

Box 8

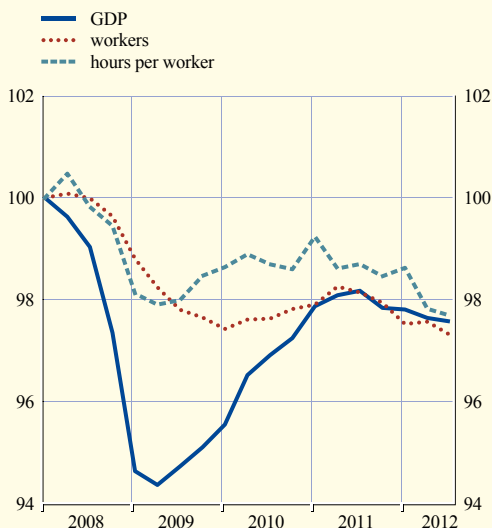
UNEMPLOYMENT DEVELOPMENTS IN THE EURO AREA

The situation in euro area labour markets has worsened significantly since the start of the economic and financial crisis in 2008. After reaching a record low of 7.2% in February of that year, the unemployment rate for the euro area rose to an all-time high of 11.7% in December 2012. Young and low-skilled workers have been severely hit by the crisis, although a substantial degree of heterogeneity is found across euro area countries. This box describes developments in unemployment, particularly youth unemployment, in the euro area since the start of the crisis and points to the need for further structural reforms and policy action to address the situation.

Until early 2009, headcount employment adjustment at the aggregate euro area level was relatively muted in comparison with the fall in GDP. This development mostly reflected labour hoarding in several euro area countries,

Chart A Cumulative changes in euro area GDP, number of employees and hours worked per worker

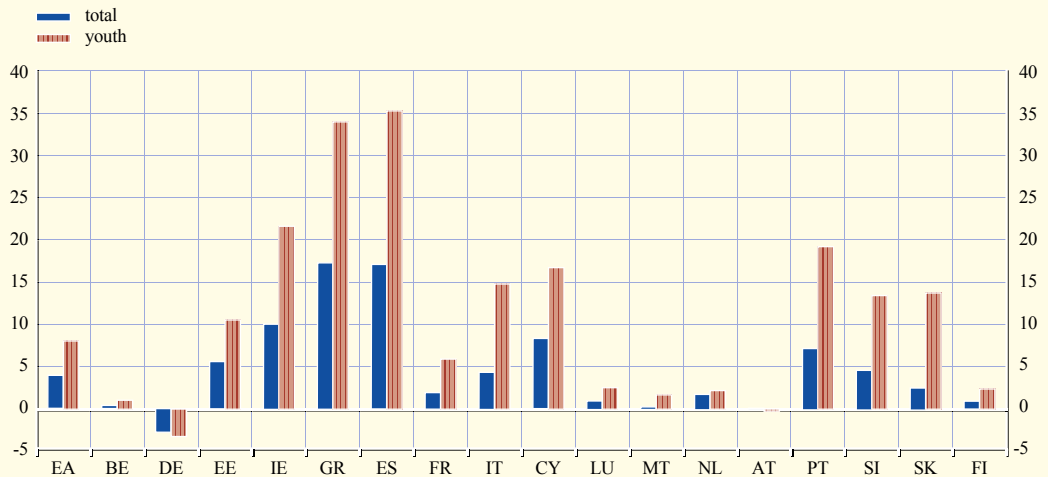
(index: Q1 2008 = 100)



Sources: Eurostat and ECB calculations.

Chart B Changes in unemployment rates between the third quarter of 2007 and the third quarter of 2012

(percentage points)



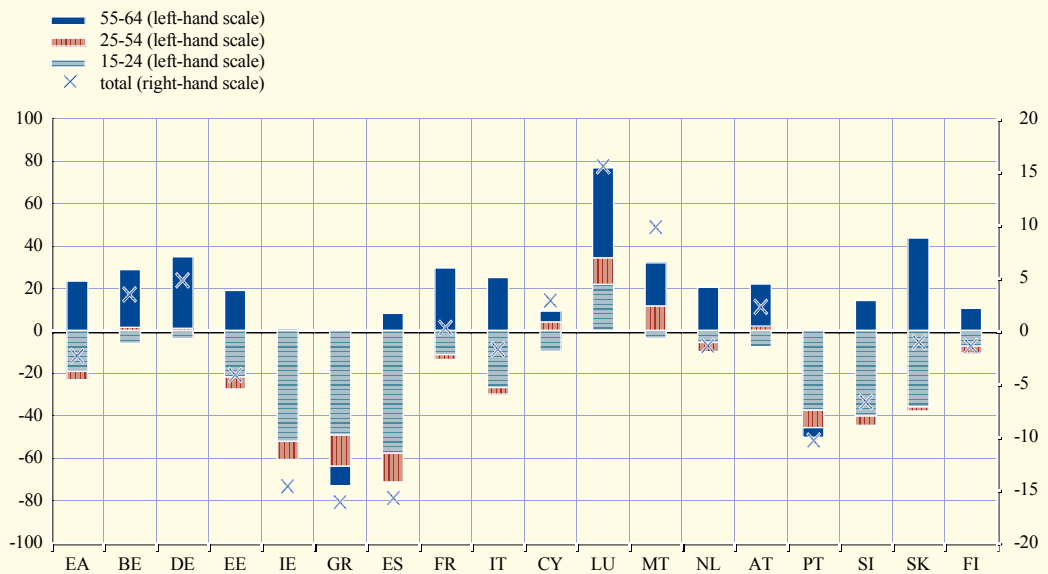
Source: Eurostat.

Notes: The youth unemployment rate refers to the unemployment rate among people under 25 years old. EA stands for euro area.

associated with a downward adjustment in working hours rather than in headcount employment (see Chart A). However, there were some differences at the country level: Spain, Ireland, Greece, Estonia and Portugal recorded a decline in employment considerably larger than the fall in total hours worked.

Chart C Change in employment by age group between the third quarter of 2007 and the third quarter of 2012

(percentage changes)



Source: Eurostat (Labour Force Survey).

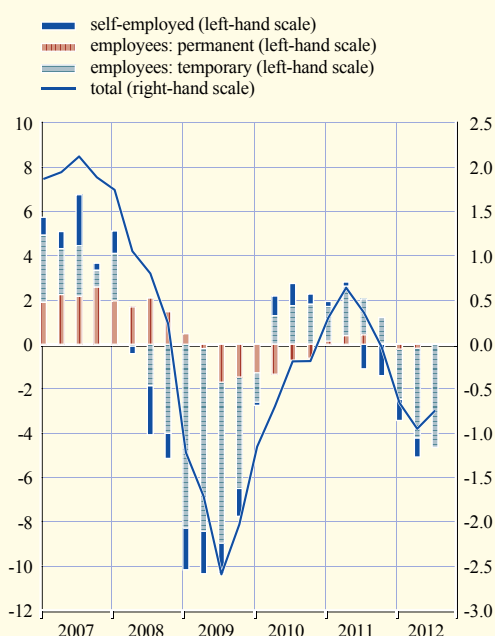
Notes: Percentage changes in employment refer to the second quarter of 2012 for Greece, Italy, Austria and Finland. EA stands for euro area.

A key feature of the rise in total unemployment since the start of the crisis is the sharp increase in youth unemployment in many euro area countries. In Spain and Greece, the youth unemployment rate increased by more than 30 percentage points between the third quarter of 2007 and the third quarter of 2012, to stand above 50% (see Chart B). Furthermore, the decline in youth employment has been mostly in full-time jobs. In Germany, the Netherlands and Austria, youth unemployment has remained well below 10%. Part of the reason for the disproportionate rise in youth unemployment in some countries is that young people are more vulnerable to being made redundant, as they are more likely to be employed on temporary contracts and tend to be less experienced than older workers; the latter are generally in jobs which are better protected by government regulation and contracts. Rigid labour market regulations imposing relatively high minimum wages, insufficient wage differentiation across different types of workers and sometimes excessively high employment protection for permanent workers can also make it more difficult for young workers to find jobs. By contrast, the employment of workers in the 55-64 age group, particularly females in part-time jobs, has continued to rise in most euro area countries since the start of the crisis (see Chart C). This may also reflect the impact of reforms introduced in a number of countries in recent years, including pension reforms, which have encouraged an increase in labour market participation among these workers.

In terms of professional status and types of contract, temporary workers whose contracts are coming to an end are usually the first to be made redundant when firms need to reduce staff numbers. This makes them more vulnerable than permanent workers in the initial phase of a recession (see Chart D). However, when the economy starts to pick up, employers may be uncertain about the magnitude and duration of the recovery and may first recruit workers

Chart D Employment breakdown by professional status and type of contract

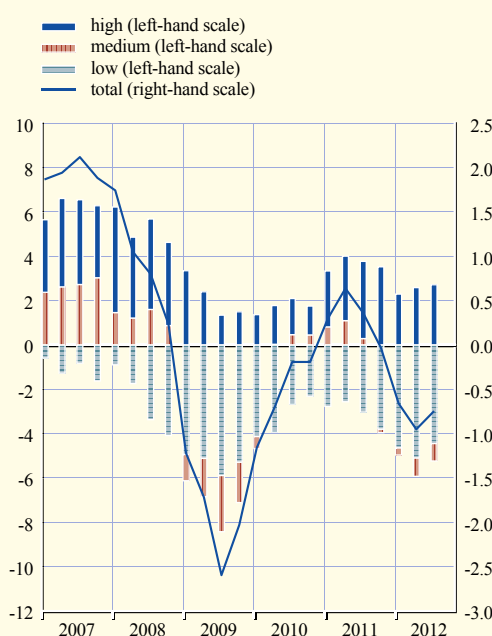
(annual percentage changes)



Source: Eurostat (Labour Force Survey).

Chart E Employment breakdown by skills

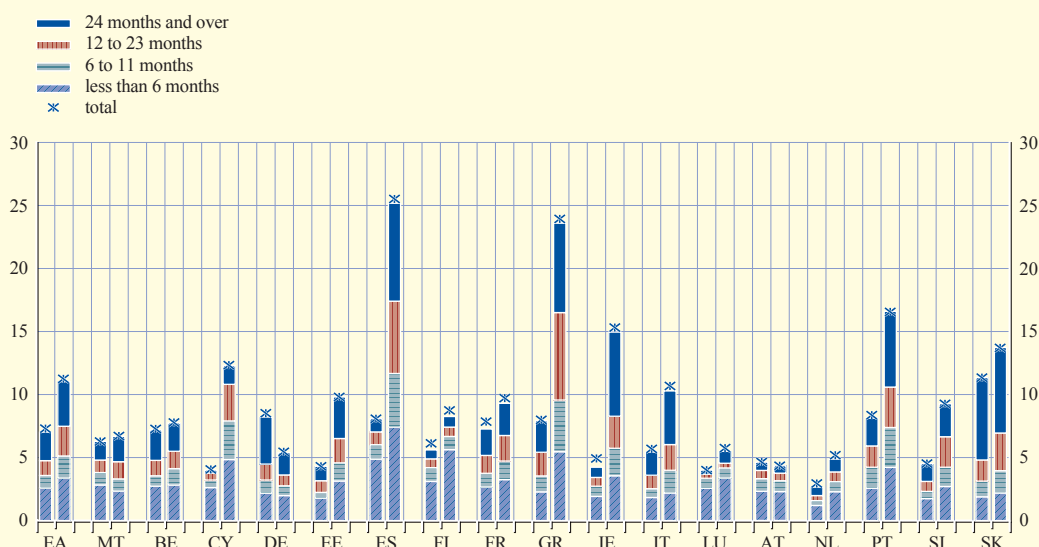
(annual percentage changes)



Source: Eurostat (Labour Force Survey).

Chart F Unemployment breakdown by duration

(percentages of total labour force)



Source: Eurostat (Labour Force Survey).

Notes: First bar shows the third quarter of 2007; second bar shows the third quarter of 2012 (the second quarter of 2012 for Greece, Italy, Austria and Finland). EA stands for euro area.

by offering temporary contracts. Thus, temporary employment is more sensitive to the business cycle.

However, there are notable differences at the country level. In Spain, many young workers on temporary contracts have been made redundant since the start of the crisis, while in Ireland and Greece the number of permanent employees has dropped considerably.

Low-skilled and high-skilled workers have been affected differently by the crisis. Employment among low-skilled workers has decreased significantly (see Chart E) and their unemployment rate has increased by more than that of high-skilled workers. By contrast, employment of high-skilled workers has continued to grow since the start of the crisis, albeit at a slower pace than previously. The divergent evolution of unemployment rates among high-skilled and low-skilled workers is more pronounced in some of the countries most affected by the crisis, e.g. Ireland and Spain. This is partly due to sectoral effects, for example employment in the construction sector – characterised by employment of low-skilled, younger workers – has been disproportionately hit by the crisis.

Turning to the duration of unemployment, the crisis has clearly resulted in a rise in longer-term unemployment. Since the start of the crisis a rising share of unemployed people have been without a job for more than a year, with this trend accelerating from the second half of 2009 onwards (see Chart F). Significant differences can be observed across countries, with larger increases in longer-term unemployment in Portugal, Greece, Ireland and Spain. A key reason behind the sharp increase in unemployment and its duration in many euro area countries is the presence of rigidities which prevent sufficient downward adjustment of compensation per employee.

The longer the above groups of workers remain unemployed, particularly young and low-skilled workers, the greater the risk of cyclical unemployment becoming structural unemployment, further impairing long-term economic growth potential. These developments point to a need for further comprehensive reforms to remove rigidities in labour and product markets in euro area countries. In particular, easing employment protection legislation and removing rigidities in wage-setting institutions in order to increase wage flexibility would facilitate the access of new labour market entrants, especially younger workers, to jobs.¹ Priority should also be given to active labour market policies which help the unemployed to find work by supporting job searches, and to policies aimed at improving human capital and workers' skills. In this context, the European Commission is proposing to introduce "Youth Guarantee" schemes, whereby every young person under 25 years old receives an offer of employment, continued education, an apprenticeship or a traineeship within four months of leaving formal education or becoming unemployed.

¹ For further analysis of euro area labour market developments and policy recommendations, see "Euro area labour markets and the crisis", *Occasional Paper Series*, No 138, ECB, Frankfurt am Main, October 2012.