

Benchmarking Unemployment Benefit Systems

by Klara Stovicek and Alessandro Turrini, European Commission

The paper evaluates unemployment benefit systems in the EU using various benchmarks. The data are taken from the European Commission – OECD Tax and Benefit Project and are available over the period 2001-2010. The analysis considers a multiplicity of dimensions of unemployment benefit systems – such as entitlement conditions, unemployment and inactivity traps, benefit duration, time profile of replacement rates and job search and work availability. Cross-country comparisons are performed not only on the basis of the EU average but also on the basis of the average of a homogenous group of countries with similar labour market institutions.

A synthetic measure of the total generosity of unemployment benefit systems is constructed taking into account net replacement rates over the whole unemployment spell of both unemployment insurance and unemployment assistance. This synthetic indicator is compared with a benchmark estimated from multivariate cross-country regressions and takes into account differences across countries in GDP per capita, labour market performance, fiscal constraints and expenditures on activation policies.

A number of relevant results emerge as follows from the comparison of the different dimensions of unemployment benefit systems:

- Belgium, Denmark, Portugal, Spain, Finland and the Netherlands appear to be relatively generous in terms of unemployment insurance replacement rates and duration compared with the EU average, while in the UK, Malta, Slovakia, Estonia, Poland and Romania benefit conditions are relatively tight.
- Regarding entitlements conditions, they are particularly loose in Denmark, Austria, Cyprus, while in Portugal, Italy, Slovenia, they are rather tight. As for job search conditionality, it is loose in Belgium, Greece, Bulgaria, while tight conditions apply in Germany, Denmark, Slovakia. While a decline in the net replacement rate is nearly absent in Ireland, Malta, the UK, Austria and Belgium, the decline is rather abrupt in Italy, Latvia, Luxembourg, Greece, Estonia, Poland, Slovenia and Lithuania.
- Within the EU, there are groups of countries with relatively homogenous benefit systems. Nordic and Continental countries are characterised by relatively generous unemployment benefit systems both in terms of entitlement conditions and income support per unemployed. In both groups, activation and active labour market policies have a prominent role, with job search conditionality being strong especially in Nordic countries. In Anglo-Saxon countries, unemployment insurance benefits are relatively modest, while unemployment assistance plays a major role. Monitoring of job-search activity is strict whilst active labour market policies play a less important role. In Southern countries, access to unemployment insurance is strict and benefit generosity varies widely depending on age

and contribution period. Activation policies play a relatively minor role, while participation in active labour market policies is widespread. Finally, Central and Eastern countries tend to exhibit a tight unemployment benefit system both in terms of benefit support per unemployed and benefit coverage. Although replacement rates at the beginning of the unemployment spell can be high in some cases, benefits drop sharply over the unemployment spell. Strict conditions on job search and availability often apply.

- Some countries that stand out as particularly generous in terms of replacement rates and duration as compared with the overall EU average turn out instead broadly in line when compared with the average for their respective groups. This is the case of Finland, the Netherlands, Spain. Symmetrically, Malta, the UK, Poland, Romania and Estonia which have tight benefits as compared to the whole EU appear broadly in line with the other countries of their own groups.

The benchmarking of the synthetic measures of overall generosity of unemployment benefit systems reveals a number of insights as follows:

- The overall generosity of unemployment benefit systems exhibits a high degree of variation across EU countries, with Belgium, Malta, Austria, Denmark, Ireland, Finland and Portugal having much more generous benefit systems than EU average while opposite is the case in the Czech Republic, Lithuania, Slovakia, Italy, Poland, Hungary, Latvia and Estonia.
- A somehow different picture emerges when the overall generosity of unemployment benefit systems is benchmarked against the prediction from multivariate regressions that take into account differences in fundamental factor affecting unemployment benefit systems. While unemployment benefit systems in Malta, Belgium and Portugal appear even more clearly highly generous, the evidence becomes weaker for Denmark and Finland. The reason is that high income per capita, strong activation policies, and sufficient fiscal space in these countries, justify more generous benefit systems. These benchmarks strengthen the case that Luxemburg and Sweden are characterised by relatively tight benefit systems, while for Slovakia, Greece, Poland and Hungary results become more nuanced: benefit systems are still relatively tight, but, in light of a combination of low income per capita, fiscal deficits, and high long-term unemployment, not as much as coming out from a simple comparison with EU average.

Overall, results confirm the usefulness of considering a wide range of elements when comparing unemployment benefit systems and of referring to alternative benchmarks. Looking at all relevant dimensions permits to better gauge how unemployment benefit systems perform in terms of their multi-faceted objectives (income support and stabilisation, incentives to take up work,...). Using alternative benchmarks offers the possibility of assessing against more meaningful country comparators, which take into account similarities in terms of economic fundamentals, institutions and policy settings.