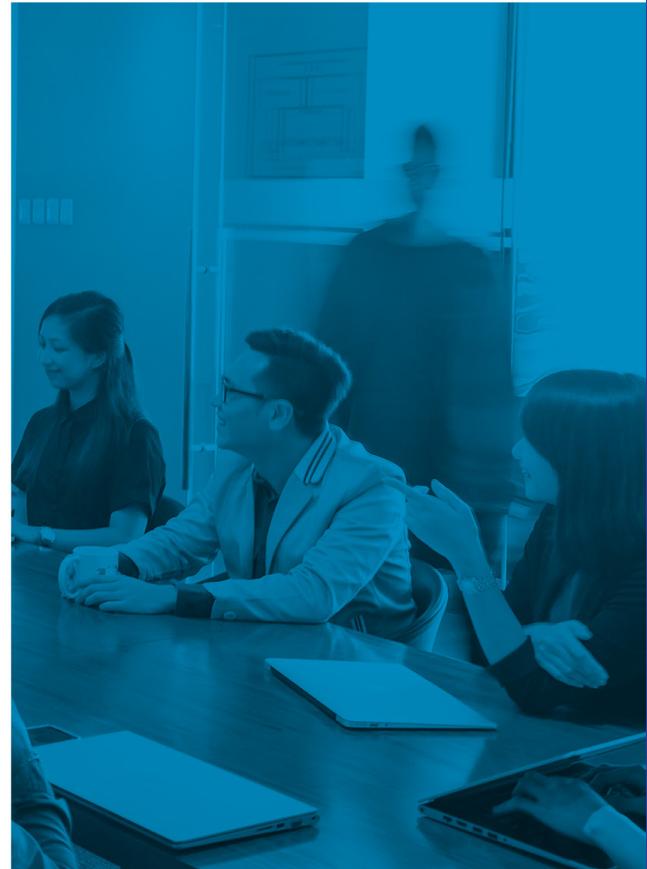


Labour market policy after COVID-19

The use of hiring credit wage subsidy programs after COVID-19



Professor Jeff Borland

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Introduction

The initial severity of the COVID-19 recession forced government policy in Australia into job-saver mode. Large-scale and broad-based support through programs such as JobKeeper has alleviated the substantial negative impacts on households and business and preserved employment connections. However, with recovery now underway, the orientation of policy must shift towards job creation.

An often-used policy to promote employment creation is a wage subsidy program – or more specifically, a subsidy payment attached to the hiring and employment of a new worker. A wage subsidy program is intended to motivate extra hiring by lowering the cost of employing new workers, by making it profitable for a business to add workers whose value added to revenue would otherwise be less than the costs associated with employing them.

This article provides a brief overview of wage subsidy programs and options for their application in Australia in the COVID-19 recession.¹ I begin by presenting a framework for understanding the labour market impact of wage subsidy programs and a description of their main elements. This is followed by ideas for how wage subsidy programs might be used in Australia to assist with recovery.

The impacts of wage subsidy programs

Figure 1 provides a framework for understanding the objectives and impact of wage subsidy programs. Two main outcomes of wage subsidy programs (and hence bases for evaluating their performance) are identified: the impact on employment and the fiscal cost of job creation. Outcomes depend on the design of the wage subsidy scheme; with the effect of design being mediated by the macroeconomic environment and labour market regulation. The government's choice of design of a wage subsidy is likely to depend on the expected outcomes of alternative designs and on their feasibility.

The first outcome is the impact on employment. Primarily this is about the increase in total employment achieved and duration of time period over which that impact occurs. In some cases, the extent to which employment of specific types of jobs or workers is increased will also be important. The impact of a wage subsidy program on employment will depend on the take-up of the program by employers and the 'additionality' of jobs that are subsidised.

Only if employers are willing to use the subsidy program to hire workers can the program have an impact. That will depend on the size of the subsidy and the ease of accessing the program for employers. Increasing the size of the subsidy should, for example, make it profitable for an employer to hire from a set of jobseekers with relatively lower skills and hence value added to revenue.

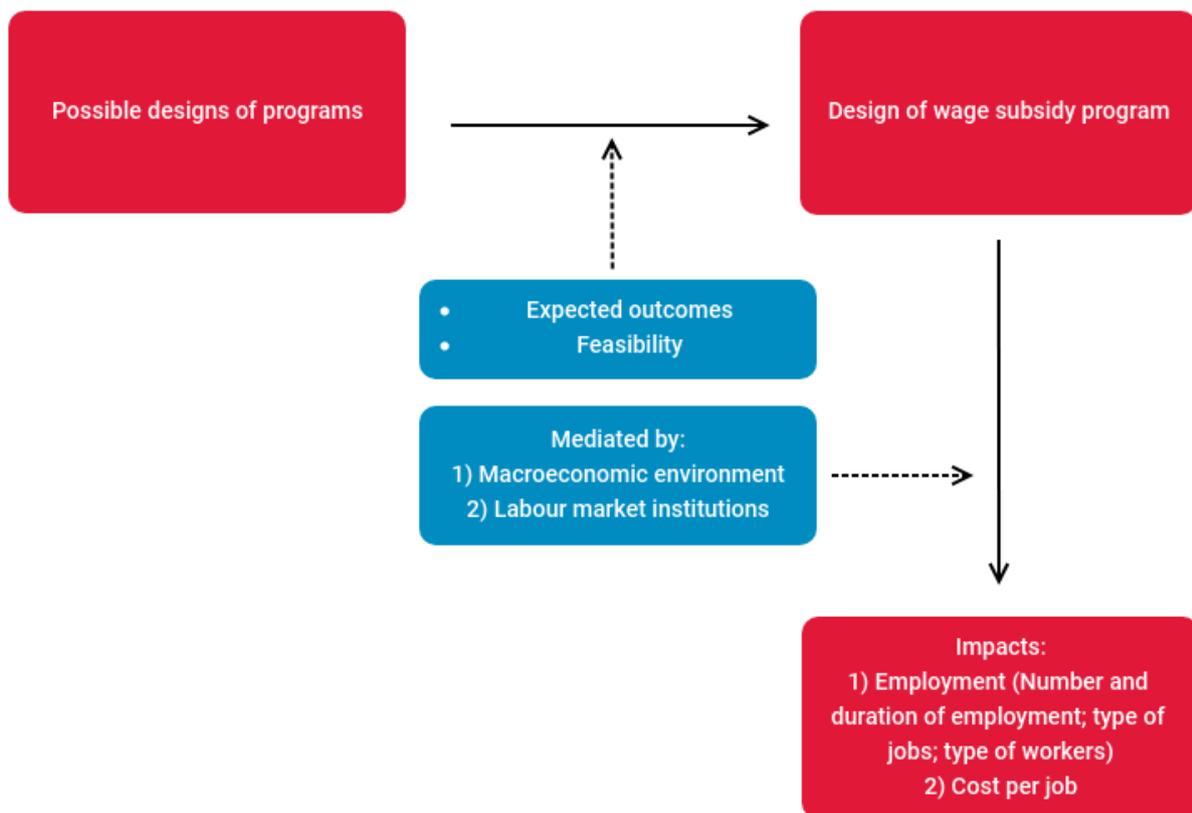
Additionality is the increase in employment due to the wage subsidy program that would not otherwise have been generated. The increase in employment would usually be expected to be less than

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the number of jobs subsidised. For example, a wage subsidy may pay for a job that would have been created anyway or employers who do not hire workers using the wage subsidy may lose business to those who do use the subsidy. Previous research suggests that this 'undoing' of wage subsidy effects on employment may be substantial.²

The second outcome is the fiscal cost per extra person employed (or extra hour worked). This outcome recognises the need to evaluate wage subsidy programs, as with any policy, by weighing costs against benefits.

Figure 1: Wage subsidy programs – A framework for analysis



Outcomes from a wage subsidy program will depend on its design. Wage subsidy programs have many moving parts and the details of those parts make a big difference to the impact of the program. Table 1 presents a summary of main design elements of a wage subsidy program.

Each element by itself will affect outcomes. For example, increasing the level of wage subsidy makes an increase in employment from the program more likely but would also raise the cost of generating an increase in employment. Importantly, the interaction of design elements may also matter.

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As an example, increasing the size of the subsidy payment may increase take-up in a program with universal eligibility yet have no impact on take-up in a program restricted to jobseekers with high barriers to employment.

The impact of a wage subsidy program will be mediated by external influences. The macroeconomic environment is the first important influence. For example, a wage subsidy is more likely to be paying for jobs that would have been created anyway when there are buoyant macroeconomic conditions. The second influence is labour market regulation. For example, wage subsidy programs may be most effective in increasing employment of low-skill jobseekers where a high minimum wage is in place.

Table 1: Main elements of wage subsidy programs

Main element		Examples
1. Targeting of program	Worker-level	i) All; unemployed; long-term unemployed ii) By age
	Firm/organisation level	i) Size of firm; ii) Sector
	Job level	i) Wage ii) Hours of work
	Conditions on eligibility	Relating to recent history of laying off employees
	Application of targeting	Rule or by tender
	2. Design of payment	Size/level of payment
Structure of payment		Lump sum or percentage of wage
Hours of work		Minimum/maximum number of hours of work for which subsidy would be paid?
What is payment made conditional on		i) Net addition to workforce/ payroll versus number of new workers hired; ii) Whether payment varies by characteristics of new worker hired; iii) State of the business cycle

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	Duration of payment	
	Timing of payment to employer	Up front; spread over time; at end of scheme
3. Other conditions	Whether there is a requirement to provide training	
4. Administrative details	Application and approval process	
	How payment is made	Cash versus tax rebate
	How information about the program is reviewed	

Ideas for using wage subsidy programs

1. Match the level of subsidy to the state of the macroeconomy

Worse macroeconomic conditions imply that additionality is more likely (jobs would not have been created without the subsidy), but take-up may be low (employers have a low willingness to pay for extra employees due to them making little contribution to revenue). Both these considerations would argue for a higher level of wage subsidy in worse macroeconomic conditions, such as are being experienced at present. At the same time, it is important to consider that, in a severe downturn, the pool of jobseekers will include a large proportion of short-term unemployed who may not need substantial assistance to find a job. This is magnified in the COVID-19 recession by reopening of economic activity already bringing a rapid increase in employment. These latter considerations suggest that a higher level of subsidy should be accompanied by targeting by type of worker/job, to ensure a high degree of additionality and so that the program is focused on jobseekers for whom having a wage subsidy will make a difference to their employability.

That the optimal design of a wage subsidy program varies with the state of the macroeconomy has a further implication: it is critical to fit the program design to the conditions at the time of implementation of a program and to perhaps allow scope for the program to vary as macroeconomic conditions vary. For example, once recovery gathers pace, a lower level of subsidy will be sufficient to induce take-up and will reduce the fiscal cost in conditions where additionality of wage subsidy programs is likely to be lower.



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2. Target to the young and medium-term unemployed

Pushing employment creation towards the young via wage subsidies appears to be one way to offset the major impact that COVID-19 will have on their employment opportunities.³ Young people, who do not have extensive employment experience as a way of signalling their capabilities, would benefit from the information provision aspect of wage subsidies. Given that young people from all education backgrounds are likely to be adversely affected, whether a subsidy should be universal or targeted at specific categories of young people seems an open question. One difficulty with targeting wage subsidies at young people may be the need to distinguish between those employed in part-time jobs in industries most adversely affected but now rebounding from COVID-19 (such as accommodation and food services) where additionality may be low, and those seeking to make the transition from education to work into jobs where additionality may be higher.

The other main group at whom wage subsidy programs might be targeted are jobseekers with medium barriers to employment (perhaps unemployed for six to 18 months) for whom wage subsidy programs appear to most improve their employment prospects.

3. Duration and repayment

The duration of a wage subsidy program needs to be sufficiently long to allow the employee for whom the subsidy is paid to accumulate work experience and skills, and to have the opportunity to demonstrate their capabilities to the employer. For that duration, which might be six months, an employer who is receiving the subsidy should be required to retain the employee for a minimum number of hours per week. Where the subsidy is paid up-front and the employee is not retained for the minimum duration, repayment should be required. It does not seem feasible to impose a requirement that an employer retain an employee beyond the duration of the subsidy.

4. Conditions for eligibility

Employers receiving a wage subsidy should certify that the job for which the subsidy is being paid is an additional job that is only being created due to availability of the subsidy. Some programs further restrict eligibility by only allowing employers to apply if they have not laid off staff in the immediate past (for example, the previous six months). This would not be a sensible requirement in the initial phase of a COVID-19 wage subsidy program, given the lay-offs many businesses have had to make. However, it could be built in as a condition of continuing access to the wage subsidy program for a business. For example, once a business has already received a wage subsidy for an employee (or employees), it can only receive subsidies for further employees if it has retained the employee(s) for whom the subsidy was initially paid.



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5. Hours of work/structure of payment

Imposing minimum and maximum numbers of hours per week for which a subsidy would be paid seems important to achieve a balance between guaranteeing sufficient work experience and limiting fiscal cost. A lump-sum payment (or perhaps set of lump-sum payments varying according to hours worked) or a fixed rate per hour worked are administratively simplest, and have the advantage of providing a higher level of subsidy to lower skill workers.

6. Programs by jurisdiction

Optimal wage subsidy design is likely to differ between levels of government. Because of their extensive coverage, Commonwealth wage subsidy programs need to be general in design and the scope for targeting restricted to broad categories (such as the young). State or local government programs can be more tailored to economic conditions at that geographic level and lesser scale and greater information also allow scope for more specific targeting (such as via tender-type processes).

7. Timing of payment/administrative complexity

Take-up is an important determinant of the employment impact of wage subsidy programs – and hence should be incorporated as an explicit consideration in program design. Making subsidy payments up-front (at least in part) and minimising administrative burden associated with programs have been found to contribute to take-up.

Endnotes

1 For previous surveys see: Borland, Jeff (2016), 'Wage subsidy programs: A primer', *Australian Journal of Labour Economics*, 19(3): 131-44; Brown, Alessio and Johannes Koettl (2015), 'Active labor market programs – employment gain or fiscal drain', *IZA Journal of Labor Economics*, 4(12): 1-36.

2 See: Martin, John and David Grubb (2001), 'What works and for whom: A review of OECD countries' experiences with active labor market policies', *Swedish Economic Policy Review*, 8: 9-60; Brown, Alessio and Johannes Koettl (2015), 'Active labor market programs – employment gain or fiscal drain', *IZA Journal of Labor Economics*, 4(12): 1-36.

3 Borland, Jeff (2020), 'The next employment challenge from coronavirus: How to help the young', *The Conversation*, April 15; accessed at: <https://theconversation.com/the-next-employment-challenge-from-coronavirus-how-to-help-the-young-135676>