JobMatcher

Real unemployment insurance

Blueprint Institute

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About Blueprint Institute

Every great vision starts with a blueprint. We help move ideas to action. Blueprint Institute exists to inspire reform by presenting bold ideas, honest conversations, and evidence-based research. We offer fresh thinking to help leaders take a step back from the day-to-day and see the bigger picture. We design blueprints for practical action as a step towards creating a more resilient and prosperous Australia.

Blueprint Institute was established in the era of COVID-19, in which Australians have witnessed how tired ideologies have been eclipsed by a sense of urgency, pragmatism, and bipartisanship. The challenges our nation faces go beyond partisan politics. We have a once-in-a-generation opportunity to rethink and recast Australia to be more balanced, prosperous, resilient, and sustainable.

For more information on the institute please visit our website—blueprintinstitute.org.au.

Acknowledgements

This work was originally inspired by a figure designed by Matt Cowgill at the Grattan Institute (see Figure 1), which visualised how out of step Australia's unemployment benefit is relative to the step-down systems that are ubiquitous among other wealthy countries. Thanks to the various experts who have been consulted on the development of this work, and for the excellent research assistance provided by Matthew Elias.

Images courtesy of UnSplash.

Attribution

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Summary

Australia doesn't have true unemployment insurance. Not really. Instead what we have is a fairly meagre form of permanent welfare—not too high to prevent recipients from accepting whatever work they can get, but not high enough to ensure a dignified standard of living. With its universal, flat, and very low rate, our one-size-fits-all unemployment benefit fits nobody well. By lumping together the short- and long-term unemployed into one system, the Government is left hamstrung—forced into a trade-off between living standards and work incentives.

But there's a better way. Almost every other rich, advanced country—Canada, South Korea, Israel, you name it—does it differently. They all offer a high initial rate—usually a portion of the former wage—that steps down at some point to a lower level. The high initial rate helps people weather the temporary income shock, and provides them ample opportunity to search for the job that's right for them and for their employer.

It's hard to believe that today Australians receive very little protection from income risk due to unemployment. A significant portion of people live paycheck-to-paycheck. And for many, the only source of debt finance is a high-interest credit card. The private market for unemployment insurance is virtually non-existent, with super funds refusing to cover it and only a small handful of insurers offering it under restrictive terms and at high prices. It's hard to imagine a stronger case for government intervention.

Australia should introduce real unemployment insurance, called 'JobMatcher', which would:

- top up the existing benefit to 70% of the individual's former wage for the first six months;
- be capped at $35,000 and limited to a cumulative six months every two years; and
- be fully funded by a 1% JobMatcher Premium administered like the Medicare Levy.

By paying into the system, people earn the right to access it when they fall on hard times. Because an unemployment spell can happen to any of us, everyone who contributes also benefits.

JobMatcher would offer substantial benefits to recipients, employers, taxpayers, and the economy, including:

- getting people off the dole faster;
- getting workers back into better jobs;
- smoothing the temporary income shock; and
- serving as an automatic stabiliser.

In the debate about the unemployment benefit, the only thing anyone ever talks about is the rate. While the rate for the long-term unemployed should rise, we're much further out of step with the rest of the world when it comes to our short-term benefit. The Government recognised as much by supplementing JobSeeker during the crisis—but only for a limited time. Job losses don't only occur during recessions—the risk is ever-present. A real unemployment insurance system should be one of the few good things we take with us beyond the crisis.

Our one-size-fits-all unemployment benefit fits nobody well

Australia has a single system, called JobSeeker (formerly Newstart), to support all unemployed people. During normal times, it provides a flat payment of $565.70 per fortnight (for single people aged 22–66 without children), which is just 38% of the full-time minimum wage and 17% of the full-time average wage. The payment remains at that rate indefinitely, provided the recipient fulfils a set of mutual obligations, and satisfies income and assets tests. The Government also provides supplementary rent assistance of up to $139.60 per fortnight.

Around a million Australians receive unemployment benefits each year. Australia's flat, one-size-fits-all JobSeeker benefit attempts to service two distinct groups. The first is those who experience short stints of unemployment lasting less than a year—half of people who've ever been unemployed. The second is the long-term unemployed. The current system serves neither group particularly well.

As it stands, JobSeeker isn't a true form of unemployment insurance, though we rely on it to serve as one. With its open-ended structure and low rate, which differs neither across people nor time, JobSeeker is really a fairly meagre form of permanent welfare geared towards the long-term unemployed. By being forced to be all things to all people, JobSeeker fails to fully satisfy anyone.

All OECD countries, other than the UK, Ireland, and New Zealand, provide unemployment benefits that step down, offering a high but time-limited initial payment that reverts to a lower rate at a later date (see Figure 1). But even the UK and Ireland have an initial period (26 and 39 weeks, respectively) partly funded by prior social security contributions. During this period, the recipient isn't subject to assets or partner income tests, which means the system functions more like true unemployment insurance. In Ireland, the initial payment is based on prior income, later reverting to a flat rate.

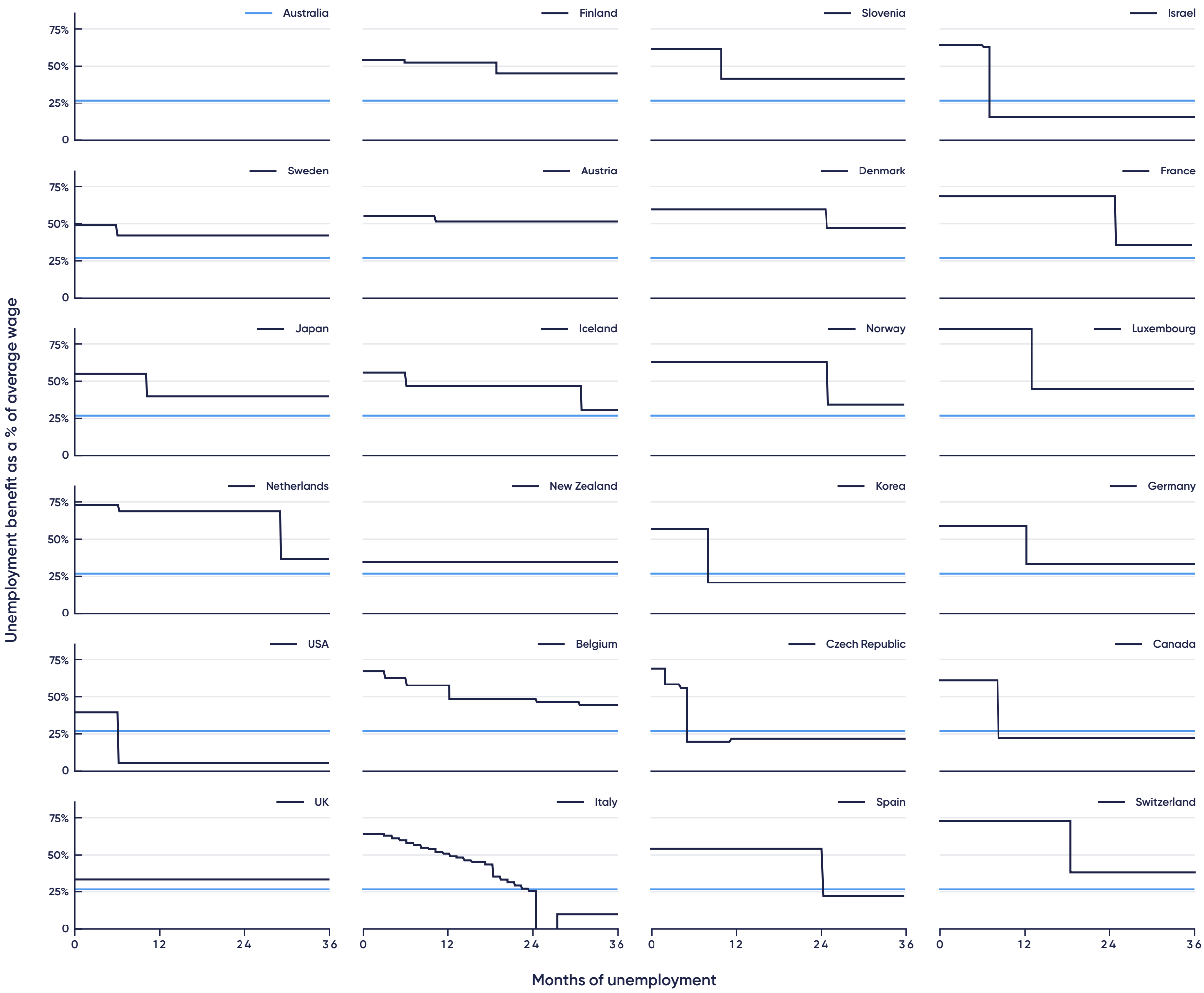

Figure 1 Unemployment support relative to the average wage among OECD countries

Source Designed by Matt Cowgill at the Grattan Institute; OECD; Blueprint Institute analysis

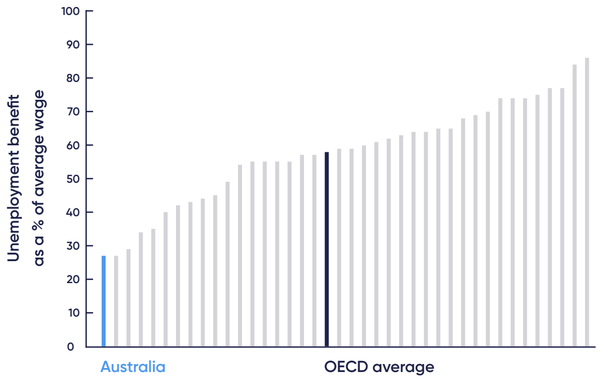

Figure 2 Unemployment benefit replacement rate after two months of unemployment

Source OECD

Note Includes social assistance and housing benefit.

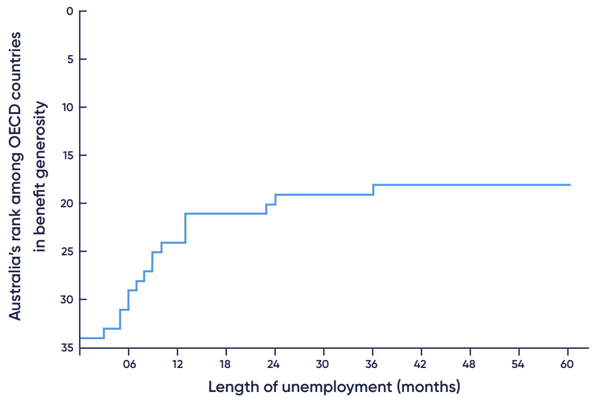

Figure 3 Australia's rank among OECD countries, in terms of the unemployment benefit as a percentage of the average wage, by length of unemployment

Source OECD

Note This replicates the relative support nations provide to unemployed people; Australia is joint lowest in short-term benefits, before arriving at the middle-of-the-pack for long-term support.

All of these systems recognise there is a difference between short- and long-term unemployment. The initial high rate, typically related to the recipients' prior income, cushions the temporary income shock. Time limiting the payment provides workers the opportunity to find new employment and discourages them from transitioning to long-term unemployment.

By providing the same payment to all recipients regardless of their fixed financial commitments, JobSeeker fails to adequately cushion the temporary income shock caused by unemployment. And by providing that same payment indefinitely, any attempt to raise the rate to better fill this income gap runs into a trade-off against the desire to prevent long-term unemployment. The Government is hamstrung by this flat payment structure.

As a result, at just 27% of the average wage, Australia's short-term unemployed receive the lowest unemployment benefit among OECD countries—and less than half the OECD average (see Figure 2). In Canada, a close peer to Australia in many ways, the initial payment is 62% of the average wage, falling to 23% after nine months. Canadians pay an insurance premium of around 1.6% of earnings to fund these benefits. In South Korea, the initial payment is 57% of average wages, before falling to 21% after eight months. In Israel, the initial payment is 64% of average wages, falling to 16% after eight months. Step-downs are ubiquitous in Europe too.

Figure 3 shows how Australia's unemployment benefit ranks relative to 33 other OECD countries depending on how long the unemployment spell lasts. While Australia's flat rate falls well below the poverty line, it is in fact right in the middle of advanced countries globally in terms of long-term unemployment compensation. While we could (and should) offer more generous compensation to the long-term unemployed, it is plain that we are most out of step in terms of how we compensate the short-term unemployed.

The Government has already acknowledged this problem, at least implicitly. In the first three months of the pandemic, the number of JobSeeker recipients doubled to nearly 1.5 million. Recognising this surge in short-term unemployment, the Government nearly doubled the base rate of JobSeeker, but only for a limited time—initially for six months, then for a further six at lower rates.

For anyone who entered their unemployment spell during the pandemic, Australia's unemployment benefit system has operated just like the step-down systems seen in almost all of our peer countries. But jobs aren't only lost during pandemics. Job losses occur constantly for myriad reasons beyond a person's control. The need for insurance against the risk of job loss is always present. A step-down unemployment insurance system is needed now and in the future, just as it was needed a year ago.

Step-down systems require rules to prevent overuse

To discourage gaming of step-down systems, many countries implement more stringent eligibility criteria to access the initially higher benefit payment than those required to access JobSeeker in Australia. In Germany, a worker must have paid a certain number of contributions over the two years preceding unemployment to claim support. This is mirrored in the UK, where National Insurance contributions are required in order to be eligible to claim Jobseeker's Allowance.

In other countries, a certain quantity of work must have been performed—in Canada, for example, recipients must have worked the required number of insurable hours in the last year. The required number of hours depends on the regional unemployment rate, and ranges from 420 to 1,400 hours. In 29 of 33 OECD countries, a certain value in insurance contributions or paid work is required for an unemployed worker to be eligible for these initial, generous unemployment benefits.

Some countries require a sufficient time gap between the current benefit claim and previous claims. For example, in Iceland, after three years on unemployment benefits, two years must elapse before an individual is entitled to further support. In almost all jurisdictions, unemployment must be involuntary. And, similar to Australia's mutual obligations, job seekers must complete set tasks to show they are looking for suitable work.

JobMatcher

Real unemployment insurance

The Government should introduce a system of true unemployment insurance—we call it JobMatcher. JobMatcher would overlay the existing JobSeeker scheme, topping up the existing payment to 70% of a recipient's former wage for six months (see Figure 4). This replacement rate and duration are similar to those in peer nations such as Canada, Israel, and The Netherlands. The payment would be taxable, as with JobSeeker. After six months of unemployment, the recipient could continue on the lower JobSeeker payment.

Payments would be capped at $2,692.30 per fortnight—equivalent to 70% of a $100,000 annual salary. This means that the 90% of working Australians who earn up to $100,000 a year would receive the full 70% of their prior wage. Higher-income earners can be expected to more easily rely on liquid assets to cushion the temporary income shock of unemployment.

To prevent overuse, JobMatcher would be limited to those who have not claimed Job-Matcher, JobSeeker, or Youth Allowance for more than an accumulated total of six months in the previous two years. The payment would also be independent of spousal income—there would be no spousal income test for JobMatcher, and the JobMatcher component would not be counted towards a spouse's income test.

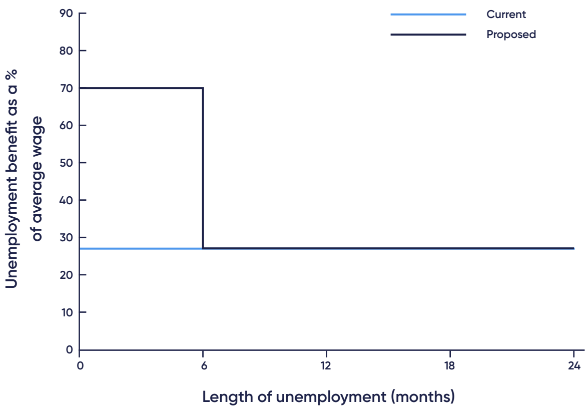

Figure 4 Step-down support under the JobMatcher scheme
Source Blueprint Institute analysis

JobMatcher would only be available for newly unemployed people from the point at which the policy is enacted (e.g., from 1 July, 2021). Job-Matcher recipients would need to continue to meet the mutual obligations that apply to Job-Seeker.

The length of time people receive JobMatcher will vary according to the pattern of unemployment duration in the population, with a fixed cap of six months. This will, of course, depend on the effectiveness of the scheme in reducing long-term unemployment. But it also affects the program's cost. At any given time since 1991, an average of 21% of unemployed Australians have been without work for less than a month, 24% for one to three months, 16% for three to six months, and 39% for more than six months.

Recurrent unemployment is a common occurrence within the Australian working population. JobMatcher would have the added benefit of better worker-firm matches that would naturally lower the re-entry rate into unemployment. Banking the savings from the program's structure, the JobSeeker payments replaced by JobMatcher, and the tax receipts generated by this additional income, our estimates place the JobMatcher scheme at an incremental annual cost of around $9 billion.

Real insurance premiums

JobMatcher is real unemployment insurance, so it should be funded by real insurance premiums. These are called JobMatcher Premiums, to be administered in the same way as the Medicare Levy. By paying into the system, people earn the right to access it when they fall on hard times. Because an unemployment spell can happen to any of us, everyone who contributes also benefits. This is critical to the scheme securing broad, lasting community support.

In order to fund the $9 billion cost of the JobMatcher scheme, the JobMatcher Premium would need to be set at around 1% of income, with all income below $22,801 exempt (see Figure 5). This is similar to the 1.58% premium set in Canada to fund their similarly generous unemployment insurance system. Given that benefits are proportional to income, and provided that the likelihood of becoming unemployed is the same for all income levels, the scheme is actuarially fair for the vast majority of taxpayers. However, because of the payment cap and the phase-in range for the premium, on net the scheme benefits the very lowest income earners and costs the very highest income earners.

This approach is budget neutral, funded by higher receipts. Alternatively, receipts could be held constant and the scheme funded by greater debt issuance. This could be achieved simply by adjusting down the income tax scales by 1% in the Medicare Levy income range. Or the cost of the scheme to taxpayers could be offset by cancelling the 1pp increase in the Superannuation Guarantee due to occur over the next 18 months, which can otherwise be expected to lower wages by 0.8pp.

JobMatcher will drive productivity and growth. A body of evidence suggests that a step-down in unemployment benefits would shorten unemployment spells and boost wages—decreasing JobSeeker spending and increasing tax revenues. While impossible to precisely quantify, these effects will undoubtedly work to partly offset the budgetary impact of JobMatcher, and could be substantial in the long run.

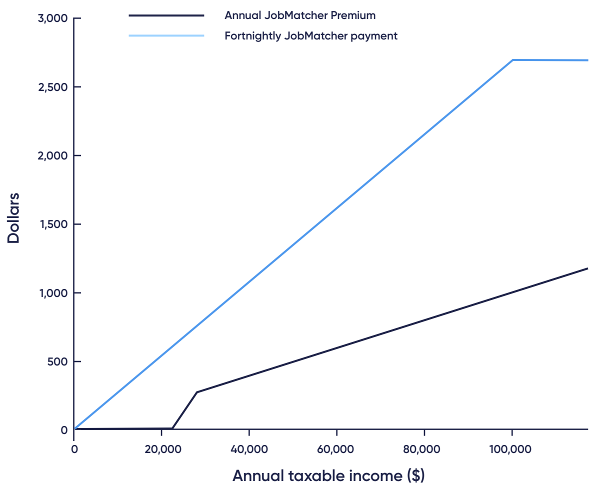

Figure 5 JobMatcher Premium and payments at different income levels

Source Blueprint Institute analysis

Note The phase-in uses the same range as the Medicare Levy, beginning at $22,801 and finishing at $28,501.

Real benefits

JobMatcher gets people off the dole faster

The relatively generous but time-limited nature of JobMatcher incentivises job searching and reduces the risk of welfare dependency. Increased support in a step-down system of unemployment insurance does not harm job search motivation, nor does it decrease the likelihood of leaving unemployment for a new job. In fact, higher, time-limited unemployment insurance incentivises active job searching. This is especially true for those who would otherwise drop out of the labour force altogether, as it provides a financial safety net to explore other options.

Providing a generous initial payment not only gives workers the freedom to find a better match, but also a hard deadline. The time-limited nature of JobMatcher leverages a behavioural concept termed loss aversion: people feel more pain in losing something than they do joy in gaining it. The impact of this effect was shown in France, where job search effort increased by 51% in the year prior to a decline in support (from 68% of the average wage to 35%).

Frontloading unemployment benefits has also been found to speed up re-employment. In Hungary, reform of a flat payment to a step-down system meant recipients received a raised level of support for the first 90 days, after which support was halved. This reduced unemployment duration by two weeks, and increased re-employment wages by 1.4%. In a similar vein, the Spanish Government passed reforms following the Global Financial Crisis (GFC) to speed up re-employment. At the start of unemployment, Spanish workers receive a benefit equal to 70% of their average unemployment contributions over the previous six months. Prior to the GFC, this was reduced to 60% after 180 days. But from 2012 onwards, support was cut to 50%. This reform increased the likelihood of a worker finding a job by 41%.

JobMatcher gets workers back into better jobs

Getting the right worker into the right job benefits both workers and firms. Preserving these valuable worker-firm matches was in fact one of the motivations for the Government's $101 billion JobKeeper wage subsidy scheme introduced during the crisis. When supported by higher unemployment benefit payments, workers are more likely to find a full-time, fixed-term, and/or permanent contract job that lasts longer and pays higher wages. In the US, this effect was shown to be particularly significant for individuals with low savings.

Consumption commitments hinder effective job search behaviour, forcing newly unemployed people to be overly risk-averse and to accept safer jobs when their skills could be utilised more productively elsewhere. The liquidity effect of higher unemployment benefits allows workers to search for longer, so they can find more rewarding jobs better suited to their skills; in turn, this generates positive knock-on effects in the labour market, boosting economic efficiency.

Firms benefit from this too. Better job-match quality leads to increased profitability, as it has wide-ranging benefits for productivity and innovation. Insufficient unemployment support also has costs. Low job-match quality correlates with high staff turnover, absenteeism, and weakened labour market performance.

JobMatcher smooths the temporary income shock

A massive 43% of Australian households spend all of their household income (or more) each month. With such a high proportion of Australians living paycheck-to-paycheck, an unanticipated income shock has the potential to devastate a large number of people. And imperfect capital markets mean many people are only able to incur a limited amount of debt at very high interest rates.

Moreover, the problems of moral hazard and adverse selection in private insurance markets are significant, making actuarially fair income insurance uneconomic for large segments of the population. While superannuation funds offer income insurance for disability, they don't offer it for redundancy. There are in fact just four redundancy insurance plans available on the market—their terms are very restrictive, and their premiums very expensive. For all intents and purposes, the private market for unemployment insurance has failed.

Without access to insurance, savings, or borrowing, households must respond to an income shock by decreasing their consumption. Were that consumption shock to be spread evenly across the household budget, it would be costly enough. But in reality, households have large, inflexible consumption commitments—making up over 50% of the household budget on average—which means the consumption reduction must be concentrated among the few items over which the household has some control. This raises the experienced impact of the income shock even further.

For all recipients, JobSeeker does a very poor job of filling the income gap—for some much worse than for others. By tracking an individual's former wage, JobMatcher would smooth the income shock of a temporary unemployment spell. Individuals would have the financial security to pay critical bills and ensure their needs are met. This would reduce the economic damage and psychosocial stress that results from short-term unemployment. JobMatcher would serve as a true safety net, preventing substantial harm.

JobMatcher is an automatic stabiliser

Unemployment insurance stabilises aggregate demand by smoothing fluctuations in disposable income during economic shocks. Countries with more generous unemployment insurance are less reliant on discretionary fiscal stimulus measures during a crisis. During the GFC, unemployment benefits alone absorbed 19% of the economic shock in Europe, compared to just 7% in the US—whereas the stabilising effect of income taxes was similar in both regions.

Providing a greater proportion of a worker's income in the initial period of unemployment would be a much more aggressive automatic stabiliser than the current JobSeeker design. Australia could wait until the next crisis to implement unemployment insurance. But rushed implementation leads to imperfect program design. And reactionary changes to benefit systems—or the creation of new benefits—take time to implement and deliver.

This was the case during Australia's response to COVID-19. JobKeeper was announced on 30 March 2020, 19 days after the WHO declared a global pandemic. But the first JobKeeper payments weren't made until May. Integrating a more generous JobMatcher payment into our benefit system now would better prepare Australia for future economic shocks, helping to minimise their negative impact on consumer confidence, economic activity, and household spending. These advantages are outlined in Figure 6.

Real benefits of a step-down system

1.

GETS PEOPLE OFF THE DOLE FASTER

Step-down unemployment support reduces the risk of welfare dependency and incentivises job seekers to find work by providing a hard deadline at which support will be reduced.

2.

GETS WORKERS BACK INTO BETTER JOBS

The liquidity effect of higher unemployment insurance for six months allows workers to search longer and find jobs better suited to their skills.

3.

SMOOTHS THE TEMPORARY INCOME SHOCK

A step-down system with a more generous initial payment will cushion the economic damage and psychological stress of short-term unemployment.

4.

IS AN AUTOMATIC STABILISER

Step-down unemployment support stabilises aggregrate demand by smoothing fluctuations in disposable income.

Figure 6 The advantages of a step-down system of unemployment support

What about JobSeeker?

Not all workers find a job in six months. Some take longer, and others may never find a job at all. Indeed, the RBA classifies 1.25% of Australians as long-term unemployed. Support for Australians experiencing long-term unemployment should be structured so that the incentives to work are maintained and the burden on taxpayers is minimised. But the wider debate surrounding an increase to JobSeeker for the long-term unemployed should be one grounded in values, not economics.

Reasonable people can disagree on exactly what the rate should be. But it's hard to disagree with RBA Governor Philip Lowe, and a large number of economists, who argue JobSeeker should be increased. Indeed, the announcement of the JobSeeker Coronavirus Supplements to support those affected by COVID-19 shows that the Government understands JobSeeker is insufficient to meet basic needs.

During normal times, JobSeeker provides only around a third of the full-time minimum wage. Australia ranks 19th out of 33 OECD countries in terms of its support for the long-term unemployed (see Figure 7). One reason for this is that JobSeeker is indexed to prices, rather than wages, so over time it hasn't risen in line with living standards. As a result, the long-term unemployed are increasingly isolated and marginalised, unable to take part in many of the same activities as average Australians.

The pension, on the other hand, is benchmarked to wages rather than prices—starting at 25% of annualised male total average weekly earnings (MTAWE) from the 1970s, followed by an increase to 27.7% in 2010—and has also increased with certain supplements over time. This has allowed it to rise during periods of rapid economic (and wage) growth. As a result, the pension rate has grown in real terms to $944.30 per fortnight—40% higher than JobSeeker (see Figure 8).

We believe the Government should do more to help those experiencing long-term unemployment. As a wealthy and prosperous liberal democracy, Australia can afford to provide generous support to those of us with the least. No Australian should be left behind; no one on JobSeeker should be forced to choose between basic necessities.

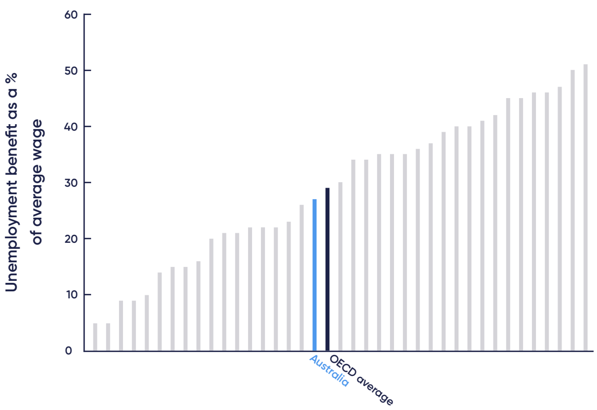

Figure 7 Unemployment benefit replacement rate after three years of unemployment

Source OECD

Note The prevalence of housing and social assistance benefits available to the unemployed in some countries, which supplement standard unemployment insurance, means that they have been included. This is in line with the OECD's analysis.

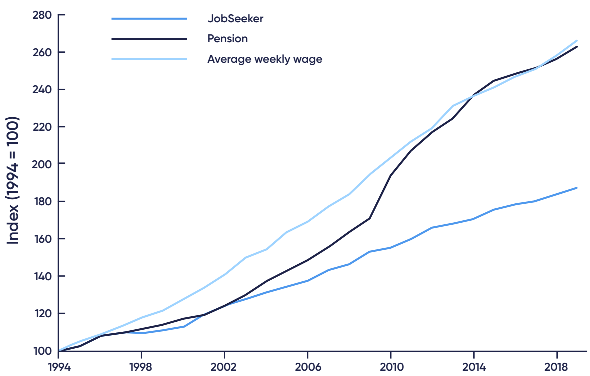

Figure 8 The growth rate of the unemployment benefit and pension compared to the average wage (1994-2019)

Source Department of Social Services, Australian Taxation Office

With that in mind, maintaining the current Coronavirus Supplement of $150 per fortnight indefinitely is warranted. This would take the total payment to $715.70 per fortnight. A one-off increase helps to make up for inadequate indexing in the past. At this level, the payment would still be a little less than half the full-time minimum wage. Additionally, going forward, the payment should be indexed to wages rather than prices in order to keep pace with living standards. The combined effect of these changes and JobMatcher is shown in Figure 9. It's important to note that any increase to Job-Seeker would reduce the cost (and premium) of JobMatcher.

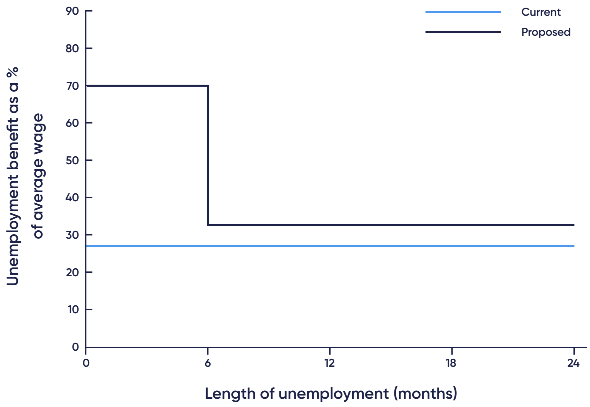

Figure 9 JobMatcher paired with an increase to the permanent rate of JobSeeker

Source Blueprint Institute analysis

Blueprint Institute