Sustaining growth to benefit all in Spain

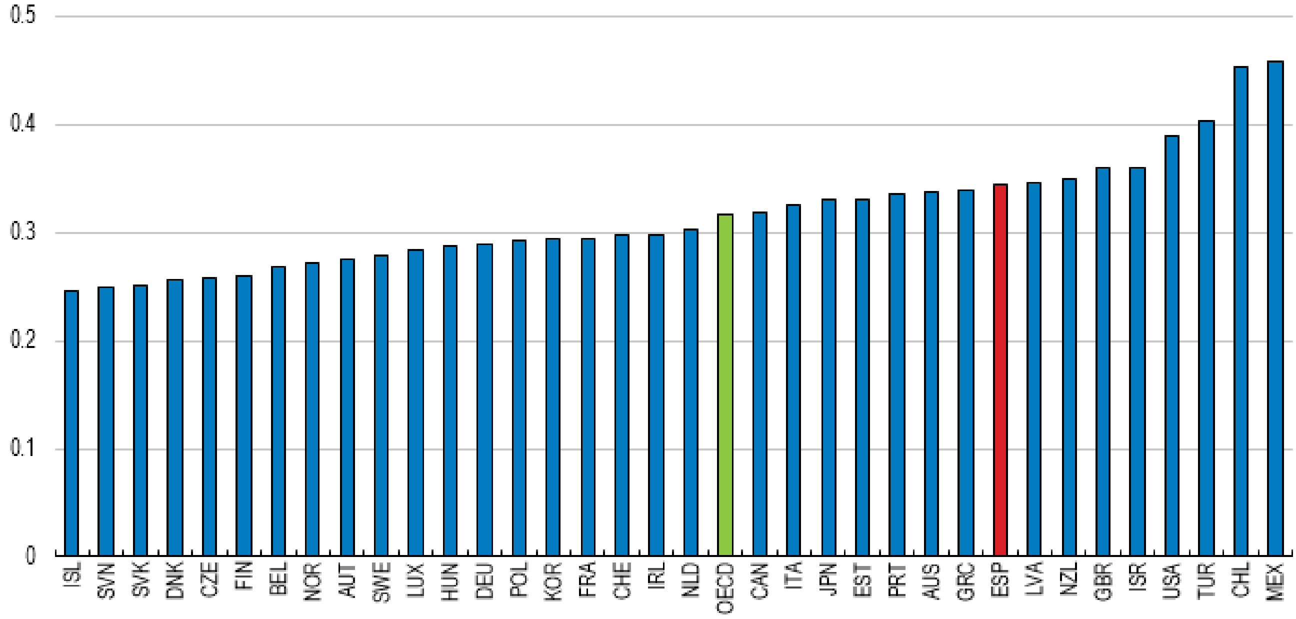
By David Law, Spain desk, OECD Economics Department

Spain continues to recover from the economic crisis with strong growth and falling unemployment, as highlighted in the latest OECD Economic Survey of Spain (OECD, 2018). If the recovery is to be sustained, it is vital that the benefits of economic growth are shared as high rates of income and wealth inequality can harm economic growth and productivity, and limit productive investment opportunities.

Income inequality is relatively high in Spain (Figure 1) and it increased during the crisis, as employment fell significantly and income disparity grew. The risk of being in poverty now varies greatly across regions and the rate of child poverty is particularly high, at 22% in 2015, which is well above the OECD average of 13%. The risk of poverty is especially high for children living in migrant and single parent families. With some positive developments in the labour market since 2015, income inequality and poverty rates are likely to have improved somewhat, however, these issues are expected to remain a concern for some time.

Figure 1: Income inequality is high

Gini coefficient after taxes and transfers, 2015 or latest year available



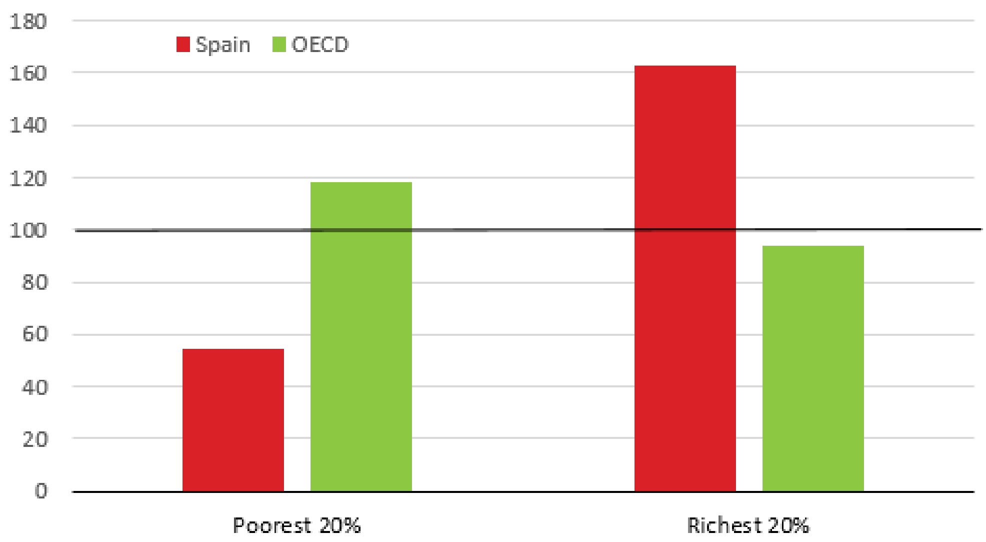
Note: The Gini coefficient has a range from zero (when everybody has identical incomes) to one (when all income goes to only one person). Increasing values of the Gini coefficient thus indicate higher inequality in the distribution of income.
Source: OECD, Income Distribution and Poverty (database).

Wealth inequality in Spain appears relatively low in international perspective, reflecting high rates of home ownership. However, as is the case in other countries, wealth inequality is higher than income inequality with the top 10% of households holding close to half of all wealth, compared to around one fifth for the bottom 60% of households. Wealth inequality seems likely to rise over time, given changes in the distribution of income and recent labour market trends. Indeed, new work undertaken by the OECD using household survey data shows that wealth inequality already increased between 2011 and 2014 in Spain, and that the income and wealth mobility of households exhibit a degree of persistence, which can exacerbate inequalities (Martinez-Toledano et al., forthcoming).

The tax and transfer system in Spain could do more to tackle inequality. Low-income households receive less cash transfers than higher-income ones, with those in the bottom 20% of the income distribution receiving only around 55% of the average payment across all families, compared to the top 20% receiving over 60% more than the average family (Figure 2). Better targeting of transfers, so more is received by those who need them the most, would reduce inequality. Additionally, the 2018 OECD Economic Survey of Spain notes the burden the tax system places on labour taxation and recommends that regressive reduced value-added tax rates be abolished and that the tax allowances granted for inheritance taxes for the most wealthy are reconsidered.

Figure 2: Social expenditures are poorly targeted

Transfers received by working-age individuals, % of average cash transfer



Note: Public social cash transfers are at the household level, adjusted for household size. Income groups refer to disposable incomes.
Source: OECD, Social Expenditure Database.

Reducing inequality in the long-run will also require sustained improvement in labour market outcomes. For instance, in 2017, unemployment among the young was 38.6%, long term unemployment as a share of the labour force was 7.7% and 27% of workers were on temporary contracts. The [2018 OECD Economic Survey of Spain] makes a number of recommendations in this regard. For example, the Survey recommends increasing spending on training and job search assistance, the introduction of a profiling tool to adapt active labour market programmes to the needs of individual workers, and measures to boost the labour market participation of women, such as extending the provision of early childhood education. The Survey also discusses the role that targeted reductions in social security contributions could play in improving labour market outcomes for low wage workers and the benefits of greater use of firm-level collective agreements, and recommends continuing efforts to fight against the abuse of temporary contracts to reduce labour market duality.

References

OECD (2018), *OECD Economic Surveys: Spain 2018*, OECD Publishing, Paris. https://doi.org/10.1787/eco_surveys-esp-2018-en.

Martínez-Toledano, C., D. Law, D. Haugh and M. Adalet McGowan (forthcoming), "The Business Cycle and Wealth and Income Mobility in Spain", *OECD Economics Department Working Papers*, forthcoming.

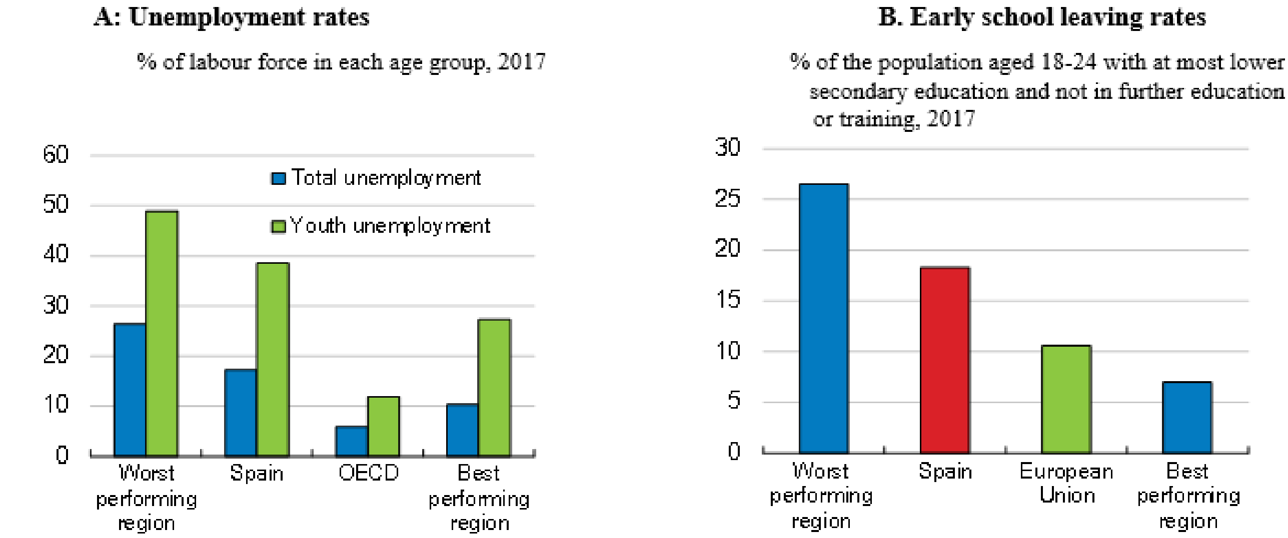
Reducing regional disparities for inclusive growth

By Müge Adalet McGowan, Spain desk, OECD Economics Department

Ensuring the benefits of growth are spread widely requires a strong focus on greater convergence of regions in terms of income and well-being. The GDP per capita in the best performing region was around double that in the worst performing region in 2016. Income inequality and poverty rates are also high, with regional differences.

High regional dispersion in education and job outcomes, compounded by low inter-regional mobility, emerge as key drivers of regional inequalities in income and well-being (Figure 1). At the same time, productivity growth has stagnated in Spain (Figure 2). Barriers to achieving a truly single market limit productivity growth of regions, including the most advanced. Hence, the 2018 OECD Economic Survey of Spain highlights that a dual approach of enhancing both the productive and employment capacities of lagging regions is needed (OECD, 2018). Reducing regional disparities will also depend on effective coordination and sharing of best practices across regions.

Figure 1. Regional dispersion of labour market and education outcomes is high



Source: OECD, Labour and Regional Statistics and Eurostat.

Stronger coordination between employment and social services is key to providing effective transitions between social support schemes and employment, given the multiple barriers that the unemployed might face (Fernandez et al., 2018). Improving coordination to provide integrated support for jobseekers *via* a single point of contact for social and employment services and assistance would improve the effectiveness of such policies.

Lack of full portability of social and housing rights across regions, due to prior residency requirements, contributes to low labour mobility. The [2018 OECD Economic Survey of Spain] recommends ensuring full portability of these benefits across regions, by providing temporary assistance either by the region of origin or the central government.

Increasing the quality of education would improve the employability of the labour force in lagging regions and should be complemented with policies to raise job quality in regions with low-skilled jobs. For example, providing individualised support to students at the risk of failing at an early stage has contributed to lower early school leaving rates in some regions. Increasing the adaptability of workers, *via* lifelong learning policies better targeting the participation of low-qualified adults, would improve the matching of skills to labour market needs.

Reducing regional regulatory differences is key to achieving a truly single market and firm growth. The 2018 OECD Economic Survey of Spain recommends strengthening the implementation of Market Unity Law through enhanced cooperation and coordination across different levels of government and the assessment of the compliance of new legislation at all levels of government with the principles of the Market Unity Law. Removing the remaining barriers in some professional services would also improve competition and boost productivity.

References:

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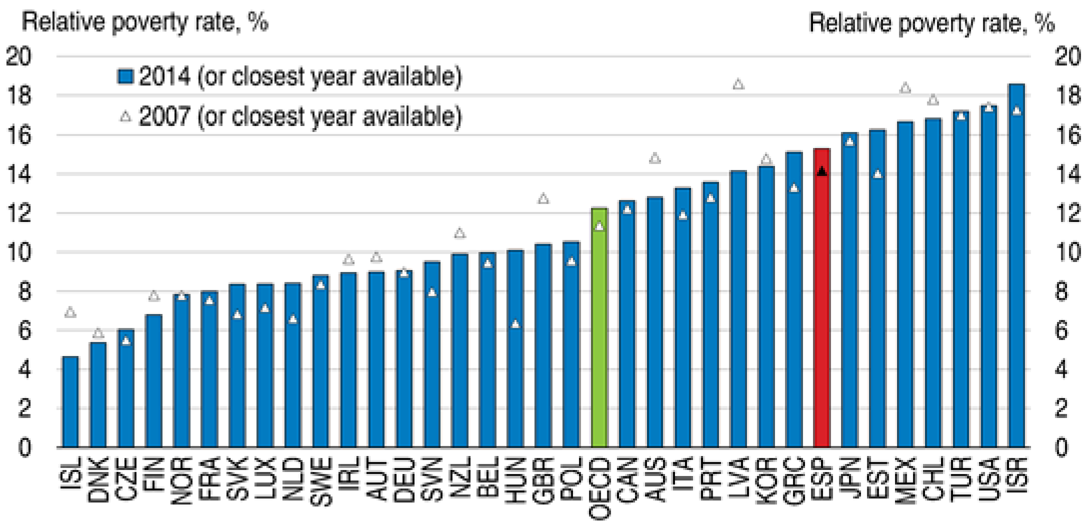
Reducing poverty durably is a key challenge in Spain

By Yosuke Jin, Spain Desk, Country Studies Branch, OECD Economics Department

Poverty has risen in Spain in the wake of the crisis (Figure 1), mainly due to lack of quality jobs that provide enough hours of paid work to support decent incomes (OECD, 2017). The risk of poverty is concentrated on jobless households and households with only temporary workers (OECD, 2015). As employment has grown strongly over the past three years, poverty is likely to have declined. However, the level of poverty is also likely to remain high as the unemployment rate still stands at around 19% and a quarter of those who are employed are on temporary jobs. The risk of poverty is particularly intensified among jobless households with children.

Figure 1. Poverty increased during the crisis



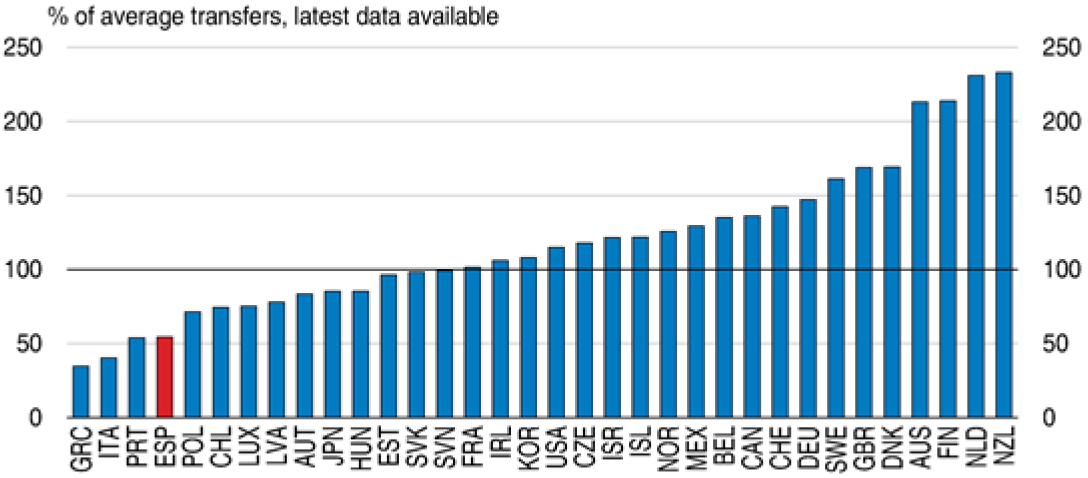
Note: The relative poverty rate is defined as the share of people living with less than 50% of the median disposable income (adjusted for family size and after taxes and transfers) of the entire population. The OECD aggregate is calculated as an unweighted average of the data shown.

Source: Provisional data from the OECD Income Distribution Database.

The tax and transfer system could do more to relieve poverty. Total social spending as a percentage of GDP is higher in Spain than the OECD average. However, social benefits are poorly targeted with relatively well-off households benefiting more than the poor. Cash transfers are particularly low at the bottom 20% of the income distribution (Figure 2), as less than half of the unemployed are covered by unemployment benefits and minimum-income safety nets are weak (OECD, 2017).

Figure 2. Transfers for the poor are very low

Cash transfers to working age individuals in 20% lowest income group



Note: Public social cash transfers at the household level, adjusted for household size.

Source: Calculations based on the OECD Income Distribution Database.

A substantial number of unemployed people have exhausted their unemployment benefits as their unemployment spell gets longer or are not entitled to them at all. This is particularly the case for those who separate from temporary contracts due to very short contribution periods in the social security system. The 2017 OECD Economic Survey on Spain recommends extending the coverage of the standard unemployment benefit by reducing its minimum required contribution period, in line with many other EU countries (OECD, 2017).

The minimum income support provided by safety nets is weak and its coverage is very limited. Social protection in Spain consists not only of the unemployment insurance system managed by the central government, but also of minimum income support schemes run by the central and regional authorities. Only 1.5% of households received minimum income support in 2014 from the regional schemes. The *Renta Minima de Insercion* (RMI) is the most common income support scheme for those who are not eligible for unemployment benefits, aimed at alleviating poverty by means of cash benefits for basic living needs. For those who do receive the RMI, the benefit amount is low compared with similar social assistance in other OECD countries, in particular for those with children due to weak top-ups for children. The Economic Survey recommends increasing the amount and coverage of the regional minimum income support programmes, in particular, for families with children (OECD, 2017).

While improving the coverage of social protection, the benefits should be strictly conditional on active job search. This would not only provide immediate income support but also allow benefit recipients to stay connected to the labour market, as long as relevant employment support measures are put in place. From this perspective, the Economic Survey also discusses the importance of improving the efficiency of public employment services by: employing profiling tools and specialisation of counsellors; increasing resources and staff-to-job seeker ratios; and improving co-ordination to provide integrated support for jobseekers via a single point of contact for social and employment services and assistance (OECD, 2017).

References

OECD (2015), In It Together: Why Less Inequality Benefits All, OECD Publishing, Paris.

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Fiscal policy in the euro area: in the current juncture, don’t apply sanctions

By Alvaro Pina, Head of European Union and Euro Area Desk, Country Studies Branch, OECD Economics Department

Tomorrow the European Commission will assess again the fiscal situation of Portugal and Spain, and decide whether to recommend to the Council that the Excessive Deficit Procedure be stepped up for those countries, exposing them to various sanctions. This momentous decision can have major consequences for the countries concerned, but also wider implications. It sets a landmark in the application of the Stability and Growth Pact rules, and therefore begs the question of how best those rules should be applied, especially in the current juncture of weak growth in Europe. In turn, this question hinges on what fiscal policies should do to support the recovery more. The recent OECD Survey of the Euro Area provides analysis on what should be done.

Growth has picked up gradually over the past two years, but demand is still weak and unemployment remains very high in several countries, including Portugal and Spain. In the euro area as a whole, support to the recovery has essentially come from monetary policy, with little or no fiscal help. After three years (2011-13) of strong and widespread fiscal consolidation, fiscal policy has turned broadly neutral (Figure 1), but it needs to go further in supporting demand as monetary policy alone cannot do everything. Budget support should mainly come from countries with fiscal space. Those without, like Portugal and Spain, should nonetheless avoid a return to austerity.

Figure 1. Euro area fiscal stance[1]

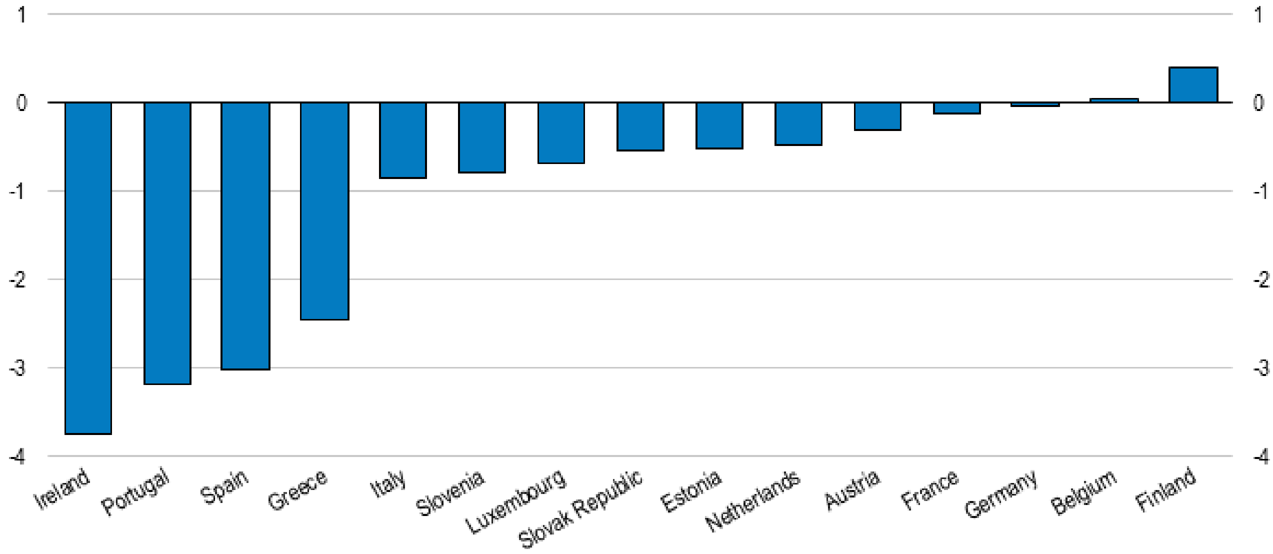
Change in the underlying balance as a share of potential GDP, percentage points

1. Euro area member countries that are also members of the OECD (15 countries).
Source: OECD (2016), "OECD Economic Outlook No. 99", *OECD Economic Outlook: Statistics and Projections* (database), June.

To maximise growth impacts and make them lasting, budget support should be targeted. Post-crisis consolidation often led to increases in labour taxes and large reductions in public investment (Figure 2), making public finances less growth-friendly. Policy levers to improve the composition and efficiency of public spending and taxes remain largely at national level, and progress on this front across the euro area has been insufficient. But European sanctions could make matters worse. For instance, they would likely imply a suspension (even if only temporary) of structural funds to the countries concerned, putting further downward pressure on public investment.

Figure 2. Change in public investment over recent fiscal consolidation episodes[1]

Percentage points of potential GDP



1. Consolidation episodes considered are those starting in 2009 or later.

Source: See Figure 21 of OECD (2016), *OECD Economic Surveys: Euro Area 2016* for futher details and source information.

In the current juncture, sanctions would be an economic mistake. In the absence of temporary fiscal expansion by countries with enough space, sanctions will somewhat tilt the euro area fiscal stance towards austerity, the opposite of what is needed. Further, they risk inducing further cuts to investment, thus hampering potential growth. Not to mention rekindling political tensions and animosities, again the opposite of what is needed. In a word: don’t.

See also:

OECD (2016), OECD Economic Surveys: Euro Area 2016, OECD Publishing, Paris.