

The Principles of Job Creation

By Mohammed Amin

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Many countries have a pressing need to create more jobs. For example many countries in the Middle East have very large numbers of unemployed or underemployed young people. The same problem blights some of the economies of southern Europe, such as Spain and Italy. Conversely other countries such as the USA and UK have much better employment records.

Why is this?

In my view the fundamental reason is that many governments pursue policies that are not conducive to private sector employment creation. Sometimes they are pursuing bad policies for well meaning reasons, because they fail to understand the correct policies to follow. On other occasions the reasons are more malevolent, and economic policies are deliberately designed to favour a small ruling clique at the expense of citizens in general.

The universe is a complicated place. However, physics makes it easier to understand. From the cacophony of data around us, it extracts fundamental principles, such as [Heisenberg's uncertainty principle](#), the [conservation of mass/energy](#) and the [principle of equivalence](#).

Economies are also complex systems and less susceptible than the material universe to formal experiments. None the less, there are basic principles which give clear guidance about what kinds of policies lead to particular kinds of outcomes. No government anywhere in the world says that it wants to stop jobs being created. However some are much more effective at creating jobs than others, because they adhere more closely to the basic principles.

If it is easier to start a business, more businesses will be started

Businesses are the most important creator of jobs, both for employees and for the self-employed roles of business owners. It appears self-evident that if someone wants to start a business, the state should put as few obstacles in the way as possible. In the real world, we find the opposite.

In "*The Mystery of Capital*" by Hernando de Soto, (my review is [here](#)) the author's team carried out practical experiments in several countries to find out how many permits were required to start a small garment workshop with one employee, and how long they took to acquire. In Peru it took 289 days, spending 6 hours per day on the application process.

Why do governments behave this way?

There are many reasons, some good, some misguided and some reprehensible. For example:

- **Good** – I don't want to be operated on by a surgeon who has had no training. I am reassured that the Government ultimately oversees a scheme run by the medical profession which pre-qualifies those who are entitled to practice as surgeons within the UK.
- **Misguided** – Many American states such as [Kentucky](#) regulate who can become a hairdresser. In the UK there is a voluntary registration scheme which the [Hairdressing Council](#) would like to make compulsory. At present, anyone can call themselves an accountant or a tax advisor, but every so often the relevant professional bodies express a wish for the state to stop people doing that unless they are properly qualified. No profession ever mentions the desire to reduce competition and new entrants as a reason for wanting restrictions; they always claim it is a desire to protect the public.
- **Reprehensible** – In many countries the government has been captured by a clique of kleptocrats, such as Tunisia before the Arab Spring. They ensure that only the favoured few can have licenses to operate businesses, which then earn monopoly profits shared by the business owners and those in government.

• **Policy prescriptions**

We should have a zero base review of every regulation that applies to any professional or business activity. In my view there is a clear hierarchy of policy approaches.

- **No regulations at all.** Caveat emptor applies, with dissatisfied customers being free to sue the business. The role of the state should be to make small claims courts quick and cheap.
- **Regulations regarding information disclosure.** For example the law requires lenders to publish the APR they will charge. In this category the law is still not limiting who can go into the business, but it does require the business to disclose certain information that customers will require.
- **Regulations requiring insurance.** The state protects customers by ensuring that the business cannot be a "*man of straw*." There is logic in requiring hairdressers to carry liability insurance. The insurance companies will then screen out poor commercial risks.
- **Formal regulation.** For some activities, such as running nuclear power stations or providing surgery, regulation is probably necessary. This applies most strongly where financial compensation may be insufficient, e.g. if people may be killed or seriously injured.

• **The easier it is to fire people, the more people will be hired**

Parts of continental Europe are plagued by high levels of youth unemployment. In my view the principal reason is that they are too dangerous to employ. In many

European countries, it is so hard to terminate an employee and the compensation that must be paid is so high that businesses will bend over backwards to avoid taking on an extra permanent member of staff.

Conversely in the USA where firing is relatively easy and cheap, when business turns down companies terminate people and when it picks up they hire them. The UK is somewhere in between the USA and continental Europe.

Why do European governments behave this way?

I am now retired. For just over half of my working career I was self-employed as a partner in accounting firms, and for the other half I was an employee. When an employee, I would always have preferred more job security to less; that is human nature.

The problem is that many European governments are primarily responsive to the interests of insiders; people who are already working and who have strong legal protections against termination. Persuading them to vote for lower termination protections really is like asking turkeys to vote in favour of Christmas!

Despite that, democracies can still make the change. For example look at the [Hartz Reforms](#) in Germany in the early part of the last decade, which dynamised the German economy. More locally, look at how Margaret Thatcher's government transformed the UK labour market. However both cases illustrate how tough it can be, and how much people resent their own situation being made more difficult even when the change is good for the country as a whole. Decades later, some people still moan about Thatcher's changes.

Policy prescriptions

As Conservatives, the first requirement is to resist any siren voices calling for more protections against employee terminations, redundancies etc. Under no circumstances should anything be done which makes it harder to get rid of employees who are under-performing or simply surplus to requirements.

It needs a better spin doctor than me to come up with an appealing way of presenting a policy platform that says we will make it easier for employers to sack people!

However, it remains true that the easier we make terminations, the more employment will be created. That is a message worth promoting.

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