



Should the maximum duration of fixed-term contracts increase in recessions? Evidence from a law reform[☆]

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ABSTRACT

Fixed-term labour contracts (FTCs) may be an important tool to promote employment, particularly in recessions and when dismissal costs of open-ended contracts are high. In this case, making FTCs more flexible during downturns may be useful. We assess this idea by examining the effects of a law that increased the maximum duration of FTCs in Portugal during the 2012 recession. Our analysis is based on regression-discontinuity and difference-in-differences methods and employer-employee panel data. We find a considerable take up of this measure, as conversions to permanent contracts drop by 20%. Worker churning is reduced, as mobility of eligible fixed-term workers to other firms drops by 10%. Employment also increases but only for younger workers.

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1. Introduction

Labour market institutions are shaped by multiple parameters that establish how they operate in practice. These parameters include the replacement ratio of unemployment benefits, the amount of severance pay, the Kaitz index of minimum wages, and many other aspects. This paper presents and discusses the case for greater responsiveness of such parameters with respect to the conditions of the labour market. We argue that instead of enshrining parameters in the law and then adjusting them on a case-by-case basis, it may be useful to establish rules determining varying values of these different parameters depending on the macroeconomic context. We argue that this approach may serve as a tool to reduce the employment volatility of business cycles.

To our knowledge this approach – letting labour regulations respond to the business cycle – has only received some attention

in the case of unemployment benefits. These have been extended in periods of high unemployment (see [Hagedorn et al. \(2016\)](#) and its references for the evaluations of the U.S. case), as recently in the context of the pandemic recession. However, we argue that it may be fruitful to work towards ‘Taylor’s rules’ [Taylor \(1993\)](#), [Martins \(2021b\)](#) for many other labour market institutions than unemployment benefits. Collective bargaining, activation, employment protection laws, and other labour market institutions can also have significant effects [OECD \(2014\)](#) and benefit from greater responsiveness to the business cycle. These are institutions that already exhibit considerable international and, occasionally, within-country variability, through legal reforms.

The specific empirical evidence that we present here, in relation to the more general case above, is derived from the effects of a temporary increase in the flexibility of fixed-term contracts (FTCs, henceforth) in recessions. We consider the particular case of the maximum duration of FTCs, another parameter that exhibits considerable international variation. For instance, in France, such maximum duration is 18 months in the general case, further varying from 9 to 24 months, depending on the nature of the contract [OECD \(2014\)](#). In Spain and the UK, the maximum duration is 48 months, while in other countries with generally more flexible

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employment laws, including Poland and the US, there is no limit at all.¹

Of course, FTCs have received considerable attention in the academic literature, in particular in the context of the debates on the costs and benefits of FTCs and, more generally, about labour market segmentation Booth et al. (2002), Blanchard and Landier (2002), Bentolila et al. (2012), Garcia Perez et al. (2019). Although FTCs tend to be associated with a large number of negative outcomes (wages, training, productivity, health, etc.), this may reflect selection effects concerning the different profiles of firms and/or workers that participate in such contracts. On the other hand, by potentially facilitating the creation of jobs (compared to the case of sometimes more cumbersome permanent contracts), FTCs may increase employment, particularly for the young. FTCs may also potentially reduce the number of even more informal alternative relationships, such as individual contractors or service providers, who are not regulated by labour law at all. The literature above has also discussed different motivations for FTCs, which we group and describe below, in terms of screening, bargaining/incentives, insurance and uncertainty drivers. However, we do not know of any studies that examine the effects of specific parameters of FTCs, such as their maximum duration, as we do in this paper. Our approach focused on the analysis of specific components of labour regulations can therefore be useful in bridging the gaps between academics and policy makers.

This paper conducts an evaluation of a reform of FTCs implemented in Portugal in 2012, in the midst of a recession. This reform involved an increase in the maximum duration of FTCs, from three years to up to four and a half years. The reform was also designed in such a way that only some workers already in FTCs were eligible. In particular, only those hired sufficiently late to hit the old maximum duration once the new law was in force could be subject to the extended duration, a fact which we exploit for identification purposes. Drawing on matched employer-employee longitudinal data and regression discontinuity Hahn et al. (2001) and difference-in-differences methods, we evaluate the effects of the reform in terms of different outcomes of interest, including contract conversion, employment, and inter-firm (job-to-job) mobility probabilities. We find that all of these outcomes are affected, with large drops in conversions to permanent contract, an increase in employment (although only for young workers), and a decrease in worker churning or mobility to other firms. We also regard these results as supportive of our idea of greater responsiveness in labour regulations with respect to the business cycle.

The structure of the paper is as follows: the next Section presents the FTC reform. Section 3 presents the data sets and their descriptive statistics. The main results on both take up and outcomes of interest are presented in Section 4. Section 5 presents robustness checks and extensions. Finally, Section 6 concludes.

2. The fixed-term contracts reform

Similarly to several other countries, FTCs in Portugal are subject to a number of restrictions. Specifically, the country's labour code establishes that FTCs can in general only be made to meet a specific, well-defined temporary employment need experienced by the firm. FTCs also can only last the period required to meet that need, subject in any case to a maximum duration of 36 months in

total.² FTCs are also subject to a maximum number of renewals (three), implying that in cases of shorter contracts, FTCs will reach their maximum duration even before the time limits above. These restrictions are in line with the EU Directive that regulates FTCs (1999/70/EC) and which seeks to ensure that workers on FTCs do not suffer unjustified discrimination and to prevent excessive successive fixed-term contracts between the same employer and employee for the same work.

Before or by the maximum duration of an FTC, the firm and the worker decide on the termination of the FTC employment spell or its conversion into a permanent contract. In the latter case, the contract is automatically subject to much greater protection against dismissal. This applies not necessarily only in terms of grounds for required motives, severance costs, or dismissal procedures. The increase in protection follows above all in terms of the legal uncertainty surround a potential dismissal, including possible judicial reinstatements when the dismissal is successfully challenged in court.³ Any FTC that lasts longer than the applicable FTC maximum duration can also be automatically (even if implicitly) converted into a permanent contract. Similarly, any new FTC created for the same job immediately or soon after (over a period less than one third of the total duration of the previous contract) the old one is terminated may also be regarded as permanent by an employment tribunal, even if the new contract is made with a different worker.

The large gaps in protection between FTCs and permanent contracts and the resulting potential costs for firms in the latter case are relevant in most countries Hijzen et al. (2017). However, they are particularly important in Portugal, where individual dismissals are the most restrictive across the OECD OECD (2014). These circumstances explain the very large percentage of workers under FTCs in Portugal (22%), the third largest in the European Union.⁴ Additional factors include the relatively large size of seasonal or volatile sectors (such as tourism, construction or agriculture) and the economic uncertainty following from low economic growth rates (or recessions), which drive the growth of temporary employment needs that underpin FTCs from a legal perspective, as indicated above.

It was in this context that the government of Portugal decided in late 2011 to temporarily reduce the FTC restriction regarding its maximum duration. This policy was originally proposed during the June 2011 general elections by a political party that then became the junior member of the ruling coalition, although it did not receive much attention at that time. The measure – referred to as 'extraordinary renewal' ('renovação extraordinária') – was motivated by the view that, given the ongoing recession and economic uncertainty and the existing restrictions applicable to the termination of permanent contracts, many firms would not convert their current FTCs approaching their maximum duration. Such firms would instead terminate otherwise productive matches, with significant negative consequences upon employment. Following a discussion of the draft law with union and employer confederations in late September 2011 and the submission of the draft law to parliament in October, this law was approved in December 9th, 2011, finally being published and coming into force in January 11th, 2012.

² However, FTCs can also be established when a firm launches a new activity of uncertain duration (including a new establishment Cahuc et al. (2021)), when a firm hires a long-term unemployed individual or a worker searching for her first job. In these cases the maximum total durations are 18 or 24 months (articles 140 and 148).

³ See Cahuc et al. (2016) for the different case of France, characterised by greater protection of FTCs.

⁴ From a flows perspective, these shares are even higher: 70% of the workers employed in October 2011 and hired in that year were employed under FTCs (own calculations, based on the 'Quadros de Pessoal' data described below). Moreover, over 40% of the registrations of newly-unemployed individuals with the public employment service in any month also arise from terminations of FTCs.

¹ In Germany, the general maximum duration is even longer at 24 months, but can increase further to 48 months, when a new business is launched, or 60 months, when hiring older unemployed, or even unlimited, if there is an objective reason. In Italy, it is 36 months, with extensions possible in some cases or through collective bargaining, but only 12 months if no particular reason offered.

Specifically, the new law (3/2012) allowed FTCs that would reach their maximum duration between the time the law came into force up to June 2013 to be subject to two additional renewals. In total, these two renewals could not be longer than 18 months (or shorter than one sixth of the maximum duration of the contract). This represented a considerable increase of the until then maximum duration of FTCs (three years in the general case).⁵

The setup of the law in terms of its coming into force was such that, amongst the FTCs approaching their maximum duration towards the end of 2011 or early 2012, only those FTCs reaching that duration threshold after January 11th, 2012, would be allowed to extend further their duration. In particular, three-year FTCs started up to early January 2009 would necessarily not be eligible. In contrast, similar FTCs originally signed from late January 2009 could benefit from further extensions according to the new applicable law. In other words, some workers were hired 'too early', in the sense that they would have necessarily reached the conversion deadline before the FTC extension was legally possible. These workers were therefore confronted with the until then standard 'up or out' (conversion or dismissal) decision. However, workers hired even only a few days later qualify for a third possibility: one or two further extensions, still under an FTC. This legal setup creates a sharp discontinuity in eligibility which we exploit in our econometric analysis described below.

From a theoretical perspective, what may be the mechanisms underlying the effects of a reform of this type? We believe that screening or stepping-stone issues [Booth et al. \(2002\)](#), [Portugal and Varejao \(2010\)](#), [Faccini \(2014\)](#) will play a negligible role in our results, namely in the degree of take-up of the measure. This is because the workers affected will already have been in the firm for up to three years, a time period likely to be long enough to reduce significantly any information asymmetries about match quality. On the other hand, bargaining/incentives and uncertainty considerations are likely to be important factors. These make us expect a significant take up of the measure, as well as positive effects on employment and negative effects on inter-firm (job-to-job) mobility. First, a weaker labour market implies fewer outside options for workers, resulting in a weaker bargaining position and stronger incentives for them [Ichino and Riphahn \(2005\)](#), [Martins \(2009\)](#). Second, a recession will typically imply that the firm will face greater uncertainty in the product market and in the resulting derived labour demand, with negative effects on their propensity to invest [Bloom \(2009\)](#), including in permanent contracts.⁶

3. Data and descriptive statistics

We use the 'Quadros de Pessoal' data set, a comprehensive linked employer-employee panel. This data set provides detailed annual information on all firms based in Portugal that employ at least one worker and on all their employees, including time-invariant firm and person identifiers. All worker-level information concerns the month of October of each year and includes gender, date of birth, schooling, occupation, salary, hours of work, etc. Critically for the purposes of our paper, the data set includes the type of contract of each employee (permanent and different types of

non-permanent contracts, such as FTCs) as well as the hiring date (month and year when their contract started).⁷ However, the data does not include information on the expected duration of the FTC, the number of FTCs during the employment spell of the worker with the firm nor the number or dates of the FTC renewals. In our analysis, we focus on data for 2011 and 2012, the critical years of the reform.

Given the nature of the FTC maximum duration measure, we restrict our sample of interest to workers employed under FTCs in the 2011 data (i.e. employed in October 2011), and originally hired between October 2008 and September 2009 (excluding workers employed in more than one firm in 2011.) This time window is defined so that we are certain that these individuals are approaching the maximum duration of their FTCs either immediately before or immediately after the day when the longer FTC maximum duration became legally possible.

As indicated above, individuals hired between October 2008 and early January 2009 (and still employed in October 2011) will reach the maximum possible duration of their FTC before the 2012 law is in force. On the other hand, individuals hired between late January 2009 and September 2009 (and, again, still employed in October 2011) will reach the maximum possible duration of their FTC when the 2012 law is in force and are therefore eligible to have their FTC extended. Moreover, we do not consider individuals hired before October 2008 as they could not be observed as FTC (with the same firm) in October 2011. Similarly, we do not consider individuals hired from October 2009, as they would not necessarily be subject to the new law if they were to be observed as FTC in October 2012. Given that the QP data indicates the month and year of hiring (start date) but not its day, we assume that those hired in January 2009 are hired before the 11th (the day the measure comes into force, in 2012) as most contracts tend to start in the first day of the month, particularly those that have longer durations as the FTCs considered in this paper.⁸

Finally, we use the worker identifiers to track these individuals in the 2012 data and create a number of outcome variables. These include the employment status of the individuals (employed in the same or a different firm or, alternatively, not employed), their type of contract (in particular if they are employed in a permanent contract or not), and if they are employed by the same or a different firm. [Table 1](#) presents descriptive statistics of the resulting data, of the nearly 50,000 individuals observed in 2011, including these key dependent variables. We find that the conversion rate is 21%, while the employment probability (in 2012) is of 77%. Only 8% of the total number of workers are observed in a different firm in 2012.

[Table 1](#) presents additional statistics about our sample, including that 73% of individuals were originally hired from February 2008 (and are therefore assumed to be eligible under the new FTC duration law). This results into an average month of hiring of

⁵ The law that we study in this paper was subsequently subject to a further extension itself. A new law (76/2013) came into force in November 2013, outside the time frame of our analysis, allowing for additional renewals of FTCs, for up to 12 months, over the following two years. However, following the recovery of the economy and employment levels since 2013, the maximum duration of FTCs has returned to three years. See [Silva et al. \(2018\)](#) for the analysis of an earlier reform also involving FTCs.

⁶ [Caggese and Cunat \(2008\)](#) presents evidence that financially constrained firms in recessions tend to use fixed-term workers more intensely and make those workers absorb a larger fraction of the total employment volatility than financially unconstrained firms.

⁷ See [Portugal and Varejao \(2010\)](#), [Centeno and Novo \(2012\)](#), and [Damas de Matos and Parent \(2016\)](#) for earlier studies using the FTC variable in QP. See also [Martins \(2021a\)](#) for an analysis of a different form of non-standard work, individual contractors or service providers, not available in QP, which covers employees exclusively.

⁸ We underline that the group of workers that we examine in this paper is not the only one that would be subject to the reform. Potentially many other workers on FTCs but on shorter employment spells would be bound by the maximum renewals criterion. Moreover, one may expect a greater employment effect for such low-tenure workers, when compared to the higher-tenure counterparts. In fact, shorter employment matches are more fragile as they tend to generate less surplus (wages are known to increase very strongly during the first years of tenure – see [Snell et al. \(2018\)](#) and the references therein). Furthermore, the key screening process conducted by firms through FTCs is more likely to still be on-going in short FTC employment spells, making the conversion decision even more challenging. In other words, the analysis of our sample may result in smaller employment effects than those what would follow from the analysis of a more comprehensive range of tenures.

Table 1
Descriptive statistics.

	Mean	SD
Conversion	0.21	0.41
Employment	0.77	0.42
Firm mobility	0.08	0.27
Longer FTC maximum duration in force	0.73	0.44
Month of hiring (centered)	2.23	3.48
Female	0.46	0.50
Age	35.50	10.17
Secondary education	0.24	0.43
Higher education	0.18	0.38
Monthly wage	807.49	2126.93
Sales	26127.65	114089.66
Firm size (workers)	225.41	616.65
Equity	6104.56	78487.65
Manufacturing	0.17	0.38
Construction	0.14	0.34
Retail	0.16	0.37
Lisbon	0.33	0.47
Porto	0.16	0.37
Observations	49266	

Notes: 'Conversion' is a dummy variable (dv) equal to one if the worker is employed under a permanent contract in (October) 2012. 'Employment' is a dv equal to one if the worker is employed in (October) 2012. 'Firm mobility' is a dv equal to one if the worker is employed in a different firm in (October) 2012. 'Longer FTC max duration' in force is a dv equal to one taking value one for individuals hired from February 2009 onwards. 'Month of hiring (centered)' is a variable centered at February 2009 (i.e. -1 for individuals hired in January 2009, 1 for individuals hired in March 2009, etc.). 'Female' is a dv equal to one for women. 'Age' indicates the worker's age in 2011. 'Secondary' and 'Higher education' are dv's indicating a worker's highest schooling attainment. 'Monthly wage' indicates the worker's monthly salary in October 2011 (in nominal euros). The remaining variables refer to firm characteristics (of the firm where the worker is employed, in 2011): sales (in thousands of euros), number of workers, equity (in thousands of euros), sectors (manufacturing, construction and retail) and region (Lisbon and Porto). The sample is all individuals employed under fixed-term contracts in October 2011 and hired in their current employment spell between October 2008 and September 2009. Own calculations based on the 'Quadros de Pessoal' data set.

2.23 (in which 0 corresponds to February 2009). Workers are on average 35.5 years old, 24% and 18% have at most secondary or higher education, respectively, and earn an average gross monthly salary of 807 euros. Their firms have average annual sales of 26 million euros, capital equity of 6 million euros and employ 225 workers. The most important one-digit sectors are manufacturing, construction and retail, while the most important geographical districts (Lisbon and Porto) represent nearly 50% of the sample.

Given our regression-discontinuity analysis next, we also present graphically the distribution of our sample across the running variable, the month of hiring. Fig. 1 indicates little dispersion in this respect, except for the role of the standard seasonal monthly effects in hirings. In particular, December and August exhibit lower hirings, as they are months of holidays in most sectors, while the following months of January and September exhibit higher hirings. In any case, the blips in these four months cannot be interpreted as direct manipulation driven by the law, as they occurred three years before the introduction of the new law. A second important conclusion from visualising the data in Fig. 1 concerns the marked difference in the average conversion percentages before and after the time (three years after) the new law is introduced. In fact, the blue dots to the left of the vertical dashed line (February) are, on average, significantly higher than those to the right. This constitutes 'prima facie' evidence of a significant take up of the new law, opening up the possibility of other effects in terms of employment and mobility. These issues are addressed in greater detail in the next section.

4. Results

Our main analysis of the effects of the increased maximum duration of FTCs is based on a regression discontinuity approach Hahn

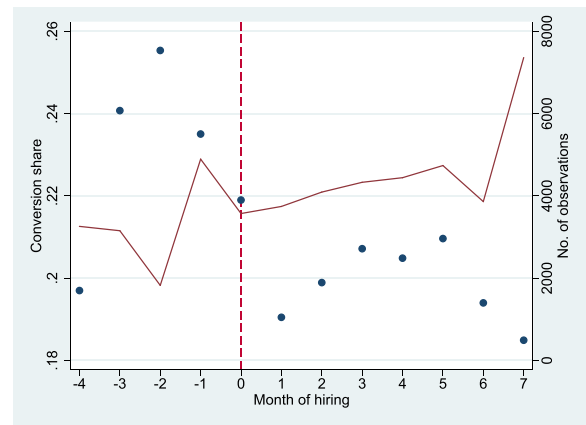


Fig. 1. Number of workers and conversion rates per hiring month. **Notes:** The red line indicates the number of hirings per month (measuring along the right-hand-side vertical axis); the blue dots indicate the mean conversion rates per month (measured along the left-hand-side vertical axis). Month 0 refers to February 2009. These will be the first group of individuals subject to the longer maximum duration of FTC, introduced in mid-January 2012, should their contracts last the until the maximum duration of three years. All 49,266 individuals in the sample (described in more detail in Table 1) were hired between October 2008 and September 2009 and still employed in the same firms and in fixed-term contracts as of October 2011.

et al. (2001), Lee and Lemieux (2010). Essentially we compare a number of outcomes of interest between a group of workers that is not eligible – because they will necessarily reach the maximum duration of their FTC (three years) before the extended duration is in force – and another group of workers that will be eligible – because they will reach their presumed maximum duration of their FTC once the extended duration is in force.

At the same time, we control for any direct effects from differences across workers related to the timing of their hiring. We do this through the control for different polynomials of our running variable (the month when the individual was hired, centered at February 2009). Given that this timing was determined three years before the introduction of the FTC extension, it will not have had a direct effect upon outcomes. Moreover, we are also not aware of any systematic differences between worker profiles at that threshold, even 2009 was a time of financial crisis. In any case, we conduct a number of robustness checks, including the analysis of a large number of pre-determined covariates that describe workers and their firms at the two sides of the January/February 2009 threshold.

It is important to note that while the individuals hired earlier could not be subject to the new law (they reach the three-year maximum duration before the new law is in force), a small number of workers hired later may also have been in the same circumstances. The latter group are those that are subject to the maximum number of renewals restriction (until the new law applicable to all FTCs) or the shorter maximum durations (18 and 24 months, applicable to the hiring of the long-term unemployed and the unemployed searching for their first jobs). In other words, their FTCs would effectively come to an end in the short time period between November 2011 and January 2012 (but not before as they are still employed under FTCs in October 2011, by sample construction). Given the limited three-month time window above, we believe that the magnitude of this bias in the estimates presented below will not be large. In any case, to the extent that this issue implies that we are considering as 'treated' individuals that are in fact 'controls', the resulting bias in our estimates will be downward, towards zero, e.g. any potential (positive) employment effects will be smaller than if this bias did not apply. Alternatively, we may approach our estimates as 'Intention to treat' results.

Given the discussion above, we estimate the following regression-discontinuity equation on a cross-section of all work-

Table 2
Conversion effects.

	(1)	(2)	(3)	(4)
Longer FTC max duration in force	-.021 (.013)	-.048 (.018)***	-.046 (.018)**	-.045 (.016)***
Month of hiring (centered)	-.001 (.002)	.005 (.003)	.004 (.004)	.011 (.006)*
Month of hiring (centered) ²		-.001 (.0004)***	-.001 (.0006)**	
Month of hiring (centered) ³			.00005 (.0001)	
Month of hiring (cent.)*Longer FTC max dur.				-.013 (.006)**
Const.	.226 (.010)***	.249 (.011)***	.249 (.011)***	.255 (.014)***
Obs.	49266	49266	49266	49266
R ²	.001	.002	.002	.002

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is converted to a permanent contract in (October) 2012. The running variable (month of hiring) is centered at February 2009, when it takes value zero. The key regressor (Longer FTC max duration in force) is a dummy variable taking value one for individuals hired from February 2009 onwards and value zero otherwise. The sample is all individuals employed under fixed term contracts in October 2011 and hired in their current employment spell between October 2008 and September 2009. Own calculations based on the 'Quadros de Pessoal' data set. Standard errors clustered at the month of hiring level. Significance levels (two-sided tests): * 0.10, ** 0.05, *** 0.01.

Table 3
Employment effects.

	(1)	(2)	(3)	(4)
Longer FTC max duration in force	-.002 (.008)	.006 (.012)	.006 (.012)	.003 (.013)
Month of hiring (centered)	-.0003 (.001)	-.002 (.002)	-.002 (.003)	-.003 (.004)
Month of hiring (centered) ²		.0003 (.0003)	.0003 (.0005)	
Month of hiring (centered) ³			-2.96e-06 (.00009)	
Month of hiring (cent.)* Longer FTC max dur.				.003 (.005)
Const.	.775 (.006)***	.768 (.010)***	.768 (.010)***	.768 (.012)***
Obs.	49266	49266	49266	49266
R ²	.00002	.00006	.00006	.00004

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is employed in (October) 2012. See more details in notes to Table 2.

ers hired between October 2008 and September 2009 and still employed under FTCs in October 2011:

$$Y_i = \alpha + \beta D_i + \lambda S(Z_i) + \varepsilon_i \quad (1)$$

The key dependent variables considered, Y_i , are dummy variables referring to different potential transitions (conversion to permanent contract, employment status, and mobility to a different firm, in all cases in October 2012). D_i is a dummy variable equal to one for individuals hired from February 2009 (as opposed to between October 2008 and January 2009). $S(Z_i)$ are different polynomials of the running variable, the month of hiring (from October 2008 up to September 2009), centered at February 2009. Standard errors are clustered at the month of hiring level.

Table 2 presents the first set of results, when the dependent variable is the conversion dummy (i.e. one if the worker is under a permanent contract in October 2012). Except for the first column (linear polynomial), all coefficients of interest (β) in the remaining three specifications (quadratic, cubic and linear-spline polynomials) indicate statistically significant negative effects. Moreover, all three coefficients are very similar, at -.048, -.046 and -.045. Compared to the sample mean of 0.21 (Table 1), these coefficients translate into an economically significant counterfactual reduction in conversion rates for the individuals affected of over 20%. This result can be interpreted as evidence of considerable take up of the measure and of its relevance in the labour market, especially as it may be seen as a lower bound of the true effect. This take up is

also in line with the widespread public discussion about the measure at the time it was prepared and again when it came into force, including amongst employer representatives.⁹ This result may also be regarded as a necessary condition for other potential effects to emerge, which we examine below.

First, we consider the case of employment effects – Table 3 – using a dummy variable equal to one if the worker is employed in October 2012 (in the same or a different firm in our data set).¹⁰ As before, we find similar coefficients in the three specifications other than the one based on a linear polynomial but in all cases they are statistically and economically insignificant. In other words, in contrast to the expected effects of the measure, employment does not appear to have increased significantly. As mentioned above, these results may represent lower bounds of the true effects, given that some workers regarded as treated may in fact not be subject

⁹ Martins (2016) examines the take up of a different measure introduced later, in August 2012 – greater flexibility in the setting of overtime premiums –, finding that half of eligible firms did implement the measure at least as soon as three months after it came into force, despite the significant international evidence about downward nominal wage rigidity. This result is consistent with the findings of this paper about the considerable interest by firms of greater flexibility in labour regulations, at least in times of recession.

¹⁰ Employment outside the data set, such as a civil servant or a contractor, is excluded and is therefore classified as non-employment. However, given the regression-discontinuity framework employed, this would not affect our results.

Table 4
Interfirm (job-to-job) mobility effects.

	(1)	(2)	(3)	(4)
Longer FTC max duration in force	.001 (.007)	-.013 (.008)*	-.015 (.007)**	-.007 (.007)
Month of hiring (centered)	-.0009 (.001)	.002 (.001)*	.004 (.002)**	.003 (.003)
Month of hiring (centered) ²		-.0005 (.0002)***	-.0003 (.0003)	
Month of hiring (centered) ³			-.00005 (.00005)	
Month of hiring (cent.)*Longer FTC max dur.				-.004 (.003)
Const.	.079 (.004)***	.091 (.006)***	.090 (.005)***	.089 (.005)***
Obs.	49266	49266	49266	49266
R ²	.0001	.0004	.0004	.0002

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is employed by a different firm in (October) 2012 (compared to 2011). See more details in notes to Table 2.

Table 5
All effects – young workers.

	Conversion effects		Employment effects		Mobility effects	
	(1)	(2)	(3)	(4)	(5)	(6)
Longer FTC max dur in force	-.042 (.023)*	-.038 (.023)	.022 (.012)*	.022 (.012)*	-.013 (.010)	-.016 (.009)*
Month of hiring (c)	.004 (.004)	.002 (.004)	-.005 (.002)**	-.005 (.003)*	.002 (.002)	.003 (.002)
Month of hiring (c) ²	-.001 (.0005)**	-.002 (.0008)**	.0005 (.0003)	.0004 (.0005)	-.0005 (.0003)*	-.0001 (.0004)
Month of hiring (c) ³		.0001 (.0001)		2.12e-06 (.0001)		-.00008 (.00006)
Const.	.265 (.014)***	.266 (.015)***	.772 (.010)***	.772 (.010)***	.099 (.007)***	.098 (.006)***
Obs.	29686	29686	29686	29686	29686	29686
R ²	.002	.002	.0003	.0003	.0005	.0006

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is converted to a permanent contract in (October) 2012 (first two columns), if the individual is employed in (October) 2012 (second pair of columns), or if the individual is employed by a different firm in (October) 2012 (compared to 2011) (third pair of columns). The running variable (month of hiring) is centered at February 2009, when it takes value zero. The key regressor (Longer FTC max duration in force) is a dummy variable taking value one for individuals hired from February 2009 onwards and value zero otherwise. The sample is a subset of all individuals employed under fixed term contracts in October 2011 and hired in their current employment spell between October 2008 and September 2009. Own calculations based on the 'Quadros de Pessoal' data set. The subset varies depending on the column. Standard errors clustered at the month of hiring level. Significance levels (two-sided tests): * 0.10, ** 0.05, *** 0.01.

to the measure if their contracts reached their maximum duration before the measure was in force.

Second, we consider the case of inter-firm (job-to-job) mobility effects – Table 4. We use a dummy variable equal to one if the worker is employed by a different firm in October 2012 (compared to her employer in October 2011). Here we find a statistically insignificant result with the linear polynomial and the linear-spline but significant results (at the 10% or 5% levels) with the quadratic and cubic splines. Moreover, in those two cases (and also in the case of the linear spline), we find economically meaningful effects, of between approximately 10% and 20% of the average mobility (a sample mean of 0.08 in Table 1).¹¹

Given our particular concern for the young, those who may benefit more from the opportunities that may follow from FTCs, we repeat the analysis above for those below the mean age in our sample of 35, considering the two main polynomial specifications (quadratic and cubic). Tables 5 presents the results, which are broadly similar to those from the full samples. However, we now find significant employment effects, even if only at the 10% level. At 2.2% in both cases, they amount to relative effects of nearly 3% when considering the average employment rate of 77%.

¹¹ We also considered an additional potential outcome, salaries (monthly or hourly), finding no significant effects across the different specifications.

Taken together with the previous findings, these results indicate that, even if the extension of the maximum duration of the FTCs does not increase employment significantly for the entire sample, inter-firm mobility is reduced in that case. Moreover, young workers, who may face greater challenges in their labour market transitions, benefit in terms of increased employment chances if they are eligible to benefit from the extension in their FTCs. The stronger results on inter-firm mobility than employment for the entire sample may also imply that workers in our sample that lose their jobs as a consequence of the non-renewal of their FTCs tend to find other jobs relatively quickly, even in the recession period considered. In other words, despite not continuing in the same jobs, such movers are statistically equally likely to be employed in the following period. Such employment outcome may reflect a good balance between the experience that these workers gained from their jobs, having been employed consecutively for at least two years, while not being too distant from the external labour market either, as may be the case for workers employed in the same job for longer periods. In any case, such high employability levels for non-renewed workers may not necessarily apply at other levels of the FTC duration, namely workers that hit the legal constraints before the three-year threshold.

However, reducing inter-firm mobility – and therefore worker churning Burgess et al. (2000), Martins (2008) – may be regarded as a positive outcome. Indeed, it may reflect a joint decision between the employer and the employee to continue an FTC employment

Table 6
Conversion effects – different subgroups.

	(1) Women	(2) Low schooling	(3) Low wage	(4) Small firms
Longer FTC max dur in force	-.041 (.017)**	-.043 (.013)***	-.037 (.011)***	.006 (.008)
Month of hiring (c)	.009 (.003)***	.005 (.002)**	.002 (.002)	-.002 (.002)
Month of hiring (c) ²	-.0006 (.0007)	-.0007 (.0004)	-.0008 (.0003)***	-.0005 (.0002)**
Month of hiring (c) ³	-.0001 (.0001)	-8.52e-06 (.00006)	.00007 (.00006)	.0001 (.00005)**
Const.	.238 (.014)***	.218 (.008)***	.212 (.004)***	.149 (.003)***
Obs.	22899	28704	23754	24772
R ²	.0007	.0008	.0007	.00008

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is converted to a permanent contract in (October) 2012. The running variable (month of hiring) is centered at February 2009, when it takes value zero. The key regressor (Longer FTC max duration in force) is a dummy variable taking value one for individuals hired from February 2009 onwards and value zero otherwise. The sample is a subset of all individuals employed under fixed term contracts in October 2011 and hired in their current employment spell between October 2008 and September 2009. The subset varies depending on the column. In the first column: only women. In the second column: only workers with less than secondary schooling. In the third column: only workers earning less than four euros per hour. In the fourth column: only workers in firms with 38 workers or fewer. Own calculations based on the 'Quadros de Pessoal' data set. Standard errors clustered at the month of hiring level. Significance levels (two-sided tests): * 0.10, ** 0.05, *** 0.01.

Table 7
Employment effects – different subgroups.

	(1) Women	(2) Low schooling	(3) Low wage	(4) Small firms
Longer FTC max dur in force	.006 (.022)	.006 (.017)	.013 (.018)	.002 (.012)
Month of hiring (c)	-.006 (.003)*	-.003 (.004)	-.007 (.004)	-.003 (.004)
Month of hiring (c) ²	-.0004 (.0008)	.0007 (.0007)	.0003 (.0006)	-.0002 (.0005)
Month of hiring (c) ³	.0001 (.00009)	-1.00e-05 (.0001)	.00009 (.0001)	.00007 (.0001)
Const.	.787 (.020)***	.752 (.014)***	.758 (.012)***	.751 (.010)***
Obs.	22899	28704	23754	24772
R ²	.0005	.0002	.0004	.0002

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is employed in (October) 2012. See more details in notes to [Table 6](#).

spell that, before the new law was in force, would not be legal. In fact, the productivity of such a match is likely to be greater than its alternatives, creating the necessary conditions for continuing employment in the case of no legal impediments.

These results may be seen to be at odds with the negative views of the labour market segmentation literature regarding FTCs. In fact, this literature [Blanchard and Landier \(2002\)](#), [Bentolila et al. \(2012\)](#) tends to consider FTCs and their greater flexibility as a negative development in the architecture of labour markets, potentially increasing turnover in entry-level jobs. Of course, measures that erode the high levels of rigidity of permanent contracts in some countries may be more appropriate. In the case of the flexibility-increasing FTC reform studied here, although conversion rates have fallen, employment spells have increased their duration as worker turnover fell.

5. Robustness and extensions

In this section we present the findings from four robustness checks and four extensions. Starting with the robustness checks, we first examine the results of our main analysis by specific subgroups. We consider five dimensions available in our data, namely gender, schooling, wage and firm size, rerunning our models for women and for the values below the median of the remaining variables (schooling below secondary level, hourly wage below four euros, and firm size below 38 workers). The results, presented in

[Tables 6–8](#), are based on the cubic polynomial (but similar to other polynomial specifications, in particular the quadratic one). We find very similar results to those of the full sample, in terms of both economic and statistical significance, despite the smaller sample size. There is perhaps only one exception: we do not find significant effects amongst smaller firms (column 5 of [Table 6](#)), at the 10% significance level, which may reflect lower awareness about the reform for these firms.

In a second robustness test, we conduct balancing tests, in which we estimated Eq. (1) using as dependent variable a number of pre-determined (2011) variables: gender, age, hourly pay, secondary and higher education dummies, firm sales, firm size (number of workers), firm equity, firm sector dummies (three main sectors), and firm regions (two main regions). Moreover, to make the test more challenging, we considered only the two polynomial specifications where we found significant results in our main analysis in Section 4 (quadratic and cubic polynomials). We found that, out of the resulting 26 specifications, only three returned coefficients significant at the 5% level (results available upon request). We take these findings as evidence that the threshold at which the measure will be in effect does not coincide with systematic differences in the profiles of the workers involved, further supporting a causal interpretation of our main findings, including the worker mobility effects.

In a third robustness test, we check the extent to which our results are sensitive to the inclusion of control variables. In par-

Table 8
Interfirm (job-to-job) mobility effects – different subgroups.

	(1)	(2)	(3)	(4)
	Women	Low schooling	Low wage	Small firms
Longer FTC max dur. in force	-.015 (.007)**	-.018 (.010)*	-.008 (.015)	.005 (.006)
Month of hiring (c)	.005 (.001)***	.003 (.003)	.002 (.002)	.001 (.001)
Month of hiring (c) ²	-.0001 (.0002)	-.0004 (.0003)	.0002 (.0006)	1.00e-05 (.0002)
Month of hiring (c) ³	-.00008 (.00003)**	-5.68e-06 (.00007)	-.00008 (.00007)	-.00003 (.00004)
Const.	.076 (.004)***	.089 (.006)***	.077 (.012)***	.066 (.003)***
Obs.	22899	28704	23754	24772
R ²	.0003	.0002	.0001	.0003

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is employed by a different firm in (October) 2012 (compared to 2011). See more details in notes to [Table 6](#).

Table 9
Conversion effects – including control variables.

	(1)	(2)	(3)	(4)
Longer FTC max duration in force	-.016 (.012)	-.042 (.016)***	-.039 (.017)**	-.041 (.013)***
Month of hiring (centered)	-.003 (.002)	.004 (.003)	.002 (.004)	.010 (.005)**
Month of hiring (centered) ²		-.001 (.0003)***	-.001 (.0005)**	
Month of hiring (centered) ³			.00007 (.00009)	
Month of hiring (cent.)*Longer FTC max dur.				-.014 (.005)***
Const.	.299 (387.314)	.321 (539.562)	.321 (144.878)	.328 (99.937)
Obs.	47742	47742	47742	47742
R ²	.031	.032	.032	.032

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is converted to a permanent contract in (October) 2012. All specifications include the following control variables: female indicator, age, secondary and higher education indicators, hourly wage, log firm sales, log firm size (number of workers), multi-establishment dv and foreign and public ownership dv's, industry and region dummy variables (firm-level information refers to firm affiliation in 2011). See more details in notes to [Table 2](#).

ticular, we include the same set of variables described above (plus greater detail in terms of sectors and regions). We then estimate Eq. (1) for the case of conversion effects, considering the same range of polynomials as in the [Table 2](#). The results are presented in [Table 9](#) and indicate again very similar effects, ranging between -0.045 and -.048, and in all cases highly significant.

Our last robustness test concerns the role of our control for global high-order polynomials in our main regression discontinuity analysis. According to [Gelman and Imbens \(2018\)](#), this approach can be problematic, leading to 'noisy estimates, sensitivity to the degree of the polynomial, and poor coverage of confidence intervals'. Indeed, observations far from the cut-off can gain undue influence in the estimation under cubic or higher polynomials, potentially leading to large variations in the results depending on the degree of the polynomial adopted. [Gelman and Imbens \(2018\)](#) also show that confidence intervals can be artificially tight, leading to biases in favour of statistically significant effects. In our main results above, we find that the quadratic, cubic and spline specifications deliver similar results (namely significant negative conversion effects) but this is not the case under the linear specification.

We thus also consider *local* linear regression [Calonico et al. \(2020\)](#), restricting our analysis to different ranges of months around the cutoff. It is however also important to acknowledge potential bias under this approach, namely from a smaller sample. In addition, as we indicated before, in our specific case, while the observations to the left of the cut-off are necessarily in the control group, those to the right are not necessarily in the treatment group.

The former will have reached the maximum FTC duration before the reform while the latter may or not be subject to the extended FTC duration prompted by the reform. Moreover, the shorter the range on the right-side of the cut-off (e.g. if considering only one month after February 2009), the lower the likely percentage of contracts that are effectively subject to the reform. By extending the range considered, as in our main analysis, we can thus better capture the effects of the reform, although the scope for the challenges highlighted in [Gelman and Imbens \(2018\)](#) also increases.

Our results are presented in [Table 10](#), in which each row corresponds to a separate regression. These regressions follow from the three outcome variables (conversion to permanent contract, employment in the second period, and mobility to different firms, respectively) on the reform indicator variable (February 2009 or later hiring date), across a particular range of months around the cut-off (1, 2, or 3 months both before and after). The results again indicate negative effects on conversion, of at least -0.03, significant in two of the three time ranges (two and three months). In the remaining two outcomes, the effects are again generally not significant, with one exception (at the two-month range) in the case of interfirm mobility (and another in the case of employment, but of the opposite sign). The increasing absolute size and statistical precision of the coefficients in the main outcome regarding conversion is consistent with our discussion above about the trade-offs between the polynomials and local linear regressions approaches.

Turning to our extensions, first we implement a falsification test in which we shorten the FTC duration at which the binding restric-

Table 10

Local linear regression results – different outcomes and ranges.

Time range (months)	Coefficient	Rob. std. err.	t-ratio	p-value	Observations
<i>Conversion</i>					
1	–.030	.012	–2.48	0.131	12,207
2	–.038	.009	–3.91	0.017	18,124
3	–.036	.006	–5.44	0.002	25,607
<i>Employment</i>					
1	–.006	.000	–49.12	0.000	12,207
2	–.002	.009	–0.24	0.820	18,124
3	.001	.006	0.15	0.884	25,607
<i>Interfirm mobility</i>					
1	–.007	.003	–2.17	0.162	12,207
2	–.007	.002	–3.34	0.029	18,124
3	–.005	.005	–1.07	0.326	25,607

Notes: Each row corresponds to a separate regression of each one of the three outcome variables (conversion to permanent contract, employment in the second period, and mobility to different firms) on the reform indicator variable (February 2009 or later hiring date) across a particular range of months around the cut-off (1, 2, or 3 months both before and after).

Table 11

Conversion effects – falsification exercise.

	(1)	(2)	(3)	(4)
Longer FTC max duration in force	.032 (.023)	–.022 (.021)	–.026 (.022)	–.003 (.023)
Month of hiring (centered)	.001 (.003)	.015 (.006)***	.017 (.006)***	.020 (.012)
Month of hiring (centered) ²		–.002 (.0007)***	–.002 (.001)	
Month of hiring (centered) ³			–.0001 (.0002)	
Month of hiring (cent.) * Longer FTC max dur.				–.020 (.013)
Const.	.324 (.019)***	.370 (.017)***	.369 (.017)***	.366 (.020)***
Obs.	39740	39740	39740	39740
R ²	.001	.003	.003	.002

Notes: The columns present different specifications of a (sharp) regression discontinuity model. The dependent variable is a dummy variable equal to one if the individual is converted to a permanent contract in 2012. The running variable (month of hiring) is centered at February 2010, when it takes value zero. The key regressor (Longer FTC max duration in force) is a dummy variable taking value one from February 2010 onwards and value zero otherwise. The sample is all individuals employed under fixed term contracts in October 2011 and hired in their current employment spell between October 2009 and September 2010 (not October 2008 and September 2009, as in previous tables) – the large majority of these individuals would not be subject to the extended maximum duration of fixed-term contracts. Own calculations based on the 'Quadros de Pessoal' data set. Significance levels (two-sided tests): * 0.10, ** 0.05, *** 0.01.

tions would apply before (but not after) the measure, from three to two years. Although as discussed above some workers would be subject to maximum FTC durations of two years (when a firm launches a new activity of uncertain duration or through the limit of three renewals), in most cases these would not apply unless that threshold happens to coincide with some other feature of the labour market unknown to us.¹² However, the results in Table 11 indicate no significant effect for any specification, a finding that constitutes further support to a causal interpretation.

Our second extension analyses potential firm-level effects of the increased maximum duration of FTCs. Firms that had greater flexibility in the conversion vs non-renewal decision of some of their workers may benefit in terms of different outcomes. For instance, greater flexibility in employment contracts (FTCs in this case) may increase productivity (through incentive effects Ichino and Riphahn (2005), Martins (2009), with subsequent positive scale effects in terms of the employment of other individuals too. We consider three variables of potential interest, sales, number of workers and firm exit, all measured in 2012 or in percentage differences between 2012 and 2011, again in the same regression-discontinuity framework of Eq. (1). However, in no case do we find significant, robust

results (available upon request). This is also the case if we restrict the sample to individuals in firms where only one worker was potentially affected by the new law, in order to control better for potentially intensity of treatment issues.

Our third extension seeks to measure the effect of the reform in terms of the number of months worked over the period November 2011–October 2012. As we do not know the month when movers leave their previous firm, we assume this to be the month when the contract reached its 36th month or when the new contract started, if earlier. We then consider this duration variable, which ranges between 0 and 12, the latter case when a worker stays in the same firm or when hired by the new firm before or when the 36th month of the previous contract was reached, as our outcome variable in the context of the same regression-discontinuity framework of Eq. (1). We find some evidence (available upon request) of increases in the (log) duration of employment spells, of between 10 to 20%, even if not always significant. This result is consistent with our previous findings of no significant effects upon employment status in 2012 for the full sample (in contrast to the specific case of younger workers) but increased inter-firm mobility. In other words, as workers move less between firms, they also spend less time unemployed in between spells.

Finally, we conduct one additional extension, in which we exploit the availability in our data of information on both FTC and permanent contracts, as well as each worker's firm identity. One possible, even if unlikely, threat to identification may involve dif-

¹² Incidentally, the entire sample is equally eligible for unemployment benefits, as they are conditional on 12 to 15 months of employment before job loss, a criterion that all workers considered will already have met by October 2011.

Table 12
Conversion effects – difference-in-differences.

	(1)	(2)	(3)	(4)
FTC	–.558 (.005)***	–.559 (.005)***	–.555 (.005)***	–.485 (.011)***
Longer FTC max duration in force	–.005 (.003)*	–.006 (.003)*	–.006 (.003)*	–.003 (.005)
FTC*Longer FTC max dur	–.033 (.007)***	–.031 (.007)***	–.029 (.007)***	–.051 (.011)***
Worker controls		X	X	X
Firm controls			X	X
Firm fixed effects				X
Obs.	84201	81697	81515	81515
R ²	.276	.287	.293	.761

Notes: The columns present different specifications of a difference-in-differences model. The dependent variable is a dummy variable equal to one if the individual is in a permanent job in (October) 2012. 'FTC' is a dv equal to one for workers under fixed-term contracts in 2011, 'Longer FTC max duration in force' is a dv equal to one for workers hired from February 2009, and 'FTC*Longer FTC max dur' is the interaction (DID) effect of interest. The sample considered includes workers hired between November 2008 and April 2009. Worker controls are a gender dv, age in 2011, hourly total earnings and two schooling dv. Firm controls are sales, equity, number of workers, multi-establishment dv and foreign and public ownership dv's. Significance levels (two-sided tests): * 0.10, ** 0.05, *** 0.01.

Table 13
Firm (job-to-job) mobility effects – difference-in-differences.

	(1)	(2)	(3)	(4)
FTC	.028 (.003)***	.029 (.003)***	.028 (.003)***	.038 (.006)***
Longer FTC max duration in force	.004 (.002)**	.004 (.002)*	.003 (.002)*	–.004 (.003)
FTC*Longer FTC max dur	–.014 (.004)***	–.013 (.004)***	–.012 (.004)***	–.014 (.007)*
Worker controls		X	X	X
Firm controls			X	X
Firm fixed effects				X
Obs.	84201	81697	81515	81515
R ²	.002	.003	.005	.612

Notes: The columns present different specifications of a difference-in-differences model. The dependent variable is a dummy variable equal to one if the individual is in the same firm in (October) 2012, compared to (October) 2011. See more details in notes to Table 12.

ferences across sectors and firms in their economic outlook coupled with different seasonal patterns in middle 2012 compared to late 2011 and early 2012. For instance, workers hired earlier in 2008/9 may tend to be in firms that, on average, face more challenging economic circumstances and are more likely to move to other firms upon job loss. Although this interpretation of our results may be too extreme and, in any case, largely addressed by a regression discontinuity approach, we test it using a difference-in-differences setup, using data on both FTCs and permanent workers. Our assumption here is that FTCs and permanent workers will be exposed in a similar way, in relative terms, to the business cycle in each firm, so that any resulting differences in the outcomes of interest will be driven by the new FTC law.

Given the above, the difference-in-differences equation we consider is the following:

$$Y_i = \beta_1 FTC_i + \beta_2 D_i + \beta_3 FTC_i * D_i + \beta_4 X_i + \beta_5 F_i + \alpha_i + \varepsilon_i \quad (2)$$

The dependent variable considered, Y_i , is a dummy variable referring to conversion (or, more generally, permanent employment status) in 2012, or mobility to a different firm, always comparing 2011 and 2012 (October in both cases); D_i is a dummy variable equal to one for individuals hired from February 2009; and FTC_i is a dummy variable equal to one for individuals under a FTC in October 2011. Depending on the specification, we also consider worker controls (X_i), firm controls (F_i), and firm fixed effects (α_i). To increase the comparability of the two groups of workers, given the lack of a running variable in this difference-in-differences model, we restrict the analysis to the hiring period November 2008 to April 2009.

Table 12 presents the results regarding conversion effects, where we again find evidence of considerable take-up. The inter-

action coefficients range between –.029 and –.051, the latter in the case of the specification including firm fixed effects. Moreover, as in the regression-discontinuity approach, we do not find large significant employment effects for the full sample (unlike in the case of young workers), despite positive coefficients (results available upon request). However, we also find supporting evidence of negative effects on worker mobility – Table 13. In particular, the coefficients of the interaction variable are always significantly negative, ranging between –.013 and –.02. If anything, the inclusion of firm fixed effects (i.e. potentially comparing workers hired at similar times by the same firms but in either FTCs or permanent contracts in October 2011) increases the magnitude of the coefficients (in absolute terms). The four estimates are particularly similar to the two significant coefficients presented in Table 4, –.013 and –.015. It is also interesting to note that, as expected, the coefficients on FTCs are statistically and economically significantly negative, while the coefficients on later hiring are very small and either positive or negative. All these difference-in-differences results are also robust to small changes in the range of the window adopted.

6. Conclusions

Academics and policy makers exert great effort in understanding and minimising the negative employment effects of business cycles. This paper evaluates one specific but widely applicable measure in this regard, namely introducing some degree of responsiveness in the maximum duration of fixed term contracts (FTCs) to labour market conditions. The simple rationale of the measure is that, when faced with an uncertain economic outlook (and particularly in a context of restrictive permanent contracts), firms may be

more likely to dismiss workers in FTCs if the only legal alternative is to convert them. By allowing more time, during recessions, until this 'in or out' decision becomes fully binding, increased employment and or reduced worker turnover may follow.

The empirical evidence that we contribute to this question is based on the evaluation of the effects of a law introduced in Portugal, during the 2012 recession, which increased the maximum duration of FTCs from three to four and a half years, but only for workers hired from a specific date. Specifically, we exploit the sharp differences in the possibility to renew FTCs introduced by the law, between workers hired just before or after a specific month three years before the law was introduced. Our analysis is based on regression-discontinuity (and difference-in-differences) methods and matched employer-employee panel data that covers virtually all eligible workers.

We find a considerable take up of this measure, as conversions to permanent (open-ended) contracts drop by 20%. However, we do not detect significant short-term effects on overall employment, except in the important case of young workers. The lack of large effects for the full sample is possibly because data limitations generate attenuation bias (some individuals considered as treated may actually not be eligible for an FTC extension) and prevent us from considering the lower-tenure workers (for whom this employment margin may be more sensitive). On the other hand, and despite the data issues above, we find that worker churning is reduced significantly, as mobility of eligible fixed-term workers to other firms drops by 10%. The two results (on employment and mobility) can be reconciled through relatively good employment opportunities in other firms for non-eligible workers in our sample. The findings also imply a negative effect on unemployment spell durations between jobs, i.e. the law leads to longer employment spells, which can lead to higher total labour income.

In conclusion, we find that longer, more flexible FTCs can promote employment, at least in recessions. This is the case at least for the young and more generally in terms of reduced worker mobility and longer matches, even if at the cost of fewer conversions. Our findings highlight the potential of greater flexibility in the legal parameters of FTCs – and possibly other labour market regulations and institutions (not only unemployment benefits but possibly also tax wedges, activation practices, minimum wages, severance pay, etc) – over the business cycle as a tool to minimise employment fluctuations. Such rules in labour market policy making could successfully complement those in place in macroeconomics Taylor (1993), especially when countries face constraints in their monetary and fiscal countercyclical policies.

Declaration of interests

None.

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