Spanish labour market still very tight, but a turnaround is in the making

The Spanish unemployment rate rose slightly to 12.7% in the third quarter, but is still very low. However, a sharp decline in hiring intentions shows that a cooling-off in the labour market is on the way. We expect unemployment to rise further in the coming quarters due to the deteriorating economic outlook, peaking at 14.3% in the third quarter of next year

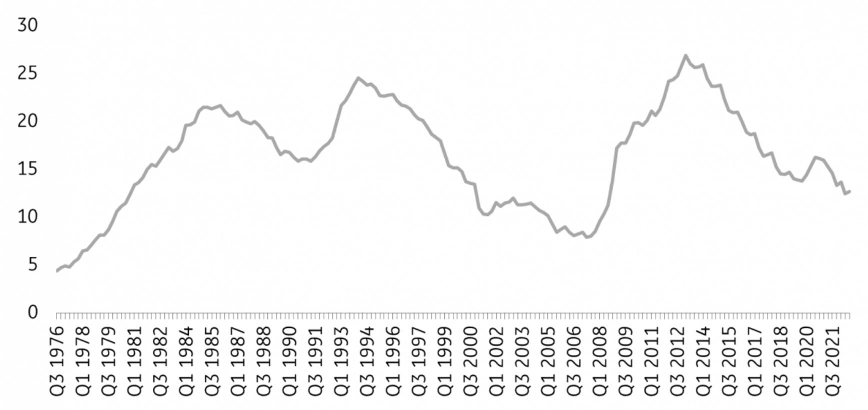
We expect unemployment to continue to rise in the coming quarters due to deteriorating economic conditions

Unemployment rate slightly up in the third quarter

According to INE figures released this morning, unemployment rose to 12.7% in the third quarter from 12.5% in the second quarter. With the exception of the previous quarter, this still puts unemployment at its lowest level since the third quarter of 2008, the start of the financial crisis. Although the unemployment rate is historically low, it is still well above the euro average. Eurostat's harmonised figures, which differ slightly from those published by INE, show that Spain's unemployment rate was 12.4% in August, compared with the eurozone average of 6.6%, a difference of 5.8 percentage points. For under-25s, the deviation from the eurozone average even runs to 12.7 percentage points. This average harbours large differences between regions. In the south of the country (Andalusia, Extremadura, Murcia etc) unemployment is typically above the national average, while the northern regions (Cantabria, Navarre, Catalonia, and so on) pull the average down a bit.

We expect unemployment to continue to rise in the coming quarters due to deteriorating economic conditions. We predict that the Spanish economy will enter a mild recession starting in the fourth quarter of 2022 that will continue until the first quarter of next year. This will put some upward pressure on unemployment rates. Since unemployment rates usually lag somewhat behind the economic cycle, the biggest impact will be next year. We think that Spanish unemployment will peak at 14.3% in the third quarter of 2023.

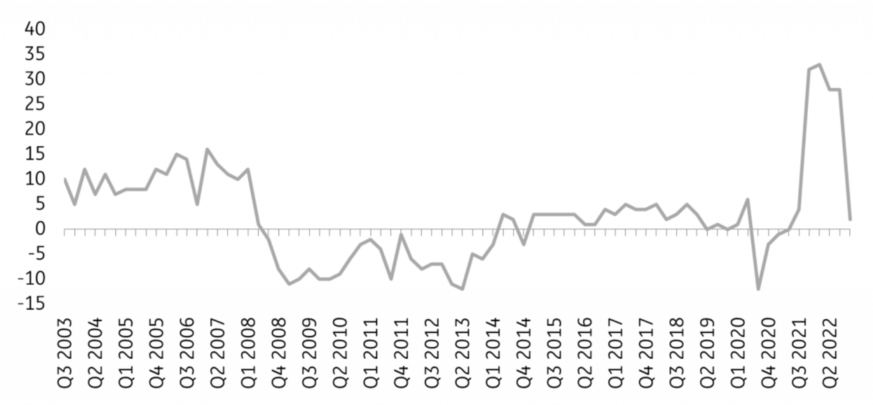
Unemployment rate, 1976-2022



Hiring intentions dropped sharply

Although the labour market is still very tight, more signals point to a cooling in the coming months. The 12-month moving average of the number of vacancies has been stabilising for several months and seems to be at a peak. Business confidence has also deteriorated sharply in recent months, which will encourage companies to be more careful with new hires. This is already reflected in the latest Manpower survey, which polls every three months on the hiring intentions of companies. The latest results polling hiring intentions in the fourth quarter of 2022 show the largest quarterly decline in the index since the start of the survey in 2003. Although the index was historically high, this points to a turnaround in the labour market. The deteriorating economic outlook is already causing companies to be more cautious about hiring new people.

Manpower survey – hiring intentions in the next three months, 2003-2022

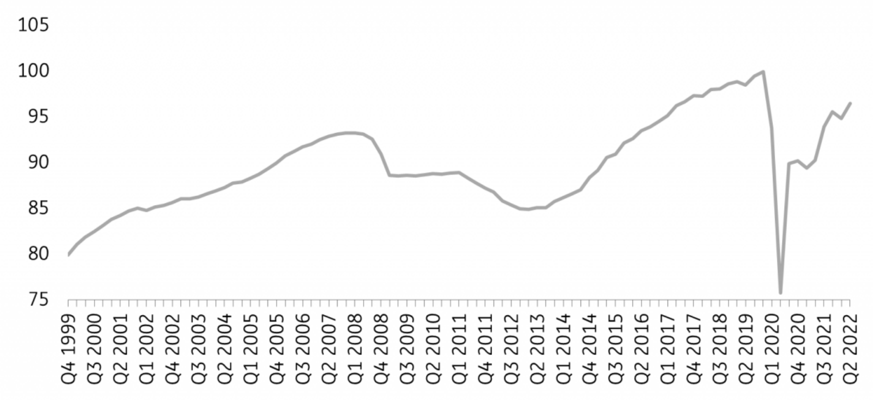


A cooling economy will take longer to restore productivity to pre-Covid levels

GDP per person of working age, a good measure of an economy's productivity, is still below its pre-Covid levels. Since 2014, following the financial crisis and debt crisis, the productivity parameter was on a strong remount. Between 2014 and 2019, GDP per working age population rose by an average of 2.6% per year. This came to an abrupt end with the onset of the Covid-19 pandemic. In the first two quarters of 2020, GDP per person of working age fell 24.2% from the last quarter of 2019 due to a sharp drop in activity. Afterwards, the measure recovered strongly. In each of the past three quarters, it grew more than 6% year-on-year but is still 3.5% below its 4Q19 pre-Covid levels.

However, this increase is likely to be strongly driven by the activation of lower-productivity workers. This pushes GDP per person of working age higher, but puts pressure on real labour productivity per hour worked. We see that the latter has been under strong pressure since the beginning of this year (-3.1%). The end of Covid restrictions has allowed a lot of employees in the tourism and hospitality sector to get back to work, but these are typically employees who contribute relatively less to GDP. The tight labour market also makes it easier for less skilled and recent graduates to find a job – in general, these are also people with lower productivity. With activity again under strong pressure from the energy crisis and high inflation, productivity is likely to fall. Over the winter months, we forecast a contraction of 0.8% in the Spanish economy. As a result, it will probably take until 2024 before GDP per working age person returns to its pre-pandemic level.

Productivity – GDP per working age population, Q4 2019 = 100

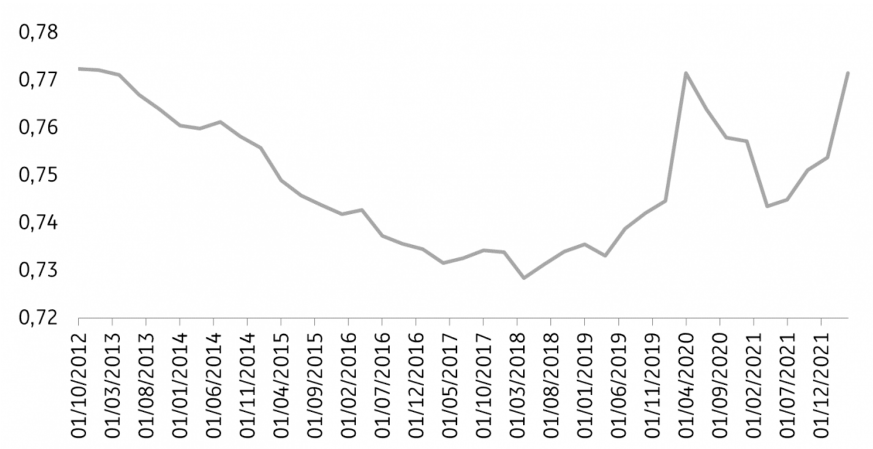


Spanish labour market supported by strong growth in open-ended contracts

The high number of temporary contracts in Spain has long been one of the weaknesses of the Spanish labour market. According to Eurostat data, about 22% of Spaniards were on temporary contracts before the pandemic, compared to an average of 14.4% in the EU. However, the number of open-ended contracts has increased over the past year. The number of permanent employees reached a record high in the second quarter to 13.5 million employees (seasonally adjusted figures), an increase of 8.7% compared to the second quarter of last year. The number of employees on temporary contracts has fallen by 6.7% in the past year to just over four million. The increase started in the middle of last year but was accelerated by the labour market reform approved by the government in December. The share of permanent contracts has increased by three percentage points in one year, from 74% in the second quarter of last year to more than 77% in the second quarter of this year.

It is too early to estimate the long-term effects of the labour market reform, but we can already say that the reform, which imposes additional restrictions on the use of temporary contracts, has resulted in many temporary contracts being converted into open-ended contracts. These also offer better protection during economic headwinds. A higher share of permanent contracts is also likely to mean that the rise in the unemployment rate, which usually follows a fall in economic activity, will be less pronounced than during previous recessionary periods.

Share of permanent contracts



Bleak economic outlook will lead to higher unemployment rate

All in all, despite a slight rise in the unemployment rate in the third quarter, the labour market remains very tight. The bleak economic outlook, which is already prompting companies to be more cautious about new hires, will ease the pressure on the labour market in the coming months. We expect the unemployment rate to rise further to 14.3% in 3Q23, partly held back by a higher number of permanent contracts, before slowing down again.