CHAPTER 4

Employing workers

- Nearly 40% of low- and lower-middle-income economies prohibit the use of fixed-term contracts for permanent tasks. In many of those economies, such legislation is obsolete.
- Six economies revised legal restrictions on nonstandard working hours in 2018/19.
- In economies with flexible employment regulation, more young women join the labor force.

Employment laws—introduced in response to market failures including worker exploitation, discrimination in hiring and working policies, and unfair dismissal practices—are vital to worker well-being. At the same time, firms should also be free to conduct their business in the most efficient way possible. When labor regulation is too cumbersome for the private sector, economies experience higher unemployment—most pronounced among youth and female workers.[1] With fewer formal job opportunities, workers turn to the informal sector.[2] Flexible labor regulation provides workers with the opportunity to choose their jobs and working hours more freely, which in turn increases labor force participation.[3]

For example, if France were to attain the same degree of labor market flexibility as the United States, its employment rate would rise by 1.6 percentage points, or 14% of the employment gap between the two countries.[4] When Sweden increased labor market flexibility, by giving firms with fewer than 11 employees the freedom to exempt two workers from their priority list, labor productivity in small firms increased 2–3% more than it did at larger firms.[5]

Governments face the challenge of striking a balance between worker protection and labor market flexibility. As argued in the World Bank's *World Development Report 2019: The Changing Nature of Work*, extending protection is the task of the government, not the firm.[6] The employing workers indicator set measures the flexibility of employment regulation. The indicators follow the life span of a typical employment relationship—from hiring to work scheduling and eventually to redundancy in a manner consistent with international conventions.[7]

Who regulates employment the most?

Low- and lower-middle-income economies tend to regulate employment more than do high- and upper-middle-income economies (figure 4.1). For example, regulation in the Central African Republic, Madagascar, and Senegal presents significant obstacles for employers hiring new workers or dismissing redundant ones. Among lower-middle-income economies in East Asia and the Pacific, Indonesia is one of the economies with the most rigid employment regulation, particularly on hiring. In the same region and income group, Mongolia allows the use of fixed-term contracts for permanent tasks with no limit on their renewal. In the Europe and Central Asia region, regulation on hiring in Serbia is relatively rigid, and authorities could benefit from the experience of Hungary where employers have the freedom to use fixed-term contracts of up to five years for tasks of a permanent nature.

Many high- and upper-middle-income economies, including Denmark, Namibia, and the United States, have flexible labor regulation. In other advanced economies, including Luxembourg, Slovenia, and Spain, strict labor rules make the process of hiring employees arduous. Research shows