

# Small States Economic Development

Luxembourg

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## Economic Development– Historical Background

### • Overview

- Luxembourg enjoys the highest per capita gross domestic product(GDP) in the world. It is classified as advanced high-income economy

### • Economic history

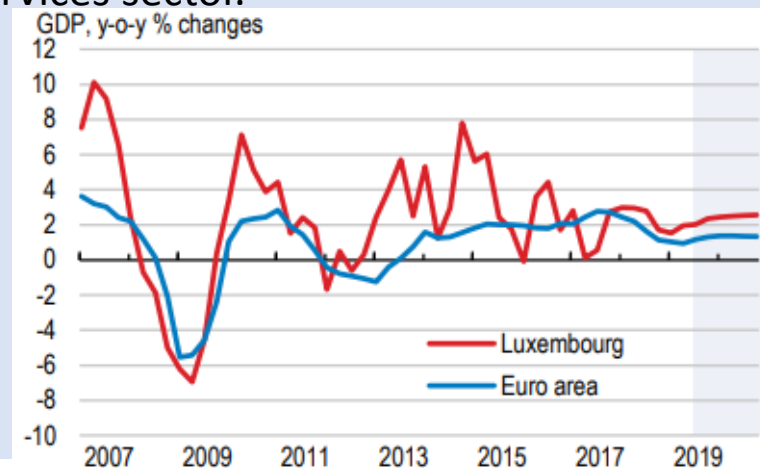
- 1876 marks an introduction of English metallurgy. The refining process led to the development of the steel industry in Luxembourg.
- 1970's marks the beginning of the expansion of the services sector.

### • Structure

- The economy of Luxembourg is largely dependent on the banking, steel, and industrial sectors.  
87% of GDP is produced by service sector (including the financial sector).

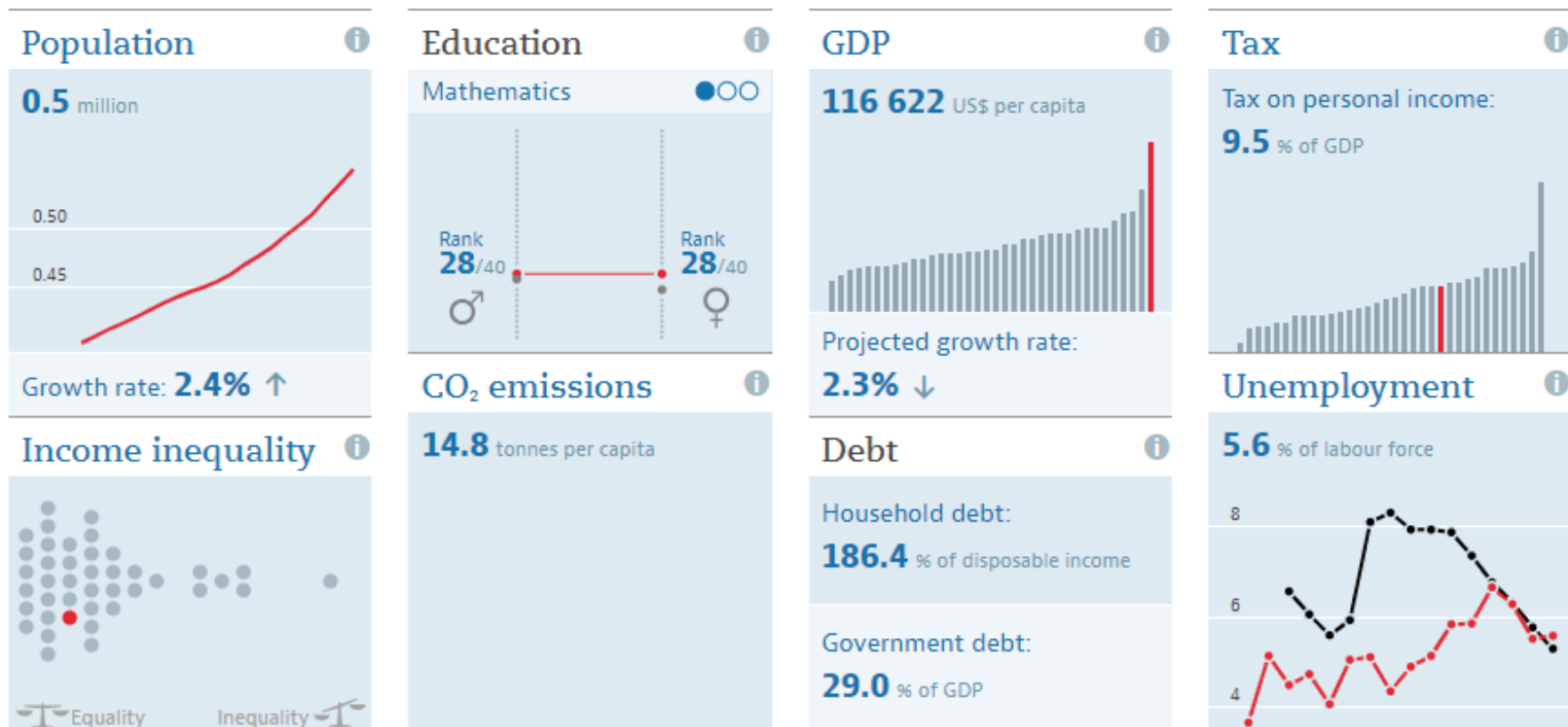
### • Trend

- Steady economic growth. GDP grew by 2.6% in 2018.



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## Economic Development– Country Overview



# Small States Economic Development– Well-being

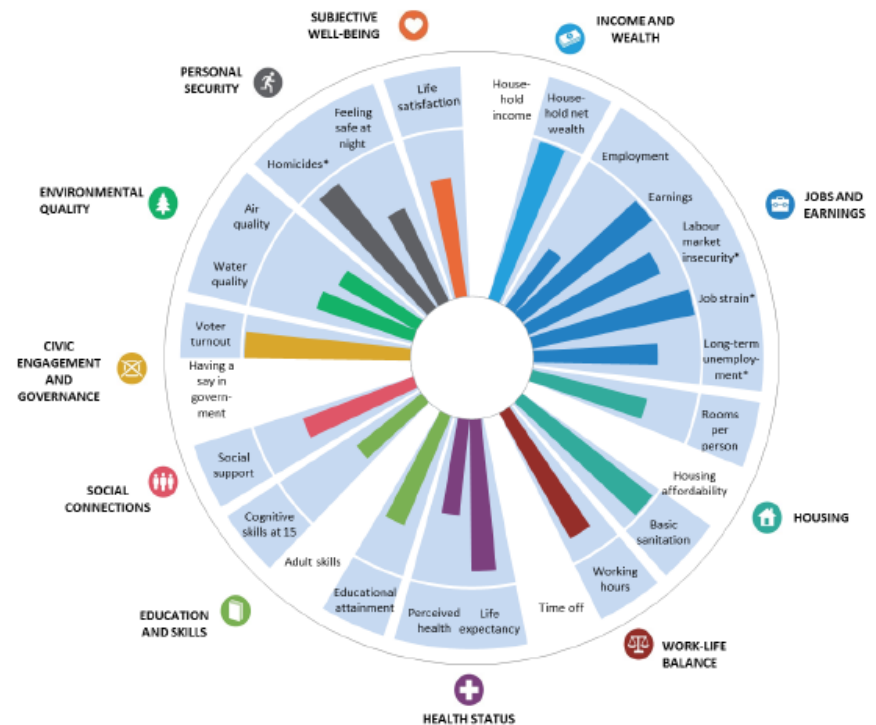
- **Well-being**

- Luxembourg ranks top in income and wealth, above average in social connections, civic engagement, jobs and earnings, work-life balance, personal security, subjective well-being, health status, environmental quality, and housing, but below average in education and skills – Better life Index (OECD).

- **Public Opinion**

- For Luxembourgish users of the Better Life Index, health, life satisfaction and income are the three most important topics

Luxembourg's average level of current well-being: Comparative strengths and weaknesses



# Small States Economic Development – Country Comparison

## • Human Development Index

- Luxembourg is ranked as 21<sup>st</sup> in the world for human development, after countries such as Norway or Belgium

## • Child well-being Index

- Luxembourg ranked as 7<sup>th</sup> overall, behind Germany or Netherlands

## • Sustainable Development Goals

- According to child related SDGs indicators, Luxembourg is placed as 14<sup>th</sup> overall, but 19<sup>th</sup> for child poverty only 25<sup>th</sup> for quality education

TABLE 1

Human Development Index and its components

HDI rank	Human Development Index (HDI)	SDG 3 Life expectancy at birth (years)	SDG 4 Expected years of schooling (years)	SDG 4 Mean years of schooling (years)	SDG 8 Gross national income (GNI) per capita (2011 PPP \$)	SDI per capita rank minus HDI rank	HDI rank
	Value	2018	2018 <sup>a</sup>	2018 <sup>a</sup>	2018	2018	2017
<b>VERY HIGH HUMAN DEVELOPMENT</b>							
1	Norway	0.954	82.3	18.1 <sup>b</sup>	12.6	68,059	5
2	Switzerland	0.946	81.6	16.9	19.4	64,976	4

		Overall well-being	Dimension 1	Dimension 2	Dimension 3	Dimension 4	Dimension 5
		Average rank (all 5 dimensions)	Material well-being	Health and safety	Education	Behaviours and risks	Housing and environment
			(rank)	(rank)	(rank)	(rank)	(rank)
1	Netherlands	2.4	1	5	1	1	4
2	Norway	4.6	3	7	6	4	3
3	Iceland	5	4	1	10	3	7
4	Finland	5.4	2	3	4	12	6
5	Sweden	6.2	5	2	11	5	8
6	Germany	9	11	12	3	6	13

League Table – Country performance across nine child-relevant goals

Country	No poverty	Zero hunger	Good health and well-being	Quality education	Decent work and economic growth	Reduced inequalities	Sustainable cities and communities	Responsible consumption and production	Peace, justice and strong institutions
Norway	1	4	5	9	5	2	2	13	30
Germany	8	8	4	7	6	9	24		15
Denmark	4	2	21	5	10	3	20	19	10
Sweden	6	9	13	16	7	11	6	21	5
Finland	2	15	16	1	15	4	5	11	29
Iceland	3	17	2	27	18	1	8	27	1
Switzerland	5	3	12	11	2	7	27	31	7
Republic of Korea		5	10	3	12	16		22	23
Slovenia	11	27	11	23	9	10		2	13
Netherlands	7	6	6	17	8	12	34	33	14
Ireland	9	31	22	13	37	8	1	8	9
Japan	23	1	8	10	1	32	33	36	8
United Kingdom	16	24	15	20	31	6	14	9	16
Luxembourg	19	12	14	25	3	15	31	28	19
Austria	10	10	9	26	24	13	18	30	28
Spain	28	26	3	12	36	28	16	16	4
Estonia	18	20	26	21	14	29	4	4	35

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## Economic Development: Challenges ahead

- **Housing**

- Strong demographic growth, coupled with a trend towards smaller households, have fueled housing demand, while structural constraints have hampered supply. Limited use of land available for construction and cumbersome zoning restrictions have made land prices soar.

- **Economic Dependency**

- As a small open economy with strong trade and financial links with international markets, Luxembourg remains highly exposed to external risks. Uncertainty, and any financial turmoil that may ensue, could result in a less benign outcome for Luxembourg's economy. The large investment fund industry is sensitive to external risks.

- **Slower growth is projected**

- Productivity growth has long been slow, partly due to skill shortages.

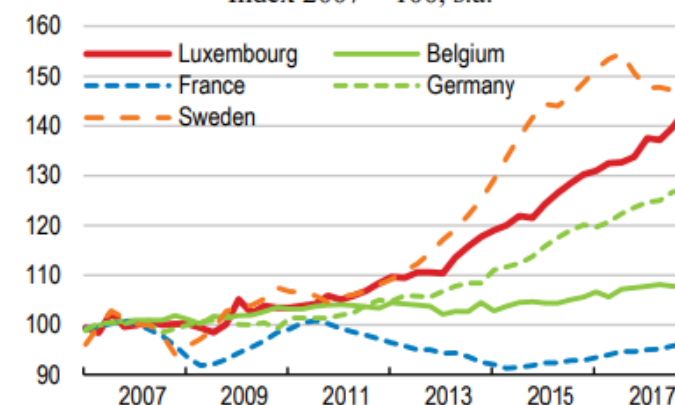
- **Inequality:**

- There is a considerable gap between the richest and poorest – the top 20% of the population earn nearly five times as much as the bottom 20%.

- **Fiscal challenge**

- The fiscal position is very strong, but ageing creates a long-term fiscal challenge. Ageing-related costs are projected to rise substantially, posing a long-run fiscal sustainability challenge.

**Figure B. Real house prices are growing strongly**  
Index 2007 = 100, s.a.



Source: OECD, Analytical house prices indicators database.

StatLink  <https://doi.org/10.1787/888933951000>

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## Economic Development : Key Recommendations

- **Address pressure and improve inclusiveness in the housing market**
  - Increase residential density, in particular around transport network hubs, namely by building higher buildings.
  - Rising house prices and household indebtedness create vulnerabilities for some families and for some banks.
- **Reduce financial risks**
  - Reinforce financial supervision, namely by continuing to monitor credit risks
- **Reviving economic growth**
  - A fiscal stimulus could be envisaged in case of a severe downturn, which might result from rising trade tensions and financial volatility
  - Undertake regular skill foresight exercises and ensure their outcomes feed into enhanced training offers.
- **Addressing fiscal challenge to make growth sustainable and inclusive**
  - Increase the retirement age with life expectancy and/or reduce the generosity of pensions.
  - Continue to engage in international efforts to address tax challenges of cross-border activities and to strengthen tax transparency

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## Economic Development: Current Strategies and Policies

The government has outlined its planned policy reforms for the 2018-2023

- **Housing**

- Increasing the public rental housing stock and limiting the sale of public social housing;
- Reforming the housing assistance system, focusing on single parents and families with children

- **Taxation**

- Increasing excise duties on fuel and petrol
- Increasing net minimum wages by introducing a minimum social salary tax credit
- Revisiting the tax system for cross border commuters to facilitate working from home

- **Mobility**

- Making public transport free of charge from 2020

- **Digitalisation**

- Providing 5G coverage across the country



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## Economic Development: Forecast

- **Steady growth ahead**

- steady pace at around 2.6 % GDP growth over the forecast horizon, driven by domestic consumption
- Investment rebounded following the sharp drop recorded in 2018.
- Financial funds have continued to expand despite some volatility in global financial markets.
- Banks have maintained their profitability, mostly by increasing lending.

- **Strong labour market:**

- In 2019, employment growth was around 3.7%, its highest rate since the crisis but job creation is likely to slow in 2020 and 2021.
- Wages (and pensions) are expected to be raised by 2021 due to indexation
- Unemployment projected to remain around 5.5% over the forecast period.

- The general government surplus is set to decline from a high level

Graph II.12.1: Luxembourg - Real GDP growth and contributions, output gap

