

# The growth in permanent contracts and its potential impact on spending

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## Rationale

This article analyses what impact the increase in permanent contracts observed over the course of 2022 might have had on household spending.

## Takeaways

- In 2019, workers on permanent contracts devoted 81% (on average) of their household income to spending, compared with 72% for those on temporary contracts.
- In the past, having their temporary contract converted to a permanent one has prompted households to increase their spending-to-income ratio by approximately 20% over the following two quarters.
- Based on those figures, the conversion of temporary to permanent contracts observed in 2022 could have increased the spending-to-income ratio by between 0.18 and 0.24 percentage points.

## Keywords

Permanent contracts, permanent seasonal contracts, spending-to-income ratio, saving.

## JEL classification

JEL classification: D12, D14, E21.

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## Introduction

According to the Spanish Labour Force Survey (LFS, or EPA by its Spanish abbreviation), between 2021 Q4 and 2022 Q4 the number of workers on permanent contracts increased by around 1.6 million, lifting their share of the population aged over 16 by around 3.6 percentage points (pp). At the same time, the number of workers on temporary contracts declined by around 1.2 million. These developments may have implications for household spending patterns, given that, in the past, workers on temporary contracts have had a higher probability of transitioning to unemployment – and therefore higher perceived job insecurity – than those on permanent contracts. This is because households may delay certain spending when faced with increased uncertainty over their future income, preferring to hold a savings buffer (known as precautionary saving) to help maintain consumption should their income decline, for instance due to loss of employment.<sup>1</sup>

This article simulates how the increase in job stability may have affected household spending. First, we show that, before the last labour market reform, households whose reference person was on a temporary contract or unemployed devoted 9 pp less of their income to spending than those whose reference person was on a permanent contract. Further, where the household reference person's contract is converted from temporary to permanent, it is estimated that the household's spending-to-income ratio increases by some 20% in the quarters immediately before and after the conversion.<sup>2</sup> Accordingly, an increase in permanent hires can be expected to lead to some households devoting a higher share of their income to spending.

This article goes on to analyse how the increase in permanent contracts in 2022 may have affected the spending-to-income ratio of households as a whole. To do this, the previous results are combined with household spending and income data drawn from the Household Budget Survey (HBS, or EPF by its Spanish abbreviation) and the Living Conditions Survey (LCS, or ECV by its Spanish abbreviation), respectively. It is significant here that “permanent seasonal contracts” accounted for a relatively large share (approximately 25%) of the increase in permanent contracts in 2022. These differ from conventional permanent contracts in that they entail a higher probability of transition to unemployment – and more so following the latest labour market reform – and therefore greater wage instability. Thus, based on the spending growth assumptions for households whose reference person has gone from a temporary contract to a permanent seasonal

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1 See Blundell and Stoker (1999) or Banks, Blundell and Brugiavini (2001), who analyse how income uncertainty affects household spending developments in the United Kingdom. Hendren (2017) discusses how, among US households, spending decreases and labour market participation increases as their perceived probability of job loss rises. In Spain, Campos and Reggio (2015) examine precautionary saving during the Great Recession.

2 See Chart 7 of Anghel, Barceló and Villanueva (2019) or Barceló and Villanueva (2016), who estimate that spending and income increase by around 24.5% and 2.8%, respectively, in the quarters immediately before and after the conversion. These figures imply a 20% rise in the spending-to-income ratio. Applying 20% growth to the ratio for 2019 (72%) yields a 14 pp increase in the spending-to-income ratio as defined in this article.

one, the increase in permanent contracts is estimated to have lifted the spending-to-income ratio by between 0.18 pp and 0.24 pp in 2022.

The article concludes with some caveats regarding the omission of factors that might cause spending to rise (e.g. household formation) and the current lack of disaggregated data to accurately quantify the extent to which the decline in job insecurity has been prompted by the growth in permanent contracts.

## The increase in the share of permanent contracts and perceived job insecurity

On LFS data, between 2021 Q4 and 2022 Q4 the number of individuals with permanent contracts increased by roughly 1,591,000 (from 12,666,000 to 14,257,000). At the same time, the number of workers with temporary contracts declined by around 1,194,000 (from 4,308,000 to 3,115,000) (see Chart 1.a). As a share of the total population aged over 16, individuals on permanent contracts rose from 31.9% to 35.5%. In terms of households (rather than individuals), the LFS shows that the number of those whose reference person had a permanent contract rose from 7,003,000 in 2021 Q4 to 7,647,000 in 2022 Q4 (see Chart 1.b). This represents an increase of 3 pp (from 36.9% to 39.8%).

It is a well-known fact that flows between employment and unemployment and perceived job insecurity are both higher among workers on temporary contracts than among those on permanent contracts (Banco de España, 2022). Therefore, the increase in the number of workers on permanent contracts may be associated with higher perceived job security.

However, this growth in permanent contracts has been accompanied by a rising proportion of both permanent part-time and permanent seasonal contracts, which in certain cases may entail lower job security (Banco de España, 2022). Indeed, according to social security registrations data, the transition rate to unemployment among those on permanent seasonal contracts grew in 2022 and was similar to that of workers with temporary contracts in that year. Likewise, LFS flow data indicate that quarterly transitions to unemployment for workers on permanent seasonal contracts are similar to those on temporary contracts (see Chart 2.a).<sup>3</sup> This evidence suggests that new workers on permanent seasonal contracts have less job stability than those on other types of permanent contract. Meanwhile, according to the LFS, at end-2022 workers on permanent seasonal contracts had, on average, accumulated almost five years' tenure at their company (58 months), while that figure for workers on temporary contracts was just 22 months.<sup>4</sup> These figures suggest that workers on permanent seasonal contracts have greater job stability than those on temporary contracts, given that they have been at the same company for a longer time.

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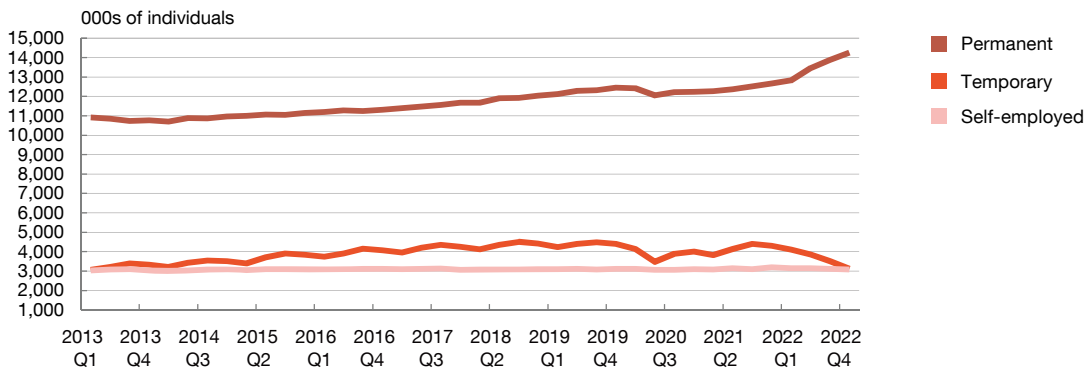
3 Transitions from permanent seasonal contracts to unemployment show a seasonal peak in the third quarter, which may owe to the seasonal nature of the jobs in those economic activities where such contracts are more widely used.

4 The median tenure of workers on permanent seasonal contracts is 20 months (i.e. 50% of such workers have been in their job for less than 20 months and the other 50% for longer). Among workers on temporary contracts, the median is five months.

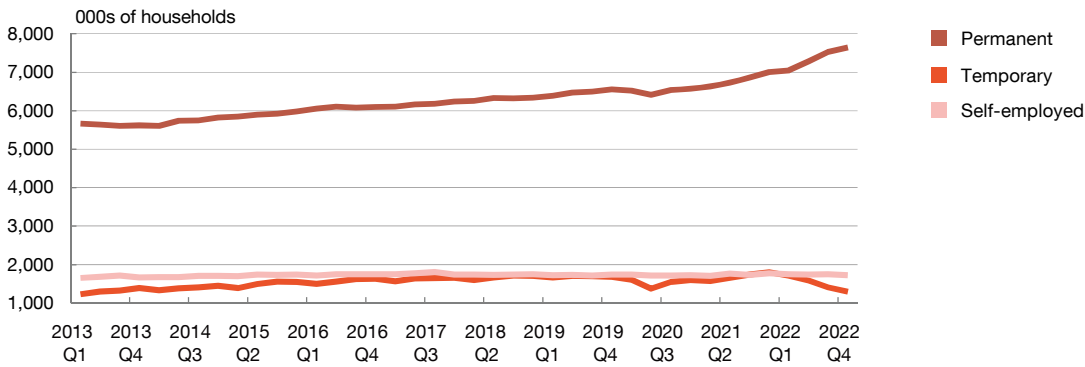
Chart 1

The number of workers and households with permanent contracts increased between 2021 Q4 and 2022 Q4, while the number of those with temporary contracts declined

1.a Workers, by employment status



1.b Households, by employment status of the reference person



SOURCE: INE (EPA).

Note: In the EPA, the category “self-employed” includes the following groups: “Entrepreneur with employees”, “Independent worker or entrepreneur without employees”, “Member of a cooperative” and “Assists in the family firm or business”.



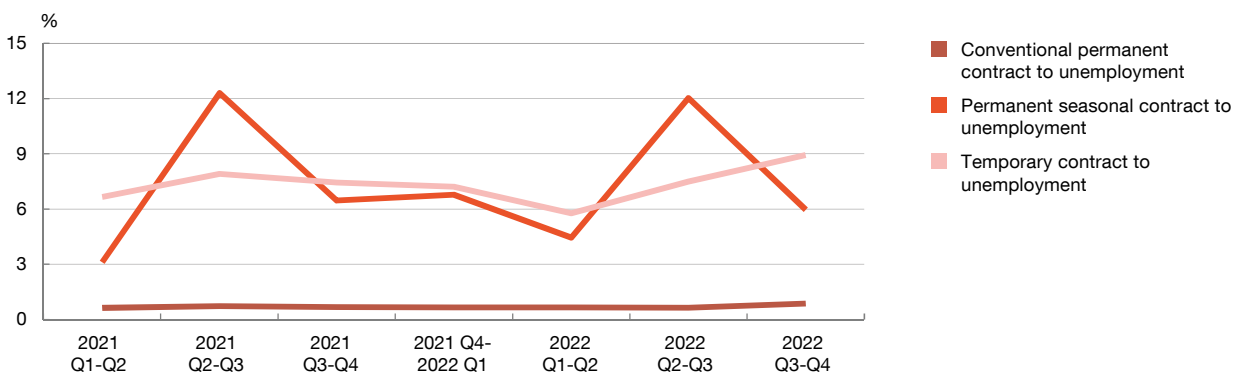
Further information on perceived job stability can be found in the European Central Bank’s Consumer Expectations Survey (CES). The CES results for Spain suggest that, among workers who had been in their job for less than a year, the perceived probability of job loss in the next three months was between 5 pp and 10 pp lower in 2022 than the average reported in 2021. Among those who had been in their jobs for a year or more, this probability of job loss was 2 pp lower (down from 5% to 3%) (see Chart 2.b). Perceived job stability is shaped by various factors, including the cyclical position of the labour market. That said, the higher incidence of permanent hires, insofar as it is associated with the improved perception of job stability, appears to have helped to underpin household spending over the course of 2022.<sup>5</sup>

<sup>5</sup> The literature on precautionary saving refers to uncertainty about future income linked to more than job losses alone. Arellano, Bonhomme, De Vera, Hospido and Wei (2022) relate wage volatility with days worked in short-term temporary employment.

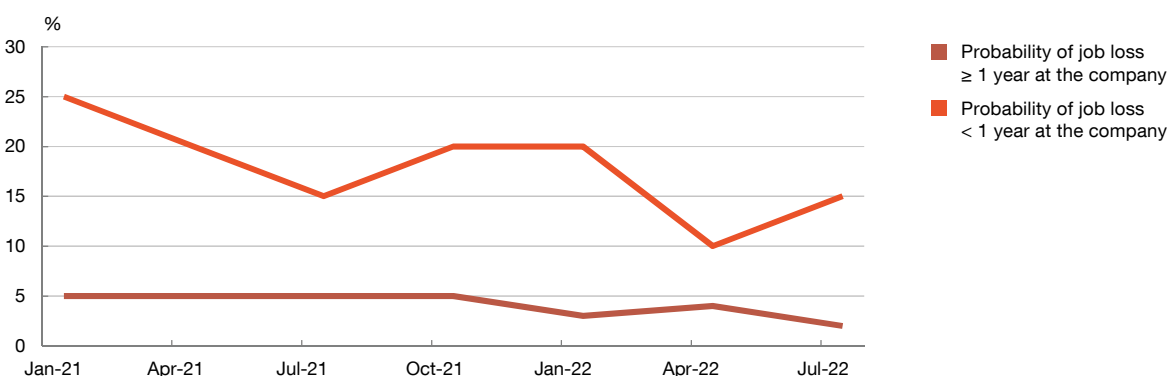
Chart 2

### Transitions to unemployment and perceived job insecurity

2.a In 2022, quarterly transitions from employment to unemployment, expressed as a percentage of the number of workers in each group, followed the same patterns as observed in 2021



2.b In 2022, the perceived probability of job loss in the following three months declined among workers who had been in their job for less than a year



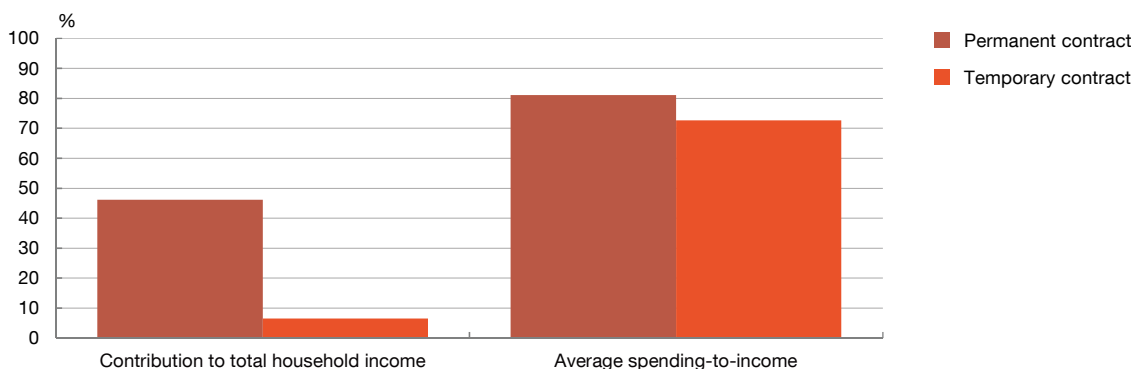
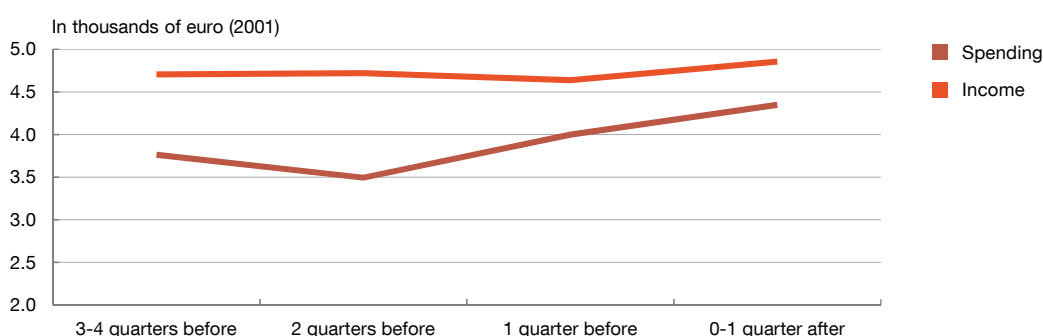
SOURCE: Banco de España calculations, drawing on data from the INE (EPA) and the ECB (CES).



## The relationship between household spending and the job insecurity of household members

According to the life cycle theory, household spending is inversely related to the expected volatility in future income, and the more risk averse the household, the more pronounced this relationship will be (Blundell and Stoker, 1999). Given that workers on temporary contracts have less job stability, they would be expected to consume a lower proportion of their income. To ascertain whether this relationship is observed in the data, we construct a measure of spending as a proportion of income, with a breakdown by the household reference person's employment status (permanent contract, temporary contract or unemployed, self-employed, retired or economically inactive), combining information from several surveys. In this article, households whose reference person is on a temporary contract or unemployed are grouped together, given that Charts 2.a and 2.b show frequent transitions between the two statuses, meaning the same individuals may be in one situation or the other throughout the time horizon. We focus on the spending-to-income ratio

Chart 3

**Spending-to-income ratio, by type of contract of the household reference person****3.a Contribution to total household income and spending-to-income ratio, by employment status of reference person (2019)****3.b Households' non-durable spending and income before and after a temporary contract is converted to a permanent one**

SOURCES: Banco de España (EFF), INE (EPF and ECV) and Barceló and Villanueva (2016).

for two reasons. First, according to the life cycle theory, the main determinant of spending is a household's long-term income. Therefore, a household's level of spending needs to be compared with its actual resources. Second, the effects of a temporary contract converting to a permanent one can vary depending on the permanent contract type. As mentioned above, around 25% of the increase in the number of permanent contracts in 2022 was accounted for by permanent seasonal contracts. These contracts can entail periods of inactivity and may therefore have a lesser impact on expected future income than other permanent contracts (Banco de España, 2022). By taking the spending-to-income ratio, we mitigate the potential effect associated with, for example, expected income linked to new permanent contracts being lower than permanent contract wages in past periods. To construct the ratio for 2019, we combine household income data drawn from the LCS with spending data for the corresponding population groups taken from the HBS.<sup>6</sup>

As Chart 3.a shows, households whose reference person is on a temporary contract or unemployed devoted 72.1% of their income to spending, 9 pp less than those whose reference person is on a

<sup>6</sup> In this article, spending includes both durable and non-durable goods, but excludes imputed rent for main residence. See Anghel, Barceló and Villanueva (2019) for details on how these ratios are compiled.

permanent contract. This lower spending percentage may owe in part to higher precautionary saving.<sup>7</sup>

Before the 2022 labour market reform, the transition to a more secure job led to an increase in spending as a percentage of income.<sup>8</sup> Thus, as shown in Chart 3.b, based on an analysis of household spending and income in the quarters before and after a temporary contract is converted to a permanent one, spending per quarter rises by around 24.5% (from €3,494 to €4,350), while income increases by roughly 2.9% (from €4,720 to €4,855). Part of the spending increase is observed one quarter before the contract is converted, possibly because the workers learn that their contract will be converted before it actually occurs.<sup>9</sup> In any event, in the two quarters preceding contract conversion and the following quarter, the household spending-to-income ratio increases by around 20%, which appears to be funded through a reduction in their financial assets (see Chart 3.b).<sup>10</sup>

## Quantifying the impact of the growth in permanent contracts on consumption: two possible approaches

The impact that the growth in permanent contracts may have had on consumption in 2022 is quantified in two alternative exercises.

The first is based on the observation made in the foregoing section: in 2019 households whose reference person had a temporary contract devoted, on average, a lower proportion of their income to spending than those whose reference person had a permanent contract (see Chart 3.a). Specifically, the exercise simulates a rise in the share of total income accounted for by households whose reference person has a permanent contract, in proportion to the increase in the population of this type of household. Given that the increase has been accompanied by a decline in the weight of households whose reference person has a temporary contract or is unemployed (and that therefore have a lower average propensity to spend), the aggregate spending-to-income ratio can be expected to rise. It should be noted that this exercise assumes that the spending ratio of households whose reference person's contract is converted from temporary to permanent increases by 9 pp, i.e. the difference observed between the average ratios of the two household groups in 2019.

In Panel A of Table 1, column 1 shows the household income distribution in 2019, while column 2 shows the aggregate household spending-to-income ratio, both by employment status of the household reference person. By definition, the aggregate ratio is the average of each

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7 Among other factors, these households may have less access to credit and save more for the purchase of their main residence.

8 Lugilde, Bande and Riveiro (2018) construct a job insecurity indicator, combining job tenure, hours worked, contract type and firm size, and document how changes in this index over the three-year reference period correlate negatively to those in spending. The increase may owe to the fact that contract conversion increases income in the long term (García-Louzao, Hospido and Ruggieri, 2023).

9 Hendren (2017) argues that knowledge of a job loss affects spending even before the job is lost. Using a simple theoretical model, Blundell and Stoker (1999) show how consumption growth is affected by the time frame during which the future income uncertainty is resolved.

10 Barceló and Villanueva (2016) and Anghel, Barceló and Villanueva (2019).

Table 1

**According to several quantification exercises, the increase in the number of workers with a permanent contract may have boosted spending in 2022 by between 0.18 pp and 0.24 pp of income**

Panel A	Observed		Exercise 1 (a)	Exercise 2 (b)
	Contribution to total household income (2019) (%)	Average spending 2019 / Average income 2019 (%)	Contribution to total household income (%)	Average spending 2019 / Average income 2019 (%)
<i>Employment status of the household reference person</i>	(1)	(2)	(3)	(4)
Employees - permanent contract	46.10	81.00	49.05	81.00
Employees - temporary contract + unemployed	11.68	72.08	8.95	74.11
Self-employed	9.67	71.66	9.30	71.66
Retired	26.09	58.96	26.32	58.96
Economically inactive	6.46	63.20	6.38	63.20
Total (average spending as a percentage of income weighted by contributions, %)		72.15	72.39	72.39
Panel B: Alternative estimates, excluding permanent seasonal workers from the group with permanent contracts (c)				
<i>Employment status of the household reference person</i>	(1)	(2)	(3)	(4)
Employees - permanent contract	46.10	81.00	48.51	81.00
Employees - temporary contract + unemployed	11.68	72.08	9.49	73.60
Self-employed	9.67	71.66	9.30	71.66
Retired	26.09	58.96	26.32	58.96
Economically inactive	6.46	63.20	6.38	63.20
Total (average spending as a percentage of income weighted by contributions, %)		72.15	72.35	72.33

**SOURCE:** Banco de España, drawing on INE data (EPF and ECV).

- a** In exercise 1 (column 3), the 2019 spending-to-income ratios remain constant, but the proportions of each group in the total population change based on the LFS data between 2021 Q4 and 2022 Q4.
- b** In exercise 2 (column 4), the weights in the income distribution in 2019 remain constant, but the spending-to-income ratio changes based on the conversions of temporary contracts to permanent ones and the elasticities of the spending-to-income ratio to conversions to permanent contracts in Anghel, Barceló and Villanueva (2019).
- c** The simulation exercises conducted in this panel are identical to those of Panel A, with the following two exceptions to exclude permanent seasonal contracts from conventional permanent contracts: i) in column (3), households whose reference person has a permanent seasonal contract are excluded from the group of households whose reference person has a permanent contract, and included in the group of households whose reference person has a temporary contract or is unemployed, and ii) in column (4), a conversion rate of temporary to permanent contracts of 10.5% (rather than 14%) is assumed as, on social security registrations data, 25% of new permanent contracts are permanent seasonal contracts (with the remaining 75% therefore being considered as conventional permanent contracts).

group's ratios, weighted by their share in the income distribution. Thus, assuming a 2.9 pp increase in the proportion of households whose reference person has a permanent contract and a 2.7 pp decline in that of households whose reference person has a temporary contract or is unemployed (as observed between 2021 Q4 and 2022 Q4 according to the LFS),<sup>11</sup> the

<sup>11</sup> The shares in total income of the other groups considered (the self-employed, retirees and economically inactive persons) are also adjusted, according to the change in these groups' weight in the total population according to the LFS between 2021 Q4 and 2022 Q4.



aggregate household spending-to-income ratio would rise by 0.24 pp, from 72.15% to 72.39% (see Table 1, column 3).

The second exercise is based on the studies analysing the short-term behaviour of household spending and income when the reference person moves from a temporary contract to a permanent one (see the third section). This alternative quantification entails estimating the number of temporary contracts converted to permanent ones and applying the consequent increase to the spending-to-income ratio. One possible estimate of the proportion of temporary contracts that were converted to permanent ones is the reduction of 13.5 pp (approximately 14%) in the temporary employment rate observed in the social security registrations data (Banco de España, 2022).<sup>12</sup> Assuming that 14% of the temporary contracts in force in 2022 are converted into permanent contracts and that, in line with the results of the third section, the spending-to-income ratio of the households affected by these conversions rises by 20% (from 72.08% to 86.50%), the ratio for all households whose reference person has a temporary contract would increase by 2 pp (from 72.08% to 74.11%). When these households are weighted by their share in aggregate income (11.68%), this suggests the aggregate spending-to-income ratio would increase by 0.24 pp (from 72.15% to 72.39%) (see Table 1, Panel A, column 4).

As mentioned, a potential caveat is that, on social security registrations data, around 25% of the growth in permanent contracts relates to permanent seasonal workers and the fact that labour turnover among such individuals (which has traditionally been high compared with that of conventional permanent workers) rose over 2022 (page 36 of Banco de España, 2022). To accommodate this, in the first quantification exercise, an extreme assumption may be made that, for the purposes of uncertainty as regards future labour income and consequently household spending patterns, permanent seasonal contracts are similar to temporary contracts. Therefore, households whose reference person was a permanent seasonal worker in 2022 are classified as having a temporary contract, and only those households whose reference person was in permanent employment (be it full or part time) are classified as having a permanent contract. The results of this scenario (presented in Table 1, Panel B, column 3) suggest that, under these assumptions, the spending-to-income ratio would increase by 0.20 pp to 72.35%.

Similarly, in the second quantification exercise, workers with a permanent seasonal contract are excluded from the calculation of total new permanent workers, under the implicit assumption that their future labour income uncertainty remains unchanged despite the change in contract. Given that 25% of the growth in workers with a permanent contract corresponds to permanent seasonal contracts, a conversion rate of temporary to permanent contracts of 10.5% (i.e. 75% of 14%), rather than 14%, may be assumed. Again assuming that the spending-to-income ratio of the households benefiting from these conversions increases by 20%, the ratio would increase by 1.5 pp (from 72.08% to 73.60%) in the case of households whose reference person has a temporary contract. When these households are weighted by their share in total income (11.68%), this

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12 Page 36 of Banco de España (2022) provides a breakdown of the 13.5 pp decline in the temporary employment ratio based on the contributions by type of permanent contract. In keeping with this breakdown, this article assumes that the reduction in temporary contracts has been the result of conversions to permanent contracts.

suggests the aggregate spending-to-income ratio would increase by 0.18 pp (rather than by 0.24 pp, as obtained in Table 1, Panel A, column 4).<sup>13</sup>

In sum, the simulations presented suggest that the growth in the number of workers with a permanent contract may have helped sustain spending in 2022. Taking as reference the total income of €660,680 million reported in the LCS in 2019, a rise of between 0.18 pp and 0.24 pp (the range of estimates obtained) in the spending-to-income ratio would be equivalent to an increase in total spending of between €1,189 million and €1,586 million, or of €1,846-€2,462 per additional household whose reference person is on a permanent contract.<sup>14</sup> Using the total income according to the National Accounts (around 15% higher than that reported in the LCS) obtains a spending increase of €2,137-€2,849 per additional household whose reference person is on a permanent contract.

## Conclusions

This article presents a series of simulations of the possible effects on spending of the growth in the number of workers with a permanent contract in 2022. The quantifications derive from estimates made using data prior to the 2022 labour market reform. An initial quantification exercise is based on the fact that in 2019 the spending-to-income ratio of workers with a permanent contract was higher than that of workers with a temporary contract. The second quantification is founded on the previous studies' findings that households increase their spending when their perceived job insecurity decreases. Combining this information with the weight of the different groups of individuals in aggregate income shows that the increase in workers with permanent contracts may have boosted the spending-to-income ratio by between 0.18 pp and 0.24 pp in 2022.

As a caveat, this exercise has sought to isolate just one channel of the impact of the growth in permanent workers: job insecurity. However, other factors may act in the opposite direction, such as the spike in inflation, which has pushed up food and energy prices. Further, it is possible that households are perceiving greater instability associated with the new permanent contracts than they have in the past. In this respect, a more accurate and comprehensive assessment of the effects of the labour market reform requires aggregate data on flows between contract types. Lastly, the additional effect that greater job security may have on household formation, which would further boost spending, has not been considered.<sup>15</sup> In any event, further examination is needed of the labour flows of the different groups, to monitor developments in job security and the related economic implications.

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13 Other robustness checks have been performed, such as considering the unemployed and workers with temporary contracts separately. In this case, the aggregate spending-to-income ratio would rise by between 0.10 pp and 0.20 pp, around 0.10 pp less than when the two categories are grouped together. These alternative estimations need to be considered with caution, as the breakdown of the spending-to-income ratio should be based on groups that remain unchanged over time (an assumption which does not hold if temporary workers and the unemployed are disaggregated over the economic cycle), and transitions of unemployed workers to employment (be it temporary or otherwise) are not taken into account.

14 Between 2021 Q4 and 2022 Q4 the number of households whose reference person had a permanent contract increased by 644,100 (see Chart 1.b).

15 Barceló and Villanueva (2018) document that greater job security on account of contract conversion leads to an increase in the proportion of individuals who decide to leave the family home and form a household, mainly by renting their principal residence.

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