

# Doctrinal approaches to the labour market activity

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**Andrei COJUHARI**

Doctor habilitate, University Professor

**Tatiana MUNTEANU**

Doctor, Associate Professor

Department of *Economic Theory and Marketing*  
Technical University of Moldova

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**Abstract.** *The labour market is one of the most important components of the market economy. This article presents the analysis of the specific characteristics, features and functions of this market, as well as the analysis of different doctrinal approaches regarding the activity mechanisms of the labour market.*

**Keywords:** *workforce, labour market, primary market, secondary market, unemployment, labour demand, labour supply, labour market equilibrium, price equilibrium, employment contract.*

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**B**efore describing the doctrinal approaches to the labour market, it is necessary to make a brief analysis of the general as well as of the more specific characteristics of this market. The defining elements of the labour market are: social actors in the labour market, namely the carriers of labour demand and supply; legislative and normative acts regulating the relationships on the labour market; the activity mechanisms of the labour market, which define the labour market conjuncture, the balance between labour supply and demand, the equilibrium wage and the employment; labour market related institutions; social security system of the labour market.

Unlike other markets in the national economy, the labour market has the following specific characteristics: workforce is not an ordinary commodity, since each employee is a unique personality, possessing special abilities (physical and intellectual) and a personal attitude towards work, and each job imposes its own requirements and conditions on the worker; labour cannot be “stored” if the supply exceeds the demand in the market of the labour force; transferring labour to other regions and spheres of application requires more time and effort than transferring usual goods within the labour market; the worker income, unlike prices of other goods, cannot be reduced below the subsistence minimum in the country; state intervention is more pronounced in the labour market than in other markets.

The labour market has several features:

- it is the most **imperfect** of the markets from the perspective of the adjustment mechanisms of labour demand, supply, and mobility
- it is the most **organized and regulated** market because it uses several regulatory mechanisms simultaneously (freedom of labour movement, decision of social partners regarding workplace; conditions of employment, salary and mechanisms of state intervention in the normal functioning of the labour market)
- it is a **negotiated** market in which social partners from enterprises negotiate the content of collective agreement at the level of the company (based on an employment contract), company branch and national levels. Negotiation issues stipulated in the contract refer to the volume and structure of employment, wage level, the relationship between wages, relations between direct and indirect wages etc.
- it is a **structured and segmented** market, which means that the labour market comprises several segments according to specific criteria. Labour market analysis requires the use of the concept of *segmentation*, which means that the labour market appearing as a single market on the national scale is divided into several segments according to specific

criteria. Different fields of activities offer different working conditions to their employees from the perspective of the working conditions, wages and opportunities of a professional career. Labour market segmentation also implies the existence of barriers when moving a worker from one segment of the labour market to another and the manifestation of the labour mobility within each segment and between various segments of the labour market; the contemporary labour market is a market with pronounced contractual and participatory features.

In this way, the labour market is a complicated system that can only operate in correlation with the other markets and as a part of the general economic system, while remaining autonomous at the same time. [1]

The labour market is an organic component of the market economy, which has several functions:

- the function of ensuring the achievement of a balance between the needs for labour resources of the national economy and the possibilities for the fulfilment of these needs. This function manifests itself at the micro-, meso- and macro levels, and it aims to achieve the balance mentioned above over a long period of time, but it does not preclude the occurrence of temporary imbalances as a result of the inconsistent movement of the human factor compared to other factors of production.
- the function of influencing the educational and training system from the perspective of the demand of the labour force for obtaining qualification and requalification. The mechanism of the labour market determines the flexible nature of the supply of the labour resources, which are supposed to correspond to the demand for these resources, deriving from the needs of the production process.
- the function of orienting the labour resources in every country with a view to increasing the efficiency of their utilization, by distributing them according to profession types, economic sectors and units, geographical location. For this purpose, a series of labour

market mechanisms are put into action, such as wage differences and mechanisms from outside the labour market.

- contributing to the achievement of the optimal combination between the human factor with the material factor in the production process with a view to reaching the goals pursued by each economic agent and by the national economy as a whole. Labour market provides complex information on the availability of human resources. This information can be subsequently used to establish correlations with the markets of the other production factors.
- the function of determining the process of income formation and distribution, based on a system of criteria established by the state legislation or by the individual or collective contracts. This function of the labour market has multiple ramifications and implications. The evolution of the supply-demand ratio determines both the labour wages (and the income, in general) and the mechanisms by which the distribution and redistribution of the national income are realised, the economic and financial methods used for this purpose.
- the function of adopting and implementing measures of social protection of the suppliers of the labour force. These measures are, essentially, the result of negotiations between businesses within the market. Among the measures of social protection of labour force suppliers, that of providing alternative income/unemployment aids to persons who have lost their jobs and have not yet found a new one has an extremely important role.

The functions of the labour market listed above are closely interdependent, forming a *whole*. The organisation of the labour market must ensure the optimal conditions for carrying out all the functions specific to this market.

There are many doctrinal approaches regarding the content and the operation of the labour market. Below, we attempt to analyse the main approaches.

## **The approach of the classical liberal school**

In the doctrine of the classical liberal school, represented by A. Smith, D. Ricardo, J.B. Say et al. the problem of the labour market used to be looked at from the perspective of the phenomenon of unemployment: when unemployment appears and/or increases, wages fall, workforce becomes cheaper, costs decrease, which allows the manufacturer to intensify the production process and employ a higher number of workers, thus causing the rate of unemployment to decrease. The representatives of the classical liberal school believed that maximising the use of the profitable production capacities and the flexibility of wages can ensure the balance of the labour market, in terms of achieving the full employment of the workforce. They claimed that a normally functioning market cannot generate *involuntary* unemployment. Instead, *structural* and *frictional* types of unemployment occur. In J.B. Say's view, supply and demand inside the labour market and inside other markets are *self-regulating* and there is no need for state's intervention in this area, the unemployment and the imbalances between supply and demand arising in the labour market and having only a temporary character. In our opinion, the classical-liberal school contributed greatly to the development of the concept of a labour market. However, we must note that the correlation between supply and demand in the labour market does not establish itself automatically, requiring a moderate intervention from the state. [6]

## **Karl Marx's approach**

Karl Marx's doctrine presents a new, modern hypothesis regarding unemployment and the labour market. In his famous work "Capital" (Vol.1, cap.21-23), K. Marx formulated the general law of capitalist accumulation, according to which "*greater the capital and the size of the proletariat – larger the industrial reserve army and official pauperism*". In Marx's view, if the capitalists failed to invest, they would not be able to produce goods. In this case, they would be forced out of the labour market, causing a decrease in wages and in the rate of employment. The decrease in the profits would lead to the bankruptcy of numerous businesses,

would reduce the investment in plants and machinery, and would, therefore, result in unemployment. The structural excess of the supply of labour force represented by the "industrial reserve army" keeps the salary at the subsistence level and makes the workers powerless in the face of the capitalists. Marx emphasises the connection between the use of the labour force and the production methods, claiming that unemployment is an important factor in regulating the capitalist production. He claims that unemployment emerges as a surplus of labour resources, which occurs under specific conditions of valorising the capital factor. [4]

## **The neoclassical approach**

According to the neoclassical approach to the labour market, represented by L. Walras, J.B. Clark, A. Marshall et al., employers hire workers up to the point where the cost of the labour force becomes equal to its marginal productivity. On the other hand, suppliers of labour force appear when the salary they are being offered is higher than the disutility of labour. Consequently, the supply and demand are balanced by the evolution of the price, that is – the real wage. Thus, the concept of the *labour market* emerged, a market in which there is *involuntary unemployment*. With respect to employment, the neoclassical school supported the idea of a full exploitation of the labour force in the context of the general economic equilibrium. We believe that this approach seems logical at the first sight, but it is not realistic, because, during economic crises and depressions, workers cannot find jobs even at the lowest salary. J. B. Clark's approach regarding employment in the context of income distribution is of great interest. He proposes a new concept of income distribution based on the marginal productivity of the production factors. Clark suggests that wages tend to the value of the marginal product of the last employee hired; rent tends towards the difference between the market value of the product and the value of the marginal product (the product from the least fertile plot); interest tends towards the lowest return on capital (marginal yield). Clark reached the following conclusion: the method of distributing the incomes according to their marginal productivity ensures the full employment of the labour force, the absence of

any exploitation, and the owner of each factor of production getting the part of social wealth he created. The problem of the labour market was also extensively approached by the neoclassical A. Marshall. In his work "Principles of Economics" (1890), the workforce is looked at from the perspective of orienting the human physical and intellectual capacities towards the production of economic goods. According to Marshall, the following measures should be taken in the view of increasing the productivity of the labour force: raising the level of labour force qualification; increasing the level of professionalism; improving employee's general and special skills; providing the worker with advanced equipment and appropriate technical training; increasing investments in the field of workforce training; financially stimulating the worker. Marshall had also thoroughly analysed such factors as the physical, intellectual and moral conditions that influence the productivity of the workforce, worker's muscular energy, the climate (which influences the natality), the food, clothing, the availability of living space, organization of recreational activities, optimism and personal freedom, the impact of the environment.

We would like to note that the current neoclassical approaches on the operation of the labour market, significantly differ from the neoclassical approaches in the 19<sup>th</sup> and 20<sup>th</sup> centuries. Contemporary neo-classicists believe that, from the microeconomic perspective, the labour market is divided into two submarkets: the primary and secondary markets.

- The primary market comprises all companies that offer highly paid, secure jobs and opportunities for being promoted and building a career. When a vacant position appears, such companies prefer to promote one of their own workers rather than offering the position to a previously unemployed individual or to a worker from another company – the external labour market. The domestic labour market is defined as an administrative unit, in which price and allocation of labour are governed by rules and procedures, so it does not work *freely*, as L. Walras assumed.

- The secondary market comprises businesses that provide jobs of "poor quality", where the salary level is low and little skill (or no skill) is required, where there are no opportunities for promotion and career building, and finally, where the job position is insecure.

These two segments of the labour market strongly influence each other. For example, if highly qualified individuals cannot find a suitable job in the primary market, adequate for their level of qualification, then, they usually apply for a job in the secondary market, thus managing to avoid unemployment. At the same time, some individuals who hold a job in the secondary market might obtain a decent job in the primary market. It is this dualism of the labour market arising from a mismatch between qualifications and skilled jobs that causes an increase in the rate of unemployment.

### **The Keynesian approach**

Keynes's approach to labour market suggests that the conceptual approaches of the classical and neoclassical liberals are not realistic because, in the capitalist system, unemployment becomes a *permanent* phenomenon. In his famous work "General Theory of Employment, Interest and Money", J.M. Keynes starts from the hypothesis that the labour market is in disequilibrium and the involuntary unemployment is a permanent phenomenon. To solve the problem of unemployment and to ensure a balance between the aggregate supply and demand in the labour market, Keynes suggests making a public spending that would stimulate the economic activity and increase the demand for goods and services in the economy. Because of the increase in this aggregate demand, businesses start considering increasing the number of employees in line with the requirements of the market. Keynes notes that unemployment is not an absolute evil and might even become a positive factor to a certain extent, encouraging people to work better. At the same time, he believes that in a capitalist society, there is no mechanism that would be able to ensure a full employment of the labour force. He claims that unemployment can be reduced only through state intervention, by means of promoting investment and creating new jobs. Unlike the classical and neoclassical

liberals, Keynes believes that spontaneous market mechanisms are not sufficient for the achievement of such basic goals as a full employment of the labour force, an absence of economic crises, a sustainable economic growth. He states that these objectives can only be achieved through an involvement of the state with its regulatory role, in the economy, with the use of such means as the state budget, monetary emission, regulation of the interest rates as well as of other economic levers [3].

We believe that Keynes's approach to labour market has played an important role in the employment policy of the workforce and in combatting unemployment in the 30s-60s of the last century. It has been implemented in several European countries and in the USA. However, because of the substantial socio-economic changes, many of its postulates have lost their original value.

### **The neo-institutionalist approach**

The doctrinal approaches of the neo-institutionalists to labour market focus on analysing the situations of imbalance within the labour market. The advantage of these models resides in their ability to reflect the currently existing institutions and economic order. Indeed, many workers are engaged in formal contracts, which establish the nominal salary in advance. Thus, the nominal wage allows the financial state institutions to control the real wages and thereby the level of employment. However, models that are based on contracts targeting nominal wages are controversial and cannot be explained in terms of the microeconomic principles:

a) if collective agreements are the cause of the large fluctuations in production and employment, which undermine effectiveness, then why do individuals and firms sign these contracts?

b) it is also inexplicable why optimal agreements are not compatible with low nominal wage flexibility in the labour market covered by collective bargaining agreements;

c) it is not clear why the collective bargaining agreements do not allow obtaining considerable obvious potential gains that could

be achieved during the negotiations of both sides. Both the economic and the socio-institutional factors exert their influence on the functioning of the labour market. The economic factors influence, in particular, the demand for the labour force. According to Marshall, the demand for the labour force - as a production factor - represents a *derived demand*. This means that the volume and the structure of the labour demand are determined by the final demand for goods and services, wage costs, but also the technological state of the system expressed by labour productivity and the intermediate consumption. Labour demand is simultaneously modelled by economic factors (the level of wages - as the price of this factor of production) and by social and institutional factors. In our opinion, the wages are not the real expression of the *price* of the labour force, but rather a representation of the social perception of the level of income, and of the systems for negotiating the wages. So, wages are "set" according to the present price level of the consumer goods and the expectations regarding the inflation rate. Also, wage differentiation is influenced not only by the level of qualification or other factors related to the technological progress but also by the "positions" that different occupations hold based on social conventions. The institutional system (system of training labour, property relations, recruitment and employment system of labour etc.) exert a major influence on the adaptability of the workforce to the changes made in the functioning of the labour market.

### **The monetarist approach**

The monetarist approach to the labour market, represented by M. Friedman et al., starts from the rigid structure of the prices of the labour force and from the premise that they "travel" in only one direction. Monetarists introduce the concept of "natural level of unemployment", which reflects the structural characteristics of the labour market, makes its prices inflexible, hinders its normal functioning, aggravates its imbalances and extends unemployment. In the opinion of representatives of this school, the negative factors intensifying the imbalance of the US labour market are the setting of the minimum wage by the state, strong syndicates, lack of

information about the available vacancies and the reserve army of labour. Monetarists suggest that, in order to balance the market, one needs to draw on the monetary-credit policy, and resort to such leverages as the official discount rate fixed by the central bank and the rates of the obligatory reserves for the commercial banks. This approach is also supported by some economists in the Republic of Moldova.

In the last decades of the 20<sup>th</sup> century and the beginning of the 21<sup>st</sup> century, new approaches to the labour market appeared in the frame of *the theory of the supply economy*. The latter was mainly based on the deregulation of the economic life and the reduction of public spending. Studies on the important role of the professional qualifications in the development of modern markets have resulted in two new theories that have had a strong impact on the development of new employment policies: the theory of *dualism of the labour market*, which highlights specific difficulties in hiring low-skilled workers, and the *human capital theory*, which reflects the role of the education and vocational training in economic development. The current stage in the evolution of the concept of labour employment is characterised by important qualitative transformations related to the rapid increase in the education level of the population of the developed countries, changing the conditions for the entry of young people in the labour market. Another characteristic is the implementation of the new employment requirements of workers in the process of developing their career, but less thoroughly instructed, who find themselves competing with young people. Currently, a set of programs and projects related to the issue of employment are elaborated in the European Union and in other developed countries. [2]

In conclusion, we would like to mention that the policies related to the adjustment of the

employment process will be reoriented in the future. Thus, fewer state policies of general application will be adopted, and more branch and enterprise policies, which will become the object of a socially active dialogue between employers and trade unions - a dialogue that will result in contracts covering a shorter period of time and revisable in accordance with the socio-economical conjuncture.

## Conclusions

The labour market has several functions, such as: assuring the equilibrium between the demand and supply of the labour resources; determining the efficient use of the labour resources; contributing to the achievement of the optimal combination of the human factor with the material factor in the production process with a view to obtaining positive financial economic results; impacting the formation and distribution of the income; assuring the social protection of the labour resource owners.

There are several doctrinal approaches to the content and mechanisms of the labour market, the most prominent of which are: the classical and neoclassical liberalist doctrines, the Marxist and Keynesian approaches, and finally, the institutionalist and the neoliberalist doctrines.

Unlike other markets in the national economy, the labour market has specific characteristics, such as: being the most imperfect from the perspective of adjustment mechanisms of labour demand and supply; being the most organized and regulated market since it operates with several regulatory mechanisms; being a negotiated market in which social partners negotiate the content of the collective labour contract at micro- and macroeconomic levels.

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