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The Social Wage as a Mechanism for a Widespread Recovery in Living Standards

Daragh McCarthy

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SUMMARY

Recovery is underway. However, the economic collapse and years of considerable reductions in government spending mean the recovery is starting from a position where key public services are stretched, state-sponsored family supports diminished, and a lack of public investment in infrastructure around the country is hampering prospects of sustained economic growth.

Enhancing the non-pay returns to workers, the "social wage", involves improving standards of living through increased state support for households via transfer payments and expanded public services. The social wage can take the form of public provision of childcare services, state provided illness benefit, or enhanced support during periods of unemployment.

Maintaining the social wage requires the state's revenue base is protected. This can be made consistent with enhanced international competitiveness.

KEY POINTS

- The social wage offers the prospect of improved access to education and healthcare services regardless of ability to pay, while allowing the state to make job creating investments in infrastructure and enterprise
- Boosting the social wage comes at a cost. It is vital the overall level of revenue collected by the state is be protected
- Reduced government spending and a diminished social wage increase reliance on compulsory spending on essential services. Increased barriers to access for lower income households are a prominent feature of this model
- It is possible to be internationally competitive and prosperous with higher taxation and lower taxation

Nevin Economic Research Institute (NERI)

31/32 Parnell Square
Dublin 1
+ 353 (1) 8897722

e-mail: info@NERInstitute.net
Web: www.NERInstitute.net

Carlin House
4-6 Donegall Street Place
Belfast
BT1 2FN
Northern Ireland
+ 44 28 90246214



Research for new economic policies

Economic recovery and the social wage

Recovery is underway. However, the economic collapse and years of aggressive reductions in government spending mean the recovery is starting from a position where key public services are stretched, state-sponsored family supports diminished, core welfare rates cut for those under 26, and a lack of public investment in infrastructure around the country is hampering prospects of sustained economic growth. For workers in many sectors of the economy it is a recovery that has been characterised by an absence of wage increases and a consolidation of flexible patterns of work based on precarious terms of employment. In short, recovery in living standards has been sluggish.

Ireland has a low pay problem. As shown in the NERI's recent Quarterly Economic Observer, there are 345,000 people (25 per cent of all employees) below the Living Wage threshold of €11.45 per hour (NERI, 2015). The issue is compounded by the association of low pay with low hours and temporary contracts of employment. In this context, there is a strong case to start shifting wages to a point where they are sufficient for workers to meet the essentials of everyday life.

Wages and conditions of employment remain paramount, but making important aspects of life less dependent on take-home pay improves living standards and offers economic security for workers and their families. Enhancing the non-pay returns to workers, the "social wage", involves improving standards of living through increased state support for households via transfer payments and expanded public services. The social wage can take the form of public provision of childcare services, state provided illness benefit, or enhanced support during periods of unemployment. It offers the prospect of improved access to education and healthcare services regardless of ability to pay, while allowing the state to make job creating investments in infrastructure and enterprise.

Boosting the social wage comes at a substantial cost. With this in mind, the

overall level of revenue collected by the state should be protected. Plans to announce reductions in the contribution worker's make through the income tax system (including the Universal Social Charge) in Budget 2016 will diminish the state's capacity to meet demographic challenges and sustain public services at current levels.

Maintaining the level of revenue raised by the state is compatible with reforms to the mix of tax contributions made through labour, capital and goods. The "Quarterly Economic Observer, Summer 2015" (forthcoming) outlines a number taxation measures that tend to be consistent with the goal of enhancing economic growth and equity.

A model based on diminished government spending and a retrenchment in publicly provided goods and services is strongly linked with greater reliance on compulsory spending on essential services. This model increases barriers to access for low income households. An inadequate public revenue base results in households facing higher out-of-pocket charges. This dynamic has been visible across the economy over the past number of years as the government sought to reduce its expenditure by pushing higher charges on to citizens in the form of increased prescription fees, substantially higher public transport fares, and the introduction of water charges. Higher out-of-pocket payments mean households at the lower end of the income distribution will continue to struggle to gain access to healthcare services and social housing, for example.

Inadequate investment and infrastructure development damages the capacity of the economy to grow over the medium-to-long term. The state has a crucial role to play in making investments that enhance the capacity of the economy to grow (Mazzucato 2014). The European Commission estimates capital formation will reach 2 per cent of GDP this year—a level the IMF (2014) and IFAC (2014) have identified as problematic for the long-run prospects of the economic. Put plainly,

reducing the state's revenue base is likely to come at a cost to the wider economy.

Government revenue and international competitiveness

Public spending in the Republic of Ireland is at the lower end of the spectrum, with current budgetary projections on course to leave the primary—non-interest—expenditure share of economic output at a very low level historically (IFAC, 2014). Table 1 sets out a comparison of public spending in the Republic against the average for EU 15 countries. The IMF (2015) project the gap between primary spending as a percentage of GDP in Ireland and the EU 15 will widen over the coming five years, with current fiscal policy resulting in public spending levels well below comparable government expenditure levels in most advanced economies.

When compared to most EU states, the age profile of the population in Ireland puts less pressure on government spending. The European Commission's (2015) baseline scenario estimates total age-related government spending to be 22.1 per cent of GDP in the Republic, 4.2 per cent below the EU 15 average. In addition, defence spending in Ireland is consistently a percentage point below the EU 15 average. Presenting spending as a per cent of GDP is

standard international practice, though the appropriateness of using this measure in the case of Ireland is subject to long-standing, ongoing debate. Accounting for these factors, the Irish Fiscal Advisory Council points out the budgetary plans imply considerable pressures on government services, public investment and social payments (IFAC, 2014).

Diminishing the tax base is often justified on the grounds it improves competitiveness. However, higher levels of government revenue and spending can be made consistent with enhanced international competitiveness. The notion that high-to-moderate levels of taxation dim the prospect of economic growth is a fallacy; it is possible to be internationally competitive and prosperous with higher taxation and lower taxation (Wolf, 2015). Figure 1 ranks EU member states according to a ten-year average level, from 2005 to 2014, of government revenue as a percentage of GDP and compares this ranking against the same countries performance in the Global Competitiveness Report 2014-2015. The result shows no clear trend between high levels of government revenue and reduced international competitiveness.

Table 1: General government spending less debt interest payments, percent of GDP

	'11	'12	'13	'14	'15	'16	'17	'18	'19	'20
Public Spending										
Rep of Ireland	46.1	42.2	40.5	38.5	36.1	34.5	33.0	31.7	31.3	30.9
EU 15 average	49.4	49.8	49.2	48.9	48.0	47.3	46.7	46.2	45.9	45.7
Interest payments										
Rep of Ireland	-2.9	-3.6	-3.8	-3.6	-3.0	-2.9	-3.0	-2.8	-2.9	-2.8
EU 15 average	-2.3	-2.2	-2.1	-2.1	-1.9	-1.9	-1.8	-1.7	-1.7	-1.7
Public spending less interest										
Rep of Ireland	43.2	38.6	36.7	34.9	33.1	31.6	30.0	28.9	28.4	28.1
EU 15 average	47.2	47.5	47.1	46.8	46.1	45.4	44.9	44.5	44.2	44.0

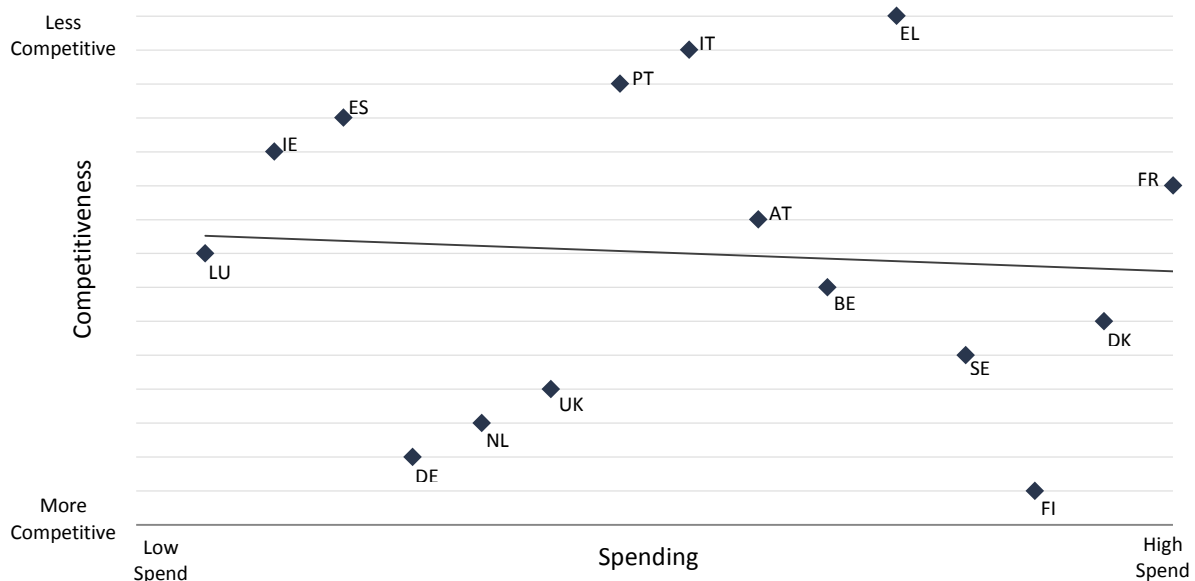
Source: Author's calculation based on International Monetary Fund (2015) Fiscal Monitor, April 2015; ; Table A1 & Table A2 <http://www.imf.org/external/pubs/ft/fm/2014/01/pdf/fm1401.pdf>

Conclusion

Unemployment, illness and parenthood are permanent features of working life. Core pay rates remain crucial, but good public services have an important role to play in helping households manage costs associated with these events. Reduced government spending and a diminished social wage increase reliance on compulsory spending on essential

services—increasing barriers to access for lower income households. In addition, undermining the state’s revenue base will likely reduce the scope for public investment that enhances the capacity of the economy to grow. There is no clear evidence reducing taxation enhances international competitiveness.

Figure 1: Ten-year average general government spending (2005 - 2014) and 2014 global competitiveness rankings, EU28 countries



Source: International Monetary Fund (2015) *Fiscal Monitor*, April 2015 <http://www.imf.org/external/pubs/ft/fm/2014/01/pdf/fm1401.pdf> and European Commission (2015) *Government Finance Statistics database* <http://ec.europa.eu/eurostat/web/government-finance-statistics/data/database>

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