

Indicators of financial incentives to work

Discussion introduced by :

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Banco de Portugal Research Department

The OECD-EC approach

- Compute indicators of the tax burden on “labor supply” decisions
 - Low wage trap: put on more hours
 - Unemployment trap: leave UI Benefits and enter employment
 - Inactivity trap: leave minimum income schemes or joint spousal working decisions
- METR and NRR computed for each case using EUROMOD

The results

- METR computations show very high figures for several countries: in Belgium, Denmark, Germany, France, Luxembourg, Portugal and Sweden it is close to 90% for individuals earning 67% of APW
- For lower earnings figures are even higher, often more than 100%

Some questions

- Are the high METR countries low employment rates countries?
- Not completely satisfactory use of elasticities of participation in micro studies.
- How does the elasticities of unemployment duration and reservation wages to unemployment benefits relate with the computed METRs ?
- What is the role of labor demand in the matching process (minimum wage, employment protection)?
- What do we know about the arrival rate of job offers for different labor market groups?

Leaving Unemployment

- Job search theory
 - Unemployment hazard depends
 - Reservation wage
 - Arrival rate of job offers
 - Wage offer distribution

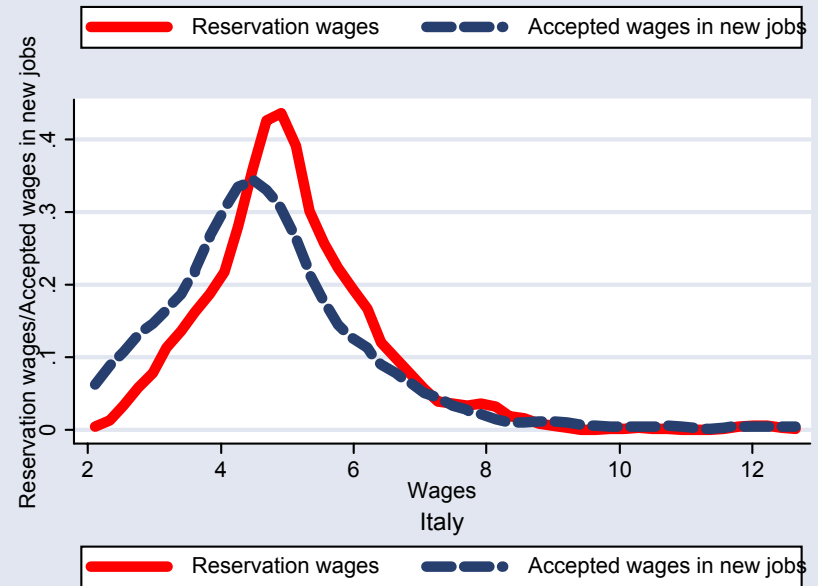
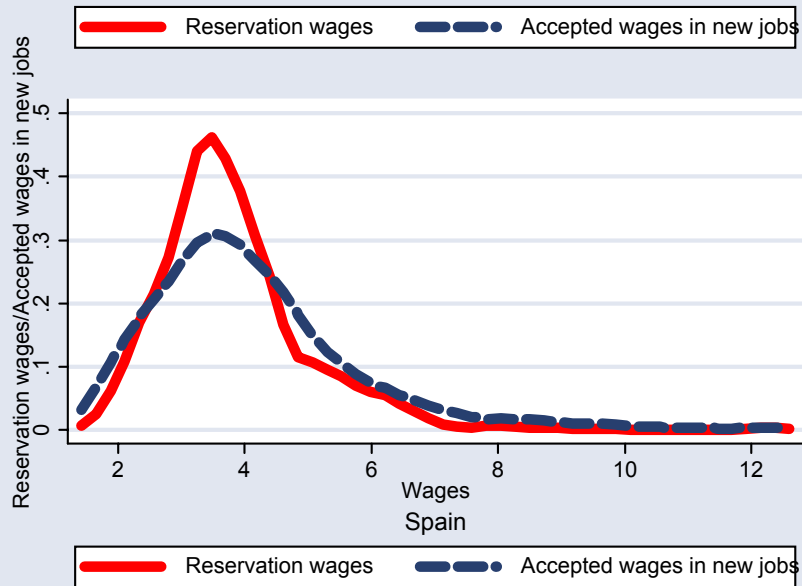
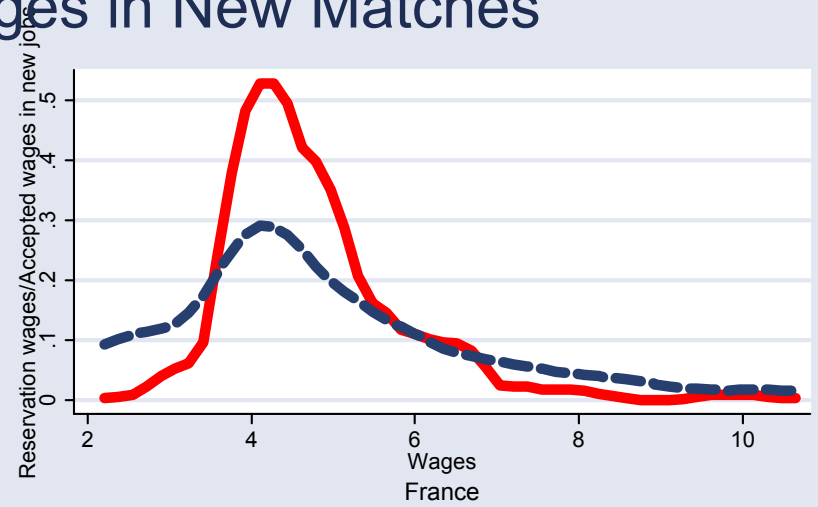
What dominates the declining U to E hazard functions ?

- To Gauge the Main Determinants
 - Structural models
 - Reduced form estimates
 - Key elasticities

Evidence on the arrival rate of job offers (Extreme Value Regression Estimate)

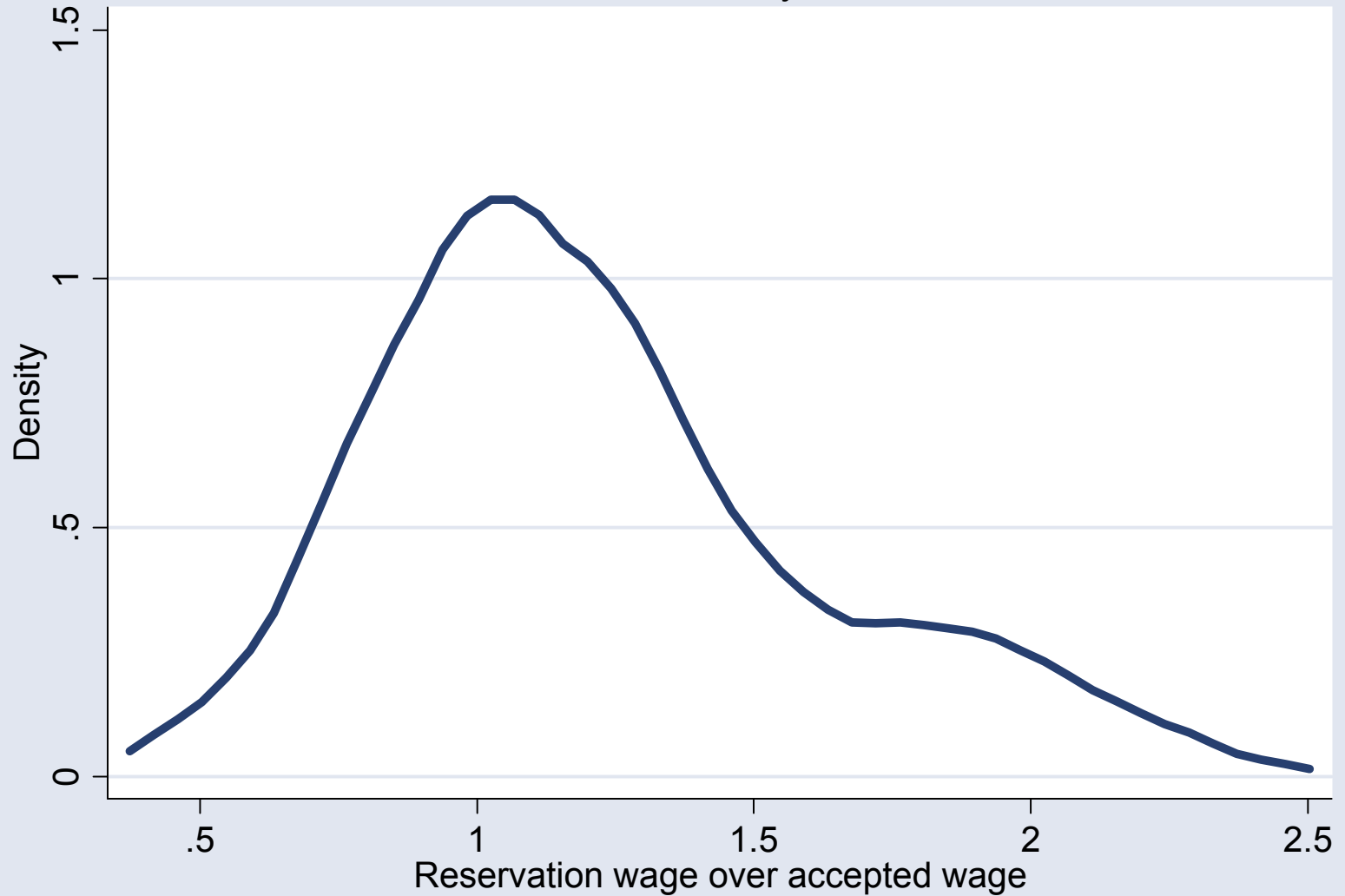
Variables	Coefficient	Std Dev	Marginal Effect
UE Duration	-0.356	0.012	-0.131
UIB	-0.047	0.004	-0.019
Male	0.241	0.025	0.099
College Grad	0.294	0.036	0.121
Age 18-25	1.285	0.080	0.530

Res. wages and Wages in New Matches



Reservation Wage over Accepted Wage

Germany



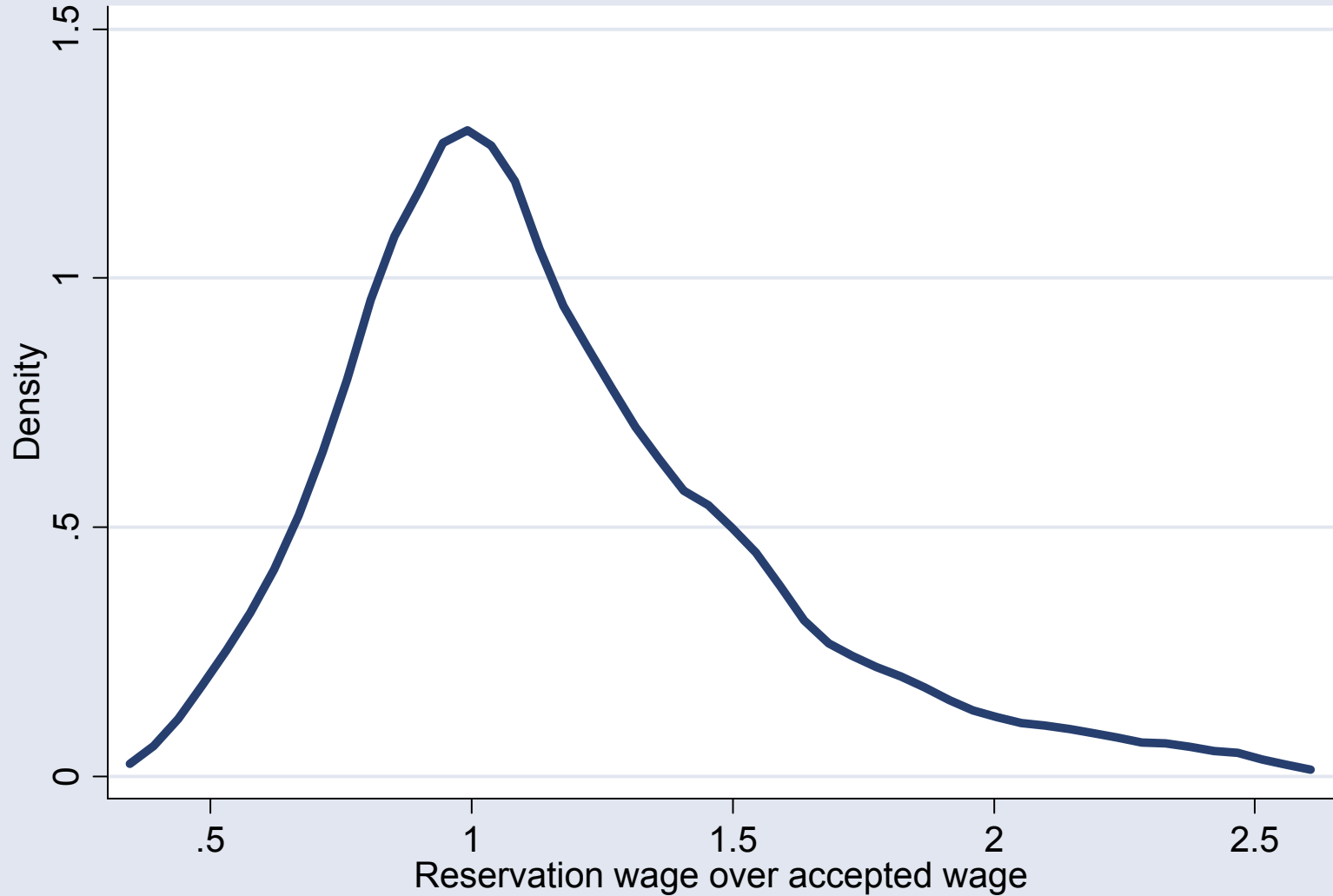
Reservation Wage over Accepted Wage

United-Kingdom

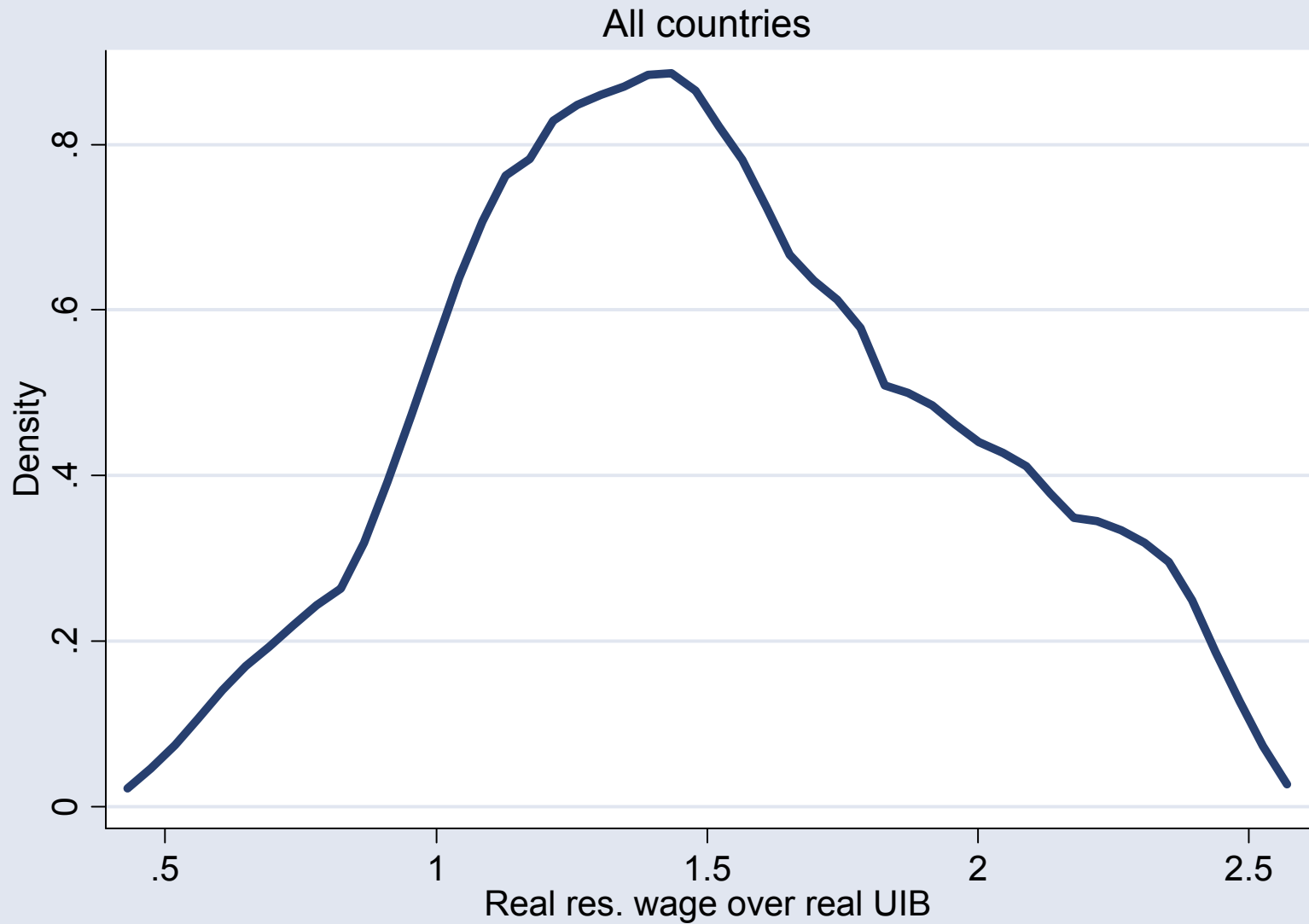


Reservation Wage over Accepted Wage

All countries



Reservation Wage over UIB

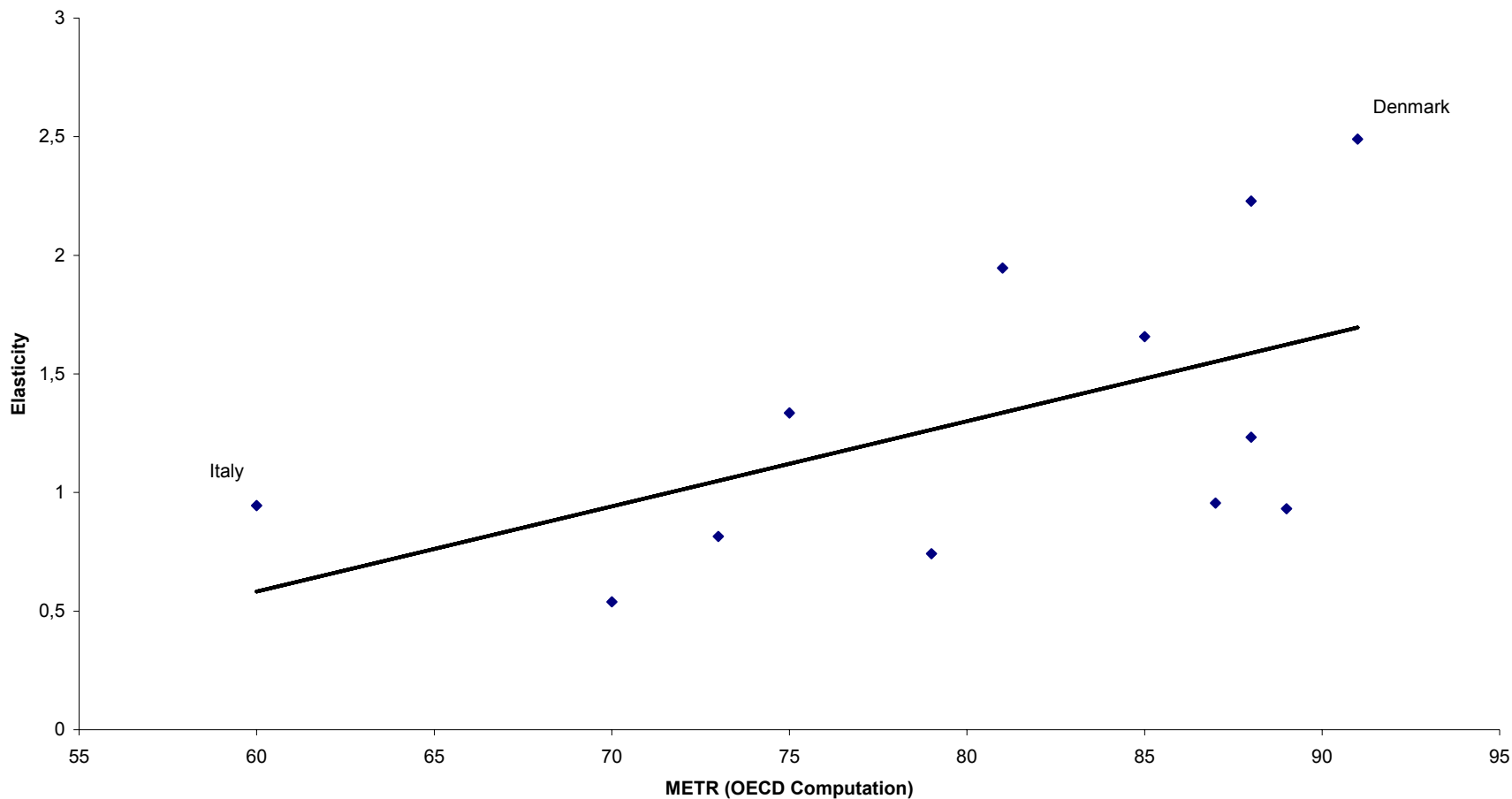


Median Benefit and Offer Probability Elasticities of Reservation Wages and Unemployment Duration

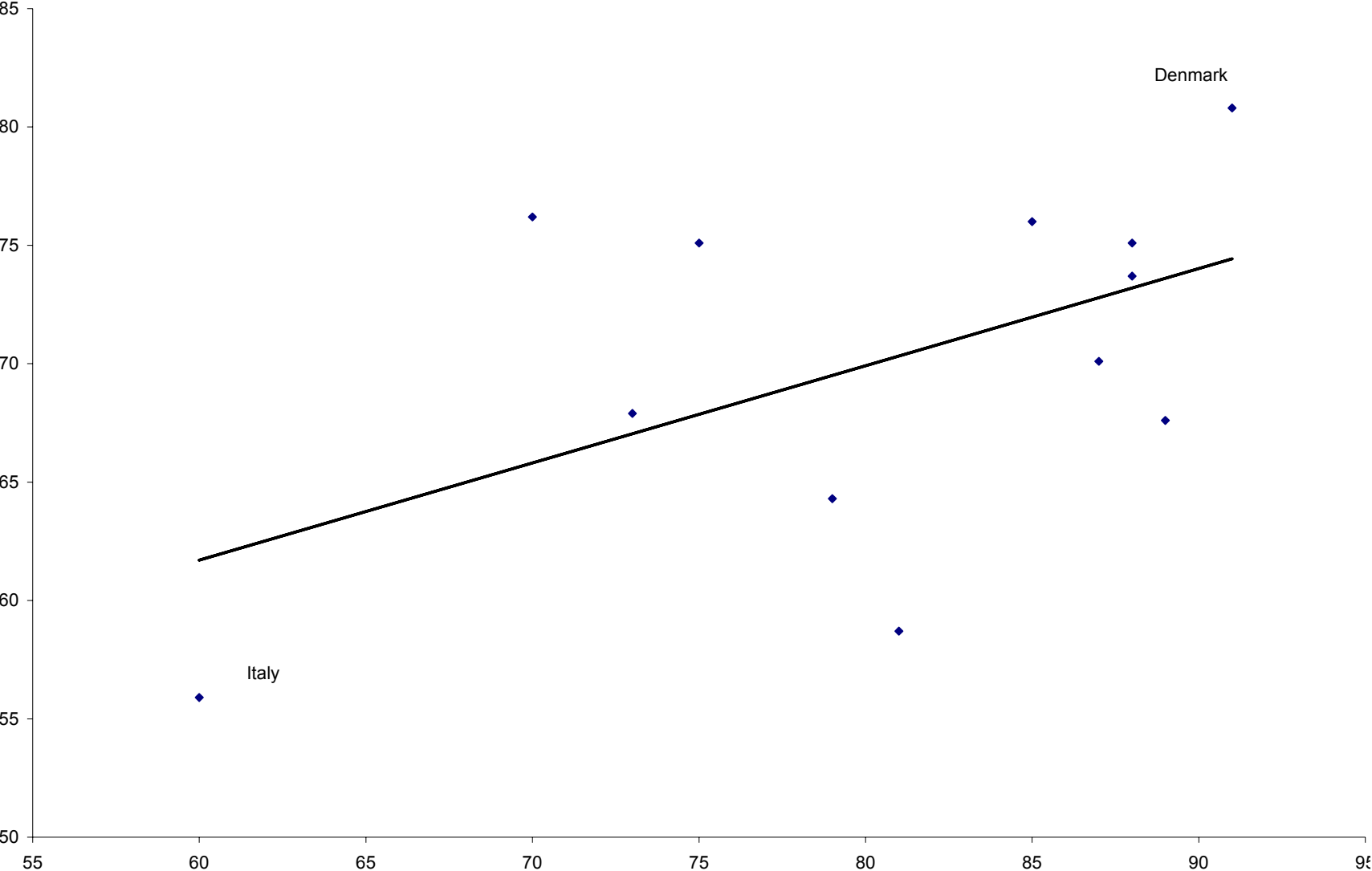
Country/ Elasticity	Germany	Denmark	France	UK	Spain
Elasticity of reservation wages to unemployment benefits	0.2273	0.3269	0.2917	0.3138	0.3118
Elasticity of reservation wages to arrival rate of job offers	0.1000	0.0628	0.1029	0.1757	0.0615
Elasticity of unemployment duration to unemployment benefits	1.2328	2.4894	0.9314	0.5394	1.9465
Elasticity of unemployment duration to arrival rate of job offers	-0.2457	-0.4046	-0.1561	-0.3138	-0.3845
Number of observations	111	159	103	87	163

Source: Addison, Centeno and Portugal “Key Elasticities in Job Search Theory: International Evidence”, Banco de Portugal Working Paper 12-04.

Unemployment Duration Elasticities and METR (unemployment)



Participation Rate and METR (unemployment)

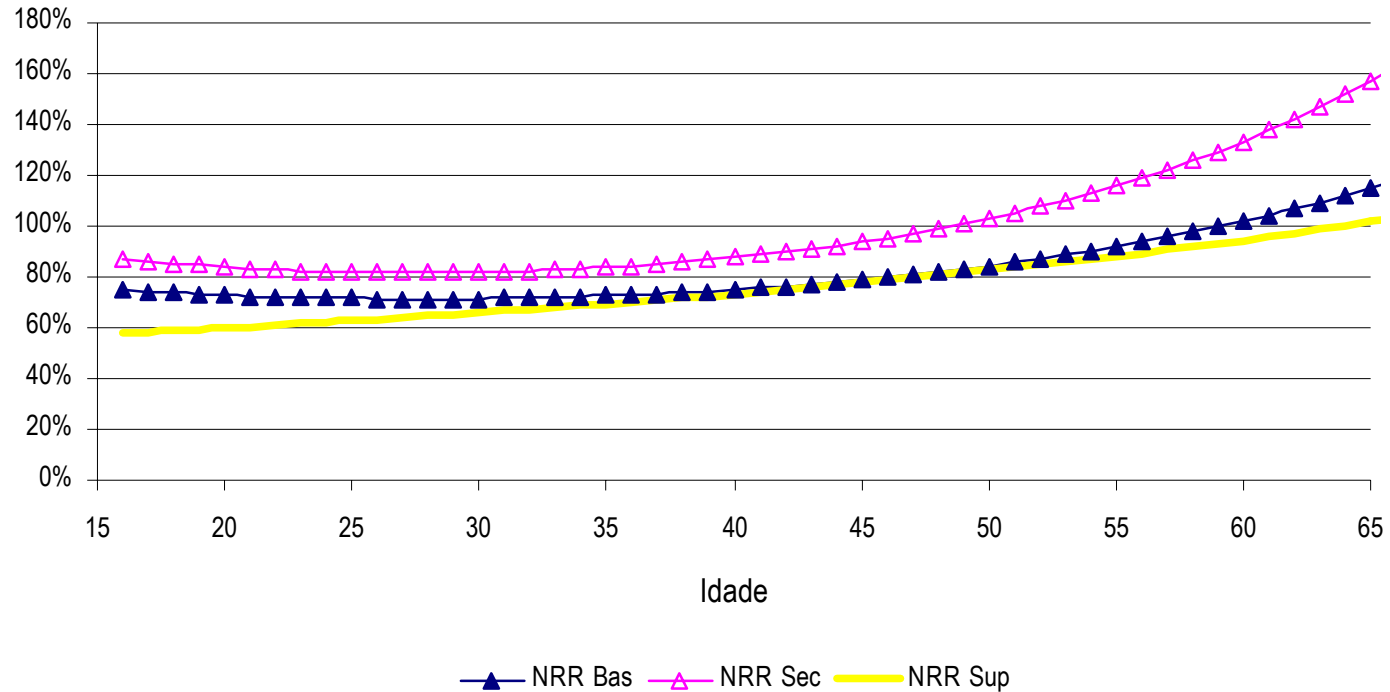


Some more questions on the methodology ...

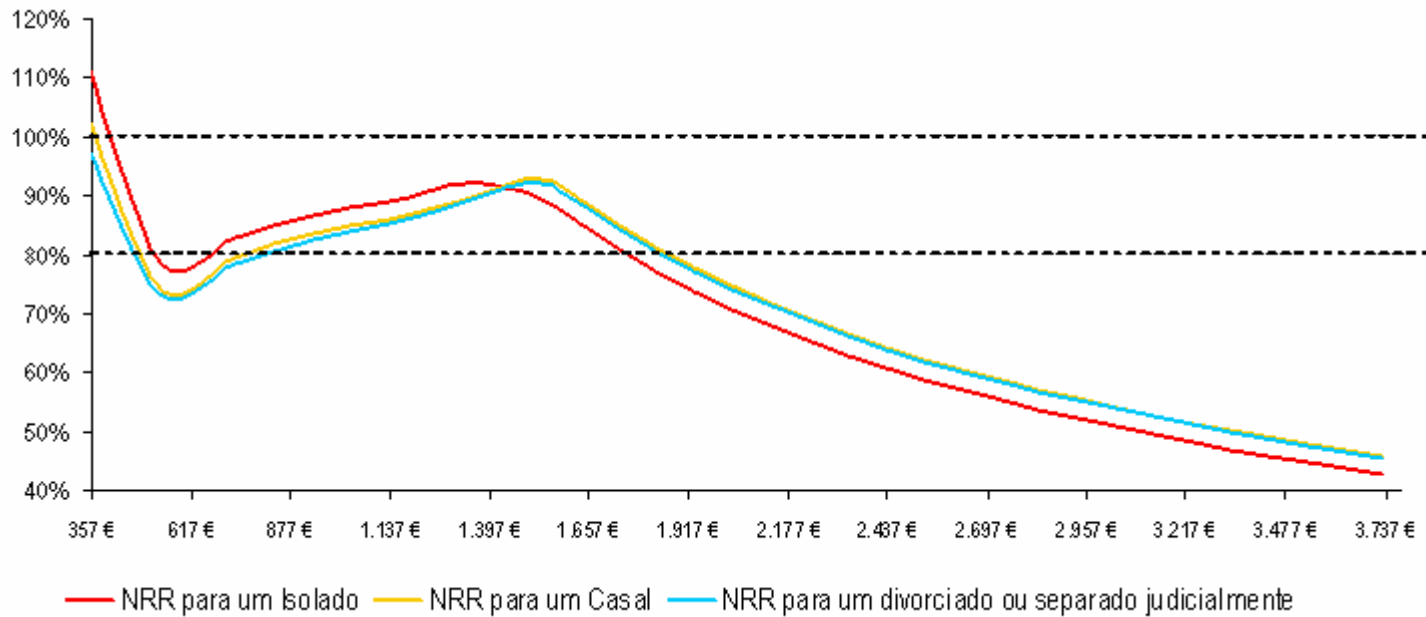
- The costs of these programs and reforms
 - The windfall beneficiaries: they vary by education and past history
 - The focus on poverty alleviation versus labor market efficiency
 - The need to exercise a better control over benefits and eligibility (employment services and search effort by the non-employed)

Heterogeneity in NRR

D1, Taxas Líquidas de Substituição do Rendimento (NRR)



Looking at the whole income distribution



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