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Productivity, the labour market and Spain's (non-)convergence with the euro area*

3rd Conference on the Spanish Economy – Banco de España, Centro de Estudios Monetarios y Financieros and Universidad Internacional Menéndez Pelayo

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* English translation from the original in Spanish.

I would like to thank the Rector of the Universidad Internacional Menéndez Pelayo and everyone who has helped organise this conference, and all the speakers and panellists and each of you here today for taking part.

Allow me to open this second day of the Conference on the Spanish Economy by underlining its purpose and the importance of the issues it addresses.

This is the third edition of this annual conference organised by the Banco de España, the Centro de Estudios Monetarios y Financieros (CEMFI) and the Universidad Internacional Menéndez Pelayo (UIMP). Its aim is to provide a forum for discussion to share insight into the main problems facing the Spanish economy and possible solutions.

These discussions must be rooted in rigorous economic research and that is why each year we seek to gather the academic and research community with a particular interest in the Spanish economy.

This year, we are focusing on two fundamental challenges that, although addressed last year, merit special attention owing to their importance and continuing relevance.

The first is the **high unemployment rate**, the theme of yesterday's two sessions and panel. The second is **low productivity growth**, which will be discussed in today's sessions and panel. Both of these problems have hampered convergence between income levels in Spain and in other European countries since the end of the last century. In particular, Spain has not narrowed the gap with per capita income in the EU since the 1990s. Measured in purchasing power parity terms, Spain's GDP per capita was 92% of the EU's in 1990, falling to 85% in 2022. Spain's lower productivity explains most of this difference. In fact, if productivity per worker in Spain were equal to the EU average (it is currently 11 percentage points (pp) lower), Spain's per capita income would be just 4% lower than the EU average.

And if the Spanish employment rate were equal to the EU average, the income gap per capita would shrink by a further 7 pp.

When making this comparison, Spain still benefits from a slight demographic advantage, since the working age population as a share of the total population – another component of income per capita – is 3 pp higher than in the EU. However, this advantage will soon disappear, since the ageing process in Spain is going to take place more markedly and quickly than in the rest of the EU. The Banco de España's 2022 and 2023 Annual Reports pointed out, in relative detail, the importance of productivity and unemployment for convergence and the current state of the Spanish labour market.

In addition, it should be noted that we are living in an age of profound technological and demographic change, which, among other consequences, will make it more difficult to replace the working population in the coming decades. Indeed, the effects of demographic change, employment policies, the determinants of productivity and the role of technological change sit high on the Banco de España's research and analysis agendas.

Returning to the first of the challenges I mentioned, **unemployment**, the labour market in Spain, as in many other countries, has shown remarkable resilience to the shocks caused by the COVID-19 pandemic and the war in Ukraine, which, along with other events, have caused a surge in inflation not seen since the 1970s. The inflation rate is coming down without the interest rate rises that were needed having significantly dented Spain's growth

or employment, which has remained robust, although we should not forget that the unemployment rate here is still twice as high as the EU average.

The persistence of unemployment at relatively high levels and the fact that, even with a double-digit rate, the labour market is showing signs of tightness owing to labour shortages in some segments of the market, offer more than enough reason to continue analysing the existence of structural unemployment, which may originate in dysfunctional labour market behaviour.

In addition, there are other factors that will affect the labour market in the coming years that I would like to mention.

Future technological changes will have huge implications for the functioning of the labour market, and especially for labour demand and supply, and thus the level of employment and productivity. The new technological revolution based on the deployment of robotics and artificial intelligence (AI) innovations may eventually enable machines and algorithms to independently perform tasks (whether routine, specialised or otherwise) that could only previously be done by humans. This has given rise to some concern about the possibility of greater job destruction and lower job creation than in previous technological revolutions.

It is still too early to anticipate future developments in robotics and AI and how they will be integrated into productive tasks and thus to predict the scope and effects of new generative AI models that are capable of carrying out tasks requiring creativity and innovation – previously the sole domain of humans. However, the reallocation of employment across sectors and occupations and the demand for new professional qualifications reflecting new technological developments will undoubtedly accelerate.

Employment policies have a pivotal role to play in minimising the fallout of this shift on employment and productivity and in adapting labour supply to the new technological environment.

Demographics are another important factor to take into account: specifically, the ageing of the working population, which also has implications for the volume of employment, its sectoral and occupational composition and productivity. These implications reflect both composition effects, owing to differences in employment and productivity rates by age, and the fact that employment opportunities for older people and labour productivity across all age groups tend to be lower in older societies.

As noted, the high structural unemployment rate in Spain is one of the economy's main challenges and the object of study by the Banco de España. In this regard, Chapter 3 of our 2023 Annual Report¹ offers a thorough review of the Spanish labour market. It concludes that there is room for improvement both in passive policies, which protect workers when they lose their jobs, as well as in active policies, which seek to promote the employability of unemployed workers and their adjustment to the labour demand existing at any given time.

¹ https://www.bde.es/f/webbe/SES/Secciones/Publicaciones/PublicacionesAnuales/InformesAnuales/23/Files/InfAnual_2023_Cap3_En.pdf

Moreover, it suggests that anything that hinders sectoral and occupational reallocation of employment will exacerbate job destruction linked to technological change.

This means that employment protection legislation and collective bargaining regulations must also be reconsidered in the light of the new technological and demographic environment.

All of the aforementioned aspects of the Spanish labour market also bear on the second challenge facing our economy – its **low level of productivity**, which is a result of many factors that interact with each other and should be tackled together.

These factors include, for example, any aspects that constrain business growth and business demographics in general and the reallocation of productive resources across sectors and firms, as well as Spain's shortfall in terms of technological capital and investment in innovation, as described in Chapter 2 of our latest Annual Report.²

The role of these factors in limiting productivity growth in Spain has been comprehensively documented in the literature, at least to the extent allowed by the limitations of productivity measurement.

However, if policymakers are to be properly informed, the root cause of these shortfalls must also be identified.

In this regard, we can highlight two possible underlying factors that ultimately govern what firms produce and how they produce it and, thus, productivity growth.

First, the regulatory and institutional framework that essentially shapes product markets (for goods and services) and factors of production (labour and capital). Second, the availability of human capital, in relation to which education and professional training play a key role.

As a result, this conference revolves around these two challenges to our economy.

Two complementary papers were presented and discussed during yesterday's sessions. José Azar and Javier Sanz-Espín put forward estimates of the gap between wages and the marginal productivity of labour that make it possible to characterise the degree of monopsony³ in the Spanish labour market and how it changed following the 2012 labour reform.

In addition to its usefulness in measuring monopsony among firms in the Spanish labour market, their work will help guide new lines of research that link competition in markets and productivity to employment and wages.

Carlos Carrillo presented new results on the dynamics of labour flows between sectors of the economy and the rigidity of the labour market in specific sectors. His findings on job search intensity since the pandemic and the tightening of the labour market, as well as cross-sector heterogeneity, allow us to better understand the factors behind the

² https://www.bde.es/f/webbe/SES/Secciones/Publicaciones/PublicacionesAnuales/InformesAnuales/23/Files/InfAnual_2023_Cap2_En.pdf

³ A market condition in which there is only one buyer for a product or service.

coexistence of a high unemployment rate and labour scarcity in various segments of the Spanish labour market.

At the upcoming session on productivity, Matilde Mas will present her work highlighting the importance of complementarity between technological capital, intangible capital and worker upskilling when maximising the impact of new technologies on productivity growth.

The apparent paradox in recent years of intense technological change existing alongside low productivity growth could owe, at least in part, to a certain inability to retrain workers and adapt firms' organisational structures to this change.

Carolina Villegas-Sánchez will present her work on the role of growth and business demographics as a driver of productivity in Spain, from an international perspective.

Among other stylised facts, she will show that business start-ups and the differences in size between younger and more mature firms have been in decline since the financial crisis. In the case of Spain, this could point to more robust business growth and an improvement in the sharing of know-how between frontier firms and others, in contrast to what is seen in countries such as the United States.

I am convinced that the papers presented at this conference and the discussions that take place around them, and in each of the panels, will make a significant contribution to improving our understanding and communication of the Spanish economy's structural problems.

Thank you very much.