Summary

Sweden has experienced a rise in net immigration since the 1980s, and humanitarian migrants have come to account for a large proportion of those who have immigrated. How well foreign-born people integrate into society and can become established in the labour market is naturally important for the immigrants themselves but also has consequences for the economy. Not least, foreign-born people represent both an opportunity and a risk when it comes to addressing the future challenge of an ageing population and the conditions for financing public expenditure.

Sweden has an ambitious and active policy for the reception and labour market integration of newly arrived humanitarian migrants. But the entry process is slow. Employment and income from work are also lower over the long term for immigrants than on average in the labour force.

It is difficult to identify a single measure that could make a significant difference to shorten the time for newly arrived humanitarian migrants to become established in the labour market. Rather, measures in a number of areas are needed to influence supply, demand and matching in the labour market. Although the significance of financial incentives for labour supply has also been addressed in different contexts, no systematic review of financial work incentives has been conducted.

The main purpose of this report is to create knowledge concerning the financial incentives encountered by newly arrived humanitarian migrants before becoming established in the labour market. What are the financial work incentives for newly arrived humanitarian migrants? In what way and why are these financial work incentives different for newly arrived refugees than for the rest of the population? This report is limited to a review of the short-term financial incentives to work.

Simulations for reviewing the financial incentives to work in 2017

The review is based on income distribution statistics for 2015 that is projected onto economic and demographic conditions in 2017 and the rules applying in 2017 using the microsimulation model FASIT, used for calculating the effects of changes in taxation, fee and transfer systems for individuals and households (Statistics Sweden).

Financial work incentives depend on the relationship between disposable income and hours worked. Two dimensions of financial incentives to work are considered in this report: the financial incentive to work compared with not working, and the financial incentive of increasing one's earnings slightly. The participation rate and replacement rate are used as measures of financial incentives to work compared with not working. The effective marginal rate is used as a measure of the financial incentive to increase one's earnings slightly.

Financial work incentives are presented using both model-estimated statistical averages for population groups aged 20–64 and typical-case calculations. Comparisons are made between four groups. The first group consists of humanitarian migrants, including their relatives, who have lived in Sweden for one to up to four years, largely corresponding to people covered by the introduction system at Arbetsförmedlingen (Swedish public employment service). The remaining groups are: other foreign-born people who have lived in Sweden for one to up to four years; foreign-born people who have lived in Sweden for more than four years; and people born in Sweden.

Financial incentives to work compared with not working in 2017

The model-estimated replacement rates are based on individuals working full-time for the full year, taking part in introduction activities or, alternatively, being unemployed. According to the model's assumptions, unemployed individuals are presumed to receive income-based benefits from the unemployment insurance fund. Individuals taking part in introduction activities are presumed to receive a monthly wage of SEK 18 000 when in work.

For newly arrived humanitarian migrants receiving introduction benefits, the average replacement rate is calculated to be approximately 70 per cent, which means that their disposable income when taking part in introduction activities is 70 per cent of what they would receive if they were in work. But the variation is considerable and also depends on household composition. Households without children have a lower replacement rate, approximately 60 per cent on average, and thus stronger financial incentives to work. For households with children, financial work incentives are weaker, with an average replacement rate of 80 per cent.

The average replacement rate on introduction activities is at the same level as the average replacement rate on unemployment without benefits under a collective agreement. Taking benefits under a collective agreement into account, the average replacement rate is slightly higher, at 78 per cent. The average replacement rate during unemployment also varies for other groups in the population, but low replacement rates are more common for introduction benefits than for unemployment benefits. Replacement rates during unemployment have been calculated for those who had an income of at least approximately SEK 135 000 for the year.

Very few newly arrived humanitarian migrants qualify for unemployment benefits. The model calculations include only 17 per cent of this group, but even this is an overestimation of the number who actually qualify for income-based unemployment benefits. A review of the groups' incomes reveals that very few newly arrived humanitarian migrants receive unemployment benefits for the year. However, activity support is a common benefit, alongside introduction benefits. A large proportion of those who have left the introduction plan transition to the job and development guarantee, and thereby receive activity support, which is at such a low level, however, that supplementary income support is often needed.

Typical-case calculations for those who have or can expect to have low incomes reveal that the gain of being in work compared with not working can vary considerably depending on whether an individual receives introduction benefits or income support.

For cohabiting couples, income support provides very high replacement rates for the first person in the household who begins to work, but significantly less for the second, assuming they do not have many children. For those receiving introduction benefits, financial work incentives are stronger for the first partner who begins to work. But compared with income support, financial work incentives are weaker for the other partner.

Compared with other low-income earners who have qualified for the unemployment insurance fund's income-based benefits, financial work incentives are often stronger. For typical cases, the replacement rates for those receiving unemployment benefits are between 82 and 93 per cent. An important difference in principle between unemployment benefits and introduction benefits is that the unemployment insurance fund is an insurance against loss of income that individuals must qualify for by working.

Financial incentives to increase earnings by the effective marginal tax rate in 2017

For many who are out of work, full-time employment is not the first option; rather the first jobs may instead involve shorter periods of work. The average effective marginal tax rate reveal that any additional hours worked (corresponding to increased earnings of SEK 12 000) on average are more profitable for newly arrived humanitarian migrants than for the population on average. This is partly due to the fact that the average marginal effect is largely determined by the marginal tax rate, and newly arrived refugees often have low income from work. The introduction benefit is not means-tested and has no direct impact on the model-estimated effective marginal tax rate.

For newly arrived humanitarian migrants receiving introduction benefits and working alongside the introduction plan, the effective marginal tax rate is often the same as the total of a low marginal tax rate and – if they have housing allowance and children in preschool – the marginal effects due housing allowance and to the childcare fees for 2017.

For newly arrived humanitarian migrants who get a job within the framework of the introduction plan, financial incentives to work are weaker than transitioning to full-time work, and here, too, means-tested support for families comes into play.

Without introduction benefits, the effective marginal tax rate is high for those with low incomes, and as long as there is entitlement to income support, they are very high. The incentive to work within income support means that those who qualify are currently entitled to retain 25 per cent of any increase in income, while those who do not qualify receive no increased income from any extra hours worked as long there is still a need for income support.

Several explanations as to why the financial incentives experienced by newly arrived humanitarian migrants arrivals are different than for others

Financial work incentives thus vary, for both newly arrived migrants and others in the population, but they also differ between the groups.

Human capital and the income an individual earns are very important for financial work incentives. Newly arrived humanitarian migrants are generally younger, and many have very low levels of education. Their expected wage is therefore often low, which contributes to the weak financial incentive to work. Becoming established in the labour market takes time, and few qualify for income-based benefits. For those receiving income support, financial incentives to work are weak, but when introduction benefits are an alternative to income support, the incentive to work strengthens for many new arrivals.

Household composition is also a factor that plays a role in financial work incentives, both because an individual's earnings are relatively less important if there are other incomes and because there is means-tested support for families.

For households with children, and above all for households with many children, financial work incentives are often weak for those with low incomes. This applies to both financial incentives to work compared with not working, and the financial incentive to increase the hours worked (earnings) slightly. The effective marginal tax rate become substantial even for relatively high incomes, which means that many newly arrived humanitarian migrants may have a hard time finding a job that precludes the need for supplementary income support.

Almost half of the newly arrived humanitarian migrants are cohabiting with children. Compared with the rest of the population, there is a slightly larger proportion of single parents, even though this group is small in all the groups reported on. It is also slightly more common that newly arrived refugees have many children, although this group is also relatively small. But because newly arrived humanitarian migrants usually have low incomes, they are more dependent on means-tested family support than others, which leads to family support reducing financial work incentives more for this group than for other groups.

Households without children have the greatest financial incentive to work. Slightly more than one third of newly arrived humanitarian migrants are single adults without children. The introduction benefit is very important to ensure that any extra hours spent in work alongside the introduction plan are profitable in 2017. For single adults without children, the replacement rate is largely the same irrespective of whether they receive income support or introduction benefits.

Not clear whether or how financial incentives for new arrivals should be strengthened

The financial incentives to work have been strengthened in recent years, both generally and for those with low incomes. The launch of the introduction benefit has led to strengthening financial work incentives for many newly arrived humanitarian migrants. The benefit is often higher than income support. Denmark, for example, has chosen to strengthen these financial incentives through lower benefit levels for new arrivals than for the rest of the population.

The impact of financial incentives on people who have poorer prospects in the labour market is uncertain. Studies indicate that strengthened financial work incentives increase the likelihood of working for those who have the best prospects, while those with the poorest prospects are at risk of leaving the labour force. One impact assessment of the introduction reform indicates that it has had a small positive impact on employment and wage earnings. Swedish research also supports the idea that foreign-born people benefit greatly from individualised and enhanced employment services. Sufficiently high benefits during the time new arrivals improve their prospects may motivate them to remain in the labour force. It is therefore not self-evident that reduced benefit levels result only in positive outcomes.

Measures in a number of areas are needed to shorten the time to become established in the labour market. A sound incentive structure is naturally an important part of this, but based on what has emerged during our work on this report, it is not clear how incentives to work can best be strengthened for newly arrived refugees.

Since the introduction benefit was launched, the rules have changed on a number of occasions and financial incentives have been both strengthened and weakened, most recently on 1 January 2018. In the memorandum that preceded the amended regulatory framework for the introduction system, the matter of the benefits' design and their significance for financial work incentives were not discussed at all. Nor does it seem in earlier amendments that any analysis was conducted of how the changes would interact with other transfer systems or how they would affect different groups. The area is complex and needs to be investigated thoroughly. In particular, light must be shed on the significance of family policy support. In this report, proposals for changes have emerged that should be considered in a review of the introduction benefit.

- *Individualise the introduction supplement.* Receiving introduction benefits makes financial work incentives stronger for the first member of a cohabiting couple who begins to work. Compared with income support, financial work incentives are weaker for the second partner. It is likely more often a woman who is in the situation that a partner is already working. This effect could be mitigated by individualising the introduction supplement (which would then be at the expense of a slightly weaker financial incentive to work when the first partner begins working). This could be designed so that the effect can be evaluated, for example by having the new rule apply to those who are granted the introduction supplement from a certain date.
- *Review the benefit levels for children in the introduction supplement and income support.* When the introduction benefit was launched in 2010, it was considered important that the level be such that supplementary income support would be possible only in exceptional cases. Since that time, the benefit has remained unchanged, while prices, wages and other benefits have risen. In general, it is relatively unusual to receive supplementary income

support for a long period of time. It is more common for families with many children, which is likely due to the fact that the extra allowance for those with many children is higher in income support.

- *Review coordination between the introduction supplement and maintenance support.* Child support paid by the other parent does not reduce the introduction supplement for a single parent with children, which the national maintenance support does. This means that single parents with children may have different disposable incomes, depending on whether the other parent takes responsibility to support their children. The question is whether this is reasonable or whether child support and maintenance support should be handled in the same way. In the case of income support, no difference is made between child support and maintenance support.

In conclusion, low benefit levels can encourage the transition to work but can also involve increased income disparities and an increased risk of financial vulnerability, not least for children. Although the regulatory framework, except for the introduction benefit, applies to everyone, many in the newly arrived humanitarian migrants group can expect weak short-term financial work incentives and therefore risk ending up in a poverty trap, while also living in financial hardship. This means that the choice between strong financial incentives to work and reasonable living conditions is brought to a head.