Universal Basic Income: a solution for labour challenges in GCC States?

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A growing number of countries globally are considering and sometimes experimenting with Universal Basic Income (UBI), as an instrument for wealth distribution and social equity. GCC states could be the ideal testing ground for new distributional policies such as UBI which could reduce the fiscal burden of an over-extended public sector workforce while maintaining the social contract.

Introduction

Since at least the 1970s, the social contract between GCC states and their citizens has been based on a unique system of wealth distribution that provides a wide range of in-kind benefits, including free education and healthcare, energy and food subsidies, and housing support.The most important and unusual benefit of all, however, has been an open-ended guarantee of government employment, particularly for male citizens. This has led to significant overemployment in GCC public sectors, with the majority of nationals holding public rather than private jobs –a situation that is almost unparalleled in the world. The only other country with a comparable welfare system is the small Southeast Asian petro-monarchy of Brunei.

While this arrangement has maintained a broad middle class and kept social peace, it has come at inordinate fiscal cost: In Bahrain, Kuwait, Oman and Saudi Arabia, spending on government salaries and benefits now reaches 50% and more of total government expenditure, which is more than twice the share in advanced non-oil countries. While the share is lower in Qatar and the UAE, their wage bills have also been creeping up quickly.

Public employment guarantees have become fiscally unsustainable in an era of double-digit fiscal deficits. They are also highly economically distortive, as they discourage nationals from becoming active in the private economy, resulting in very low overall labour market participation by citizens. They lead to distorted education and skills acquisition choices and, in many cases, unrealistic expectations regarding work hours and working conditions in the private sector. Especially in the GCC countries with relatively lower oil income per capita relatively less oil-abundant Bahrain, Oman and Saudi Arabia, public employment has also become a highly exclusive and inequitable benefit as not all new job seekers have access to it anymore. Finally, excess employment in public sectors has been bad for administrative efficiency, as de facto job guarantees break incentive systems and make targeted, needs-based recruitment difficult.

It is clear that this system cannot continue – but what can replace it? Simply rescinding job guarantees without compensation is not feasible socially or politically: GCC nationals arguably have a moral and political claim to minimal welfare given the riches of their countries. Wages in the low and mid-skilled segments of the local private sector, moreover, are pulled down by the easy availability of low-cost expatriate labour – another unique feature of GCC labour markets – which makes it difficult for all but the most skilled nationals to compete effectively even if they decide to do so.

GCC economies instead need smart wealth distribution reform, converting spending on surplus public jobs into less distortive, more inclusive and market-conforming welfare mechanisms. The debate on such reforms started across the region after the collapse of oil prices in 2014, and several governments have already experimented with new wealth sharing mechanisms. Some of the debate has been inspired by broader international discussions of a universal basic income (UBI) and other innovative welfare policies, themselves motivated by increasing labour market inequality and threats to traditional employment through automation and artificial intelligence – trends that potentially augment the national employment challenge in the GCC too.

Distributional reforms ideas

There are two basic approaches to distributional reform: unconditional sharing of cash (as through a UBI) or means-tested support payments.

Unconditional cash grants would go to all adult citizens and could serve as a more transparent and inclusive replacement for the wealth sharing implicit in government employment. Such grants should only be available for citizens who do not already hold a government job, thereby incentivizing more entrepreneurial public employees to potentially leave government and try to top up their newly acquired UBI with incomes from private employment or entrepreneurship.

“Golden handshake” policies of early retirement could further help trim the public payroll. New recruitment in government would happen only selectively, leading to significant long-fiscal term savings through gradual, needs-based government downsizing. The leadership would need to give a clear political signal that the government employment guarantee has ended – and stick to this decision. In the short run, complementary financing for a new UBI could be mobilized through energy subsidy reforms, effectively replacing another regressive and distortive, if somewhat smaller, wealth sharing mechanism with a more inclusive one.

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The beauty of a well-designed UBI would be that it would provide basic security and a clear and transparent commitment to citizen welfare, while being low enough to incentivize nationals to seek complementary private income to reach the middle class lifestyles they desire. Thanks to a UBI, they could do so even with relatively modest supplementary private income.

A second, somewhat less radical approach to distributional reform would be to gradually replace the public sector employment guarantee with **more conventional means-tested benefits.** One version of these would be a basic income guarantee under which welfare payments are phased out with increasing (private) income. While fiscally less costly, such a system would result in implicit taxation of private incomes, thereby disincentivizing private effort compared to a UBI arrangement.
To reduce this disincentive effect, at least some of the means-tested benefits could be made contingent on private employment, providing wage subsidies that would again be phased out with higher wages – similar to the Earned Income Tax Credit in the US or the Workfare Income Supplement in Singapore. Such wage supplements would encourage citizen labour market participation and improve take-home incomes. At the same time, as some of the subsidies would be indirectly captured by employers due to lower gross wage demands, they would help to narrow the labour cost gap with expatriate workers.
This gap is especially large in lower-skilled segments of the labour market [see first graph below]. Again, a combination of transfers and market income could together allow nationals to maintain a middle-class lifestyle.

Any of the above scenarios would be cheaper in the long run than mass public sector employment. The schemes are also less distortive of economic incentives, more conducive to private economic activity, more inclusive, and distributionally progressive compared to the status quo. They are also sensitive to the particular social and economic context in the Gulf, where nationals are exposed to particularly harsh competition from low-wage foreigners, justifying levels of assistance that go somewhat beyond what is offered on advanced labour markets that are less reliant on low-cost migrant workers.

Practical experiences and obstacles

Several countries in the region have gathered initial experiences with innovative distributional reforms. In December 2017, Saudi Arabia introduced a "citizens' account" system that provides mean-tested cash grants to Saudi households to compensate them for energy subsidy reforms and tax increases. While the means-testing has not been perfect, the program has had a positive distributional effect, primarily aiding poorer households, while under the previous energy subsidy system rich ones tended to benefit disproportionately.

Kuwait has been providing wage subsidies for nationals in the private sector since the early 2000s, which has helped the country reach higher levels of private citizen employment than in Qatar and the UAE. The system's efficacy has been undermined by repeated increases of public sector wages, however, and it is not means-tested but rather disproportionately benefits Kuwaitis with higher levels of education. There is also evidence of subsidy fraud, highlighting the need for strict monitoring and sanctioning mechanisms in any such system.
Kuwaiti and Saudi technocrats are now discussing UBI and augmented wage subsidy policies internally. While means-tested systems are harder to implement and also are a harder political sell, high-deficit countries like Bahrain, Oman and Saudi Arabia might not have the fiscal luxury anymore to move to a full UBI. For high-rent countries Kuwait, UAE, and Qatar, the UBI option remains feasible and attractive.

In the short- to medium term, the trickiest part of moving to a new distributional system could be the temporary cost of transition. To make public sector downsizing politically acceptable, governments likely have to offer golden handshakes and while UBI or wage subsidies would kick in immediately, the savings from government shrinkage would likely accrue only gradually. In this context, fiscal savings from complementary reforms such as a reduction in energy subsidies could be very helpful: In a recent research paper on distributional reforms in Kuwait, I estimate that the savings from energy subsidy reform alone could finance an ongoing monthly grant of 212 KD per adult ($692) outside of govern-ment.

Outlook

The GCC is coming late to the international debate about welfare innovation but is in fact an ideal testing ground for new distributional policies, given that its existing distributional regime is so distortive. Notably, none of the arguments against universal basic income schemes that are routinely made in the Western context apply in the Gulf: different from OECD countries, a UBI in the GCC would necessitate no new taxes and no new net expenditure; it could instead be financed through reforms of existing distributional structures. While a UBI could create work disincentives in OECD labour markets, the incentive distortions of the status quo in the GCC are significantly worse than they would be under a UBI. Finally, the issue of fairness – why should wealthy citizens also receive UBI? – is much less acute in the GCC given that inherited employment and subsidy systems are quite regressive and disproportionately benefit better-off citizens. A move to a UBI would be distributionally progressive.

Fortunately, the GCC's current wealth distribution regime is so lopsided that smart distributional reform can produce more winners than losers and still produce long-term fiscal savings. While the GCC has come late to industrialization and economic diversification, it has the potential to become a true global leader on welfare reform.

The Way Forward

In practice, the best policy mix for the GCC is likely to be a combination of different distributional tools, including both conditional and unconditional ones, though probably with a stronger focus on condi-tional benefits in higher deficit countries. This should not be rushed, however: before settling on a specific package, governments and thought leaders need to increase public awareness about the problems of the status quo and facilitate robust debate about new ideas of welfare reform. Reforming the social contract is a complex undertaking that requires buy-in from a wide range of stakeholders.

Governments willing to consider UBI will want to follow a rigorous approach in the process of design-ing the policy. This will involve first determining the optimal number of public sector employees under reasonable assumptions of institutional and individ-ual efficiency levels that can be achieved. It will then require the definition of a process by which the surplus will be migrated to a UBI scheme, privileging a gradual process (e.g. non-replacement of employees retiring, or nudging employees towards early retirement) with the right incentives. The most delicate step will be in setting the UBI level, in a way that is sufficient for a modest middle-class lifestyle yet still creates an incentive for private sector employment. This will also have to account for the varying socio-economic contexts of recipients, requiring the development of complementary payments for those that require it.