UNEMPLOYMENT INSURANCE: WHAT TO DO DURING GROWTH?

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During the recent financial crisis, unemployment insurance served as a countercyclical measure instrument for nations that had them in place. The benefits of these instruments were reinforced by increases in the duration of benefits and their integration with job retention programmes.

In a phase of economic recovery and employment growth like the one we are experiencing today, there is a need to evaluate the operation of this insurance and the impact of the reforms applied in order to strengthen them and determine which changes are to be institutionalised. The main contribution of unemployment insurance to an economic recovery process with job creation is improved efficiency of the job search process to help workers find positions that match their skills during the time when they receive benefits. Adequate design can contribute to a better fit between job supply and demand by improving the quality of searches for new employment as well as attaining productivity increases associated with better wages in the new job. In this sense, unemployment insurance and active labour market policies should be better coordinated. Developing appropriate and integrated intermediation and training services will allow beneficiaries to take advantage of the new opportunities for productive employment created by an expanding economy.

Countries that have yet to introduce unemployment insurance should consider the possibility of including this insurance in their social protection systems in order to improve their position in a future crisis.

1. Introduction

Those Latin American countries that have unemployment insurance based on contributions and formal labour relationships are Argentina, Brazil, Chile, Ecuador, Uruguay and the Bolivarian Republic of Venezuela. In general, unemployment benefits are provided for a limited amount of time, offer low levels of income, and protect individuals facing cyclical unemployment or unemployment related to information shortfalls in the labour market. Insurance coverage is limited by the informality of these economies and high turnover rates that keep workers from meeting minimum eligibility requirements. Part of these limitations is being addressed through transfer programmes, but another part can be corrected by adjusting unemployment insurance. These tasks can be undertaken during times of economic growth, when systems are under less pressure.

2. The Countercyclical Role

Unemployment insurance is typically countercyclical. This means that resources spent on such initiatives increase as the economy enters a recession and unemployment increases. However, when the economy grows and net jobs are created, the use of this benefit drops. This process occurs automatically and acts as a stabilizing force during recessions by sustaining the consumer spending of unemployed individuals. The effectiveness of unemployment insurance depends on the effective coverage provided to beneficiaries, the size of the benefits, and the ability to fund them.

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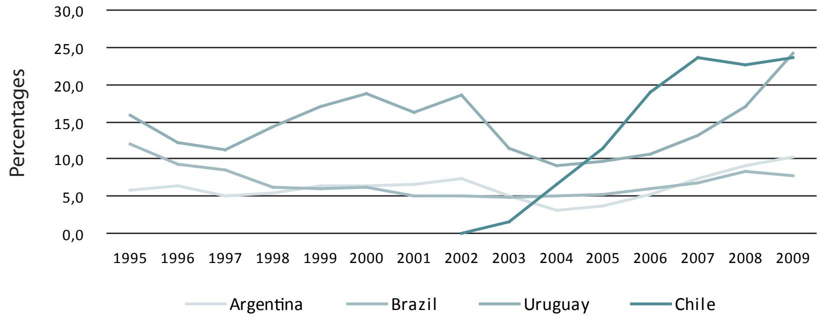
Figure 1 provides a general idea of effective coverage[2] measured as the number of beneficiaries compared to the total number of unemployed individuals for the four countries for which data were available.[3] Note the increase produced during the recent economic crisis.

Figure 1
Unemployment insurance coverage in Argentina, Brazil, Chile and Uruguay, 1995-2009
(as a percentage of the total number of unemployed individuals)



Source: Prepared by the author based on data from MTESS (Argentina), MTE (Brazil), Sistema de Pensiones (Chile) and BPS (Uruguay), 2010.

It is important to bear in mind that these systems present significant differences. For example, in Argentina unemployment insurance functions as a distribution or share fund with contributions made by employers, while in Brazil funding comes from the Workers' Protection Fund (*Fondo de Amparo del Trabajador*), which is funded in turn by corporate taxes, and provides contributory, non-contributory (fishermen) and voluntary (domestic workers) benefits. In Chile, unemployment insurance is based on individual accounts and a distribution fund, and domestic workers have an individual account for all events. Finally, in Uruguay benefits are funded through a single general contribution that is used to fund all types of social security benefits.

It is a fact that the duration of unemployment increases during recessions. Some of the recent reforms or specific measures that were implemented in response to the economic crisis have to do with the extension benefits during such periods. In Brazil, benefits were extended for two months for workers fired from the mining sector and the iron and steel industry between December 2008 and January 2009, which is when the greatest number of layoffs occurred. By contrast, Chile's 2009 reform allows for the activation of two additional payments whenever the unemployment rate exceeds the trend of the past four years. It also included fixed term contract workers and granted new benefits to labour retention programme beneficiaries. Although Uruguay's 2008 reform established an extension of the subsidy in case of recession, this mechanism was not activated because the two consecutive quarters of negative growth that define such a situation were not observed. By contrast, there was increased use of "worker suspension", which is a mechanism by which enterprises can place workers on unemployment insurance for up to six months when they are facing difficulties without having to break the labour relationship. Under this condition, enterprises retain the option of reincorporating these workers into their staff when their situation improves.

The increase in coverage in Brazil during the economic crisis was moderate because expansion of the insurance had a more limited reach given that it was only applied in specific economic sectors. While coverage was extended in Argentina during 2009, the change was moderate because efforts were aimed at increasing the coverage of non-contributory programmes (such as the Training and Employment Insurance Programme) and priority was given to employment retention mechanisms through subsidies in the context of the Productive Recovery Program (REPRO - Programa de Recuperación Productivo) in order to avoid lay-offs. In this case, the focus has been moving towards active policies centred on regional economic development and municipality-specific initiatives, through the creation of a broad network of public employment services.

3. Recent reforms

Over the past few years, a series of improvements have been made to the design of these programmes. To increase beneficiary coverage, special benefits were given to specific groups. For example, in Chile, coverage of

2 In order to measure coverage more precisely, one must consider the total population that potentially meets benefit eligibility requirements as well as the sufficiency and duration of such benefits.
3 Data for Ecuador's system were unavailable.

the Solidarity Unemployment Fund was extended to fixed term contract workers, while the duration of benefits for workers over the age of 50 was increased in Uruguay. In Argentina, coverage was extended to farm workers in 2004, a change that came on the heels of the introduction of protection for construction workers in 2000.

In Brazil, unemployment insurance is paid to workers in the fields of traditional fishing and to those rescued from forced labour (non-contributory benefits). Since 2000, domestic workers have been included in the programme if the employer makes voluntary contributions to a Service Guarantee Fund. Finally, all workers, apprentices, domestic workers, workers who provide services in the home and rural workers have been covered in the Bolivarian Republic of Venezuela since 2005, as have self-employed workers, those who belong to cooperatives, and others engaged in productive or service-type activities.

Furthermore, complementary measures have been considered to protect the balance between income and expenditures. For example, Chile decided to reassign part of the employer's contribution to the Solidarity Unemployment Fund to finance new benefits for fixed term contract workers. In 2005, the Bolivarian Republic of Venezuela increased employer contributions from 1.7% to 2% of wages while establishing full contribution payments for self-employed workers. The government was authorised to subsidise up to 50% of that contribution for low-income workers.

Still other initiatives are designed to keep workers in their jobs, such as those introduced in Uruguay (suspension) and Chile (training leave), which are linked to unemployment insurance to ensure the funding of cash benefits. The purpose of these actions is to keep workers in their jobs and train them so that they will have an increased ability to retain jobs or to rejoin the labor market once the effects of the economic crisis subside. In Chile, training was financed through public resources through the use of the tax franchise, while the cash benefit had corporate financing as well as funding through unemployment insurance. Finally, an effort was made to strengthen integration through active policies, linking monetary benefits with support services for unemployed workers who are searching for a new position. Such policies are meant to reduce the search times and improve the efficiency of job markets.

4. Contributing to growth through employment

The experience analysed serves to illustrate the scope of protection provided by unemployment insurance as well as the boundaries. It also allows identifies the priority functions of insurance, either providing partial compensation for a limited amount of time for the loss of wages or providing support during the search for a new position, considering the stages of the economic cycle. Table 1 provides a structured vision of the priorities that inform the operation of these programmes in contexts of crisis, recovery and growth.

During a contractionary phase of economic activity, there is an increase in the number of unemployed workers, as well as an increase in the duration of unemployment. In order to adapt to this phase of the cycle, the length of the benefit period must increase and coverage extended. The inclusion of clauses for adding new beneficiaries during crises and the incorporation of atypical beneficiaries along with the complementary operation of job retention or labour suspension programmes provide support for this function and increase both the number of beneficiaries and the period during which protection is provided. If this is not done, effective coverage is limited to those who have met eligibility requirements and have not exhausted the regular benefits period.

Table 1
Unemployment insurance: Priorities by economic cycle phase

Component	Drop in activity	Recovery and growth
1. Cash benefits	Expansion due to countercyclical role	Designed to finance the job search period
2. Coverage	Expansion through the operation of job retention programmes	Depends upon eligibility conditions
3. Employment services	Identification of beneficiaries and coordination of employment programmes	Information on job vacancies and intermediation services
4. Training services	Incorporated into job retention programmes	Key role in supporting the expansion of dynamic sectors

Source: Prepared by the author.

During a downtoun, labour training services play a key role in worker retention programmes because they allow for investment in human capital and facilitate job retention. For their part, the typical functions of labour information and intermediation employment services are weakened because they are under greater pressure as they face both an increased number of unemployed workers and fewer vacancies. As a result, these institutions typically provide services to beneficiaries and coordinate public policies in specific geographic areas in these cases.

The experience analysed suggests that countries should institutionalise the measures adopted in order to adapt the insurance benefits to labour market cycles and strengthen them against future shocks. There seems to be a need to establish clear regulations to activate and deactivate benefits or modify their duration, seek out appropriate formulas for extending coverage for atypical workers, and establish complementary activities with job retention programmes.

During a reactivation and economic growth phase, on the other hand, the pressure on the unemployment benefits funds will progressively decrease because there will be fewer applications for benefits and the duration of unemployment will diminish. Furthermore, the clauses that temporarily increased the duration of the benefits and coverage of beneficiaries will have been deactivated. As such, in a context of recovery and growth, the emphasis will be placed on training, as well as information and intermediation services aimed at supporting beneficiaries in their job searches.

In this context, those who have insurance will have the resources that they need to finance their job searches. For their part, training programs will have decreased in volume in the context of employee retention programmes and their main role will be to correct structural deficiencies in the labour supply and improve employability, thus supporting economic reactivation through increases in productivity. Meanwhile, employment services will once again function as information provision and labour intermediation services, providing guidance or referrals for labour training programmes. Despite the fact that these functions will acquire a great deal of importance in the context of the current recovery phase, as was mentioned above, the effective integration of these components is currently a weak point in many countries.