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# Economics of Immigration, Pensions and Insider Trading

The 70th Economic Policy Panel Meeting, hosted by the Bank of Finland in Helsinki on 10-11 October 2019, included papers on insider trading ahead of the financial crisis, pension reform in OECD countries and UK immigration from Eastern Europe. The three papers are summarised in this issue of *Economic Policy Digest*.

## TOP BANK EXECUTIVES WELL AWARE OF RISKS THEY WERE TAKING BEFORE THE CRISIS:

**New evidence of insider trading**

*[read]*

Top executives of US banks that experienced huge losses in the financial crisis of 2007-2008 were selling their own shares well before the crisis hit, according to new research by *Ozlem Akin, José Marin* and *José-Luis Peydró*.

What's more, the evidence of pre-crisis insider trading by senior figures who seem to have understood the high risks that their banks were taking is stronger for banks with higher real estate exposure.

The study finds that 'top-five' executives – CEO, CFO, Chairman, COO and President – were unloading part of their portfolios before the very first sign of the crisis, which was the first drop in house prices in 2006. For independent directors and other officers, there is no evidence of any unusual selling activity ahead of the crisis.

The authors conclude that regulating trading by bank insiders may be beneficial. A ban may result in lower excessive risk-taking by banks and operate as a partial substitute for bank capital regulation or macroprudential policies.

## PENSION REFORM IN OECD COUNTRIES:

**New measures are driven by the business cycle rather than demographic pressures**

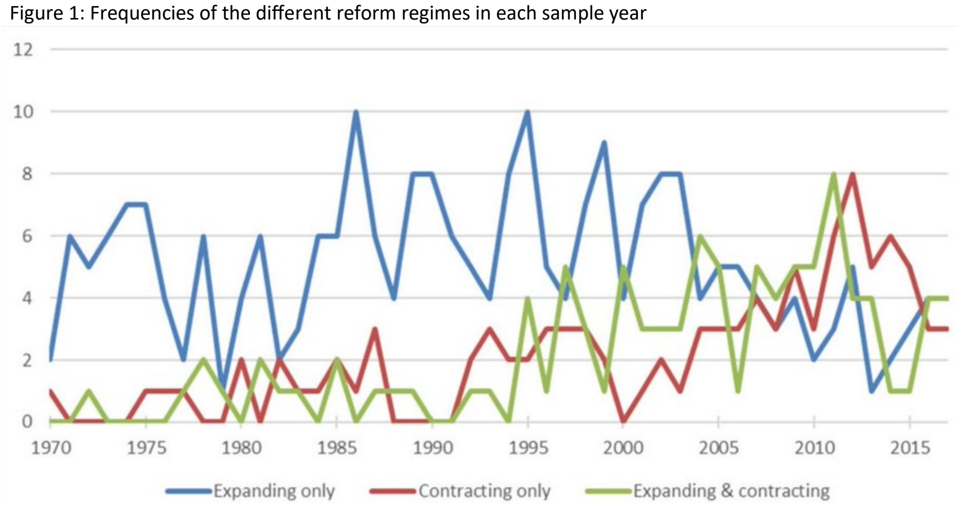
*[read]*

Reforms to public pension systems in OECD countries are driven less by the long-term pressures of an ageing population than by the short-term state of the economy. That is the central conclusion of new research by *Roel Beetsma, Franc Klaassen, Ward Romp* and *Ron van Maurik*.

Focusing on pension reform data for over 20 OECD countries since 1970, Figure 1 illustrates by year the number of countries that expanded their public pension system, contracted their system or combined contracting and expanding reform measures in the same year. Reform measures are identified by the year in which they are legalised.

Some general trends are visible. Expansionary pension reform activity dominated the scene up to the start of

Figure 1: Frequencies of the different reform regimes in each sample year



this century and has been declining since then, while contractionary reform activity has become increasingly prominent since the 1990s. These broad developments should not be surprising, as demographic projections show that old-age dependency ratios in the OECD will continue to increase, increasingly putting public budgets under pressure.

But these general trends do not explain the specific timing of the pension reform measures. Indeed, there is substantial fluctuation in reform intensity around these trends.

The new study demonstrates that the state of the business cycle is the most important trigger for pension reform – and the effects are considerable. For example, a one percentage point lower rate of economic growth makes expansionary reform about 10% less likely and contractionary reform 13% more likely. The effect of a one percentage point higher rate of unemployment makes contractionary reform 14% more likely.

What policy conclusions can be drawn from these findings? A priori, one would expect contractionary reform measures to be driven purely by increases in projected old-age dependency ratios.

But the fact that these measures tend to be concentrated during downturns – and potentially even strengthen downturns by undermining consumer confidence of those who are negatively affected by the measures – suggests that breaking the link between the state of the business cycle and the adoption of pension reform measures may yield economic benefits.

An example would be to introduce an automatic link between life expectancy projections and adjustment of the retirement age, as the Netherlands did in 2012.

## WELFARE RESTRICTIONS AND THE LABOUR SUPPLY OF EU IMMIGRANTS:

**UK evidence from the Eastern enlargment**

[read]

Widening access to benefits for immigrants from Eastern Europe, as happened in the UK in 2011, did not make more people from those countries move to the host country – nor did it induce an increase in the share of welfare-dependent individuals in the total immigrant population. But there was an increase in benefit claims and a reduction in working among sub-groups of the immigrant population who are more exposed to risks in the labour market – women and the less educated, especially if they had children.

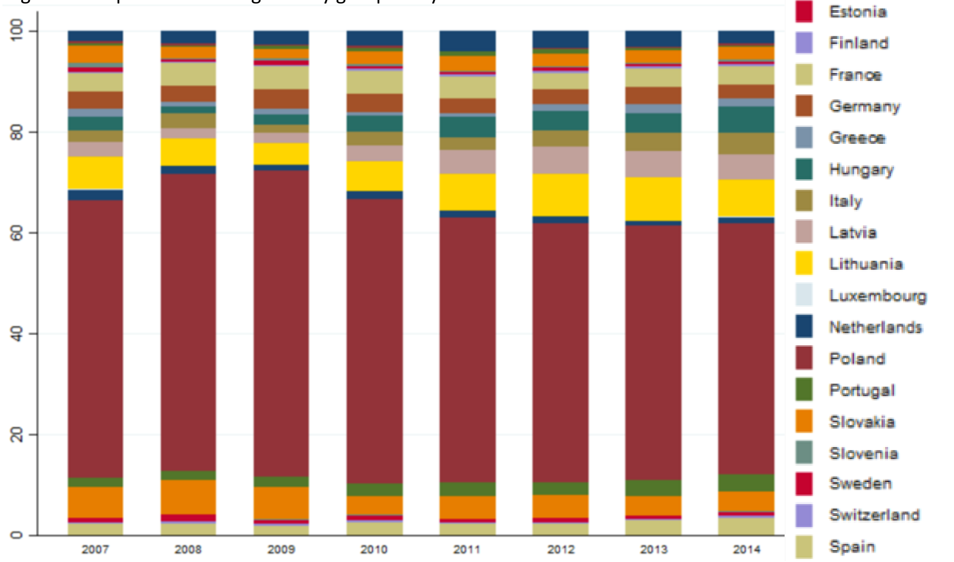
These are among the findings of a new study by *Ludovica Giua*, which analyses the effects of temporary restrictions on benefit access for immigrants in the context of the 2004 enlargement of the EU to take in the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia (the accession or A8 countries).

Enlargement increased the EU population by almost 75 million people overnight, opening the labour market to millions of potential workers. The incumbent member states (the EU15) temporarily restricted access to workers from the A8, usually through the need for a work permit. The UK, Ireland and Sweden were the only exceptions: they gave immigrants from the A8 full access to their labour markets, although the UK imposed some additional conditions for welfare purposes up to April 2011.

The restrictions devised by the UK in 2004 granted A8 immigrants the right to claim out-of-work benefits (namely, unemployment, family and child or housing benefits and tax credits) on the same grounds as other EU citizens only if they had been continuously employed for at least 12 months and registered with the UK Border Agency's Worker Registration Scheme. In May 2011, those temporary restrictions expired.

The setting provided by the design of these transitional limitations makes it possible to isolate the effects of granting immigrants access to the welfare system in the host country. This is done by comparing the likelihood of claiming out-of-work benefits and the labour outcomes of A8 immigrants with that of their EU15 counterparts before and after the change in policy. The share of UK immigrants from the EU15 and A8 countries are shown in Figure 2.

Figure 2: Proportion of immigrants by group and year




The three papers featured in this digest are forthcoming. For more information on *Economic Policy*, visit www.Economic-Policy.org