adults	-0.014 (0.006)
n. of working adults $\times d9294$	0.001 (0.010)
log local unemployment	-0.115 (0.013)
log local unemployment $\times d9294$	-0.084 (0.020)
mean log-likelihood	-2.668
No. of obs.	57,070

Note: (1) Standard errors in brackets; (2) The variable $d9294$ is equal to 1 for the years 1992 to 1994 and zero otherwise; (3) Source: EPA.

Table 6: Maximum likelihood estimates of the probability of leaving unemployment, Weibull specification: 1983 and 1992

	Coef.
α	0.738 (0.034)
$\alpha \times d92$	-0.269 (0.039)
constant	-0.384 (0.168)
constant $\times d92$	0.390 (0.211)
age	-0.014 (0.001)
age $\times d92$	0.009 (0.002)
married	0.183 (0.037)
married $\times d92$	-0.344 (0.046)
second. or univ. ed.	0.023 (0.036)
second. or univ. ed. $\times d92$	0.105 (0.045)
n. of kids	0.017 (0.011)
n. of kids $\times d92$	0.051 (0.015)
n. of working adults	-0.047 (0.017)
n. of working adults $\times d92$	0.028 (0.022)
log local unemployment	-0.282 (0.037)
log local unemployment $\times d92$	0.175 (0.048)
mean log-likelihood	-2.353
No. of obs.	9,974

Note: (1) Standard errors in brackets; (2) The variable $d92$ is equal to 1 for the year 1992 and zero otherwise; (3) Source: EPA.

Table 7: Maximum likelihood estimates of the probability of leaving unemployment, Unobserved Heterogeneity: full sample

	Coef.
α	1.066 (0.018)
$\alpha \times d8594$	-0.220 (0.022)
θ_1	-1.774 (0.044)
$\theta_1 \times d8594$	0.409 (0.040)
θ_2	-2.872 (0.068)
$\theta_2 \times d8594$	-0.752 (0.055)
ϕ	0.572 (0.063)
CONTROLS*	Y
mean log-likelihood	-3.572
No. of obs.	80,790

*Same controls as in Table 4; Notes as in Table 4.

Table 8: Maximum likelihood estimates of the probability of leaving unemployment, Weibull specification: more affected groups, 1980-1994

	(1)	(2)
	Coef.	Coef.
α	0.972 (0.023)	0.800 (0.016)
$\alpha \times d8594$	-0.197 (0.017)	-0.381 (0.017)
$\alpha \times more_affected_group^*$	0.079 (0.022)	0.131 (0.020)
$\alpha \times d8594 \times more_affected_group$	-0.037 (0.009)	-0.023 (0.008)
CONTROLS**	Y	Y
mean log-likelihood	-2.398	-2.404
No. of obs.	63,611	80,790

*Column (1): Equals to the variable NonSeasonalSector defined in Table 2.

Column (2): Equals to the variable Skilled defined in Table 2.

**Same controls as in Table 4; Notes as in Table 4.

Table 9: Maximum likelihood estimates of the probability of leaving unemployment, Weibull specification: post reform sample, 1987-1994

	(1)	(2)	(3)	(4)
	Coef.	Coef.	Coef.	Coef.
α	0.495 (0.009)	0.536 (0.009)	0.615 (0.009)	0.651 (0.010)
constant	0.133 (0.050)	-0.133 (0.051)	-0.975 (0.055)	-1.181 (0.056)
age	-0.008 (0.0004)	-0.009 (0.0004)	-0.005 (0.0004)	-0.006 (0.0004)
married	-0.030 (0.010)	-0.124 (0.011)	0.050 (0.001)	-0.032 (0.011)
second. or univ. ed.	0.054 (0.010)	0.067 (0.010)	0.034 (0.010)	0.046 (0.011)
n. of kids	0.057 (0.004)	0.064 (0.004)	0.048 (0.004)	0.053 (0.004)
n. of working adults	-0.015 (0.005)	-0.008 (0.005)	-0.008 (0.005)	-0.002 (0.006)
log local unemployment	-0.232 (0.010)	-0.234 (0.010)	-0.027 (0.011)	-0.273 (0.011)
UI		0.308 (0.010)		0.271 (0.010)
EndTC			0.819 (0.012)	0.813 (0.012)
mean log-likelihood	-2.973	-2.963	-2.911	-2.904
No. of obs.	44,053	44,053	44,053	44,053

Note: (1) Standard errors in parenthesis; (2) Source: EPA.

Table 10: Maximum likelihood estimates of the probability of leaving unemployment, Weibull specification: reason separation in the last job, 1987-1994

	(1)	(2)
	Coef.	Coef.
α	0.503 (0.020)	0.554 (0.011)
$\alpha \times \text{reason_job_separation}^*$	0.180 (0.023)	0.270 (0.014)
constant	0.416 (0.104)	-0.588 (0.036)
constant \times <i>reason_job_separation</i>	-1.281 (0.121)	-0.271 (0.011)
age	-0.017 (0.001)	0.001 (0.007)
age \times <i>reason_job_separation</i>	0.015 (0.001)	-0.155 (0.010)
married	-0.039 (0.021)	0.046 (0.021)
married \times <i>reason_job_separation</i>	0.019 (0.025)	0.073 (0.028)
second. or univ. ed.	0.219 (0.019)	-0.035 (0.008)
second. or univ. ed. \times <i>reason_job_separation</i>	-0.248 (0.023)	-0.067 (0.006)
n. of kids	0.062 (0.008)	0.017 (0.005)
n. of kids \times <i>reason_job_separation</i>	-0.017 (0.009)	0.015 (0.007)
n. of working adults	-0.002 (0.010)	-0.029 (0.010)
n. of working adults \times <i>reason_job_separation</i>	0.006 (0.012)	0.062 (0.012)
UI	0.492 (0.019)	0.118 (0.017)
UI \times <i>reason_job_separation</i>	-0.325 (0.023)	0.128 (0.022)
log local unemployment	-0.516 (0.020)	-0.052 (0.018)
log local unemployment \times <i>reason_job_separation</i>	0.355 (0.024)	-0.202 (0.021)
mean log-likelihood	-2.891	-3.015
No. of obs.	44,053	27,740

*Column (1): Equals to the variable EndTC defined in Table 3.

Column (2): Equals to the variable EndTCNonSeasonal defined in Table 3.

Note: (1) Standard errors in parenthesis; (2) Source: EPA.

Table 11: Summary of duration dependence estimates

		(1)	(2)	(3)	(4)
		1980-1984	1985-1994	1985-1991	1992-1994
(I)	α	0.841 (0.023)	0.495 (0.008)	0.402 (0.010)	0.659 (0.014)
	Source	Table 4, column 1	Table 4, column 1	Table 5, column 1	Table 5, column 1
		(5)	(6)	(7)	(8)
		End_TC	End_Other	End_TCSeas	End_TCNonSeas
(II) ^(*)	α	0.683 (0.011)	0.503 (0.020)	0.554 (0.011)	0.824 (0.011)
	Source	Table 9, column 1	Table 9, column 1	Table 9, column 2	Table 9, column 2

^(*)Includes same regressors as in (I) as well as UI dummy.

Note: (1) Standard errors in brackets; (2) Source: EPA.

Table 12: Maximum likelihood semi-parametric estimates of the probability of leaving unemployment: full sample, 1980-1994

	<i>spell months</i>	Coefficient
step1	<i>1 to 5</i>	-0.548 (0.048)
step1 × <i>d8594</i>		-0.355 (0.056)
step2	<i>6 to 11</i>	-1.218 (0.025)
step2 × <i>d8594</i>		-0.328 (0.026)
step3	<i>12 to 36</i>	-1.733 (0.044)
step3 × <i>d8594</i>		-1.157 (0.051)
age		-0.101 (0.005)
age × <i>d8594</i>		0.031 (0.006)
married		0.177 (0.009)
married × <i>d8594</i>		-0.187 (0.009)
second. or univ. ed.		-0.073 (0.015)
second. or univ. ed. × <i>d8594</i>		0.111 (0.016)
n. of kids		0.013 (0.004)
n. of kids × <i>d8594</i>		0.023 (0.005)
n. of working adults		-0.038 (0.007)
n. of working adults × <i>d8594</i>		0.025 (0.008)
log local unemployment		0.171 (0.014)
log local unemployment × <i>d8594</i>		-0.255 (0.012)
mean log-likelihood		-2.298
No. of obs.		80,790

Note: (1) Standard errors in parenthesis; (2) The variable *d8594* is equal to 1 for the years 1985 to 1994 and zero otherwise; (3) Source: EPA.

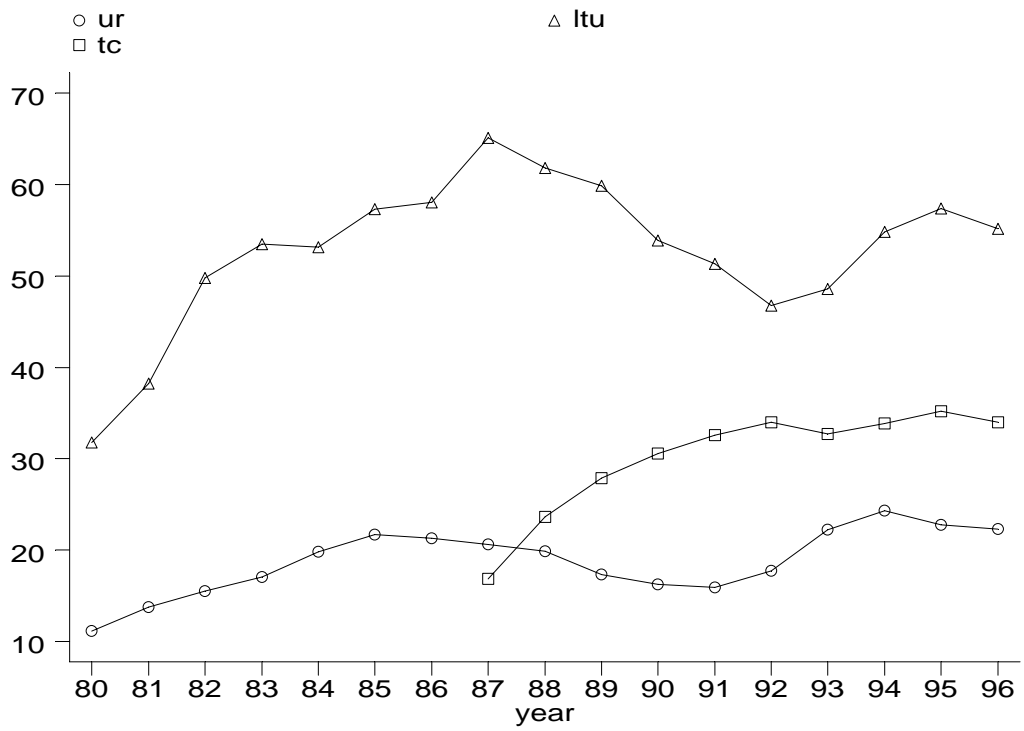


Figure 1: Unemployment rate, proportion of LTU and share of temporary contracts, 1980-1996. Source: EPA.

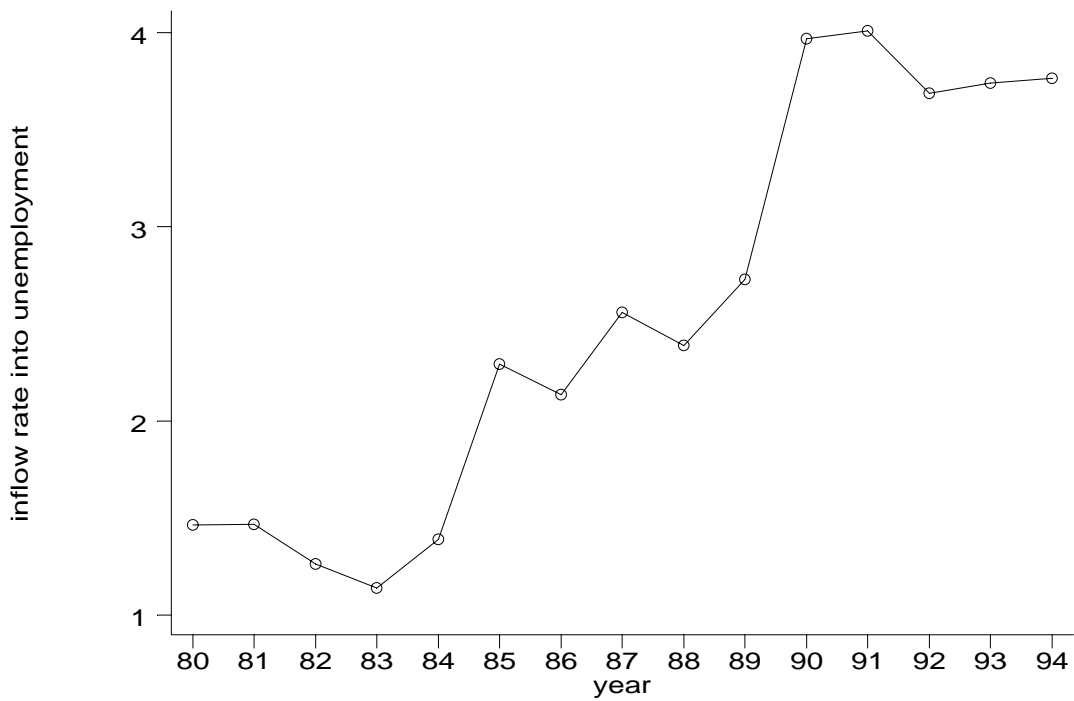


Figure 2: Evolution of inflow rates from employment into unemployment, 1980-1994. Source: MLR.

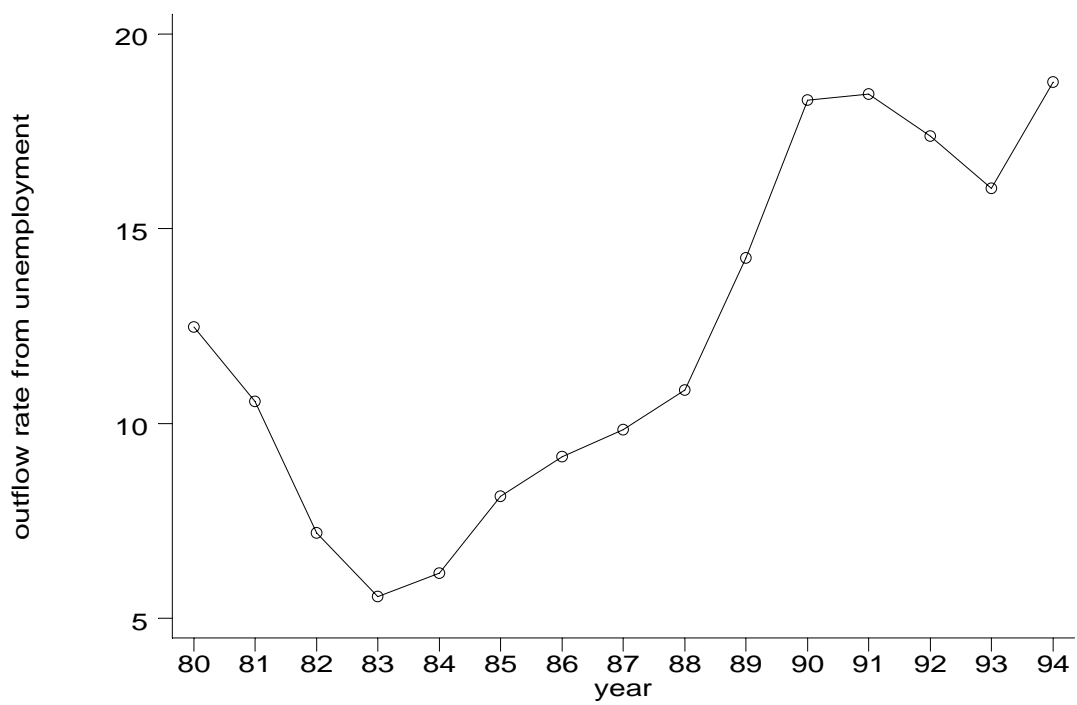


Figure 3: Evolution of outflow rates from unemployment into employment, 1980-1994. Source: MLR.

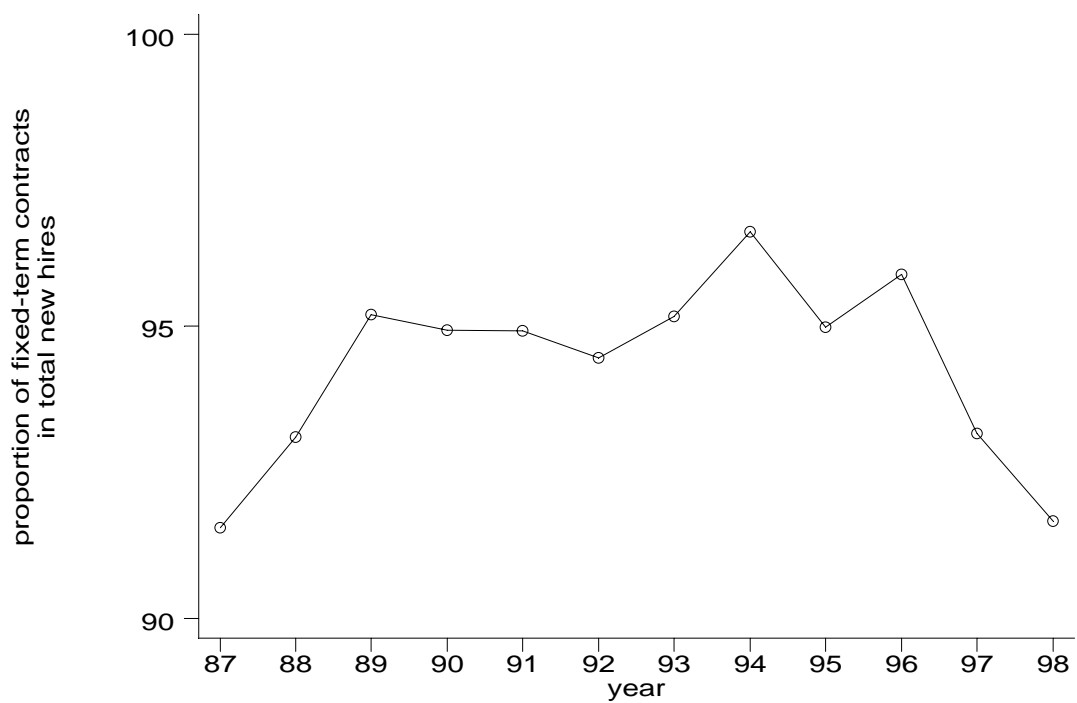


Figure 4: Evolution of the share of fixed-term contracts in new hires, 1987-1998. Source: MLR.

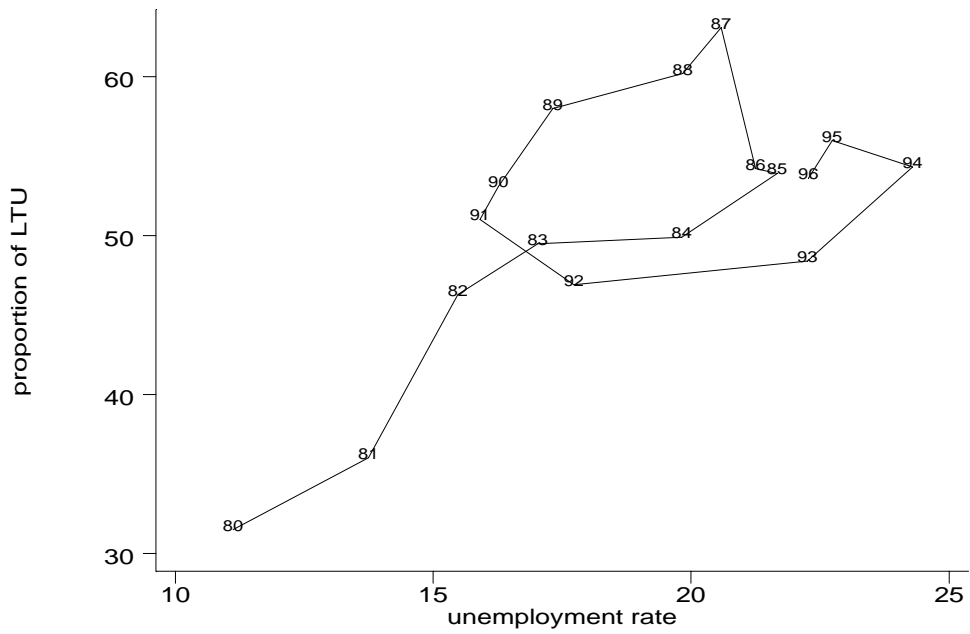


Figure 5: The incidence of LTU and the unemployment rate, 1980-1996. Source: EPA.

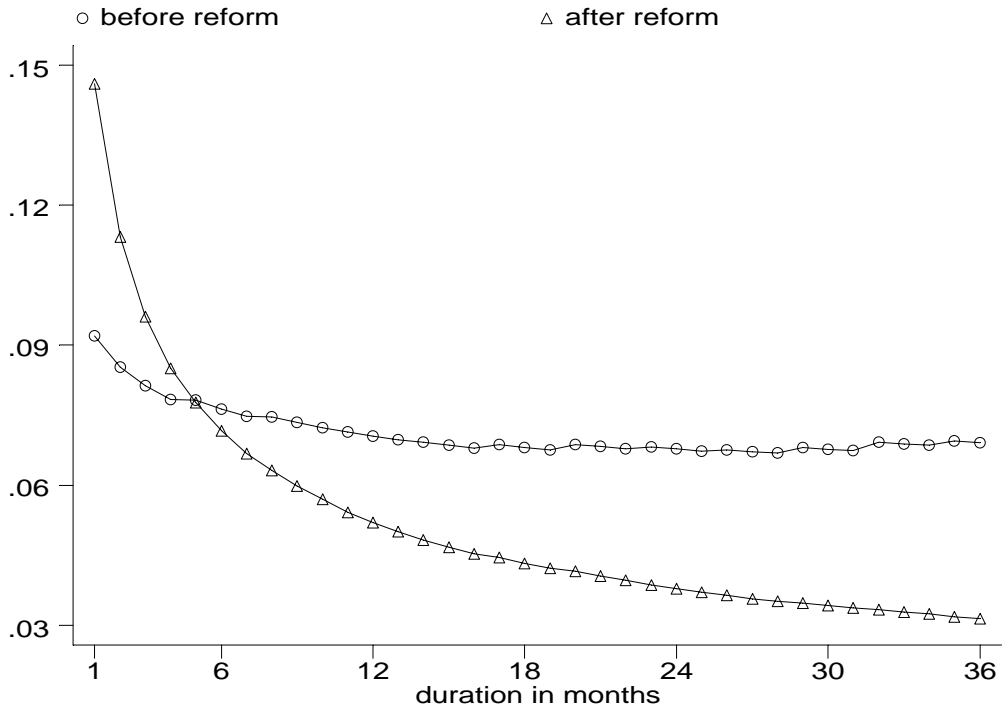


Figure 6: Hazard of leaving unemployment for the reference worker before and after the introduction of TC. Ref. category: age 35, not married, primary ed. or below, no kids, no working adults in household (see Table 3).

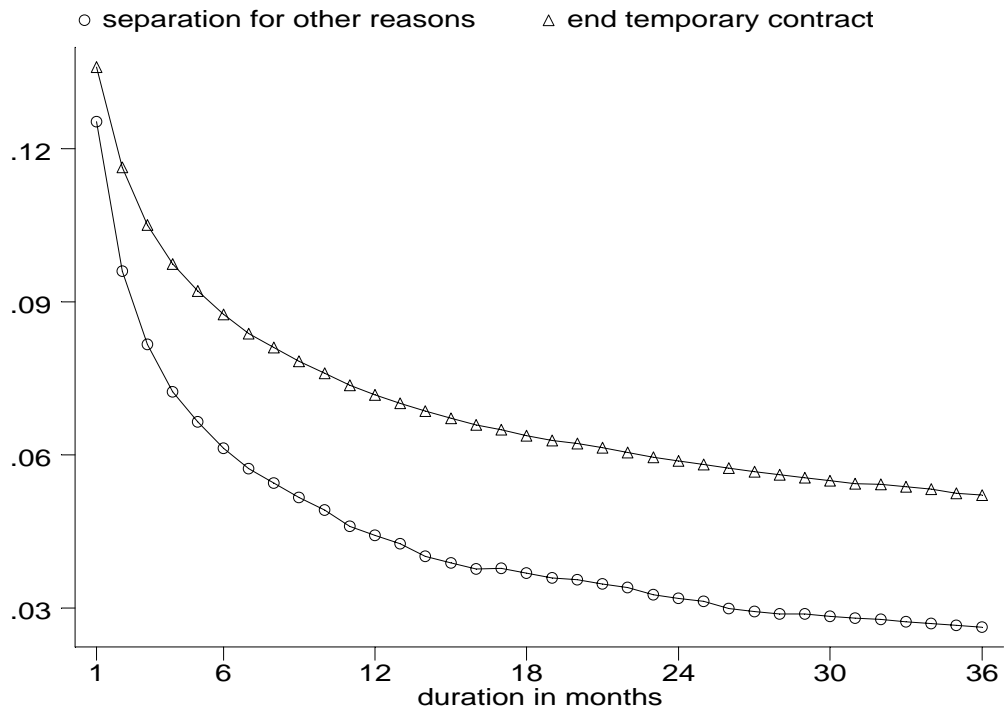


Figure 7: Hazard of leaving unemployment for workers who became jobless because ending of TC and for other reasons. Ref. category: age 35, not married, primary ed. or below, no kids, no working adults in household, no UI (see Table 7).

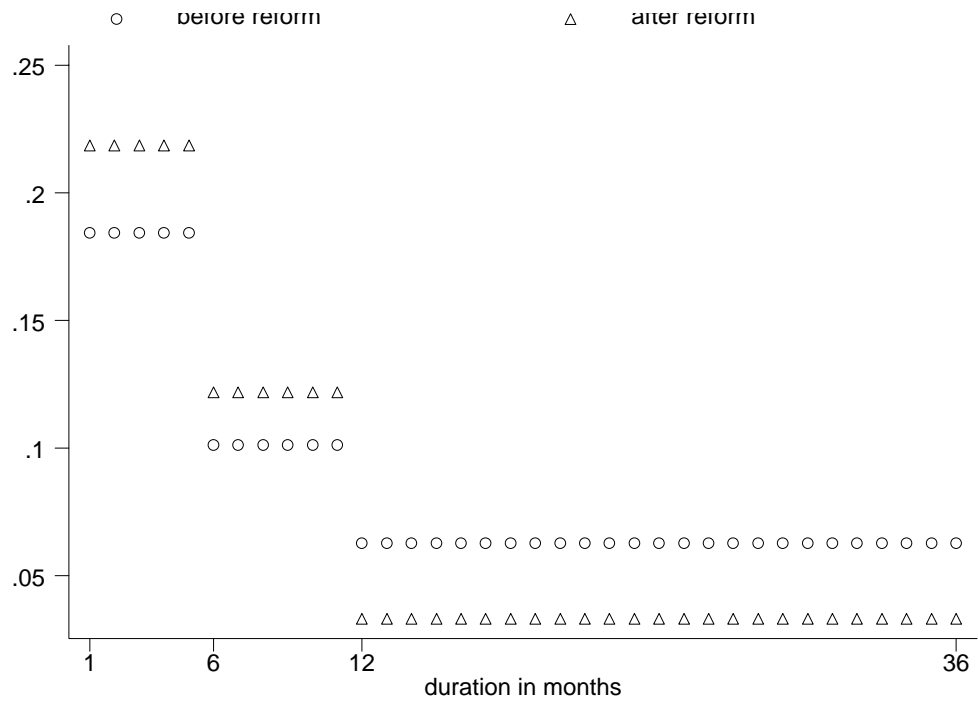


Figure 8: Hazard of leaving unemployment for the reference worker before and after the introduction of TC. Ref. category: age 35, not married, primary ed. or below, no kids, no working adults in household (see Table 9a, 9b).

Appendix

Table A: The duration of the unemployment in the EPA

until 1987 (I)	1987 (II) - 1991(VI)	from 1992 (I)
<i>How long have you been looking for a job?</i>	<i>How long have you been looking for a job?</i>	<i>Which day did you start looking for a job?</i>
<i>Less than 1 month</i>	If less than 2 years,	<i>Month</i>
<i>1 to 3 months</i>	<i>number of months</i>	
<i>3 to 6 months</i>		
<i>6 months to 1 year</i>	If 2 years or more,	<i>Year</i>
<i>1 to 2 years</i>	<i>number of years</i>	
<i>2 years or more</i>		

Table B: Correlation of UI receipt and duration of unemployment

	1987-1994
all durations	-0.109
less than 3 months	0.093
less than 6 months	0.152
more than 6 months	-0.184
more than 12 months	-0.214

Table C: Testing for the constancy of inflow composition

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	1987-89	1988-90	1989-91	1990-92	1991-93	1992-94	1987-94
age	2.27	6.79	2.12	4.94	1.05	6.29	13.11
	(0.32)	(0.03)	(0.35)	(0.08)	(0.59)	(0.04)	(0.07)
married	1.87	1.26	4.69	6.09	4.84	2.44	9.29
	(0.39)	(0.53)	(0.10)	(0.05)	(0.09)	(0.29)	(0.24)
second. or univ. ed.	0.44	1.11	2.09	0.62	0.65	2.16	6.16
	(0.80)	(0.57)	(0.35)	(0.73)	(0.72)	(0.34)	(0.52)
n. of kids	0.47	0.00	3.21	2.40	0.40	0.99	5.17
	(0.79)	(1.00)	(0.20)	(0.30)	(0.81)	(0.61)	(0.63)
n. of working adults	2.19	2.14	4.02	2.21	1.76	0.33	4.84
	(0.33)	(0.34)	(0.13)	(0.33)	(0.41)	(0.84)	(0.67)
No. of obs.	114,409	119,326	121,154	119,856	114,376	108,639	304,413

Note: (1) Reported χ^2 (2) in columns (1) to (6) and χ^2 (7) in column (7);

(2) p-value in parenthesis; (3) all regressions include year dummies; (4) Source: EPA.