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Valtion taloudellinen tutkimuskeskus
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Abstract:

This study focuses on the threat effect of the activation reform of the Finnish labour market support system in 2006. In practice, participation in the labour market programmes became mandatory for the long-term recipients of the labour market support. Mandatory programme participation may provide incentive for some individuals to look for work in order to avoid the training programmes. The study examines whether the activation reform of 2006 encouraged individuals in the target group to look for employment. According to the results mandatory programme participation has no effect on the probability to find a job or to leave labour market support for some other reason. Conversely, the long-term recipients' participation in the labour market programmes has increased considerably due to the activation reform.

Key words: labour market support, activation, unobserved heterogeneity

JEL classes: J640

Tiivistelmä:

Tässä tutkimuksessa arvioidaan vuonna 2006 toimeenpannun työmarkkinatuen aktivointiuudistuksen vaikutuksia. Käytännössä uudistus tarkoitti yli 500 päivää passiivista työmarkkinatukea saaneiden työttömien tehostettua ohjaamista aktiivisille työvoimapoliittisille toimenpiteille. Mielenkiinnon kohteena on erityisesti aktivointiuudistuksen mahdollinen uhkavaikutus. Uhkavaikutuksella tarkoitetaan tässä yhteydessä tilannetta, jossa passiivisen työmarkkinatuen saajat pyrkivät työllistymään avoimille työmarkkinoille tai muutoin poistumaan passiiviturvan piiristä ennen työvoimapoliittisiin toimenpiteisiin ohjaamista. Tulosten mukaan lisääntyneellä aktivoinnin uhalla ei ollut tilastollisesti merkitsevää vaikutusta avoimille työmarkkinoille työllistymiseen tai muuhun poistumaan passiivisen työmarkkinatuen piiristä. Sen sijaan työvoimapoliittisille toimenpiteille siirtymisen todennäköisyys kasvoi selvästi aktivointikaudella.

Asiasanat: työmarkkinatukiuudistus, aktivointi, havaitsematon heterogeenisuus

JEL-luokat: J640

Contents

1. Introduction

The Finnish labour market support system was reformed in 2006. The major aim of the reform was to create more incentives for the long-term unemployed to return to work. Thus, participation in the labour market programmes became mandatory for labour market support recipients whose passive labour market support spell exceeded 500 days. The period after 500 passive support days is denoted the "new activation period". In practice individuals belonging to the target group were guided more efficiently to participate in the active labour market programmes. In order to achieve this goal, the reform included refusal of labour market support benefits for those who refused to participate in the active labour market programmes during the new activation period. Additionally, the local municipalities were given financial incentives to allocate long-term unemployed individuals into active labour market programmes.

The activation of labour market support recipients may have twofold effects. Firstly, the activation may in general promote employment prospects of labour market support recipients. The increase in activation (or participation) rate may improve individuals' qualifications and help them back to work. There is a wide literature on the employment effects of the active programmes, while there is no consensus on the effects. The effects depend at least on the type of the programme and target group of the programme. Secondly, increased mandatory activation may provide incentive for some individuals to look for work in order to avoid training programmes. This effect is known as the "threat effect". The focus of this study is in the threat effects of the activation reform instead of the effects of different labour market programmes.

The Finnish reform of 2006 can be seen as a part of the worldwide development from welfare to "workfare". The concept of "workfare" goes back to 1980s when US government paid increasing attention to the misuse of benefits. Since then there has been tendency towards workfare in many countries including United Kingdom, Netherlands and Denmark. In practice the concept of workfare means that requirements for welfare schemes are made more restrictive and means tested.

For example, In USA the TANF program (Temporary Assistance for Needy Families) replaced the ADF program (Aid to Families with Dependent Children) in 1996.[1] As a consequence of the TANF reform the states were obliged to offer employment or labour market programmes for the benefit recipients. At first, the states were obliged to employ 20 percent share of the target group and in 2001 the share was increased to 50 percent. Furthermore, benefit recipients were

[1] The ADF program was implemented already in the 1940s.

obliged to participate in the programmes, or otherwise authorities may reject the benefit application (or at least decrease the benefit level).

Moffitt (2008) has summarized the evaluations of TANF reform. According to the Moffitt the TANF reform as a whole increased employment and earnings and reduced poverty and the number of welfare recipients. However, the positive effects were achieved solely because of the decreased use of benefits among females. Moffitt argues that as much as 40 percent of those females who did not qualify for benefits left labour market after reform. Additionally, the reform had no significant effect on those individuals who remained on the benefit.

The nearest counterpart to the Finnish activation period of labour market support can be found from Denmark, where unemployment benefits periods are divided into two different periods. The passive period at the beginning has duration of 2 years in Denmark. During this passive period unemployed individuals generally search for employment without any further guidance. After the passive period those who have not found employment enter into activation period. During which unemployed individuals are obliged to participate in the active labour market programmes. A refusal to participate in the active labour market programmes leads to sanctions. It is possible for administration to reject unemployment benefits application or at least to cut the benefits level.

Several studies in various countries have examined the role of mandatory programme participation (Gerfin and Lechner, 2002; Black, 2003; Blundell et al. 2004; Geerdsen, 2006; Rosholm and Svarer 2007). According to the Blundell et al. (2000) the New Deal for Young People in the U.K. significantly increased transitions to employment by 5 percentage points. The New Deal for Young People included job search assistance for unemployed and employment subsidies to employers. However, it is unclear whether the positive effect was due to the "carrot" of the job search assistance or the "stick" of the stricter monitoring of job search or both of them. In contrast, Black (2003) has found that most of the positive employment effects of mandatory programme participation were due to the threat effects.

In addition, Geerdsen (2006) has found out that in Danish unemployment insurance system mandatory programme participation motivates individuals to find employment prior to participation i.e. there is threat effect. Rosholm and Svarer (2007) have also found strong and positive threat effects in Denmark. However, Rosholm and Svarer found that the threat effect is not present for the long-term unemployed individuals. This may be due to the fact the long-term unemployed individuals may need qualifications and skills that the active labour market training programmes offer. Therefore, they may expect to gain from the labour market programmes and look for to participate in them.

This paper shows that the activation reform of Finnish labour market support had no significant effect on the probability of finding employment for long-term unemployed. In other words, the study in hand examines the possible threat effect of mandatory programme participation for the long-term unemployed individuals, who have accumulated more than 500 days of passive labour market support. In order to identify the threat effect I exploit the activation reform of 2006 of Finnish labour market support system that included mandatory participation for long-term unemployed individuals. The change in legislation can be used as a natural experiment, since it provides a source of variation across individuals. Because of the reform the timing of compulsory programme participation varies between different individuals. The new activation period may start at different stages of individual labour market support spell depending on start date of the labour market support spell, accumulation of previous passive labour market support spells and distance to the implementation date of the reform (1.1.2006). Obviously, there are also spells and individuals who will not enter into new activation period at all.

The rest of the paper is organized as follows. The following section discusses on the role of the labour market support in the Finnish labour market. Section three introduces the data and the empirical analysis. Section four presents the results and discussion. Section five concludes.

2. Finnish labour market support system and the activation reform of 2006

Three types of subsidies are available to unemployed individuals in Finland. According to the Finnish legislation earnings related unemployment benefits and basic unemployment allowance are targeted to the individuals who meet specific condition regarding the employment history. Firstly, members of various unemployment compensation funds can claim earnings related unemployment benefit and it can be paid for up to 500 days. Secondly, the basic unemployment allowance can be paid for those who have been employed at least 10 months during the two years preceding the unemployment. Basic unemployment allowance is also paid for a maximum of 500 days. Thirdly, those who do not qualify for earnings related unemployment allowance or basic unemployment allowance could apply for labour market support. Labour market support is means tested and it covers unemployed job seekers who enter labour market for the first time or who otherwise have no recent work experience. In addition, those individuals who have exhausted their 500 passive day eligibility for the basic or earnings related unemployment allowance may be eligible for labour market support. Those individuals who do not qualify for labour market support are entitled to apply for social assistance.

Labour market support spells include passive and active spells. In this context passive spell refers to unemployment and active spell refers to participation in the active labour market programmes. Placement on labour market support forms the active component of the labour market support (see for example Hämäläinen and Ollikainen, 2004). It consists of practical training and coaching for work life while the labour market support is paid. Practical training is targeted to the labour market support recipients below the age of 25 without vocational degree, while coaching for work life is aimed at recipients who are 25 years of age or older (or who have vocational degree). Placement on labour market support is mostly allocated to the young people and role of the other active programmes is insignificant for the unemployed persons under 20 years of age. However, along with placement on labour market support activation may sometimes include some other labour market programmes. This is especially the case for the unemployed persons over 25 years of age. In addition, active labour market support spell may be vocational labour market training that consists of classroom and practical training that may be offered as supplementary training, continuing professional education or as joint purchase training together with an employer. It provides a formal qualification or part of a degree. Preparative labour market training is aimed at offering basic skills needed in job-seeking. It may also precede vocational training if an unemployed person needs specific skills before entering vocational training. Private sector employment subsidy is a subsidy that is paid to private employer who employs unemployed individual. Public sector em-

ployment subsidy is similar measure for public institutions. Active spells may also contain different rehabilitation measures.

When labour market support was implemented for the first time in 1994 it was sketched to be a system to support young people who became unemployed for the first time, while long-term unemployed individuals were only secondary target group. It was approximated that only quarter of recipients would be long-term unemployed. However, despite good economic times in the late 1990s and early 2000s in Finland there were 130 000 labour market support recipients in the end of the year 2005. Of them only 17% were under 25 years old. On the other hand 58% of recipients had used labour market support over 500 days.

Since the early 1990s the Finnish labour market support system has progressed to the point where it is basic security for the long-term unemployed. This development and tendency towards workfare has generated a need for reforming the labour market support system. In Finland there have been several reforms in 1990s and 2000s concerning labour market support system. These reforms have included new requirements for applicants and the preconditions for the labour market support benefits are tightened. For example, young people less than 25 years old and without vocational education are required to apply for active labour market programmes in order to qualify for labour market support benefit after the reform of 1997. The law of rehabilitative work was introduced in 2001 to improve long-term unemployed individuals' prospects for employment. According to the law of rehabilitative work local municipalities have obligation to offer rehabilitation measures for those unemployed who do not meet preconditions for other types of labour market programmes. The law of rehabilitative work included individual activation plans for young individuals less than 25 years of age and who had accumulated over 500 days of passive labour market support and who already have individual job search plan.

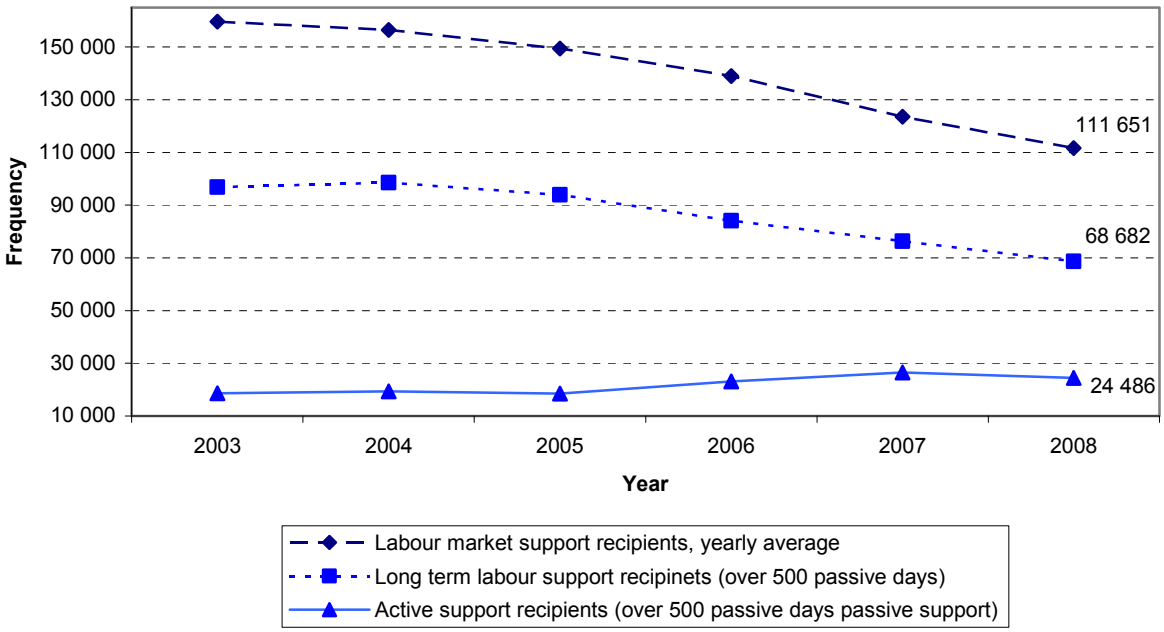
In the beginning of the 2006 labour market support was reformed once again. The reform of labour market support was aimed at long-term unemployed individuals. Labour market support recipients whose passive labour market support period exceeded 500 days were entered into the new activation period. In addition, those who have used maximum time of earning related unemployment benefits entered into the activation period already after 180 days of passive labour market support.[2] Reform included refusal of labour market support benefits from individuals who have refused to participate in the labour market programmes during the new activation period. In addition, local municipalities were offered financial incentive to guide the long-term unemployed individuals into active labour market programmes. After the reform, the Finnish government bears costs associated with labour market programmes during the new activation

[2] These individuals are not included in the analysis.

period. While before the reform, the local municipalities had to defray the costs of labour market programmes. On the other hand, costs associated with the passive support for individuals whose accumulation of passive labour market support exceeded 500 days were shared equally between government and local municipalities. Hence, more responsibility of the long-term unemployed is put to the local authorities. This can be seen as an important feature of the reform, because there were claims that before the reform local municipalities avoided their responsibility to allocate long-term unemployed into active labour market programmes. After the reform active labour market programmes are still allocated for the labour market support recipients before the new activation period. However, during the new activation period supply of services and labour market programmes is increased, which can be detected in the participation rates.

The aim of this study is to distinguish the effect of the activation reform from the trend development. In other words, the aim is to identify threat effect of mandatory programme participation introduced by activation reform. Figure 1 shows that between 2003 and 2008 total amount of passive labour market support recipients and long-term recipients of passive support has decreased while the number of active labour market programme participants increased. This development reveals that although the overall unemployment rate has decreased considerably, participation in the active labour market programmes has increased among long-term unemployed individuals after the reform. It is noteworthy that participation has increased both in absolute value and as a percentage of all support recipients i.e. participation rate has increased considerably among the individuals whose accumulation of passive support is over 500 days. It seems to be on this ground that the aim of the reform concerning programme participation is achieved. In the next chapter, I examine whether the reform has effect on the employment prospects of the labour market support recipients.

Figure 1 Labour market support recipients



Source: Employment and Economic Development Centres

3. Data and empirical analysis

3.1 Data

The data used in this study is gathered from the registers of Social Insurance Institution of Finland (KELA) and Ministry of Labour. The panel data includes detailed information on all labour market support spells commencing in 2003-2007. The resulting data contain a wide range of information on individuals' socio-economic and demographic characteristics as well as information on passive labour market support spells and labour market programmes.[3] I focus on the spells beginning in 2004-2006. There are 153949 individuals, who have a total of 298229 spells beginning in 2004-2006. However, in order to limit the number of observations estimations are performed for 20 % random sample of the data. It is possible to construct transition states for passive spells. I have divided transitions to three different categories. One state contains those who find employment in labour market and other state contains those who start in active labour market programme. Residual state contains all other exit destinations.

The data is described in table 1. Table reveals that recipients of the passive labour market support have in general long unemployment histories. The average of the passive days at beginning of the spells is over 500 days. Table 1 also shows that the average duration of the (beginning) spells is 102 days whole for whole population and 176 days for long-term unemployed. Furthermore, individuals with long unemployment history are more likely to be older males with less education. In addition, individuals who have more than 500 days of passive support are less likely to find employment from open labour market than all labour market support recipients. Instead, the long-term unemployed individuals participate more often in the active labour market programmes. Table 1 shows also that the number of passive labour market support spells has decreased steadily in the period. In other words, the unemployment rate has decreased.

[3] Passive spell is broken if there is 7 days difference between different spells.

Table 1 Descriptive statistics

All Spells	*Mean*	*Minimum*	*Maximum*	*Standard dev.*
Females, %	49.4			
Age, mean	28,4	15	65	28.4
Passive days at the beginning of the spell, mean	561.3	0	3649	711.1
Spell length, days	102.5	1	1043	133.5
Education:				
Basic education	36.5			
High school	41.9			
Secondary education	13.4			
Undergraduate education	6.4			
Graduate education	1.6			
Destination states for passive spells:				
Employed	18.6			
Labour market programme begins	33.2			
Studies	4.0			
Military service	2.0			
Employment office decision[a]	13.4			
Passive spell continues to 2008	2.2			
Other exit destination state[b]	26.6			
Number of spells:				
2004	102448			
2005	101428			
2006	94353			
Individuals	153949			
Over 500 unemployment days:	Mean	Minimum	Maximum	Standard dev.
Females, %	44.0			
Age, mean	37.5	18	65	10.8
Passive days at the beginning of the spell, mean	1376.2	500	3649	691.1
Spell length, mean	175.9	1	1521	186.6
Education				
Basic education	45.5			
High school	39.0			
Secondary education	6.0			
Undergraduate education	7.8			
Graduate education	1.7			
Destination states for passive spells:				
Employed	10.1			
Labour market programme begins	41.7			
Studies	1.1			
Military service	0.1			
Employment office decision	13.2			
Passive spell continues to 2008	5.7			
Other exit destination state	28.1			

Number of spells:	
2004	34536
2005	33557
2006	31772
Individuals	50875

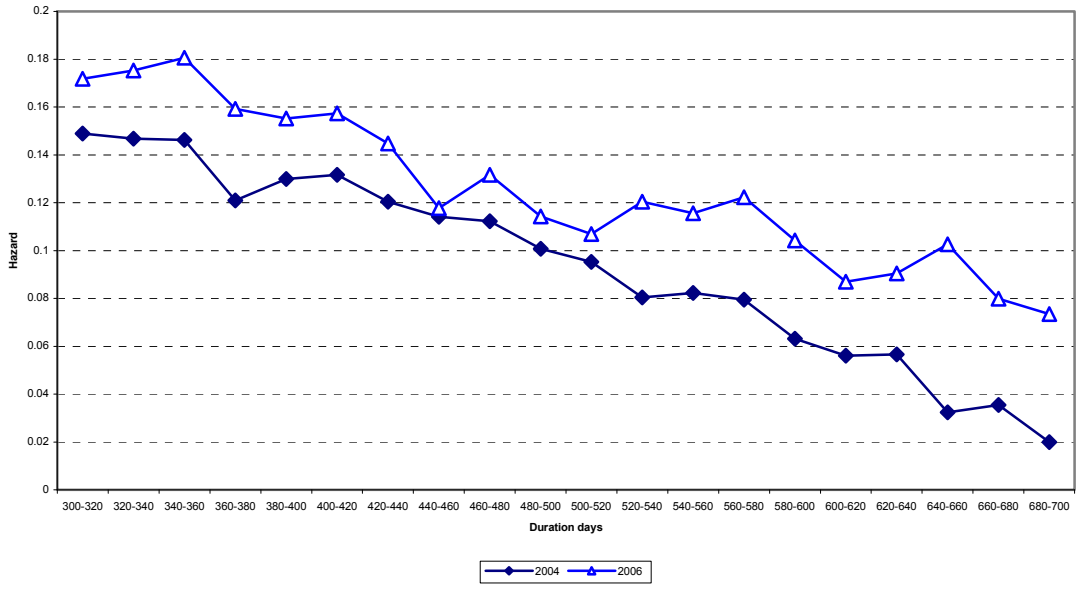
[a] Employment office decision means that for different reasons labour market support recipient does qualify for support anymore [b] Other destinations include for example moving into other benefits or actual interruption of the labour market support.

If the activation reform has a threat effect on the outcomes of the labour market support recipients, it may be possible to detect it by descriptive figures. In figure 2 the hazard of leaving passive labour market support is compared before and after reform (2004 and 2006). The hazard curves are displayed only for the spells that have already lasted at least 300 days. This is due to the fact that follow-up data ends in January 2008 and there is only 250 support days per year.[4] In addition, most of the passive labour market support spells end before duration of 500 days. Figure 2 shows that probability of leaving passive labour market support has certainly increased between 2004 and 2006. This is mostly explained by the fact that the overall unemployment rate has decreased gradually between 2004 and 2006. According to the Statistics Finland unemployment rate was 8.8 % in 2004 and 7.7 % in 2006.

Additionally, Figure 2 shows that in 2006 another upward shift is present for the probability of leaving passive support after 500 unemployment days i.e. the slope increases. This upward jump may be seen as the effect of the reform or as the threat effect. In other words, figure 2 reveals that the reform has increased exit rate from the passive labour market support. It seems to be that unemployed individuals leave passive support more likely after 500 days due to mandatory participation in labour market programmes. Hence, it is possible that some individuals try to avoid active programmes and look for employment more intensively as the activation period progresses. In addition, they may try to find some other exit out of the passive support before mandatory participation.

[4] Spells that started at 2004 are censored if ending date is greater than 31.12.2005 and spells that started at 2006 are censored if ending date is greater than 31.12.2007.

Figure 2 *Probability of leaving passive labour market support at different stages of the spell (for spells exceeding 300 days in 2004-2006 when ignoring transition state).*



Appendix 1 displays hazard rates of leaving passive labour market support for different exit destinations (employment, active labour market programmes and all other states). It seems to be that there is no difference in employment probability between years, whereas transitions into active labour market programmes and other destinations explain the upward shift in figure 2. This indicates that activation reform actually increased participation rates for the long-term unemployed. The descriptive figures also indicate that there is no sign of the threat effect for the employment hazard while there might be threat effect for the other exit hazard.

As a whole the increase in the exit rate from passive support can be regarded as a positive development. However, one has to remember that other exit destinations include various destination states. On one hand, it may be the case that labour market support is denied because support recipient has refused to participate in the labour market programmes. In this case unemployed individual can apply for the supplementary income support. On the other hand, it is possible that these individuals begin studying. Evidently, the previous situation can be considered as negative and the latter as positive development.

3.2 Empirical analysis

The reform of 2006 introduced a new concept of the activation period for the long-term unemployed individuals. On one hand, increased activation may improve individuals' qualifications and reintroduce them back to the labour market. On the other hand, there may be individuals whose motivation to look for work increases simply due to compulsory training programme participation. That is, previous studies have found that mandatory labour market programmes may in fact motivate the unemployed to look for employment or otherwise try to leave the support prior to start day of the activation programme. In this case the threat effect can also be described as the effect of the activation reform.

This study tests whether the mandatory activation increased individuals' hazard of leaving passive labour market support. The model for hazard of leaving passive labour market support is estimated in competing-risks framework for employment, active labour market programmes and all other exits. The threat effect is identified as an explanatory variable that describes individuals' remaining time until the new activation period begins. This variable counts how many months individuals have left until the new activation period begins. The threat effect is present if hazard of finding employment or otherwise leaving passive support increases when the new activation period is approaching. That is, employment probability jumps up after 500 days accumulation of passive support.

The variation in the threat effect variable comes from three sources. Firstly, the activation period was implemented 1.1.2006 and distance to the implementation date affects to the remaining time until the activation period starts. Secondly, the remaining time until the start of activation period diminishes as labour market support spell progress. Thirdly, the distance to 500 days at the beginning of the spells differs due to the previous passive spells.[5] The distance to the activation period variable is identified only if one these factors is excluded from the model. In the estimation I have omitted the distance to the implementation date based on the assumption that implementation date does not have any effect on the individuals' labour market behaviour other than through decreasing distance to the activation period.

In practice the spells in the sample can be divided into five categories. On one hand, there are two cases concerning individuals whose market support period starts during 2006 or later. Firstly, there are individuals who have already more than 500 days accumulation of passive support and activation period starts immediately. Secondly, some individuals have to wait until passive period exceeds 500 days. On the other hand, there are two cases concerning those whose labour market support spell starts before the implementation date (1.1.2006) of the reform. If the spell is still in progress in 1.1.2006 some individuals may have more

[5] Accumulation of passive labour market support days varies between 0 and 3649 days in the data.

than 500 passive days and activation period starts immediately. Of course, there are individuals who have to wait until 500 unemployment days is realized in 2006 or later. Finally, some individuals do not enter into activation period at all.

Unobserved heterogeneity is modelled as random effect using framework introduced by Heckman and Singer (1982, 1984) and the identification of mass points and their probabilities is based on assumption that each individual's unobserved part of the hazard is constant within and between spells. Suppose that destination state is employment (active programmes, other states) and all other exits are censored. There are individuals i = 1,…, N who enter each state at time t = 0 and are observed j periods, at which person either remains in the state or leaves the state. Suppose also that each individual belongs to the state v = 1,…,V, and that the membership in the each state is unobserved. The hazard function for an individual i belonging to the type v is:

$$hv_t = 1 - \exp(-\exp(m_v + b_0 + X_{it} * b)),$$

where b_0 is intercept and $X_{it} * b$ incorporates the effects of explanatory covariates including distance to the new activation period. Mass points m_v are discrete points of support of multinomial distribution and probability of belonging to each type v is p_v, while m_1 is normalized to be zero and $p_1 = 1 - \sum_{v=2}^{V} p_v$. In other words, intercept term is allowed to vary across different types. Thus, the contribution to the sample likelihood for individual with observed duration j can be written as:

$$L = \sum_v [\mathrm{p_v} * Sv(j) * (hv_j / (1 - hv_j)) \wedge C],$$

where $Sv(j)$ is a survivor function or probability of remaining in the state j periods and C in censoring indicator (one for a completed spell).[6]

The duration of the labour market support spell is also a time variant variable in the model. In addition, distance to 500 passive days at the beginning of the spell is included in the model as a time-invariant variable. Rest of the time-invariant background variables are age, gender, occupation and region. All variables except age are modelled using dummy construct. Each labour market support duration dummy variable covers 2 months' period going from 3 months to 35 months in passive unemployment. The variable for remaining passive period is modelled

[6] Maximizing log likelihood function with respect to the unknown determinants hz and p_z is carried out with Stata 10.1 and hshaz module.

with indicator variables covering 32 months period from 16 months to 12 months into activation period.

It must be noted that I estimate three different mixed proportional hazard models (MPH) (see Van den Berg, 2000). The other alternative would be multivariate mixed proportional model (MMPH), that is to say model is estimated jointly and hazard rates are dependent. However, the identification of competing risks MMPH model is more difficult than separate MPH models due to the censoring and the fact that durations to the different exit destinations are dependent.

4. Results and discussion

The odds ratios for mixed proportional hazard models are displayed in the Appendix 2.[7] The results show that females have significantly lower probability of finding employment and lower probability of entering activation programmes. Individuals with higher education level appear to have higher probability of finding employment and programme participation. Occupation has also significance on individuals' labour market transitions. Results concerning regional differences show that individuals living outside Southern-Finland have a higher probability of participating in active labour market programmes whereas probability of finding employment is usually lower. The distance to the 500 passive support days at the beginning of the spell has also significant effect on labour market transitions i.e. long term-unemployed individuals generally differ from those individuals who have short accumulation of passive labour market support benefits.

Additionally, the results indicate negative duration dependence for employment hazard. However, duration dependence is less negative than in the homogenous model and significance levels are weaker. This is due to selection process where unemployed with good unobserved characteristics leave the state of interest. Hence, composition of those who have not left the state is worse than the composition of earlier (see Van den Berg, 2000). As a consequence, exit rate is more negative if we do not take into account unobserved characteristics. In addition, the other covariate effects are somewhat different compared to the homogenous model[8]. Table A1 also shows that duration dependence is positive for labour market programme participation and other exit hazards while homogenous models produced negative duration dependences.

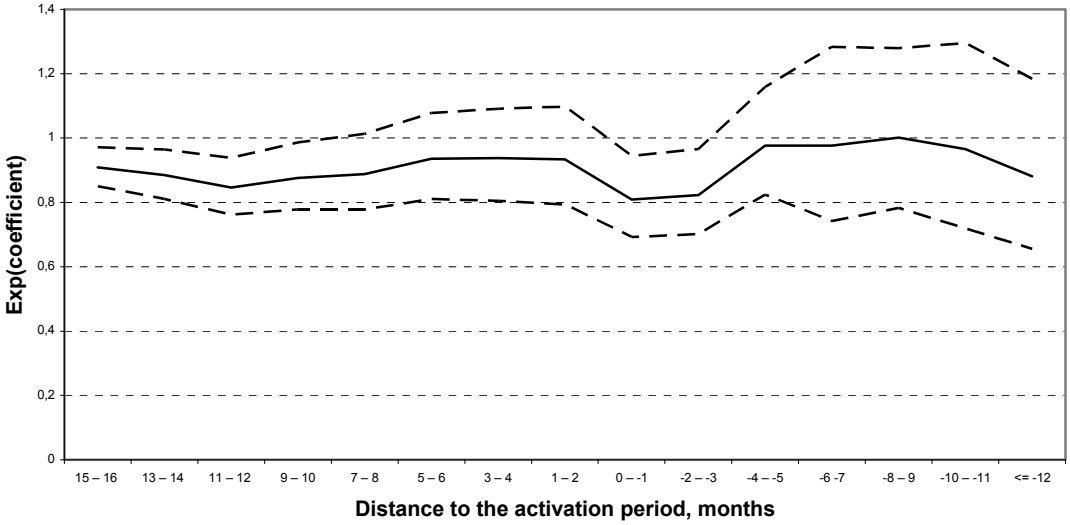
Figure 3 presents the estimated coefficients for the threat effect variable (distance to the activation period). There appears to be no threat effect present for employment hazard. All parameter values are insignificant or below one. This result is consistent with the descriptive analysis that also showed that there is no upward shift in employment probability after 500 unemployment days. In other words, it seems to be that finding employment is difficult for those individuals whose accumulation of passive support exceeds 500 days. Compared to the Denmark, this result is consistent with the finding that the threat effect was not present for long-term unemployed individuals, although, in general the threat effect was strong (see Rosholm and Svarer, 2007). It is possible that long-term

[7] The modelling of unobserved heterogeneity produced three mass points for all three models. Results indicate that labour market support recipients can be divided into three groups. Firstly, there is a small group of individuals who have strong attachment to the labour market, low usage of active labour market programmes and low incidence of all other exits, compared to the reference group. Nevertheless, majority of individuals have low attachment to the labour market, high usage of labour market programmes and low incidence of all other exits, compared to the reference group.

[8] Full results are available upon request.

unemployed individuals need skills that labour market programmes offer and finding employment is not feasible.

Figure 3 Estimated effect of activation reform on employment probability (Odds ratios)

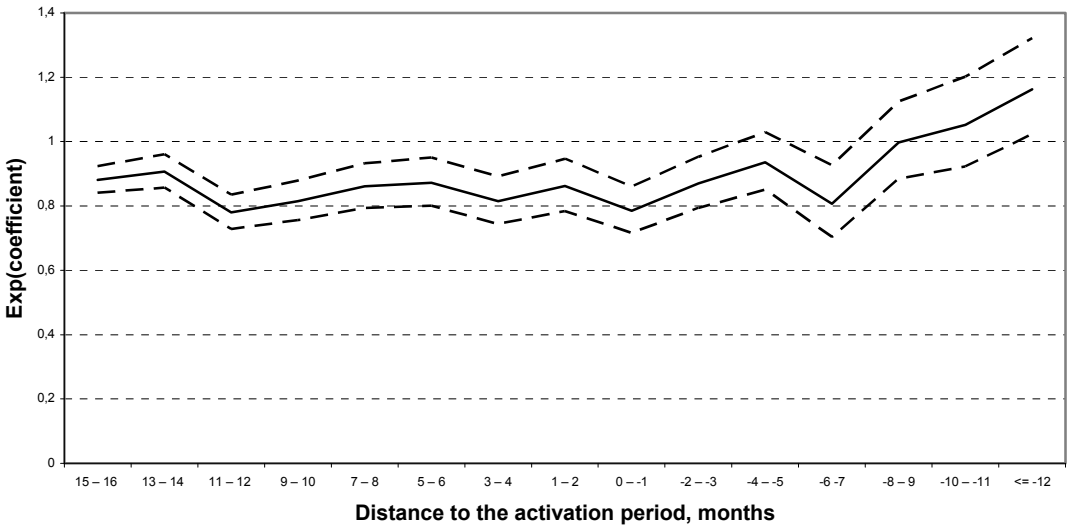


However, it is obvious that different reforms may have different effects on different types of individuals. It must be noted that activation rates are considerably lower in Finland than in Denmark. This may be reflected in the fact that threat effect is weaker in Finland. According to the Geerdsen (2006) proportion of individuals participating in the programmes reaches 80% about 10 months into the activation period. That is, proportion is close to full programme participation. In contrast, the target for overall programme participation rate has been 30% in Finland. Besides that, the unemployment benefit systems differ between countries. The study in hand focuses on Finnish labour market support, and there is no exactly similar system in Denmark. The studies in Denmark have scrutinized activation of earnings related unemployment benefits system. As a result target groups for activation reforms differ considerably. In Denmark activation is aimed at young people, whereas in Finland labour market support recipients are typically older and they might have long unemployment history behind in earnings related unemployment benefits system. Thus, it is likely that mandatory participation in the labour market programmes affect differently to older people who may have longer unemployment histories and low prospects of finding employment.

In addition, figure 4 shows that there seems to be no threat effect present for the other exit hazard, although the parameter of interest is positive and significant at the last follow-up point. This is likely to be due to the fact that follow-up data expires at the end of 2007. It is possible that the share of unknown exits increases

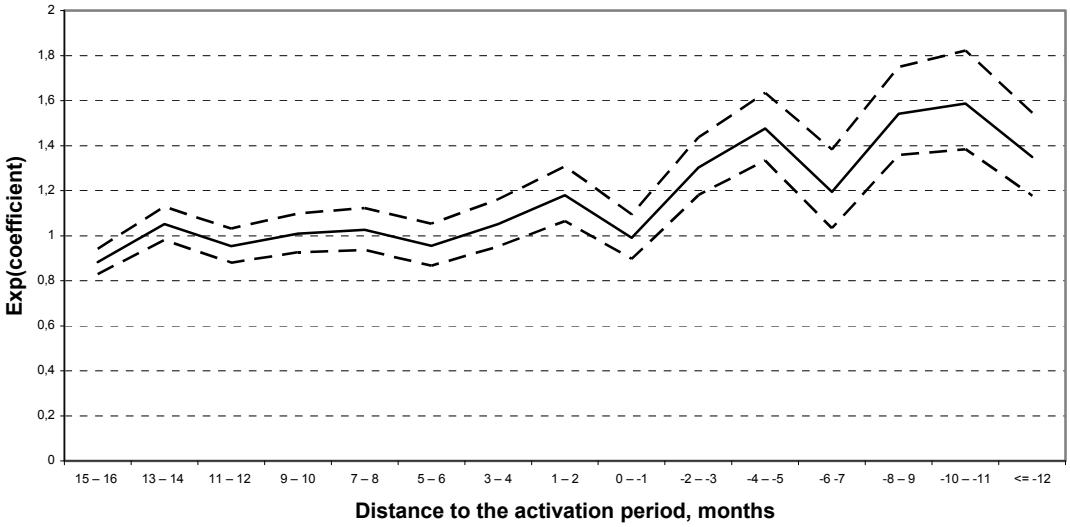
because of the practices adopted by the register administration.[9] Additionally, figure 5 illustrates that activation reform indeed increased participation to the active programmes. In other words there is an upward jump in the programme hazard after 500 unemployment days.

Figure 4 Estimated effect of activation reform on probability of other exits, excluding employment and active programmes (Odds ratios)



[9] It is possible that ongoing spells are finished at the end of the follow-up data by the register administration.

Figure 5 Estimated effect of activation reform on programme participation probability (Odds ratios)



It seems to be evident that the Finnish labour market does not offer many opportunities for long-term unemployed individuals. The long-term unemployed individuals are highly dependent on the government support policies. The reform of 2006 indeed activated long-term unemployed via labour market programmes, while the reform had no direct employment effects. Contrary to the descriptive part of the study, the reform did not increase probability of other exits from the passive labour market support. However, further research is needed to clarify the role of the other exits. It is possible that those who exit from passive support became socially excluded or otherwise they may find some other way out of the unemployment. All in all the previous option is more likely.

5. Conclusions

This study has examined the effects of the activation reform of 2006 of Finnish labour market support system. After the reform programme participation became mandatory for the long-term recipients of labour market support. In practice, after the reform individuals in the target group can be allocated more efficiently to participate in the active labour market programmes. This reform may have twofold effects. Firstly, increased participation in the labour market programmes may in general promote employment prospects of labour market support recipients. Secondly, mandatory participation may also provide incentive for some individuals to look for work prior to participating in the labour market training programmes, i.e. the threat effect is present. This study focused on the existence of the threat effect of mandatory participation.

It seems to be that mandatory participation in the training programmes does not improve job search effort or employment prospects for the long-term unemployed. According to the results mandatory labour market programme participation has no threat effect on the long-term unemployed recipients of the labour market support. The threat of compulsory programme participation has no statistically significant effect on the probability to be employed in labour market or to leave labour market support for some other reason. Conversely, the long-term unemployed recipients' participation in the labour market programmes has increased considerably due to the activation reform of 2006.

Although the threat effect was not present in this case, further research is needed to scrutinize the role of the threat effect concerning different types of policy interventions and other target groups. Some previous studies indicate that in some cases mandatory programmes can be utilized as a way to encourage individuals to look for employment more efficiently. For example, in Denmark there is evidence that although in general the threat effect can be significant and strong, the effect is not necessarily present for the long-term unemployed. In addition, the threat effect is likely to be a more relevant issue in the case of earnings related benefits system, while recipients have considerably shorter unemployment histories. It is possible that the long-term unemployed simply cannot avoid mandatory training programmes due to the fact that they have very low employment prospects and they may, on the contrary need and look for skills offered in the training programmes.

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Appendix 1

Figure A1 Employment probability for passive labour market support at different stages of the labour market support spell (for spells exceeding 300 days in 2004-2006)

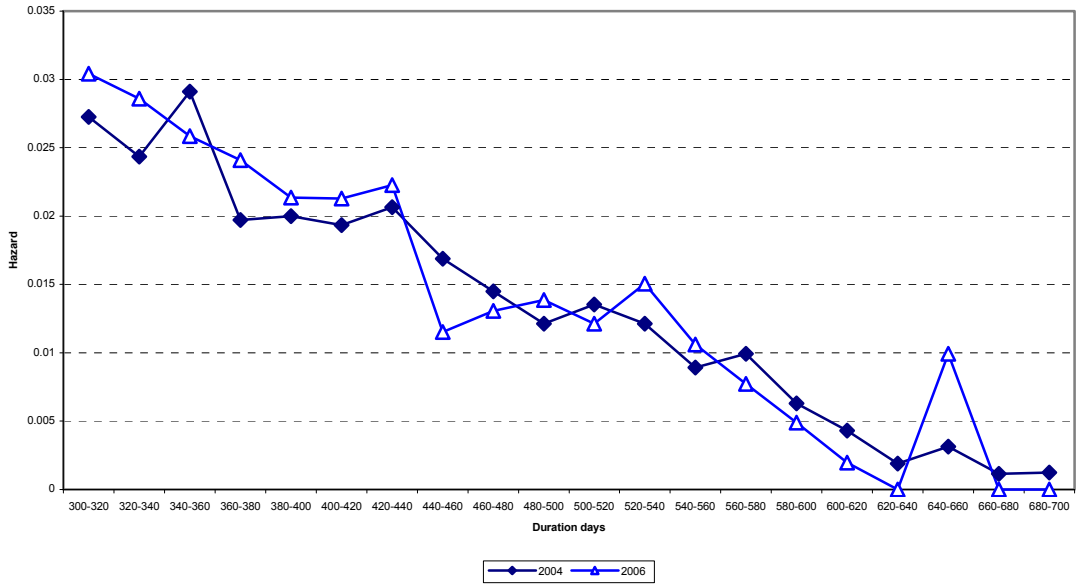

Figure A2 Probability of entering active programmes at different stages of the labour market support spell (for spells exceeding 300 days in 2004-2006)

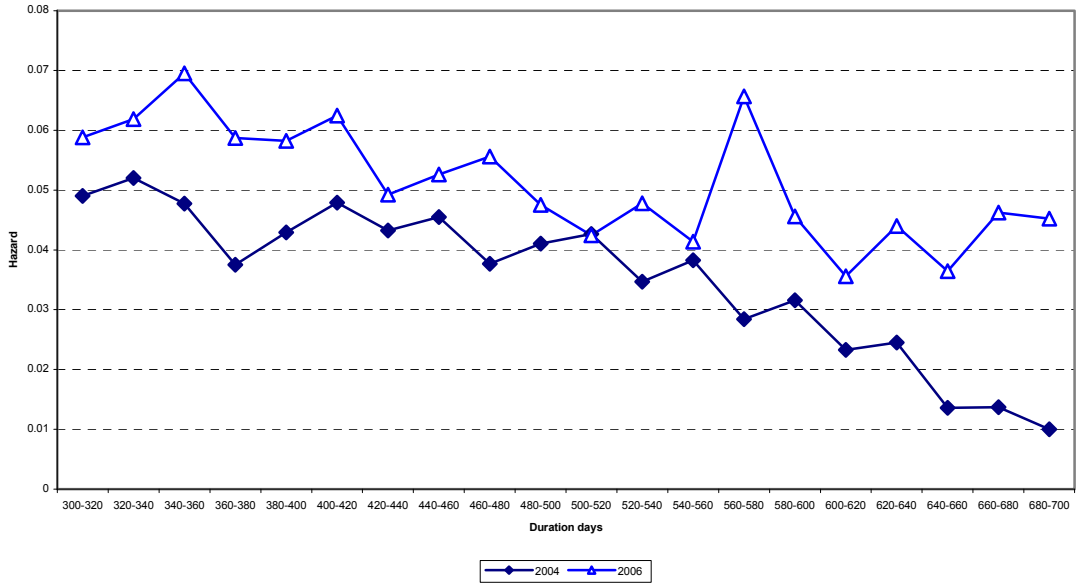

Figure A2 Probability of all other exits at different stages of the labour market support spell (for spells exceeding 300 days in 2004-2006)

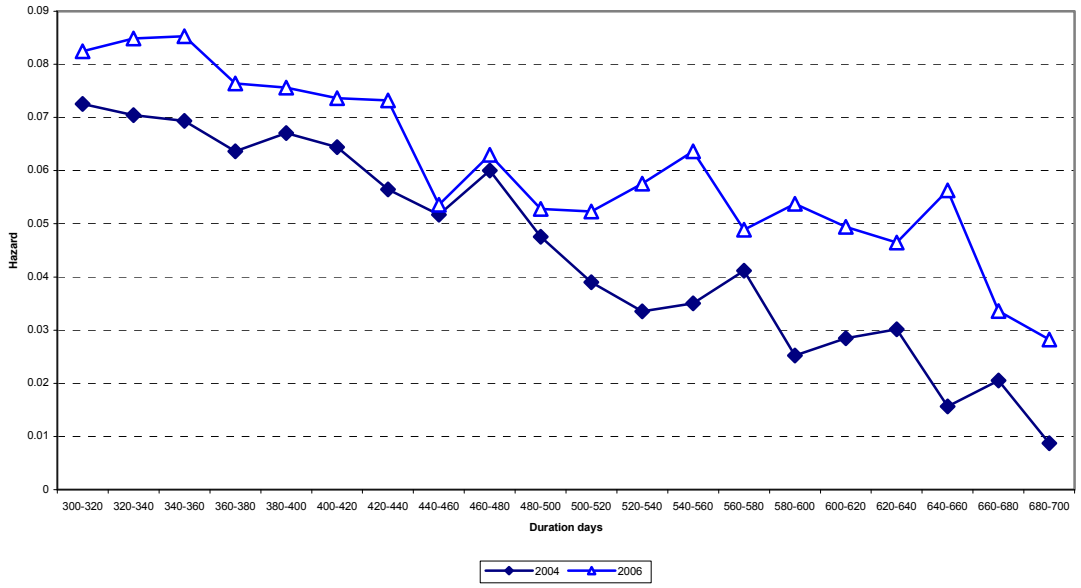

Table A1 Hazard estimates for background variables

	Into employment		Into active programmes		Into other states	
	exp (coefficient)	**s.e**	**exp (coefficient)**	**s.e**	**exp (coefficient)**	**s.e**
Age	0.976***	0.008	0.971***	0.006	0.869***	0.004
Age^2	0.999**	0.000	0.999*	0.000	1.002***	0.000
Female	0.864***	0.022	1.665***	0.035	0.935***	0.015
Occupation (reference):						
Social- and health service	2.174***	0.116	1.058	0.052	1.542***	0.058
Public administration	0.790***	0.041	1.339***	0.057	0.931**	0.033
Commerce	0.787***	0.048	1.127**	0.055	1.033	0.041
Agriculture/forestry	1.248***	0.093	1.405***	0.081	0.964	0.050
Transport	1.644***	0.148	1.103	0.090	1.278***	0.077
Manufacturing	1.099**	0.051	1.266***	0.051	1.059*	0.034
Service	0.819***	0.043	1.250***	0.053	1.080**	0.038
Unclassified	0.398***	0.020	1.287***	0.052	1.326***	0.042
Education (basic education):						
High school	1.317***	0.038	1.089***	0.024	1.032*	0.019
Secondary education	1.861***	0.071	0.920***	0.028	1.336***	0.031
Undergraduate education	1.851***	0.093	1.118***	0.044	1.218***	0.041
Graduate education	2.038***	0.183	1.031	0.083	1.288***	0.079
Province (Southern-Finland):						
Western-Finland	0.937**	0.026	1.301***	0.029	0.913***	0.016
Eastern-Finland	0.841***	0.030	1.805***	0.050	0.817***	0.019
Oulu region	0.874***	0.033	1.349***	0.041	0.868***	0.021
Lappi region	1.011	0.051	1.260***	0.052	0.844***	0.029
Distance to 500 days (over 16 months):						
14 – 16 months	0.778***	0.038	0.935*	0.036	0.759***	0.025
11 – 13 months	0.664***	0.043	0.919*	0.042	0.756***	0.031
8 – 10 months	0.597***	0.045	0.924	0.047	0.659***	0.031
5 – 7 months	0.508***	0.044	0.905*	0.051	0.643***	0.034
2 – 4 months	0.470***	0.045	0.833***	0.050	0.587***	0.034
-1 – 1months	0.446***	0.040	0.888**	0.051	0.607***	0.033
-4 – -2 months	0.381***	0.038	0.962	0.060	0.594***	0.036
-7 – -5 months	0.363***	0.039	1.111*	0.069	0.525***	0.034
-11 – -8 months	0.359***	0.037	1.010	0.061	0.556***	0.034
Over -11 months	0.219***	0.014	0.992	0.038	0.499***	0.018
Destination to activation period (over 16 months):						
15 – 16 months	0.909***	0.031	0.883***	0.029	0.881***	0.021
13 – 14 months	0.884***	0.039	1.052	0.038	0.907***	0.026
11 – 12 months	0.846***	0.045	0.953	0.039	0.780***	0.027
9 – 10 months	0.876**	0.053	1.009	0.044	0.815***	0.031
7 – 8 months	0.888*	0.060	1.026	0.047	0.861***	0.035
5 – 6 months	0.936	0.068	0.956	0.047	0.872***	0.038
3 – 4 months	0.938	0.073	1.052	0.053	0.815***	0.038
1 – 2 months	0.934	0.077	1.180***	0.061	0.862***	0.041
0 – -1 months	0.809***	0.064	0.991	0.050	0.785***	0.037
-2 – -3 months	0.823**	0.067	1.302***	0.065	0.870***	0.040

-4 – -5 months	0.977	0.085	1.476***	0.077	0.936	0.046
-6 -7 months	0.976	0.136	1.195**	0.089	0.807***	0.057
-8 – 9 months	1.001	0.125	1.541***	0.099	0.998	0.061
-10 – -11 months	0.965	0.145	1.588***	0.112	1.053	0.071
Over -11 months	0.881	0.133	1.349***	0.094	1.163**	0.076
Duration of passive labour market support (1 – 2 months):						
3 – 4 months	1.379***	0.041	1.974***	0.060	1.991***	0.044
5 – 6 months	1.487***	0.065	2.565***	0.106	2.303***	0.072
7 – 8 months	1.425***	0.080	2.970***	0.148	3.019***	0.116
9 – 10 months	1.480***	0.100	3.280***	0.186	2.933***	0.134
11 – 12 months	1.154*	0.097	3.458***	0.217	3.256***	0.167
13 – 14 months	1.121	0.110	3.446***	0.237	3.254***	0.187
15 – 16 months	0.994	0.117	3.599***	0.268	3.496***	0.222
17 – 18 months	0.672**	0.105	3.443***	0.280	3.474***	0.245
19 – 20 months	0.742*	0.129	3.367***	0.296	3.434***	0.268
21 – 22 months	0.681*	0.141	3.255***	0.312	3.339***	0.288
23 – 24 months	0.802	0.177	3.154***	0.328	3.574***	0.334
25 – 26 months	0.412***	0.137	2.873***	0.335	3.671***	0.378
27 – 28 months	0.535*	0.179	3.232***	0.400	3.807***	0.430
29 – 30 months	0.420**	0.179	2.229***	0.349	3.323***	0.433
31 – 32 months	0.383*	0.198	3.309***	0.506	3.806***	0.530
33 – 34 months	0.812	0.355	3.470***	0.604	3.169***	0.535
Over 34 months	0.299**	0.158	1.963***	0.332	3.667***	0.511
Mass point 2	1.818***	0.152	-1.956***	0.121	-3.203***	0.103
P(mass point 2)	0.059*	0.034	0.789***	0.025	0.325***	0.039
Mass point 3	-2.139***	0.144	2.529***	0.111	-1.766***	0.059
P(mass point 3)	0.619***	0.114	0.044***	0.005	0.522***	0.032
Log likelihood	-61820.773		-97054.023		-127258.190	

Number of observations 520180. * Significant at 10 %:level, ** Significant at 5 %:n level, **** Significant at 1 %:n level, Reference groups in parentheses.

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