Policy Insights
Centre on Well-being, Inclusion, Sustainability and Equal Opportunity (WISE)
OECD

Economic insecurity in Europe and potential policy responses

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Over the past few decades, economies and technologies have changed in ways that have made people's economic prospects more uncertain. This policy insights highlights the main findings from *On Shaky Ground? Income Instability and Economic Insecurity in Europe* (OECD, 2023[1]), the inaugural report of the OECD Observatory on Social Mobility and Equal Opportunity. The report uses novel techniques to identify the economically insecure in European OECD countries – i.e. those who are most exposed and vulnerable to income instability – and examines the effects income changes and economic insecurity have on people's lives, social mobility, and inequality. The report also reviews a range of policies to improve the timeliness of social protection to better support people with highly unstable incomes and explores options to help those most at risk of economic insecurity build financial buffers.

KEY MESSAGES

- In European OECD countries, people commonly experience monthly variations in their incomes in response to changes in their employment status. For the most part, income variations do not translate into a durable increase in income over the 48-month period of analysis.
- People in the bottom income quintile are most likely to experience income instability – income fluctuations from month-to-month and over the years – which inhibits their upward social mobility, and likely contributes to rising inequality at a country level.
- One in six individuals living in working-age households experience income instability and do not have sufficient liquid assets to cope. These people are considered to be economically insecure and tend to be in households with lower employment intensity and limited job security. Households headed by women also face bigger prospects of economic insecurity, since they have weaker attachments to the labour market than men.
- Given the concentration and consequences of economic insecurity, governments should support people to smooth their incomes and build their savings. Social protection systems should be responsive to people's circumstances, which can change frequently. Moreover, governments can assist people in improving their financial literacy, accessing high-quality financial advice, encouraging them to save (e.g. using well-designed matched savings schemes) and avoiding over-indebtedness.

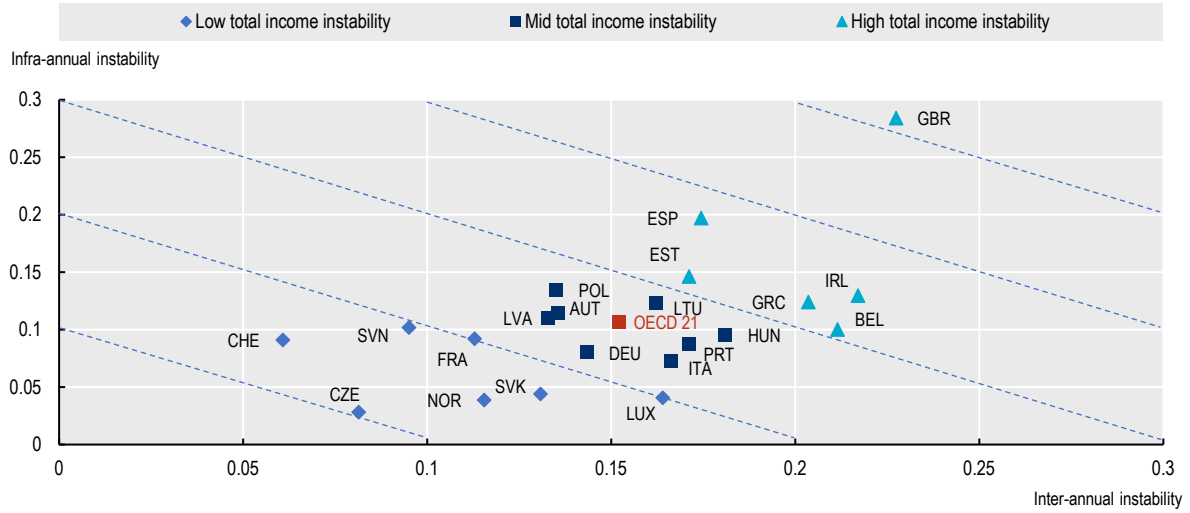
Employment statuses and incomes change frequently in Europe

The past few years have been marked by insecurity. The onset of COVID-19 caused widespread anxiety about job losses and working hour cuts in many OECD countries, while the subsequent cost-of-living pressures compounded individuals' concerns about their financial positions (OECD, 2023[2]; OECD, 2021[3]; Caisl et al., 2023[4]; OECD, 2023[5]). This has created a "perfect storm" of economic insecurity for some – predominantly those on low incomes – who lack both the opportunities and the means to smooth their incomes. While there are signs that OECD economies are recovering from the recent economic shocks, the risks of economic insecurity could persist for people exposed to the potential negative consequences of long-term structural changes (e.g. digital transformation), even though others may benefit.

Even before the economic disturbance of the COVID-19 pandemic, people's economic circumstances changed frequently in European OECD countries. Almost 10% of working-age individuals changed their employment status in the 48-month reference period ending in 2016-18 (OECD, 2023[1]). One-third of individuals who changed their employment status, did so multiple times a year. Frequent employment changes translate into monthly variations in income before taxes and transfers (called infra-annual income instability). Infra-annual instability accounts for more than two-fifths one-fifth of total income instability, which also consists of changes in incomes over the years (inter-annual income instability, x-axis in Figure 1). Among OECD countries with available evidence, the United Kingdom and Spain have the highest levels of infra-annual income instability (y-axis in Figure 1). These countries are also marked by high or above-average inter-annual income instability. In contrast, infra-annual income instability is below average in the Czech Republic, Norway, the Slovak Republic and Luxembourg (Figure 1). Nevertheless, the estimated levels of income instability are likely conservative, as they focus only on income changes linked to changes in employment status, rather than other sources of income shocks, like family breakdown.

Figure 1. Infra-annual income instability contributes to a substantial fraction of total instability

Average squared coefficient of variation of market income, averaged over 48 months ending in 2016-18

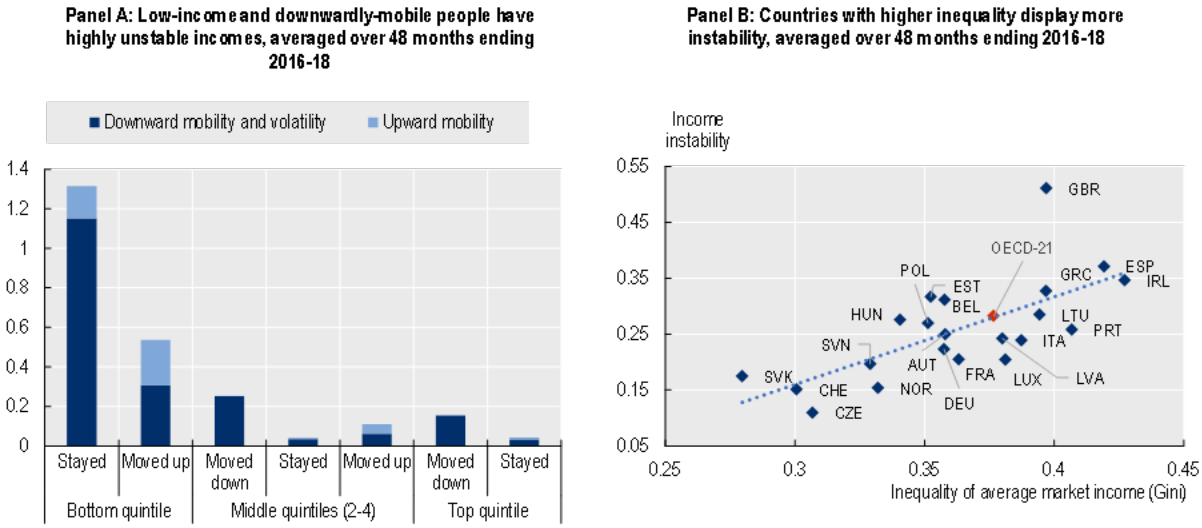


Note: Instability is measured by the average squared coefficient of variation of monthly household equivalised market income over 48 months. Infra-annual instability refers to deviations of monthly income from each year's household average; inter-annual instability refers to deviations of household annual average income from the average across the entire period of observation. Dotted "iso-instability" lines mark similar levels of total instability. The analysis is carried out only on households with stable composition over 48 months and whose main employment income earner is aged between 18 and 59.
Source: OECD calculations based on the European Union Statistics on Income and Living Conditions (EU-SILC), https://ec.europa.eu/eurostat/web/income-and-living-conditions.

In many cases, incomes changed in ways that did not imply sustained growth of living standards. Across all European OECD countries, only 20% of individuals in working-age households experienced sustained, upward income growth of at least 25% in the 48-month reference period (OECD, 2023[1]). The majority of individuals who experienced changes in their employment status saw their incomes trend downwards or fluctuate with no discernible trend (i.e. income volatility). Income instability is concentrated among people at the bottom of the income distribution, including those who are unemployed, workers on temporary or no employment contracts or people in single-income or young households (Figure 2, Panel A). As a consequence, people with unstable, low incomes have limited upward social mobility and tend to stay at the bottom of the income distribution (rather than moving into higher income brackets). Moreover, in general, countries with higher income inequality (as measured by the Gini Index) display more income instability (Figure 2, Panel B).

Figure 2. Income instability is associated with downward mobility and inequality

Average squared coefficient of variation of market income, averaged over 48 months ending in 2016-18



Note: Income instability is measured by the average squared coefficient of variation of monthly household equivalised market income over 48 months. In Panel A, quintiles are based on annual market household income in the first 12 months of the time series, and then compared with the annual market household income distribution in the last 12 months of the period. Households are split into groups depending on whether their income quintile in the last 12 months (fourth year) of the series is higher ("Moved up"), lower ("Moved down") or the same ("Stayed"), compared to the first 12 months. In Panel B, the Gini index is calculated as the average of monthly household equivalised market income over the same period. The unit of reference is the individual. The analysis is carried out only on households with stable composition over 48 months and whose main employment income earner is aged between 18 and 59.
Source: OECD calculations based on the European Union Statistics on Income and Living Conditions (EU-SILC), https://ec.europa.eu/eurostat/web/income-and-living-conditions.

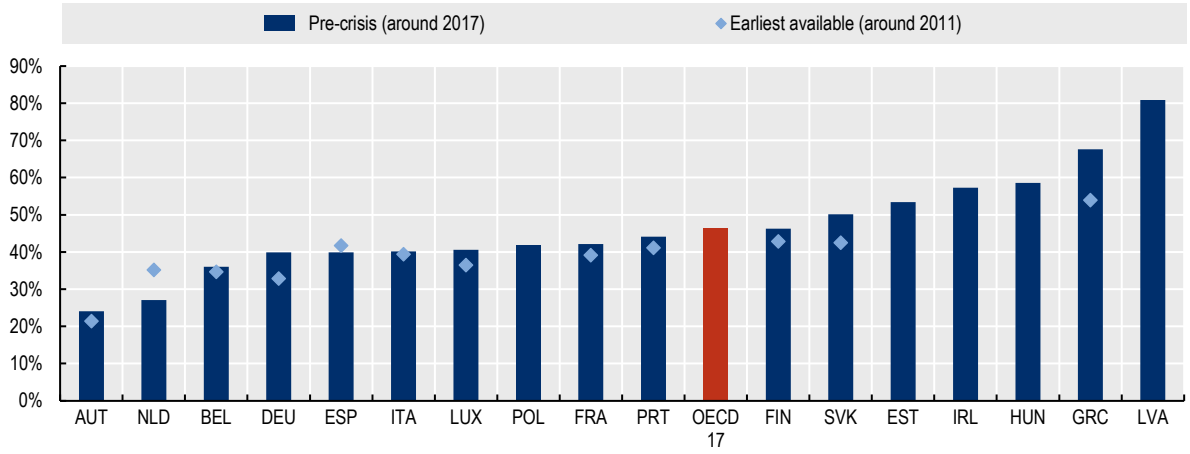
Many individuals have limited financial buffers to cope with income instability

People may be able to draw on liquid assets, take out loans, receive support from family and friends or reduce their consumption to cope with income instability – although it is becoming increasingly difficult to cut back on spending in the context of the cost-of-living crisis or to take out loans, given the already high levels of household debt and over-indebtedness. Around 2017, almost one-in-two people in working-age households were financially fragile, as they did not have sufficient liquid assets to stay above the poverty line for at least three months (Figure 3). These rates rose to 60% in Ireland and Hungary, 70% in Greece and 80% in Latvia.

Financial fragility is concentrated among, but not confined to, people in low-income households. About 67% of people in lower-income working-age households, 50% of people in middle-income households, and even 20% of those in high-income households have insufficient liquid assets to stay above the poverty line for at least three months (OECD, 2023[1]). Low education, being a renter rather than a homeowner, and living in a single-parent household are strong predictors of financial fragility. Financial fragility is also more widespread among sectors that fared worse than others during the early stages of the COVID-19 crisis (e.g. food and hospitality).

Figure 3. Almost one-in-two people in working-age households are financially fragile

Share of individuals living in working-age households whose liquid financial assets are insufficient to support them at the level of the OECD income poverty line for at least three months, around 2010-17

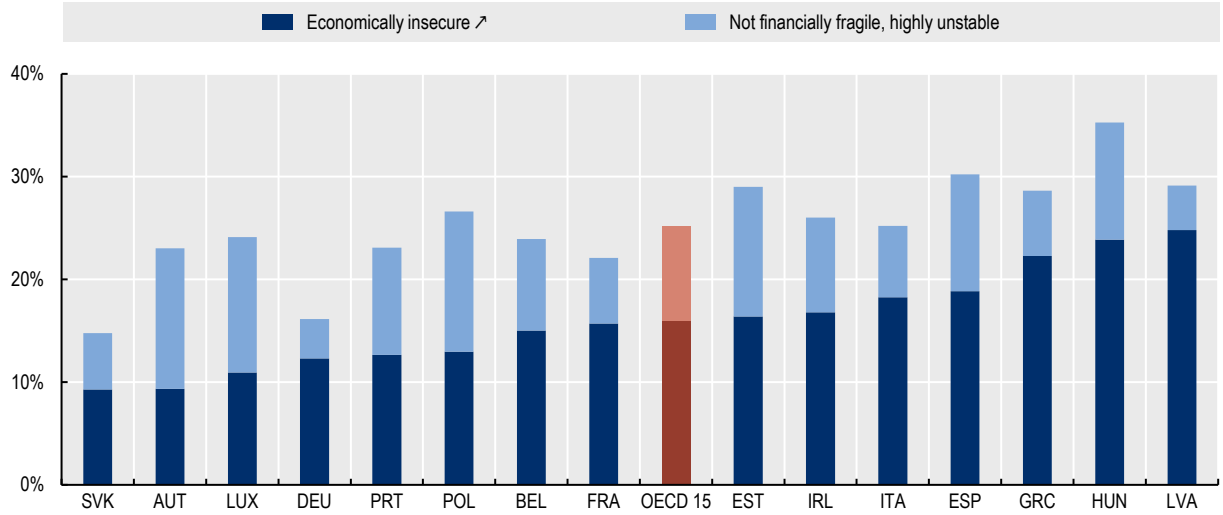


Note: Liquid assets are those that can more easily be liquidated if needed urgently, including currency and deposits; bonds and other debt securities; mutual funds and other investment funds; and other non-pension financial assets. The pre-crisis data refer to: 2016 for Finland, Italy, Lithuania, and Poland; 2017 for Austria, Belgium, Estonia, France, Germany, Hungary, Latvia, the Netherlands, Portugal, and the Slovak Republic; 2018 for Greece, Ireland, Luxembourg, and Spain. The earliest available year refers to: 2009 for France, Finland, and Greece; 2010 for Belgium, Italy, the Netherlands, and the Slovak Republic; 2011 for Austria, Germany, Luxembourg, and Portugal; and 2012 for Spain. The poverty line is based on disposable income, which is estimated by using a Machine Learning algorithm to impute disposable income from the gross income variable (the sum of wages and salaries, self-employment income, and property income and social transfers received all recorded before the payment of income taxes) available in the HFCS dataset. The analysis focuses only on those countries for which the results of the statistical matching procedure are highly satisfactory for 17 out of the 19 OECD-EU countries covered in the third wave of the HFCS. See Annex 2.A in OECD (2023[1]) for more information on the method for estimating disposable income.
Source: OECD calculations based on the European Union Statistics on Income and Living Conditions (EU-SILC), https://ec.europa.eu/eurostat/web/income-and-living-conditions; and the Eurosystem Household Finance and Consumption Survey (HFCS), https://www.ecb.europa.eu/stats/ecb_surveys/hfcs/html/index.en.html.

People who are financially fragile often face income instability (i.e. the co-occurrence of these phenomena is called economic insecurity in this policy insights). Around 2017, one in six people in working-age households in European OECD countries not only did not have sufficient liquid assets to stay out of poverty for at least three months and also had highly unstable incomes. One-quarter of people in Latvian or Hungarian working-age households were economically insecure (Figure 4). The burden of economic insecurity falls predominantly on people who lack job security, are unemployed, or are in single-income-earning households. The probability of experiencing economic insecurity is also high for young couples and single, female-headed households – reflecting gender imbalances in employment intensity. Women have lower participation rates and higher unemployment rates and are more likely than men to be in single-income-earning households. Indeed, while 78% of working-age men in the sample are employed, the same is true for only 68% of women (OECD, 2023[1]).

Figure 4. Almost one in six people in working-age households are economically insecure

Percentage of individuals in working-age households who are economically insecure or have highly unstable incomes but sufficient liquid assets to cope with an income shortfall, averaged over 48 months ending in 2016-18



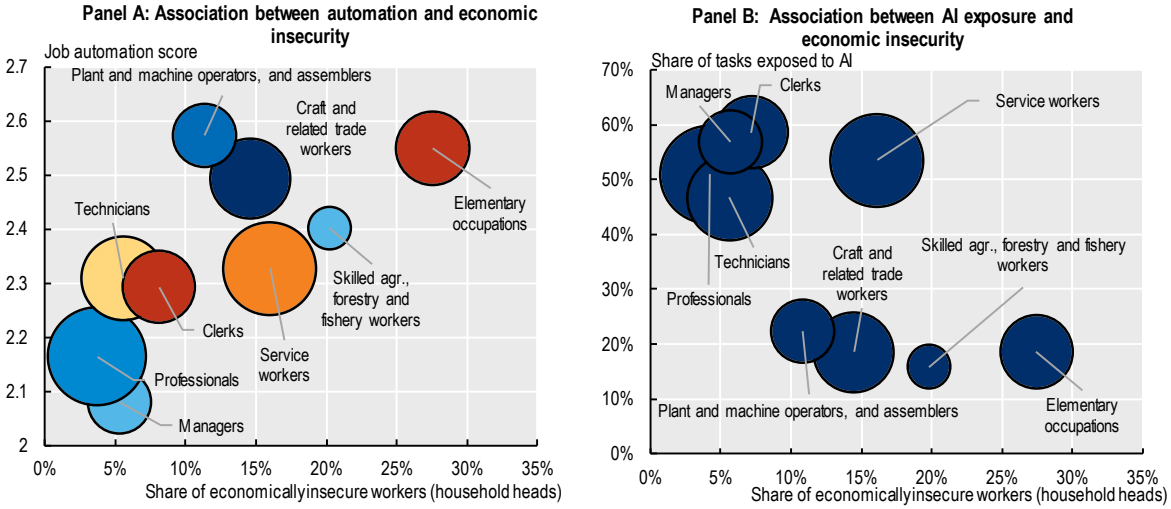
Note: The economically insecure are people living in working-age households that have insufficient liquid assets to support them at the level of the OECD income poverty line for at least three months and a level of income instability that puts them in the most vulnerable 25% of the population in European OECD countries. The income instability threshold is calculated by first excluding households with incomes that trend upward over time, and then calculating the level of income instability that corresponds with the top 25% of households in each country. These levels are then averaged to obtain the European threshold. The chart only shows countries for which information on both instability and fragility is available.

Source: OECD estimates based on the European Union Statistics on Income and Living Conditions (EU-SILC), https://ec.europa.eu/eurostat/web/income-and-living-conditions; and the Eurosystem Household Finance and Consumption Survey (HFCS), https://www.ecb.europa.eu/stats/ecb_surveys/hfcs/html/index.en.html.

Further, people who experience economic insecurity are more likely to believe themselves to be at risk in the future. Almost 70% of those who are economically insecure believe they have a high chance of losing their job in the next year compared to a quarter of those who are not economically insecure (OECD, 2023[1]). They also tend to be in occupations that have a higher risk of automation (such as elementary workers) than those who are not economically insecure (professionals and managers) (Figure 5, Panel A). The risks of future economic insecurity are particularly high for elementary workers, since they have the fewest opportunities to transition into viable and desirable jobs, are less likely to benefit from emerging technologies such as artificial intelligence, and have fewer opportunities to build up financial assets, given their low wages (Figure 5, Panel B). In contrast, occupations associated with low rates of economic insecurity have a higher exposure to artificial intelligence. Artificial intelligence has not (yet) led to a reduction in employment: some highly skilled workers have had better employment prospects after the introduction of artificial intelligence, and there is some evidence that those exposed to artificial intelligence have seen their wages increase, as they spend more time on complex work tasks, while artificial intelligence undertakes simpler tasks (OECD, 2023[2]).

Figure 5. Occupations with higher shares of economically insecure workers are less likely to reap the benefits of AI and are more at risk of automation

Economic insecurity and its association with exposure to AI and automation risk, major ISCO-08 occupation groups



Note: Exposure to artificial intelligence (AI) is based on Kanders et al (2020[6]), who map the suitability for machine learning scores developed by Brynjolfsson, Mitchell and Rock (2018[7]) to thousands of tasks in European countries. Exposure is measured as the share of tasks that are not bottlenecks to AI. Automation risk is based on Lassébie and Quintini (2022[8]), who surveyed experts on the degree of automatability for 98 skills and abilities. The risk of automation is then calculated for each occupation as the average rating for each skill or ability used in the occupation across all expert responses weighted by the skills or abilities' importance in the occupation as rated by O*NET. Finally, the scores are applied to European Skills, Competencies, and Occupations in the HFCS using the Kanders et al. (2020[6]) crosswalk. Scale is 0-5 for all occupations. Each bubble's size indicates the share of workers in a given occupation. In Panel A, bubbles are coloured based on the number of highly viable and desirable job transitions that are likely in each occupation group – ranging from dark red (5 transitions), to orange (7), yellow (8), light blue (10), medium blue (11), and finally dark blue (19-22). Highly viable transitions are those with a good fit for an individual's current occupation (based on their education, skills, experience, and types of work activities), while desirable transitions are those where the job mover can make at least 75% of their current occupation's median earnings (Kanders et al., 2020[6]). Unweighted average of Austria, Belgium, Estonia, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Poland, Portugal, the Slovak Republic and Spain.
Source: Kanders et al (2020[6]), Lassébie and Quintini (2022[8]) and OECD estimates based on the European Union Statistics on Income and Living Conditions (EU-SILC), https://ec.europa.eu/eurostat/web/income-and-living-conditions; and the Eurosystem Household Finance and Consumption Survey (HFCS), https://www.ecb.europa.eu/stats/ecb_surveys/hfcs/html/index.en.html.

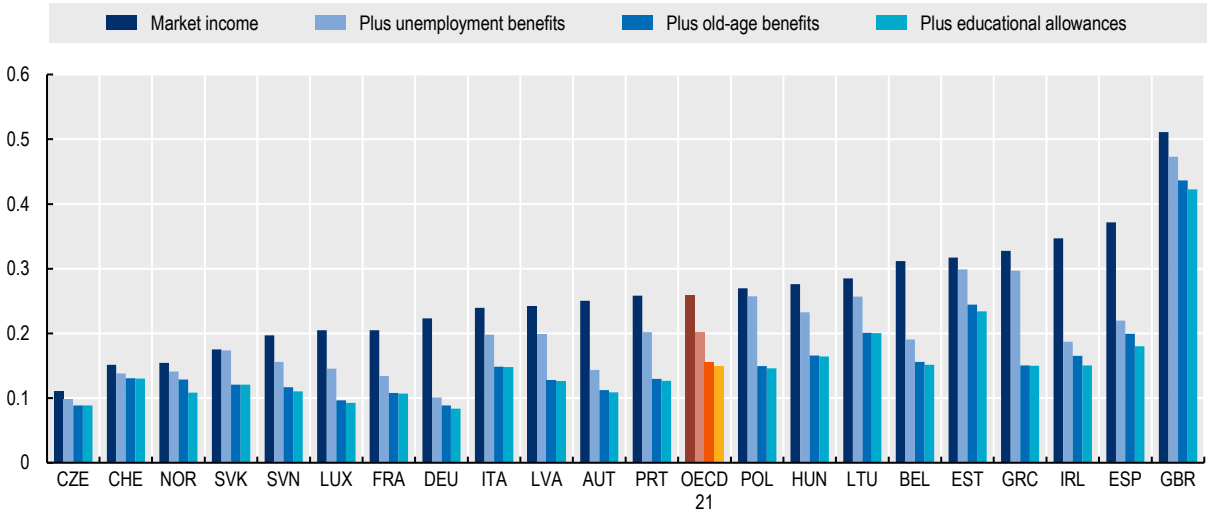
Policies to tackle economic insecurity

There is a clear role for governments to address economic insecurity, since it is concentrated among disadvantaged groups, it has severe consequences and is likely to remain a problem in the future. Policies should target both the exposure and the vulnerability to economic insecurity – by reducing the likelihood of adverse economic shocks, helping people to smooth their incomes and to build their financial resilience.

Social protection has an important role in helping to smooth people's incomes. On average, across European OECD countries, unemployment benefits, old age pensions and education allowances reduce income instability by about 40% (Figure 6). Other social benefits, such as child and housing allowances, can also help to reduce income instability, but cannot be reliably included in an analysis of infra-annual instability. In most European OECD countries, unemployment benefits make the largest contribution to reducing instability, except in Greece and in some Eastern European countries, where the old-age pension is more significant. However, social protection does not have a large effect on reducing income instability in countries with low levels of instability, including the Czech Republic, Switzerland and Norway.

Figure 6. Social benefits reduce income instability by 40% on average across European OECD countries

Average squared coefficient of variation of total monthly income pre- and post-social benefits, averaged over 48 months ending 2016-18



Note: Income instability is measured by the average squared coefficient of variation of monthly equivalised household income over 48 months. The dark blue bars measure instability before accounting for social benefits by using the market incomes constructed in Chapter 1 of OECD (2023[1]). The light blue bars add unemployment benefits to market incomes to measure instability after accounting for unemployment benefits. Next, the third set of bars adds old-age benefits to market incomes and unemployment benefits. The final set of bars adds in educational allowances and thus represents the total measurable effect of social benefits on instability. However, the total measurable effect does not include all social benefits, such as child allowances. See Chapter 1 in OECD (2023[1]) for more information. The analysis is carried out only on households with stable composition over 48 months and whose main employment income earner is aged between 18 and 59. The unit of reference is the individual.
Source: OECD calculations based on the European Union Statistics on Income and Living Conditions (EU-SILC), https://ec.europa.eu/eurostat/web/income-and-living-conditions.

Despite the power of social protection systems to reduce instability, they are not always responsive to people's needs and circumstances. In many European countries, people receive social benefits every four weeks, which can make it difficult for people on low incomes to make ends meet at the end of the month (OECD, 2023[1]). Long periods between social benefits are associated with stress, difficulty paying bills and food insecurity. Similarly, it can take weeks to receive the first benefit payment, which can cause financial distress and increase the risk of poverty. Efforts should be made to increase the frequency of payments and to reduce waiting and processing times, particularly for people at risk of poverty, including by simplifying means testing arrangements where they are used to target payments (typically family and housing benefits in the case of many European countries).

In addition, policies that promote financial literacy are important for boosting financial resilience and well-being, particularly in times of constrained fiscal environments when governments may have less capacity for large-scale social expenditure. Matched savings schemes, effective financial education strategies, appropriate advice and counselling services, cost-effective financial services and debt relief can help people at risk of economic insecurity to build up their financial resources and manage debt. Recent advances in data mining techniques and artificial intelligence can be used to identify people before they become over-indebted, which can then help governments direct services to those most vulnerable, including by developing payment plans.

WHAT CAN POLICY MAKERS DO?

Policy makers have a range of tools at hand to protect households and individuals from the adverse effects of income instability and strengthen the financial resilience of vulnerable households. These include measures to:

- increase the timeliness of unemployment benefits by reducing waiting periods, in particular when they arise from administrative delays or when they affect people who are especially vulnerable to economic insecurity, such as those who experience repeated unemployment spells;
- redesign means testing and consider automatic enrolment so it is easier for people to access all social benefits for which they are eligible;
- support households' capacity to save and accumulate financial assets, including through adequate financial services and incentive schemes (e.g. matched savings schemes). Savings incentive schemes should be carefully designed and targeted to attract low-income households. For instance, those with low incomes do not typically take advantage of tax-based savings schemes;
- improve households' financial resilience, for instance by improving financial literacy and advice in line with international best practices. This includes tailoring programs to people's needs and contexts and providing financial support for vulnerable people to access high-quality advice;
- assist households experiencing financial hardship and over-indebtedness. This includes implementing protective and rehabilitating measures, such as debt relief programs, reforms to the treatment of debt to public bodies, and regulation of high-interest lenders to avoid a vicious circle of high-indebtedness, high-interest rates and high debt delinquency. Data mining and predictive models can also be used to identify and support people at risk of debt problems.

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Resources

Read the report in full: OECD (2023), *On Shaky Ground? Income Instability and Economic Insecurity in Europe*, OECD Publishing, Paris, https://doi.org/10.1787/9bffeba6-en.

OECD Observatory on Social Mobility and Equal Opportunity

Understanding social mobility

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