

Definition and measurement

No commonly agreed measure of poverty across OECD countries currently exists. The approach followed here is based on the concept of household disposable income (i.e. income net of taxes and social security contributions paid by individuals). Individuals are classified as “poor” when their household income is less than half the median level prevailing in each country. The use of a “relative” income-threshold to measure poverty implies that poverty will increase in a country where the real income of those at the bottom of the income ladder rises by less than the median, while it will fall in a country where the real income of poor households declines by less than the median. While this may seem counter-intuitive, it does capture the notion that avoiding poverty requires access to the goods and services that are regarded as “customary” or necessary to participate fully in any given society. The measures used here capture the extent of poverty at a particular point in time. The length of the periods of insufficient income, as well as household assets and access to other services and resources, are all aspects that should ideally be considered to evaluate the extent of poverty in any society.

Larger households need more resources than smaller ones, but also realise economies of scale in consumption. Because of these considerations, household incomes of individuals are “standardized” to account for differences in household size. The “equivalence scale” used here is the square root of household size. The data on poverty and income distribution used are provided to the OECD by national consultants, and the most recent observations refer to a year around 2000. They are based on common methodologies and definitions applied to national micro data sets (most commonly, household surveys). While this approach improves cross-country comparability, many differences remain. These include a mix of survey and administrative data, differences in the periods over which income is assessed, variation in treatment of missing and extreme values and exclusion of the impact of non-cash benefits, services (such as health care) and indirect taxes.

Relative poverty has several dimensions. A first one relates to its prevalence, i.e. how many individuals in any given country fall below the poverty line (the “poverty rate”). A second is its depth, i.e. by how much the income of the poor falls below the poverty line (the “poverty gap”). Both measures are affected by features of the surveys: in particular, the poverty gap gives greater weight to the lowest reported incomes. Information on both dimensions is provided in Chart EQ1.1, which ranks countries in decreasing order of poverty (the product of poverty rate and poverty gaps) in 2000.

On average, across the 25 countries shown, a little over 10% of the population had poor incomes in the year 2000, around half a point higher than in the mid-1990s. The average poverty gap, at around 28%, is little changed from the mid-1990s.

There is much diversity, however, in country experiences. Poverty rates range from 15% or more in the United States, Mexico, Japan, Turkey and Ireland, to 5% or less in Denmark and the Czech Republic. They increased over the second half of the 1990s in a majority of countries, while they fell in Mexico, Portugal, Switzerland, Norway and Italy. Poverty gaps are largest in many of the countries with high poverty rates (e.g. the United States, Japan and Italy), where they exceed one third. However, poverty gaps (at 30%

or more) are also high in some of the countries characterised by low poverty rates, such as Switzerland, Germany, Austria and Poland.

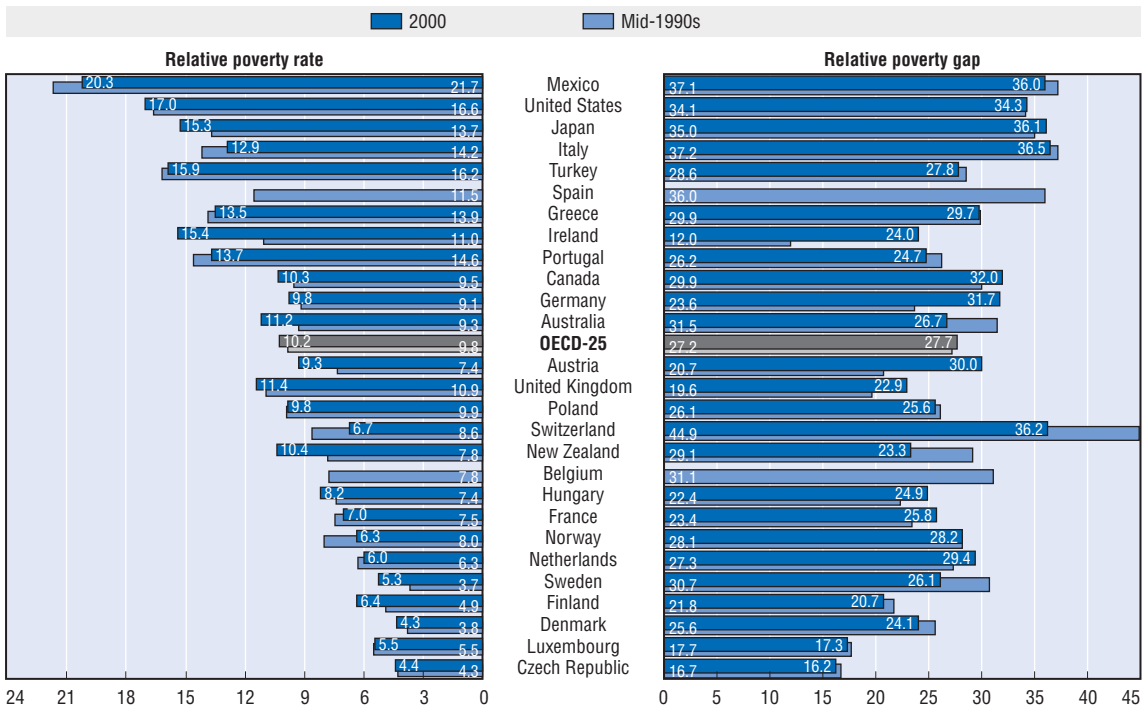
Risks of poverty vary significantly according to the age of individuals and to features of the tax and benefit systems of member countries. Information on both aspects is provided in Chart EQ1.2, which plots information in two points in time for an unweighted average of OECD countries. Poverty rates after taking account the impact of taxes and transfers are highest for children and the elderly: among persons 76 and over, in particular, the risk of poverty is more than twice that of prime aged persons (41-50 years). Taxes and transfers reduce poverty rates among all age groups, but especially among the elderly. Market-income poverty (i.e. before taxes and transfers) was broadly stable on average since the mid-1990s – a significant departure from the previous steady growth.

Status indicators: Jobless households (SS3), Youth inactivity (SS9), Income inequality (EQ2), Income of older people (EQ4).

Response indicators: Public social spending (EQ5), Old-age pension replacement rate (EQ8), Pension promise (EQ9).

EQ1.1. No uniform decline in poverty rates and poverty gaps since the mid-1990s

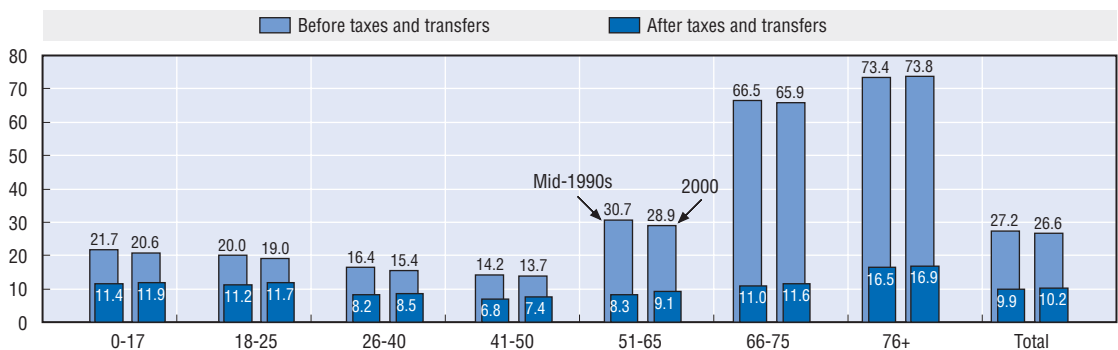
Percentages, mid-1990s and 2000



Note: Poverty rates are measured as the proportion of individuals with equivalised disposable income less than 50% of the median income of the entire population. Poverty gaps are measured as the percentage difference between the average income of the poor and the 50% of median income poverty threshold. Countries are ranked by decreasing order of poverty rate times poverty gap. "2000" data refer to the year 2000 in all countries except 1999 for Australia, Austria and Greece; 2001 for Germany, Luxembourg, New Zealand and Switzerland; and 2002 for the Czech Republic, Mexico and Turkey. "Mid-1990s" data refer to the year 1995 in all countries except 1993 for Austria; 1994 for Australia, Denmark, France, Germany, Greece, Japan, Mexico and Turkey; and 1996 for the Czech Republic and New Zealand.

EQ1.2. The young and the old are most exposed to the risks of poverty

OECD average poverty rates by age group, before and after taxes and transfers, percentages, mid-1990s and 2000



Note: Poverty rates are unweighted averages of 21 OECD countries.

Source: Förster, M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris (www.oecd.org/els/workingpapers).

StatLink: <http://Dx.doi.org/10.1787/610223184802>

Further reading: ■ Förster, M. (2000), "Trends and Driving Factors in Income Distribution and Poverty in the OECD Area", Labour Market and Social Policy Occasional Papers, No. 42, OECD, Paris. ■ Förster, M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris.

Definition and measurement

Income inequality is here assessed in terms of the distribution of household disposable income (*i.e.* income after deduction of direct taxes and social security contributions paid by households) of each individual. As in the case of indicator EQ1, household income is adjusted to take account of household size by assuming an equivalence scale elasticity of 0.5. The summary measure of income distribution used is the Gini coefficient. The Gini coefficient is defined as the area between the Lorenz curve (which plots cumulative shares of the population, from the poorest to the richest, against the cumulative share of income that they receive) and the 45 line, taken as a ratio of the whole triangle. Its values range between 0 in the case of “perfect equality” (each share of the population gets the same share of income) and 100 in the case of “perfect inequality” (all income goes to the share of the population with the highest income). As for indicator EQ1, data were provided by national experts using common definitions.

There is considerable variation in levels of income inequality across OECD countries. The Gini coefficient of income inequality is lowest in Denmark and Sweden, and highest in Mexico and Turkey – the OECD countries with lower per capita income (Chart EQ2.1). On average, across the 20 countries for which data are available since the mid-1980s, the Gini coefficient of income inequality increased marginally over the second half of the 1990s, as compared to a more significant increase over the previous decade. This average hides some different trends: there were continued declines in inequality in Turkey and Mexico. Among other OECD countries, the Gini coefficient increased in a majority of cases (notably in Finland and Sweden, but also Japan, Denmark and Canada).

The distribution of household disposable income depends on both the distribution of market income (earnings, self-employment and capital income) and on how governments redistribute market income through their tax and transfer policies. Because of the dominant role of public pensions within the income of the elderly population, and of cross-country differences in the age structure of OECD population, the role of taxes and transfers, on one side, and of market-income, on the other, can both be better assessed when focusing on the working-age population.

The distribution of market income among the population of working age tends to be relatively uneven, with 10% being received by persons in the

bottom three deciles of the distribution (Table EQ2.2). The distribution of taxes mirrors that of market income. The share of taxes paid by the middle income group does not vary much across countries – around an average value of 32% – with the exception of France and Portugal where a higher than usual proportion of state revenue comes in the form of social security contributions from employers.

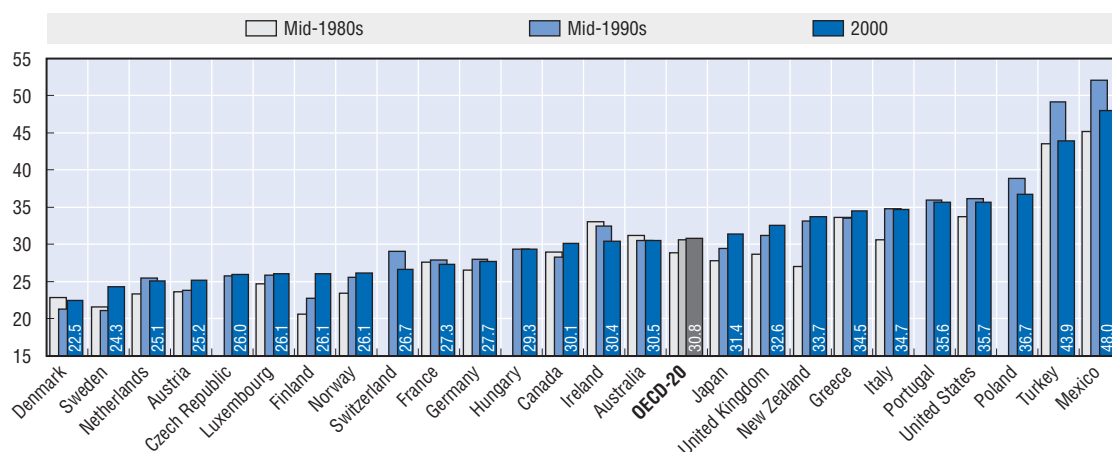
There is greater diversity in the distribution of government transfers among income groups. In Australia, New Zealand and the United Kingdom an above-average share of government transfers goes to low-income households, and a below-average share goes to high-income groups. In these countries, the payment of cash benefits is more often related to income and earnings than in Continental Europe. Norway, Australia, Denmark and the United Kingdom stand out as countries where the share of public transfers going to the bottom three income deciles is highest, and Italy and Japan as those where it is lowest.

Status indicators: Employment (SS1), Relative poverty (EQ1).

Response indicators: Out-of-work benefits (SS5), Benefits of last resort (SS6), Public social spending (EQ5), Total social spending (EQ7).

EQ2.1. Income inequality varies across OECD

Gini coefficient of inequality in the distribution of equalised household disposable income



Note: Countries are ranked in increasing order of the Gini coefficient in 2000. "2000" data refer to the year 2000 in all countries except 1999 for Australia, Austria and Greece; 2001 for Germany, Luxembourg, New Zealand and Switzerland; and 2002 for the Czech Republic, Mexico and Turkey. "Mid-1990s" data refer to the year 1995 in all countries except 1993 for Austria; 1994 for Australia, Denmark, France, Germany, Greece, Ireland, Japan, Mexico and Turkey; and 1996 for the Czech Republic and New Zealand. "Mid-1980s" data refer to the year 1983 in Austria, Belgium, Denmark and Sweden; 1984 in Australia, France, Italy and Mexico; 1985 in Canada, Japan, the Netherlands, Spain and the United Kingdom; 1986 in Finland, Luxembourg, New Zealand and Norway; 1987 in Ireland and Turkey; 1988 in Greece; and 1989 in the United States. Data for Germany in the mid-1980s refer to western Länder only.

EQ2.2. Government benefits and taxes substantially reduce inequality in the distribution of market income

Share of market income, government transfers and taxes accruing to different deciles of the working age population, percentages

	Market income			General government transfers			Taxes		
	Three bottom deciles	Four middle deciles	Three top deciles	Three bottom deciles	Four middle deciles	Three top deciles	Three bottom deciles	Four middle deciles	Three top deciles
Australia, 1999	6.7	35.8	57.4	37.2	59.2	3.7	3.5	30.6	65.8
Canada, 2000	10.0	35.0	55.0	22.0	64.0	14.0	7.9	32.1	60.1
Czech Republic, 2002	10.6	33.6	55.9	31.8	54.9	13.3	7.9	31.0	61.1
Denmark, 2000	9.7	37.2	53.1	36.1	54.6	9.3	11.6	35.4	53.1
Finland, 2000	10.3	35.9	53.8	31.3	59.4	9.3	9.0	32.8	58.3
France, 2000	11.0	34.3	54.7	27.6	51.4	21.0	10.1	23.4	66.4
Germany, 2001	10.4	35.2	54.4	22.3	59.5	18.2	8.1	34.1	57.8
Hungary, 2000	9.0	32.2	58.8	27.0	50.2	22.8	16.0	35.7	48.3
Ireland, 2000	8.9	36.3	54.8	31.3	57.5	11.2	5.5	32.1	62.4
Italy, 2000	9.8	32.4	57.8	14.1	51.1	34.8	7.5	31.2	61.3
Japan, 2000	11.4	35.9	52.7	15.7	66.5	17.8	13.9	34.5	51.7
Netherlands, 2000	11.2	37.3	51.6	29.8	60.8	9.4	11.6	36.0	52.5
New Zealand, 2001	8.0	33.3	58.7	31.2	64.3	4.5	5.6	30.1	64.3
Norway, 2000	11.5	36.0	52.5	43.8	37.4	18.8	10.5	34.9	54.6
Portugal, 2000	10.9	30.9	58.2	17.1	47.7	35.2	8.5	25.0	66.5
Sweden, 2000	10.9	36.1	53.0	29.5	55.8	14.7	12.0	34.9	53.2
Switzerland, 2001	15.0	35.8	49.2	19.6	64.5	15.9	19.4	34.7	45.9
United Kingdom, 2000	7.7	34.1	58.3	34.7	59.2	6.2	6.0	30.9	63.2
United States, 2000	9.5	34.3	56.2	17.6	71.6	10.8	6.8	29.1	64.0
OECD-19	10.1	34.8	55.1	27.3	57.3	15.3	9.5	32.0	58.4

Source: Förster, M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris (www.oecd.org/els/workingpapers).

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Definition and measurement

Children are defined as those aged less than 18, and they are counted as “poor” when they live in households where disposable income is less than half of the median of a given country. In all countries children are counted as members of the household where they live, sharing the income streams earned by adults. Household income includes earnings, transfers and income from capital, and is measured net of direct taxes and social security contributions paid by households.

Income for the entire household is adjusted for household size using an equivalence scale elasticity of 0.5. More than for other age groups, measures of poverty among children are particularly sensitive to the use of different values of the equivalence scale elasticity. As for indicator EQ1 and EQ2, data were provided by national experts using common definitions.

Poverty among children is a special concern of all OECD governments and communities. Children cannot be held responsible for their situation in life, and the experience of poverty during childhood may adversely affect their cognitive and social development. On average, across 24 OECD countries covered in Chart EQ3.1, around 12% of all children fell below the poverty threshold in 2000, an increase of 0.75 points relative to the level recorded in the mid-1990s.

Child poverty rates are especially low in the Nordic countries, where fewer than 4% of all children are poor. Slightly higher rates are found in France, Switzerland and the Czech Republic, with rates of around 7%. Child poverty is highest in Mexico, the United States and Turkey, where it exceeds 20%, but also in New Zealand, the United Kingdom, Ireland, Italy and Portugal. Austria and New Zealand experienced significant increases in child poverty over the second half of the 1990s, while Switzerland and Italy recorded large declines.

Poverty rates among children are generally higher than for the entire population, with the exception of the Nordic countries as well as Greece, France and Switzerland. While countries with higher poverty rates for the entire population also display higher poverty among children, the difference between the two is especially large in New Zealand, the United States and the United Kingdom, suggesting that specific factors in these countries increase risks of poverty among children.

While several factors contribute to child poverty, two of the most important relate to whether children live with a single parent and whether parents are

working or not. In all countries covered in Table EQ3.2, persons living in single parent households have a probability of falling below the poverty line that is more than three times that of couples with children. Even when single parents work, their poverty rates is one-third higher than that of couples with children and one parent at work.

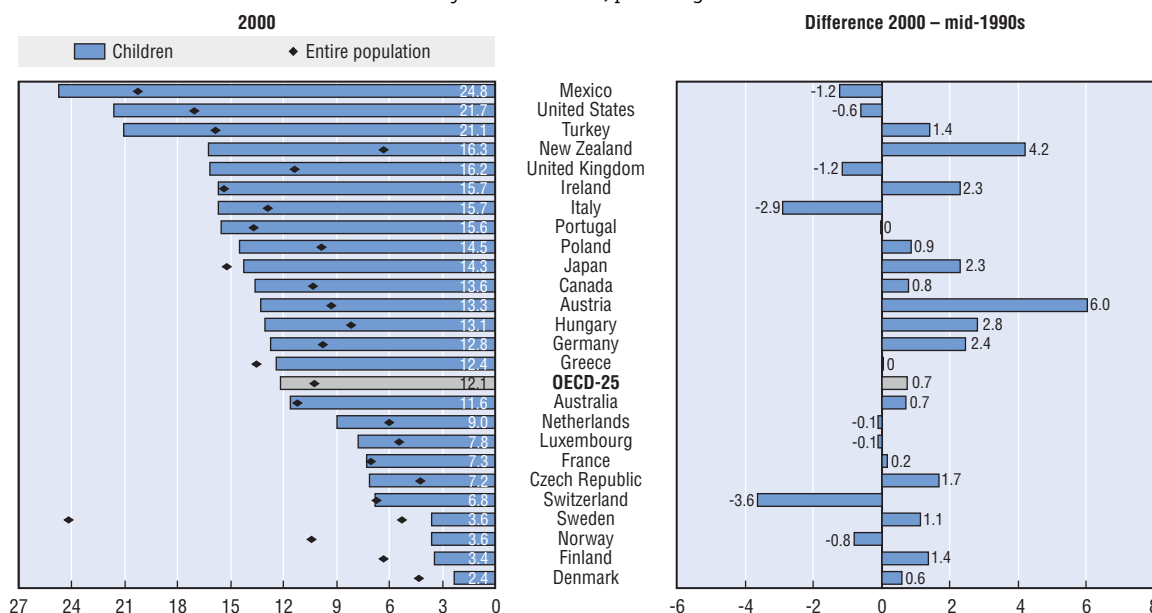
Having a job reduces the probability of households with children falling into poverty (by around three-quarters in the case of couples with children where both parents work, relative to those where only one parent does). This suggests that employment of parents is an important determinant of child poverty, but it is not the only factor. Between one-fourth and one-third of persons living in one-worker couples with children are poor in Mexico, Portugal and the United States, while in Japan, Mexico and Turkey, more than one-tenth of individuals in two-worker couples with children are poor. Also, poverty rates among households with children where no adult works vary enormously across countries (from less than 25% in Denmark, Finland and Norway, to 75% or more in Ireland, Italy, New Zealand, Portugal and the United States), suggesting that both access to, and the level of, income support for families with children also matter.

Status indicators: Working mothers (SS4), Subjective well-being (CO1), Teenage births (CO4).

Response indicators: Public social spending (EQ5), Benefits of last resort (SS6).

EQ3.1. Child poverty rates are substantially lower in the Nordic countries

Share of children 17 years and under living in households with equivalised disposable income less than 50% of median income, percentages



Note: Countries are ranked by decreasing order of the child poverty rate in 2000. "2000" data refer to the year 2000 in all countries except 1999 for Australia, Austria and Greece; 2001 for Germany, Luxembourg, New Zealand and Switzerland; and 2002 for the Czech Republic, Mexico and Turkey. "Mid-1990s" data refer to the year 1995 in all countries except 1993 for Austria; 1994 for Australia, Denmark, France, Germany, Greece, Ireland, Japan, Mexico and Turkey; and 1996 for the Czech Republic and New Zealand.

EQ3.2. Poverty rates are much higher for families with jobless parents

Poverty rates among children and households with children, by work status of adults, percentages

	Children	Families with children						
		Single parent			Two parents			
		Total	Not working	Working	Total	No worker	One worker	Two workers
Australia, 1999	11.6	38.4	58.7	11.7	6.8	43.3	5.4	3.3
Austria, 1999	13.3	30.0	67.6	23.2	10.2	35.6	12.7	8.6
Canada, 2000	13.6	42.1	89.7	27.7	8.5	75.3	22.9	3.5
Czech Republic, 2000	7.2	23.2	53.7	5.5	3.5	35.7	3.7	0.6
Denmark, 2000	2.4	7.2	22.2	4.0	1.9	19.0	6.4	0.7
Finland, 2000	3.4	10.5	25.0	7.2	2.5	25.8	5.4	1.3
France, 2000	7.3	26.6	61.7	9.6	5.1	37.9	6.3	1.6
Germany, 2001	12.8	31.4	55.6	18.0	8.1	51.5	6.4	1.9
Greece, 1999	12.4	19.8	18.8	20.0	10.8	13.4	16.8	4.8
Ireland, 2000	15.7	53.9	88.7	22.1	10.7	74.8	17.4	1.6
Italy, 2000	15.7	24.9	76.8	13.4	14.1	61.1	23.9	1.6
Japan, 2000	14.3	57.3	52.1	57.9	11.4	46.0	12.3	10.6
Luxembourg, 1999	7.8	35.1	66.3	31.4	5.7	20.8	8.5	2.9
Mexico, 2002	24.8	35.0	45.6	32.6	20.7	37.9	26.2	15.4
Netherlands, 2000	9.0	30.3	42.8	17.7	5.2	50.7	7.8	1.7
New Zealand, 2001	16.3	47.5	87.6	21.3	8.8	43.3	14.5	4.1
Norway, 2000	3.6	9.9	24.7	2.8	1.7	38.0	2.8	0.1
Poland, 2000	14.5	34.7	69.1	13.7	10.2	41.8	14.9	1.9
Portugal, 2000	15.6	32.5	84.8	20.3	12.4	50.6	32.4	4.8
Sweden, 2000	3.6	9.3	34.2	5.6	2.0	13.7	8.2	1.1
Switzerland, 2001	6.8	2.3	9.6	4.7
Turkey, 2002	21.1	57.7	51.6	65.4	16.8	25.2	17.2	15.7
United Kingdom, 2000	16.2	40.7	62.5	20.6	8.7	37.4	17.6	3.6
United States, 2000	21.7	48.9	93.8	40.3	14.5	77.9	30.5	8.3
OECD-24	12.1	32.5	58.0	20.6	8.7	41.6	13.7	4.3

Note: Poverty rates among individuals living in households with children and a head of working age.

Source: Förster, M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris (www.oecd.org/els/workingpapers).

StatLink: <http://Dx.doi.org/10.1787/875231314458>

Further reading: ■ UNICEF (2000), "A League Table of Child Poverty in Rich Nations", Innocenti Research Centre, Florence.
 ■ Förster M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris.

Definition and measurement

One important dimension of the economic well-being of the elderly population is their disposable income relative to that of the working-age population. Data used in this section are derived from household income surveys and other micro datasets that have been used in previous sections to describe poverty and income inequality. Elderly persons are those aged 65 and over, while the population of working age is here defined as those aged between 18 and 64 years of age. The income concept used includes earnings, income from self-employment, capital income and public transfers, net of direct taxes (and social security contributions, in case of continued employment) paid by households and individuals. Household income is “equivalised” by adjusting for household size. Relative poverty rates for the elderly are based on an income cut-off line set to 50% of the median income of the entire population.

It should be noted that the relative income of elderly persons partly reflects the conditions of households where the elderly live. For example, relatively large proportions of elderly people living with their working-age children will generally increase their relative income and lower their poverty rate with respect to countries where most elderly live alone. Also, household disposable income is an imperfect proxy of the economic well-being of older person, likely to underestimate their economic resources and over-estimate their poverty risks, especially in countries where home-ownership among the elderly is higher (e.g. Australia). Older persons, in all countries, have fewer work-related expenses, higher asset holdings and may have access to resources (e.g. subsidised health care and housing) that are unavailable to other population groups; and these factors are more important in some OECD countries than in others, thus affecting cross-country comparisons.

Equivalised disposable income of older people, across 23 OECD countries, is above 75% of that of the working-age population (Chart EQ4.1). Cross-country variation in the relative income of older people is large, with Mexico, Poland, France, Canada, Germany and Austria achieving the highest levels (85% or more) and Australia the lowest (60%). Cross-country differences in the relative disposable income of older people are only weakly related to different systems of retirement income provision. For example, both Canada and Australia – at the two extremes of the ranking of relative income – have substantial private pensions, whereas France – with high income of older people – does not. When incomes from public and private provisions are considered together, pension systems appear to have successfully ensured adequate living standards to the vast majority of older people, though income from work also plays a significant role in some countries (e.g. Japan).

There is also much diversity across countries when looking at changes in the economic situation of older people. In the period from the mid-1980s to the mid-1990s, relative income of older people improved in a majority of countries (in particular Sweden), mainly reflecting the maturation of their pension schemes, but it worsened in some (notably in Australia, Ireland, Japan, Netherlands and New Zealand). In the second half of the 1990s, relative income of older people declined in a majority of countries. Large declines (Canada, Poland and Sweden) are likely due to increases in working-age

incomes, not necessarily changes in income levels of older people. Significant improvements in the relative income of older people are recorded by Mexico and Greece (reversing earlier declines) and Germany and Austria (extending previous increases).

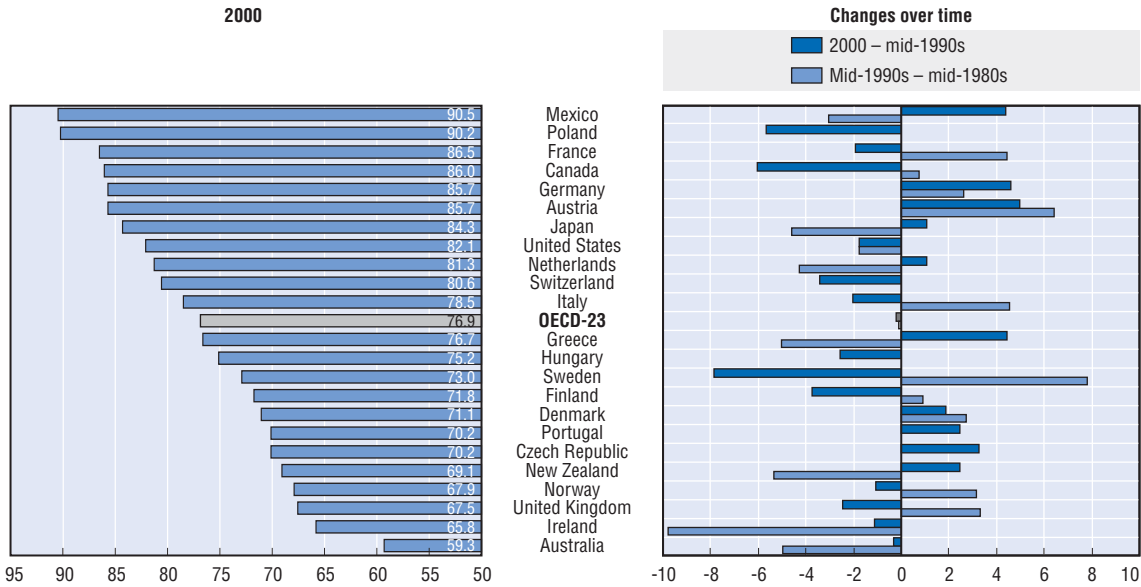
Changes in relative incomes of older people are reflected in changes in their poverty rates. Poverty rates among older people have been brought down to low levels over the past few decades in most OECD countries. Their poverty rate, at around 14% in 2000 across the 17 countries for which longer-term data are available, increased in the second half of the 1990s on average by around 1 point, reversing the improvement recorded in the previous decade. This “average” hides great diversity of experience, with almost as many countries experiencing a decline in pension poverty as those witnessing increases. By 2000, older people had a lower probability of falling into relative poverty than the total population in around one third of the countries under review (Chart EQ4.2); and they have been overtaken by children as the age group most exposed to risks of poverty across the OECD.

Status indicators: Retirement ages (SS8), Relative poverty (EQ1), Health-adjusted life expectancy (HE2), Long-term care (HE5).

Response indicators: Public social spending (EQ5), Private social spending (EQ6).

EQ4.1. Wide diversity in levels and changes of relative income of older people

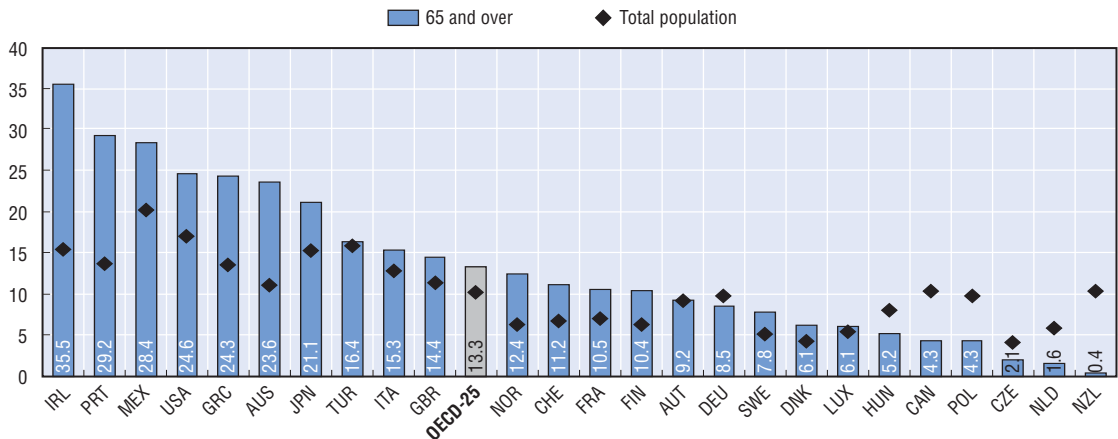
Ratio of equivalised disposable income of people aged 65 and over to that of people aged 18 to 64, percentage



Note: Countries are ranked by decreasing order of the relative income of the elderly in 2000. "2000" data refer to the year 2000 in all countries except 1999 for Australia, Austria and Greece; 2001 for Germany, Luxembourg, New Zealand and Switzerland; and 2002 for the Czech Republic, Mexico and Turkey. "Mid-1990s" data refer to the year 1995 in all countries except 1993 for Austria; 1994 for Australia, Denmark, France, Germany, Greece, Ireland, Japan, Mexico and Turkey; and 1996 for the Czech Republic and New Zealand. "Mid-1980s" data refer to the year 1983 in Austria, Belgium, Denmark and Sweden; 1984 in Australia, France, Italy and Mexico; 1985 in Canada, Japan, the Netherlands, Spain and the United Kingdom; 1986 in Finland, Luxembourg, New Zealand and Norway; 1987 in Ireland and Turkey; 1988 in Greece; and 1989 in the United States. Data for Germany refer to Western länder only. For Canada and Sweden, changes in the period from mid-1990s to mid-1980s are based on surveys different from the ones used in the most recent period.

EQ4.2. Lower poverty rates among older people than for the total population in one-third of OECD countries

Poverty rates for people aged 65 plus and for the total population, percentage, 2000



Note: Poverty rates are measured as the proportion of individuals with equivalised disposable income less than 50% of the median income of the entire population. Countries are ranked by decreasing order of poverty rates among the elderly in 2000. Data for Germany refer to western Länder only.

Source: Förster, M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris (www.oecd.org/els/workingpapers).

StatLink: <http://Dx.doi.org/10.1787/164773650058>

Further reading: ■ OECD (2001), *Ageing and Income: Financial Resources and Retirement in 9 OECD Countries*, OECD, Paris. ■ Förster, M. and M. Mira d'Ercole (2005), "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", Social, Employment and Migration Working Papers, No. 22, OECD, Paris.

Definition and measurement

Social support is the provision, by both public and private institutions, of benefits and financial contributions to households whose circumstances adversely affect their welfare. Much of this support takes the form of social expenditures, which comprises cash benefits and direct “in-kind” provision of goods and services. To be included in social spending, benefits have to address one or more social goals. These expenditures may be targeted at low-income households but also to children, the elderly, and persons who are disabled, sick or unemployed. Programmes regulating the provision of social benefits involve either redistribution of resources across households, or compulsory participation.

Social expenditure is classified as public when the general government (i.e. central, state, and local governments, including social security institutions) controls the relevant financial flows. For example, sickness benefits financed by compulsory employer and employee contributions to social insurance funds are considered “public”, whereas sickness payments paid directly by employers to their employees are classified as “private”. For cross-country comparisons, the most commonly used indicator of social support is “gross” (i.e. before deduction of direct and indirect tax payments levied on these benefits and addition of tax expenditures provided for social purposes) public social spending as a share of GDP. Measurement problems do exist particularly with regards to spending by lower tiers of government, which may be underestimated in some countries.

In 2001, gross public social expenditure represented 21% of GDP on average across 30 OECD countries (Chart EQ5.1), with cash benefits twice as large as in-kind services. Cross country variation in gross spending levels is wide, ranging between about 29% in Sweden and Denmark, and only 6% in Korea.

In terms of functional categories, the three largest items are pensions (which include spending on old-age and survivors, 8% of GDP on average), health (6%) and income transfers to the working-age population (5%); within this last category, public spending targeted to families with children and to persons with disabilities represented each nearly 2% of GDP. Spending on old-age and survivor pensions represent more than 12% of GDP in Austria, Greece, Italy and Switzerland, and less than 5% in Australia, Iceland, Ireland, Korea, New Zealand and Norway. Gross public spending on social services exceeds 5% of GDP only in the Nordic countries, where the public role in providing services to the elderly, the disabled and families is the most extensive.

Changes in gross public social expenditures over time are also significant (Chart EQ5.2). After having

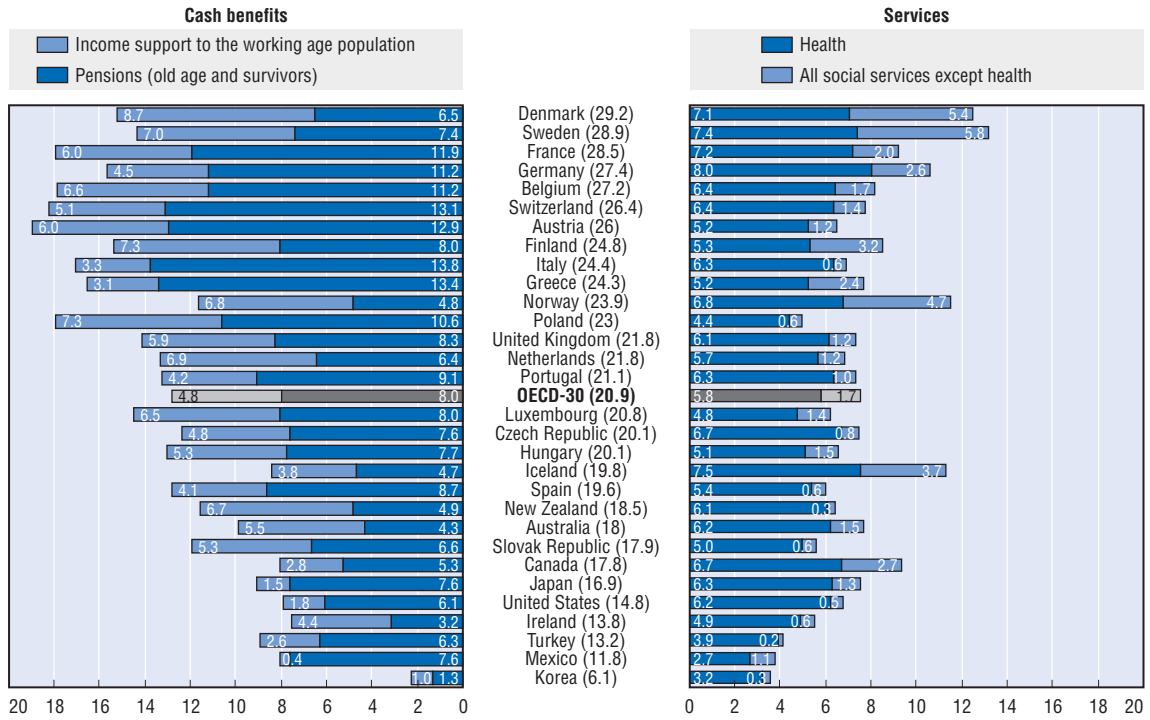
almost doubled in the 20 years to 1980, the expansion of gross public expenditure continued at a reduced rate with the OECD average peaking at 23% in 1993. Since then, gross public social expenditure has declined – on average – by around 1½ points of GDP by 2001, with all the decline accounted by non-health expenditures. In Finland, Ireland, the Netherlands and Sweden, gross public social spending declined from peak levels by more than 6 points of GDP, while in Greece, Iceland, Japan, Portugal, Switzerland and Turkey gross public social spending continued to increase.

Status indicators: Unemployment (SS2), Working mothers (SS4), Relative poverty (EQ1), Child poverty (EQ4).

Response indicators: Out-of-work benefits (SS5), Benefits of last resort (SS6), Total social spending (EQ7), Total health care expenditure (HE4).

EQ5.1. Public social spending represents close to one-fifth of GDP on average

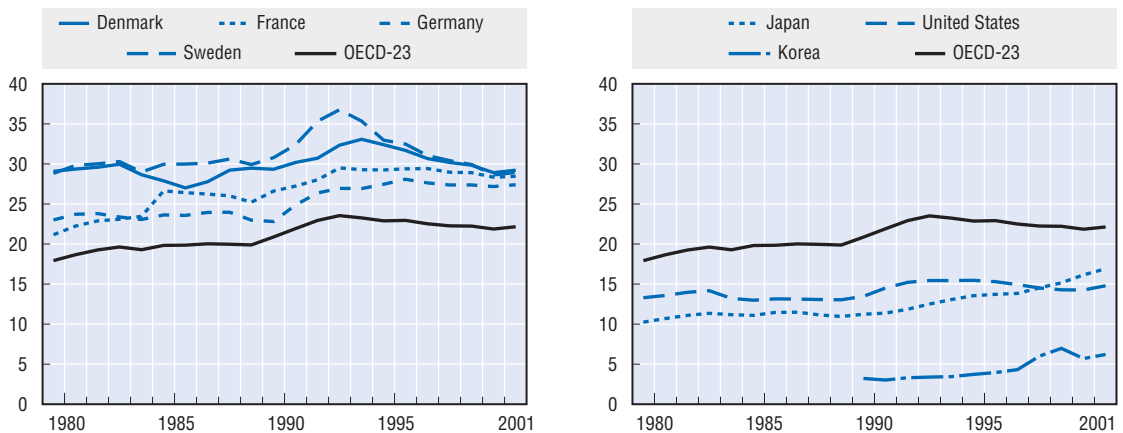
Gross public social expenditure by broad policy area, in percentage of GDP, 2001



Note: Countries are ranked by decreasing order of total public social expenditure as a percentage of GDP. Spending on Active Labour Market Programmes (ALMPs) cannot be split by cash/services breakdown. ALMPs are however included in total public spending in brackets.

EQ5.2. Small declines in public social spending since 1993

Gross public social spending for selected countries, in percentage of GDP, 1980-2001



Source: OECD (2004), Social Expenditure Database 1980-2001, OECD, Paris (available at www.oecd.org/els/social/expenditure).

StatLink: <http://Dx.doi.org/10.1787/138143773102>

Further reading: ■ Adema, W. (2001), "Net Social Expenditure, 2nd Edition", Labour Market and Social Policy Occasional Papers, No. 52, OECD, Paris (see www.oecd.org/els/workingpapers).

Definition and measurement

Households can receive social support not only from governments but also from the private sector – where the private sector is defined as including all financing flows not controlled by general government. Excluded from these flows are direct transfers between individuals (*e.g.* gifts). Gross private social expenditure concerns all programmes with a social purpose that contain an element of interpersonal redistribution. The redistributive nature of private social benefits can be due to government legislation on benefit rules (mandatory private social benefits), stipulations in collective agreements or financial support provided by governments to voluntary individual arrangements and employment-related benefit plans. Private expenditure flows presented in this section are recorded on a gross basis (*i.e.* before deduction of tax payments levied on these flows and of tax expenditures).

Measurement problems are greater for private social spending than for public spending. Even when governments set benefit rules, providers often do not have to report relevant expenditure to government agencies. When direct information about these expenditure flows is lacking, indirect measures have to be used. For example, spending data on mandatory employer-provided sickness benefits reported here are often based on information on wages and on the number of work days lost because of sickness. Coverage of private expenditure flows is not full. For example, in the case of private social health benefits, current estimates do not include individual co-payments set through government regulations.

There are considerable differences across countries in the extent to which social protection systems rely on private provision. Gross private social spending is above 10% of GDP in the United States, while it is negligible or non-existent in about of the countries covered in Table EQ6.2. Private social benefits are common in the case of occupational accidents and diseases (*e.g.* Australia), sickness benefits (*e.g.* Germany) and old-age pensions, in the form of either mandatory participation in employer-based programmes (*e.g.* the United Kingdom) or of tax-supported individual pension plans (*e.g.* the United States). On average, around $\frac{3}{4}$ of all private social expenditure takes the form of voluntary spending, with the remainder being mandated by law.

In some OECD countries at least, the role of private social benefits has increased in recent years, especially in the United States and the Netherlands (Chart EQ6.1). Different factors underlie this trend. The maturing of private pension programmes largely account for the upward trend in private social expenditure, especially in Canada. Reductions in the generosity of public employment-related social benefits (sickness and incapacity related income support) since the 1980s have also encouraged the

growth of private benefits to top-up public programmes. In Denmark, the Netherlands and Sweden, governments have legislated increased employer's responsibility for the provision of sickness benefits during the first part of the 1990s.

In the United States, higher health care costs since the 1980s contributed to trend increase in private social spending, while a decline in the proportion of employers providing health care coverage (and lower benefit rates) partly offset this increase during the first part of the 1990s.

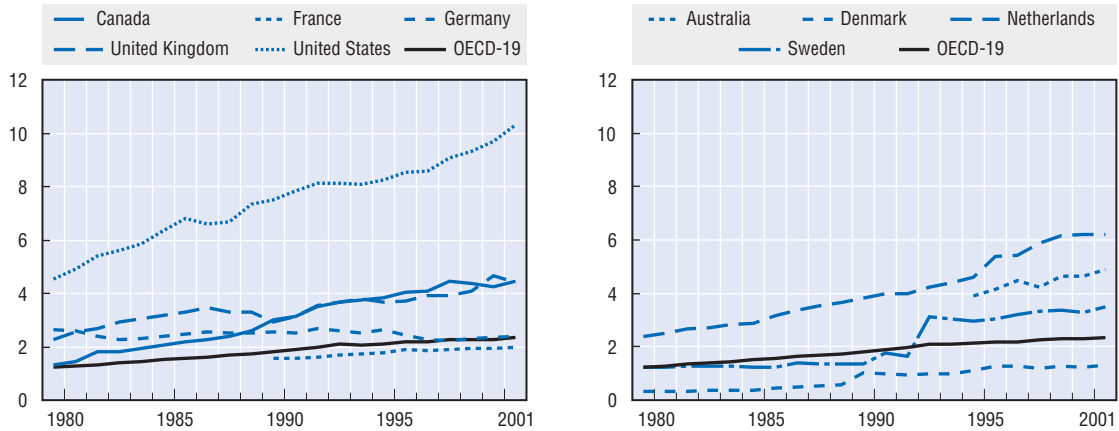
The importance of private social benefits is expected to grow in the future in most OECD countries, as capitalised pension programmes become more common and mature.

Status indicators: Employment (SS1), Income inequality (EQ2).

Response indicators: Public social spending (EQ5), Total social expenditure (EQ7), Total health care expenditure (HE).

EQ6.1. Gross private social spending is edging up in most OECD countries

Mandatory and voluntary private social spending, in percentage of GDP, 1980 to 2001



EQ6.2. Composition of private social expenditure

Total, mandatory and voluntary¹ gross private social spending, percentage of GDP, 2001

	Mandatory private					Voluntary private ¹					Total private	Share of private in total (public-private total spending) %
	Total	Old age	Incapacity	Health	Other	Total	Old age	Incapacity	Health	Other		
Australia	0.9	-	0.9	-	-	4.0	3.3	-	0.7	0.0	4.9	21.4
Austria	0.9	-	0.9	-	-	0.7	0.1	-	0.6	-	1.6	5.7
Belgium	-	-	-	-	-	-	-	-	-	-	-	-
Canada	-	-	-	-	-	4.5	3.4	-	1.1	0.0	4.5	19.7
Czech Republic	-	-	-	-	-	-	-	-	-	-	-	-
Denmark	0.3	-	0.3	-	-	1.0	0.9	-	0.1	-	1.3	4.3
Finland	0.1	0.1	0.0	-	0.0	1.0	0.1	0.7	0.2	0.0	1.2	4.5
France	-	-	-	-	-	2.0	0.2	0.3	1.2	0.3	2.0	6.5
Germany	1.4	-	1.3	-	0.1	1.0	0.6	0.1	0.3	0.0	2.4	8.1
Greece	-	-	-	-	-	-	-	-	-	-	-	-
Hungary	-	-	-	-	-	0.0	-	-	0.0	-	0.0	0.1
Iceland	1.4	-	1.4	-	-	-	-	-	0.0	-	1.4	6.7
Ireland	-	-	-	-	-	0.4	-	-	0.4	-	0.4	3.1
Italy	1.4	-	-	-	1.4	0.1	-	-	0.1	-	1.5	5.7
Japan	0.6	0.6	-	-	0.0	0.0	0.0	-	0.0	-	0.6	3.3
Korea	2.6	0.0	0.1	-	2.4	1.9	-	-	-	1.9	4.4	42.0
Luxembourg	-	-	-	-	-	0.1	-	-	0.1	-	0.1	0.5
Mexico	-	-	-	-	-	0.2	-	-	0.2	-	0.2	1.4
Netherlands	0.7	-	0.7	-	-	5.5	3.0	0.4	1.4	0.8	6.2	21.6
New Zealand	-	-	-	-	-	0.5	-	-	0.5	-	0.5	2.6
Norway	1.3	-	1.3	-	-	0.8	0.6	0.2	-	0.0	2.1	8.1
Poland	-	-	-	-	-	-	-	-	-	-	-	-
Portugal	0.4	-	0.4	-	-	0.3	0.2	0.0	0.0	0.1	0.8	3.4
Slovak Republic	0.3	0.2	0.1	-	0.0	0.1	-	-	0.1	-	0.4	2.0
Spain	-	-	-	-	-	0.3	-	-	0.3	-	0.3	1.5
Sweden	0.6	-	0.6	-	-	2.9	2.1	0.4	0.1	0.3	3.5	10.8
Switzerland	0.6	-	0.5	-	0.1	1.2	0.0	0.0	1.1	0.0	1.9	6.6
Turkey	-	-	-	-	-	-	-	-	-	-	-	-
United Kingdom	0.5	0.5	0.1	-	-	3.9	2.5	0.7	0.3	0.4	4.4	16.9
United States	0.4	-	0.2	0.2	0.0	9.9	4.7	0.2	5.0	0.0	10.3	41.1
OECD-30	0.5	0.0	0.3	0.0	0.1	1.4	0.7	0.1	0.5	0.1	1.9	8.2

--: No programme. 0.0: Programme exists, but it is less than 0.1% of GDP.

1. Estimates.

Source: Estimates based on Adema, W. and M. Ladaique (2005), "Net Total Social Expenditure", Social, Employment and Migration Working Papers, forthcoming, OECD, Paris (www.oecd.org/els/workingpapers).

StatLink: <http://Dx.doi.org/10.1787/013227035342>

Further reading: ■ Martin, J.P. and M. Pearson (2005), "Should We Extend the Role of Private Social Expenditure?", Social, Employment and Migration Working Papers, forthcoming, OECD, Paris (www.oecd.org/els/workingpapers).

Definition and measurement

A comprehensive account of the total amount of resources that each OECD country devotes to the pursuit of social goals has to take into account both public and private social expenditures, and the extent to which the tax system affects the effective amount of support provided. To capture the effect of the tax system on gross (before tax) social expenditures, account has to be taken of the government “clawback” on social spending through the direct taxation of benefit-income and the indirect taxation of the goods and services consumed by benefit recipients. Moreover, governments can pursue social goals by awarding tax advantages for social purposes (e.g. child tax allowances). From the perspective of society, “net” (i.e. after tax) social expenditure, from both public and private sources, gives a better indication of the resources used to pursue social goals. From the perspective of individuals, “net social expenditure” reflects the proportion of an economy’s production on which benefit recipients can lay a claim.

Measuring the impact of the tax system on social expenditure often requires estimates derived from micro-data sets and microsimulation models, as administrative data are frequently not available. Also, central recording of private social spending is not always available. Hence, relevant information is of lesser quality than data on gross public social expenditure. Since adjustments are required for indirect taxation, net social spending is related to GDP at factor costs rather than to GDP at market prices.

Table EQ7.1 illustrates the effect of tax payments and tax expenditures on gross social spending by governments in selected OECD countries in 2001. Three features stand out. First, the “clawback” of gross social spending through direct taxation of benefit income is highest in Denmark and Sweden, where around 13% of cash transfers returns to the government coffers through income and payroll taxes. Second, the amount of gross public spending clawed back through indirect taxation is generally larger in European than in non-European OECD countries. Third, countries with limited direct taxation levied on benefits – Canada, Germany, and the United States – make more extensive use of tax breaks granted towards non-pension expenditures. Because of gaps in data availability and of conceptual issues raised by their measurement, tax breaks towards old-age pensions – available for only a few countries – are shown in Table EQ7.1 as a memorandum item.

In general, governments claw back more money through taxation of public social expenditure than they spend on tax breaks provided for social purposes. The only exceptions to this pattern are Mexico and the United States (where net public social expenditures exceed gross outlays) and Korea (where the two spending aggregates are equal).

On average, across 18 OECD countries in 2001, net total social expenditure accounted for a little more than 22% of GDP, ranging from more than 30% in Germany to less than 12% in Korea. Accounting for both private social benefits and the impact of the tax system considerably reduces differences in social spending to GDP ratios across countries. In fact, the proportion of an economy’s domestic production to which recipients of social benefits lay claim (as measured by total net social expenditure) is rather similar in Austria, Denmark, the Netherlands, Norway, the United Kingdom and the United States (Chart EQ7.2). However, a similar size of net social spending across countries does not imply that the degree of redistribution achieved through the tax and benefit systems is also similar, nor that the impact on the economy is the same.

Status indicators: Relative poverty (EQ1), Income inequality (EQ2).

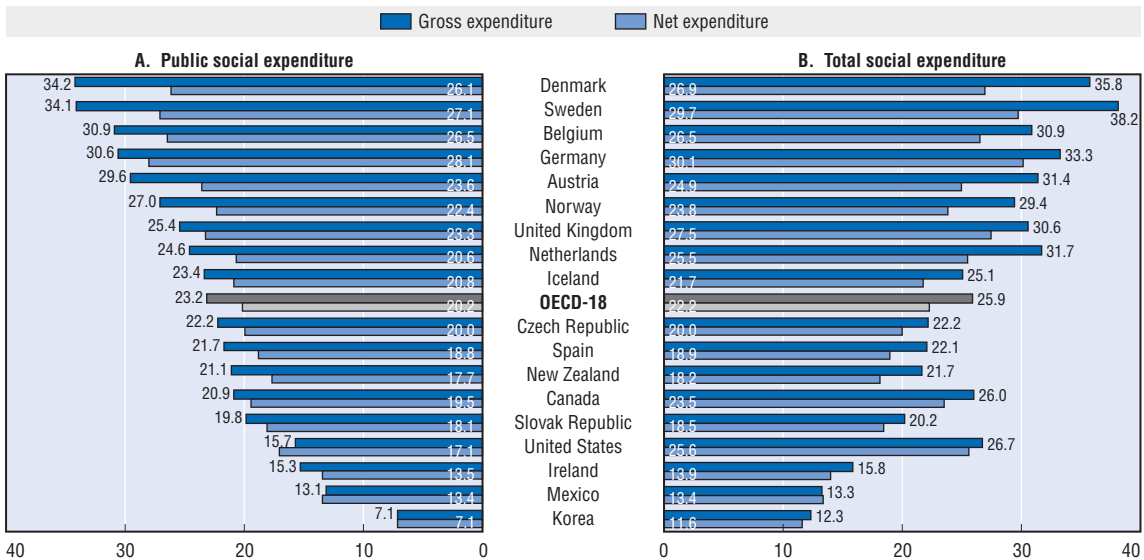
Response indicators: Public social spending (EQ5), Private social spending (EQ6), Total health care expenditure (HE4).

EQ7.1. From gross to net public social spending
Percentage of GDP at factor costs, 2001

	Austria	Belgium	Canada	Czech Republic	Denmark	Germany	Iceland	Ireland	Korea	Mexico	Netherlands	New Zealand	Norway	Slovak Republic	Spain	Sweden	United Kingdom	United States	
Gross public social expenditure	29.6	30.9	20.4	22.2	34.2	30.6	23.4	15.3	7.1	13.1	24.6	21.1	27.0	19.8	21.7	34.1	25.4	15.7	
- Direct taxes and social contributions on benefit income	2.9	2.2	0.7	0.0	4.6	1.6	0.7	0.3	0.0	-	2.6	1.7	2.1	-	1.2	4.3	0.3	0.6	
- Indirect taxes on goods and services consumed by benefit recipients	3.1	2.8	1.0	2.2	4.0	2.3	1.9	1.8	0.4	1.0	2.4	1.9	2.8	2.1	1.8	2.9	2.2	0.4	
+ Tax breaks towards non-pension social policy spending (TBSPs)	0.0	0.5	0.2	2.2	0.0	1.3	-	0.2	0.4	1.3	0.8	0.1	-	0.4	0.0	-	0.4	2.3	
= Net public social expenditure	23.5	26.4	19.0	22.1	25.7	27.9	20.8	13.5	7.1	13.4	20.4	17.6	22.2	18.1	18.7	26.8	23.3	17.1	
<i>Memorandum item:</i>																			
Tax breaks towards pensions spending	0.1	0.3	1.7	0.2	..	0.9	1.1	2.5	..	0.1	..	0.0	0.2	0.1	0.2	..	1.5	1.2	

.. Data not available.
- Zero.

EQ7.2. From public to total social expenditure
Percentage of GDP at factor costs, 2001



Source: Estimates based on Adema, W. and M. Ladaïque (2005), "Net Total Social Expenditure", Social, Employment and Migration Working Papers, forthcoming, OECD, Paris (www.oecd.org/els/workingpapers).

StatLink: <http://Dx.doi.org/10.1787/838027316736>

Further reading: ■ Adema, W. (2001), "Net Social Expenditure, 2nd Edition", Labour Market and Social Policy Occasional Papers, No. 52, OECD, Paris (www.oecd.org/els/workingpapers).

Definition and measurement

The old-age pension replacement rate is a measure of how effectively a pension system provides income during retirement to replace earnings which were the main source of income prior to retirement. The indicator here is the expected pension benefit for a full-career, single worker in the private sector entering the labour market at age 20. It includes all mandatory parts of the pension system, both public and private, while excluding voluntary pensions, which are important in some countries. This indicator aims to show the long-term stance of the pension system and takes account of all changes in rules and parameters that have been legislated; phased-in legislated changes will thus be fully in place by the time of retirement. Parameters are those for the year 2002. A standard set of economic assumptions is used for each country.

The replacement rate is defined as pension entitlement divided by pre-retirement earnings. It is calculated over the full earnings range: from 0.3 to 2.5 times average earnings. Indicators of expected replacement rates from old-age pensions are presented both on a gross (i.e. pre-tax) and net basis (i.e. taking account of the taxes and social security contributions paid on earnings when working and on pension when retired).

Chart EQ8.1 shows the pattern of gross replacement rates from old-age pensions relative to earnings in 10 countries. The countries are selected to show the full range of pension systems in the OECD area. In Australia, Denmark and the United Kingdom, the pension system pays a similar amount to people regardless of their earnings history. This means that the replacement rate declines with earnings. These countries all have public schemes that are wholly or mainly resource-tested (paying larger amounts to low-income pensioners) or flat-rate (paying the same amount to all for each year of contributions or residency).

In contrast, Finland, Italy and the Netherlands pay very similar replacement rates across the earnings range, meaning that the replacement rate curve is flat above half average earnings. Benefits are strongly related to previous earnings. Other countries are intermediate cases. France and Germany are both traditionally regarded as countries with a strong social-insurance tradition. However, ceilings in the public scheme (of around 125 and 150% of average earnings respectively), plus a generous minimum pension in France, means that replacement rates fall at higher earnings levels unlike the other three countries in the right-hand panel.

The United States' public pension has a strongly redistributive formula. At half-average earnings, the gross replacement rate is over 50%, falling to 40% at average earnings and to 30% at twice average earnings. Japan has a two-tier public pension programme, with flat-rate and earnings-related parts.

This delivers a similar pattern of benefits with earnings as in the United States.

It is the net replacement rate that matters to individuals as this is what determines their standard of living during retirement relative to when working (Chart EQ8.2). Averaging across OECD countries, net replacement rates at average earnings are 22% larger than gross replacement rates. Net replacement rates are substantially higher than gross rates in Belgium, France and Germany. The effect of taxes and contributions on low earners is more muted because they typically pay less in taxes and contributions than those on average earnings. The differential between net and gross replacement rates for low earners is 17% on average.

At average earnings, the average net replacement rate for OECD countries is 69%. There is substantial variation, with Ireland and New Zealand (which have just basic schemes) paying 40% or less, while in Turkey and Luxembourg pension entitlements exceed pre-retirement earnings. Net replacement rates at low earnings are much closer together than at high earnings.

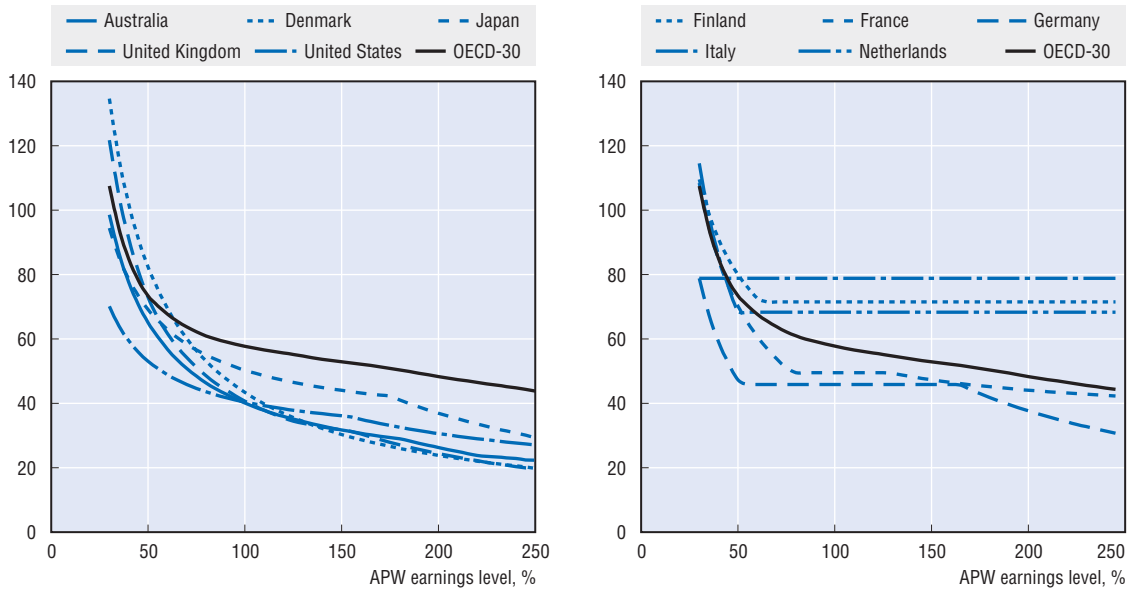
Status indicators: Age at retirement (SS8), Income of older people (EQ4), Health-adjusted life expectancy (HE2).

Response indicators: Public social spending (EQ5), Pension promise (EQ9).

EQ8. OLD-AGE PENSION REPLACEMENT RATE

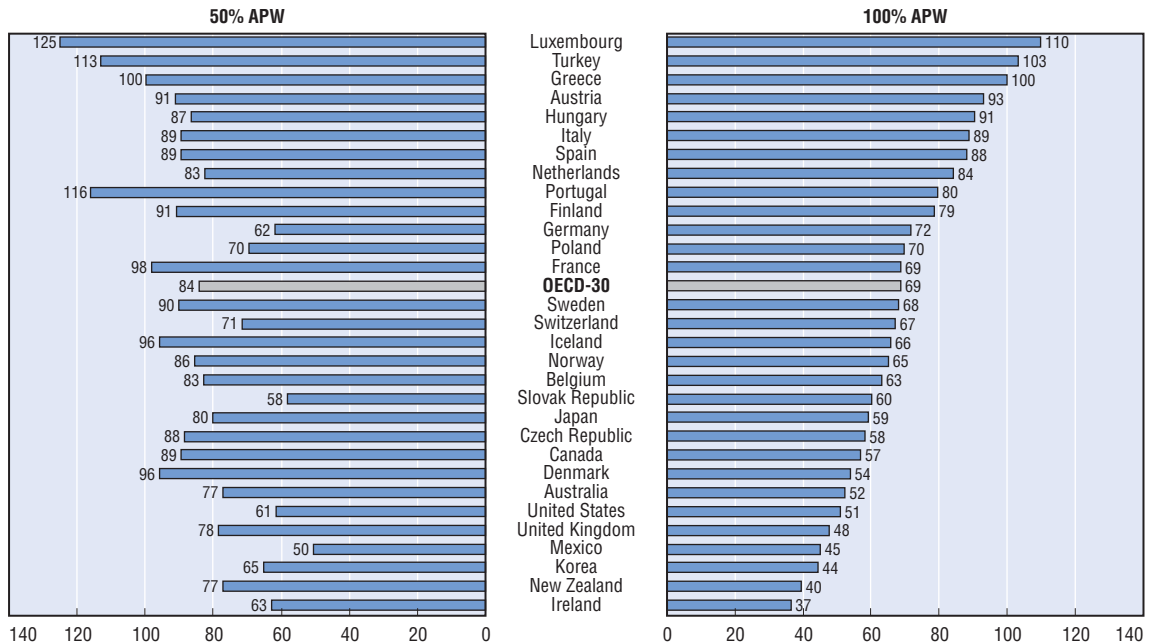
EQ8.1. Variation across countries in generosity of pension programmes

Gross replacement rates by earnings level, mandatory pension programmes, in percentage of individual pre-retirement gross earnings, men



EQ8.2. At average earnings, the average net replacement rate for OECD countries is 69%

Net replacement rates by earnings level, mandatory pension programmes, in percentage of pre-retirement net earnings at 50% and 100% of APW, men



Note: APW: Average production worker wage.

Source: OECD (2005), *Pensions at a Glance: Public Policies across OECD Countries*, forthcoming, OECD, Paris (see also www.oecd.org/els/social/ageing).

StatLink: <http://Dx.doi.org/10.1787/872465550831>

Further reading: ■ OECD (2000), *Reforms for an Ageing Society*, OECD, Paris. ■ OECD (2001), *Ageing and Income: Financial Resources and Retirement in 9 OECD Countries*, OECD, Paris. ■ OECD (2005), *Pensions at a Glance – Public Policies across OECD countries*, forthcoming, OECD, Paris.

Definition and measurement

Old-age pension replacement rates as shown in EQ8 give a snapshot picture of the value of pension entitlements at the point of retirement. But a complete picture of the worth of pension entitlements to individuals and the cost of the resource transfer to older people needs to take account of three other factors. First, pension eligibility ages differ between countries and sometimes between the sexes. Second, life expectancies vary, again both between countries and between the sexes. These two factors change the expected duration of retirement and so the period over which the pension is paid. Finally, countries have different policies for adjusting pensions in payment: some to prices, some to average earnings and some to a mix of the two. If real wages grow, then earnings indexation of benefits is more expensive than linking them to prices.

Pension promise is defined as the net present value of pension benefits at the point of retirement. It depends on the replacement rate, but also on indexation, pension age and country-specific mortality rates by age. The calculations use the same models used to calculate old-age pension replacement rates: they are modeled on the basis of the rules of mandatory pension systems (both private and public) for private-sector workers in the year 2002.

Countries can more easily afford to promise a higher pension replacement rate if the benefit is paid for a shorter period, for example if the pension eligibility age is higher. A price-indexed pension paid from age 60 is worth nearly 20% more than one of the same value paid from age 65. The expected pension replacement rate can also be higher the shorter is life expectancy at retirement. Citizens of poorer OECD countries are projected to retain lower life expectancies than their counterparts in richer economies. In Hungary, Mexico, Poland, the Slovak Republic and Turkey, total life expectancy at 65 is 1½ to 3 years shorter than the OECD average. In Turkey, for example, it would cost 15% less to pay a certain pension from age 65 than it would at OECD average mortality rates. Iceland, Japan and Switzerland have significantly longer life expectancy than the OECD mean. The cost of a pension from age 65 in Japan is 12% higher than the OECD average because of this longer life expectancy.

Luxembourg has the highest pension wealth for a worker on average earnings (Chart EQ9.1). It is worth 20 times economy-wide average earnings for

men and nearly 25 times for women. Given average earnings in that country of over EUR 31 000, the pension wealth of an average earner at the time of retirement is around EUR 470 000 for a man and EUR 600 000 for a woman.

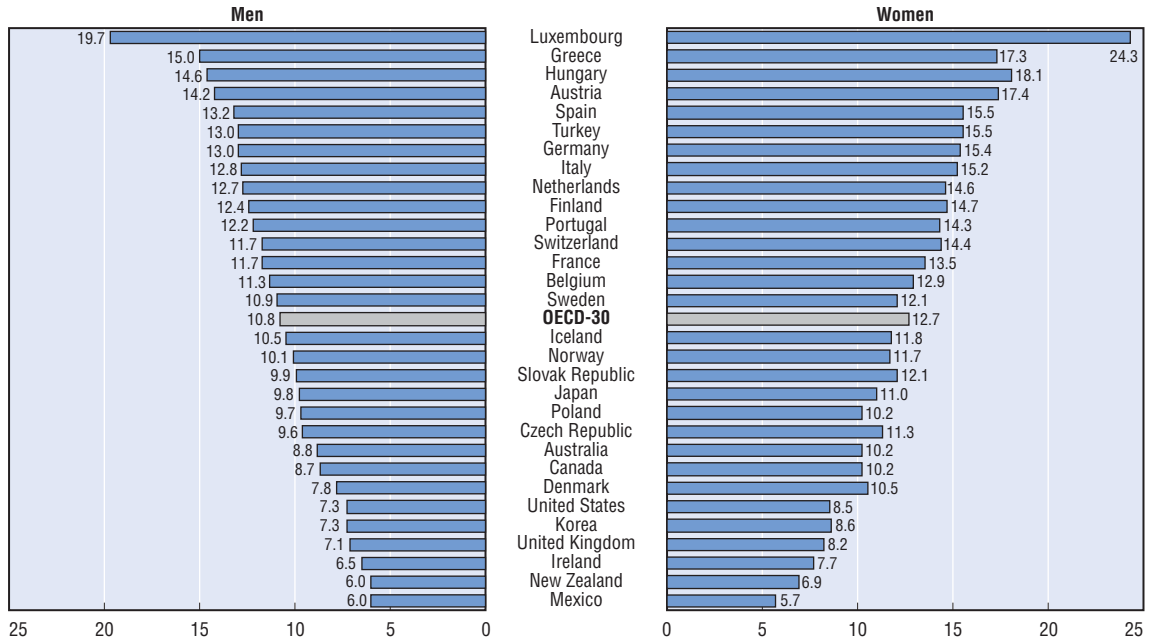
The effect of different standard pension ages is also evident. France, for example, has gross replacement rates significantly below the OECD average; however, pension wealth is above the OECD average because of lower standard pension age (60) and higher life expectancy.

Status indicators: Age at retirement (SS8), Relative poverty (EQ1), Income of older people (EQ4), Health-adjusted life expectancy (HE2).

Response indicators: Public social spending (EQ5), Old-age pension replacement rate (EQ8).

EQ9.1. Variation in pension wealth across OECD countries

Net present value of pension benefits at normal pension age, by gender, as a percentage of gross earnings of an average production worker



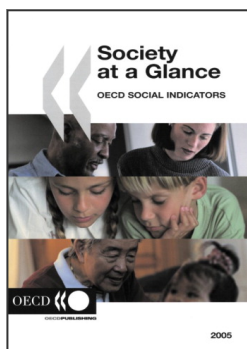
Source: OECD (2005), *Pensions at a Glance: Public Policies across OECD Countries*, forthcoming, OECD, Paris (see also www.oecd.org/els/social/ageing).

StatLink: <http://Dx.doi.org/10.1787/305030625708>

Further reading: ■ OECD (2000), *Reforms for an Ageing Society*, OECD, Paris. ■ OECD (2001), *Ageing and Income: Financial Resources and Retirement in 9 OECD Countries*, OECD, Paris. ■ OECD (2005), *Pensions at a Glance – Public Policies across OECD countries*, forthcoming, OECD, Paris.

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