Converging Unemployment Insurance Schemes in the EU: Budgetary, Distributional and Stabilizing Effects

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Strengthening economic policy coordination and setting EU wide standards, for example for labor markets, is high on the political agenda in Europe. One important aspect in the debate is the convergence of unemployment insurance (UI) schemes with the aim to strengthen the automatic stabilization effects of UI and to make the Eurozone more resilient against macroeconomic shocks. In this paper we examine the budgetary, stabilizing and distributional effects if common minimum standards in UI systems were introduced. We then assess which countries would be most affected by such harmonization measures.

Our research strives to address these questions using a detailed microsimulation model for 26 EU Member States' unemployment systems. Using longitudinal EU-SILC data, we assess the effect of convergence in key policy parameters (qualifying to reference period ratio, duration of benefits, and net replacement rates) of EU Member States unemployment insurance systems. Our detailed microsimulation model allows to precisely simulate monthly unemployment benefits based on individual characteristics and national legislation or possible reforms in EU Member States. We employ longitudinal EU-SILC micro household data to conduct counterfactual simulations for the EU Member States Austria, Belgium, Bulgaria, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Greece, Hungary, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, and the UK. The analysis is supplemented with EUROMOD and LFS data. Our simulations model both gross benefits and net budgetary costs. These net costs account for taxation of unemployment benefits as well as for changes in means-tested benefits due to more generous unemployment benefits. We additionally assess distributional impacts: Additional benefits and changes in disposable incomes are calculated separately for each household income quintile. Simulating macroeconomic employment shocks, we take the status-quo policy as a baseline and contrast effects with scenarios in which unemployment insurance schemes are more harmonized.

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Our minimum reference values for convergence are in line with EU policy considerations. They are defined as a minimum duration of unemployment benefits of 6 months, a minimum 50 per cent net replacement rate for wages below 67 per cent of average wages, and a minimum eligibility criterion defined as a ratio of qualifying to reference period of 50 per cent. The analysis includes sensitivity analyses with more generous reference values for replacement rates (minimum net replacement rate of 60 per cent for wages below 80 per cent of average wages), duration of benefits (12 months) and eligibility criteria (ratio of 40 per cent).

We identify the countries which would be affected the most in each reform scenario, while our findings also capture cross-country differences in the duration and frequency of unemployment spells. If an economy is already in turmoil prior to a negative macroeconomic shock – i.e. if many people have discontinuous employment histories – increasing UI generosity has less of an effect. This is the case as long-term unemployed individuals or individuals with just short employment spells are not covered by UI, and would thus not benefit from an extension. In line with this, we show that EU-wide minimum UI standards would increase UI coverage by only a few percent in Greece, Spain and Italy. Likewise, countries already having rather generous UI systems, such as Austria, Denmark, Luxembourg, Finland and France, would not be affected much by an introduction of minimum standards. In contrast, UI coverage and benefits would increase the most in Latvia, Malta, Slovakia, Portugal and Cyprus. Our results thus indicate that UI coverage would be extended the most in countries with rather high requirements for receiving benefits and/ or a rather stable economy. Similarly, the scope of stabilization effects following an introduction of minimum standards differs between countries subject to a longer crisis and countries with a previously healthy economy.