OECD
BETTER POLICIES FOR BETTER LIVES

# OECD Policy Note on the Venezuelan migration shock in Colombia and its fiscal implications

**In a nutshell….**

**The government is coping with a large increase in migration to Colombia.** The government has managed this challenging situation by providing timely border assistance, relaxing entry requirements, granting temporary permits and ensuring universal emergency care.

**Migration creates social and economic challenges, but also opportunities.** International experience shows that migration can be a source of growth and well-being in the medium-term. Realising these benefits requires putting in place appropriate integration policies.

**In the short term, the migration shock implies additional spending needs.** Recent experience in some OECD countries can offer some useful insights for Colombia on how to cope with the unexpected additional spending needs. Making use of unusual event clauses, several EU countries deviated temporarily from the previously agreed fiscal adjustment paths. Adopting a broader definition of the escape clause, as the EU did, could help Colombia to deal with the unexpected migration shock while maintaining its commitment to fiscal discipline.

**Colombia's strong commitment with the fiscal rule should be preserved.** Tasking the fiscal committee with evaluating every year how the migratory shock affects the fiscal reduction path would help to maintain transparency and credibility. Independent monitoring of the budgetary impact of the migration shock could also help ensure that decisions remain based on technical grounds and are insulated from other budgetary discussions.

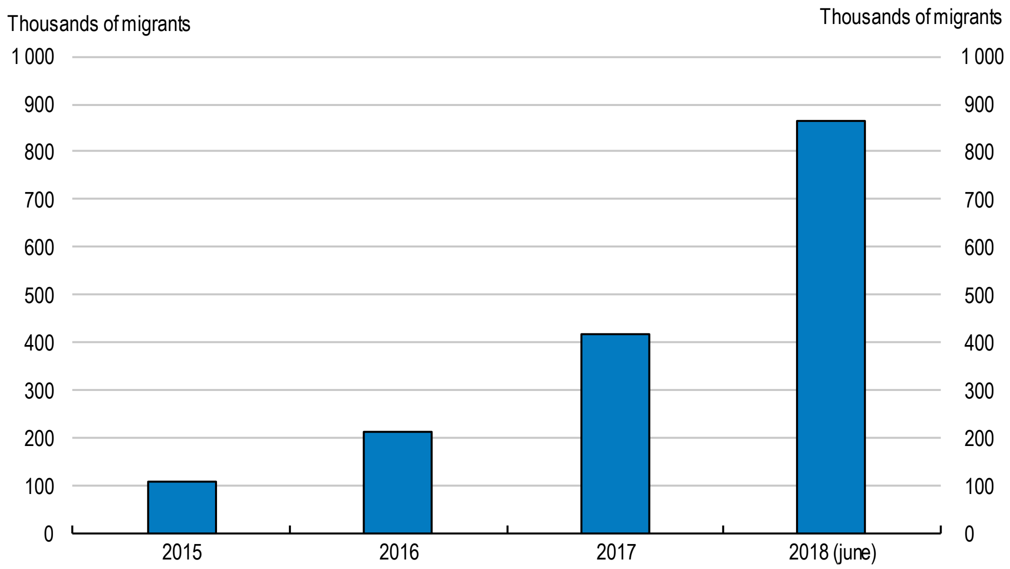
**Recent efforts by the government to improve the tax system and boost the spending efficiency are important to foster the fiscal situation.** Ongoing initiatives to implement the National Development Plan and improve budgetary processes and the targeting of social programmes would promote better the quality of public spending.

## Migration has increased substantially

**The large inflow of migrants from Venezuela represents a major social and economic challenge for Colombia.** The inflow has recently accelerated significantly. In 2018, the number of migrants doubled in just six months (Figure 1). At the end of 2018, there were more than 1.2 million Venezuelan immigrants with an intention to stay in Colombia.

Migration from Venezuela is expected to keep increasing, as international experience shows that, after the arrival of first migrants a process of families' reunification takes place. More than 70% of recent arrivals have left close relatives in Venezuela (Reina et al, 2018). The deepening of the economic crisis in Venezuela may therefore also imply greater migration towards Colombia in the future.

**Figure 1. The number of Venezuelan migrants has increased substantially**




*Source*: Colombian household surveys, GEIH.

Even though the majority of people who leave Venezuela do so for economic reasons, **the current inflow shows also some characteristics of a refugee crisis** (World Bank, 2018). This includes a sharp acceleration in arrivals (traditional economic migration tends to be slower) and a relatively high proportion of people arriving in difficult socio-economic conditions.

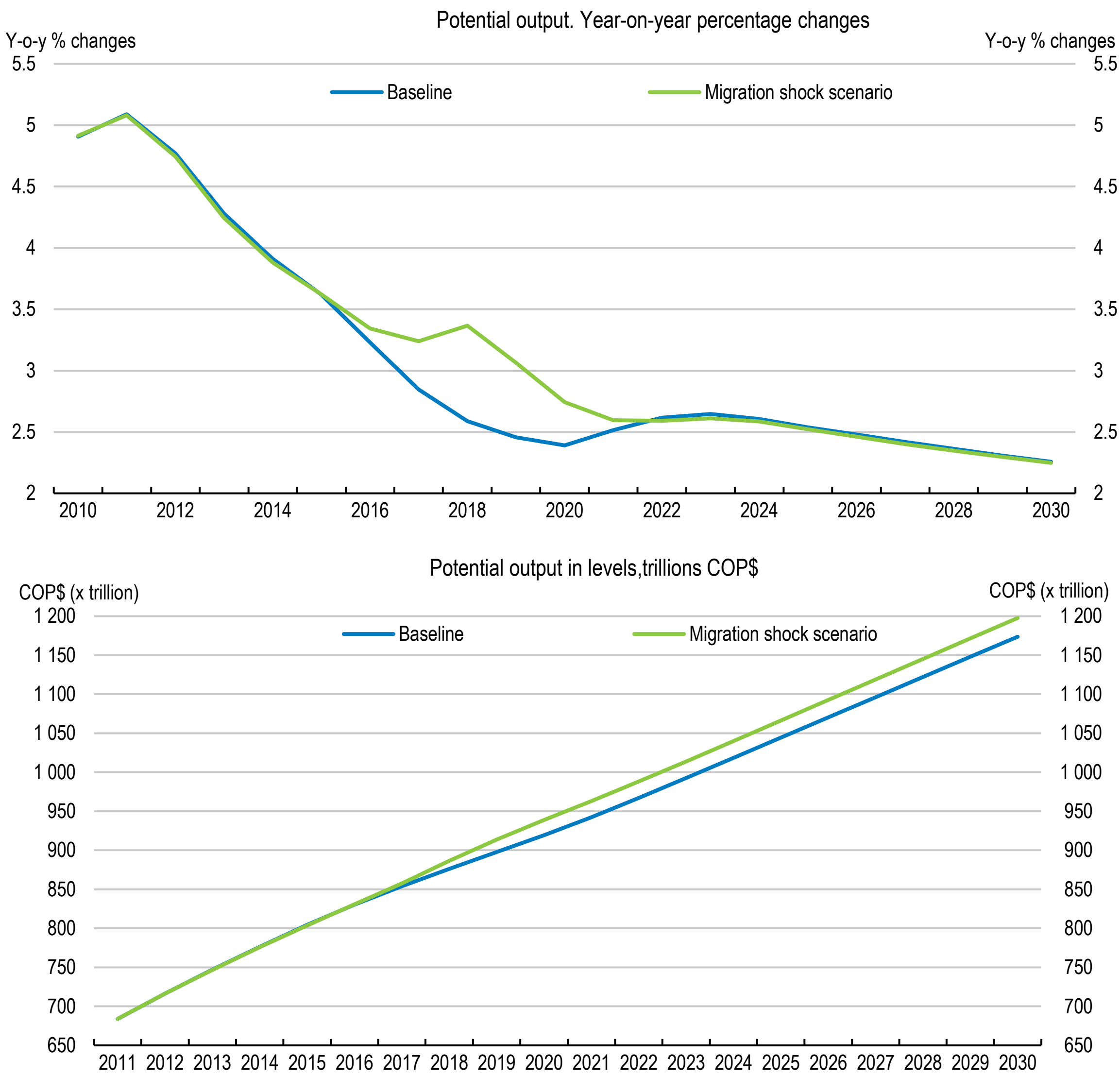
Both the unprecedented size of the migration flow and the speed of the increase imply substantial challenges for Colombia's central and local governments. There is significant variation in the local impact, with evidence of increases in unemployment and poverty among migrants in border areas, such as Cúcuta and Riohacha, and in Bogotá. Other large cities such as Barranquilla and Medellín are showing greater resilience to assimilate the migratory inflow.

**The government has managed this challenging situation**, making efforts to integrate the migrants by providing timely border assistance and ensuring universal emergency and childbirth care. Documentation requirements have been made more flexible so that school-age children can have access to education at the pre-school, basic and secondary levels. Colombia has also relaxed some entry requirements and granted temporary permits to stay in the country. An integral policy strategy for the next years has been initiated, including actions in areas such as education, healthcare, water and sanitation, labour market integration, childhood care and humanitarian help.

## Migration implies challenges and opportunities

Migration implies challenges but also opportunities. International experience in OECD and Latin American countries shows that **migration can be an important source of growth and well-being in the medium-term**. The increase in labour supply could help to boost the growth potential of the economy (Figure 2), which has experienced a decline in recent years (OECD, 2019).

**Figure 2. The impact of the migration shock on potential output: an illustrative simulation**




*Note:* The migration shock scenario assumes an increase in labour force supply by 750 thousands in 2018, 1 million in 2019 and 1,25 million in 2020. Productivity and capital formations remain exogenous.
*Source:* OECD calculations.

Migrants from Venezuela to Colombia have levels of education similar or higher to those of the receiving population, which should facilitate their integration in the labour market and could have a positive effect on productivity. Migrants from Venezuela are, on average, almost 5 years younger than Colombians (26 versus 31) (Reina et al. 2018), which will also help to mitigate the negative effects of aging on Colombian growth prospects.

Integrating migrants will require appropriate short-term integration policies, as the ones Colombia is now deploying. In the medium-term, a particular and fundamental challenge for Colombia will be to integrate migrants in the formal labour market. The Colombian labour market is still characterised by a high level of informality, negatively weighing on well-being and productivity. The integration of migrants to formal jobs would require a comprehensive strategy with actions ranging several policy areas such as education, taxes, pensions, business regulations and labour market policies (OECD, 2019).

## In the short-term, the migration shock implies additional spending needs

Realising the positive economic effect of migration in the medium-term requires putting in place in the short-term appropriate integration policies, as the ones Colombia is now deploying. Such policies entail a fiscal cost, which in the case of Colombia, is estimated to be around 0.4% of GDP per year (Table 1), according to different estimates from government, think tanks or the World Bank. This accounts for additional spending in areas such as health, education, social programmes, humanitarian aid, or housing. This additional spending is likely to be required for the next three or five years. In the medium-term, the higher output growth triggered by migration would imply higher fiscal revenues, offsetting gradually the initial negative fiscal impact.

**Table 1. Estimated short-term fiscal impact of the migration shock per year**

| | **Fiscal cost (as % of GDP)** |
|---|---|
| **Finance Ministry** | 0.4-0.6 |
| **Fedesarrollo** | 0.2-0.4 |
| **World Bank** | 0.3-0.4 |

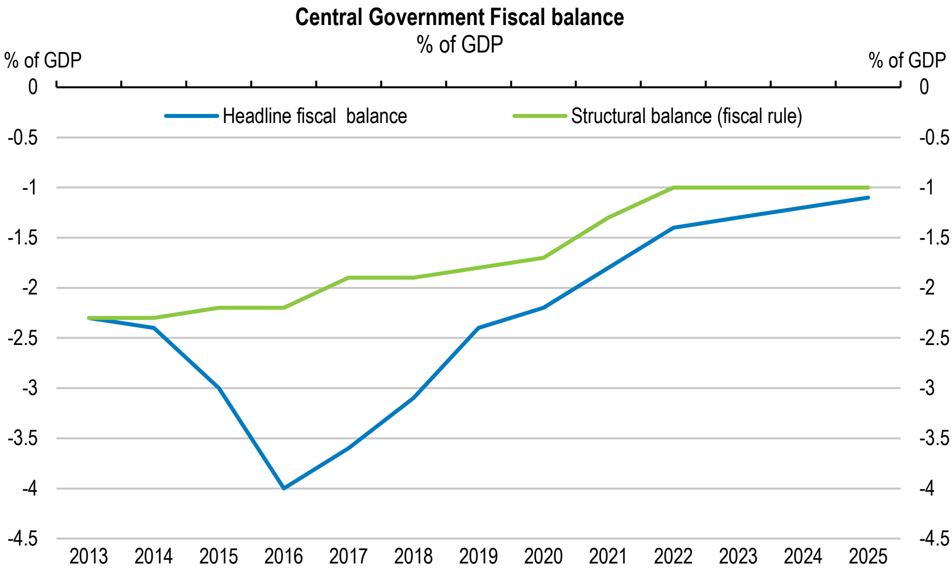
*Sources:* Finance Ministry; Reina at al. (2018); World Bank (2018).

## Incorporating the migration shock into the solid fiscal framework

An important policy question is how to accommodate the migration shock and the associated additional spending needs into Colombia's strong macroeconomic framework, which has underpinned the steady economic growth and social progress experienced by Colombia over the last decades (OECD, 2019).

Fiscal policy in Colombia is governed by a fiscal rule, which provides strong macroeconomic stability and fiscal discipline. The fiscal rule calls for the structural central government deficit to decline to 1% of GDP by 2022, implying that fiscal policy will be moderately contractionary over the next years (Figure 3). There is for the time being no predetermined adjustment or procedure in the fiscal rule framework to adjust for extraordinary shocks. The existing escape clause considers that the fiscal rule could be suspended if an extraordinary event puts at risk macroeconomic stability. The government has never made use of this provision. A council of independent experts (*Comité Consultivo de la Regla Fiscal*) is in charge of determining the central government fiscal path for the following 10 years, advising the government on technical issues and verifying the fulfilment of the fiscal rule every year.

**Figure 3. The planned fiscal consolidation path**




Source: Ministry of Finance. Medium-term fiscal plan. Figures for 2018-2025 are projections.

Recent experience in some OECD countries can offer some useful insights for Colombia on how to cope with unexpected additional spending while maintaining the fiscal deficit in a downward path. Several European Union countries faced a similar situation in 2015-2016, when an exceptional inflow of refugees implied unexpected additional spending needs. Making use of flexibility clauses in the EU fiscal framework to cope with unexpected events outside the control of governments, several EU countries were granted a delay in their fiscal reduction commitments, ranging from 0.1 to 0.3% of GDP (Box 1). To preserve fiscal discipline and transparency, the delay was temporary and its size equal to the estimated additional budgetary cost implied by the refugee crisis. Such arrangements helped EU countries to maintain their commitment to the agreed fiscal reduction paths, while addressing the additional spending needs without affecting other key parts of the budget, such as other social spending or investment needs. Switzerland used also similar provisions in their fiscal framework to accommodate unexpected migration-related spending in 2017. Spending to receive and integrate migrants has also increased significantly in Germany and Sweden (OECD, 2016; OECD, 2017). While the strong fiscal position in both countries allowed doing so without resorting to escape clauses, their experience also shows that, as a response to unexpected migratory shocks, fiscal policies tend to become more expansionary than planned before the shock hits.

**Box 1. The 'unusual event clause' in the EU fiscal framework**

In 2011, the EU fiscal framework incorporated a *'general escape clause'* to accommodate exceptional conditions. It allows for a temporary deviation from the previously agreed fiscal adjustment path, provided that this does not endanger fiscal sustainability in the medium term. This clause is applicable in two possible situations: i) a severe economic downturn affecting the euro area or the EU as a whole; ii) an unusual event outside the control of the country concerned which has a major impact on the financial position of the general government.

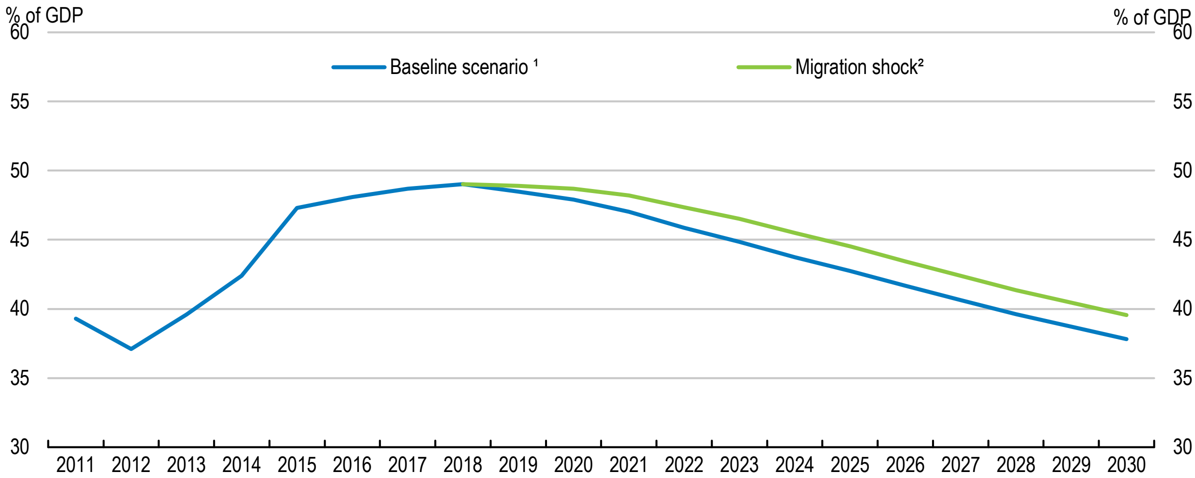
In view of the wide range of situations that could lead to the application of this clause, EU institutions are in charge of assessing each case individually to decide whether it qualifies.

Although the unusual event clause had initially been intended for events such as natural disasters, it was first activated in 2015 to accommodate the incremental spending resulting from the exceptional inflow of refugees in certain countries, as this was considered an unusual event outside the control of governments. The European Commission monitored the situation closely on the basis of observed data as provided by the affected countries to determine eligible amounts. Austria, Belgium, Finland, Hungary, Italy and Slovenia made use of the unusual event clause during the 2015-2017 period. Deviations in the fiscal adjustment paths ranged from 0.07% to 0.34 % of GDP depending on the country (EFB, 2017).

A similar arrangement could help Colombia deal with the migration shock while maintaining its commitment with fiscal discipline and the fiscal rule. Adopting a broader definition of the escape clause, as the EU did, would allow to adjust the agreed fiscal consolidation path for the estimated cost of the migration shock. Illustrative simulations suggest that medium-term debt sustainability would be preserved in that scenario (Figure 4).

**Figure 4. Public debt remains sustainable in a migration shock scenario**

Central government gross debt (% GDP)




*Note:* 1) Baseline long-term assumptions: Real long-term growth of 2.9%, long-term interest rate on government bonds of 5.6%, GDP deflator growth of 3%, primary balance of 0.3% of GDP in 2020 and 0.8% in 2030, oil price brent of 68 USD in the long-term; 2) Same assumptions as in 1, but primary balance receives a negative shock of 0.4 ppts during 3 years (2019-21) and is reduced by 0.1 ppts each year thereafter, until disappearing in 2025. Beyond 2025 positive effects of migration on growth are expected to increase revenues and improve debt dynamics. They are not incorporated into this scenario due to difficulties to estimate them.

*Source:* OECD calculations.

## Colombia's strong commitment with fiscal discipline should be maintained

Since its establishment in 2012, Colombia has always adhered to the fiscal targets embedded in the fiscal rule, granting **the authorities with a solid reputation for honouring their fiscal commitments.** This has boosted international confidence and has been fundamental to safeguard Colombia from episodes of international financial instability, as attested last autumn, when Colombia was one of the economies least affected by the bout in financial turbulence affecting other emerging economies.

**Colombia's strong commitment with the fiscal reduction trajectory embedded in the fiscal rule should, therefore, be preserved.** Providing independent monitoring and detailed technical analysis on the budgetary impact of the migration shock, either by the existing fiscal committee or by another body, would help to ensure that any decision on the fiscal path remains exclusively based on technical grounds and insulated from other budgetary discussions. Tasking the fiscal committee with evaluating every year how the migratory shock affects the fiscal reduction path would also help to maintain transparency and credibility.

**Recent efforts by the government to improve the tax system and boost the quality of public spending are also important to foster the fiscal situation.** The recent approved reform *"Ley de Financiamiento"* should provide further fiscal revenues for the upcoming years. Furthermore, on-going initiatives to implement the National Development Plan, such as improving budgetary processes and coordination, would help to increase the effectiveness and efficiency of public spending (OECD, 2019). Ongoing efforts to improve the targeting of social programmes, such as energy subsidies, are also warranted. Both initiatives are in line with recommendations made by the expert commission on spending (Bernal et al. 2017).

## References

Bernal, R., J. González, J. Henao, R. Junguito, M. Meléndez, A. Montenegro, J. Ramírez, J. Uribe and L. Villar (2017), Informe final de la Comisión del Gasto y La Inversión Pública. Fedesarrollo.

OECD (2019). OECD Economic Survey of Colombia 2019. Forthcoming. Paris: OECD.

OECD (2017). OECD Economic Survey of Sweden. Paris: OECD.

OECD (2016). OECD Economic Survey of Germany. Paris: OECD.

Reina, M, C. Mesa and T. Rámirez (2018). Elementos para una política pública frente a la crisis de Venezuela. Cuadernos Fedesarrollo 69. Noviembre 2018.

World Bank (2018). Migración desde Venezuela a Colombia. Impactos y estrategia de respuesta en el corto y mediano plazo.