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The labour market in the post-crisis economy: the case of Spain

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Abstract. *The current financial and economic crisis has led to imbalances in the labour market, imbalances manifested worse in some economies. The paper aims to analyse the causes of these imbalances, especially the case of Spain, the country with the highest level of unemployment in the European Union. Thus, the characteristics of the labour market in Spain will be highlighted in order to identify the factors responsible for the worsening of the crisis.*

Keywords: labour market; crisis; unemployment; Spain.

JEL Codes: J08, J21, J31, H12.
REL Codes: 8G, 10G, 12G.

1. Introduction

While the crisis started around the same time in most regions of the European Union, its manifestation and depth proved to be very heterogeneous. Some countries have overcome the crisis more easily, while others have experienced inflationary, employment problems and increased economic downturn.

Studies show that the performance of labour markets during the crisis depends on the following factors: state of the economy at the beginning of the crisis, the structural characteristics of the economy and labour market policies (Aiginger, Horvath, Mahringer, 2011).

Even though some countries have recovered faster from the crisis, they still experience an affected labour market (the US), others have suffered large losses following the crisis, but have had a better performance of the labour market (the case of Germany).

In terms of labour productivity, the current crisis has led to widening the disparities between the EU and the US economy and even the gaps between the EU states. The challenge for the European economy is to get out of the vicious circle of unsustainable public spending, the state of disturbance that characterizes the financial markets and the job losses. Labour market reform should be pursued by increasing labour productivity and by labour market reintegration of the unemployed people affected by the crisis.

Such measures will have a positive impact on budget consolidation, generating higher tax revenue and reducing public expenditure on social transfers as well as the risk of future macroeconomic imbalances (Traşcă, Popa, Dudian, 2011).

The economic performance of a country depends on the labour market response to the crisis, demonstrating by economic analysis that there is a direct correlation between economic performance and labour market performance. Economists Aiginger, Horvath, Mahringer, (2011) conducted a research highlighting the connection between *output performance*, at national level, analyzed by several indicators such as real GDP growth, current account balance and *labour market performance*, analyzed by the evolution of employment and unemployment, before and after the crisis. The authors classify countries into four categories from this point of view: 1) countries where economic performance is linked to labour market performance (Norway, Switzerland, France, the Netherlands, Belgium, Austria, Poland), 2) countries with low economic performance and poor labour market performance (Ireland, Iceland, Great Britain, Finland, Hungary, Spain), 3) countries with high economic performance, but poor labour market performance (the US, Portugal) and 4) countries with low economic performance, but high labour market performance (Germany, Italy, Slovakia, the Czech Republic). The study results emphasize that high labour market performance achieved by some economies after the crisis began depended on several factors, particularly on employment protection and on active policies. Given that during crisis, amid increasing uncertainty, companies could significantly reduce the number of employees, one should consider the long-term effects of these measures, which may mean loss of human capital, which could result in additional costs in adapting the company to the structural changes in the long-term. Therefore, policies to stabilize employment, to seek employment protection and adoption of active measures can help overcome the recession faster, with lower social costs.

2. Labour market in Spain – characteristics and particularities

The labour market in the EU countries has been more or less affected by the current crisis. Overcoming the effects of the crisis on employment depends not only on the measures and the policies adopted during the crisis, but also on the characteristics of each economy, on the specificity of each labour market.

Spain, along with Portugal and Greece are part of the Mediterranean employment pattern. Thus, the Spanish labour market is characterized by low flexibility, and reduced employment security. Labour market is segmented, with low internal mobility of labour, characterized by wage rigidities. Both flexibility at company level and employees' security are relatively low, and unions play an important role in the labour market. It is a model that is characterized by a high share of social protection expenditure, stiff employment protection legislation and a high level of early retirement.

Labour market analysis requires knowledge of the economic and social background, as well as the macroeconomic outcomes that the economy has because there is a close connection between these factors and labour market developments.

Spain's economic performance before the crisis was high, with a GDP per capita level above the EU-27 average in 2007. During this period of prosperity, labour market greatly expanded, absorbing an impressive number of new workers, particularly women and immigrants. Economic growth was mainly determined by construction and tourism sectors, as well as by the strong growth in consumption. For example, 25% of the newly created jobs were created in the construction sector in the period 1998-2007. Spain's vulnerabilities to the crisis that started after 2007 were determined by the high external debt and the level of household indebtedness, by the relatively low labour productivity and by the fact that the economy depended mainly on small enterprises (Eurofound, 2010).

Before the crisis, Spain had one of the lowest public debts in the Euro area and budget surplus. Extending credit, especially to the construction business (The Bank of Spain announced that 60% of loans were for construction), made the recovery of loans granted by banks become an issue. Therefore, the banks are facing financial problems and Spain's economy has suffered due to reduced economic activity, increased public debt and imbalances in the labour market. In addition to the construction sector, other sectors in Spain have also experienced a decline, namely automotive industry and even tourism, affected by a lower European living standard.

One of the features of the Spanish labour market is related to the experience of immigration in recent years. Among the OECD member countries, only the US exceeds it in absolute terms from this point of view, also being among the first OECD countries with the highest percentage of foreign-born labour force, after Luxembourg and Switzerland (in 2008). The vast majority of immigrants come mainly from the developing countries (around 90%), mainly from Latin America (53.3%) and Eastern Europe (26.7%) and the average age is around 31 years old. Most immigrants completed high school (45.4%) and were interested in working under temporary contract of employment (70,8%) (Simon, Ramos, Sanroma, 2011).

This high level of immigration in Spain is explained by the fact that Spain, like other European countries, is facing population decline and immigration replaces this natural decrease, so that the population does not suffer dramatic changes.

Before the current financial and economic crisis, in order to avoid the natural decrease of population, some countries encouraged immigration, using as reservoir the labour force from the Eastern European countries, including Romania. After the crisis started the countries' reactions to immigration usually manifested by a desire to reduce immigration, especially temporary immigration to reduce unemployment among their own people. These migratory movements generate effects both in the country of origin and in the country of destination. These effects are manifested economically, socially, demographically, affecting quality of life and economic growth (Roman, Voicu, 2010).

For destination countries, the flow of foreign labour is beneficial in supporting economic activities that cannot be covered by domestic labour market, either because there is a shortage of skilled workers in these areas or due to a lack of interest in these industries (Pociovălișteanu, 2012).

Regarding the Romanians left to work abroad, most went to Spain and Italy, especially for unskilled work. The current crisis has reduced the number of people who go to work abroad due to the problems caused by the low volume of economic activities, especially in construction.

The openness of the Spanish labour market before the crisis, the structural characteristics of the economy and labour market policies have led to significant increases in unemployment in this country.

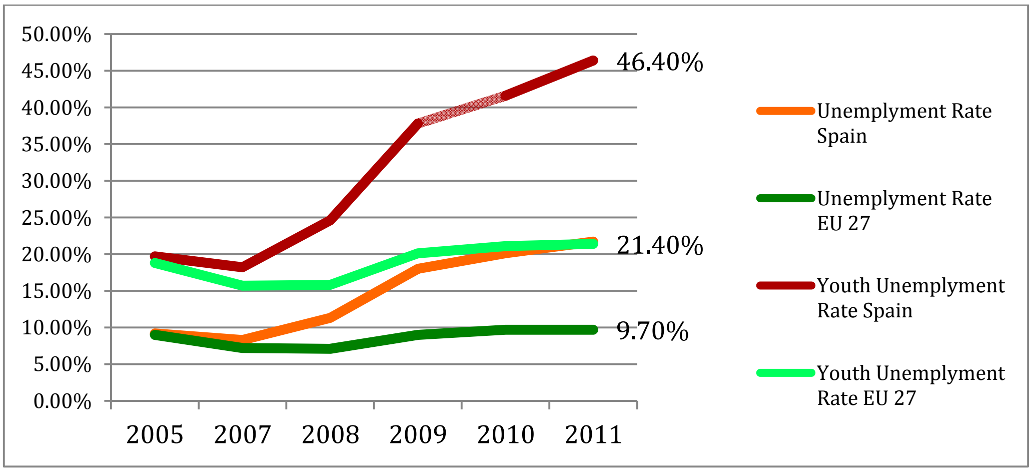
The unemployment rate in Spain has currently reached the highest level in the European Union. Increases in unemployment rate show a worsening economic situation despite all measures taken to return to a level of acceptable employment.

At the end of October 2012, the data in *The Economically Active Population Survey*, conducted quarterly by *The Spanish National Institute of Statistics*, showed that Spain saw a new record in the number of unemployed: 5,778,100 people, and the unemployment rate reached 25.02%, according to the same data.

Eurozone crisis has seriously affected the Spanish economy, manifesting itself in particular by rising unemployment and low budget revenues. The measures taken to reduce the budget deficit, especially government expenditure, have deepened the social crisis, with negative effects especially for those with low income.

In Spain, all age groups have been affected by unemployment, especially youth and women, and those with low educational level (Casado, Fernández, Jimeno, 2012).

The chart below captures the difference recorded in Spain, compared to the EU average in terms of evolution of unemployment and youth unemployment. It is noted that the unemployment rate in Spain recorded an upward trend after 2007. Youth unemployment rate was higher, exceeding by 2.16 times the youth unemployment rate registered in the European Union. In 2011, Spain's unemployment rate reached 21.7%, and youth unemployment rate was 46.4% (Eurostat, 2012).



Source: Eurostat, 2012, http://epp.eurostat.ec.europa.eu/portal/page/portal/eurostat/home/

Figure 1. *Unemployment Rate & Youth Unemplyment Rate-less than 25 years % (Spain and EU-27)*

Rising youth unemployment at EU level is explained in the literature as a result of a weak correlation between workforce training and labour market requirements. If we look at the educational situation in Spain in 2011, we notice that Spain is on first places in European rankings (Eurostat) in terms of people who drop out of school early (26.5% in Spain compared to the EU-27 average of 13.5%) and people who completed only primary education (46.2% in Spain compared to 26.6% EU-27 average). This may explain the increase in youth unemployment in Spain, because young people are not trained enough, therefore they cannot adapt to labour market requirements (Eurostat, 2012).

In order to overcome these problems, John Edmunds, Professor of Business at Babson College in Wesley, Massachusetts, considers that Spain needs to improve its tax base and invest in workforce education.

3. The causes of unemployment in Spain

The causes of these imbalances in the labour market in Spain are determined by several factors, such as the measures and the policies adopted to overcome the effects of the crisis, the structural characteristics of the labour market in Spain, employment legislation and the results achieved at macroeconomic level.

Spain, Greece and Portugal have followed the following steps to reduce the effects of the crisis: wage cuts, public social spending cuts, privatization of certain public transfers (pension system) or public services (health care). The most affected people are those with low incomes and especially those who have to pay back loans.

Professor Vicente Navarro (2012) considers that the main causes of the current crisis in Spain are related to the way in which Spain joined the Euro area. In order to reduce the public deficit according to the requirements imposed by the Stability Pact, special measures were taken to reduce public spending (especially social spending) rather than measures to increase taxes, which led to an increase in social spending deficit. On the other hand, during the housing bubble before the crisis, which led to rapid economic growth, measures aimed at reducing taxes were adopted (especially corporate taxes). Therefore, when the crisis started, the effect of these measures was also felt, amid economic downturn. Thus, the measures adopted focused mainly on public spending cuts (pensions, health and education spending and wages were reduced), as well as corporate tax cuts. Cuts in public spending and wages also reduced demand directly affecting the economic activity.

Vicente Cunat (2012) considers that the main problems facing the labour market in Spain related to job market duality, wage rigidity and conditions to conclude labour market contracts.

Job market duality refers to the relation between permanent and temporary contracts. Approximately 60% of employees have permanent employment contracts. This means that there are legal restrictions to being fired, high severance pay and a safe work environment.

The remaining 40% work under fixed term, often short-lived, *temporary* contracts, with no severance pay or other benefits. Firms prefer to hire workers on temporary contracts, especially young and low-skilled people. Amid the current crisis, this measure somehow has helped companies reduce their costs, especially because they have not invested in continuous training, being interested only in reducing labour costs and hiring/dismissal flexibility.

Thus, this job market duality affects social welfare, leading to increased volatility of the labour market, which complicates the implementation of macroeconomic stabilization policies affecting labour productivity by the fact that the people employed on short-term contracts did not benefit from training and specialization (Costain, Jimeno, Thomas, 2010).

Given the current economic climate, amid rising unemployment, one can say that most of those who work on temporary contracts have had to accept this situation, sometimes without taking into account their level of skills or their needs. On the other hand, temporary employment may reduce incentives so that employers provide training and development opportunities to employees because believing that they do not stay in the same company for a long time (Şerban, 2012).

Wage setting is also an important issue. It is based on negotiations between unions and employers. Collective bargaining covers a wide range of issues, from wage determination to establishing working time and training. Nevertheless, these negotiations are not satisfactory for all firms in a particular sector, because some firms would be willing to pay more to attract well-trained people, while other companies may seek salary cuts and freezes. Thus, a single negotiation must match both types of firms. Therefore, there are viewpoints (Ramos, 2011) that claim that wage setting must be less centralized and should dependent on market supply and demand, on economic conditions. Salary may also be influenced by internal labour migration, which is very low in Spain. This is explained by the tradition and culture of the Spaniards who are attached to their family and the place where they live and do not easily accept the change of address, even for a better salary.

The minimum wage was introduced in Spain in 1963 and is set annually by the government, after consulting the social partners, taking into account the consumer price index, the average national productivity, the labour share in national income and the economic situation. The minimum wage applies to a number of 40 hours worked per week, and if the number of hours worked is less than 40, the minimum wage is reduced proportionately. In 2012, the minimum monthly wage in Spain is 748.3 Euros. The highest monthly minimum wage is paid in Luxembourg, reaching a value of 1,800 Euros, and the lowest is in

Bulgaria (138 Euros) and Romania (161 Euros) (Eurostat, Monthly minimum wages – country-specific information, 2012).

The legal working time in Spain is 40 hours per week, close to the EU-27 average. In the last decade, people have sought to reduce working time in Europe in order to achieve a better balance between work and family life.

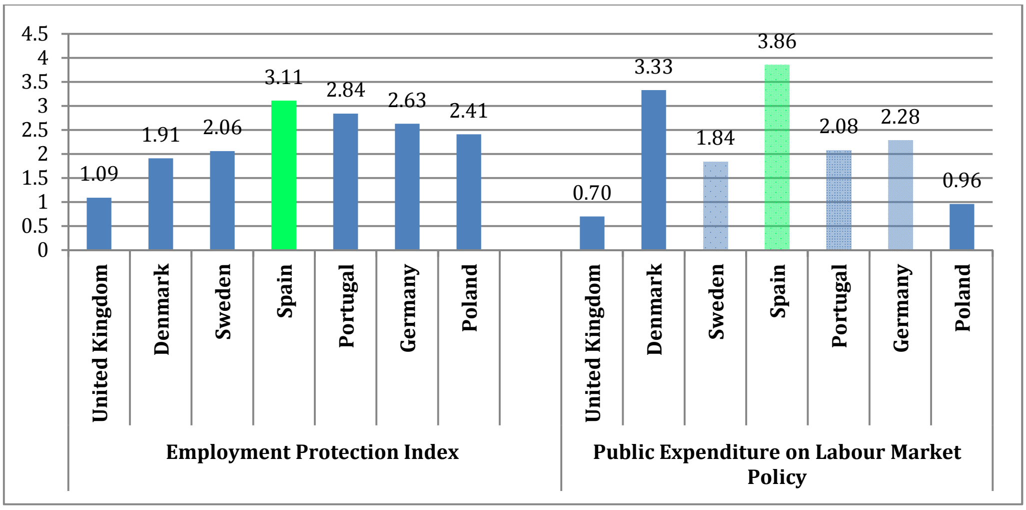
In Spain, employers' organizations and trade unions are not only involved in collective bargaining; they play a key role in social dialogue, having a great ability to influence economic and social policies.

In Spain, hiring and firing are administratively costly and complex because there are many legal forms of employment contracts, each with its own specific rules. There are also numerous lawsuits, which involve additional economic costs.

Labour market reform in Spain intends among other things to reduce employment protection for permanent contracts, as it is the case in most EU countries. This measure could reduce the gap between the two types of contracts (permanent and temporary). However, according to some economists it would not solve the duality problem (Cunat, 2012).

4. Spain's position in the major employment patterns

Analysing the main indicators underlying the employment patterns namely employment protection, generosity of unemployment benefits, expenditure on labour market policies, especially on active policies and tax burden, we can see Spain’s position in relation to the other Mediterranean and European countries.



Source: OECD, 2010 www.oecd.org/employment/employmentpoliciesanddata/42768860.xls & Public expenditure and participant stocks on LMP (Labour Market Policy), 2010, http://stats.oecd.org/Index.aspx?DatasetCode=LMPEXP#

Figure 2. *Employment protection index & public expenditure on labour market policy*

The index of employment protection refers to the protection level of employment, conditions of employment and dismissal. The Mediterranean employment pattern records the highest level of this indicator and the Anglo Saxon and Nordic one the lowest. Among the countries surveyed, the highest value of this indicator is registered by Spain (3. 11). The higher the employment protection index is, the less flexible the regulations on employment are. Thus, according to the data from the figure above, the United Kingdom, Denmark and Sweden register high flexibility in terms of occupational regulation, and Spain registers the lowest flexibility from this point of view.

Regarding public expenditure on labour market policies in recent years, these expenses have increased to support the labour market affected by the crisis. However, some countries have increased expenditures especially on active policies while others have focused on passive policies. Spain is among the countries with the highest values of this indicator; however, with regard to Spain passive measures occupy the highest share in these expenses. The Nordic countries have paid special attention to the active measures, while the Mediterranean countries have considerably increased the costs of passive policies. This may be the result of increasing the number of persons assisted (unemployed), while reducing the volume of economic activity.

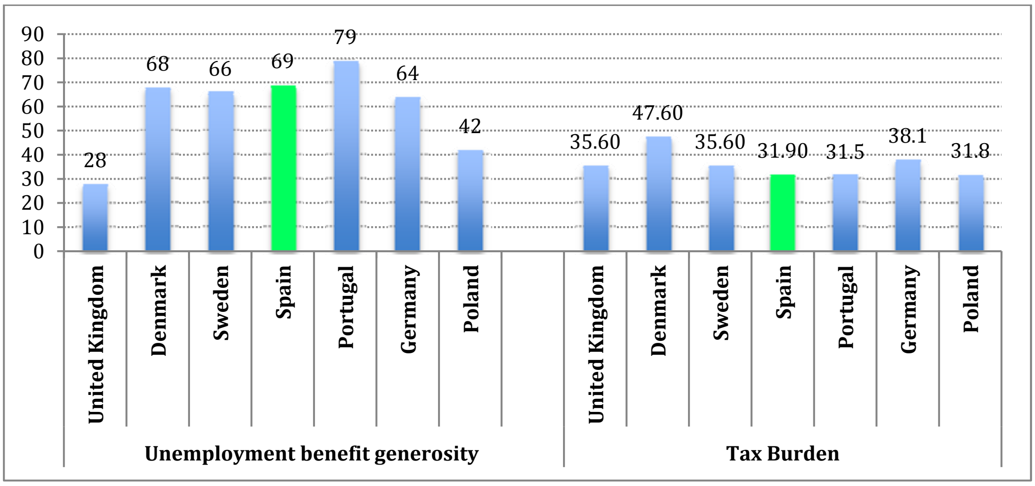
Even though the share of passive expenditure on labour market is high in Spain, there is also a high level of unemployment. The generosity of unemployment benefits, which refers to both the size of unemployment benefits and the granting period, is the highest in Portugal, Spain, Denmark, Norway and the Netherlands.

The duration of unemployment benefit is the highest in Belgium (unlimited time) and Denmark (48 months). In most countries, a social assistance programme follows unemployment benefit.

Spain has a very generous unemployment protection system. In Spain, those who lose their jobs receive 75-80% of the final salary for a period of two years, as *redundancy pay*. After those two years, the unemployed people receive *unemployment benefit* of 600 Euros per month for another nine months. Moreover, those who have not reached the minimum contribution period to have right to unemployment benefit (360 days in the last six years) may apply for *additional unemployment benefits*. Spain's government also extended the life of a 400-Euro monthly payment for jobless people whose unemployment benefits come to an end. There are also other benefits granted such as the active insertion income of 426 Euros per month for long-term unemployed. All these aids are costly for the Spanish economy, especially because some people have chosen to become unemployed or remain unemployed, under crisis, a fact that has reduced the economic activities. These high and long-term aids do not make the unemployed seek work. On the other hand, Spain's economic decline and rising debt in recent years have put pressure on unemployment and increased labour market problems.

The much too generous social protection system definitely needs to be reformed to take into account economic performance, labour productivity and tax level. However, this reform cannot be achieved during the current crisis that is already causing numerous complaints and strikes.

Spain is also facing problems with the banking system, currently pursuing the recapitalization of banks in order to smooth bank loans for both the population and the entrepreneurs. Certain economists (J. Stiglitz) do not see that this measure would have a beneficial result because the Spanish government and banks continue the vicious circle of mutual support.



Source: OECD EMPLOYMENT OUTLOOK, 2010
http://www.oecd.org/social/socialpoliciesanddata/43728718.pdf, &
Taxation trends in theEuropean Union, Eurostat, 2012,
http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2012/report.pdf.

Figure 3. *Unemployment benefit generosity & tax burden*

Tax burden considered as a percentage of GDP shows a high level of taxes especially in the Nordic employment pattern. The lowest tax burden is recorded by the Mediterranean countries. On the one hand, there is a link between the possibility to support labour market policies and the share of taxes as a percentage of GDP, meaning that a high level of taxes increases the support for these policies. This correlation is clearly visible, especially for the Nordic countries, which are recognized as effective in terms of effects of labour market policies, but which are characterized by high tax burden. On the other hand, taxes should not obstruct entrepreneurship and business. In most European countries, taxes have increased in recent years in order to support government expenditures during the current crisis.

Tax burden in Spain is lower than in the Nordic and the continental countries amounting to 31.9% of GDP. Nevertheless, Spain is a country with a generous social protection system, which has become increasingly unbearable, given the current crisis, the high budget deficit and the reduced volume of economic activities.

5. Conclusions

The current crisis has affected different European economies and created bigger and smaller labour market problems, depending on the characteristics of each economy, the economic situation existing before the crisis, the structural characteristics of the economy and the policies adopted to overcome the crisis.

The Spanish labour market has been severely affected by the current crisis, particularly as a result of the structural imbalances in the labour market, of the measures taken to reduce government expenditure, of wage rigidity, of job market duality, of low internal migration, of high immigration, of the much too generous social policies for the unemployed, of a sharp fall in economic activity and of low investment in education and continuous training.

Spain, like other European countries, has applied various austerity measures in order to reduce the effects of the crisis, manifested by reduced government expenditure, reduced wages, reduced public social spending and privatization of public transfers (pension system) or public services (health care).

The austerity measures implemented in Spain, but also in other European countries, are considered by some economists to be counterproductive. This idea is also supported by the economist Joseph Stiglitz, Nobel Laureate, who considers that the excessive austerity “will mean the suicide of the Euro area”. He agrees with budget cuts, but to the extent that they are supported by economic recovery measures. “The measures taken by the EU so far are minimal and in the wrong direction because the austerity measures aimed at risk reduction affect economic growth and increase debt” (J. Stiglitz, Revista Business 24, 2012). For the specific case of Spain, the American economist believes that external funding could allow the development of new industries that would compensate for the gap left by the real estate bubble.

Consequently, future employment policy and labour market reforms to combat unemployment and its persistence must take into account the characteristics and features of each economy. However, the experience of countries that have had success in overcoming the crisis can be used by the countries seriously affected by the crisis, even if a particular employment pattern cannot be fully incorporated.

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