

Child benefits and female labour supply – the case of Poland

Category: Uncategorized

written by oecdecoscope | March 19, 2018

by Nicola Brandt, Polish Desk, OECD Economics Department

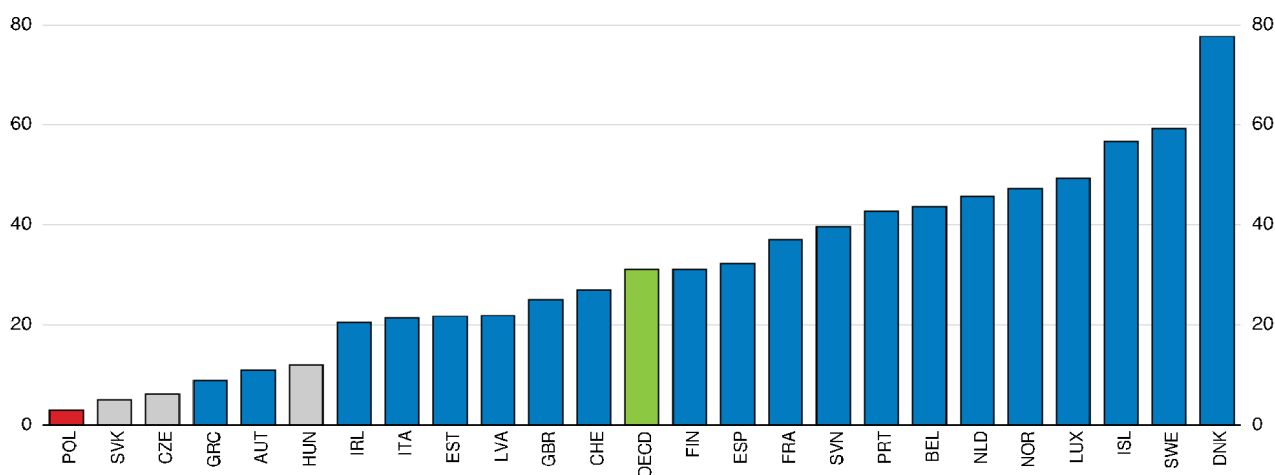
In 2016 the Polish government introduced a large new child benefit, called “Family 500+”, with the aim to increase fertility from a low level and reduce child poverty. The benefit is universal for the second and every further child and means-tested for the first child. It more than doubles fiscal support for families, making Poland one of the top spenders in the EU concerning cash transfers for families.

It is already clear that the benefit helped to materially reduce child poverty. Extreme child poverty dropped by 3 percentage points in 2016 and the effect may well strengthen, as the benefit was paid out only starting in June of that year. It is too early to gauge the effect on births, which have been rising lately, but this could be mainly a result of the booming labour market and rising incomes. Studies for other countries find that generous family benefits can have a positive impact on fertility, although estimated effects differ widely (Brainerd, 2014).

But there may also be undesirable side effects on employment. Evidence from other countries suggests that that there can be negative effects of child benefits on female labour supply, which tend to be greater for women with lower skills (Schirle, 2015; Haan and Wrohlich, 2011). Access to affordable childcare is improving in Poland, but still very limited in many areas, in particular for the smallest children. It is hardly used at all by mothers with less than tertiary education (Figure 1).

In that context child benefits can create disincentives to work for single mothers or second earners with children. This is due to its feature that the benefit is withdrawn at once when per capita family income increases beyond the eligibility ceiling. As an example, the OECD tax-benefit models suggest that an unemployed single mother of two taking up a job that pays the average wage would retain less than 20% of her earnings as a result of taxes and benefit withdrawal. If her only choice is unsubsidised private childcare, she would actually lose money.

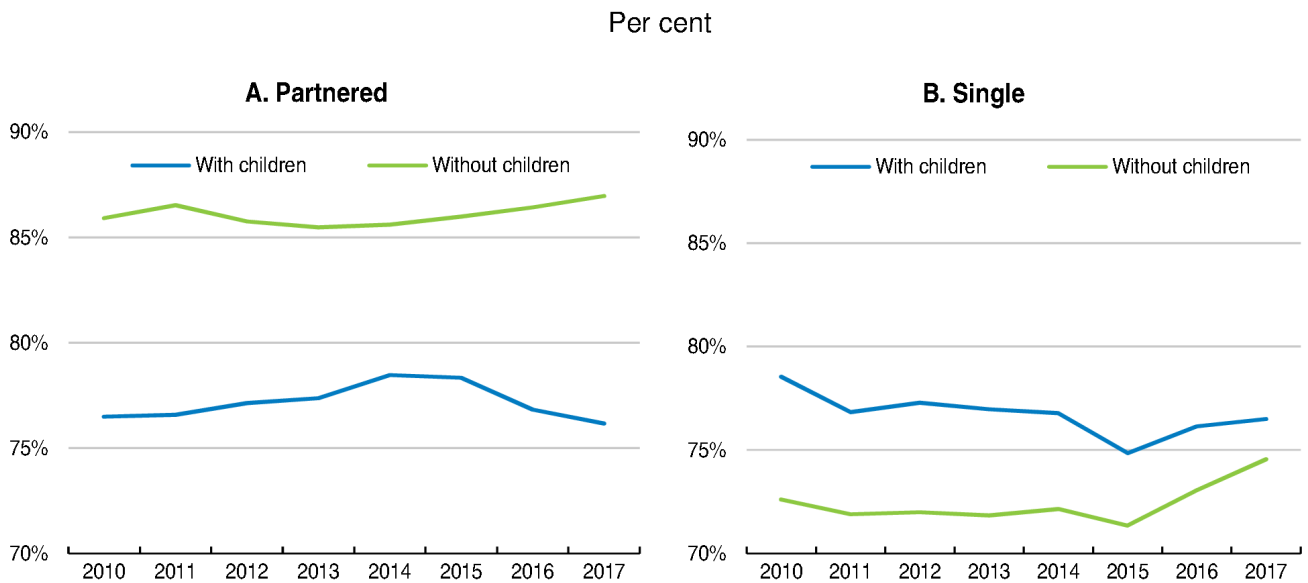
Figure 1. Participation rate in formal childcare
0-2 year olds whose mother has less than tertiary education, per cent



Source: OECD (2017), *OECD Family Statistics* (database).

Joint research by the Institute for Structural Research (IBS) in Warsaw and the OECD finds that the introduction of the child benefit has indeed had a negative effect on labour force participation and employment of mothers. The study compares labour force participation trends for mothers of up to two children and childless women, differentiating between single and partnered women, as female labour supply is thought to be influenced by the presence of a partner. Figure 2 shows that while in each subgroup labour force participation trends were similar for mothers and childless women prior to the introduction of the child benefit, they started to diverge markedly after that. For partnered mothers, labour force participation actually fell.

Figure 2. Labour force participation rates of women aged 20-49 by marital status and presence of children



Source: Own calculations based on EU Labour Force Survey data.

A more formal econometric analysis comparing labour force participation trends across these groups based on a difference-in-differences approach suggests that for both single and partnered mothers labour force participation might have been almost 3 percentage points higher in the absence of the child benefits in the first half of 2017. The analysis also reveals that the effect is strongest for relatively low-qualified mothers with basic vocational education or less.

While this research does imply that large child benefits can affect female labour force participation negatively, there is reason to believe that context and design matter. For example, by withdrawing the benefit for the first child more gradually the government could mitigate negative effects on labour supply. Another solution would be to make the benefit income-dependent for all children, but with a much higher eligibility ceiling as higher-earning mothers' labour supply seems to be less affected by the benefit. Stepping up efforts to quickly extend access to affordable childcare is also likely to reduce any undesirable side effects on female labour supply.

Further reading

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Towards an innovative and inclusive economy in Poland

Category: Labour markets, Poland, Uncategorized

written by oecdecoscope | March 19, 2018

by Nicola Brandt and Pierre Guérin, Poland Desk, OECD Economics Department

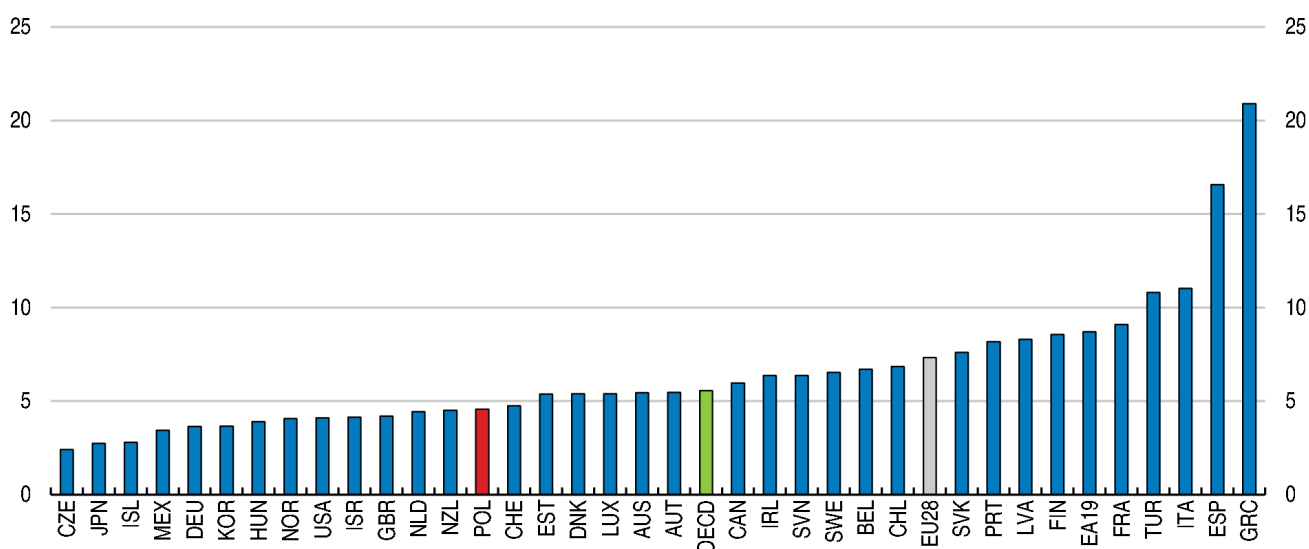
The Polish economy is in a strong position. Economic growth reached 4.6% on average in 2017 and the OECD expects it to continue at around 4% over 2018/19. A good external environment, with a solid recovery in the euro area, and the child benefits introduced in 2016, the “Family 500+” programme, are the main drivers of this strong performance.

Together with a booming labour market, that has brought down the unemployment rate significantly (**Figure 1**), the Family 500 + programme has also helped make economic development more inclusive, as larger parts of the population now benefit from new job opportunities and rising incomes.

In the longer run, there are challenges related to Poland's rapidly ageing population. The recent lowering of the retirement age back to only 60 for women risks weighing on senior employment and growth prospects and heighten risks of old-age poverty, in particular for women with patchy career paths. The OECD Economic Survey of Poland argues that the government needs to step up its efforts to improve currently limited access to affordable childcare services. Insufficient institutional care for the elderly is another barrier to female employment and improved well-being for seniors.

Figure 1. The labour market is tightening

Total unemployment rate (% of labour force), Q4 2017 or latest available



Source: OECD (2018), *Labour Market Statistics* (database), <https://data.oecd.org/unemp/unemployment-rate.htm>

Raising Poland's capacity to innovate in line with the government's Strategy for Responsible Development would help strengthen productivity growth and ensure continued convergence to higher living standards. The envisaged higher education reform with its plans to strengthen the quality of doctoral training and currently weak science-industry cooperation is crucial in this respect, as research quality

and the supply of researchers do not meet top OECD standards, yet. The Economic Survey recommends a continuous increase in funding for higher education and research over time and a better link of academics' career progression with their research and teaching achievements. The new academic exchange agency is an excellent opportunity to strengthen ties to foreign universities and the Polish research diaspora.

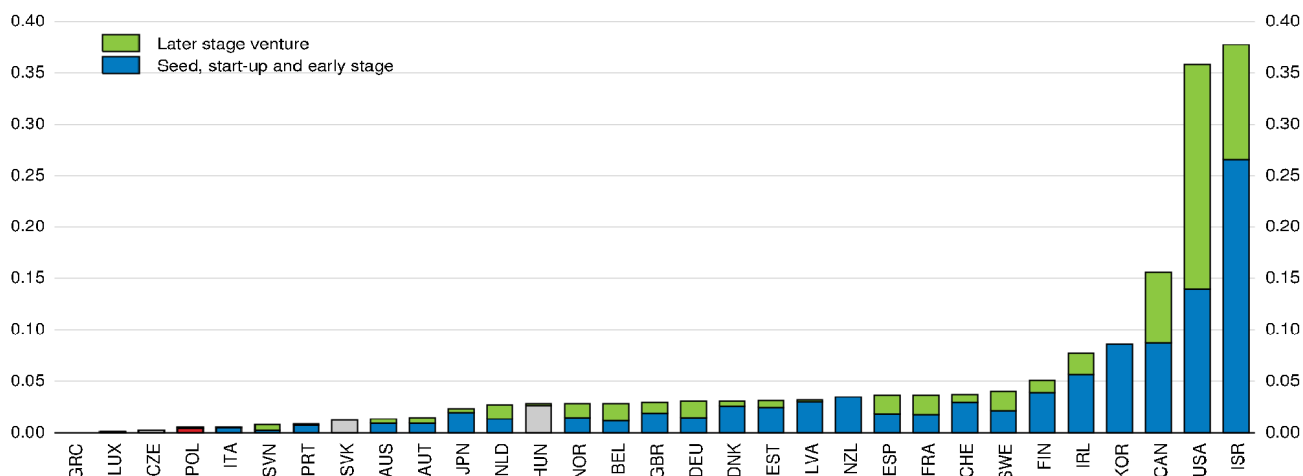
Too many adults have weak basic and digital skills, including managers and tertiary graduates, and vocational training suffers from weak employer engagement and insufficient alignment with labour market needs. Yet, participation in adult training is weak. Developing a national skills strategy with a strong basic skills component and engaging employers to develop more workplace-based vocational education and adult training would boost skills and help secure stronger and more inclusive growth by building the basis for faster productivity gains in Poland's numerous micro-enterprises.

Private-sector R&D spending is low, particularly among SMEs, hindering new technology absorption and innovation. The government has stepped up the previously limited R&D tax relief and strengthened hitherto weak venture capital investments programmes, which can be well-suited for innovative firms engaging in high risk-return projects (**Figure 2**). To ensure the quality of such programmes, it will be important to strengthen impact assessment of public support for innovation. Examples from OECD countries, including Denmark, Australia, the Netherlands and New Zealand, suggest that more systematic private sector involvement into planning and monitoring innovation support programmes can help the government to identify the right policies.

Additional revenues or spending prioritisations are required to finance additional spending in higher education and research, skills, but also infrastructure and health care, and prepare for a possible decline of the availability of EU structural funds for innovation and public infrastructure

programmes. Options include a stronger role for more progressive personal income taxes, more limited reliance on reduced VAT rates, and higher environmental taxes that would generate additional revenues with favourable effects on public health and environmental efficiency.

Figure 2. Boosting finance for innovative start-ups is key
Venture capital investments as a percentage of GDP¹, 2016²



1. Only the value of total venture capital investments is available for Korea and New Zealand.

2. Or latest year available.

Source: OECD (2017), *OECD Entrepreneurship at a Glance 2017*, OECD Publishing, Paris.

Further reading

OECD (2018), *OECD Economic Surveys: Poland 2018*, OECD Publishing, Paris.

http://dx.doi.org/10.1787/eco_surveys-pol-2018-en

The key to breaking cycle of

poverty in Israel lies in education

Category: Israel,Uncategorized

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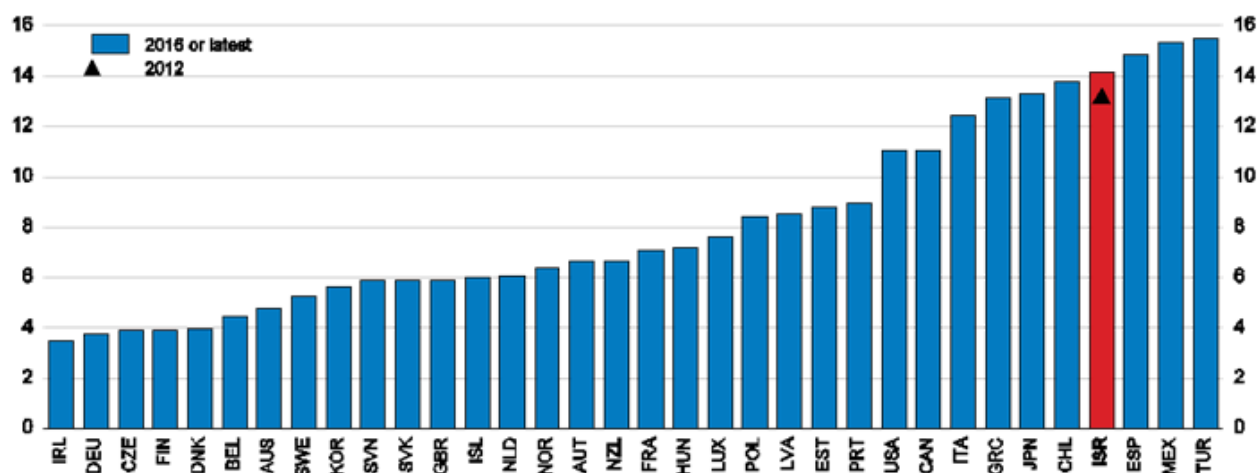
By Gabriel Machlica and Claude Giorno, Israel Desk, Economics Department

Inequality and relative poverty in Israel remain high, particularly among Arab-Israelis and Haredim (Ultra-Orthodox). Israel's social policy follows a "welfare-to-work" approach to tackle poverty in order to avoid measures that may harm work incentives among the Haredi, who value the time dedicated to religious studies, and the Arabs, who have cultural barriers to female employment. The government's strategy of encouraging employment among previously non-working families has met with substantial success. The Israeli labour market has improved markedly, and more and more Haredim and Israeli-Arabs have been able to find jobs. Moreover, the average real income of poor households has risen by almost 3% annually in the last six years, while the average annual real income of wealthier households has increased by only 2.2%.

However, inequalities remain internationally high, and the current strategy without complementary steps has its limits. Many disadvantaged workers have been able to find jobs, but their families remain poor, since in most cases these jobs are low-paid. Indeed, the share of the working poor has risen in recent years and is comparatively high (**Figure 1**).

Figure 1. The share of working poor is high

A. Share of workers in poverty¹

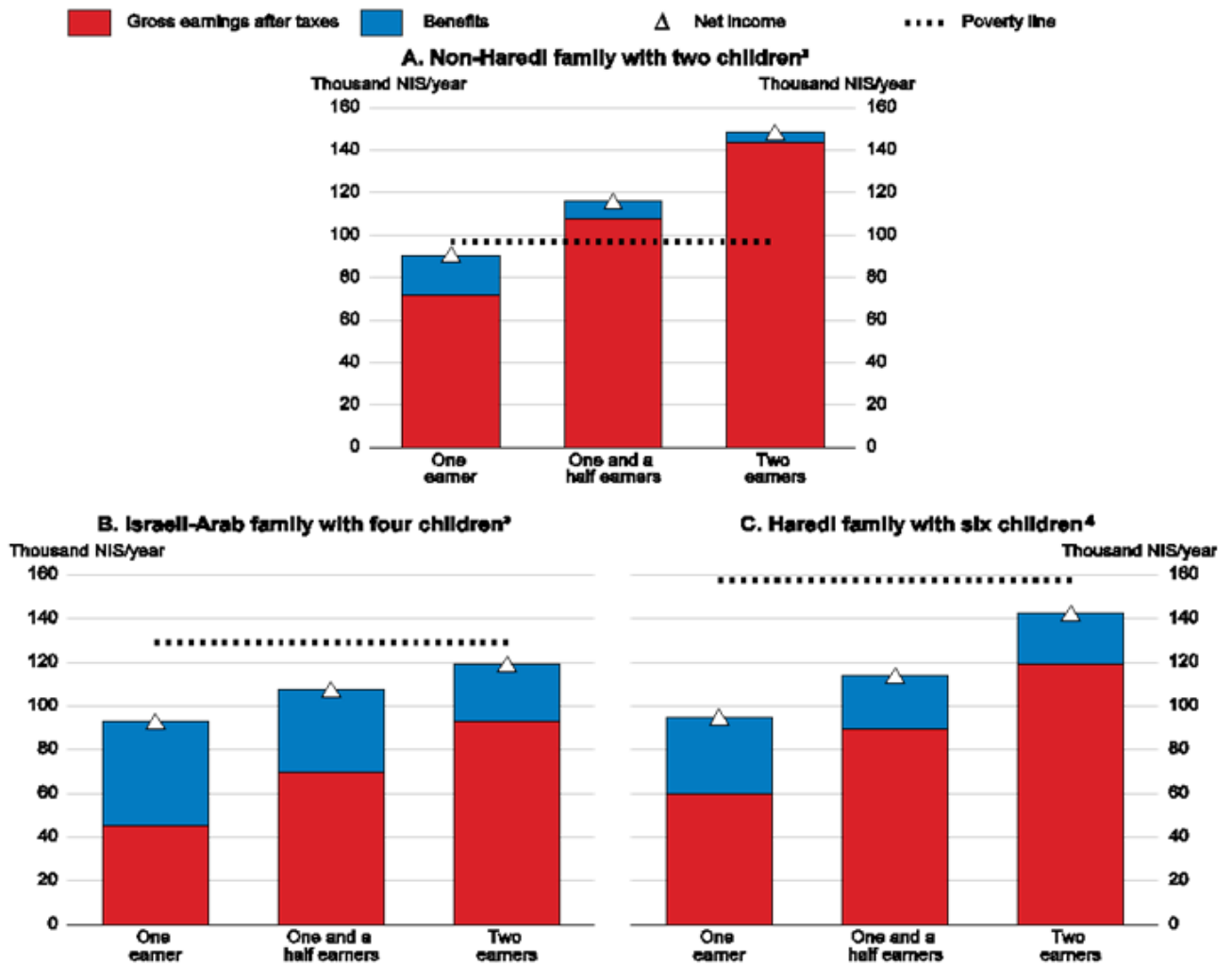


1. Those with income below the poverty line, living in households with a working-age head and at least one worker.
 Source: OECD (2017), *Income Distribution database*; National Insurance Institute

This is particularly true for the Haredim and Israeli-Arabs, who earn on average only 70% and almost 90% of the median hourly wage, respectively, mostly due to the differences in skills and typically have families with only one breadwinner. Given the current tax-transfer system and large number of children in these households, especially in the Haredi community, even two full-time working spouses would not be enough to escape from poverty (**Figure 2**).

Figure 2. Higher employment of Haredim and Israeli-Arabs may not be enough to lift them out of poverty

Estimates of family income according to the numbers of earners and the community group¹



1. One earner corresponds to a family with one earner, one and a half earner corresponds to two-earner family where one works full-time and the second half-time, and two earners corresponds to two-earner family where both work full-time.
2. Workers are assumed to earn 110% of the average wage.
3. Workers are assumed to earn 70% of the average wage.
4. Workers are assumed to earn 90% of the average wage.

Source: OECD calculations using the OECD Tax-Benefit Model. See OECD (2018), OECD Economic Surveys: Israel 2018, OECD Publishing, Paris, http://dx.doi.org/10.1787/eco_surveys-isr-2018-en for more details.

Therefore the current government strategy should be accompanied by additional measures. Extensive poverty in Israeli society is to a significant extent due to the wide dispersion of skills. The government should improve the education outcomes of the disadvantaged groups to boost their future productivity and wages. As the *2018 OECD Survey on Israel* argues, the education system needs to become more inclusive by giving all children opportunities for good-quality education to improve their skills. The government should also focus on programmes for adults who have already

left initial education without proper skills. In addition, it should further expand in-work benefits to boost take-home pay of the average eligible worker.

References:

OECD (2018), OECD Economic Surveys: Israel 2018, OECD Publishing, Paris, http://dx.doi.org/10.1787/eco_surveys-isr-2018-en.

Getting stronger, but tensions are rising

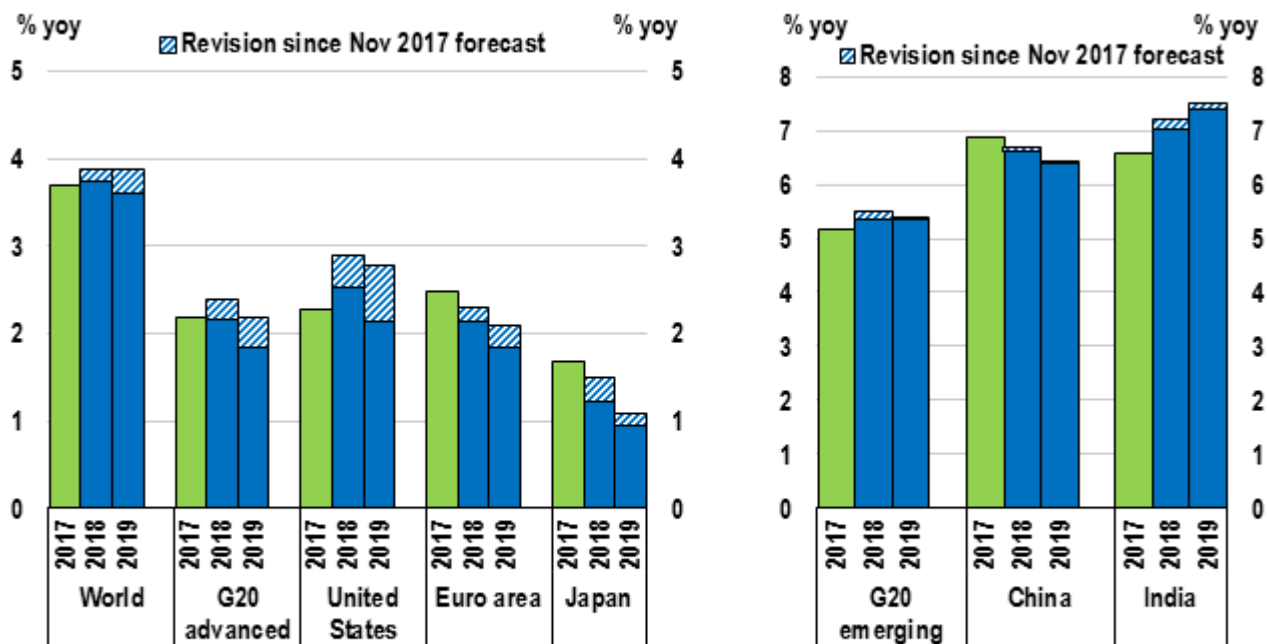
Category: Economic outlook, investment, trade, Uncategorized

written by oecdecoscope | March 19, 2018

By Álvaro Pereira, OECD Acting Chief Economist

The global economic expansion is strengthening. Global growth is projected to increase from 3.7% in 2017 to around 4% in 2018 and 2019 in our latest *Interim Economic Outlook*. In many advanced and emerging G-20 economies, the growth prospects for the next two years have improved. Global trade and investment are growing faster, accompanied by robust job creation. Fiscal stimulus in the United States and Germany will further boost short-term growth. Commodity exporting emerging market economies are recovering on the back of stronger commodity prices and firmer global demand. Inflation remains low, but is likely to rise slowly as labour markets tighten.

GDP growth projections



Note: GDP in volume. Fiscal years starting in April for India. The G20 aggregate does not include EU countries that are not G20 members in own right. G20 emerging includes Argentina, Brazil, China, India, Indonesia, Mexico, Russia, Saudi Arabia, Turkey and South Africa, and G20 advanced includes all other G20 economies.

Source: OECD Economic Outlook database.

This is welcome news. However, there are also new tensions and new policy challenges. As the expansion progresses, monetary policy support will be reduced gradually, albeit at different speeds across major advanced economies. The likelihood of faster hikes in US policy rates has already been reflected in slightly tighter short- and long-term financing conditions. Such policy normalisation is desirable, but could expose financial vulnerabilities from accumulated debt and high asset prices. Rising interest rates could create particular challenges for emerging market economies if capital flows and exchange rates were to become more volatile.

Against the positive background, an escalation of trade tensions is a serious risk. US steel and aluminium tariffs will raise costs and harm consumers, while not solving the global overcapacity problem. Escalation of trade tensions would hurt the recovery. Safeguarding the rules-based international trading system is key.

Policymakers need to make the right choices to sustain medium-

term prosperity and ensure the benefits are fairly shared by workers and households. Fiscal policy, while it remains supportive, should not excessively stimulate demand. Focusing on changes in the tax mix and spending structure holds significant potential to make growth more sustained and more inclusive in the medium term.

Keeping an eye on medium-term goals also means stepping up reform efforts to boost productivity, employment and inclusion. Some countries – Italy, France, Japan, India and Argentina – have implemented significant reforms. However, our forthcoming *Going for Growth* report (to be released on 19 March) shows that in both advanced and emerging economies overall, the pace of structural reform is once again slowing, particularly on the tax and skills policies that are so important to achieving inclusive growth. Political support for reform can dwindle in good times. Yet, good times do provide an opportunity to implement ambitious policies to develop workers' skills, promote competition, and improve the functioning and inclusiveness of labour markets so that living standards rise durably and widely across society.

Reference

OECD Interim Economic Outlook, March 2018.

**United we stand divided we
fall: the need for greater**

inclusiveness in Israel

Category: Israel,Uncategorized

written by oecdecoscope | March 19, 2018

By Claude Giorno and Gabriel Machlica, Israel Desk, Economics Department

The Israeli economy is strong. The country is enjoying its 15th consecutive year of growth, with GDP increasing on average by 4.0% annually since 2003, i.e. faster than nearly any other OECD country. Unemployment is at historically low level, and the average standard of living is improving steadily. Rapid population growth, the rise in people with jobs, strong economic fundamentals, good economic policy settings and a dynamic high-tech sector are underpinning these impressive outcomes, which are expected to continue in the short term, according to the *2018 OECD Survey on Israel*.

Today's excellent outlook offers Israel a unique opportunity to prepare for the challenges of the future which require stronger social cohesion. Israeli society is indeed marked by large inequalities. Almost 18% of the population live in relative poverty (i.e. with a disposable income below 50% of the median), higher than the OECD average (12.5%) and any other advanced economy. This reflects large disparities between different communities. Around half of Israeli-Arabs and Haredim are poor and live separately from the rest of the population. They have different school systems, live mostly in different cities and do not serve in the army. This leads to poor education results followed by worse labour market outcomes, notably in terms of earnings (Table 1). Haredi men have a cultural preference to engage in full-time religious studies, rather than participate in the labour market, and avoid core subjects in their school careers. Furthermore, Haredi women can work only part-time because of their large families. The majority of Israeli-Arab women also do not participate in the labour market due to cultural preferences.

The result is that most Haredi and Arab families have only one breadwinner, resulting in significant problems of poverty, notably among children.

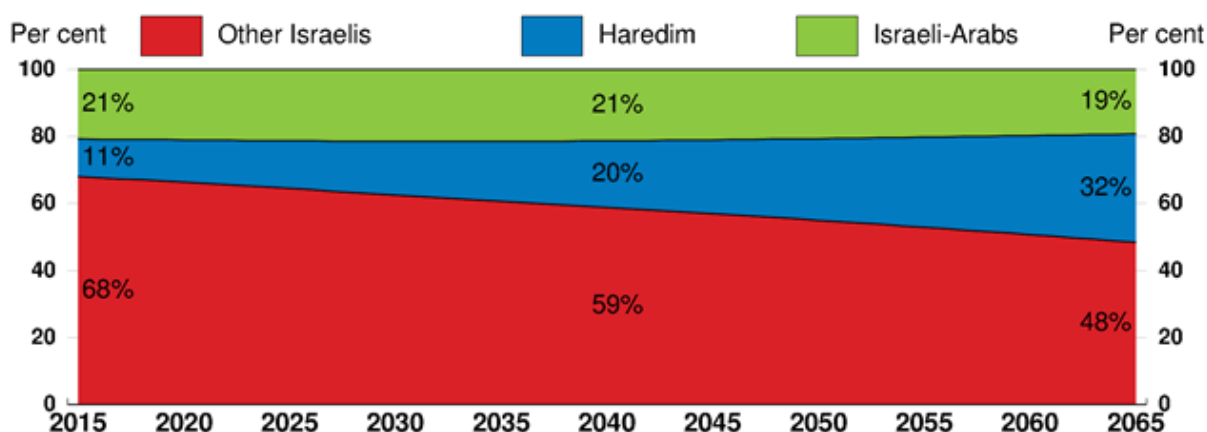
Table 1. Disparities in Israeli society

	Israeli-Arabs	Haredim	Others
Share of the population - 2016 (%)	21	11	68
Fertility rate - 2016	3.1	6.7	2.5
Number of children per household	4	6.5	2
Median hourly wage as a % of the national median hourly wage - 2015	70	87	109
Median wage as a % of the national median wage - 2015	74	68	111
Participation rate - 2016 (%)	58	66	81
PISA mean mathematics scores - 2015	391	-	495
Relative poverty rates – 2015 (%)	53.3	48.7	13.5

Source: National Insurance Institute (2016), *Poverty and Social Gaps Report, 2015*; OECD, *PISA database*; Central Bureau of Statistics.

Given the high fertility of Haredi women, the share of that community in the total population is predicted to triple in the next 45 to 50 years, with the total share of Israeli-Arabs and Haredim rising from one-third to one-half over this period (**Figure 1**). This will have a substantial impact on Israeli economic performance, given the poor labour market outcomes and low productivity of these disadvantaged groups.

Figure 1. Demographic trend by community group

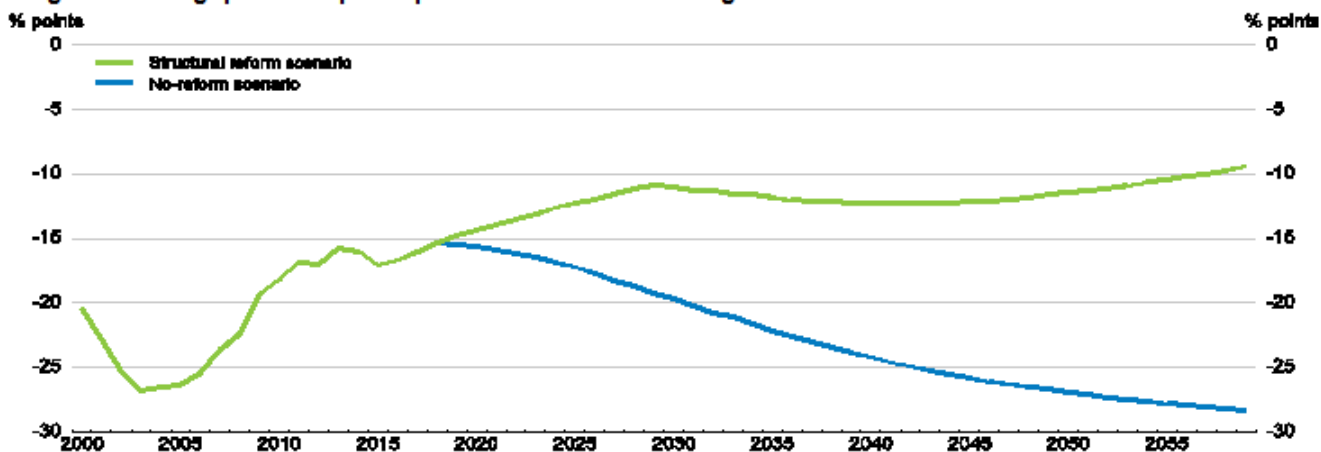


Source: Central Bureau of Statistics, http://www.cbs.gov.il/reader/newhodaot/tables_template_eng.html?hoda=201701138

In the absence of further progress in social cohesion and any further convergence of productivity and labour market outcomes of Haredim and Israeli-Arabs with the rest of the population, average Israeli incomes would fall to nearly 30% below the OECD average, almost double the current gap according to OECD

estimates (**Figure 2**). However, if ambitious structural reforms are launched to further improve the Haredi and Israeli-Arabs' (youth in particular) integration into society through better education and training, improved work incentives and more business-friendly environment, the gap in Israeli living standards with the OECD average could shrink below 10%.

Figure 2. The gap in GDP per capita with the OECD average could shrink further with ambitious reforms¹



1. The no-reform scenario extrapolates OECD short term projections using Geva (2015) and assuming no convergence of Haredim and Israeli-Arabs productivity and labour market outcomes with the rest of the population. By contrast, the structural reform scenario assumes gains from reforms in product market and education with enhanced incentives to join the labour market. In this scenario, the productivity of Haredim and Israeli-Arabs compared to non-Haredi Jews is assumed to increase from 60% currently to 80% and their employment rate to be close to the level of non-Haredi Jews in 2059.

Source: OECD (2017), *Economic Outlook 102 database*; A. Geva (2015), *Demographic Changes and their Implications for Fiscal Aggregates in the Years of 2015-2059*. For more details see OECD (2018), *OECD Economic Surveys: Israel 2018*, OECD Publishing, Paris, http://dx.doi.org/10.1787/eco_surveys-isr-2018-en.

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How do you improve the durability of a Celtic Tiger?

Category: Ireland, Uncategorized

written by oecdecoscope | March 19, 2018

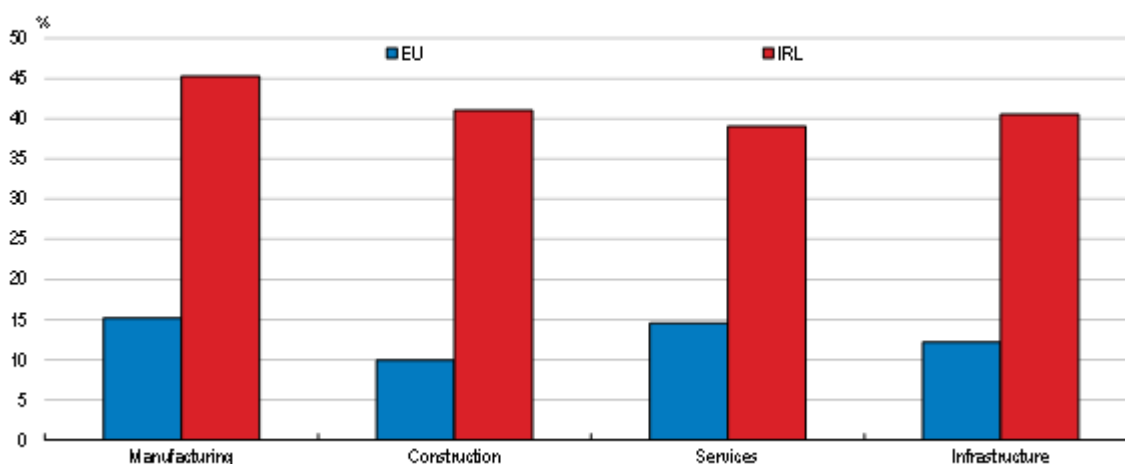
By Ben Westmore and Yosuke Jin, Ireland Desk, Economics Department

The Irish economy is booming and is expected to continue expanding at healthy rates over the next few years. But as the 2018 OECD Economic Survey of Ireland highlights, the outlook is clouded with uncertainty.

Brexit could have serious implications for the Irish economy given the close economic relationship between Ireland and the UK (Figure 1). New OECD estimates suggest that a trade arrangement between the UK and EU governed by the World Trade Organisation's Most-Favoured Nation Rules would reduce total Irish exports by 20% in some sectors such as agriculture and food.

Figure 1. Brexit uncertainty is impacting upon the Irish economy

Proportion of firms expecting a negative impact from Brexit.



Source: EIB Investment Survey.

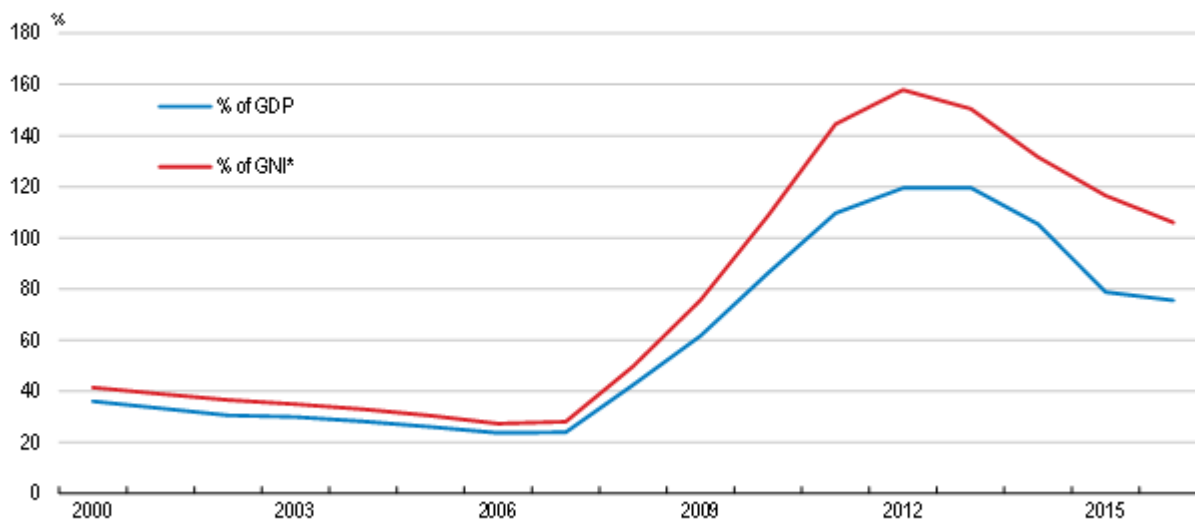
In addition to Brexit risks, rising international tax competition is a concern for Ireland. The Irish economy has been highly successful at attracting foreign direct

investment, with foreign-owned firms accounting for close to half the country's gross value added over recent years. As a result, reductions in effective corporate tax rates in other countries may have a negative impact on the Irish economy if they encourage some multinational firms to relocate their operations elsewhere.

In this context, the importance of raising the resilience of the Irish economy cannot be overstated.

Public finances have improved noticeably, but government debt remains high and tax receipts have become more subject to volatility (Figure 2). Further reducing public debt would create scope for budgetary policy to support the economy in the event of a negative shock – such as a disorderly Brexit. This could be achieved by broadening the tax base in a growth-friendly way. For example, VAT preferential rates and exemptions should be phased out and the property tax yield raised through more regular revaluations of the tax base.

Figure 2. Gross government debt ratios are declining but remain high



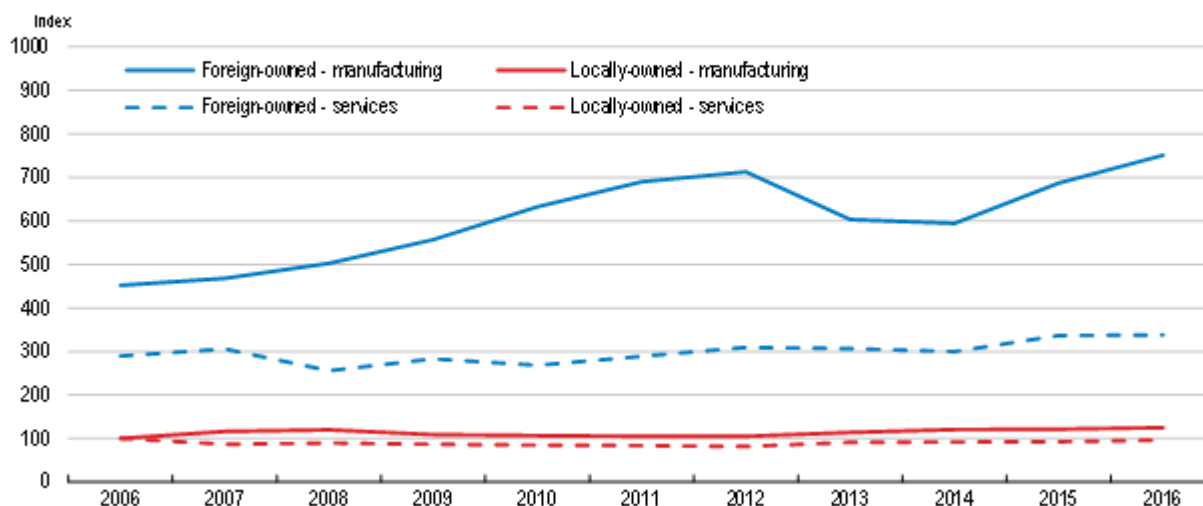
Source: Central Statistics Office and OECD.

Financial sector vulnerabilities also need to be further addressed. While non-performing loans on bank balance sheets have declined by around 60% from their peak, the stock remains high. Measures that reduce judicial inefficiencies relating to

the repossession of collateral and further encourage NPL write-offs will promote the efficient allocation of capital as well the ability of the banking sector to withstand any further adverse economic shocks.

Above all else, the long-term durability of the Irish economy will rely on policy reforms that encourage a broad-based recovery in productivity. Most Irish firms have experienced declining productivity over the past decade. This has largely reflected the poor performance of local firms, with the large productivity gap between foreign-owned and local enterprises having widened (Figure 3). New firm level analysis undertaken in tandem with this *Economic Survey* confirms this is the case (Department of Finance, 2018; the findings of this work will be discussed in more detail in a blog post over the coming days). The resilience of the Irish economy hinges on unblocking the productivity potential of these local businesses. Pruning back regulatory barriers to entrepreneurship, such as costly regulations related to commercial property and legal services, is a start. However, productivity spillovers between foreign-owned firms and local businesses also need to be fostered by encouraging the accumulation of high-level managerial skills and research and development intensity in the latter.

Figure 3. The large productivity gap has widened
Labour productivity index (Irish firms in 2006=100)



Source: Department of Business, Enterprise and Innovation.

Creating a more sustainable growth environment will raise the ability of policymakers to confront key challenges that exist for the wellbeing of the population. Particular areas that should be a focus include health, housing and getting people into work. To address these challenges, universal healthcare coverage should be provided, stringent housing regulations that are constraining dwelling supply rationalised and some social benefits withdrawn more gradually as labour earnings rise.

References

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South Africa: it is time to rekindle the economy

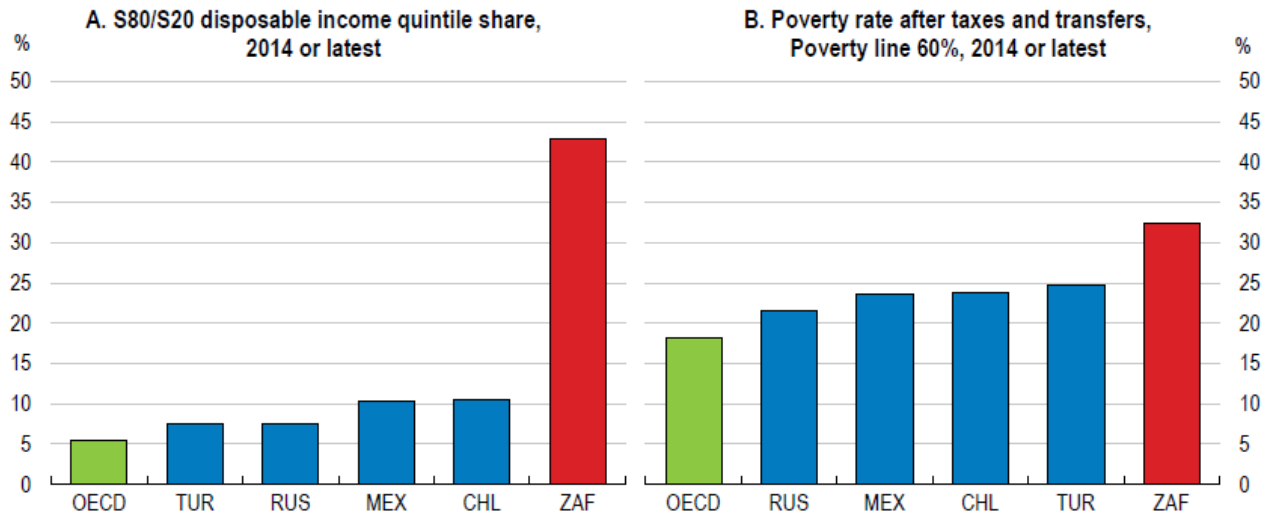
Category: South Africa, Uncategorized

written by oecdecoscope | March 19, 2018

By Falilou Fall, Head of South Africa Desk, OECD Economics Department

Growth is recovering but inequality remains persistent. Growth is projected to reach 1.5% in 2018 after many years below one percent or negative in per capita terms. Low growth and high unemployment have adversely affected the well-being of South Africans. Since 2010, inequality, measured by the Gini coefficient at 0.62, has almost stagnated withering the social contract in a context of policy mistrust (Figure 1).

Figure 1. Poverty and inequality are high

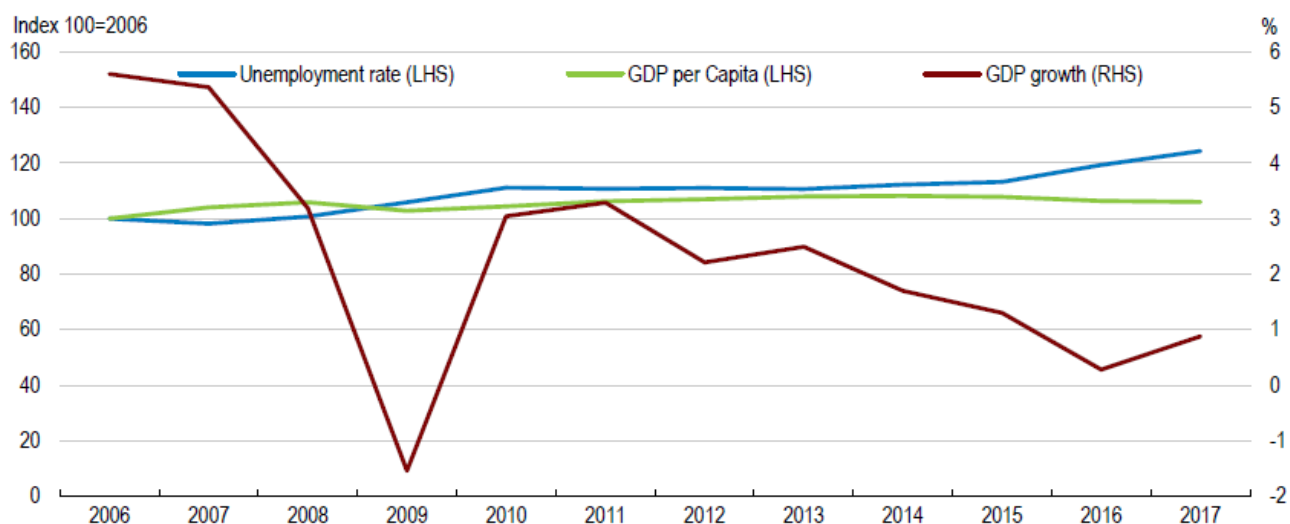


Source: OECD Income distribution and poverty database.

As pointed out by the 2017 OECD Economic Survey of South Africa, the weak growth reflects lacklustre investment and continued low business confidence and the impact of high unemployment, moderate wage increases and persistent indebtedness on sluggish household consumption (Figure 2).

Low growth and weak fiscal discipline contributed to rising public debt burden – from 41% in 2012 to 53% of GDP in 2017. The shortfalls in meeting fiscal objectives, policy uncertainty and corruption concerns in turn led to the downgrading of the government bond ratings to sub-investment level by two major rating agencies in 2017. This makes it harder to meet the large social needs of much of the population.

Figure 2. GDP per capita has been falling



Source: OECD, Economic Outlook Database.

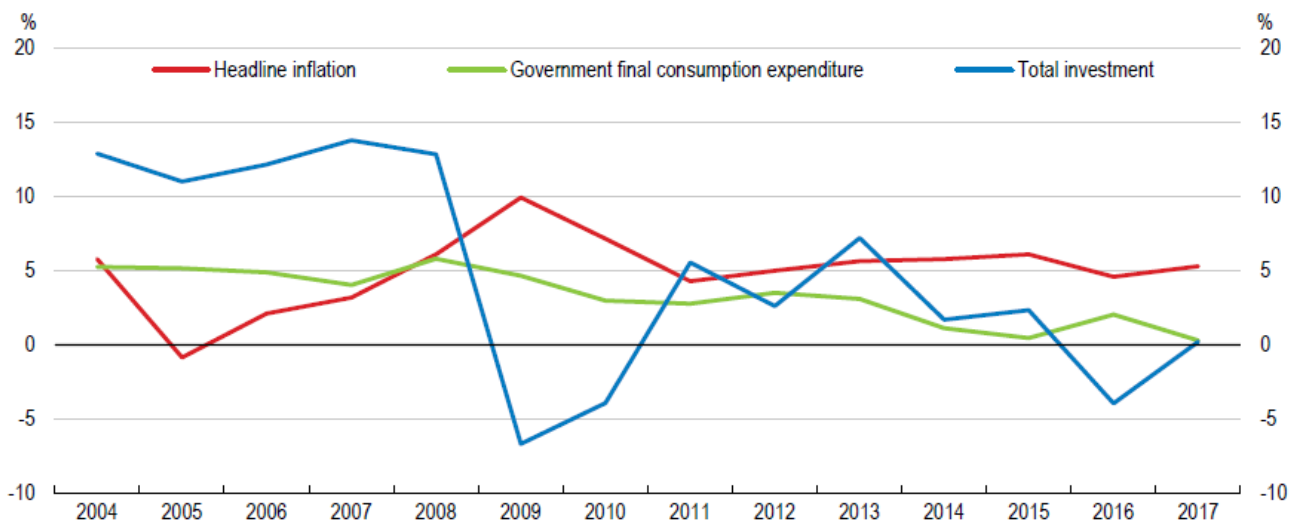
The election of a new political leadership should brighten the outlook. Business and household confidence are up. Indeed, after three years of contraction, private investment is now expected to drive growth. But, growth perspectives remain too low to create enough jobs and generate enough government revenues for spending and debt reduction, while social and infrastructure needs are high.

In the short run, a more accommodative macroeconomic policy mix can boost growth. Inflation has come down throughout 2017 and, at 4.4% in January 2018, it is in the middle of the Reserve Bank's target band. Interest rates can now be further reduced to amplify the investment pick up. Smoothing the pace of fiscal consolidation could further sustain demand and thus contribute to growth acceleration. In a low growth era, fiscal consolidation is detrimental to consumption demand, although reassuring for investors (Blanchard et al., 2013; Sutherland et al., 2012). South Africa made limited progress in fiscal consolidation over the last five years as growth kept falling.

Along with slower consolidation, budget reallocation toward more growth-enhancing investment should continue. Limiting wage growth in the public sector and subsidies and transfers to state-owned enterprises would create fiscal space for

infrastructure and social investment.

Figure 3. More accommodative macroeconomic policy-mix is needed



Source: Statistics South Africa; National Treasury; OECD, Economic Outlook Database.

Bold structural reforms are needed to increase potential growth in a longer perspective. OECD South Africa Economic Surveys (2013, 2015) have pointed to many growth boosting reforms: broadening competition in the economy, limiting the size and grip of state-owned enterprises (SOEs) on the economy, and improving the quality of the education system. Important input and technology sectors such as telecommunications, energy, transport and services in general should be opened up to more competition. In particular, telecoms or the airline company, which are in markets with enough competition could be privatised. Moreover, South Africa lacks a proper urban transport system. Putting in place a national plan to expand public transport and allowing more private operators would reduce the cost of transport on the budget and raise well-being.

Job creation remains a major challenge for the quarter of workforce without jobs. The 2017 OECD South Africa Economic survey found that boosting entrepreneurship and growing small businesses can play an important role in creating jobs. Steps have been taken to ease starting a business, but red tape remains a burden. There is room to reduce harmful product

market regulations and restrictions to entrepreneurship and entry in professional services. The quality of the education system and lack of work experience contribute to gaps in entrepreneurial skills. Policies should provide more financial and non-financial support for entrepreneurs and small businesses. But, a lack of co-ordination and evaluation hampers effective policy-making.

Greater regional integration within the Southern African Development Community (SADC) could provide new opportunities for growth. Despite large growth potential, economic integration in the sub-region has not advanced much. Intra-regional trade in the Community is only 10% of total compared to about 25% in the ASEAN or 40% in the European Union. Better implementation of SADC protocols and agreements would advance integration and create jobs. Reducing non-tariff barriers by improving customs procedures and simplifying rules of origin would reduce trade costs in the region. Weak infrastructure and institutions and barriers to competition limit industrial development. More ambitious and effective infrastructure and investment policies are necessary at the regional level.

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Finland: growing and reforming, but no time for complacency

Category: Finland, Uncategorized

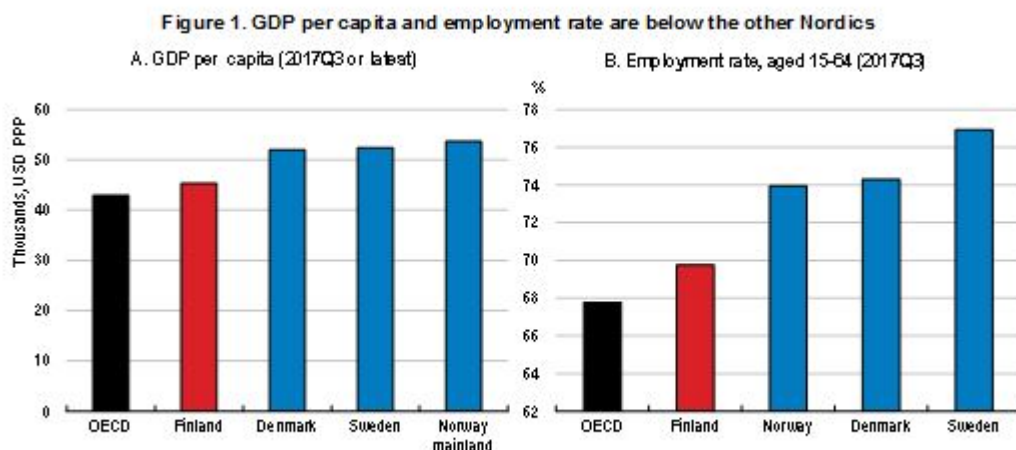
written by oecdecoscope | March 19, 2018

By Christophe André and Jon Kristian Pareliusson, OECD Economics Department

After a long period of lacklustre economic performance, robust growth has resumed. The Finnish economy suffered a series of sizeable adverse shocks alongside the global financial and economic crisis, facing major difficulties in the electronic and forest industries, in addition to a severe recession in Russia. Sound fundamentals and policy settings helped weather the impact of those shocks, and by early 2017 the economy had regained strong momentum. The recovery is broad-based across economic sectors, employment is picking up, and high business and consumer confidence point to a strong expansion going forward.

But challenges remain, as the 2018 OECD Economic Survey of Finland shows. GDP *per capita* exceeds the OECD average, but is significantly lower than in Denmark, Germany and Sweden, reflecting differences both in productivity and labour

utilisation (Figure 1). A rapidly ageing population reduces labour supply and puts pressure on public finances. Hence, future growth and well-being will hinge on a higher employment rate and productivity gains, both in the private and public sectors. Reassuringly, these challenges are well understood by the government, which has been implementing structural reforms across a wider range and with more determination and coherence than in most other OECD countries.



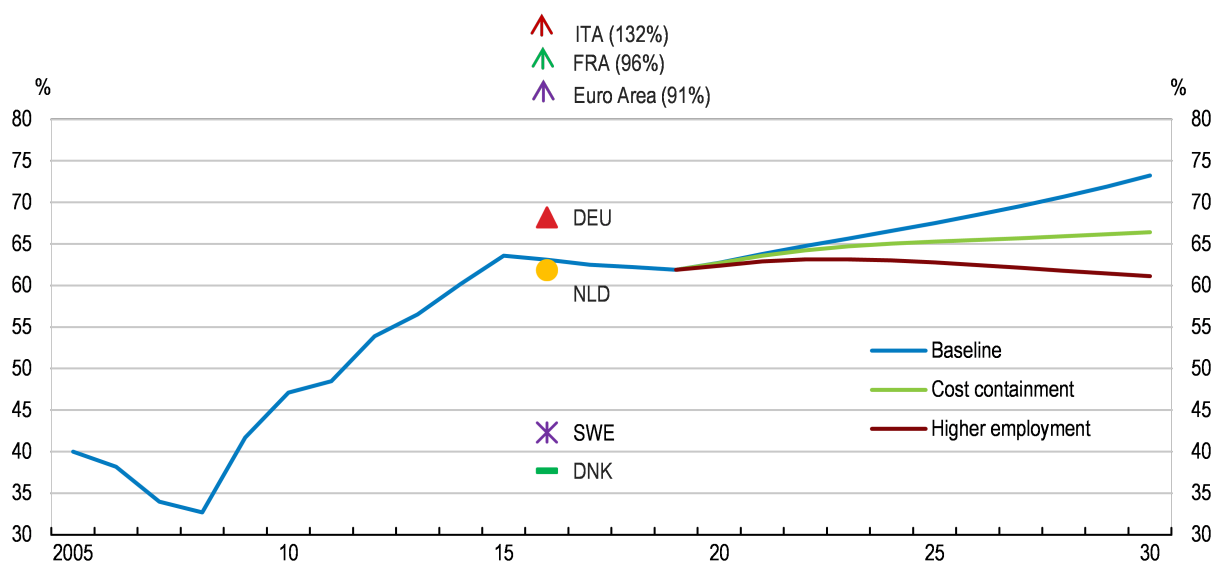
Source: OECD Economic Outlook database; and OECD Labour Force Statistics database.

Many of these reforms concern the labour market. The 2016 Competitiveness Pact between the government and the social partners lowers unit labour costs by about 4% from 2017 by internal devaluation. The social partners have also moved from a system of national-level collective agreements towards a system of “organised decentralisation”, where sector-level collective agreements are coordinated following the lead of export industries, and more leeway is given to local-level bargaining. Furthermore, the duration of unemployment benefits was reduced by 100 days in 2017, a job search requirement and a new activation model for the unemployed were introduced, the trial period for new hires was extended and education made more modular and nimble to better respond to evolving skill needs.

The health, social services and regional government reform will shift the responsibility for organising health care and social services from municipalities to 18 newly created

autonomous counties from January 2020, bringing the sub-national government structure closer to that of the other Nordic countries. Goals of the reform include providing people with more equal services, increasing freedom of choice and improving the sustainability of general government finances. The reform is welcome, and its success is crucial to meet the needs of an ageing population and ensure long-term fiscal sustainability (Figure 2).

Figure 2. Health reform and higher employment would help stabilise debt¹



1. Economic Outlook No.102 projections are used until 2019. Thereafter, in the ageing-related cost pressure scenario, increases in health and long term care spending are based on the cost pressure scenario in de la Maisonneuve and Oliveira Martins (2013), and increases in pension outlays are based on OECD (2017c). The cost containment scenario assumes that reforms to the provision of health care and social services reduce growth in related spending by half. The higher employment scenario assumes cost containment in age-related spending and a higher employment rate of the population aged 15-64, which rises to 74% in 2030. Source: OECD Economic Outlook database and OECD calculations.

The strong pick-up in economic growth and an impressive reform record are reasons for optimism, not complacency. Social welfare reform could boost employment further, as many unemployed today will see only small net income increases or even incur a loss upon return to work. Coordinating the tapering of various working-age benefits against earnings could drastically improve work incentives and transparency, while preserving the current level of social protection, and is hence a more promising route for future reform than a basic income. Furthermore, specific measures could lift work incentives for parents and older workers. Combined with the new income registry linking benefit payments to real-time

incomes from 2019, such reforms would make for a truly efficient and inclusive benefit system, adapted to evolving work patterns. Work incentives could be further strengthened by reducing the tax burden on labour while further increasing indirect and property taxes and reducing tax expenditures. Such a tax shift, along with measures to support business development and entrepreneurship could also give productivity a welcome boost.

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Towards a more prosperous and inclusive Brazil

Category: Brazil, Uncategorized

written by oecdecoscope | March 19, 2018

By Jens Arnold and Alberto González Pandiella

Over the past two decades, strong growth combined with remarkable social progress has made Brazil one of the world's leading economies. However, Brazil remains a highly unequal country, recent corruption allegations have revealed significant challenges in economic governance and the situation of its fiscal accounts is challenging with high and rising public debt (OECD, 2018). This calls for wide-ranging reforms to sustain and continue progress on inclusive growth. The government has started to put in place significant reforms, including a fiscal rule and a financial market reform that aligns directed lending rates with market rates. The long

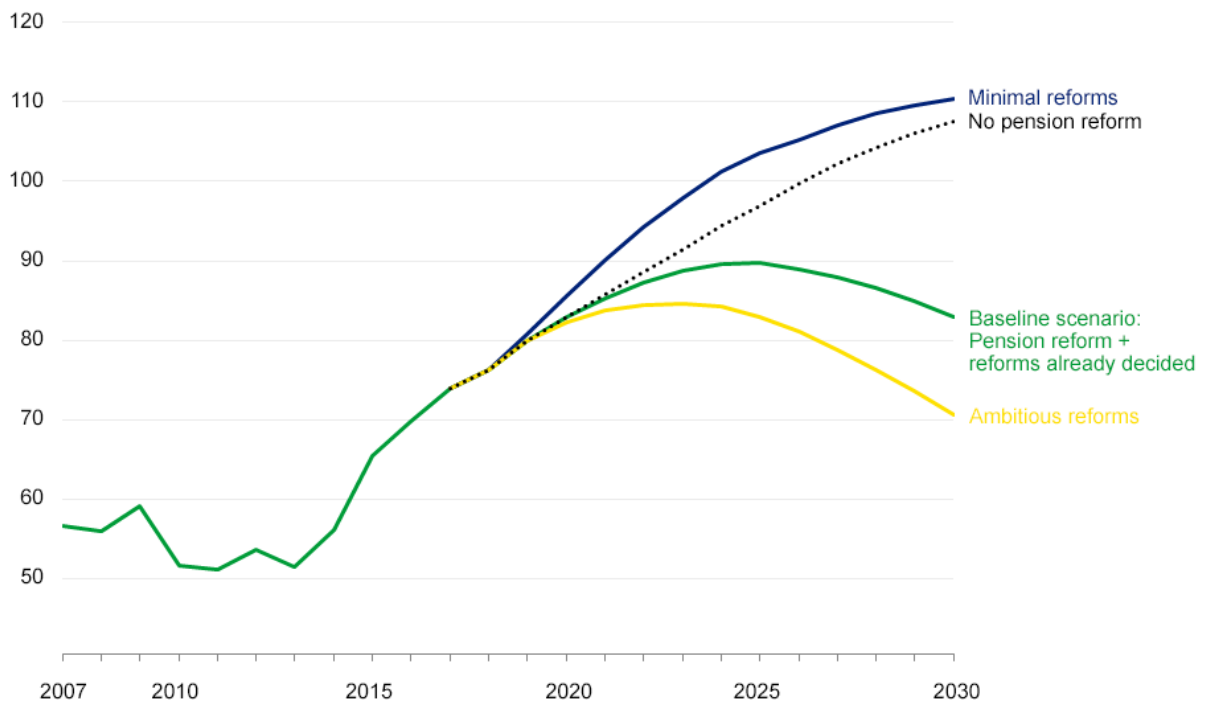
and deep recession is over and growth is projected to accelerate significantly this year. But more needs to be done to improve the living standards of all Brazilians.

The overall budget deficit is close to 8% of GDP driven by rising expenditures. Gross public debt has increased by approximately 20 percentage points of GDP over the last 3 years and stands around 75% of GDP. Implementing the planned fiscal adjustment and achieving fiscal targets is crucial for restoring the credibility of fiscal policy and avoiding a fiscal crisis. A comprehensive social security reform has become the most urgent element of the fiscal adjustment, as much of the worsening of the deficits is due to rising pension spending. A pension reform is also an opportunity to make growth more inclusive through better targeting of benefits. Aligning Brazil's pension rules with those practiced in OECD countries could be done in a way to preserve the purchasing power of pensioners while significantly improving the sustainability of the pension system. For example, in OECD countries people retire on average when they become 66 years old, while the effective retirement age in Brazil is 56 years for men and 53 for women. Establishing a formal minimum retirement age would help, in addition to rethinking the current benefit indexation mechanisms. Without reform, pension expenditure will more than double by 2060 (OECD, 2017), which would lead to unsustainable fiscal dynamics (Figure 1).



Brazil's public debt trajectory under various scenarios, 2007-2030

General government gross debt, % of GDP



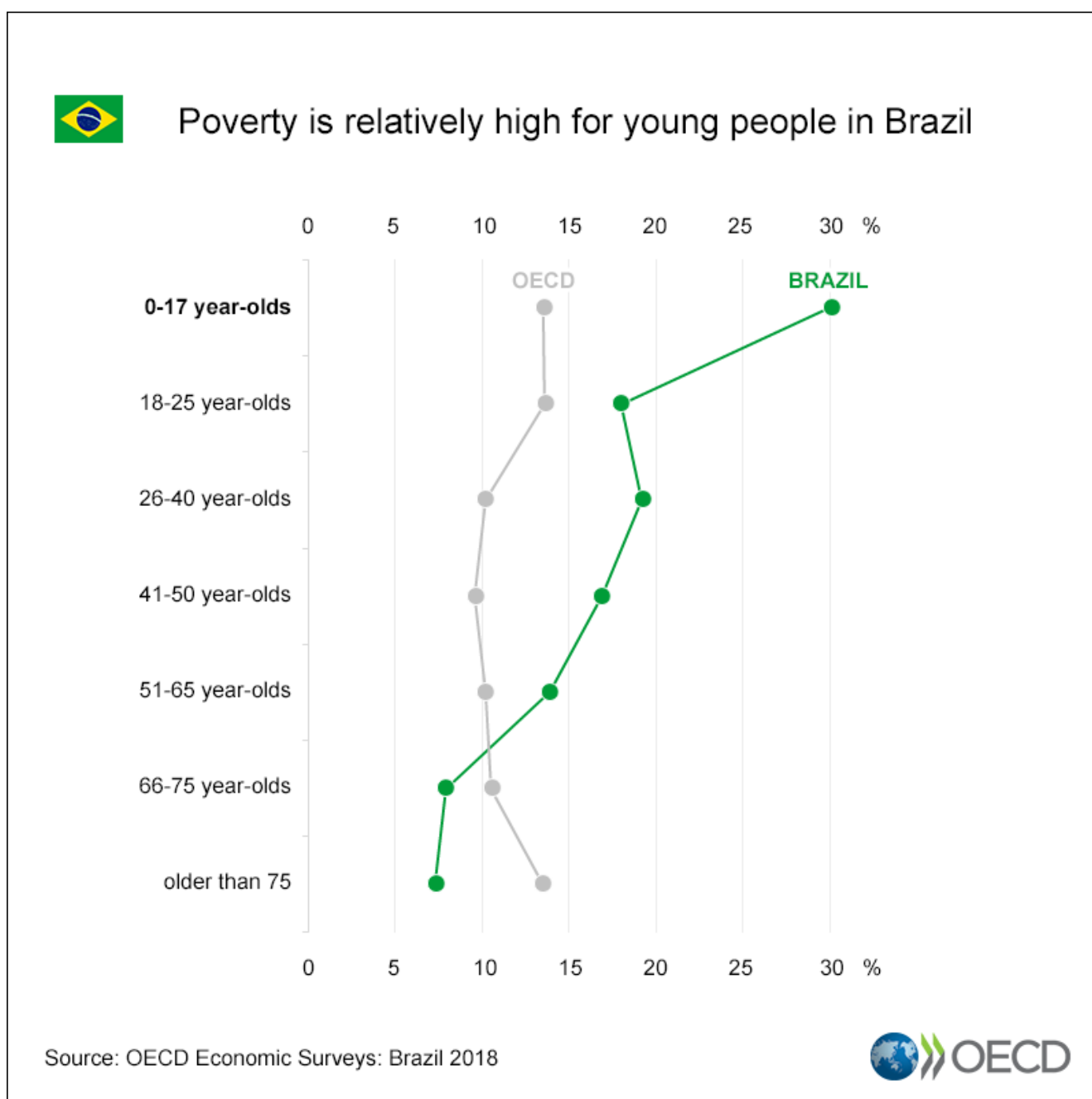
Note: See OECD (2018) for a definition of the different scenarios. The ambitious reforms scenario assumes structural reforms boosting productivity growth, such as lowering trade barriers or reducing barriers to entrepreneurship. See table 1 in OECD (2018) for additional details. The no pension reform scenario assumes the absence of any noticeable parametric reform to the pension system.

Source: OECD Economic Surveys: Brazil 2018



Improving the effectiveness of public spending, and in particular public transfers, will also be crucial for further social progress. At present a large and rising share of social benefits is paid to households that are not poor, which reduces their impact on inequality and poverty. Already, poverty is more than three times higher among children and youths than among those aged above 65 (Figure 2). Limiting future increases in those social benefits that do not reach the poor would be a first step. That would instead allow shifting more resources towards transfers that do reach the poor, such as Bolsa Família, which is highly regarded across the world and reaches the poor like hardly any other social programme in Brazil. This would help particularly children and

youths. Currently Bolsa Família only represents 0.5% of GDP out of the 15% of GDP that Brazil spends on social transfers (OECD, 2018). There is also scope to reduce transfers to the corporate sector, which have increased markedly over recent years. These transfers, often granted in the form of tax exemptions or subsidised lending, have not been associated with visible improvements in productivity or investment, but they benefitted primarily the more affluent, besides creating fertile ground for corruption and political kick-backs.



Further advances in living standards will also hinge on

finding a new inclusive growth strategy, ensuring that the benefits of growth will be broadly shared across the population. Productivity will have to become the principal engine of growth in the future, because the demographic bonus that has supported growth in Brazil is reversing. But raising productivity will require significantly higher investment and trade. Brazil has one of the lowest investment rates among OECD and emerging market economies and it is also less integrated into global trade. Boosting investment and trade would raise productivity, helping Brazilians to access higher wages and living standards.

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Why would a universal credit be better than a basic income for Finland?

Category: Finland,Uncategorized

written by oecdecoscope | March 19, 2018

By Jon Kristian Pareliussen, Economist, OECD Economics Department

"If you don't know where you are going, you might wind up

someplace else.”

– Yogi Berra

Many Finns seem to agree that the social welfare system should be reformed, but there is no agreement as to which form such change should take. Recognising that the decades-long process of piecemeal welfare reform responding to the pressing issues of the day is behind many of the current problems, the OECD Economic Survey of Finland 2018 argues for developing a common vision for the future of social welfare in Finland, so that upcoming reforms can consistently pull towards the same goal.

In Finland, as elsewhere, income taxation and the withdrawal of benefits reduce the pay-off for individuals who go from benefits to work. Multiple benefits interact in complex ways, trapping individuals in unemployment, underemployment or inactivity. Complex benefit rules combine with administrative practices to create “bureaucratic traps” when individuals taking up temporary, part-time or unstable employment face a real or perceived risk of losing eligibility or receiving benefits with a delay as their claims are re-evaluated. This can further reduce the attractiveness of work for risk-averse, often cash-strapped, recipients. A third weakness of existing welfare systems is that they are built around traditional employer-employee relationships, and are thus ill-adapted to the future of work, which is likely to involve more changes in careers, part-time work, self-employment and platform work.

Two different benefit reform scenarios are developed in the *Survey* to inform a common vision for the future of social welfare in Finland. The first is a uniform benefit for all, a universal basic income. The second is a universal tapering rule inspired by the universal credit welfare reform in the United Kingdom. This scenario radically simplifies the existing benefit system and makes it more transparent by merging various benefits and withdrawing them at a single and

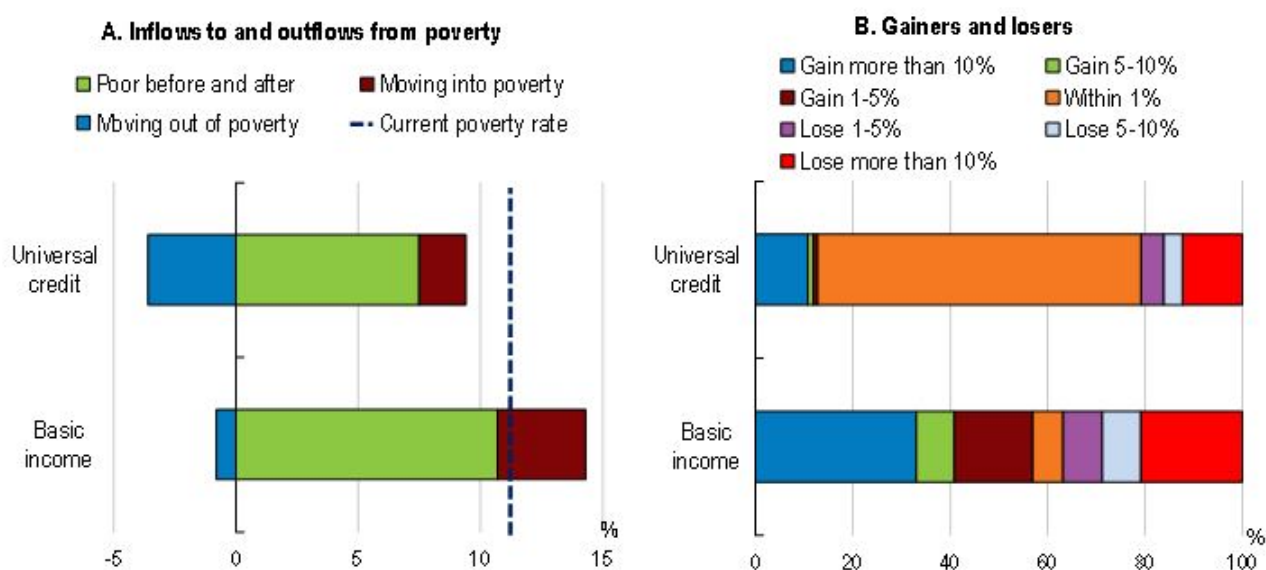
moderate rate as income from work increases.

Comparing these scenarios with the current system illustrates the inevitable trade-offs between work incentives, inclusiveness and fiscal cost, the policy trilemma at the heart of social insurance and redistribution policy. Neither a basic income nor a universal credit can defy the laws of gravity. But some specific incentive issues can be resolved without much sacrifice by improving benefit design, and the general direction of reform has great consequences for outcomes.

A universal credit would consistently improve work incentives and reduce complexity, with limited changes to the income distribution and limited fiscal cost. A basic income would also remove some incentive traps, but would entail a major redistribution of income, widening inequality and increasing poverty. This happens because the design of a basic income with one uniform benefit for all is too simple to achieve the redistribution of the current system or a universal credit, where benefits are targeted to those who need them more. Assuming that the distribution of income in a longstanding democracy reflects Finns' social preferences, it seems clear that merging and simplifying existing benefits is a better solution for Finland than a universal basic income. This conclusion is also likely to be relevant for other developed countries with solid and targeted social safety nets.

A basic income scenario would alter the income distribution

Share of individuals in working-age households



Source: Simulations with the TUJA model, in Parelissen et al. (2018a).

Simulating reforms is one thing but implementation can be a quite different story: experience has shown that major welfare reforms can come with significant costs. Implementation should hence be stepwise and build on the existing institutional context. Important technical building blocks, such as harmonised tax treatment and income definitions for different benefits as well as the new income registry should be fully operational and tested before reforming the overall architecture of the system.

Moreover, many current weaknesses, such as the cliff-edge loss of unemployment benefits once an individual works a certain amount of hours per week, the extended unemployment insurance for older workers and barriers to work for mothers created by childcare fees and the homecare allowance, can be overcome with relatively limited changes to the current system. Such measures should be taken without delay, but every step forward should be a stride towards an agreed vision for the future of Finnish social welfare – a vision where benefits continue to support Finnish citizens throughout their lives, protecting them from shocks and misfortune, but in a coherent, transparent and flexible way, fit for the future of work.

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