

# A Case for Public Sector Job Creation Schemes? Not Really

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## 1. Introduction

In a recent article appearing in this journal, Burgess (1992) argues the case for the immediate introduction of a public sector job creation scheme. He claims that on "both efficiency and equity grounds there is a strong case for public sector job creation schemes (PSJCS)" (p. 116). In this short note, we show that it is extremely unlikely that PSJCS can promote any substantial net job creation which will be sustained beyond the short-term. Moreover, we argue that such schemes typically promote less efficient outcomes. In effect, the case for PSJCS boils down to the equity effects. However, even here the case remains relatively weak given there are considerable doubts whether PSJCS actually impart valuable skills to participants or enhance their employment prospects.

## 2. Arguments Against a PSJCS

### 2.1 *Fiscal Substituting*

Burgess (p. 125) states that one of the major advantages of PSJCS is that they do not have the substitution problems associated with wage subsidy schemes much in vogue in Australia, such as JOBSTART.

That is, he argues that wage subsidies cause employers to substitute labour subsidized under the scheme for non-subsidized labour, whereas such an effect will be absent in the case of PSJCS. This view is mistaken. Many projects undertaken as part of the PSJCS would have been undertaken in the absence of the program – the phenomenon referred to as fiscal substitution – the main difference being that the project sponsors are compelled to use labour which meets the scheme's requirements rather than labour of their own choosing. That is, non-subsidized labour is displaced by subsidized labour. The extent of such fiscal substitution is likely to be large, especially if the scheme is permanent as Burgess advocates. Evaluations of the Wage Pause Program (WPP) initiative of the Fraser Government, for example, indicate that over half of the projects (53 per cent) had been brought forward because of the program (Creigh 1986, p. 39) but would have been undertaken in the absence of the program. More sobering are the estimates for the US reported in Johnson and Tomola (1977) which indicate that the fiscal substitution effects of public sector job creation programs are relatively small in the first six months, but thereafter rise sharply, reaching 100 per cent five quarters after commencement. Such findings make a lot of sense. If a scheme is around long enough, rational economic agents will build the presence of such schemes into their expectations. The only way such schemes can create net additional jobs in the long-term is if they are restricted to projects that would never have been undertaken in the first place. Thus, in contrast to the claims made by Burgess, any employment creation effects of PSCJS are likely to be confined to the short-term.

There is also the wider issue of the financing of PSJCS and what may be termed 'general equilibrium' effects. Even taking into account the income support foregone, PSJCS are relatively expensive, particularly where capital as well as labour costs are involved. Clearly, these costs have to be financed in some way, raising the spectre of 'crowding out' and the choking off of job creation in the private sector. For instance, if PSJCS are financed by higher taxes, the latter is likely to dampen the expansion of employment opportunities. Alternatively, the public sector deficit could be enlarged, but this will ultimately impact on employment via financial market effects. There is no 'magic pudding'.

## *2.2 Inefficiency*

PSJCS are not only likely to lead to little net job creation in the long-run, they promote less efficient outcomes. As Burgess notes, one of the key features of PSJCS is that they can be directly targeted on disadvantaged job-seekers and the long-term unemployed. But there are reasons why these people cannot find employment and one of the most important is that they generally have few skills. Consequently, in the presence of PSJCS, relatively more skilled and experienced labour is displaced by unskilled labour with little work experience, giving rise to less efficient outcomes.

Even less efficient outcomes are likely where there is some net job creation. As noted above, fiscal substitution of less than 100 per cent is possible over the longer-term only if projects that would not otherwise have occurred take place. However, if these projects are of any great economic and/or social value, it begs the question as to why they would not have been undertaken in the absence of the program. In general, projects which do not involve fiscal substitution are likely to be less profitable and/or more wasteful of community resources. This is the 'make work' charge frequently levelled at the Regional Employment Development Scheme (REDS) and Community Employment Program (CEP) projects of the past.

### *c) Equity Considerations*

Burgess argues that on equity grounds alone, there is a strong case for PSJCS. Clearly, even without any net job creation effects, job creation schemes help share the unemployment around, and thus, by Burgess' reasoning, break the cycle of long-term unemployment. The problem with this thinking is that it assumes that the main feature which distinguishes the long-term unemployed from other labour force participants is the duration of their unemployment. However, there have been numerous examples from overseas where employment prospects are actually made worse by participation in PSJCS. This arises because persons are stigmatized by their participation (Schmid 1982). Even in cases where participants' employment prospects appear to be enhanced by employment in PSJCS, the size of the effect is generally found to be small (Sloan and Wooden 1987).

Arguably, more important than mere employment is the quality of jobs obtained and the quality of the skills and training received,

and it is on this front that the Australian experience suggests PSJCS fare very badly indeed. One survey established that 53 per cent of WPP participants were in very low to low skilled jobs, while only 26 per cent were in jobs described as medium to highly skilled (BLMR 1985, p. 101). Similarly, information from the first year of operation of the CEP program indicated that nearly 60 per cent of placements were in unskilled positions (DEIR 1984, Table 3.10). While public sector job creation continues to revolve around labour-intensive, 'public works' type projects, the extent to which useful new skills are imparted to program participants will remain minimal.

### 3. Conclusions

In periods of high unemployment, governments have an obvious desire to be seen to be doing something. Large-scale public sector job creation schemes targetted at the unemployed and at the long-term unemployed in particular, are therefore, very appealing. They can be implemented quickly, they are associated with tangible activity and, in the short-run at least, do allow people to leave the dole queues. In times of severe recession, such schemes, by encouraging project sponsors to bring forward investment plans, can be very valuable. On the basis of past experience and evaluation, there are two 'golden rules' governments should adhere to when considering such schemes. First, schemes should not be targetted on the disadvantaged. Second, they should only be temporary. Burgess advocates that the Australian government break both these rules.

As noted above, schemes targetted on the long-term unemployed give rise to inefficient outcomes, since project contractors will be constrained to hire people who would not otherwise represent sensible hires. Such problems seem to have been recognized by the Keating Government in both its *One Nation* statement and the August 1992 Budget. In both these statements, the Government committed itself to a large expansion in infrastructure spending aimed at providing funds for worthwhile projects which local governments were not able to fund at the time because of recessionary fiscal constraints. None of this expenditure, however, is tied to jobs targetted on any particular group.

Even more important, any PSJCS should only be temporary. PSJCS, despite their name, cannot create jobs; they can only redistribute them, both between people and over time. Since they give rise to less efficient outcomes and do not appear to enhance the employability of participants, their main virtue is their ability to shuffle jobs around. Of course, this latter function may be seen as sufficient justification for PSJCS; they should not however be over-sold.

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