



**ACTIVE LABOUR MARKET POLICIES:  
RELEVANCE, EXPENDITURE AND  
EFFECTIVENESS**

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## **ABSTRACT**

From a theoretical point of view active labour market policy may improve labour market outcomes. It consists of the types of measures that seem to be suited to deal with the labour market imperfections causing unemployment. However, for a number of reasons the effects are often relatively poor in practice. One reason is that publicly subsidized employment services may lead to crowding-out of private employment services. Another reason might be that the government is unable to organize implementation efficiently. However, there are no obvious alternatives that are likely to produce better results.

OECD data on ALMP expenditure shows that the structure of ALMP expenditure has changed between 1991 and 2003. The average picture for the Western OECD countries is a shift away from training and towards information, counselling and mediation services, and related services. In recent years job creation measures have lost ground in favour of subsidies for placement in regular jobs.

To what extent is this change in line with the relative performance of the various measures? Do the changes in the structure of ALMP expenditure imply a shift from less effective to more effective measures? A review of the international literature based on 130 studies suggests that this is, to some extent, the case. From the literature job counselling, job search monitoring, sanctions and placement subsidies for regular jobs come out favourably. For training the picture is mixed. A closer look at the results, however, shows that mainly youth training gives poor results. For adult and particularly for older unemployed training might be quite effective. Job creation comes out most poorly.

In our meta-analysis of the evaluation literature we looked at what percentage of the studies produced significantly positive effects of ALMP measures on job entry rates. A next step could be to try and extract an indication of the size of the effects from the literature. Together with information on the costs of the measures that would allow us to give better policy recommendations.

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# 1 INTRODUCTION

In this paper we deal with three questions. The first question is what theory has to say about the potential effects of ALMPs. Can we expect positive outcomes at all? The second question is how expenditure on active labour market policies (ALMPs) is divided over the various types of measures and what changes have occurred in the use of the different types over time. The third question is what the international evaluation literature tells us about the performance of the various measures. And do we observe an increasing use of measures that come out favourably from the evaluation literature?

Active labour market policy aims at reintegrating the unemployed in the labour market. The OECD (see the various Employment Outlooks) understands by active labour market policy both the core (job mediation) activities of the public employment service as well as specific reintegration measures such as training and subsidized labour. Traditionally, the latter activities, which are often targeted towards disadvantaged groups, were also largely implemented by the public employment service. However, recently governments are more and more inclined to outsource the implementation of specific active measures to private agencies. Australia and The Netherlands are the most pronounced examples of this development (see for example Bruttel (2005), De Koning (2004) and Struyven et al (2002)).

In this paper we use a broad definition of active labour market policy, comprising both the core activities of the public employment service and specific reintegration measures. Sanctions such as cuts in benefits in case of inactive job search behaviour and bonuses when unemployed find jobs, are also included. In sum, in our definition active labour market policy consists of the following measures and instruments;

1. information instruments and job mediation;
2. job counselling;
3. sanctions, bonuses and job search monitoring;
4. training;
5. placement subsidies and wage subsidies for regular jobs;
6. job creation schemes.

Information instruments and job mediation are based on registration systems for vacancies and jobseekers that can be used to improve the matching process. Most public employment services have such registrations. Simply providing information on jobseekers to employers and information on vacancies to jobseekers already improves the matching process, particularly when the

information is computerized and search engines are available for use by jobseekers and employers. This is also referred to as 'open' forms of mediation, in contrast to 'closed' forms of mediation. We speak of the latter form of mediation when the public employment service makes a selection of jobseekers for a given vacancy. There is information about the resources spent on information instruments and mediation, but we hardly know anything about the effectiveness of these instruments for individual jobseekers.

Just as job mediation comes in different forms, also the other ALMPs vary in content. Job counselling consists of advice and assistance in job search. Examples are help in writing application letters, learning how to behave in application interviews, motivating clients, etc. The activities may be either oriented towards individual clients or group-oriented. In practice job mediators may also provide counselling to clients and the two activities may be strongly intertwined. The same is true for what one could call incentives for jobseekers (job search monitoring, sanctions in case of inactive job search behaviour and bonuses in case of job acceptance). Training is also a very heterogeneous concept. There is variation in level, field, duration, training method (for example class-room training versus e-learning) and the type of training provider (a public school or a private training agency). All these factors may affect both the costs of training and its effectiveness. Heterogeneity is also strong with respect to subsidized labour and job creation schemes. They may vary according to duration, type of work, sector and target group. Given the heterogeneity in the broad categories of instruments a further differentiation than the one given earlier would be important. However, there is simply not enough information available to make a more detailed breakdown of types of instruments. That implies that variation in outcomes among evaluation studies will be at least partly due to variation in design and implementation strategies.

This paper is structured as follows. Section 2 deals with the policy theory behind ALMPs. Then, section 3 uses OECD data to give a picture of the changing pattern in the use of ALMPs. Section 4 gives a review of the international evaluation literature. The final section, section 5, sums up the conclusions.

## **2 WHAT CAN WE EXPECT FROM ACTIVE POLICIES ON THEORETICAL GROUNDS?**

The theoretical justification for labour market policies is that the labour market functions inefficiently and produces outcomes that are considered to be undesirable from a social point of view. Inefficiency can be inferred from the fact that in real-life labour markets, unemployment and unfilled labour demand exist side-by-side. Furthermore, aggregate labour supply is usually larger than aggregate labour demand. So, the labour market is never cleared and

unemployment rates tend to be relatively high. From a social point of view, unemployment is a problem because most people depend on labour for their living. Being unemployed is particularly troublesome when people remain it for a long time. However, also the fact that unemployment is unevenly distributed over the different social groups makes it a social problem. Even during periods of low aggregate unemployment, some individuals and some social groups may still suffer from long-term unemployment or recurrent short spells of unemployment.

Two types of measures have been developed to deal with these problems. Firstly, minimum wages and social protection measures (or passive measures) have been introduced to safeguard people from poverty. While protecting people against poverty and loss of income caused by unemployment, these institutions may at the same time increase unemployment<sup>1</sup>. Firstly, minimum wages may imply that for some categories of workers wages become higher than productivity, making it unattractive for employers to hire these workers. This is also known as the productivity trap. Secondly, income protection measures may reduce the incentive for unemployed jobseekers to accept jobs. Since both minimum benefit levels and minimum wages are often based on minimum needs, the difference between the two tends to be small. Then, for people depending on low-paid labour, the financial incentive to accept a job will be low. This is often referred to as the unemployment trap.

So, one could argue that passive measures are causing unemployment and that reforms in social benefit schemes are a more logical answer to the unemployment problem than active measures. However, although social protection may worsen the unemployment problem it is not the principal cause for it<sup>2</sup>. It is the unemployment problem that led to social protection and not the other way round. Governments introduced social protection measures to reduce the extreme poverty that arose from the frequent periods of unemployment that capitalist economies produced during times when social protection hardly existed. Therefore, other, more fundamental factors, i.e. market failure, must be behind the unemployment problem.

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<sup>1</sup> In addition to the points mentioned one could also argue that social benefits will have to be financed. Particularly when the financial burden of social protection weighs primarily on labour, this may have a negative effect on labour demand.

<sup>2</sup> The effect of reducing benefits and minimum wages is probably rapidly declining the lower the levels get. The empirical effects found in the literature are surprisingly small (see for example the review of the economic literature on minimum wages in Ehrenberg and Smith, 1997).

The following points can be mentioned:

1. Friction between vacancies and jobseekers exists even in relatively homogeneous submarkets, implying co-existence of vacancies and unemployment and positive search durations for employers and unemployed.
2. Mismatch between labour demand and labour supply owing to discrepancies between the competencies of the people that offer themselves on the labour market and the skills requirements set out by employers.
3. Wage rigidity. The fact that wages tend to stay above a certain level is not only caused by institutions such as statutory minimum wages, but is also a fundamental characteristic of the labour market, which has to do with phenomena such as monopoly power of workers and efficient wages.
4. Uncertainty about the productivity of unemployed workers. Employers are often reluctant to hire unemployed (particularly long-term) unemployed workers because they fear that personal characteristics (lack of motivation, low productivity, etc.) caused the unemployment. A specific situation occurs when the average productivity of a certain category is lower than that of other groups and employers assume that this holds for each member of the group (statistical discrimination<sup>3</sup>).
5. Unemployment due to business cycle movements. Partly due to the above factors and also to institutions, adjustments process after external shocks are sometimes slow, leading to mass long-term unemployment for quite a long period.

These factors explain why unemployment occurs, why unemployment and unfilled demand tend to co-exist and why some groups suffer more heavily from unemployment than others. Active measures can, in principle, solve these problems. Information and mediation, training and direct job creation can reduce friction, mismatch and a general shortage of jobs, respectively. Furthermore, temporary subsidies can induce employers to hire unemployment individuals when they are uncertain about the latter's productivity. By increasing the employability of unemployment jobseekers and by providing employers with information on jobseekers, active policies may also add to wage flexibility.

However, the question is whether it is necessary that the government delivers employment services for free. Private employment services may solve at least some of the problems mentioned. Under private employment services we

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<sup>3</sup> It is also possible that employers *believe* that the average productivity of a specific social group is below average, while this is actually not true. In other cases discrimination has nothing to do with competencies, but expresses the dislike for certain groups. In practice, it is often very difficult to disentangle the different forms of discrimination.

understand services by private employment and training agencies bought by jobseekers and firms without any government subsidies<sup>4</sup>. Jobseekers and firms can also use newspaper advertisements, the Internet and informal channels as search channels. In fact, they do so in practice. In the Netherlands, for example, many employers and jobseekers use temporary work agencies to fill vacancies and find jobs. Temporary work is then used as a kind of probation period. A considerable number of firms hire and train unemployed person and even some unemployed persons follow courses on their own expenses (De Koning et al, 2004 and 2005). Finally, a considerable percentage of vacancies are filled through informal channels, advertisements and the Internet.

However, there are several reasons why government subsidies may still be needed. Firstly, the search channels mentioned may not be effective enough for disadvantaged groups. The latter often lack the social network for effective informal search. Secondly, buying the services of private employment and training agencies is financially impossible for many unemployed<sup>5</sup>. But could firms then not take the initiative for hiring and training? For firms risk aversion is less important than for individuals and is it more the uncertainty about an unemployed person's motivation and productivity that makes them hesitate to hire and train unemployed jobseekers<sup>6</sup>. This is particularly true when the latter are long-term unemployed or belong to categories with above-average unemployment rates. As employers pay for the services of temporary work agencies the latter usually start from the employers' requirements and may therefore be of limited use to disadvantaged groups. Therefore, problems associated with friction and mismatch will only partly be solved by private agencies.

Another limitation of private agencies is that each of them has only a partial view of the labour market. Public employment services have the opportunity to register most unemployed and a large part of the vacancy market. This makes mismatch visible and reduces information shortages. Even for private placement and training agencies such information is helpful. Some public employment

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<sup>4</sup> Private employment services should be sharply distinguished from involvement of private agencies in public employment services and other active measures. In principle, implementation of most active measures can be outsourced by the private sector with the government still paying for the services.

<sup>5</sup> If markets would function perfectly with complete knowledge of the effectiveness of the services, people could borrow the money. However, using employment services and getting trained does not guarantee that a person finds a job, particularly not if he has a low profile in the labour market.

<sup>6</sup> In case of general training there is also the danger, from the employer's point of view, that a worker leaves the firm after being trained.

services produce labour market forecasts, which may be helpful in educational and occupational choice<sup>7</sup>. It is unlikely that such information can be sold on a commercial basis as buyers of the information can easily share the information with others. Basically, it is a public good.

Private employment services cannot solve the problems associated with the productivity trap, the unemployment trap and situations with a general shortage of jobs, or only to a limited extent. Only the government can take measures to increase the incentives for the unemployed (by applying sanctions, for example) to accept jobs and for employers (by applying subsidies) to hire unemployed and to create additional jobs.

To sum up, in theory active measures may improve labour market outcomes. However, that does not guarantee that they have the desired effects in practice. There are several reasons why theoretically expected effects are not or only partly realized in practice:

- a.* Crowding-out of the private employment services market. Although the added value of the public employment service is often highest when it provides services to weaker groups, it does not always do so in practice. Particularly, when the number of placements is seen as an important target, the public employment service may be tempted to concentrate on the stronger groups that are already being served by the private agencies. Crowding-out of the private employment services market is likely then.
- b.* Displacement and substitution. Measures aimed at improving the job entry chances of disadvantaged groups may go at the expense of other workers. Job creation schemes, for example, may displace existing employment.
- c.* No proper organization by the government. In case of implementation by public agencies the lack of competitive pressure may cause inefficiency and ineffectiveness. Furthermore, politics with its changing priorities may heavily influence the day-to-day work of the public employment service. Such phenomena make economists such as Barro (1996) highly sceptic of government interventions, even if market failure occurs.
- d.* Implementation costs may outweigh the benefits. Even if active labour market policy has positive effects, it may not be enough to outweigh the costs.

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<sup>7</sup> See Schömann and Neugart (2002) which contains examples of labour market forecasting in several countries.

These factors may explain the fact that the results of active labour market policy have been somewhat disappointing (although later we show that some measures are probably quite effective). One way of reacting to this fact is reforming active labour market policy, by improving the measures or by improving the delivery system. The other way is to examine the possibility of alternative measures such as:

- Agreements of the government with big companies, branch organizations and other organizations (local authorities, schools, etc.) in which the latter commit themselves to hire a larger share of their staff from specific disadvantaged groups. In the Netherlands such agreements have been made, for example, for ethnic minorities.
- Legal prescriptions for employers for hiring certain categories of workers. In some countries, for example, employers are fined if the share of handicapped workers is below a certain threshold. The government may also use the threat of making such prescriptions to stimulate self-regulation or the type of agreements under a).
- Preferential treatment in government procurement procedures of companies that hire a certain percentage of their workers from the pool of unemployment.
- General measures to reduce wage costs for employers (such as tax reductions or exemption of social premiums for low-paid labour) or to create financial incentives limiting the use of social security (for example earnings tax credits and experience rating).

*Table 1 Labour market problems and the possible added value of ALMPs*

Labour market problem	Source of problem	Relevant ALMP measure(s)	Alternatives	Why could ALMP have added value?	Risks in applying ALMPs
Friction between labour supply and labour demand	Information not freely available	Registration of jobseekers and vacancies and provision of self-service search tools Mediation Counselling	Private agencies collecting and selling labour market information Private employment agencies	Information is to some degree public good, limiting the scope for private firms to collect and supply it  Private services may be less accessible for disadvantaged groups	Crowding-out of private initiatives (applies mainly to mediation and counselling)
Mismatch	Information not freely available	Training combined with mediation and counselling	Private employment and training agencies  Agreements between the government, branch organizations and other relevant organizations	Coordination by PES  PES information on training options and future job prospects  Firms may be unwilling to train and hire workers coming from different sectors with different professions without financial compensation	Crowding-out of private initiatives  Forecasts used for training planning may not be accurate enough  Unemployed may lack sufficient motivation and ability for training
Productivity trap	Social benefits and minimum wages exceeding the productivity of certain categories of workers  Downward wage rigidity	Training Wage subsidies Job creation schemes	Agreements with big companies, branch organisations, etc.  Legal prescriptions for companies to hire disadvantaged groups  Preferential treatment of companies that hire (long-term) unemployed	Effectiveness and applicability of alternatives is questionable  For specific groups such as the handicapped some of these alternatives may not be appropriate	Unemployed may lack sufficient motivation and ability for training  Wage subsidies may evoke displacement  Job creation may lead to crowding-out  Job creation may imply lock-in effects

*Continuation of table 1*

Labour market problem	Source of problem	Relevant ALMP measure(s)	Alternatives	Why could ALMP have added value?	Risks in applying ALMPs
Unemployment trap	Social benefits hardly differing from wages	Sanctions, bonuses, job search monitoring, work-first measures	Earnings tax credit Reducing benefit levels	Effectiveness and applicability of alternatives is questionable	
Unemployment much higher than average among specific groups	Uncertainty about jobseeker's motivation and productivity Prejudice and statistical discrimination Cultural differences Productivity trap and unemployment trap more relevant for some groups than for others	For productivity trap and unemployment trap, see above Counselling Wage subsidies	Agreements Legal prescriptions Preferential treatment	Effectiveness and applicability of alternatives is questionable Coordination by public employment service	Most risks mentioned earlier apply also here
High unemployment owing to an economic recession	Slow adjustment processes in the economy	Job creation	Macroeconomic policies stimulating the economy Increasing the flexibility of the labour market to speed up adjustment processes	Alternative measures may not prevent that many people become long-term unemployed	Danger of lock-in effects, reducing the transition from subsidized jobs to regular jobs Danger of crowding-out of private sector employment

An evaluation of these alternative measures is beyond the scope of this paper. However, no miracles can be expected from them. Clearly, there is a limit to prescribing companies how the composition of their staff should be in view of the inflexibility such prescriptions create. Self-regulation, on the other hand, implies little engagement<sup>8</sup>. The measures mentioned under 4) seem to be interesting. However, high deadweight costs are a concern<sup>9</sup>. Finally, we do not know of any evaluations concerning alternative 3.

From a theoretical point of view then, we could probably say that there is a role to play for active labour market policy. Table 1 summarizes the previous discussion. For a proper judgment we would need of course information about the costs and the effects of the various measures too.

### **3 PATTERNS IN THE USE OF VARIOUS TYPES OF ACTIVE MEASURES**

We used the OECD database with data on ALMP expenditure<sup>10</sup> to analyze whether any trends can be observed in the use of the various instruments. The breakdown according to types of measures used by the OECD is a bit different from the one defined in section one. We have re-arranged the OECD data into the following categories:

- the public employment service;
- training;
- subsidies for regular jobs;
- direct job creation;

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<sup>8</sup> In the Netherlands several examples can be mentioned of agreements between the government and the business sector, particularly for employing more ethnic minorities. The net effects seem to be small (see Zandvliet et al, 2004).

<sup>9</sup> In the Netherlands several years ago a measure was introduced reducing social premiums on low-paid labour. This measure led to a 10 per cent decrease in wage costs for low paid labour, which resulted in an employment effect of approximately 1 per cent (see Polanen Petel, et al, 1999). In view of the high deadweight and the low unemployment rate during the late 1990s and the start of the new century, the measure was abandoned.

<sup>10</sup> The OECD database also contains data on participant inflows. However, no such data exists for public employment services. One could define the participants in case of public employment services as the number of registered clients or the number of registered using public employment services. The Dutch employment service, for example, carries out surveys among jobseekers from which one can derive which percentage of the registered clients actually use the services. But we do not have such data for other countries.

- measures for the disabled;
- other measures.

The activities of public employment services include job mediation but in many cases also job counselling, job search monitoring and perhaps also other services. Training includes 'training for the unemployed and those at risk' as well as subsidies for youth training (including subsidies for apprenticeship training). This means that expenditure on training partly applies to training of employed workers. Subsidies for regular jobs also include support for unemployed individuals starting their own business.

*Table 2 Average percentage shares of different types of active labour market measures for 18<sup>a)</sup> OECD countries (1990-2003<sup>b)</sup>*

	Public employment service	Training	Subsidies for regular employment	Direct job creation	Measures for the disabled	Other	Total
1991	20	31	9	11	18	10	100
1992	21	31	9	12	16	10	100
1993	22	31	10	12	16	10	100
1994	22	32	10	13	16	8	100
1995	21	32	11	13	16	8	100
1996	23	31	10	13	15	7	100
1997	24	31	10	13	15	7	100
1998	24	29	11	13	15	7	100
1999	24	28	11	12	16	9	100
2000	24	27	12	11	17	9	100
2001	26	27	12	10	18	8	100
2002	27	27	12	9	17	8	100
2003	28	24	14	9	18	7	100

a) Greece, Luxembourg and Italy not included owing to lack of data

b) For 2002 and 2003 the figures for training and 'other' are estimates

Source: OECD Employment Outlook, various years

To a considerable degree measures for the disabled consist of wage subsidies. However, we lack the data to break down expenditure on measures for the disabled to the other categories. Also the category 'other' measures may contain measures that belong to the earlier mentioned categories.

Recently, the OECD has changed the classification in its ALMP database. In order to construct a time series, we had to use the old classification. The 2002 and 2003 data that follow the new classification were re-arranged as to fit the pre-2002 data as good as possible. The results are given in table 2. The table gives the average shares in expenditure for the different types of measures for 18 OECD countries (12 'old' EU countries (Greece, Luxembourg and Italy are not included), plus Australia, Japan, New-Zealand, Norway, Switzerland and The United States). The figures are un-weighted averages for this group of countries and concern the period from 1991 to 2003<sup>11</sup>.

From table 2 we observe that the share of public employment services (mediation, counselling) is increasing, from 20 per cent in 1991 to 28 per cent in 2003, while the share of training is declining from 31 to 24 per cent over the same period. We also see an increasing share of subsidies for regular jobs from 9 per cent in 1991 to 15 per cent in 2003. The share of direct job creation initially increased but has recently fallen to a level somewhat lower than the 1991 figure. Finally, the share of measures for the disabled has remained relatively stable throughout the 1991-2003 period. Given the fact that wage subsidies form a considerable share of measures for the disabled, together wage subsidy measures make up approximately 40 per cent of total ALMP expenditure. This figure has remained relatively stable between 1991 and 2003.

In addition to the quantitative changes also qualitative changes have occurred. This is clearly the case in public employment services. Owing to the developments in ICT self-service instruments for jobseekers and employers have become more important. Such self-service instruments include search engines allowing jobseekers to find vacancies that fit their competencies and employers to find workers that fit their job requirements without interference of counsellors.

Table 2 indicates that in recent years direct job creation has lost ground. Within the framework of the so-called 'work first' approach it tends to become more popular again. However, the focus is quite different from the older job creation programmes. In the 'work first' philosophy subsidized work is foremost a disciplinary measure. It implies that the unemployed have to do simple work, which is often below their skills level, to 'earn' their benefit. Often the work is not full-time to offer the person the opportunity to look for a real job. The unattractiveness of the work and the low pay are supposed to provide sufficient incentive to look for a regular job. In that sense this type of subsidized work is

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<sup>11</sup> For the first year and the last years there are missing observations for some countries. If, for example, for 2003 data is only available for a subgroup of countries than the averages for this subgroup are computed for 2002 and 2003. Consequently, the differences are added to the 2002 figures for the whole group.

more in spirit with benefit sanctions and job search monitoring than with traditional job creation programmes.

There also seems to be more emphasis on sanctions. In some countries such as the UK and Switzerland sanctions seem to play quite an important role in active labour market policy. In other countries such as Germany and The Netherlands the growing interest in sanctions becomes visible in the fact that the government commissions studies into this topic<sup>12</sup>.

According to table 2 the average share of training in ALMP expenditure for the Western OECD countries has diminished. However, these averages disguise considerable variation among the countries. The increasing tendency is apparent in all Anglo-Saxon countries (Australia, Canada, New Zealand and the United Kingdom), and furthermore in France, Germany, Japan, New Zealand, Norway and Sweden. Four countries (Belgium, The Netherlands, Portugal and Spain) do not show a clear trend in the share of training in ALMP expenditure. In the four remaining countries (Austria, Denmark, Finland and Switzerland) training has become more important. For Austria the increase is relatively small, but particularly for Finland and Switzerland it is considerable. Denmark shows an increasing trend in the share of training in ALMP expenditure, but the most recent figure is much lower. However, that might be partly due to the change in the OECD classification system.

Why do some countries attach more priority to training in active labour market policy than others? One could argue that labour market institutions play a role. In countries with higher social benefits and minimum wages, unemployed individuals will need a higher productivity to be employable than in countries with lower benefits and lower minimum wages. That might explain why a country such as Denmark emphasizes the role of training so much. However, this argument also seems to apply to some of the countries in which the role of training has diminished.

The shift away from training in Australia may be partly due to the system change according to which implementation of active measures became largely outsourced to private providers that have to compete for the contracts (see Grubb (2003)). As training is relatively expensive but often does have a visibly stronger effect on short-term placement results than other instruments of active labour market policy, price competition induces the providers to reduce the use of expensive measures such as training. Since 2002 The Netherlands followed the example of Australia and outsourced a considerable part of the service delivery in

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<sup>12</sup> See for Germany: Müller and Oschiansky (2005). In the Netherlands a study is in the process of being carried out.

active labour market policy to private providers. There are indications that the same phenomenon is occurring as in Australia (De Koning et al, 2004). However, in the OECD figures for The Netherlands such a development is not (yet) visible.

It must be said again that for some countries the figures also contain training for employed workers. Therefore, in some cases trends in the use of training could reflect trends in training for the employed. Finally the relatively poor results produced by evaluations of training measures (see the next section) may have induced the government in some countries to limit the use of training. But apparently, countries differ in their views on the returns to training for the unemployed. In the next section we go more deeply into the results of the international evaluation literature.

## **4 A REVIEW OF THE INTERNATIONAL LITERATURE<sup>13</sup>**

In this section we review a large number of international evaluation studies to find out what the evidence is concerning the effectiveness of the various ALMP instruments. We concentrate on the net effect of ALMP's on job entry rates as much studies concentrate on this effect. However we will also look at other aspects.

In total 130 evaluation studies were collected. Most of them were taken from earlier review studies (Heckman et al, 1999, Calmfors et al, 2002 and Hujer and Caliendo, 2000). Since, some of these studies deal with more than one measure or estimate the net impact on job entry chances for different groups, the number of cases is 161. Slightly more than half of the cases (85) refer to training. For job creation 24 studies have been found, followed by 22 for counselling and 17 for incentive measures for jobseekers. The remaining number of cases (13) is about placement and wage subsidies to employers for regular jobs.

Only in one-fifth of the cases an experiment has been used to estimate the net impact on job entry chances. In those cases a sample of participants is compared with a control group that has not been treated. When the people selected for participation in the experiment have been taken randomly from the target group and when they are assigned randomly to the treatment group and the controls, the difference in job placement rates between the two groups can be solely attributed to the measure. Although real-life experiment will not completely fulfil the conditions for an ideal experiment (Heckman and Smith, 1996), there is general agreement that experiments are the most reliable method for measuring impacts.

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<sup>13</sup> To a considerable part based on De Koning et al (2005).

In the other 80 per cent of the cases non-experimental methods have been used. Three main approaches can be distinguished:

1. Comparing the situation of the treated after the treatment with the situation before the treatment (see, for example, Ridder, 1986). This method makes it necessary to follow people over a relatively long period before and after treatment. Such data is often not available. Furthermore, when using this method, one has to account for the influence of time-variant factors affecting job entry chances such as the business cycle, institutional changes and changes in personal circumstances.
2. Comparing the job entry chances of the treated with a control group taken from those that have not participated. It is, of course, essential to control for differences between the participants and the controls. One way of doing this is by selecting for each participant a look-a-like non-participant. This is the matching method. The other possibility is to control for differences ex post by using an econometric model: the so-called timing of events method. However, in both cases the outcomes may be biased because of the fact that the control group was not formed on the basis of random assignment. We can never be sure that all relevant factors have been taken into account. Psychological factors, for example, are often not included in the analysis simply because no information on them is available. Suppose that more motivated people are more likely to participate in the measure and that motivation is also a factor affecting job placement directly. If we would then find that participants have higher job placement chances than non-participants, this might not be due to the measure, but simply to the fact that participants tend to be more motivated persons. For the type of model used for analyzing the process of job entry, it is not easy to correct for this selectivity bias. Only recently methods have been developed that deal with this problem in a more satisfactory way (Abbring and Van den Berg, 2003). Therefore, more recent non-experimental studies using more advanced methods might be more reliable.
3. A combination of 1) and 2). From a methodological point of view this seems to be optimal. But, as already have been indicated, the problem is that one would need data covering quite long periods before and after the treatment, data that is often not available.

*Table 3 Distribution of evaluation studies according to the net impact found on job entry chances, divided by type of measure and evaluation method*

	Experiments	Non-experimental studies	Total
<b><i>Incentive for jobseekers</i></b>			
Total number of studies found, of which	13	4	17 (100 %)
Significant positive effect on job entry chance	11	3	14 (82 %)
Significant positive effect but results are not robust	1	-	1 (6 %)
Effect on job entry chance not significant or negatively significant	1	1	2 (12 %)
<b><i>Counselling</i></b>			
Total number of studies found, of which	13	9	22 (100 %)
Significant positive effect on job entry chance	11	3	14 (64 %)
Significant positive effect but results are not robust	-	2	2 (9 %)
Effect on job entry chance not significant or negatively significant	2	4	6 (27 %)
<b><i>Training</i></b>			
Total number of studies found, of which	6	79	85 (100 %)
Significant positive effect on job entry chance	4	32	36 (42 %)
Significant positive effect but results are not robust	1	16	17 (20 %)
Effect on job entry chance not significant or negatively significant	1	31	32 (38 %)

	Experiments	Non-experimental studies	Total
<b><i>Placement and wage subsidies for regular jobs</i></b>			
Total number of studies found, of which	-	13	13 (100 %)
Significant positive effect on job entry chance	-	8	8 (62 %)
Significant positive effect but results are not robust	-	3	3 (23 %)
Effect on job entry chance not significant or negatively significant	-	2	2 (15 %)
<b><i>Job creation</i></b>			
Total number of studies found, of which	-	24	24 (100 %)
Significant positive effect on job entry chance	-	8	8 (33 %)
Significant positive effect but results are not robust	-	2	2 (8 %)
Effect on job entry chance not significant or negatively significant	-	14	14 (58 %)
<b><i>Total instruments</i></b>			
Total number of studies found, of which	32	129	161 (100 %)
Significant positive effect on job entry chance	26	54	80 (50 %)
Significant positive effect but results are not robust	2	23	25 (16 %)
Effect on job entry chance not significant or negatively significant	4	52	56 (35 %)

Source: De Koning et al (2005)

From table 3 we can infer that if we take all measures together, a significantly positive effect on job entry chances is found in half of the cases. In approximately one-third of the cases the impacts found are not significant or even significantly negative. However, the cases in which measure seem to be clearly counterproductive are relatively rare. In the remaining (16 per cent of the) cases the results are sometimes significantly positive, but they are not robust, depending for example of the estimation method applied. Therefore the outcomes are diverse, but there is more evidence for a positive than for no or an adverse effect.

Different studies use different indicators to measure the impact on. Furthermore, many studies give no information on what the results imply for the difference in job entry chances between treatment and no treatment. Therefore, it is difficult to say much about the size of the impact. The mean estimates will probably range between 5 to 10 percent points.

It is interesting to observe that experimental studies, which are more reliable, tend to have more positive results (more than 80 per cent positive). However, with only a few exceptions experiments have been primarily used for incentive instruments for job seekers and for counselling. And the results for the latter instruments are quite positive in general.

The results differ considerably between the various types of measures. For incentives for jobseekers (job search monitoring, sanctions and bonuses) the evidence overwhelmingly points to a positive effect on job entry chances. The same is true, although to a slightly lesser degree, for counselling and placement and wage subsidies for regular jobs. The picture is less positive for training: the number of training studies pointing at positive effects is more or less the same as the number of studies showing insignificant or significant negative effects. Job creation measures show the worst results with a majority of the studies pointing at insignificant or adverse effects.

Some types of ALMPs can be seen as disciplinary measures. The very threat of being subjected to a measure may even speed up the jobfinding process. There is evidence (Lalive, Van Ours and Zweimüller, 2002) that benefit sanctions for inactive job search behaviour do not only increase the job chances of those subjected to the sanction, but also the job chances of other unemployed jobseekers. Clearly, the latter want to avoid being sanctioned. For other measures, such as being subjected to job search monitoring, also demonstration effects have been found (see Rosholm and Soarer (2004) for Denmark and Klepinger et al (1997) and Black et al (2002) for the United States).

The negative results for training need further discussion. Most training studies concern the young and on the basis of the outcomes we can conclude that youth

training is not effective. However, things might be different for adult unemployed. The number of international studies containing separate results for adult unemployed is too small to derive conclusions for older age categories. In a number of Dutch training studies the net effects are given for different age categories. The results, which are given in table 4, suggest that training might be effective for older unemployed.

The results discussed so far refer to the impact of training on the length of the unemployment spell in which the training took place. One might argue that the negative effects for training are due to the fact that training often takes a lot of time. It is logical then, that training does not have a shortening effect on the unemployment spell in which the training takes place. However, training may reduce the chance of future unemployment. Therefore, in the case of training one should look at the long-term effects. However, the relatively few studies that measure long-term effects of training, do not point at more favourable long-term effects. In fact, most studies dealing with long-term effects find that the effects get smaller over time (De Koning, Koss and Verkaik, 1988, Hujer, Maurer and Wellner, 1999, Fitzenberger and Prey, 2000, Lechner, 2000), while only one (Larsson, 2000) finds that the long-term effects are larger than the short-term effects.

*Table 4 Survey of Dutch studies with results for older unemployed*

Authors (year of publication)	Training measure	Method	Outcomes
De Koning and Van Nes (1989)	General subsidy scheme for training unemployed	Perceptions of participants	Positive impact on job entry chance. Impact is bigger than average for older unemployed (>40 years of age)
De Koning en Van Nes (1990)	Centre for professional orientation and training	Control group through matching; OLS with job entry chance as dependent variable No correction for selection bias	Positive impact on job entry chance. Impact is bigger than average for older unemployed (>40 years of age)
Zandvliet et al (1995)	General subsidy scheme for training unemployed (KRS)  Centre for professional orientation and training (CBB)	Logit-analysis with job entry chance as dependent variable No correction for selection bias	On average no net impact for CBB; considerable positive net impact for KRS. In both cases net impact considerably bigger for older unemployed
Gravesteijn et al (1995)	Training projects within ESF-programme	Control group through matching No correction for selection-bias	Only positive effect on job entry chance for unemployed older than 35 years of age
Olieman et al (1998) and De Koning (1999)	Training projects within ESF-programme	Control group through matching OLS No correction for selection bias	On average negative impact of training on job entry chance in case of direct comparison with control group. After correction for observed heterogeneity small significant positive effect. Net effect for older unemployed (>40 years of age) is higher than average. One and a half year after training completion effect is still intact
CPB (2000)	No information on type of training	Timing of events method Correction for selection-bias	On average impact not significant. For older unemployed (>45 years of age) positive and significant net effect
Heyma et al (2003)	No information on type of training	Timing of events method No correction for selection-bias	On average significant positive. Effect is higher than average for older unemployed

The disappointing effects of training for young unemployed may be due to the fact that the young people involved often did not finish school and are not motivated to go to school again. Practical forms of training resulting in an approved qualification might be more effective than theoretical class-room teaching. However, there is not enough information available to draw conclusions about the relationship between training form and content on the one hand and training impact on the other hand. In most evaluations training is seen as a black-box (Friedberger et al, 1997).

It is important to note that most evaluations of job creation schemes focus on the net effect on the chance that an unemployed person finds a regular job. In many cases this net effect is even negative, which is caused by the lock-in effect. Many participants in job creation schemes tend to stay in their subsidized job with little ambition to move to a regular job. However, this is not the only criterion to judge job creation schemes on. Job creation schemes often target the most vulnerable groups in the labour market that tend to have little chance to get a regular job. Placement in a job creation schemes often implies a shortening of the unemployment spell. This ambiguous result of job creation comes out clearly in a recent study into a Bulgarian job creation scheme. Both the negative effect on unemployment duration (which should be valued positively) and the negative effect on the job entry chance in a regular job (which should be valued negatively) are highly significant (De Koning, Kotzewa, and Tzvetkov, 2005). Also the output produced by participants in job creation schemes should be valued positively, provided that there is no displacement and no crowding-out. Therefore, the case for job creation is perhaps stronger than one might conclude from table 4. Still, the lock-in effect is a real danger even in case of the most disadvantaged groups. It might be better to try and place people in regular jobs even if it implies a permanent subsidy for the employer<sup>14</sup>.

On the basis of the available information not much can be said about the effectiveness of ALMPs for different groups. We earlier indicated that training comes out negatively for young people and probably positively for older unemployed. The results also indicate that the results are probably better for women than for men. Our impression is that disadvantaged groups tend to benefit more from ALMPs than those with a higher profile in the labour market.

Net effects should be set against costs. Training and job creation are the most costly measures. Given the relatively poor record of training in producing net effects on job entry chances, the shift away from training observed in the OECD

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<sup>14</sup> Job creation schemes could then still play a role as the first step in a pathway to a regular job. In that case the emphasis in job creation schemes should be on personal development. See for instance Nicaise et al (2005).

data is understandable. The same is true for job creation in its traditional form. Only few studies make a comparison between costs and benefits of ALMPs. One of the exceptions is Meyer (1992). On the basis of the results of four experiments with bonuses in case of job acceptance, he concludes that the benefits of the bonuses outweigh the costs (including the implementation costs). However, this should be seen as an example, which is not necessarily representative for other measures. In general, we know little about the cost-benefit ratio of ALMPs.

Earlier we saw that almost one-fifth of ALMP expenditure goes to measure for the disabled. However, De Koning et al (1995) find remarkably few studies dealing with the impact of measures for this group on the disabled. The study by Heyma et al (2003) that was included in table 4 is one of the few exceptions.

So far, we discussed the impacts of ALMPs on the job entry chance of (individual) participants. However, positive effects on the individual level do not guarantee positive effects on the aggregate level. Displacement and crowding-out effects were already mentioned. Surveys among participants and firms suggest that in case of wage subsidy measures and job creation schemes these effects can be considerable. However, these are short-term effects. If ALMPs improve the employability of its participants the mid-term and long-term employment effects can still be positive. Positive effects of ALMPs on the size and the quality of the labour force are likely to enhance the level of aggregate employment (see for example De Koning, Layard, Nickell and Westergard-Nielsen, 2004).

There are basically two ways to measure the aggregate impact of ALMPs<sup>15</sup>. One method is to use a general equilibrium model of the economy to simulate the effects of active measures (taking, of course, also account of the financing of these measures). An example of this approach is study by Jongen, Van Gasteren and Graafland (2002). The second method is a cross-regional or cross-national aggregate impact analysis. If we can assume that cross-border effects are small, such analyses may give an accurate picture of the effects. Aggregate impact analyses are more sensitive for flawed data and model specification than micro impact studies. However, it is interesting to observe that the overall conclusion coming out of the aggregate impact literature is not too different from the outcomes of the micro evaluation literature (De Koning, 2001). Also aggregate impact studies show a mixed picture with perhaps a slight tendency towards positive employment effects of active labour market policy as a whole.

The core activities of public employment services have hardly been the subject of evaluation as far as we know (although these activities may be partly reflected in studies about counselling services and incentives for jobseekers). The recent

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<sup>15</sup> A third method might be time series analysis.

reform of Dutch ALMP offered the possibility to (more or less) isolate the effect of the information products and mediation services provided by the employment offices. Under the new system the public employment service mostly offers services to clients that are unemployed shorter than six months. Those longer in unemployment are sent to the organizations responsible for social benefits. From that moment on the latter become responsible for reintegration. Not the public employment offices but private agencies are then contracted to carry out the reintegration.

By pooling short time series for the 127 employment offices Van Donk and De Koning (2005) analyze to what extent the outflow chance from short-term unemployment depends on the number of clients per staff member dealing with job placement and counselling. In the analysis other factors such as the situation on the regional labour market and the composition of the pool of short-term unemployed in the region are controlled for. The results point to a positive effect of the staff-client ratio on the outflow chance<sup>16</sup>.

So far, we concentrated on the employment effects of active labour market policies. Some of the studies that we used for our literature review also estimate the impact of ALMPs on the participants' wages. This impact tends to be smaller than the impact on employment. Hardly anything is known about the non-market effects of ALMPs. By non-market effects we understand, for example, the effects on health and social participation. Nicaise et al (2005) is one of the few examples. It suggests that these effects should not be neglected. Particularly for training and job creation the outcomes might be more favourable if such effects are taken into account.

## **5 CONCLUSIONS**

There is a case for active labour market policies on the basis of theoretical reasoning. Both market failure and unintended effects of social protection lead to problems such as (long-term) unemployment and friction and mismatch between labour demand and labour supply. The private employment services market is not capable of redressing these problems sufficiently. Public employment services and other active measures may a) reduce information shortages, the productivity trap, the unemployment trap and underinvestment in training, b) increase the incentives for jobseekers to accept jobs and for employers to hire workers from

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<sup>16</sup> The results are consistent with the results of an earlier study by Arents and De Koning (2001) in which ALMP expenditure excluding expenditure on training, wage subsidies and job creation was used as a proxy for the efforts of employment offices in the field of information, counselling and job mediation.

the pool of (long-term) unemployed fight and c) create jobs for those who are either temporarily or structurally not employable in the (regular) labour market.

This does not necessarily imply, of course, that ALMPs work in practice. It is still possible that ALMPs lead to crowding out of private employment services. Furthermore, governments may not be able to organize ALMPs in such a way that the latter are effective and efficient. There is also no guarantee that the effects are large enough to outweigh the costs. However, there are no obvious alternatives to active labour market policy. Alternative measures for ALMPs exist, but their effectiveness can be questioned even more. Therefore, in stead of or in addition to implementing alternative policies, one should look for ways to improve active labour market policies. One way, which was already mentioned in the introduction, is to make the delivery system more efficient. In this paper we have concentrated on the possibility of a shift in the use of measures from less effective to more effective ones.

There is considerable diversity among the active measures that are applied in practice. Both design features and implementation strategies differ widely. Statistical data is only available for broad categories of measures. According to OECD data on ALMP expenditure there seems to be a shift away from training and (more recently) job creation, and a shift towards the use of public employment services (mediation, counselling, information) and placement subsidies for regular jobs. In addition to this we also see a number of qualitative changes such as the increasing use of ICT and self-service in public employment services and an increasing emphasis on disciplinary measures.

Do active labour market policies work in practice? And are the observed changes in the use of the various measures in accordance with what is most effective? A review of the international evaluation literature indicates that some ALMPs may work. For the category of measures consisting of job search monitoring, sanctions and bonuses the evidence for positive effects on job entry chances is strongest. However, also for job counselling and placement and wage subsidies for regular jobs we see that most studies point to positive effects and only few to in significant or counter-productive effects. The picture for training is mixed. Closer examination reveals that training produces negative results for young people mainly; for adult unemployed and particularly older unemployed the results may be positive. For job creation measures the results are predominantly negative. Therefore, we conclude that the shifts observed in the shares of the various measures in ALMP expenditure seem to be in line with the outcomes from the international evaluation literature.

For future research two things seem to be most important. Firstly, it would be important to distract indications for the size of the effects from the literature. And secondly, more information on the costs of the various measures is badly needed.

Then it would be possible to compare the costs and benefits for the various measures. Only then reasonable policy recommendations could be made.

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