JobMaker isn't ambitious enough

Submission to the Senate Economics Legislation Committee inquiry into the Economic Recovery Package (JobMaker Hiring Credit) Amendment Bill 2020

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1 Summary

We welcome the opportunity to make a submission to the Senate Economics Legislation Committee inquiry into the Economic Recovery Package (JobMaker Hiring Credit) Amendment Bill 2020. This submission summarises recent Grattan Institute work on the design of a hiring credit scheme, and on the broader imperative of reducing unemployment as quickly as possible.

COVID-19 has left many Australians out of work. Unemployment has risen to its highest level since the 1990s, and hours worked have plummeted in a way never before seen. Getting Australians back to work as quickly as possible – and therefore avoiding long-term scarring from sustained high unemployment – is an urgent priority.

The Government's JobMaker hiring credit scheme ('JobMaker') is a positive step that will support employment as the economy recovers. But the eligibility criteria for JobMaker are unnecessarily narrow and preclude important opportunities for accelerating employment growth.

Targeting the credit towards younger Australians who previously received JobSeeker probably maximises the benefits – in terms of avoiding long-term scarring – for a given budgetary outlay on hiring credits. But such targeting is undesirable given the scale of the employment challenge we face. More than half of Australians currently on unemployment benefits are older than 35. Eligibility for JobMaker should therefore be broadened to cover new employees of all ages, not just those younger than 35. And the requirement that new hires were previously on JobSeeker (or a related payment) should be abolished.

Other aspects of the design of JobMaker could also be improved. Many of the almost one million employers on JobKeeper will be effectively excluded from the scheme; this could be remedied by excluding employers' JobKeeper receipts from the payroll baseline test. The test itself should be more demanding: the current requirement for payroll to increase only by the amount of the hiring credit claimed will create incentives to convert full-time jobs to part-time and make the scheme less cost-effective. And the low, fixed-rate credit of $200 a week (or $100 a week for 30-to-35 year-olds) for new employees will bias the scheme towards part-time and low-wage jobs, providing little incentive for firms to employ full-time staff.

Fixing these flaws would improve JobMaker. However a better model altogether would be an incremental payroll rebate, which would encourage employment growth across all possible margins, creating stronger incentives to hire full-time workers and expand hours for existing staff. Such a scheme would generate more employment, albeit at substantially higher cost, and be much simpler to administer.

But even an expanded hiring credit is no substitute for stronger labour demand, underpinned by faster economic growth. Unemployment is forecast to hit 8 per cent by Christmas, but then take three-and-a-half years to fall to 5.5 per cent by mid-2024. That would be a slower recovery from this recession, as far as unemployment goes, than from most recessions in Australia's history. Such a slow recovery will create great harm – to the unemployed themselves, and to other Australians in the form of sluggish wages growth.

The Government must aim to create jobs and reduce unemployment as rapidly as possible. A further $50 billion in fiscal stimulus over and above what was announced in the 2020 Budget is needed to drive unemployment back down to 5 per cent by the end of 2022, a result that would kick-start wages growth nearly two years ahead of the Government's schedule. Australians should not settle for a prolonged slump, with all the scarring and misery it would bring.

2 Getting Australians back to work is an urgent national priority

The pandemic has thrown many Australians out of work. Unemployment has risen to its highest level since the 1990s, and hours worked plummeted in a way never before seen.

Job losses have been concentrated among younger people – they are disproportionately employed in industries such as hospitality and the arts that have borne the brunt of the COVID shock. But older Australians have suffered as well. Unemployment and, particularly, underemployment have risen across the board, for all age groups.

Unemployment rose very quickly, but is expected to fall slowly. A sustained period of high unemployment has long-lasting effects for people directly affected by it. And sustained high unemployment hurts the economy in the long term.

Much of this pain can be avoided if unemployment falls quickly. Getting Australians back into work as quickly as possible is therefore an urgent national priority.

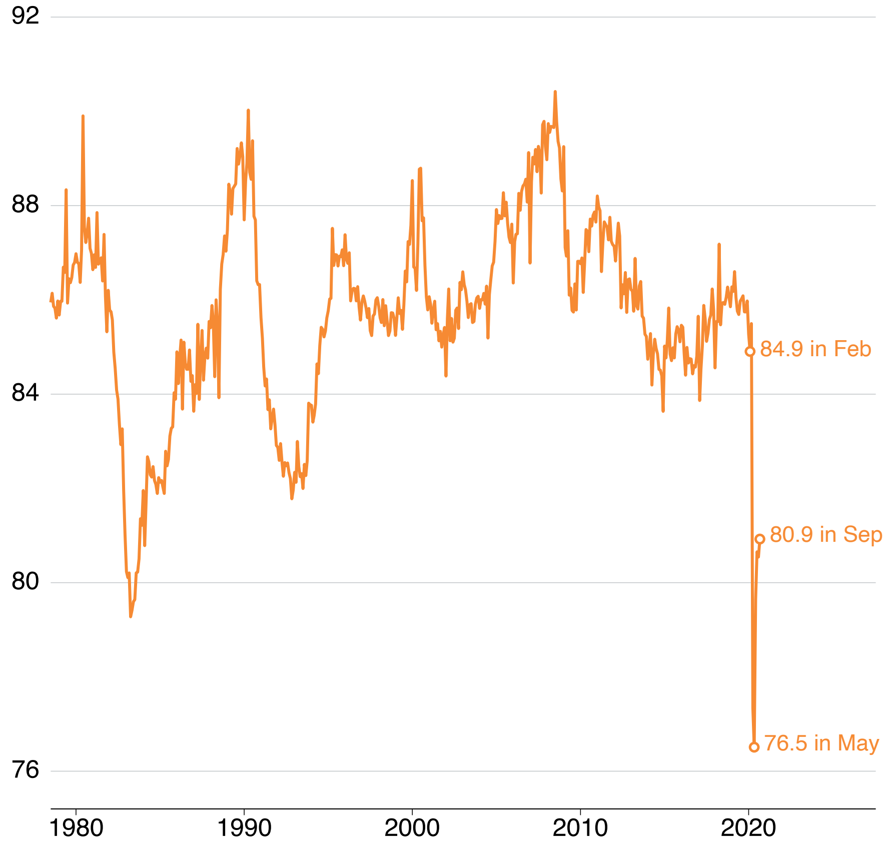
2.1 COVID-19 has thrown many Australians out of work

COVID-19 and the public health response to the virus have hit the Australian labour market hard. Jobs and hours worked have fallen sharply, and the proportion of people either looking for work or looking for more hours has risen to levels not seen in several decades.

The unemployment rate shot up from 5.1 per cent in February to 7.5 per cent in July, its highest rate in about 22 years.[1] It has since fallen a little, to 6.9 per cent in September, but the Treasury expects it will peak at 8 per cent in the coming months.[2] This is a stark rise. But the

Figure 2.1: The number of hours worked per person fell dramatically after the COVID shock

Total hours worked per Australian adult per month



Notes: Seasonally adjusted monthly data. 'Adult' refers to civilians aged 15 and older.

Sources: ABS (2020a) and Grattan analysis.

1. ABS (2020a).
2. Australian Government (2020a).

change in the unemployment rate understates the effect of COVID on the labour market.

The effect of COVID on the labour market can be seen more clearly in other measures. In Australia, people who are stood down from work but are still receiving payment – such as through the JobKeeper program – are classified as 'employed' and therefore are not counted as unemployed.[3] The ABS has calculated that if people who were 'stood down' or working zero hours because there was no work were counted as unemployed, Australia's unemployment rate would have hit 11.8 per cent in April.[4]

The underemployment rate – the proportion of the labour force that has a job but would like more hours – has also shot up, from 8.6 per cent in February to 11.4 per cent in September. The under-utilisation rate – the proportion of the labour force that is either unemployed or underemployed – rose from 13.7 to 18.3 per cent.[5]

The size of the COVID shock is seen most clearly in data on the number of hours worked. Back in February, there were 1.76 billion hours worked; on average, that's 84.9 hours for each civilian adult in Australia.[6] This plummeted to 76.5 hours per person in May, by far the lowest on record. In September, the figure was 80.9 hours per adult – a rapid recovery, but one that still leaves Australia with less work per person than at any stage except in the depths of the 1980s recession (Figure 2.1).

3. The Australian labour force measurement framework is in line with standards agreed through the UN's International Labour Organisation. See discussion in Appendix C of Coates et al (2020a).
4. ABS (2020b).
5. ABS (2020a).
6. 'Adult' here means someone aged 15 or older. ABS (ibid).

2.2 Young people have lost the most jobs and hours, but all Australians have been affected

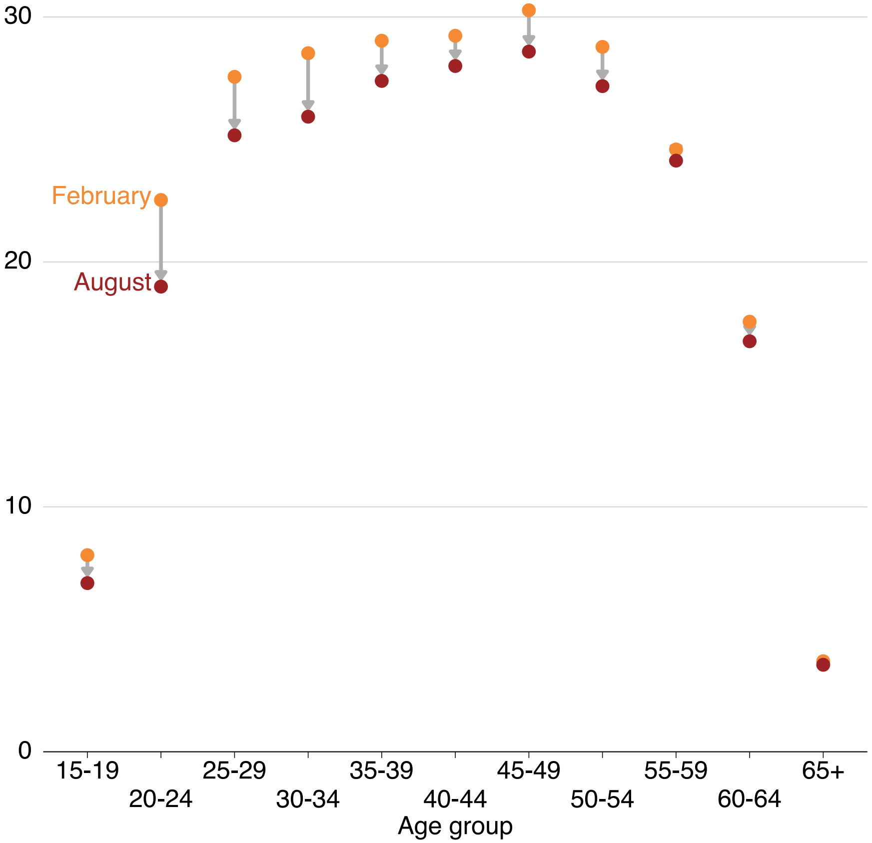
The coronavirus shock hit young people the hardest. The hardest-hit industries – arts and recreation, and hospitality – employ younger Australians in disproportionate numbers. The youth unemployment rate rose from 12.3 per cent in February to 14.5 per cent in September (Figure 2.3). It peaked at 16.4 per cent in June.

But young people are not the only ones to have lost jobs and hours since COVID-19 struck. Unemployment rates have risen for all age groups, and underemployment has risen markedly (Figure 2.2). The under-utilisation rate has also risen across the board (Figure 2.4). The under-utilisation rate for people aged 15-to-24 rose sharply in the initial phase of the pandemic, but has fallen rapidly since. The rate for young people was around 3 percentage points higher in September than in February; other age groups suffered a bigger rise in under-utilisation.

The data on hours of work confirm that Australians in all age groups have suffered as a result of COVID. On average, people in their early 20s worked 22.5 hours per week in February. This fell to 19 hours in August, a 3.5 per cent fall. This is the largest decline in hours worked for any age group, but other groups also suffered large falls. For Australians aged between 35 and 54, hours worked per person fell by about 1.6 per cent.[7]

7. ABS (ibid) and Grattan analysis. Note that these figures refer to the total number of hours worked divided by the total number of civilians in the age group.

Figure 2.2: All age groups have suffered a decline in hours of work
Average hours worked per person per week, by age group, February and August 2020



Note: Not seasonally adjusted.

Sources: ABS (2020a) and Grattan calculations.

Figure 2.3: Unemployment and underemployment have risen among every age group
Unemployment and underemployment rates by age group, February and September 2020

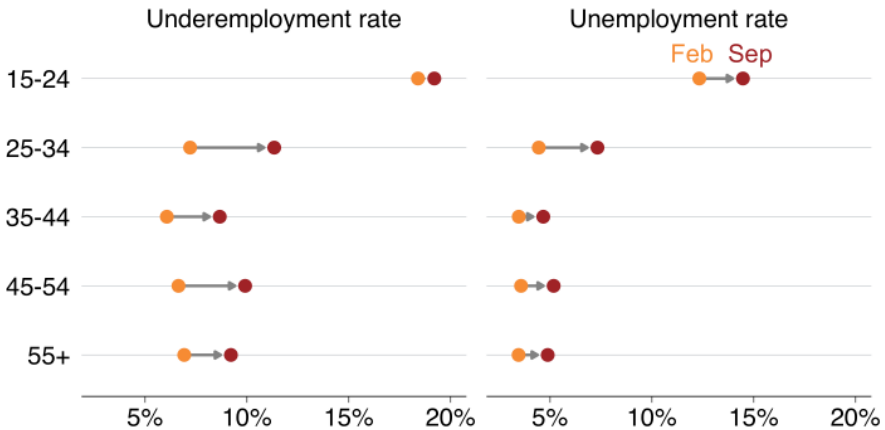
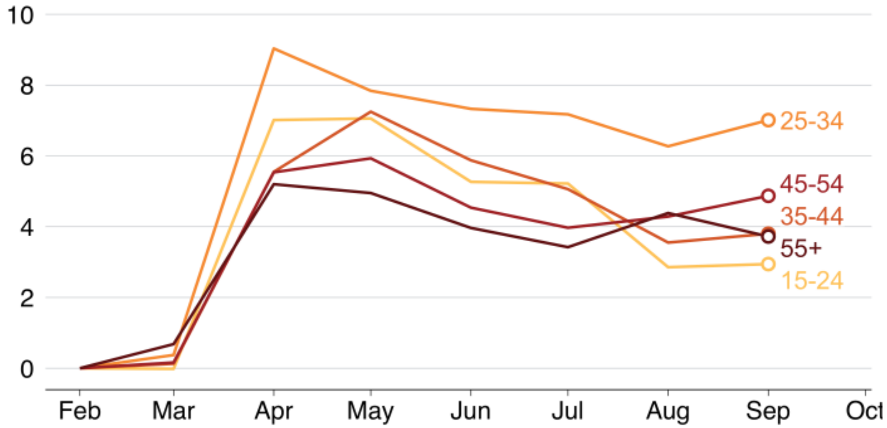


Figure 2.4: The under-utilisation rate has risen for all age groups
Change in labour force under-utilisation rate since February (percentage points)



Note: Seasonally adjusted monthly data.

Sources: ABS (ibid) and Grattan calculations.

2.3 Unemployment is forecast to remain high for years

Although unemployment is now not expected to reach double digits – as was widely anticipated in the early phase of the pandemic – the pace of recovery is now expected to be slower than was earlier envisaged. The federal Budget, released in October, forecasts that the unemployment rate will rise to 8 per cent in the final quarter of 2020. It's then expected to take three-and-a-half years to fall to 5.5 per cent (Figure 2.5).[8]

That's a relatively slow recovery, with the unemployment rate expected to fall by an average of just 0.71 percentage points per year. It would be a slower recovery than Australia had after the 1990s and 1980s recessions (Figure 2.6), and slower than many other recoveries in OECD nations in recent decades.[9]

This means that, with current macroeconomic policy settings in place, Australia looks set to endure about half a decade with elevated unemployment. This will impose real costs on Australians. The unemployed themselves will endure a period – for too many, an extended period – of meagre income, lost opportunities for career progression, and lost social connection. Employed Australians will have stagnant incomes: the Budget anticipates that inflation-adjusted wages will be around the same level in 2024 as in 2020.[10] This is to be expected with an unemployment rate well above the level that could be sustainably attained.[11]

8. Australian Government (2020a).
9. Coates and Cowgill (2020).
10. Australian Government (2020a, Statement 1, Table 2).
11. Pre-pandemic, the Reserve Bank estimated that the an unemployment rate of around 4.5 per cent would be attainable without sparking excessive inflation: Ellis (2019). The Budget suggests this figure is 5 per cent: Australian Government (2020a, pp. 2–32).

2.4 Prolonged unemployment has long-term costs

Unemployment is harmful in the short run. Unemployment also has long-lasting effects. People who suffer unemployment can be 'scarred' by the experience, particularly if they're out of work for a long time – their skills erode, their experience becomes less relevant, they lose touch with professional networks, and become less attractive to employers.[12] Young people who graduate during recessions suffer long-term consequences, with worse average labour market outcomes over their lifetimes than cohorts that graduate into booming labour markets.[13]

Treasury researchers have recently examined the 'scarring' effect of recessions. Their findings are in line with earlier work that suggests unemployment can cast a long shadow over individual careers. They found that when the youth unemployment rate goes up 5 percentage points, wages for graduates are around 8 per cent lower than they would otherwise have been, and remain depressed for years (Figure 2.7).

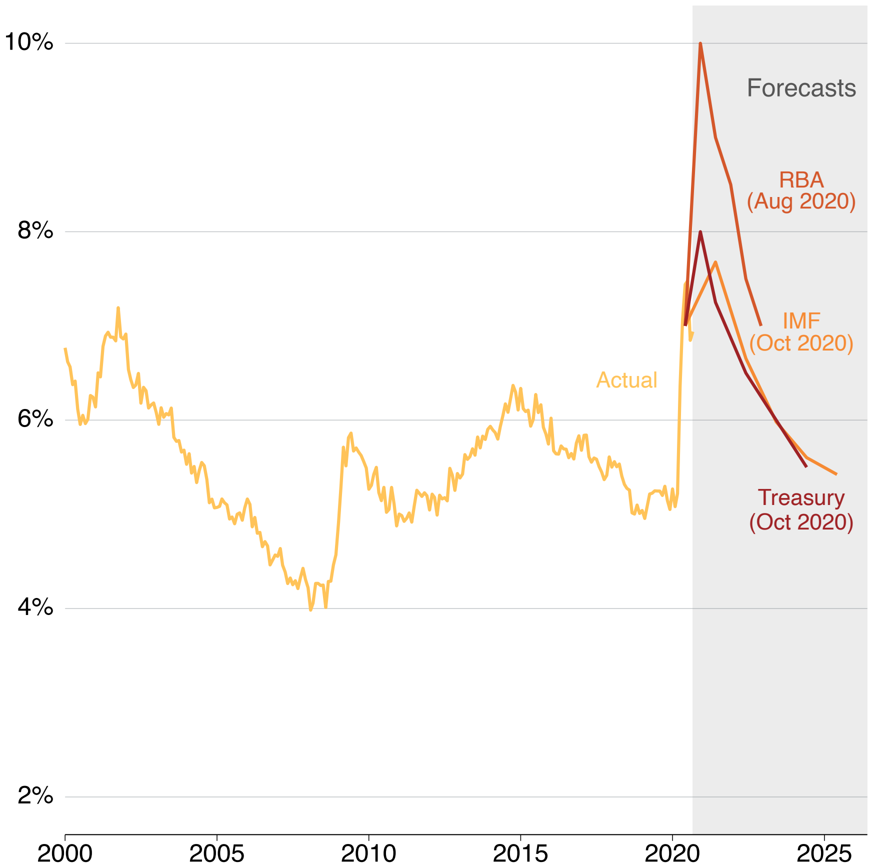
The cost of this scarring is substantial: over a decade young workers lose the equivalent of half a year's salary compared to otherwise-equivalent young people who graduated into more benign economic conditions.[14]

And past recessions also hit older Australians hard (Figure 2.8). For example, after the 1990s recessions many older Australians never worked again.

12. There is an extensive literature on this; see for example: Arulampalam et al (2001) and Rothstein (2020).
13. International studies of scarring commonly find that entering the labour market at a time when the rate of unemployment is 3-to-4 percentage points above average causes a decrease in annual earnings of 3-to-6 per cent per year for a decade: Borland (2020a).
14. Andrews et al (2020).

Figure 2.5: The unemployment rate is expected to remain above pre-COVID levels for half a decade

Unemployment rate, per cent of labour force

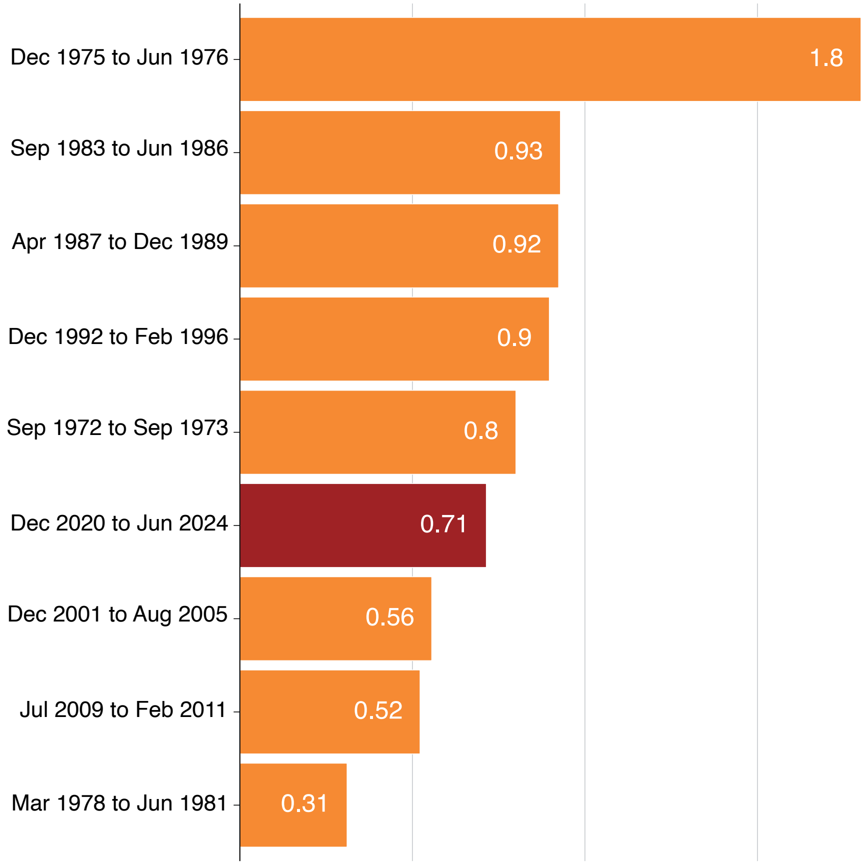


Notes: IMF forecasts are for calendar years; RBA and Treasury forecasts are for quarter averages. Actual data is seasonally adjusted.

Sources: ABS (2020c), RBA (2020), IMF (2020) and Australian Government (2020a).

Figure 2.6: Australia's recovery from the COVID recession is forecast to be sluggish

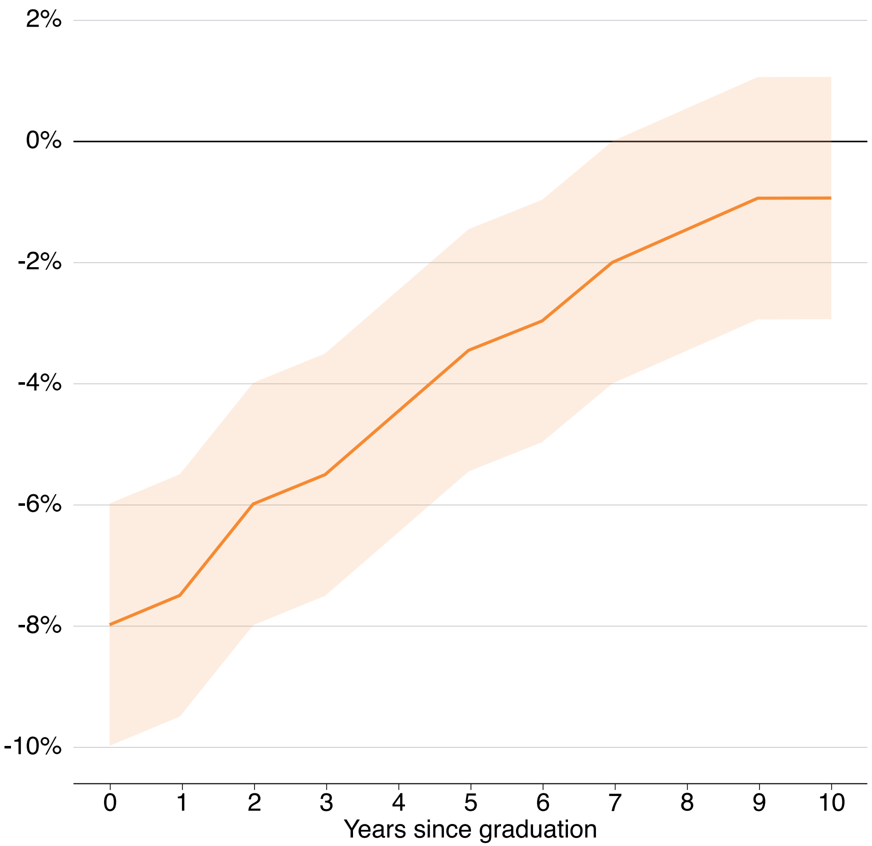
Average rate of decline of the unemployment rate following its peak (percentage points per year)



Notes: Three-month moving average of unemployment rate used. The end date is the month with the lowest unemployment rate in the four years following the recession peak, excluding any that occur after a subsequent recession.

Sources: OECD (2020a) and Grattan calculations.

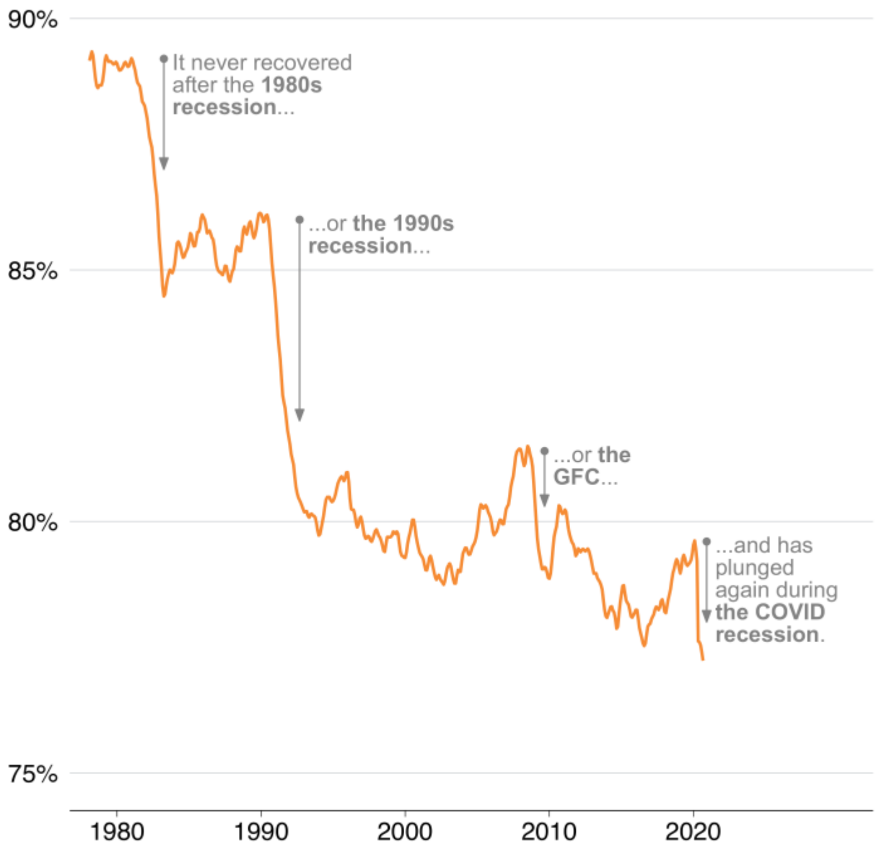
Figure 2.7: Graduating into a bad labour market depresses wages for years after graduation
Effect on wages of a 5 percentage point increase in the state youth unemployment rate



Note: Shaded area is 2 standard error confidence band.

Source: Andrews et al (2020).

Figure 2.8: During recessions, middle-aged men lose full-time work and never find it again
Percentage of men aged 35-to-54 who are in full-time employment



Note: Seasonally adjusted by Grattan Institute using the standard X13-ARIMA procedure.

Sources: ABS (2020a) and Grattan calculations.

Sustained periods of high unemployment also have long-lasting effects on the economy as a whole. There is now considerable evidence that recessions reduce the productive capacity of the economy in the long term.[15] Recessions are not just cyclical deviations from a stable long-run growth path – recessions themselves can affect the long-run growth path. Other things being equal, a higher unemployment rate in 2022 is likely to mean a higher unemployment rate a decade from now, when the COVID-19 crisis has (presumably) long passed, than would otherwise have been the case.[16]

2.5 Much scarring can be avoided if unemployment falls faster

Deep recessions leave long-term scars. But many of the long-term costs are avoidable – provided unemployment comes down quickly.

For instance, if unemployment returned to pre-recession levels within three years – by the end of 2022 – the total hit to young workers' wages over the decade would decline by one-third. For a younger worker on the average wage of $55,000 a year, that could mean a boost to their wages of $15,000 over a decade.[17]

That makes getting Australians back to work an urgent national priority.

15. See a recent review of the evidence in Cerra et al (2020).
16. Fatas and Summers (2015) found that every 1 per cent reduction in GDP brought on by tight fiscal policy translated into a 1 per cent decline in potential output five years later. Ball (2014) similarly found that countries with deeper downturns after the GFC suffered bigger falls in long-run potential output. Yagan (2019) found that each extra percentage point of unemployment in 2007-09 reduced the employment rate by 0.3 per cent in 2015, nearly a decade later.
17. Grattan analysis of Andrews et al (2020).

3 JobMaker isn't ambitious enough

JobMaker is a positive initiative that will support Australians to get back to work as the economy recovers. But the hiring credit scheme lacks ambition: the eligibility criteria are unnecessarily narrow, and exclude important opportunities for employment growth. They make the scheme significantly less effective – in reducing unemployment – than it could be.

The current eligibility criteria give priority to cost effectiveness – minimising the fiscal cost per extra person employed – over the total increase in net employment that the scheme could generate. Such a strong focus on targeting is misguided.

Employment subsidies are one of the more effective forms of fiscal stimulus available. JobMaker should be modified to broaden eligibility and generate a larger boost in employment.

3.1 There is good evidence that hiring credits can be effective, especially during deep recessions

Hiring credits, such as JobMaker, are often used to lower the cost of employing new workers whose expected value added to revenue would otherwise be less than the cost of hiring them. Credits can also be used to help otherwise-disadvantaged job-seekers, such as the long-term unemployed.

The consensus from Australian and international evaluations is that wage subsidy programs increase employment.[18] But the actual job creation from wage subsidy programs that wouldn't have otherwise occurred is typically smaller than the number of people who are provided the subsidy, for two reasons. First, the subsidy often pays for a job that would have been created anyway, so the subsidy merely changes who gets that job. Second, employers who hire workers that don't attract the subsidy may lose business to firms that do. Experience suggests about 10 per cent of jobs supported by hiring credit schemes tend to be truly additional – jobs that wouldn't have been created without the subsidy.[19]

Hiring credits are typically used to help people who are struggling to find work, such as the long-term unemployed, or groups often overlooked due to discrimination.[20] Helping such people get a job can help prevent long-term poverty – even if it means other qualified candidates take longer to find work. Such an approach is often accompanied by a strong focus on cost effectiveness (the net jobs created) for each dollar of hiring credit spent.[21]

However, hiring credits can also be effective fiscal stimulus during recessions since they directly target the main objective of boosting jobs growth.[22] With interest rates already approaching zero, and much slack in the labour market, the impact of hiring credits on employment are likely to be more enduring.[23]

18. Borland (2016, p. 134). In a survey of the international literature, Card et al (2018) find wage subsidy schemes tend to have little to no effects on participants' employment prospects in the short term, but do increase the likelihood that participants are employed in the medium term and long term.
19. Borland (2020b).
20. Groups that might be discriminated against include older people, people with disabilities, and the long-term unemployed. Borland (2016).
21. For example, see Borland (2020b).
22. By definition hiring credits, provided they lead to additional employment, boost output in employment-intensive sectors.
23. For example, Faia et al (2010) estimate large fiscal multipliers in the range of $3 for each $1 spent on hiring subsidies across EU countries.

3.2 JobMaker is targeted too narrowly

JobMaker will be available to employers for each new job they create for which they hire an eligible person aged 16-to-35. Firms will be able to claim on a quarterly basis for up to 12 months from the date the new position is created at a rate of:

- $200 a week for each additional eligible employee they hire aged 16-to-29 (up to $10,400 per job created); and
- $100 a week for each additional eligible employee aged 30-to-35 years old (up to $5,200 per job created).

To be eligible, the employee must have received the JobSeeker Payment, Youth Allowance (Other), or Parenting Payment for at least one of the previous three months at the time of hiring. The employee must work an average of at least 20 hours a week for each quarter in which the employer is claiming the credit.

The Government expects that about 450,000 positions for young Australians will be supported by JobMaker, at a cost of $4 billion from 2020-21 to 2022-23.[24]

Yet some 1.5 million Australians are on JobSeeker or Youth Allowance, including close to 700,000 aged under 35 years (Figure 3.1). Assuming that one in 10 jobs attracting the hiring credit are truly additional, as Treasury expects, JobMaker will put just 45,000 young Australians into jobs. But that barely puts a dent in the economy-wide unemployment problem – it is only one in 15 of the target group of unemployed.

As Section 2.1 explains, the unemployment impacts of the crisis go well beyond young people and low-wage jobs. Australia should be aiming to rapidly reduce unemployment to pre-COVID-19 levels and then beyond until healthy wage growth returns. We should aim higher than simply reshuffling the queue for an inadequate pool of new positions.

24. Australian Government (2020b).

3.2.1 JobMaker should be available for workers of all ages

Eligibility for JobMaker should be broadened to cover new employees of all ages, not just those younger than 35.

The current design excludes the more than half of Australians currently on unemployment benefits who are older than 35 (Figure 3.1). Targeting younger workers – who arguably stand to lose the most in the long-term should they remain unemployed for an extended period – would make sense if expenditure on the hiring credit needed to be highly constrained. But narrow targeting is the wrong priority when so many Australians are on unemployment benefits – and most of them are older than 35. Expanding the scheme to new employees of all ages would probably cost an additional $4 billion, roughly doubling its cost, but still leaving it as a moderate expense in the context of needs for further fiscal stimulus (Chapter 4).

3.2.2 JobMaker should encourage creation of jobs, regardless of who fills them

The requirement that, to qualify for JobMaker, new hires previously received JobSeeker (or a related payment) should be also abolished.

Limiting the credit to jobs filled by unemployed workers is unnecessarily constraining. If the most suitable candidate for a role is already employed, then hiring them provides an opportunity for someone else to fill their old position. It is creation of a new job, regardless of who fills it, that ultimately puts an unemployed person into work – even if that happens indirectly via a chain of hiring. The goal should be to strengthen overall labour demand, not to encourage only the subset of job creation where the new role happens to be a good match for someone currently unemployed.

The requirement to employ people already on the unemployment rolls excludes current JobKeeper recipients. About 3.5 million Australians were on JobKeeper at the end of September, although that figure is expected to fall to 1.4 million from October, 1 million in January, and zero when the scheme winds up in March 2021.[25] While many workers will remain in their jobs as JobKeeper ends, there will inevitably be a large number of workers left unemployed by that transition.[26] It's a big reason the unemployment rate is expected to rise to 8 per cent by December.

3.2.3 Many firms will be excluded from JobMaker, reducing its impact

The eligibility criteria governing firms' access to JobMaker are also too restrictive.

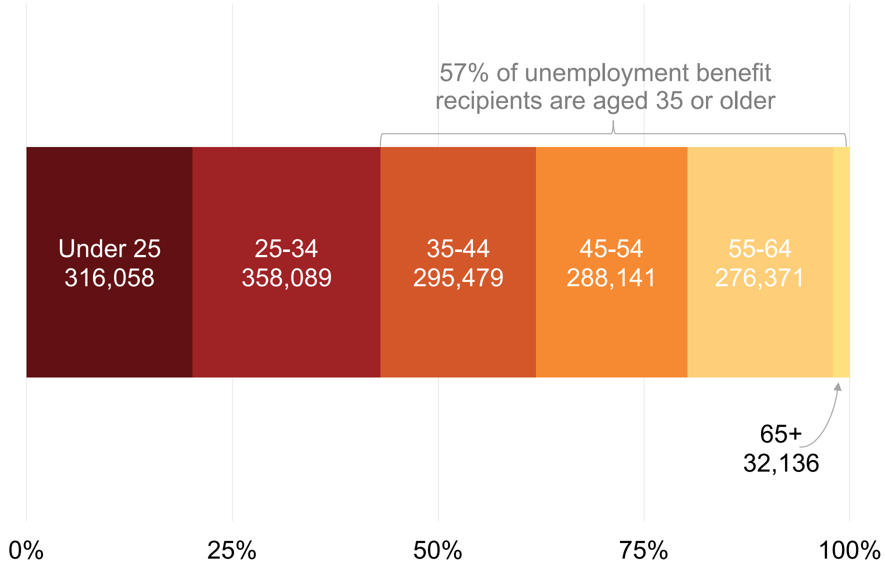
For firms to be eligible for JobMaker for new hires, they have to demonstrate:

- an increase in their total employee headcount from the reference date of 30 September 2020; and
- an increase in their quarterly payroll as compared to the three months to 30 September 2020.[27]

These criteria are intended to make the scheme more cost effective by targeting the credit at increases in employment that would not

25. Maiden (2020).
26. A survey of Australian businesses in July suggested 13 per cent would shed staff when support was removed, and one in 10 would close their doors permanently. ABS (2020d).
27. Although employers will claim the hiring credit from the ATO on a quarterly basis (for up to a year per new employee), these 'baseline values' will not be updated on a quarterly basis – instead, the employer's headcount at 30 September and payroll in the September quarter will determine whether a new job counts as additional for the entire first year of the scheme. Australian Government (2020b).

Figure 3.1: Most unemployment benefit recipients are older than 35
Number of recipients of JobSeeker and Youth Allowance (Other) payments, September 2020



Note: Youth Allowance (Other) is the payment for job-seekers younger than 22.

Source: Department of Social Services (2020).

otherwise have occurred.[28] These criteria also reduce the incentive to lay off and re-hire staff purely to harvest the subsidy.

Yet these criteria will effectively exclude many of the almost one million employers on JobKeeper from getting JobMaker.[29] Many JobKeeper-reliant firms – those hit hardest by COVID-19 – will be operating below capacity as the program is phased out over the next six months. Many will be in no position to maintain employee headcount and payroll at September-quarter levels as they exit the scheme, and they are likely to lay off staff. Other firms that largely employ part-time or long-term casual staff will have had their payroll inflated because the fixed-rate JobKeeper payments of $1,500 a fortnight – which were passed on in full to employees – exceeded the wages they would normally pay their staff.

For these employers operating below their September-quarter payroll baseline, the hiring credit provides no incentive to retain staff as they come off JobKeeper, nor to increase working hours or hire staff as conditions improve. That effectively excludes from the scope of the subsidy an important source of job growth: the expansion of working hours.

Former JobKeeper recipients with growing turnover may be in a position to expand their use of labour in late-2020 or in 2021. As business picks up they may wish to increase hours for continuing staff or, having let staff go upon losing eligibility for JobKeeper, they may in time be in a position to re-hire.

28. While not all new jobs supported by a hiring credit will be truly additional, because many recipients would have expanded employment regardless, the requirement to increase overall headcount and payroll beyond September-quarter levels means subsidy expenditure is targeted at net job growth.
29. About 920,000 firms were enrolled in JobKeeper in April-May. Australian Government (2020c).

From the perspective of overall employment, expansion within the margin of September-quarter payroll is every bit as important as expansion beyond this baseline, yet will attract no hiring credit. September is an arbitrary baseline, and many positions were being preserved by JobKeeper at that time.

JobKeeper recipients will not only lose the effective reduction in labour costs the wage subsidy currently provides, but will now face an absolute disadvantage in labour costs against their competitors. The risk is that this leads to business closures and job losses, offsetting the effect of the hiring credit.[30]

Therefore the Government should change the criteria to make the payroll baseline *net* of JobKeeper subsidies paid to the firm in the September quarter.[31]

3.2.4 The low, flat-rate credit will skew job creation towards lower-paid and part-time positions

JobMaker offers a modest, flat-rate payment for every new job created with an average of 20 hours or more worked per week. This design makes the hiring credit most effective at putting under-30s into lower-wage, part-time jobs, for which the flat-rate subsidy will be a larger proportion of labour costs. The credit offers relatively little incentive to create higher-paying full-time positions.

For example, the credit would cover 50 per cent of the wage of a worker working 20 hours per week at the adult minimum wage, and 75 per cent of a 20-hour fast food job filled by a 16-year-old (Figure 3.2).[32] But the same subsidy would cover only 18 per cent of the wage of the typical

30. Daley et al (2020); and Hamilton (2020).
31. Limitations in publicly available data prevent us from estimating the additional cost of this change.
32. These figures refer to a person aged 16 to 29, eligible for the $200 per week credit.

(i.e. median) worker (earning $58,000 a year), and just 15 per cent of the wage of the typical full-time worker (earning $70,000 a year).[33]

In practice, it may be difficult to design JobMaker to offer a hiring credit proportional to the wage of the new employee. Section 3.3 proposes a different scheme design, where the credit is paid in proportion to the net increase in total firm payrolls relative to some baseline period.

3.2.5 The 'additionality' test should be strengthened

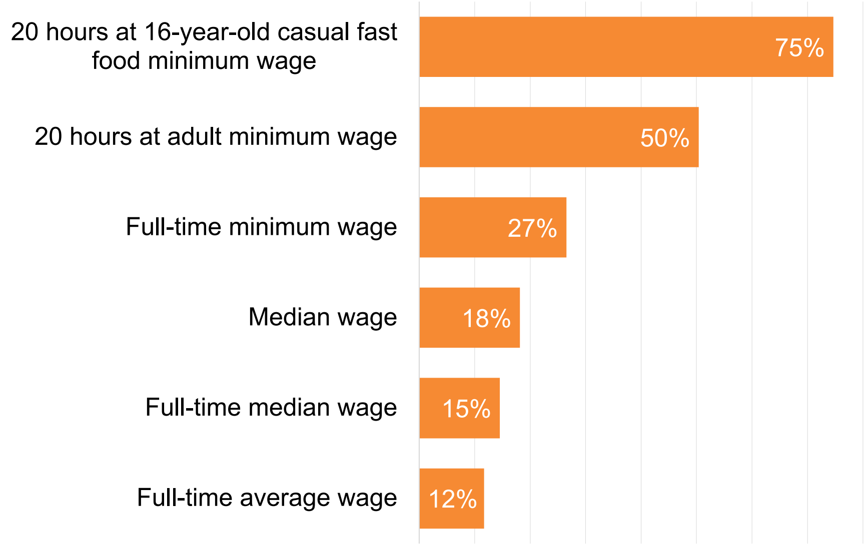
The additionality test for firms to get JobMaker should be strengthened.

The Budget factsheet on JobMaker states that 'the amount of the hiring credit claim cannot exceed the amount of the increase in payroll for the reporting period'.[34] This is not demanding enough. It allows employers to replace full-time staff with part-time staff, claiming multiple hiring credits with just a small increase in total payroll (Box 1).[35]

For example, since the $200 per week credit for 16-to-29 year-olds is about 50 per cent of the adult minimum wage for a 20-hours-per-week employee, in principle each subsidy dollar should generate at least two dollars in additional payroll expenditure.[36] But by splitting full-time

33. The flat-rate design in combination with a weak payroll additionality test also creates incentives for savvy employers to farm the subsidy by splitting full-time jobs into multiple part-time roles; see Section 3.2.5 and Box 1.
34. Australian Government (2020b).
35. Even though the payroll additionality test is easy to meet, the headcount additionality criterion appears to preclude employers from claiming hiring credits as a result of pure churn, e.g. when filling a vacated role with a previously-unemployed candidate younger than 35. However the JobMaker factsheet is ambiguous as to whether the criterion requires headcount to have increased by the number of employees the employer is claiming the credit for, or simply to have increased, regardless of the number of credits claimed. The latter would be a significant design flaw.
36. The credit is higher as a percentage of junior wages, and so leverages less private wage expenditure. The national adult minimum wage is $19.84 per hour, or about $400 for a 20-hour working week, while junior minimum rates are at set

Figure 3.2: JobMaker subsidises a larger proportion of wage costs for low-paid jobs than high-paid jobs
JobMaker ($200 per week) as a proportion of different wage benchmarks for new employees younger than 30



Notes: $200 per week hiring credit is for people younger than 30. Fast food minimum wage is inclusive of casual loading; casual loading not included in other wages.

Sources: Fair Work Commission (2020), ABS (2019) and ABS (2020e), and Grattan calculations.

jobs, savvy employers can use the hiring credit to fund up to 100 per cent of the incremental increase in payroll, which would result in a significant portion of the subsidy flowing to profits and would reduce the cost-effectiveness of the scheme in generating wage and job growth.

Raising the bar for the payroll additionality test would remove incentives for job splitting and would better leverage public dollars into private payroll expenditure. The payroll hurdle per hiring credit claimed could be a fixed multiple of the $10,400 a year credit, or a firm-specific multiple based on September-quarter average wages.[37]

3.3 A rebate on additional payroll would be more effective than JobMaker

Since the policy objective is to leverage additional private sector payroll expenditure – so as to maximise the impact – a broad-based job creation incentive should apply to all possible margins for employment growth.

A generalised incremental payroll rebate would achieve this goal.[38] Rather than paying firms on a flat-rate per-employee basis with a minimum hours threshold, it would subsidise any increase in a firm's payroll expenditure by providing an ad valorem (percent of expenditure) rebate of incremental payroll growth above a baseline (e.g. September quarter payroll net of JobKeeper).

percentages of the adult rates, with the 16-year-old minimum wage about 50 per cent of the adult minimum. It is estimated that some two-thirds of the wage of a typical 18-year-old fast food worker might be covered by the hiring credit in the worker's first year: Marin-Guzman (2020).

37. A firm-specific multiple would be functionally equivalent to an eligibility criterion limiting the number of hiring credits paid to the lesser of (a) the increase in actual headcount, and (b) the increase in payroll divided by the September-quarter average wage. The effect would be to avoid rewarding firms for replacing full-time jobs with part-time jobs.
38. The scheme was first proposed by economist Peter Downes of Outlook Economics; see Cranston (2020).

Box 1: Employers can split jobs to harvest the hiring credit: a case study

During the September quarter a firm has two full-time employees each paid $50,000 a year (total annual payroll = $100,000).

One employee resigns and the employer replaces them with two part-time employees, as well as hiring a third part-time employee in response to improved trading conditions. Each part-time employee is younger than 30, works 20 hours per week, and is paid $25,000 per year (new total annual payroll = $125,000).

The firm's total headcount has increased by two, allowing it to claim the $10,400 per year hiring credit for two employees. Total annual payroll has increased by $25,000, which is greater than the $20,800 per year hiring credit being claimed, so the 'additionality' test is met.

Although the hiring credit covers only 21 per cent of a full-time equivalent wage at this firm (= $10,400 / $50,000), and only 42 per cent of the wage of the new part-time job that the firm created, for this firm the hiring credit covers 83 per cent (= $20,800 / $25,000) of additional wage costs thanks to the conversion of a full-time position to part-time positions.

In contrast to the hiring credit, a payroll rebate would encourage expansion of hours worked by existing staff, and would not bias job creation towards part-time instead of full-time roles. In effect, the rebate would ensure better *matching* of employees to their employers, than Jobmaker. Establishing a payroll baseline *net* of JobKeeper would mean that any expansion of an employer's contribution towards wages and salaries would be subsidised, no matter how many staff they were previously supporting via JobKeeper.

And by relying solely on data already reported to the ATO, a payroll rebate would probably also be more administratively straightforward and have lower employer compliance costs than the hiring credit.

The rebate could be set at (for instance) 30-to-50 per cent of the growth in payroll. Economist Peter Downes has estimated that such a scheme could cost an estimated $10 billion to $15 billion over 12 months, and generate an estimated 150,000 to 200,000 additional jobs.[39] In contrast to JobMaker, providing hiring credits only for net additions to aggregate firm payrolls would avoid paying hiring credits for new employees that are not additional (such as those replacing departing employees), where the firm satisfies the additionality tests as both their payroll and employee headcount increase during the qualifying period.

3.4 Targeted incentives for disadvantaged job-seekers could complement a broad-based scheme

This submission argues that JobMaker should be redesigned as a broad-based hiring credit to accelerate employment growth during the economic recovery from COVID-19. As noted in section 3.2, JobMaker may well succeed in putting an extra 45,000 young Australians into jobs. Yet that would be a small share of the 700,000 Australians younger than 35 who are on JobSeeker or Youth Allowance, let alone the 1.5 million Australians of all ages who are on one of these forms of income support today.

Some commentators have highlighted the need for explicitly targeting the long-term unemployed.[40] As discussed in section 3.1, hiring credits can boost the employment prospects of disadvantaged job-seekers. There is no reason why a broad-based JobMaker scheme could not be complemented with a more generous hiring credit targeted at the long-term unemployed. Similar schemes already exist for older workers, and to support apprenticeships.[41]

Australia does not need to choose between reshuffling the queue to support disadvantaged people, and wielding employment subsidies as a tool for rapidly reducing unemployment across the board – we can and should do both.

39. Cranston (2020). Note that the modelling behind these estimates assumed that the rebate would be limited to the hardest-hit sectors, in part as a business support measure. However there would be no reason to target a rebate aimed at maximising job growth to specific sectors in this way.

40. Davidson (2020).
41. The JobTrainer program will provide wage subsidies for 100,000 new apprenticeships and traineeships for school leavers. This will largely benefit young men, who make up 75 per cent of all apprentices and trainees (see Borland (2020c) and Department of Education, Skills and Employment (2020)). The Restart wage subsidy scheme provides financial incentives of up to $10,000 to encourage businesses to hire and retain employees who are 50 or older: see Department of Education, Skills, and Employment (2020).

4 Australian governments should deploy further fiscal stimulus to reduce unemployment faster

An expanded and better-designed hiring credit scheme would help push unemployment down faster. But a hiring credit is no substitute for a stronger labour market. The federal and state governments must aim to create jobs and reduce unemployment as rapidly as possible. At a macroeconomic level, this requires more fiscal and monetary stimulus.

4.1 Inject more fiscal stimulus

Australians should not settle for a prolonged slump, with all the scarring and misery that would bring. Australian governments need to adopt further plans now to get unemployment down as quickly as possible.

Although the Federal Government announced substantial fiscal stimulus in the October Budget, unemployment is still forecast to remain at 5.5 per cent by mid-2024, well above the Treasury's estimate for full employment of 5 per cent, let alone the RBA's pre-pandemic estimate of 4.5 per cent.[42] Every year that unemployment remains too high is another year that Australians can expect close to zero real wages growth, and another year that Australians young and old will continue to confront a dearth of job opportunities.

The forecast rapid recovery in unemployment peters out from mid-2022 because stimulus is set to be withdrawn quickly – the deficit is set to more or less halve next year, and then halve again over the following two years. In addition, stimulus announced in the 2020 Budget is made up of measures not particularly likely to create jobs, such as income tax cuts (where much of the money is likely to be saved rather than spent) and transport infrastructure, which creates fewer jobs per dollar spent than services such as child care, health care, and aged care.[43]

42. Australian Government (2020a, pp. 2–32) and Ellis (2019).
43. Wood et al (2020a); and Coates and Cowgill (2020).

Treasury believes the support measures adopted since the onset of COVID-19 have been effective. It estimates that without the support measures, the unemployment rate would have peaked at about 13 per cent instead of the predicted 8 per cent, and would have remained above 12 per cent through to mid-2022, rather than falling to 6.5 per cent as currently forecast.[44] Which raises the question: why isn't the Federal Government being more ambitious and aiming to bring unemployment down faster?

We estimate that extra stimulus of about $50 billion over and above what was announced in the federal Budget will be needed over the next two years to drive unemployment back down to 5 per cent by the end of 2022, a result that would kickstart wages growth nearly two years ahead of the Government's schedule (Figure 4.1).[45] This could mean 430,000 more Australians back in work by the end of 2022 than the Government currently expects.

A more ambitious target should be perfectly achievable. In fact returning unemployment to 5 per cent by the end of 2022 would still only be the 27th fastest recovery – measured by the rate of decline in unemployment each year – out of 150 recessions recorded across OECD countries in recent decades (Figure 4.2).[46] And arguably we

44. Australian Government (4-10 2020a).
45. Past Grattan estimates of the impact of fiscal stimulus have assumed a boost to GDP (i.e. a fiscal multiplier) of 80c to $1 for every $1 of fiscal stimulus (See: Daley et al (2020)). The estimates of required fiscal stimulus in this submission use a fiscal multiplier of $1.20 for each $1 in fiscal stimulus. This change reflects our judgment that the remaining candidates for stimulus are likely to have a larger boost to GDP and employment than measures adopted to date, and multipliers tend to be higher in the second year after stimulus is introduced than in the first.
46. In contrast Australia's current forecasts for unemployment would make this only the 93rd fastest recovery among all recessions recorded in OECD countries.

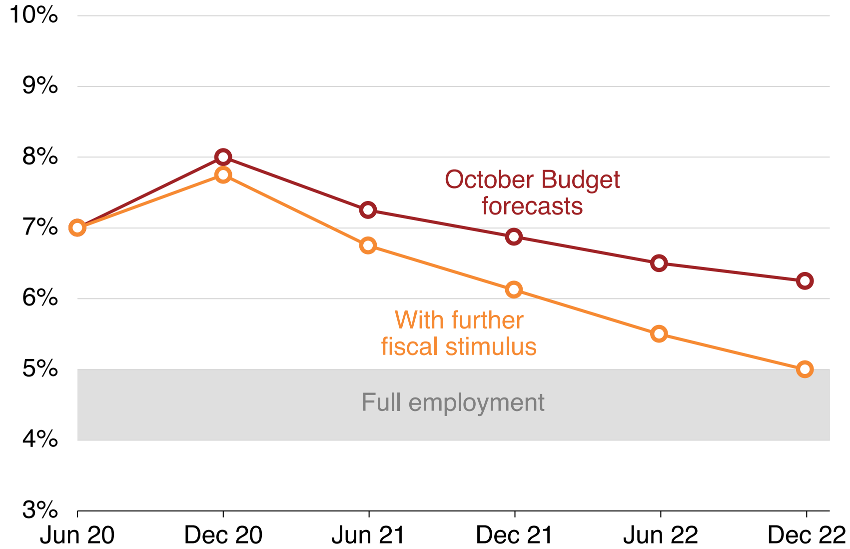
should expect the recovery from this recession to be faster than the recoveries from previous recessions, because past recessions haven't involved the government requiring businesses to close their doors.

Upcoming state budgets are likely to include some further stimulus. But the states are unlikely to deploy stimulus on the scale that's needed: the federal government taxes and spends more than all the states combined, and can borrow at cheaper rates. Designing further stimulus should therefore be a priority for the Federal Government ahead of the mid-year economic and fiscal update in December, and the 2021 Budget next May.

First, the Federal Government should fund the building of more **social housing**.[47] Even before COVID-19, the construction pipeline was drying up, especially for apartments.[48] The Government's $25,000 Homebuilder grants for new builds and renovations coincide with a recovery in greenfield land sales, but they're doing little to support urban apartment construction. Building 30,000 new social housing units today would cost about $10 billion.[49] Social housing is typically faster to roll out than most infrastructure stimulus.[50] Just as importantly,

Figure 4.1: A further $50 billion in fiscal stimulus could push unemployment down to 5 per cent by the end of 2022

Projected unemployment rate with and without extra fiscal stimulus



Notes: Unemployment rates are quarterly averages. Full employment band represents the RBA's pre-pandemic estimate of a 'full employment' unemployment rate of 4.5 per cent, plus or minus one standard error.

Sources: Australian Government (2020a) and Ellis (2019), and Grattan analysis.

47. Social housing – where rents are typically capped at no more than 30 per cent of household income – provides a safety net for vulnerable Australians. OECD (2020b) also recommends that Australia invest in social housing as fiscal stimulus.
48. Firm payrolls data published by the ABS suggests the number of construction jobs has fallen by 5.4 per cent since March, and the pace of declines has accelerated recently: ABS (2020f). Consultancy group McKinsey is forecasting 150,000-to-205,000 construction workers could lose their jobs in the year to March 2021, which would mean 12-to-18 per cent of all construction jobs would have been lost since the onset of COVID-19. Caroline Armour et al (2020)
49. Daley et al (2020).
50. A similar initiative during the GFC resulted in 19,500 social housing units being built and another 80,000 refurbished over two years, at a cost of $5.2 billion. The boost to residential construction was nearly immediate: public residential construction approvals spiked within months of the announcement. Coates and Horder-Geraghty (2020).

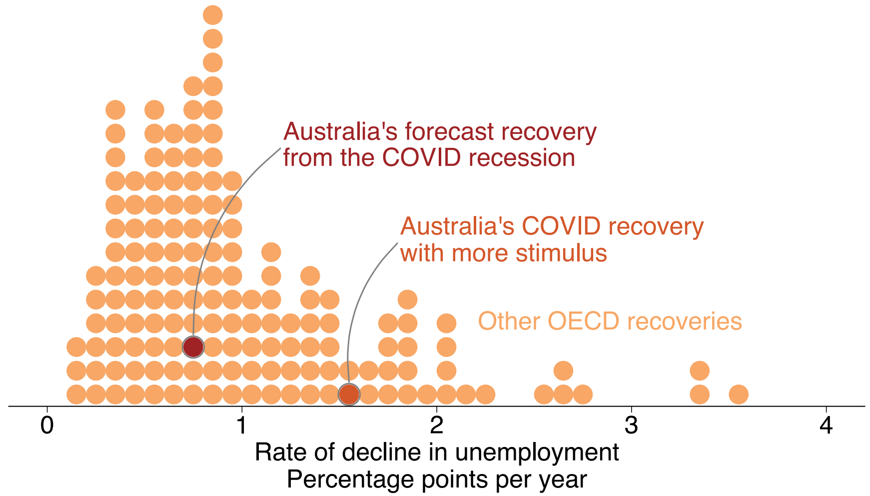
building social housing would also help tackle the growing scourge of homelessness.[51]

Increasing the rate of **JobSeeker and Commonwealth Rent Assistance** would also be effective stimulus measures, because low-income households are more likely to spend, rather than save, any additional income they receive.[52] This would constitute a permanent increase in government spending, but extra income assistance for Australia's poorest is long overdue.[53]

Given the increase in unemployment due to the crisis, the full-year cost of an increase to JobSeeker of $100 a week would be about $7.5 billion in 2021-22.[54] An increase of about $180 per week would be needed to lift the JobSeeker payment above the poverty line.[55] This would also lift unemployment benefits to about the same level as the single Age Pension. The argument to lift the payment by this amount is compelling. Lifting Commonwealth Rent Assistance by 40 per cent, which would raise the maximum weekly Rent Assistance payment for a single person by $28, would cost a further $1.5 billion a year.[56]

51. The number of social housing dwellings has barely grown over the past two decades, while Australia's population has increased by 33 per cent: Coates et al (2020b, Figure 3.4).
52. Estimates suggest that each dollar of cash payments made to low-income or liquidity-constrained households boosts GDP by between 60 cents and one dollar (the 'fiscal multiplier'), with more recent estimates being higher, and most of the benefit is derived in the first few months after the payments are made. However some studies find that when interest rates are as low as they can go, government spending multipliers can be three or even four times larger than in normal time. For example, see: Ramey and Zubairy (2018).
53. The base JobSeeker payment rate of $287.25 a week is so low that the payment is not adequately fulfilling its core function of providing a minimum, adequate income. People on unemployment benefits have an income below the poverty line – using any reasonable definition of that line – as well as heightened levels of financial deprivation and stress.
54. Daley et al (2020).
55. Daley et al (ibid)
56. Daley et al (ibid).

Figure 4.2: Australia should aim for a quicker recovery in unemployment
Average rate of decline of the unemployment rate following its peak, in past OECD recessions



Notes: Three-month moving average of unemployment rate used. The end date is the month with the lowest unemployment rate in the four years following the recession peak, excluding any that occur after a subsequent recession. Excludes 'micro recoveries', defined as those with less than 6 months or 0.5 percentage points between peak and trough. Recessions defined using the Sahm Rule. In the 'more stimulus' scenario, Australia's unemployment rate reaches 5 per cent in Q4 2022.

Sources: OECD.Stat and Grattan calculations.

Government spending on services to deal with the fallout from the COVID-19 health crisis should also be a priority. Estimates suggest such government spending typically boosts GDP by between 80 cents and $1.50 dollar for each dollar spent – in part because there is a guarantee the funds will be spent, rather than saved.[57] The federal and state governments should, for example, increase funding for aged care, mental health, and domestic violence services, because demand for those services has risen during the lockdown and is expected to remain higher.[58] There is also a strong case for more, permanent, funding of aged care.

Increasing **childcare subsidies** to reduce parents' out-of-pocket costs, thereby increasing incentives to work, is one of the more significant economic reforms that governments could implement. Grattan Institute's recent report, *Cheaper childcare*, estimated that higher workforce participation from an additional $5 billion a year in childcare spending would boost GDP by about $11 billion a year.[59] And reducing childcare costs would give groups hit hard by the pandemic the best chance of being 'job ready', because it would help those who have lost jobs or hours keep their children in care.

Time-limited vouchers to boost spending in hard-hit sectors such as hospitality and tourism would also provide a big short-term boost to the economy for every government dollar spent. The Northern Territory and Tasmania have launched time-limited vouchers for spending on local tourism.[60] Britain adopted a similar scheme, 'Eat Out to Help Out', which provided government-funded discounts for dining on Monday to Wednesday nights.

57. Tulip (2014, p. 5) and Coenen et al (2010, p. 32). CBO (2014, p. 5) estimates mutlipliers of between 50 cents and $2.50 for a dollar of government consumption in the US.
58. See Towell and McCauley (2020) and Bavas (2020).
59. Wood et al (2020b).
60. NT Tourism (2020) and Tasmanian Government (2020).

Australian governments should also consider initiatives and investments consistent with a **low-emissions future**, such as mandatory roll-out of smart meters (subject to a technology review) and retrofitting buildings to improve energy efficiency.[61]

4.2 Concerns over rising public debt shouldn't hold Australia back

The budgetary cost of further stimulus spending naturally raises concerns about the burden rising debt will place on younger generations. But concern over the cost of public debt shouldn't hold the Government back.

Australia has the fiscal space to borrow to support the economic recovery, having come into this crisis with low debt by international standards. And it has never been cheaper to borrow. The Australian Government 10-year bond rate is now less than 1 per cent. Adjusted for inflation, the *real* interest rate at which the Federal Government can borrow is below zero.

Following further stimulus announced in the October Budget, Australia is expected to spend 0.9 per cent of GDP on interest this financial year, falling to 0.8 per cent by 2023.[62] That's lower than the 1 per cent it spent in 2018–19, despite a big growth in debt. And debt is expected to shrink as a share of GDP over the next 40 years, despite projections that interest rates will gradually rise from 1 per cent today to 5 per cent within the next two decades.[63]

Younger generations are bearing much of the economic costs of the shutdown: they are more likely to have lost their jobs. If Australian governments refuse to provide more stimulus, younger generations

61. OECD (2020b) argues that Australia should invest in energy efficiency as part of fiscal stimulus measures.
62. Australian Government (2020a).
63. Ibid.

will also bear the bulk of the long-term costs of a severe and prolonged recession.

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