

Assessing the impact of the 2012 labour market reform in Spain

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Paris, March 14th, 2016

Main Objectives & Measures (I): COLECTIVE BARGAINING

1. OBJECTIVE: Labour costs reduction to implement “*internal devaluation*” (promote wage moderation).
 - **Collective Bargaining Agreements (CBA) at the Firm level get priority**
 - **Firms can opt-out more easily** from CBA
 - Expired CBA can now be **extended for a maximum period of one year**
2. OBJECTIVE: To promote internal flexibility helping firms use other ways (rather than external flexibility) to adjust when hit by adverse shocks.
 - Employers can **unilaterally change working conditions** (wages, working hours, work schedules) whenever there are objective reasons

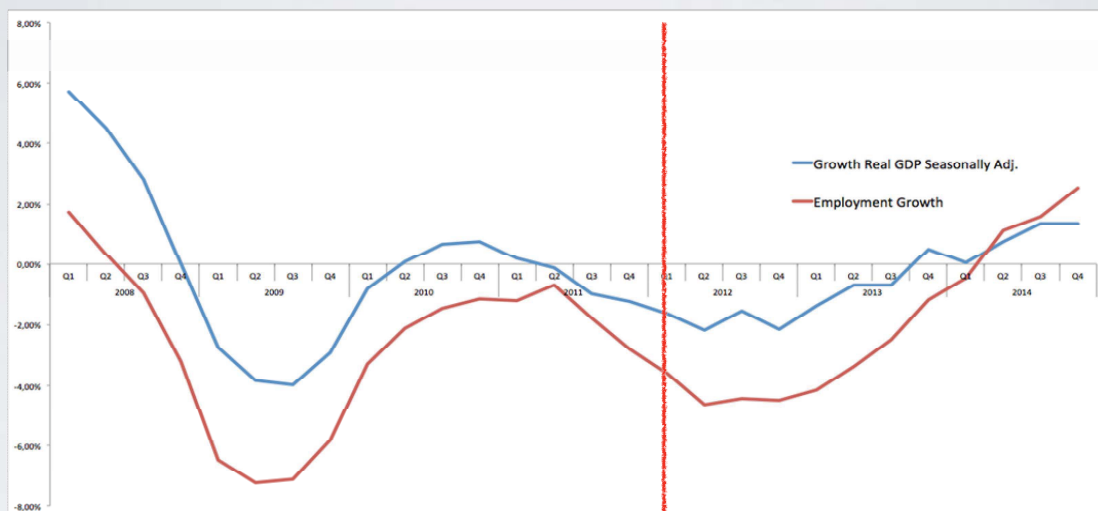
MAIN OBJECTIVE: To reduce DUALITY

1. Extension & clarification of **objective dismissals** (20 days – max 12 months).
 - Dismissal is always justified if the firm faces a persistent (3 consecutive terms) decline in revenues/sales/profits.
2. Reduction of severance pay for **unfair dismissals** (from 45 days to 33 days)
3. Elimination of **procedural or interim wages**.
4. **Increase in termination compensation for temporary workers at end of TC** remains as in 2010 reform (from 8 days to 12 days)
5. **Collective dismissals** no longer require ex-ante administrative approval.
6. A **new full-time permanent contract for small firms** (under 50 employees) is introduced: it allows for an extended trial period of one year and it entails important SS rebates & subsidies.

Short-run Outcomes (WARNING)

The evaluation of the labour reform is a difficult task:

1. comprehensive nature
2. approved in the middle of a double-dip recession

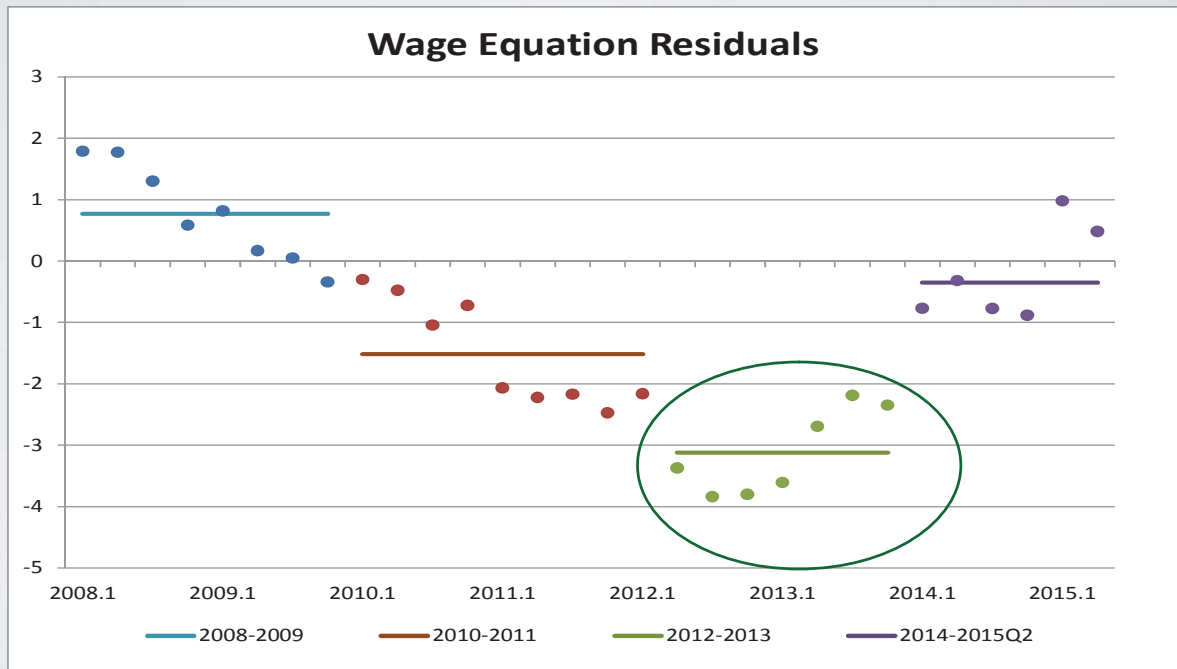


OECD (2014) Evaluation results (with just 10 months):

- The reform promotes hiring (in particular for permanent contracts).
- The reform does not seem to have affected much firing decisions.---

Short-run Outcomes: Collective Bargaining & Wages

- Wage moderation has exceeded predictions of conventional wage equations...



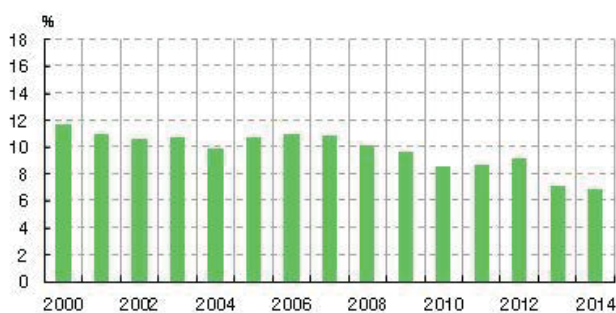
$$\Delta W_t = \alpha + \beta * CPI_{t-1} + \lambda * \Delta U_t + \omega * \text{Labor Prod}_t$$

Source: National Accounts data from 1981Q1 -2014Q4

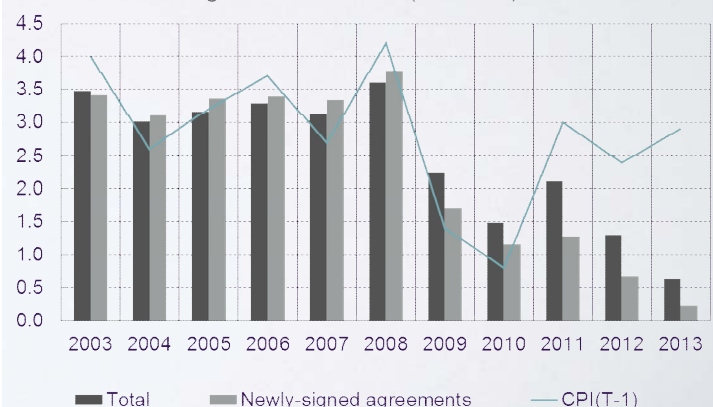
First Outcomes: Collective Bargaining & Wages

- Bank of Spain's (2013) report concludes that the 2012 reform has had a moderate impact on collective bargaining:
 - Lower coverage.
 - Not much change in the prevalence of sector agreements.
 - Fall in indexation clauses.
- But Font, Izquierdo & Puente (2015) point out that wage sensitivity to unemployment increases after 2012 (-0.13 vs. -0.26) .

Workers under Firm Collective Bargaining Agreements

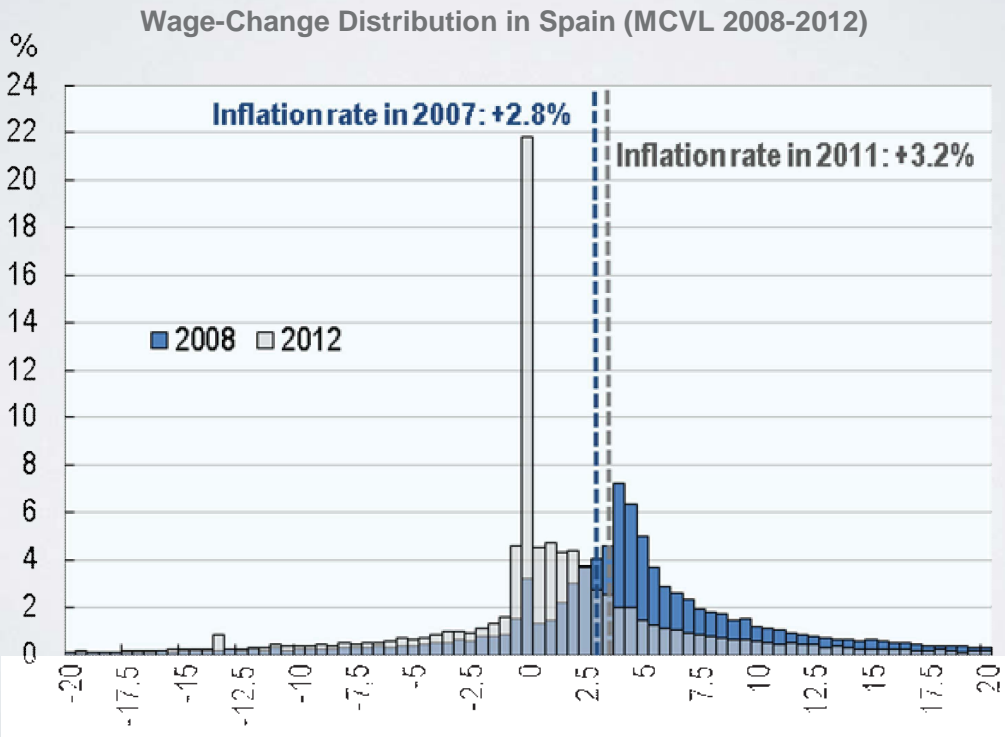


Wage rate increases (from CB)



First Outcomes: Collective Bargaining & Wages

- The “internal devaluation” process in Spain has been very intense: incidence of nominal wage cuts increased from 13% to 24%, while the incidence of wage freezes increased from about 3% to 22%.



First Outcomes: Employment Protection Legislation

Protection of permanent workers against individual and collective dismissal: 2008 vs 2013



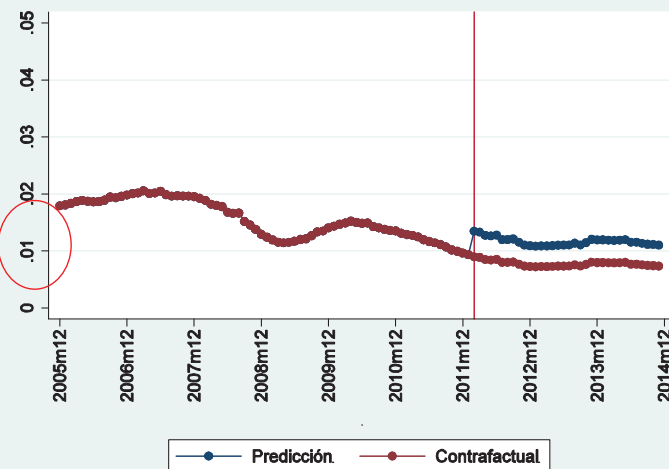
EPL has decreased according to standard OECD indicators

First Outcomes: EPL- Duality

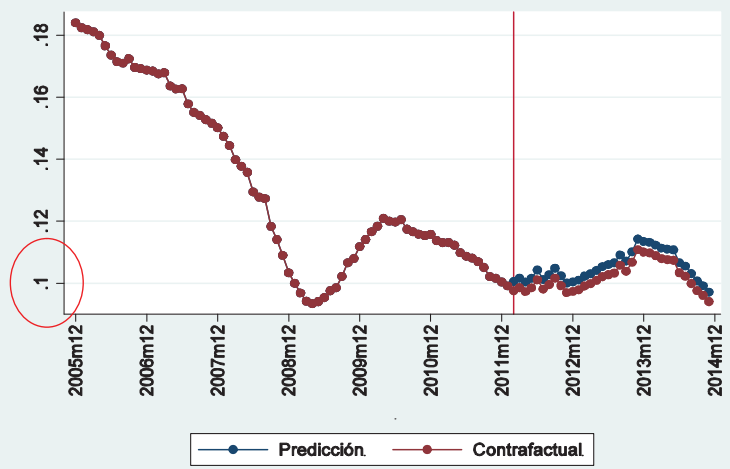
García-Pérez (2016): About 1/3 of the reduction in U during 2012-2015 is due to the reform

- The monthly exit from Unemployment to Permanent Employment has increased from 1.7% to 2.6% (first 12 months) due to the reform.
- The exit from Unemployment to Temporary Employment remains at the same level (11.8%).

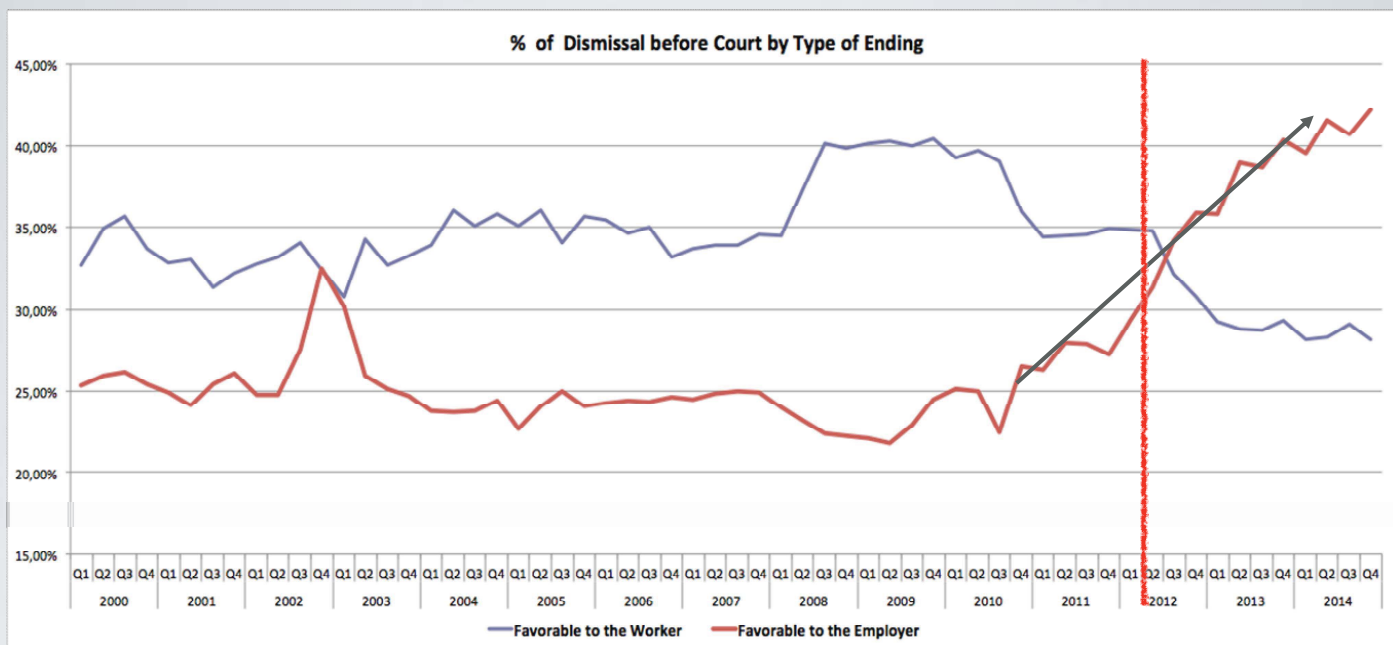
Exit to Permanent Empl. (average)



Exit to Temporary Empl. (average)



First Outcomes: Dismissals



- There seems to exist a huge increase in Court decisions in favor of employers.
- But only 2.5pp (out of a 12pp increase) can be attributed to the reform (Bank of Spain, 2015).

Which lessons can be drawn?

FOR THE DEBATE

Judges and Courts can devirtualize the 2012 Labor Reform

1. Collective Dismissals (CD) no longer require ex-ante administrative approval. However:
 - The reform reintroduces nullity. Judges are declaring null collective dismissals due to procedural mistakes. (53 out of 111 first CD have been declared null).
2. The EPL reform is being “slowly” implemented by Labour Courts:
 - The strategy of the 2010 & 2012 reforms, focused on changing the legal definition of fair economic redundancies, has not fully delivered a substantial reduction of "effective" firing costs.
 - According to Jimeno et al. (2016) the fraction of dismissals being declared fair by labour courts is basically the same before and after 2012.

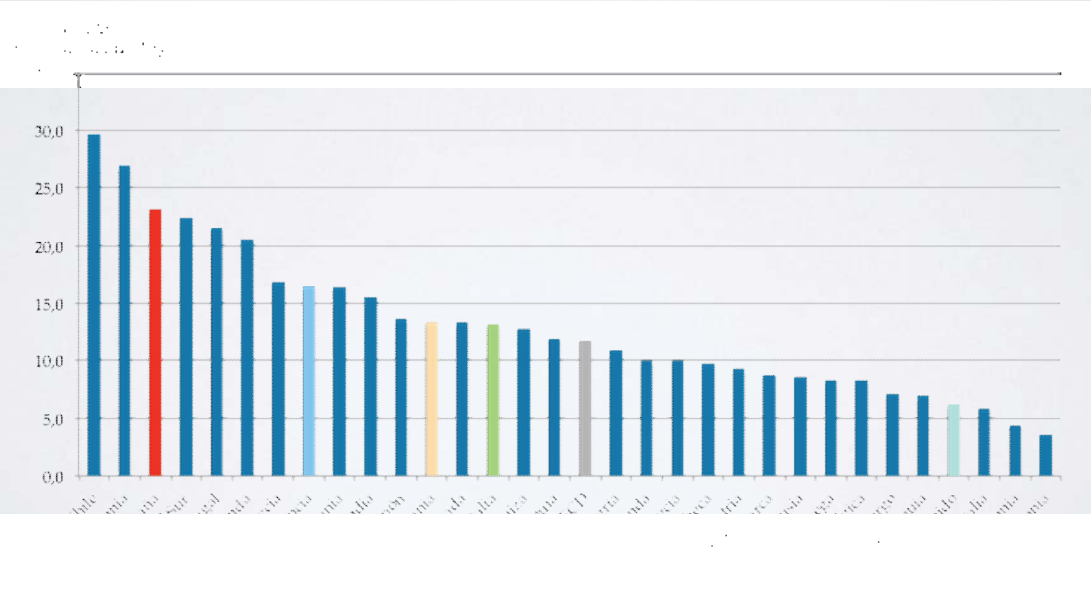
Which problems will the next generation of reforms have to address?

Duality and ALMPs

Measures to solve the Duality...

The high and unjustified rate of temporary employment is the main problem of the labor market in Spain.

- It is inefficient because it does not encourage the accumulation of human capital.
- It is also unfair because it prevents youth from leaving the nest and low-skilled workers from forming households (fertility decisions) ➔ **TCs are a source of inequality.**



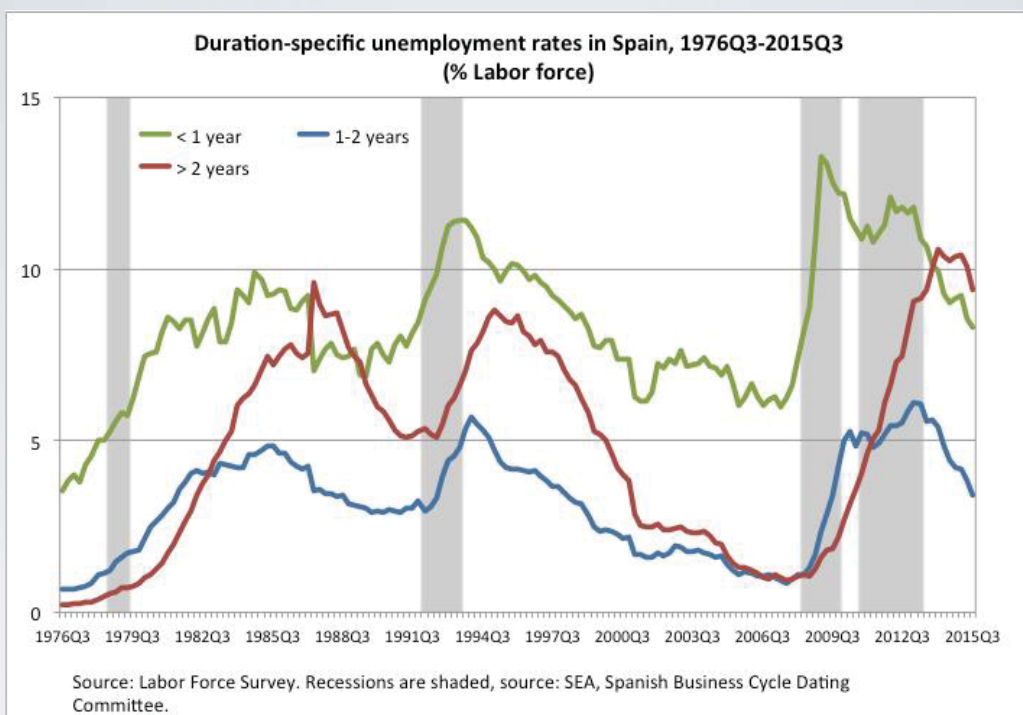
Measures to solve the Duality...

- The best and more efficient way of reducing duality is by reducing the gap in EPL (severance payments + red tape litigation costs)...
- A SINGLE CONTRACT (or MUCH BETTER AN **Unified Severance Payment system for all contract types**) is needed:



➔ Severance payments should smoothly increase with seniority for ALL new hires (independently of the contract type)

... and long Term Unemployment (LTU)



BENTOLILA, GARCIA PEREZ & JANSEN (2016): Chances of entering LTU are quite high and alarmingly so for very long LTU, which has doubled from expansion to recession (27.7% vs. 49.0%) ➔ **ACTIVE LABOR MARKET POLICIES are urgently needed!!**

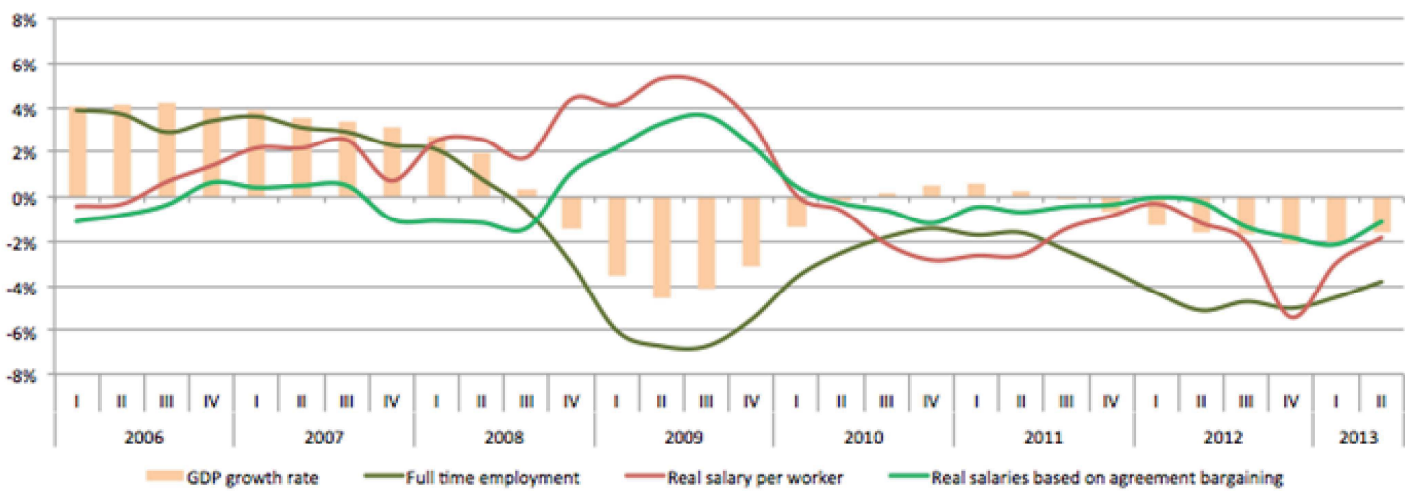
SOME QUESTIONS FOR THE DEBATE

- 1) Why did Spain choose this kind of reforms?
 - We need to adjust **prices instead of quantities**.
- 2) In which sense was the Spanish labour market reform *successful*?
 - Reduction in labour costs: **SUCCESSFUL** – Reduction in duality: **FAILURE**
- 3) The desirability of an internal devaluation: **IN 2012 AND NOW**
 - Maybe required to get out of the crisis but now a different policy to sustain growth is needed
- 4) Should we be concerned about the resilience of dualism? **YES!!**
- 5) Why is it so difficult to overcome the *status quo*? **INSIDERS vs. OUTSIDERS**
 - The political equilibrium: Political parties + Unions + Employers' organizations
 - The role of education: who understands a dynamic or a stochastic problem??
- 6) What about inequality.....and productivity? **Crucial for the future**

Main Labor Market Challenges before 2012

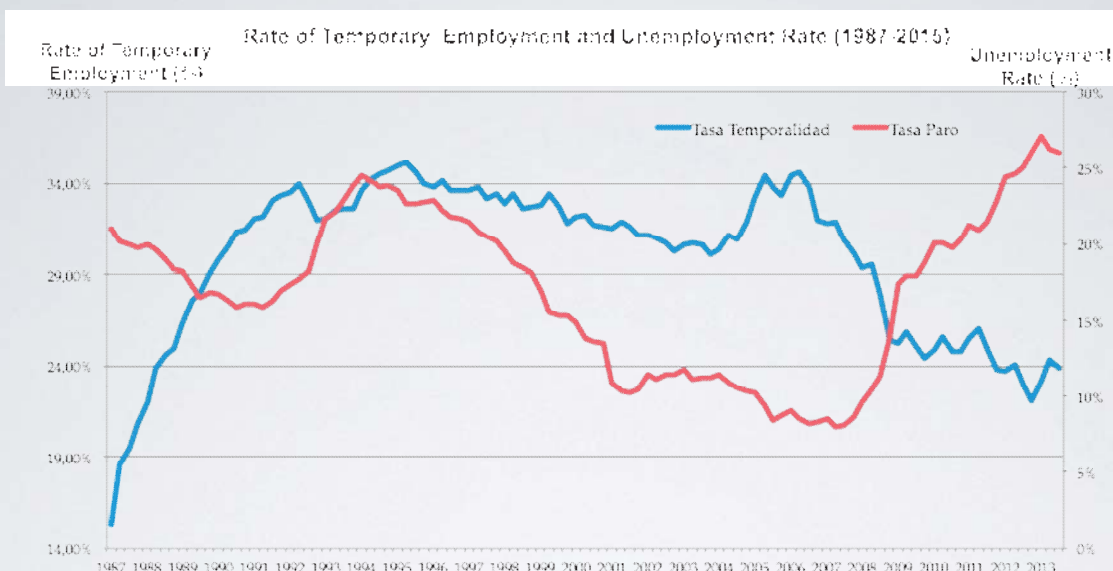
(NOT TO BE SHOWN)

Lack of Internal Flexibility



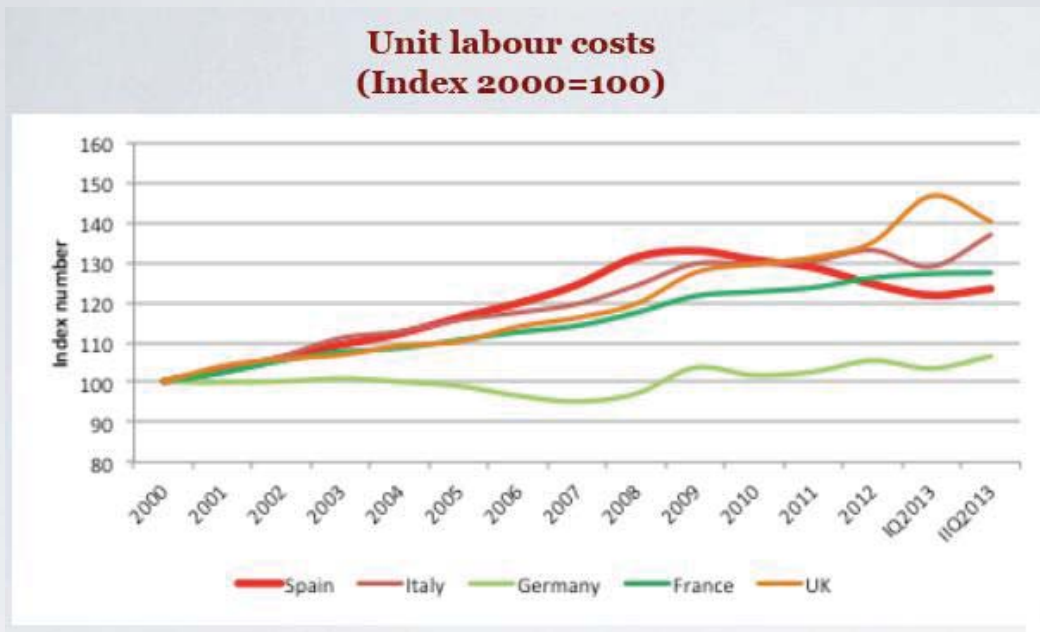
- Labour market adjusted through **QUANTITIES** (i.e employment) instead of **PRICES** (i.e wages).
- Very rigid collective bargaining:
 - Too centralized in some cases.
 - Insufficiently coordinated in others.
 - Almost total lack of firm-level bargaining.

Dual Labor Market



- **High employment volatility** generated by a dual labor market with about 1/3 of temporary workers.
- In economic booms this model generates strong job creation, albeit concentrated in low-productivity industries, whereas in recessions it exacerbates job destruction.
- Firms respond to economic fluctuations through labor turnover, rather than looking for alternatives such as changes in workplace organization or wages.

Lack of competitiveness



- The **wage bargaining system** was very inefficient.
- Nominal wages grew with nominal GDP rather than productivity, leading to higher unit labor costs.
- Lack of sectorial competition.