

7. Social protection in the time of crisis

Introduction

In the course of the past year social protection systems have been subjected to an unsolicited stress test. The financial and economic crisis has created an upsurge in unemployment, as a result of which the social protection systems have been operating at full stretch in their capacity as automatic stabiliser. Meanwhile, the financial sustainability of these systems is also being challenged as growing unemployment and negative GDP growth impact negatively on the revenue side of the equation, an effect compounded in certain cases by the extent to which funded pension schemes – public as well as private – are dependent on financial markets.

On a more abstract level, the economic and financial crisis has also contributed to a shift in the focus on social protection systems and the role they should play. During the past decade the debate on social protection systems has focused on how to make them financially sustainable and, at the same time, how to build employment incentives into them. Though this debate has not been abandoned entirely, the current emphasis is on how to reform the systems to ensure that they can play the role for which they were originally set up, namely to act as a safety net and protect against risks stemming from a lack of income from employment.

Governments have indeed undertaken swift and rigorous action to adapt the passive and active unemployment insurance system in order to maintain, sustain and promote employment, while at the same time providing a safety net for unemployed and low-income workers. Not all the discretionary reforms embarked upon can, however, be hailed as positive, some countries having already begun to introduce cost-containing reforms, with many others likely to follow in the coming year. However this may be, the crisis has put the activating welfare state to a test; governments have reacted, but only the future will show how social protection systems have stood up to the test and to what extent the social crisis has been alleviated by the various discretionary measures adopted.

This chapter will focus on the type of reforms to which unemployment insurance systems have been subjected in the light of the crisis, discussing them in some detail and drawing up a list of warning signs for the future. While the impacts of the crisis on other aspects of the social protection systems – for instance, pension systems and retirement income – are also relevant, these aspects will not be dealt with here. The reforms implemented in the field of unemployment insurance and assistance schemes testify to the swift reaction of

governments to the employment crisis in terms of extending the coverage and action of both the active and passive branches of the unemployment insurance and assistance systems.

Themes

- 7.1 Social protection expenditure
- 7.2 The crisis and the reforms of the social protection systems
- 7.3 Conclusions

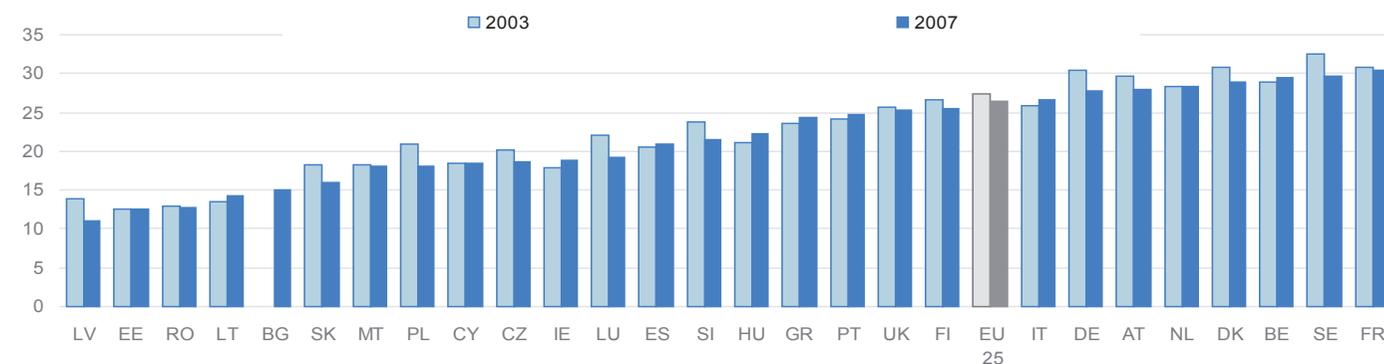
7.1 Social protection expenditure

Decrease or stabilisation of expenditure

In 2007 (latest available data), gross average expenditure on social protection accounted for 26.4% of GDP in the EU25, down from 27.4% in 2003 (see Figure 7.1). The countries with the highest ratios spent (in relation to GDP) more than twice as much as the five countries with the lowest ratios, namely the Baltic countries, Bulgaria, Romania and Slovakia.

In general, social protection expenditure as a percentage of GDP was stable or decreased slightly in most EU member states during the “between-crisis” period (2003-2007); very few countries saw any increase in their expenditure as a percentage of GDP. In most countries, while more resources have been devoted to social protection per capita, this increase has not been proportional to the growth in GDP, indicating that the “between-crisis” period has been used to reform social protection systems while focusing on their long-term financial sustainability and incentive structures. Only in Germany, Denmark and Slovakia has per capita social expenditure decreased.

Figure 7.1 Social protection expenditure 2002-2007 (%GDP)



Source: Eurostat (2010) *European System of Social Protection Statistics (ESSPROS)*. Note: Data for Bulgaria 2003 missing.

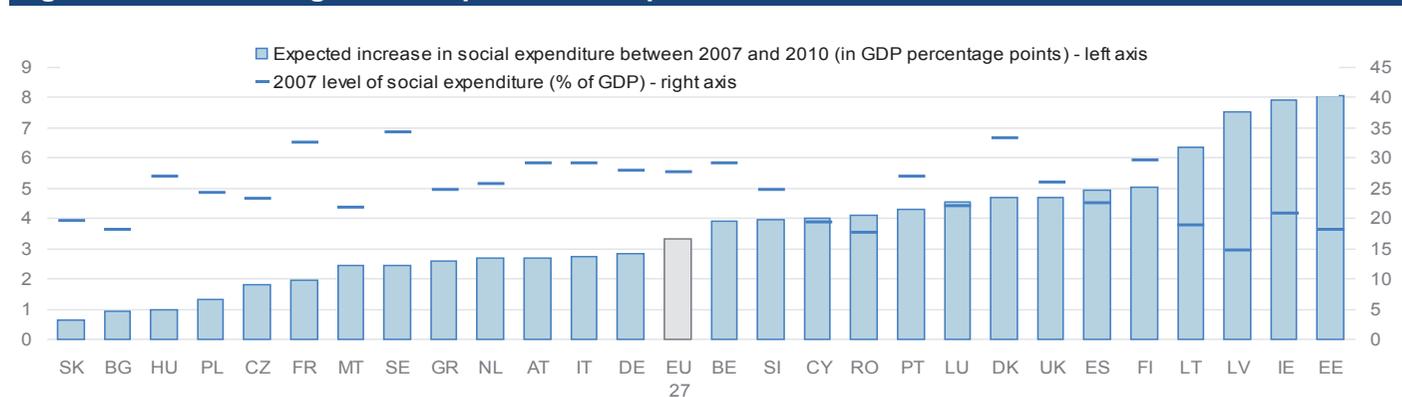
7.1 Social protection expenditure

Sharp increase in social protection expenditure expected for 2010

The financial, economic and resulting social crisis has challenged this stabilisation of expenditure, given that the social protection system has had to play its role as automatic stabiliser, in particular by providing income replacement for persons losing their employment, and assisting them in finding new jobs, but also by alleviating the income shortfall suffered by workers affected by short-time working arrangements (see chapters 3 and 5). As shown in Figure 7.2, in 2010 social protection expenditure is expected to rise by an average of 3.2 percentage points over the EU27 as a whole, with only a minimal increase in Slovakia and one of above 6 percentage points in the Baltic countries and Ireland, countries which start out at a rather low level of social spending as a percentage of GDP. The responsiveness of social expenditure to the crisis depends on a broad set of factors, including the design of rules granting different kinds of passive and active benefits, and the extent to which expenditure is linked to unemployment rates. However, the expected increase in social expenditure is also the result of discretionary measures taken to reinforce social benefits in view of weaknesses in the current design, and particularly the lack of coverage. It can be said that the stress test to which social protection systems have been so abruptly subjected has

identified in them a certain number of gaps and weaknesses, as a result of which governments have been forced, given the gravity of the crisis, to take action and extend the system to groups that were poorly covered and also to raise benefits to more adequate levels, by way of corrective to some of the reforms (or absence of reform) that have taken place during the past 10 years.

Figure 7.2 Forecasting of social protection expenditure 2007-2010



Source: EC Economic Forecast Autumn 2009 in Social Protection Committee (2009).

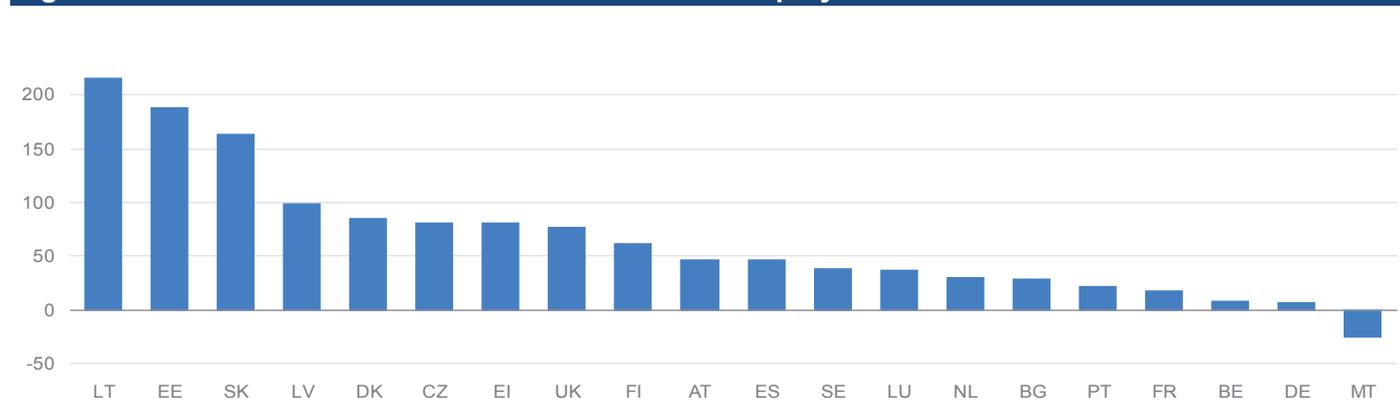
7.2 The crisis and the reforms of the social protection systems

Sharp increase in unemployment benefits beneficiaries

To understand the strain placed upon social protection systems, it is necessary only to consider the percentage increase in the numbers of persons in receipt of unemployment benefit. Since there are no harmonised European data on this issue, when, in October 2009, the Social Protection Committee circulated a questionnaire on the social impact of the crisis, it included a question on the increase in numbers of beneficiaries. This data, presented in Figure 7.3, is not harmonised, so that no strict comparison is possible, but it does provide an overview of the pressure under which unemployment insurance systems are currently labouring. Most figures provide the increase during the period stretching from the third quarter of 2008 to the third quarter of 2009. Among the EU member states that have responded, more than half report an above 50% increase in the number of beneficiaries, the extreme cases being Latvia (an increase of nearly 220% between September 2008 and September 2009) and Estonia (190% during the same period). In Germany and Belgium, on the other hand, the increase has been less than 10%, while Malta has even seen a decrease. Accordingly, unemployment insurance systems in many EU member states, and most particularly the Baltic States, are under severe pressure. Nor do all EU member states have

unemployment insurance systems that are geared to cope with such an influx, be it for paying out income replacement, or with regard to the provision of training or assistance in the search for new employment. For this reason, a very considerable number of discretionary measures had to be adopted in order to handle the sharp increase in unemployment benefit recipients.

Figure 7.3 Increase in number of beneficiaries of unemployment benefits



Source: Social Protection Committee (2009).

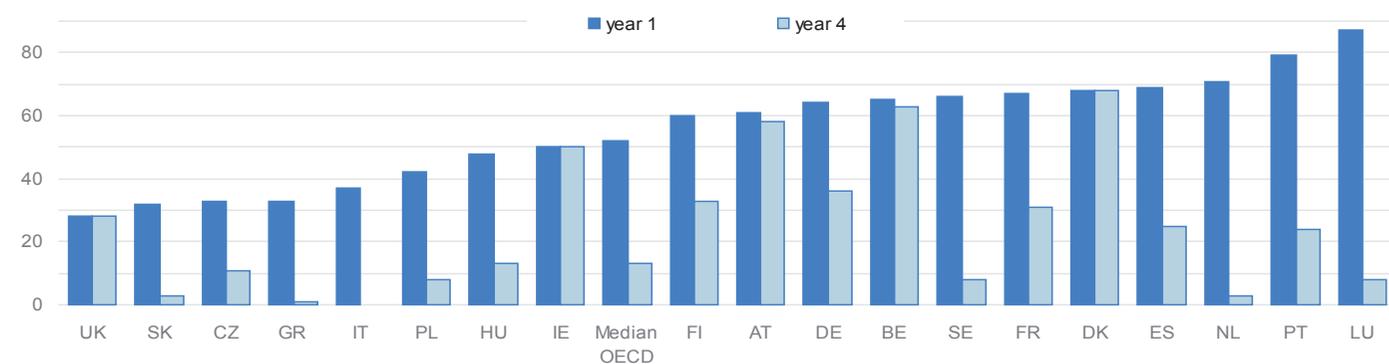
7.2 The crisis and the reforms of the social protection systems

Unemployment benefits as protection

A key element in sustaining confidence during a crisis is the ability of the state to assure workers that, should they lose their employment and hence their income, the social protection system will provide them with adequate income replacement as well as quality assistance in finding new employment within a reasonable period. Adequate employment safety nets are also important in order to avoid pressure upon and an increased influx into schemes that lead to permanent inactivity, e.g. disability and early retirement. Figure 7.4 displays the net replacement rates (averaged over different earnings levels and family situations) for the first and fourth years of unemployment for some EU member states. The generosity of the unemployment benefits varies greatly not only across EU member states but also across the time period. The median replacement rate in OECD countries is 52% for the first year of unemployment but this figure conceals a large variation ranging between a net replacement rate of 87% in Luxembourg and only 28% in the UK. There appears to be a grouping of southern and eastern member states that provide a net replacement rate below 50% and a grouping of Continental and Nordic member states providing one of above 50%. The net replacement rate for long-term unemployed decreases dramatically in

most countries, the exceptions being the UK, Ireland, Austria, Belgium and Denmark.

Figure 7.4 Net replacement rates (averaged over different earnings and family situations), 2007 (%)



Source: European Commission (2009a). Note: The net replacement rates displayed here are for prime-age workers (age 40) with a "long" and uninterrupted employment record. They assume that no social assistance or housing-related benefits are available as income top-ups for low-income workers.

7.2 The crisis and the reforms of the social protection systems

Adaptation of unemployment benefit systems

As already described in previous chapters in this issue of *Benchmarking Working Europe*, the social protection system has contributed to the prevention of job losses, especially via the various short-time working schemes that, in many countries, have been extended in terms of their duration, reason and eligibility (see Chapters 3 and 5). At the same time, however, there has been a sharp increase in the number of workers having lost their jobs (see Chapter 3) and these persons have been turning to the social protection systems for income support and assistance in their search for new employment (see Figure 7.3). With respect to these passive and active measures, while foundations were in place everywhere, these were much better designed in some countries than in others, so that the need for consolidation or reinforcement differs from one country to the next. Even so, all EU member states have taken a number of discretionary measures designed to alleviate the hardship suffered by the unemployed and to assist them in finding new employment.

When it comes to passive measures, at least sixteen countries have, as shown in Figure 7.5, introduced measures, both permanent and temporary, increasing the replacement rate, extending the duration of unemployment insurance and, finally, extending coverage to

groups of workers previously poorly covered with young people, especially, having been taken into consideration and granted better access to the unemployment benefit system. In Bulgaria and Poland the discretionary measures also included some that were designed to offer incentives to return to work. Certain countries, on the other hand, already hardly generous in a comparative perspective, have tightened up the eligibility criteria, duration or replacement rate. Hungary, for example, has tightened the conditions governing eligibility for long-term unemployment benefit; in the Czech Republic its duration has been shortened and the replacement rate made regressive

with the duration; in Ireland, finally, the jobseekers' allowance paid to new claimants aged under 20 years is to be reduced by 100 € per week.

To complement the unemployment insurance systems many countries (Belgium, Bulgaria, Cyprus, Czech Republic, Germany, Spain, France, Italy, Lithuania, Luxembourg) have also increased the generosity of their minimum income schemes, especially towards pensioners, families and children; in Hungary, however, the amounts have been frozen (Social Protection Committee 2009).

Figure 7.5 Discretionary measures on unemployment benefit systems

country	replacement rate or base of assessment	duration	eligibility criteria
AT	+		
BE	+		+
BG	+	+ (if training)	
CZ	+	-	-
GR	+		
ES		+	
FR	+		+
IE	- (below 20 years)		
IT			+
LV		+	+
LT		+	
PL		+	
PT	+	+	+
RO		+	
SE			+
FI			+
UK	+		

Source : OECD (2009), Social Protection Committee (2009), European Foundation for the Improvement of Living and Working Conditions (2009b).

7.2 The crisis and the reforms of the social protection systems

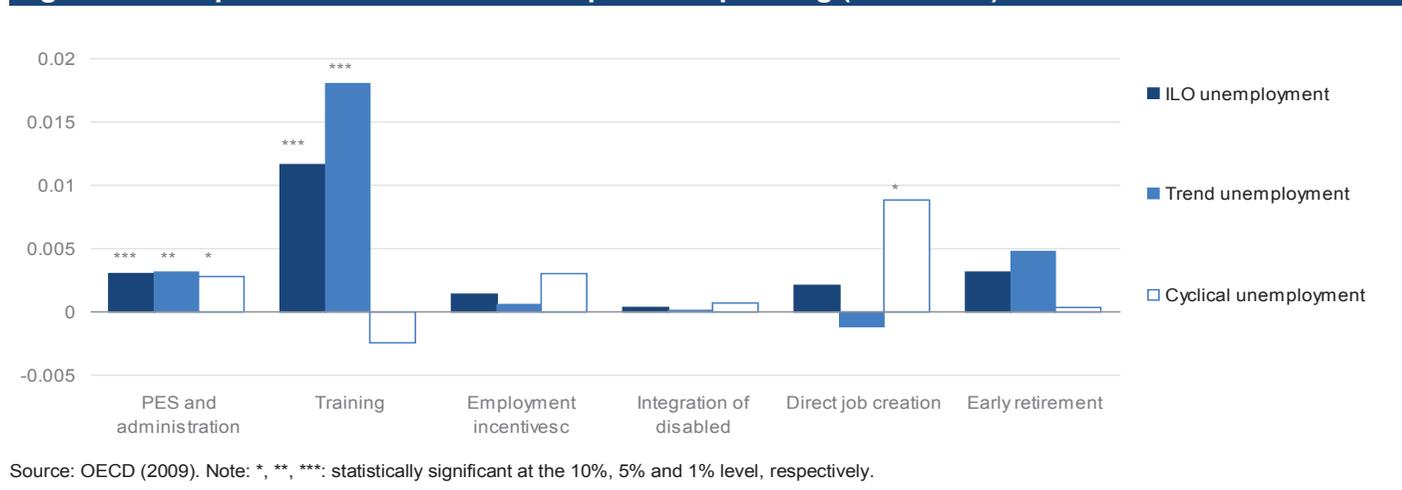
Extending and reinforcing the active measures

All EU member states have reported discretionary measures to reinforce training and counselling for unemployed; in particular the more vulnerable groups, like low-skilled and older workers, are targeted by these measures. The reported measures mostly focus on ensuring that the unemployed are counselled at an earlier stage than before and that a more individualised approach is taken with regard to the counselling; these measures aim at tightening the activation requirements, thereby promoting an active approach to unemployment benefits. Furthermore, there is considerable emphasis on ensuring that the unemployed are offered training at an early stage, even though it is somewhat doubtful – as shown in Table 3 – whether the institutions are actually able to provide more individualised and intensive counselling/training at a time of such large inflows. This raises the question of the extent to which the actions foreseen are actually realistic and able to be implemented and the doubts in this respect are compounded by the fact that, while the activation requirements imposed upon the unemployed are being increased, there seems to be less reporting on measures taken to reinforce the employment and outplacement agencies whose task it is to ensure that the planned measures are actually carried out. Hence

the main issue is whether the planned discretionary measures can be implemented in an adequate manner, given the divergence in the types of measures taken. The results presented in OECD (2009) on the reactivity of active and passive measures to cyclical unemployment (see Figure 7.6) seem to cast doubt on the ability of countries to set up, on a rather short-term basis, training measures as a response to cyclical unemployment. Past experience seems rather to indicate that it is easier to implement measures that promote direct job creation, reinforce public employment services and administration, and this observation points to the conclusion that, in order to react to cyclical

unemployment in a timely manner, there is a need to be able to build on existing structures. If there are no or only limited foundations on which to build training measures, then it proves very difficult to set up the appropriate training measures as a response to crisis. As such, this crisis will represent a litmus test for the efforts to provide training to the unemployed that have been promoted at policy level over the past ten years (European Commission 2009).

Figure 7.6 Responsiveness of active and passive spending (1985-2006)



7.2 The crisis and the reforms of the social protection systems

Beyond unemployment compensation and activation

It is not, however, only the activation, training and unemployment benefits functions of the social protection system that contribute to maintaining individuals and helping them back into employment. A large number of EU member states are using the social protection system to create incentives for direct job creation and subsidising the short-time working schemes. Several member states (Belgium, Germany, Finland, France, Czech Republic) are cutting employer social contributions on either a temporary or more permanent basis. Some of the reductions are targeted exclusively towards new hires or specific groups, especially youth and low-skilled workers.

Other measures that have been used extensively during previous economic and social crises are those that enable permanent withdrawal from the labour market, namely disability pensions and early retirement. While there is as yet little evidence that these measures are being used to any considerable extent, further restructuring can be expected during 2010 and 2011 and an increase in the use of these types of measure can probably be expected, in spite of the fact that they have undergone a roll-back over the past ten years.

The countries that have been hardest hit by the crisis have begun to see

the emergence of measures that are more negative in scope. Lithuania and Estonia have moved towards less generous health care regimes; pension increases have decreased in Estonia and there has been a pause in the pension contribution transfers to the second pillar. Ireland has abolished the early childhood care allowance, put in place a special pension levy on public wages and transferred pension fund assets from certain pension funds in universities and non-commercial state agencies. Romania plans to introduce a pension freeze, except for social pensions. Decreases in social transfers are foreseen in Ireland, while Lithuania has reduced the maternity leave benefits previously in force.

7.3 Conclusions

The current crisis has sparked unprecedented measures and not only those designed to stimulate the economy and save the financial markets. Governments have also reacted promptly to the looming social crisis and have consolidated and reinforced the safety net that serves to protect the unemployed and low-income workers. An unprecedented volume of discretionary measures have been adopted in the field of active labour market measures that have been revamped and reinforced in order to assist the unemployed in finding new employment and to help prepare the labour markets for a strong recovery. Unfortunately, this sudden upsurge in measures does not seem to have been matched to the same extent by additional funding (OECD 2009). Hence, the effectiveness of this upsurge in active measures needs to be closely monitored in order to evaluate its effectiveness during a steep downturn. Questions remain as to whether the EU member states are really in a position to implement the measures effectively; whether the financial means that have been set aside are adequate; and whether the proposed measures are, taken together, really the most appropriate ones under the circumstances.

As restructuring and unemployment will continue in the coming years, the

pressure on social protection expenditure will continue to increase; at the same time, there will be a major loss of revenue given that social contributions will decrease due to less employment, declining GDP and reductions in social contribution. As public deficits rise and exit strategies are put in place, social policies and social protection are likely to become the areas in which containment strategies are introduced. This vicious circle will be further exacerbated by the need to foresee the effects of demographic ageing. Hence the relatively few reforms so far introduced with the aim of cutting transfers and targeting health care and pensions could be precursors of the fate that awaits other social protection systems in the future.

However, the urge to contain costs within social protection systems should be tempered by an awareness of the financial sustainability mechanisms that are actually built into these systems. In other words, costs are anti-cyclical and will go down as employment goes up. Meanwhile, this crisis does seem to be providing substantial evidence that, in those cases where social protection systems are able to partly absorb and alleviate the stress of the downturn (thus playing the role for which they were originally set up), the crisis seems to entail less economic and social costs in the short term, and probably in the

long run too, insofar as productive capacity will not be eroded. The effects of the crisis and the reactions designed to offer protection against them should be monitored and evaluated in order allow us to build on the experience gained and to reform our systems in the light of such experience, rather than on the basis of a conviction that public deficits need to be reduced at any cost.