

Spanish Labour Market Monitor

Presentation

The March employment data, though not good, do not signal as decidedly as those of January and February a return to the pattern of severe deterioration observed in 2009. Even so, this does not mean that it has not been a terrible first quarter for the labour market, which will be reflected as such in the EPA labour force survey in a few weeks time (we expect employment to have fallen by more than 400,000 and a rise in the unemployment rate to levels of 24.6%). Neither do they signal a recovery in the labour market, even in seasonal terms, as the public sector spending begin to materialize following the publication of the national budget.

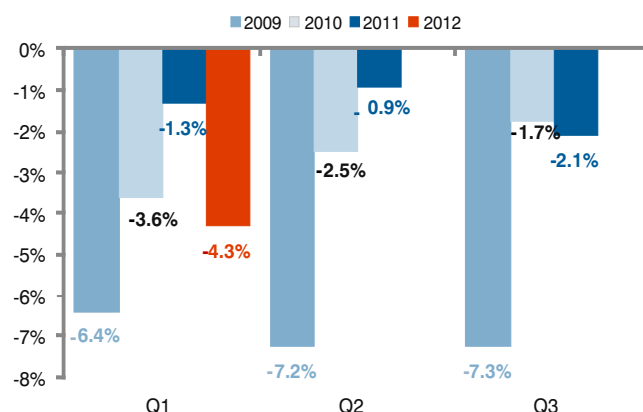
Key Points

- The March employment data mark a break with the negative pattern of the first two months of the year, but not sufficiently to prevent falls in Social Security enrolment and increases in the number of unemployed of more than 300,000 in 1Q12, which could result in a decline in EPA employment on the order of 436,000.
- Registered unemployment increased by 38,769 in March, with all sectors contributing, especially services and those without previous employment.
- Social Security enrolment increased slightly in March, by 5,400, a negligible number when compared with the monthly increase of a year ago, and not enough to compensate for the poor performance in the first two months of the year.
- 1Q12 ends with unemployment up 328,500 and enrolment down 327,400 compared with the previous quarter, figures only exceeded by those registered in 1Q09.
- The number of labour contracts signed is still falling at double-digit YoY rates. Permanent contracts mitigated their YoY decline, with the fall in temporary contracts gaining strength.
- The number of self-employed enrolments increased slightly in March, although the balance of 1Q12 remains negative (20,800 down since the end of 2011).
- It is noteworthy that the unceasing rise in the unemployment rate (to over 21% in 2011), has been accompanied by sustained growth in labour costs.
- The pace of growth in labour costs has slowed significantly over the last decade.
- In 2011, labour costs continued to increase (by 2.2% annually), with all their components having contributed to this.
- Severance payments account for an important part of the increase in labour costs in 2011, especially in sectors such as finance and insurance (reflecting the restructuring process in banking).
- The labour cost per hour is higher in those regions with a greater proportion of skilled workers.
- The regions with lower labour costs are also those that recorded the largest increase in 2011, with the "other costs" category being particularly relevant.

Afi-Agett SLM Indicator

The fall in Social Security enrolment in the first quarter of 2012, substantially higher than in the previous years of the crisis, except 2009, suggests a loss of EPA employment on the order of 436,000 (4.3% YoY). Even if the labour force continues to decline at a YoY rate similar to the previous quarter (0.102%), the number of unemployed will register a significant increase (394,000), taking the unemployment rate to levels of 24.6%.

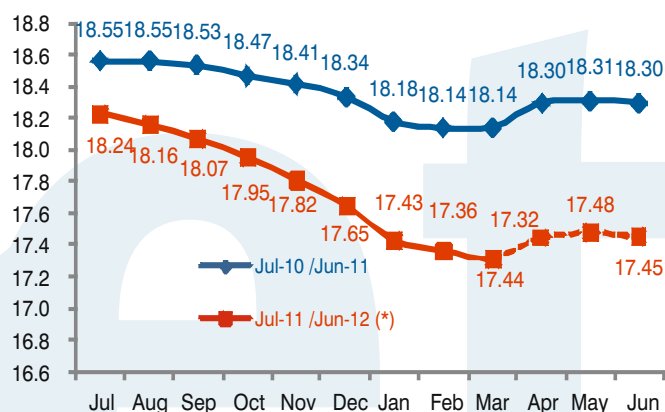
Change in EPA employment



Source: EPA (INE) and Afi forecasts

The favourable seasonality of the spring months should partially offset the deterioration in employment expected in the sectors most affected by the public spending cuts. The Afi-Agett SLM Indicator reflects this, with monthly increases in employment until May, but in any case insufficient to take aggregate employment back to the levels of end 2011.

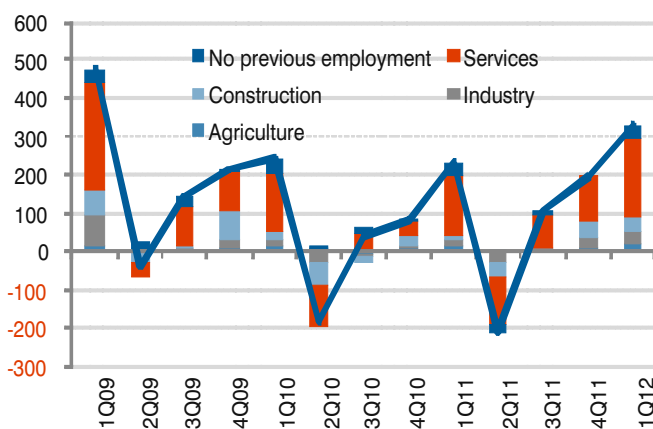
SLM monthly forecast of workers in employment (millions)



Source: Afi. (*) Apr-Jun 2012 figures are forecasts

"The March employment data, though negative, do not continue the strong deterioration of the first two months of the year, but neither will they prevent falls in Social Security enrolment and increases in unemployment of more than 300,000 in 1Q12"

Quarterly change in unemployment by sector



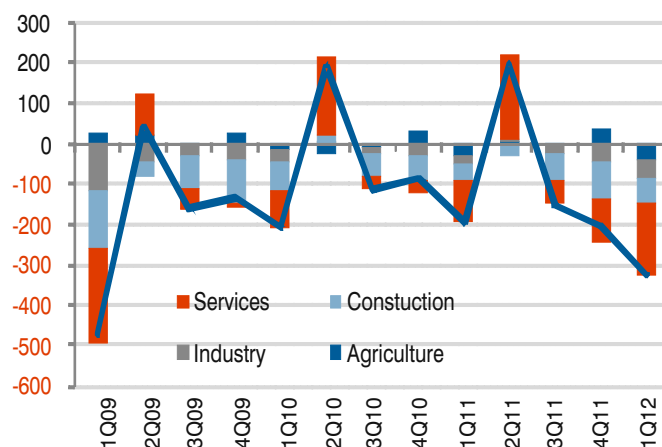
Source: Ministry of Employment and Social Security

Registered unemployment increased by 38,769 in March, slowing the rapid pace of deterioration in the first two months of the year. Nevertheless, 1Q12 ended with 328,500 more unemployed than in the previous quarter, a figure only surpassed by 1Q09. **All sectors of activity contributed to the monthly increase, but the bulk was concentrated in services and those without previous employment**, with rises of 15,062 and 11,393 respectively. In industry and construction the declines have moderated, thus conforming less closely to the pattern seen in 2009. However, this is not true of services. This situation will worsen as a result of the budget restrictions and will only improve, in part, thanks to the seasonably favourable period now beginning (Easter Week and the pre-holiday period).

"Social Security enrolment increased slightly in March, up 5,400, a negligible number compared with monthly increase of a year ago, and not enough to compensate for the poor performance in the first two months of the year."

Social Security enrolment, in turn, increased slightly in March, with the system gaining 5,419 additional contributors. This is a negligible number compared with the increase of 45,660 in March 2011, and insufficient to compensate for the fall seen in January and February 2012. 1Q12 ended with enrolment down 327,400 on the previous quarter, a quarterly fall that, like the increase in unemployment, is exceeded only by 1Q09. One factor clearly missing this year has been the boost to tourism recorded last year due to the "Arab spring". Even so, it was hotels and catering which underpinned the increase in Social Security enrolment in March (25,700), while manufacturing industry led the decline (10,900). Lastly, the number of companies registered with the Social Security decreased by 36,852 in March, a YoY decline of 2.56%, the biggest fall since May 2010.

Quarterly change in Social Security enrolment by sector



Source: Ministry of Employment and Social Security

"The number of labour contracts signed is still falling at double-digit YoY rates. The number of self-employed enrolled increased slightly in March, although the balance of 1Q12 remains negative (with a fall of 20,800 since the end of 2011)."

Change in Social Security enrolment: total, wage workers and self-employed



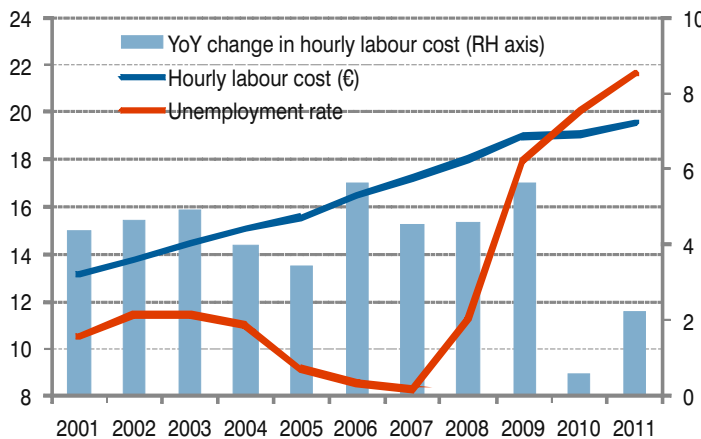
Source: Ministry of Employment and Social Security

Contracts signed in March still show strong declines, specifically 11.09% YoY. On this occasion, however, permanent contracts mitigated their YoY decline (to 11.37% in March, half the rate observed in January and February), while the fall in temporary contracts accelerated, with a YoY decline of 11.06%, three times faster than that observed in January-February. Lastly, **the number of self-employed enrolled in the Social Security, which has fallen less than that of salaried workers since the beginning of the crisis, recorded a slight improvement in March, with an increase of 4,800.** However, the balance of 1Q12 remains negative, with a fall of 20,800 since the end of 2011.

"Labour costs do not cease to grow: in 2011 they increased by 2.2% compared to 2010, with all their components having contributed to this."

In a moment of crisis like the present, there are main two ways in which the labour market of an economy can adjust: via quantities (increased unemployment) and/or prices (reduction of labour costs). In the case of Spain, it is noteworthy that the unceasing rise in the unemployment rate (above 21% in 2011) has been accompanied by sustained growth in labour costs.

Hourly labour cost (in € and YoY change) and unemployment rate



Source: National Statistics Institute (INE)

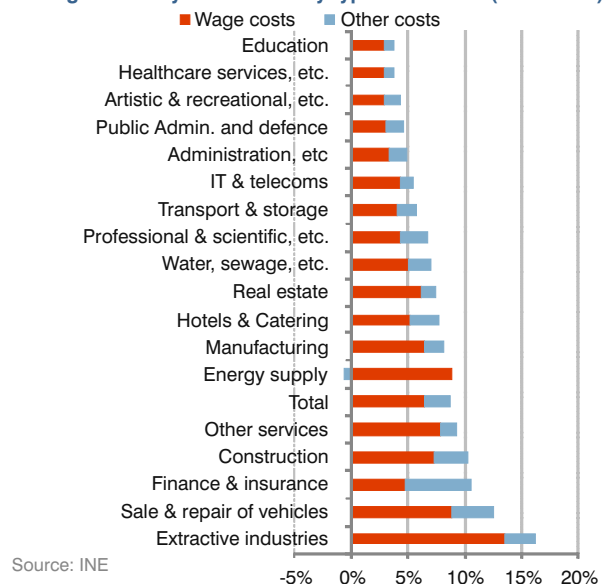
Nevertheless, it is true that the **pace of growth in labour costs over the last decade has slowed significantly**. In the 2001-2007 period, coinciding with the expansionary phase of the business cycle and hence with low rates of unemployment, labour costs were growing at an average annual rate of 4.6%. However, with the outbreak of the crisis and its aggravation, the annual increase recorded in 2010 was only 0.6%. **In 2011, labour costs again increased (by 2.2%), with all their components having contributed to this, although at a much lower pace than in the pre-crisis years.** This progressive increase, which represents an accumulated 48%, means that the labour cost per hour worked has risen from an average €13.2 in 2001 to €19.6 in 2011.

"Severance payments are largely responsible for the increase in labour costs, especially in sectors such as finance and insurance (reflecting the restructuring process in banking)".

Between 2008 and 2011, labour costs increased by 8.6%, with 6.5 percentage points being attributable to the increase in wage costs (regular wages, overtime pay and back pay) and the rest to "other costs" (Social Security contributions paid by the employer, non-wage remuneration such as compensation for dismissal, and subsidies and bonuses). The greater significance of the first category is due both to the fact that it has grown as rapidly as the second (8.7% and 8.3%, respectively), and to its greater share of the total (in 2011, for example, wage costs, including "13th month" payments and arrears, made up 74% of the total).

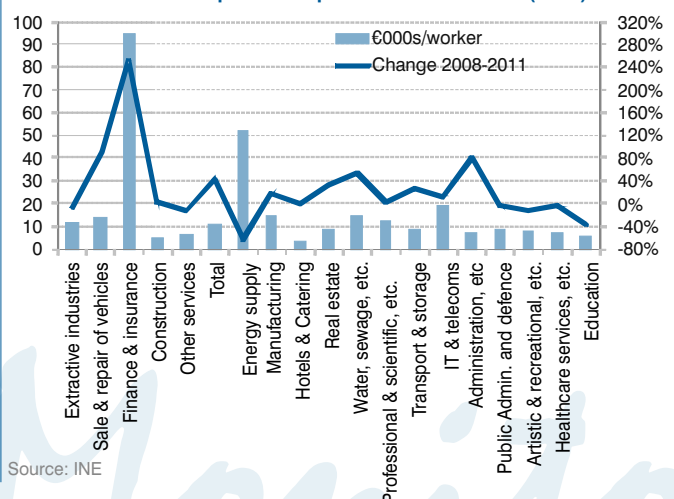
There are wide variations in the behaviour of labour costs between sectors. On the one hand, **extractive industries, trade and repair of vehicles, financial and insurance activities, and construction recorded cumulative increases in labour costs of more than 10%**. Of these sectors, two require explanation. On the one hand, in finance and insurance more than half of the increase in labour cost was due to "other costs", closely related to the banking restructuring process (cost of early retirement schemes). In fact, it is the sector with the highest severance pay costs (€94,000 per worker) and in which it has increased most compared to 2008 (up 252%). On the other hand, it is surprising that a sector like construction, which has seen an unprecedented fall in its productive capacity, has recorded an increase in its labour costs, even though it has one of the lower dismissal costs per worker. On the other hand, there are sectors such as education and health, where the cumulative increase in labour costs from 2008 to 2011 has been less than 5%.

Change in hourly labour cost by type and sector (2008-2011)



Source: INE

Cost of compensation per worker dismissed (2011)

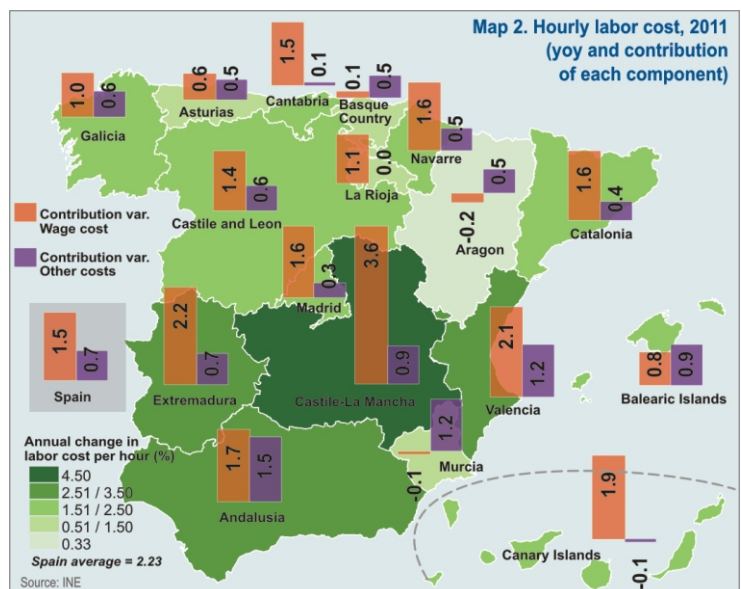
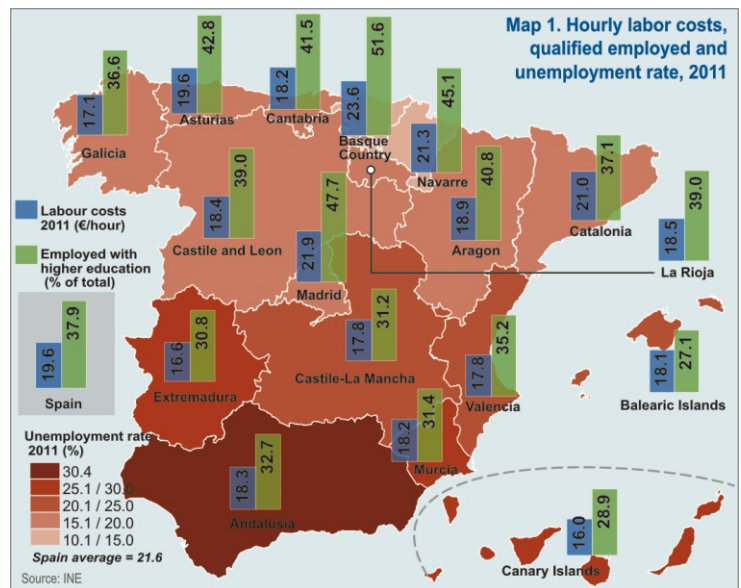


Source: INE

"The labour cost per hour is higher in those regions with a greater proportion of skilled workers. The regions with lower labour costs are also those that recorded the largest increase in 2011, with the "other costs" category being particularly relevant.

The labour cost is a function of workers' skills, among many other aspects, so that the better their education and training, the higher their productivity and, therefore, the labour cost to be borne by the employer. The same behaviour is observed when analysing regional differences in labour costs. In 2011, **the regions with higher labour costs per hour were those where a higher percentage of the employed population is qualified**, in the sense of having higher education (i.e. university degree or PhD). Thanks to this higher productivity and the better training of their employed population, they also present some of Spain's lowest unemployment rates. This is the case of the Basque Country, Navarre and Madrid. Total labour costs in these regions exceed €21 per hour, because more than 45% of the employed population possesses high qualifications and, despite this, they have unemployment rates below 17%.

At the other extreme are **Castile-La Mancha, Valencia, Andalusia and Extremadura**, because in addition to having some of the lowest labour costs in Spain, they are the regions where they have increased most since the previous year. In fact, the first two of these regions are the only ones where labour costs have also risen in real terms (that is, discounting regional inflation), by 1.3% and 0.1%, respectively. **Although wage costs are the biggest contributor to this variation, the "other costs" category, which includes severance pay, acquires greater significance in these regions.** The case of Murcia, for example, though one of the regions where labour costs have been more contained, stands out as the region where almost all the variation in labour costs has been due to the increase in non-wage "other costs".



THE MONTHLY FOCUS

It's the competitiveness...

The punishment suffered by our labour market is unceasing. The March data brought to an end a very bad quarter which recalls the pattern seen in the worst moments of the crisis, between 2008 and 2009. As we continue to traverse this situation, however, the various indicators are warning us of the lack of progress in those factors which would provide a basis for recovery. Such is the case of competitiveness. Between 2008 and 2011, labour costs rose by more than 8%, and wage costs by more than 6%. These are not good figures, especially if we consider that, in certain sectors and regions most affected by the crisis and unemployment, labour cost increases have been even higher. The labour market reform has a difficult road ahead; its achievement, if finally successful, should be to facilitate the improved competitiveness of business, to stabilize company workforces, and thus to promote an economic recovery with a high employment content.

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