Luxembourg

The recovery after the COVID-19 crisis requires a prompt labour market rebound and addressing skill shortages that weighed on firm growth and innovation prior to the crisis. Sustainable public infrastructure investment can improve environmental outcomes. Improving housing affordability and labour market participation of women will render the recovery more inclusive.

Performance prior to the COVID-19 crisis

**Economy**
- GDP per capita is 56% higher than OECD best performers.
- Productivity is 47% higher than OECD best performers.
- Employment rate is low but was increasing before the 2020 crisis.

**Inequality**
- Inequality is higher than in most advanced economies.
- The poorest 20% of households earn 7.6% of total income.

**Environment**
- Two-thirds of the population is exposed to harmful levels of air pollution.
- GHG emissions are high but have decreased in recent years.

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Economy: Percentage gap with respect to the population-weighted average of the highest 18 OECD countries in terms of GDP per capita (in constant 2015 PPPs). In the case of Luxembourg, the population is augmented by the number of cross-border workers in order to take into account their contribution to GDP.

Inequality: The Gini coefficient for disposable income measures the extent to which the distribution of disposable income among households deviates from perfect equal distribution. A value of zero represents perfect equality and a value of 100 extreme inequality.

Environment: Greenhouse gas (GHG) emissions include emissions or removals from land-use, land-use change and forestry (LULUCF). A high exposure to air pollution refers to above 10 μg/m³ of PM2.5.


StatLink https://stat.link/7b2xor
Easing skills constraints and improving equity outcomes

Despite healthy job creation prior to the COVID-19 crisis, structural unemployment remained high and firms often faced skill shortages. To favour a stronger recovery, both of these issues need to be addressed by improving the education system and enhancing educational outcomes. Grade repetition in both primary and secondary schooling should be reduced, as it contributes to a high age-grade discrepancy in the educational system (Panel A). Quality and accessibility of vocational training should be improved by, for instance, better linking students with the corporate sector, strengthening co-operation between enterprises and research institutions in Luxembourg and abroad, as well as the establishing of circular study programmes, that would allow students to return to Luxembourg after studying abroad.

Luxembourg has the lowest effective retirement age and the second highest replacement rate in the EU, providing older workers with weak incentives to continue in the labour market. Moreover, the participation rate of women lags behind that of men. There is scope to facilitate labour market participation of older workers and women. A pension reform should entail abolishing early retirement schemes, allow a gradual rise of the effective retirement age, limit pension credits for time spent outside work, and insure more actuarial neutrality around the statutory retirement age and indexation of the latter to longevity. To boost female labour force participation it is important to charge health care contributions for each spouse individually, while introducing a fully separate income tax assessment of spouses should also be considered.

Housing prices have grown strongly over the past decade (Panel B), weighing on housing affordability, in particular for low-income households who do not profit from highly subsidised social housing. To improve housing affordability and make the housing market more inclusive, a mix of policies is needed: supply side restrictions should be eased, to tackle land hoarding and resistance to densification; the mortgage interest deductibility phased out or reduced; and fiscal support to social housing should be better targeted.

Vulnerabilities and areas for reform

Source: Panel A: OECD, PISA Database; Panel B: OECD, Analytical House Price Indicators Database.

StatLink 2 https://stat.link/dlgh1u
Cross-border workers already fill a large part of the skill gap in the economy, but commuting poses a burden on the environment and climate. To facilitate connectivity while improving environmental outcomes infrastructure investment should increase. This requires a boost in public investment in cross-border railway connections, more sustainable transport infrastructure and construction. A reduction in traffic congestion and air pollution could be achieved by exploring a system of congestion charges. Investment in smart electricity grids and better interconnectivity in electricity and gas markets can increase efficiency in energy production.

Restrictive regulations in professional services hamper productivity in those sectors but also in downstream production. Moreover, in services, less productive firms have tended to fall further behind, which weighs on aggregate productivity. Lifting anti-competitive product market regulations would contribute to stronger market selection and post-entry growth of efficient firms in the professional services sector and may aid in the recovery from the pandemic. Regulation of professions, especially for civil engineers, should be relaxed, while restrictions on advertising and marketing for architects and engineers should be eliminated. Reforms to bankruptcy law, easing early restructuring and second chance opportunities can facilitate the post-COVID reallocation of resources.

Luxembourg: Summary of Going for Growth priorities and recommendations

<table>
<thead>
<tr>
<th>2019-2020 Reforms</th>
<th>Recommendations</th>
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<tr>
<td><strong>Education and skills: Improve the education system to enhance skill matching in labour markets</strong></td>
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<tr>
<td>☑ In 2019 the government began to develop a new national strategy for attracting, developing and retaining talent. Various measures have been taken concerning the regulatory framework governing immigration procedures, communication campaigns and participation in specialised recruitment fairs.</td>
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<td>☑ The personalised process for job seekers has been rolled out.</td>
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<td>☑ In early 2020, the Ministry of Education presented an initiative to step up digital education from primary school to secondary technical and general education.</td>
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<td>☑ A revision of the law on the organisation of higher education aims at optimising the governance of the programmes leading to the professionally oriented higher education qualification “Brevet de technicien supérieur” (BTS) and at reviewing the accreditation and monitoring procedures for BTS programmes as well as for foreign higher education institutions and programmes in Luxembourg. At the beginning of the 2019-2020 academic year, eight courses offered by three private higher education institutions were accredited.</td>
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<tr>
<td>☑ Reduce grade repetition in secondary education, provide more school autonomy and better monitor education quality.</td>
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<td>☑ Improve the quality and accessibility of vocational training. Enhance the apprenticeship system to reduce structural unemployment and address skill mismatches.</td>
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<tr>
<td>☑ Strengthen the co-operation between enterprises and research institutions in Luxembourg and abroad.</td>
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<td><strong>Labour market: Facilitate labour market participation of women and older workers</strong></td>
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<td>☑ The voluntary supplementary pension has been extended to self-employed workers in 2019.</td>
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<tr>
<td>☑ The fiscal and social frameworks have been amended to ensure an equal treatment for both wage earners and self-employed workers.</td>
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<tr>
<td>☑ Improve the long-run sustainability of the pension system by increasing contributions, reducing replacement rates, and increasing the retirement age.</td>
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<td>☑ Charge health care contributions for each spouse individually.</td>
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2019-2020 Reforms

**Housing: Improve the functioning of the housing market**

- The government started to acquire land slated for housing in 2019. Consequently, the Ministry of Housing has set up a unit responsible for evaluating land with a view to a possible acquisition made up of representatives of the Ministry of Housing and the Ministry of Finance.
- The adoption of the *Pacte Logement 2.0* aimed at enhancing the supply of affordable housing.
- A proposal for another draft law (No. 7495), voted on 21 March 2020 in parliament, foresees the creation of a special fund to help finance the construction of dwellings, as well as the buying of land by the state. Another major planned change concerns the general law regulating housing subsidies that will be completely revised.

**Environmental policy: Increase infrastructure investment to improve environmental outcomes**

- The government and network managers monitored the installation of 800 public charging stations for electric cars as well as for chargeable hybrid electric cars.
- Tax deductions for electric vehicles were replaced on 1 January 2019 by direct and higher financial assistance.
- Luxembourg will implement a levy of €20 per tonne of carbon from 2021, as part of its efforts to slash greenhouse gas emissions by 55% by the end of the next decade.

**Competition and regulation: Increase competition in the non-financial services sector**

- Reforms facilitating the recognition of professional qualifications and eliminating fixed prices in public contracts for architects and engineers have been implemented.
- A bill reforming the right of establishment has been presented with the aim of de-regulating professions to promote and facilitate access to professions.

**Recent progress on structural reforms**

Reform progress has been good in some areas, such as the ones concerning the improvement of environmental outcomes and the green transition. Efforts have also been made to improve access to housing and in reforming the education system to improve students’ employment outcomes.