Reviving Broadly Shared Productivity Growth in Spain

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Foreword

Spain has been confronted with weak wage and productivity growth for several decades. This report analyses the sources of weak and productivity growth and puts forward concrete policy recommendations for reviving broadly shared productivity growth. The report is structured as follows. Chapter 1 provides an overview of the key messages. Chapter 2 documents the decline in broadly shared productivity growth and its underlying mechanisms and discusses of how policies can enhance the adaptability of the economy and labour market to structural change. Chapter 3 provides an in-depth discussion of the role of selected labour market policies for promoting broadly shared productivity gains. The emphasis is on wage-setting institutions, employment protection and job retention support consistent with the focus of recent reforms.

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Executive Summary

Spain has been confronted with weak wage and productivity growth for several decades. This report provides an overview of the role that labour market policies as well as other policies can play in reviving broadly-shared productivity growth in Spain. The emphasis is on wage setting institutions, employment protection and job retention support, consistent with the focus of recent reforms.

Wage-setting institutions have been strengthened to promote a broader sharing of productivity growth

Spain has significantly increased its minimum wage and strengthened sector-level collective bargaining to promote a broader sharing of productivity gains with workers, particularly those with low wages.

The minimum wage has become an important part of the policy toolkit in Spain. It was increased from a relatively low level of about 45% of the gross median wage in the private sector in 2018, well below the OECD average, to 58% in 2022 and is set to increase further to 62% of the gross median wage (which corresponds to 60% of the net average wage). Most of the increase was realised in a single step in 2019.

The OECD's evaluation of the 2019 minimum wage reform suggests that it significantly boosted the wages of low-wage workers without causing substantial job losses: it increased the wages of directly affected workers by almost 6%, while it reduced employment by only 0.6%.

Progress has been made in addressing labour market duality, with potentially important payoffs in terms of higher productivity growth

A key feature of the labour reform of December 2021 was to reduce the excessive reliance on temporary contracts by restricting their use. As a result, Spain is now the country in the OECD with the third strictest rules for the use of fixed-term contracts according to the OECDs Employment Protection Indicators.

The reform has resulted in a large reduction in the incidence of temporary contracts. It fell from 21% in 2021 Q4, the second highest in the OECD, to less than 15% in 2023 Q1. The fall in temporary contracts did not result in lower employment as it was more than offset by an increase in permanent contracts. Indeed, the employment rate is now at a record high.

About a fifth of the increase in permanent employment reflects the increased use of open-ended intermittent contracts (*contrato fijo-discontinuo*). Such contracts offer more employment stability than temporary contracts, although earnings and hours can vary within certain limits.

Reforms to the system of job retention support have enhanced labour market resilience

Ever since the devastating experience of the global financial crisis, there was an ambition to strengthen the Spanish job retention scheme (ERTE) to support labour market resilience. However, it was not until the COVID-19 crisis struck that an effective scheme was put in place. As a result, support was provided promptly and widely, covering almost one in four workers at its peak.

Job retention support played a crucial role in preventing a surge in job losses in response to the COVID-19 crisis. Rather than shedding jobs, as during the global financial crisis when job retention support was little used, adjustment mainly took the form of reductions in working hours as in most other countries where job retention schemes were widely used. The positive impact of job retention support on employment is also confirmed in an ongoing evaluation by the OECD.

Building on the success of ERTE during the COVID-19 crisis, the labour reform of December 2021 introduced an explicit framework for scaling up support in times of exceptional need (the RED mechanism). It allows for government discretion over its activation while the parameters of the crisis scheme are defined in advance.

1 Overview

Alexander Hijzen

Spain has been confronted with weak wage and productivity growth for several decades. This chapter provides an overview of the role that labour market policies as well as other policies can play in reviving broadly shared productivity growth in Spain. To set the scene, it starts with documenting the decline in broadly shared productivity growth and its underlying mechanisms. It then provides a discussion of how policies can enhance the adaptability of the economy and the labour market to structural change. It concludes with a discussion of the role of selected labour market policies for promoting broadly shared productivity gains. The emphasis is on wage-setting institutions, employment protection and job retention support, consistent with the focus of recent reforms.

1.1. Introduction

A well-functioning labour market is crucial for sustaining gains in productivity which underpin high and inclusive growth and rising levels of well-being. Yet, productivity growth has tended to slow in Spain since the mid-1990s. While many other OECD countries also experienced a slowdown in productivity growth, in Spain this started earlier and has been more pronounced. At the same time, average real wages have failed to keep up with even diminished productivity growth, making growth less inclusive. Thus, not only have productivity gains become smaller, but the share transmitted to workers has also declined, resulting in stagnating real wages.

This decline in broadly shared productivity growth reflects to an important extent the difficulty of workers, firms and the labour market more generally to adapt to structural change (adaptability), and more recently, also the long shadow cast by the global financial crisis (resilience). While the experience during the COVID-19 crisis suggests that labour market resilience has improved, considerable uncertainty remains about the ability of the labour market to adapt to rapid structural changes (e.g. artificial intelligence, green transition). Indeed, seizing upon new opportunities may be a challenge unless the causes of weak productivity growth are effectively addressed.

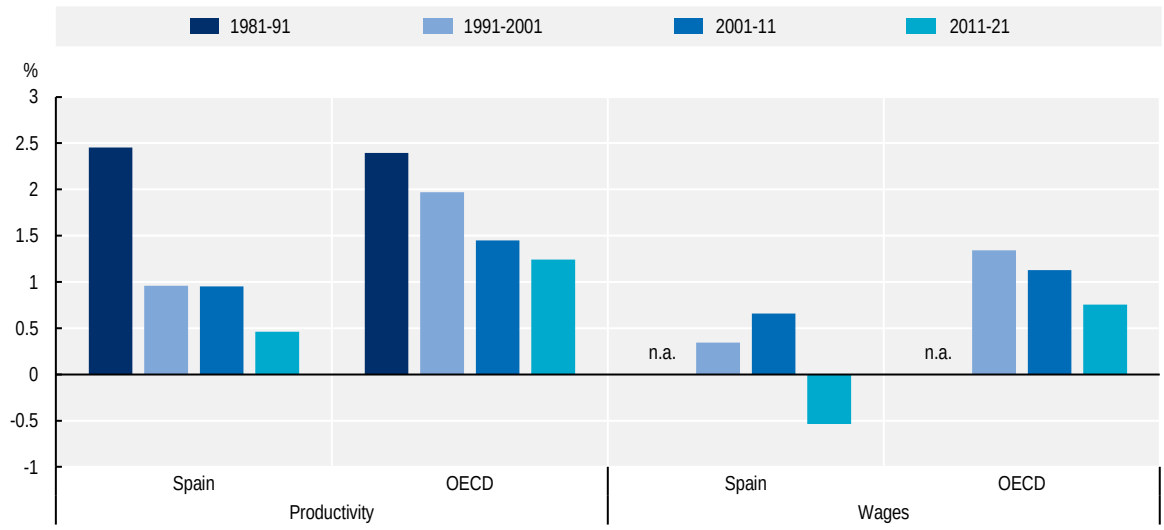
The objective of this chapter is to provide an overview of the main messages of the report with respect to the role that labour market and non-labour market policies can play in reviving broadly shared productivity growth in Spain. To set the scene, it starts with documenting the decline in productivity growth and its underlying mechanisms. It then provides a brief discussion of how policies can enhance the adaptability of the economy and the labour market to structural change. It then discusses in more depth the role of selected labour market policies in promoting broadly shared productivity gains. The emphasis is on wage-setting institutions, employment protection and job retention support, consistent with the focus of recent reforms in Spain. The chapter concludes with concrete recommendations to revive broadly shared productivity growth and enhance labour market performance more generally.

1.2. The slowdown in productivity and wage growth in Spain

For several decades, Spain has experienced consistently low levels of productivity and wage growth. The decline in productivity growth began in the mid-1990s, earlier than in many other OECD member countries, and this slowdown has been particularly significant. In recent years, the rate of productivity growth, measured in terms of total output per hour worked, has only averaged 0.5% per year in Spain, whereas the OECD as a whole has seen an average of 1.2% (Figure 1.1). Consequently, Spain's productivity performance has fallen below the OECD average, with significant implications for the growth of real wages and the overall standard of living. In fact, real wage growth in Spain has remained close to zero since the 1990s, and it even turned slightly negative in the 2010s, failing to keep pace with already weak productivity growth. Weak real wage growth is therefore not just a sign of lagging productivity growth but also reflects additional factors, related to for example changes in wage-setting due to a decline in the bargaining of power of workers or composition effects due to the growing concentration of productivity gains in capital-intensive firms. This suggests that to restore real wage growth, there is a need not only to revive productivity growth, but potentially also for strengthening wage-setting institutions.

Figure 1.1. Productivity and wage growth have been particularly weak in Spain

Average annual growth (%)



n.a. Not available.
Note: Productivity is GDP per hour worked. Wages refer to the average across full-time and full-year employees. See Chapter 2 for full details.
Source: OECD Productivity Statistics Database; see Figure 2.1 of this report (Chapter 2) for more details.

The slowdown in labour productivity growth in Spain reflects three fundamental challenges. While many OECD countries have been confronted with similar challenges, they have tended to be more pronounced in Spain.

1.2.1. Slower labour productivity growth mainly reflects a slowdown in making efficiency gains

The bulk of the decline in productivity growth reflects a slowdown in multifactor productivity (MFP) growth, i.e. the slower pace of advancements in the efficiency with which labour and capital are used in the production process thanks to, for example, the adoption of more advanced production technologies and management practices in firms, and the reallocation of capital and labour from less to more efficient firms. MFP growth fell from about 1% in the late 1980s to about 0.25% in the 1990s and even turned slightly negative in the 2000s. Low MFP growth in Spain reflects in part the difficulties of firms and workers to adapt to rapid structural change driven by technological developments and globalisation.

1.2.2. But lower labour productivity growth also reflects a persistent decline in investment

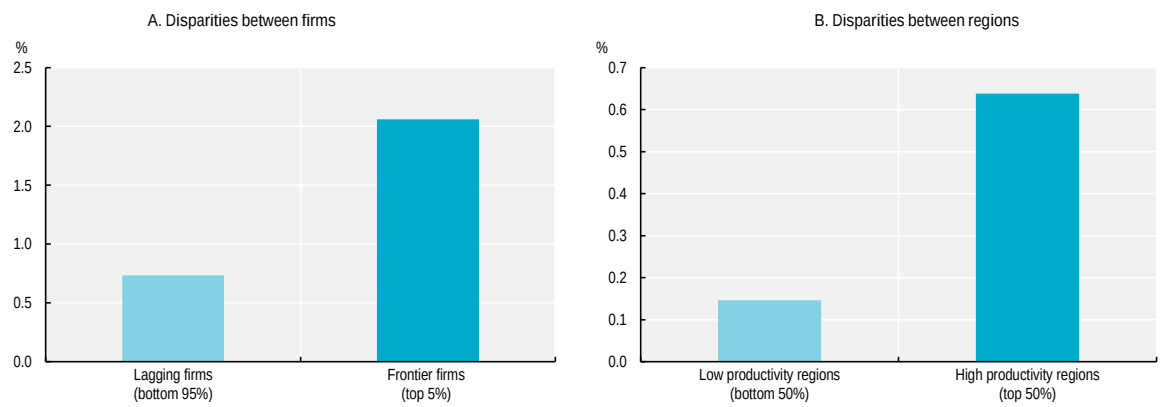
Slow growth in labour productivity also reflects a decline in the pace of capital deepening due to persistently weak investment in the aftermath of the global financial crisis. The decline in investment was particularly sharp in Spain due to the collapse of a housing and real estate bubble as well as the banking sector's exposure to the housing sector. While investment in Spain held up well during the COVID-19 crisis and its aftermath until 2022, thanks in part to the role of crisis-support and recovery packages put in place by the government, it remains well below its historical average, its level in the OECD on average or nearby countries such as France and Italy. Factors that continue to weigh on investment include weak MFP growth, high economic uncertainty, and enduring financial weaknesses.

1.2.3. Weak labour productivity growth is concentrated in lagging firms and regions

Slow growth in labour productivity is concentrated in lagging firms and regions and hence coincides with deepening economic inequalities (Figure 1.2). While the top 5% of most productive firms in Spain, so-called frontier firms, exhibit healthy labour productivity growth (about 2% per year on average), comparable to that of their counterparts in other OECD countries, labour productivity growth among other firms, so-called lagging firms, has fallen behind considerably (Panel A). A similar pattern is observed across regions, with productivity growth in lagging regions falling behind that of more advanced regions (Panel B). Weak productivity growth in lagging firms and regions is likely to reflect various factors: difficulties in adopting increasingly complex technologies that require high levels of human and organisational capital; weak incentives for firms with structural difficulties to downsize; and barriers to the mobility of workers from lagging to more advanced firms and regions.

Figure 1.2. Slow labour productivity growth is concentrated in low productivity firms and regions

Labour productivity average growth rate



Note: Panel A. Average growth in value-added per worker across firms (2010-18). Panel B. Average GDP growth per worker (2011-19). Firms and regions are classified into lagging and leading categories based on the initial productivity level at the start of the period.
Source: Preliminary calculations following the methodology in Andrews, Criscuolo and Gal (2016[1]) using the 2021 vintage of the Orbis firm-level financial accounts database by Moody's/BvD, with acknowledgments to Natia Mosiashvili for carrying out the calculations. OECD Regional Statistics Database. See Figure 2.3, Panel A and Figure 2.4, Panel B of this report (Chapter 2) for more details.

1.3. Policies to enhance labour market adaptability

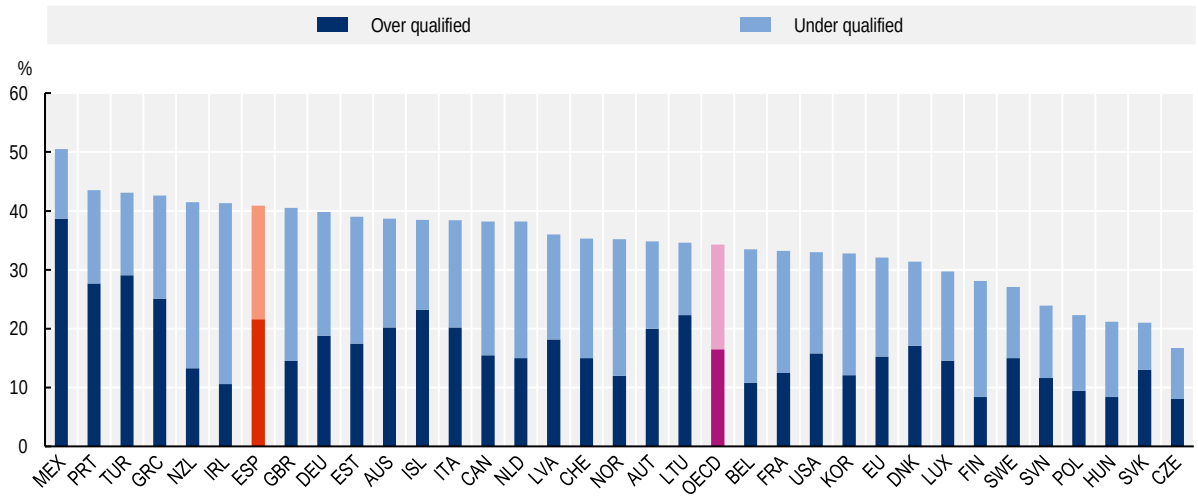
To revive labour productivity growth, a key challenge is to enable firms and workers to increase their efficiency by allowing them to seize upon the opportunities provided by technological change and globalisation. This requires amongst others addressing persistent skill imbalances that limit the adoption of new technologies, promoting the adoption of more advanced technologies while supporting the allocation of resources from less to more productive firms, and tackling regional disparities in productivity.

1.3.1. Significant skill imbalances prevent the full use of new technologies

In Spain, a mismatch between the skills provided by workers and those required by firms hamper productivity growth. Compared to other OECD countries, a sizeable share of workers report having higher qualifications than required for their job (22% compared with 17% for the OECD), and to a lesser extent, that they lack the qualifications that are needed (19% compared with 18% for the OECD) (Figure 1.3). While some mismatch is inevitable in a rapidly changing economy, its relative importance in Spain is likely to hold back productivity growth and contribute to persistently high levels of unemployment.

Figure 1.3. Qualification mismatch is common in Spain

Percentage of mismatched workers, 2019



Note: Data refer to 2019, with the following exceptions: they refer to 2017 for Korea; to 2016 for Australia; to 2015 for Türkiye.
Source: OECD Skills for Jobs database (2022), https://www.oecdskillsforjobsdatabase.org/.

To improve the relevance of skills for labour market needs, Spain needs to confront a number of challenges. First, it needs to tackle early school leaving, which remains more common than in most other countries despite progress in recent years: in 2021, 13% of the 18-24 year-olds leave school without having gone beyond lower secondary education, compared to an OECD average of 9%. Prevention can work through measures that enhance attitudes to learning such as investments in early education and care and targeting educational resources at disadvantaged students. Second, there is a continued need for building stronger links between the world of education and the world of work. Expanding student enrolment in vocational education and training (VET) in particular should be a priority. The new Organic Law on Vocational Education (March 2022) may help, but its success crucially hinges on its implementation. Involving businesses more closely in the design of degrees and curricula can further help to improve the match between the skills acquired in education and labour market needs. Third, as in most other OECD countries, continued efforts are needed to promote a culture of adult learning and training to ensure that worker skills evolve in line with changing labour market needs. This requires investing more in adult learning to ensure that adults, particularly those with low skills, can upgrade their skills, and in doing so, remain employable and contribute to productivity growth.

1.3.2. Supporting productivity growth in firms

Low productivity growth in Spain mainly reflects low growth among low-productivity firms whereas growth among frontier firms has remained robust. A first priority therefore is to support productivity growth in lagging firms by promoting the diffusion of new technologies. Tackling skills imbalances will facilitate the adoption of advanced technologies in lagging firms, but specific measures that focus directly on lagging firms are also needed. This includes measures that promote investment in intangible assets (e.g. managerial talent, software and R&D) by easing financial frictions and scaling up support for R&D. It also involves initiatives that enhance access to digital communications networks in underserved areas through a combination of private and public investment. Providing a sound regulatory framework that supports the reallocation from less to more productive firms by removing barriers to entry and exit is also important and can help to alleviate skill mismatches between firms and workers (e.g. insolvency procedures, product market regulations, employment protection).

1.3.3. Tackling regional disparities in productivity

Tackling disparities in productivity across regions requires a combination of place-based policies to support disadvantaged regions (e.g. education, training, activation) and policies that can promote geographical mobility from disadvantaged regions to high-performing ones. Since the implementation of active labour market policies (ALMPs) is the responsibility of regions, more attention could be devoted to assessing the effectiveness of regional skills and training policies, identifying best practices, providing policy guidance and promoting the adoption of more effective policies in lagging regions, in line with the recent *Programa de Aprendizaje Mutuo*. Geographical mobility can also help reducing regional disparities but tends to be low in Spain. It can be promoted by making location-based welfare entitlements portable, as was done through the introduction of the "social card" and ensuring that affordable housing is available for workers from lagging regions through the use of housing allowances, rent ceilings or social housing targeted to low-income households.

1.4. Policies to enhance the functioning of the labour market

Labour market policies also have an important role to play in reviving broadly shared productivity growth. The discussion below mainly focuses on wage-setting institutions, employment protection and job retention support, consistent with the focus of recent labour market reforms.

1.4.1. Wage-setting institutions have been strengthened

Wage-setting institutions in the form of minimum wages and collective bargaining have significantly been strengthened to promote a broader sharing of productivity gains with workers, particularly those with low wages.

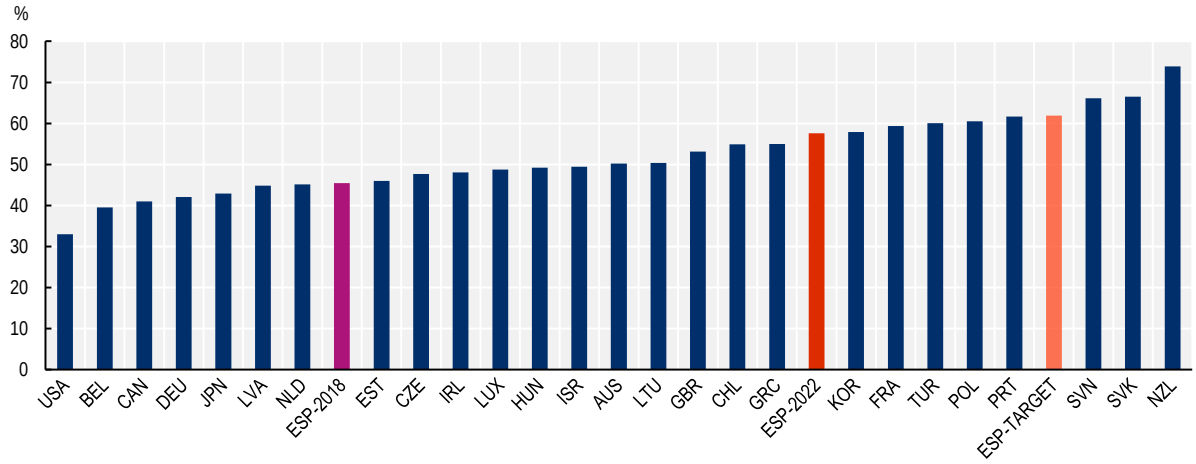
The renewed importance of the minimum wage as a policy tool should not just reflect its level but also its design

The minimum wage has gained significant importance as a policy tool in recent years (Figure 1.4). Until 2018, it only played a modest role as it was set at a relatively low level by OECD standards, around 45% of the median wage in the private sector. However, since then it has rapidly increased. It reached 58% of the median wage in 2022, with most of the increase taking place in 2019, and is set to increase further to 60% of the average net wage, which corresponds to about 62% of the gross median wage, the fourth highest in the OECD. Evidence on the effects of the minimum wage reform of 2019 tend to suggest that this significantly increased the wages of low-wage workers without significantly undermining their employment opportunities (see Box 1.1). These findings are broadly in line with similar studies for other countries.

To ensure that the minimum wage continues to support a broad sharing of productivity gains without undermining employment, a number of actions could be considered. First, continue supporting the work of the minimum wage commission by strengthening its resources to monitor and evaluate the effects of the minimum wage on the labour market, while ensuring that both trade unions and employers take part. This also requires investing in data that allow tracking the wages of individual workers in a timely manner. Second, explore ways to enhance the effectiveness of the minimum wage in supporting the incomes of low-wage workers. For example, an in-work benefit could be introduced to further reduce in-work poverty. More generally, it will be important to ensure that the increased relevance of the minimum wage as a policy tool is reflected in its institutional set-up and design.

Figure 1.4. The minimum wage in Spain is being revalued

Minimum wage as a share of median wage, 2022 unless indicated otherwise



Notes: The figure represents the minimum gross wage in 1 January 2022 as a share of the 2022 gross median wage in the private sector (unless stated otherwise). ESP-2018 refers to the 2018 minimum gross wage as a share of the gross median wage for 2018. ESP-target refers to the target minimum gross wage equivalent to 60% of the average net wage as a share of the median gross wage in 2022.
Source: OECD Tax-Benefit model, see Figure 3.1 (Chapter 3) of this report for more details.

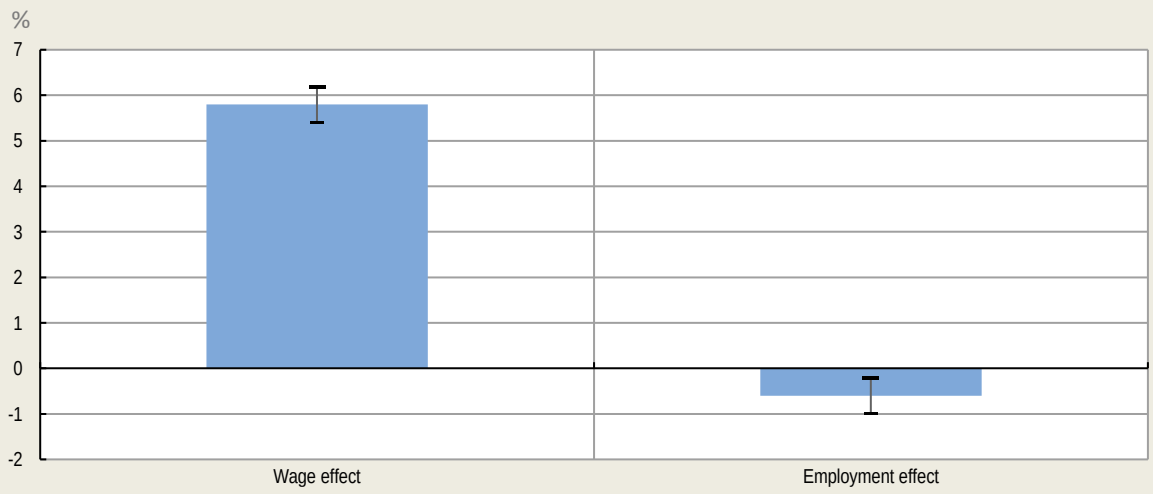
Box 1.1. An assessment of the 2019 minimum wage hike in Spain

In the context of this review, the OECD conducted an evaluation of the impact of the minimum-wage reform that took place in Spain in 2019 (Hijzen, Pessoa and Montenegro, 2023[2]). The reform increased the minimum wage by a 22% in a single step, affecting approximately 7-8% of employed individuals. The evaluation relied on an in-depth analysis of individual-level data in which the outcomes of workers employed in the year prior to the reform are tracked over time.

The results of the evaluation indicate that, among the workers directly affected by the minimum wage increase, the reform increased monthly earnings by on average 5.8% and reduced employment by 0.6% or about 7 000 jobs (Figure 1.5). Further analysis indicates that job losses were more pronounced among workers holding fixed-term contracts. In summary, the 2019 minimum-wage hike had a significant positive effect on the wages of low-wage workers, without causing substantial job losses.

Figure 1.5. The wage and employment effects of the 2019 minimum wage hike in Spain

Change in outcome between 2018 and 2019 relative to that between 2017 and 2018



Note: Estimated coefficients plus 95% confidence intervals based on clustered standard errors by province, industry and wage bin.
Source: Hijzen, Pessoa and Montenegro (2023[2]), "Minimum wages in a dual labour market: Evidence from the 2019 minimum-wage hike in Spain", https://doi.org/10.1787/7ff44848-en.

Continue efforts to promote social dialogue in the workplace and at national level

To further promote a broad sharing of productivity gains, the labour market reform of 2021 has considerably strengthened sectoral collective bargaining and the position of sectoral trade unions. To some extent, this reverses the 2012 labour market reform that sought to decentralise the system by providing more scope for negotiation at the firm level. The initial hope was that this would contribute to more flexibility at the firm level and support employment and productivity growth. It is not clear however whether the 2012 reform has indeed led to more negotiation at the firm-level, possibly due to the lack of worker representation in smaller firms. However, there are concerns that it has undermined the bargaining position of trade unions at the sectoral level and that this has contributed to the decoupling of wage growth from productivity growth.

To allow making use of the remaining scope for negotiation at the firm-level and support the quality of labour relations more generally, further efforts could be made to promote the representation of workers in the workplace, especially in smaller firms, as has been done for example in Italy (see Chapter 3 for details). At the same time, there is a continued need to involve the social partners at the national level in the co-ordination of wage agreements across sectors, including to ensure that the costs of increased energy prices are fairly shared between firms and workers, and the development of broad-based forward-looking reforms that can help to make the labour market more adaptable to future challenges.

1.4.2. The use of temporary contracts has been curtailed

Employment protection can contribute to stronger productivity growth by strengthening incentives for the accumulation and preservation of firm-specific human capital in the workplace based on stable employer-employee relationships and the use of high-performance work and management practices. However, evidence for OECD countries suggests that it can also undermine productivity growth by reducing the tendency of firms to adjust employment in line with changing business conditions and strengthening incentives for the use of flexible work arrangements, resulting in labour market duality. From a productivity perspective, it is therefore crucial that employment protection strikes the right balance between supporting job reallocation and providing incentives for learning and innovation.

The excessive reliance on fixed-term contracts presented a major challenge for Spain. To tackle labour market duality, the use of fixed-term contracts has been significantly restricted. Since the entry into force of the 2021 labour market reform, open-ended contracts became the default contract, while the use of fixed-term contracts has been strictly limited to temporary staff needs. More specifically, i) the very flexible and widely used contract for work and service (*contrato por obra o servicio*) has been abolished, ii) the existing training contracts (*contrato de trabajo en prácticas* and *contrato para la formación y el aprendizaje*) have been replaced with two shorter training contracts (*contrato para la obtención de la práctica profesional* and *contrato de formación en alternancia*); and iii) the requirements to justify the temporary nature of needs have been strengthened. As a result, Spain has become the country with the third strictest rules for the use of fixed-term contracts in the OECD (Figure 1.6). Another important part of the reform, but one that is not reflected in the OECD Employment Protection indicators, is the increased scope for the use of open-ended intermittent contracts (*contrato fijo-discontinuo*) to all intermittent activities, temporary agency work, and contract work. Consequently, open-ended intermittent contracts can be used for many of the activities that were previously conducted with temporary contracts.

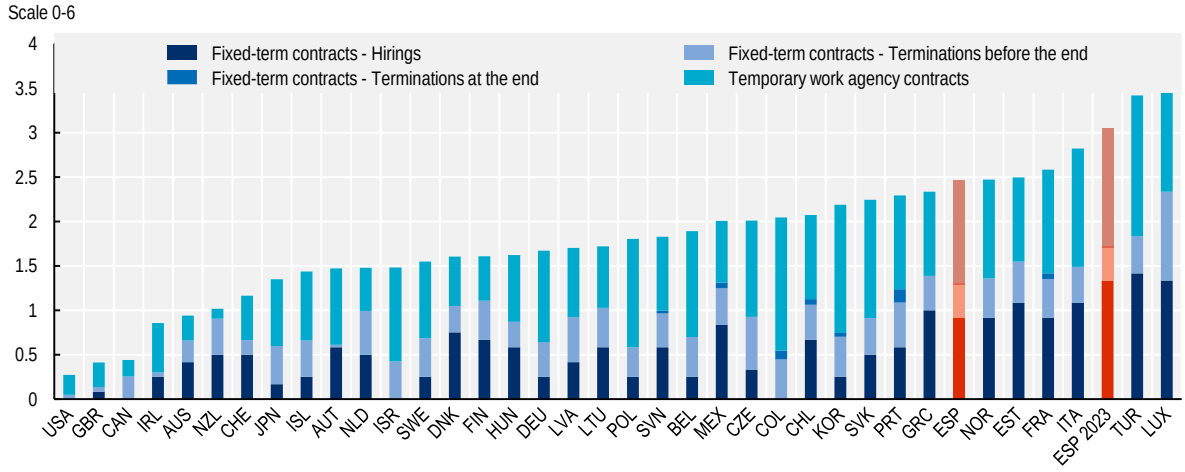
The reform has resulted in a sharp reduction in the incidence of fixed-term contracts during the first year following its implementation. The incidence of fixed-term contracts declined by about a quarter from more than 20% in 2021, the second highest in the OECD, to less than 15% in the first quarter of 2023. Moreover, the decline in the number of fixed-term contracts is offset by a similarly sized increase in the number of open-ended contracts, suggesting that for now the reform did not have major effects on overall employment. A significant fraction of the increase in permanent employment, about 20%, reflects the increased use of *open-ended intermittent contracts.* Its incidence in employment doubled from 2.7% in 2021Q1 to 5.3% in 2022Q4. Such contracts offer more employment stability than temporary contracts but not necessarily more income security for workers. Although working hours are known in advance, they may vary over time depending on the length of the period of activity and the season, within the limits of the applicable sectoral collective agreement. The medium-term implications of the reform need to be closely monitored. The government has committed to a full evaluation of the reform by 2025.

Looking ahead, there may be a case for further adjusting the regulation of contracts. First, the appropriate use of all contracts should continue to be closely monitored and transitions from temporary and intermittent contracts to regular open-ended contracts could be promoted further. While efforts are already made to promote such transitions (e.g. systematically informing workers of vacancies for regular open-ended positions in the same firm; promoting training during periods of inactivity) more could be done (e.g. paying

more attention to career guidance, developing flexible courses that can be combined with intermittent contracts). Second, workers could be given greater incentives to terminate open-ended contracts by mutual consent under certain circumstances. Unlike in many other OECD countries, workers who end their contract by resignation or mutual consent are not entitled to unemployment benefits and cannot easily access public employment services. This reduces the willingness of workers to terminate contracts voluntarily and increases the cost of dismissal for firms. Third, the balance between the length of notice period and other aspects of employment protection could be adjusted. Notification periods are currently relatively short, which makes it hard for the public employment services to intervene early before dismissal takes place. To allow intervening earlier and provide more effective support to displaced workers, the notification period could be increased, while other aspects of employment protection could be adjusted to keep the overall stringency of employment protection constant.

Figure 1.6. The regulation of employment contracts is relatively strict in Spain

Regulation of fixed-term and temporary work-agency contracts (0-6), 2019 and 2022



Source: OECD EPL database, see Figure 3.7 (Chapter 3) of this report for more details.

1.4.3. The scheme of job retention support has become a model for best practice

Job retention schemes aim to safeguard temporarily vulnerable jobs by enabling companies to adjust their workforce in response to economic downturns while also providing financial support to employees facing suspensions or reduced working hours. From a productivity standpoint, the primary benefit of these schemes lies in the preservation of company-specific skills and expertise in positions that may be temporarily unprofitable but have long-term viability. A potential drawback is that job retention support might be used to sustain jobs in businesses experiencing structural challenges, potentially impeding the efficiency-enhancing reallocation of jobs among different companies that differ in their productivity.

While the use of job retention support was negligible during the global financial crisis, it played a major role in preventing job losses during the COVID-19 crisis in Spain. In April 2020, just one month after the outbreak of the pandemic, almost one in four workers were covered by *Expedientes de Regulación Temporal de Empleo* (ERTE). Thanks to the widespread use of job retention support, the increase in unemployment in response to the decline in economic activity was several times smaller during the COVID-19 crisis than during the global financial crisis when unemployment surged. The positive impact of job retention support on employment is also confirmed in an ongoing evaluation by the OECD (2024, forthcoming[3]). Moreover, the use of job retention support declined quickly as economic restrictions were withdrawn and the generosity of support scaled back. The fact that take-up did not persist long into the

recovery is reassuring and suggests that ERTE is unlikely to have had a major impact on slowing job reallocation from low-productivity firms with structural difficulties to high-productivity ones with healthy growth prospects.

The labour market reform of 2021 also affected the regulation of ERTE. It established the parameters for the permanent scheme and introduced an explicit framework for scaling up support in times of exceptional need (the "RED mechanism") (OECD, 2024, forthcoming[3]). More specifically, the reform created two new types of ERTEs that can be "activated" in the case of either (i) macroeconomic cyclical downturns, or (ii) sectoral transformations that require substantial labour reallocation. These schemes are activated by the government, in the second case, following the request of a tripartite committee. This possibility is referred to as the "RED Mechanism". Once this mechanism is activated, firms can apply for the use of ERTE under a special procedure while benefiting from favourable exoneration rates to social security. Spain is now one of the few OECD countries with an explicit framework for scaling up support in times of exceptional need (RED Mechanism). It allows for government discretion over its activation while the parameters of the crisis scheme are defined in advance.

While ERTE already presents a well-designed job retention scheme, it may still be possible to further enhance its effectiveness in the future. For example, the effectiveness of training while on short-time work could be strengthened by requiring work-related training to be provided externally by certified external suppliers and monitoring the effectiveness of training courses through the use of regular evaluations. Moreover, the targeting of support could be enhanced by replacing direct co-financing by firms with experience-rated employer contributions. This could be part of a broader reform that introduces a bonus-malus system for the financing of unemployment insurance, following the examples of France and the United States. Such a system would provide incentives for employers to internalise the costs of short-time work, intermittent inactivity and layoff decisions for society without affecting the benefits for employees.

1.4.4. There is a growing debate on the potential role of a shorter working week for well-being and productivity

In Spain as well as in several other OECD countries, there is a growing debate on the possible role that working-time reductions can play in promoting well-being and productivity and the possible introduction of a four-day working week. Indeed, there is clear evidence that very long working hours increase health risks and reduce job satisfaction and hourly labour productivity. There is also some evidence based on working time reforms in different EU countries that reducing the normal working week can raise wages and productivity, with little or no effect on employment. The evidence on reducing the number of weekly working days to four remains patchy and tends to be based on small-scale trials with voluntary participation.

The current regulation of working time in Spain is similar to that in most EU countries. It limits statutory normal working hours, excluding overtime, to 40, while overtime has to remain within the limit of 80 hours per year. These rules comply with the EU Working Time Directive which limits total weekly hours including overtime to 48. However, it also allows for flexibility through the use of collectively agreed derogations in certain sectors and activities. The flexibility in the Spanish system suggests that collective bargaining can play a potentially important role in reducing normal and maximum weekly working in cases where this is likely to increase worker well-being as well as productivity.

The government should build on the strong involvement of the social partners in the regulation of working time to promote policy experimentation and expand the evidence base. This should help to better understand to what extent a shorter working week can generate sufficiently large productivity effects to compensate employers for the increase in hourly labour costs and/or workers for the loss in earnings (depending on the way the shorter working week is implemented), and the extent to which any productivity effects depend on the way the shorter working is organised (more compressed worker schedules over fewer days or fewer hours per day) and the economic activity of the firm.

Box 1.2. Recommendations to revive broadly shared productivity growth in Spain

Framework conditions

- Support lagging firms by fostering the adoption of advanced digital technologies and efficient management practices, promoting investment in intangible assets and enhancing access to digital communications networks.
- Continue efforts to provide a regulatory framework that supports the reallocation of resources from less to more productive firms (e.g. insolvency regulations, product market regulations, employment protection).

Education and training policies

- Increase the inclusiveness of the education and training system by tackling early school leaving and remedying skills gaps through second-chance schools and adult learning programmes.
- Enhance the responsiveness of the education and training system to changing labour market needs by promoting a culture of life-long learning, increasing the number of places in vocational education and training (VET) and involving employers more strongly.

Minimum wages, working time and collective bargaining

- Continue supporting the work of the minimum wage commission, by ensuring that both trade unions and employers take part and strengthening its resources to monitor and evaluate the effects of the minimum wage on the labour market.
- Explore ways to further enhance the role of the minimum wage by leveraging its co-ordination with the tax-and-benefits system.
- Support social dialogue and organised decentralisation by further promoting the local representation of workers in firms.
- Continue supporting the efforts of the social partners to reach broad and forward-looking agreements such as that that led to the 2021 reform or the 2023 social pact on wages.
- Build on the strong involvement of the social partners in the area of working time to promote a better understanding of the effects of a shorter working week by facilitating policy experimentation and expanding the evidence base.

Employment protection and job retention support

- Continue monitoring the appropriate use of all types of contract and further support transitions to regular open-ended contracts.
- Establish procedures to promote termination by mutual consent while maintaining access to unemployment benefits under certain circumstances.
- Increase the length of the notification period to allow providing early support to dismissed workers, while adjusting other aspects to keep the overall stringency of employment protection constant.
- Promote the effectiveness of training while on short-time work by requiring work-related training to be provided externally by certified suppliers and conduct regular evaluations to assess the effectiveness of training courses.

Unemployment benefits and activation policies

- Experience-rate employer social security contributions for unemployment insurance and short-time work.

- Provide employment services to workers who are at risk of job loss by intervening early during the notice period for dismissal or reaching out to workers on short-time work for structural reasons.
- Enhance the effectiveness of active labour market policies in lagging regions by identifying best practices and providing technical and financial support to local providers.

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2 The challenge of weak wage productivity growth and possible policy responses

Alexandre Georgieff and Alexander Hijzen

In Spain, productivity growth has been persistently weak in recent decades. This reflects lower multi-factor productivity growth due to difficulties in adapting to technological change and globalisation, lower capital deepening due to the persistent decline in investment following the global financial crisis and growing disparities in productivity due to weak productivity growth in lagging firms and regions. Reviving productivity growth requires amongst others investing in worker skills, promoting the adoption of new technologies in lagging firms while enhancing the reallocation of resources from less to more productive firms and tackling large and widening disparities in productivity between regions.

2.1. Introduction

Productivity growth has almost come to a halt in Spain, with important implications for real wage growth and the standard of living. During the decade from 2011-21, productivity growth averaged just 0.5% per year, less than half that of the OECD average. The primary objective of this chapter is to set the scene by providing an overview of the main factors that drive the slowdown in productivity. It also provides a first discussion of the main policy avenues for reviving productivity growth by i) investing in worker skills, ii) promoting technology diffusion and job reallocation between firms and iii) tackling regional disparities in productivity performance. Chapter 3 will provide a detailed overview of the specific role of labour market policies in reviving productivity growth in Spain, with an emphasis on wage-setting institutions and job-security provisions, since these were at the heart of the 2021 labour market reform.

2.2. The slowdown in productivity growth

Labour productivity in Spain has been growing slowly over the past three decades, resulting in a considerable decline in productivity performance compared to other OECD countries. While a productivity slowdown was observed in many other OECD countries, it began earlier in Spain and has been particularly marked. This has put downward pressure on wage growth and living standards and was exacerbated by the declining share of productivity gains that was passed on to workers, particularly those in the middle and bottom of the wage distribution. Slower multifactor productivity (MFP) growth was the main factor behind the low productivity growth in Spain until the global financial crisis (GFC). Since then, lower capital deepening has accounted for about one-third of the productivity slowdown.

2.2.1. Productivity has been rising slowly for three decades

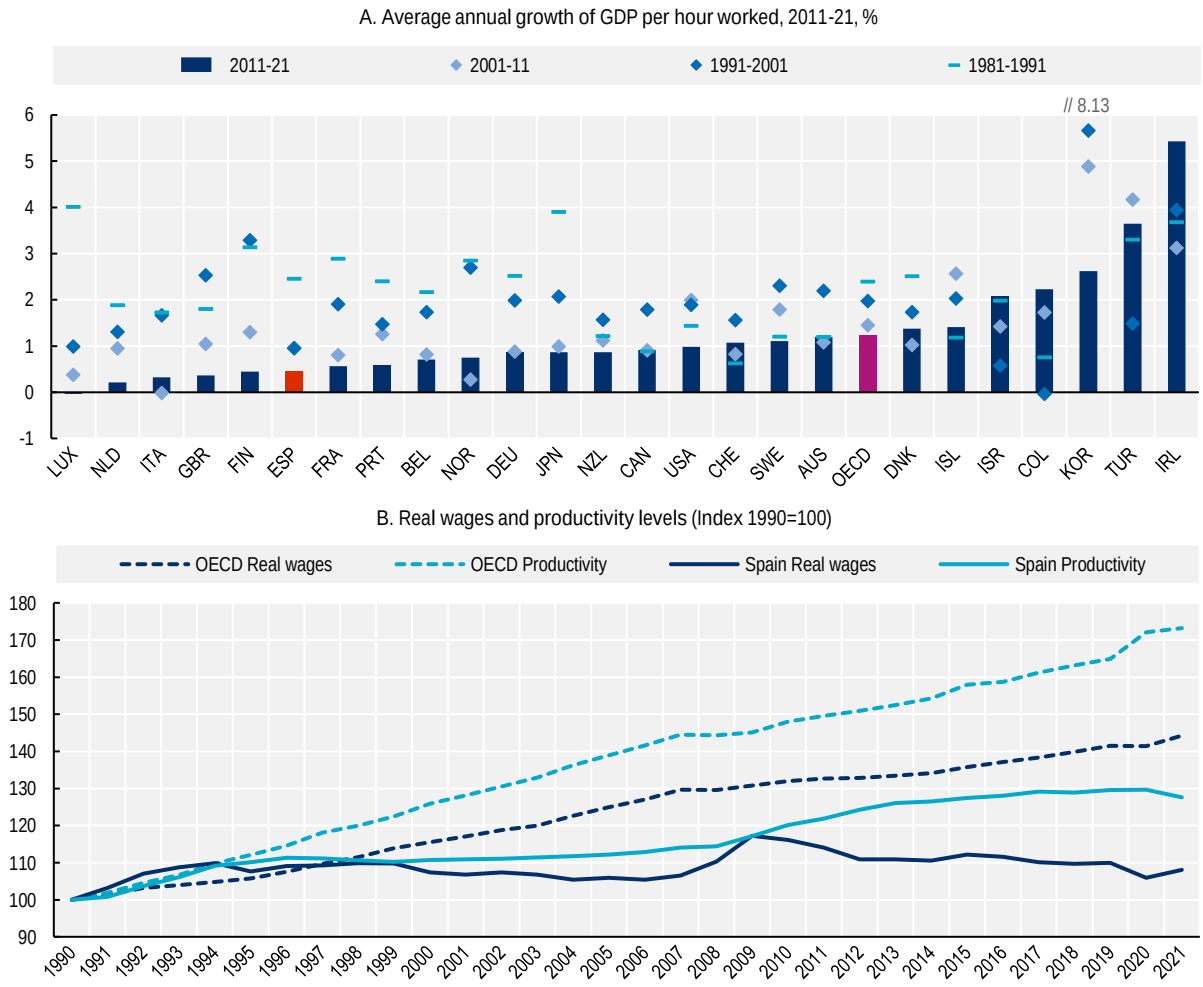
Labour productivity growth, measured in terms of real gross domestic product (GDP) per unit of labour, has been particularly weak over the past three decades in Spain (see Box 2.1 for details on the measurement of labour productivity). Over the period 2011-21, it grew by an average of 0.5% per year, one of the lowest rates among OECD countries and less than half of the OECD average (Figure 2.1 Panel A). The productivity slowdown in Spain began in the 1990s, well ahead of most other OECD countries, and has been particularly pronounced (Figure 2.1, Panel B). Productivity growth in Spain fell from 2.5% in the 1980s to less than 1% in the 1990s and 2000s and just 0.5% in the 2010s. For the OECD as a whole, the slowdown was less strong. Productivity growth declined from 2.5% in the 1980s to 2% in the 1990s, 1.5% in the 2000s and 1.2% in the 2010s. As a result, Spain's labour productivity performance has deteriorated considerably in recent decades, both in absolute terms and relative to other OECD countries, from above-average in 1991 to below-average in 2021 (Figure 2.2).[1]

Low productivity growth puts downward pressure on wage growth and the rise in living standards. Real wage increases are one of the main channels through which productivity gains are passed onto workers, along with better working conditions and enhanced employment opportunities (OECD, 2018[1]). It is therefore not surprising that real wage growth has been low in Spain compared with other OECD countries over the last couple of decades (OECD, 2021[2]). However, average real wage growth was considerably lower still than productivity growth, resulting in a decline in the labour share. Indeed, real wage growth was close to zero between 1995, at the time when productivity growth stalled, and 2021. Declining labour shares and weak real wage growth have been observed in many other OECD countries, suggesting that this is in part the result of common structural developments, such as globalisation and technological change that have eroded the bargaining power of workers.

In addition, limited productivity gains have not been broadly shared. Wage growth at the bottom and at the middle of the wage distribution has not kept pace with average wage growth, resulting in rising wage inequality and negative real wage growth for some groups of workers. For example, the real wage of young

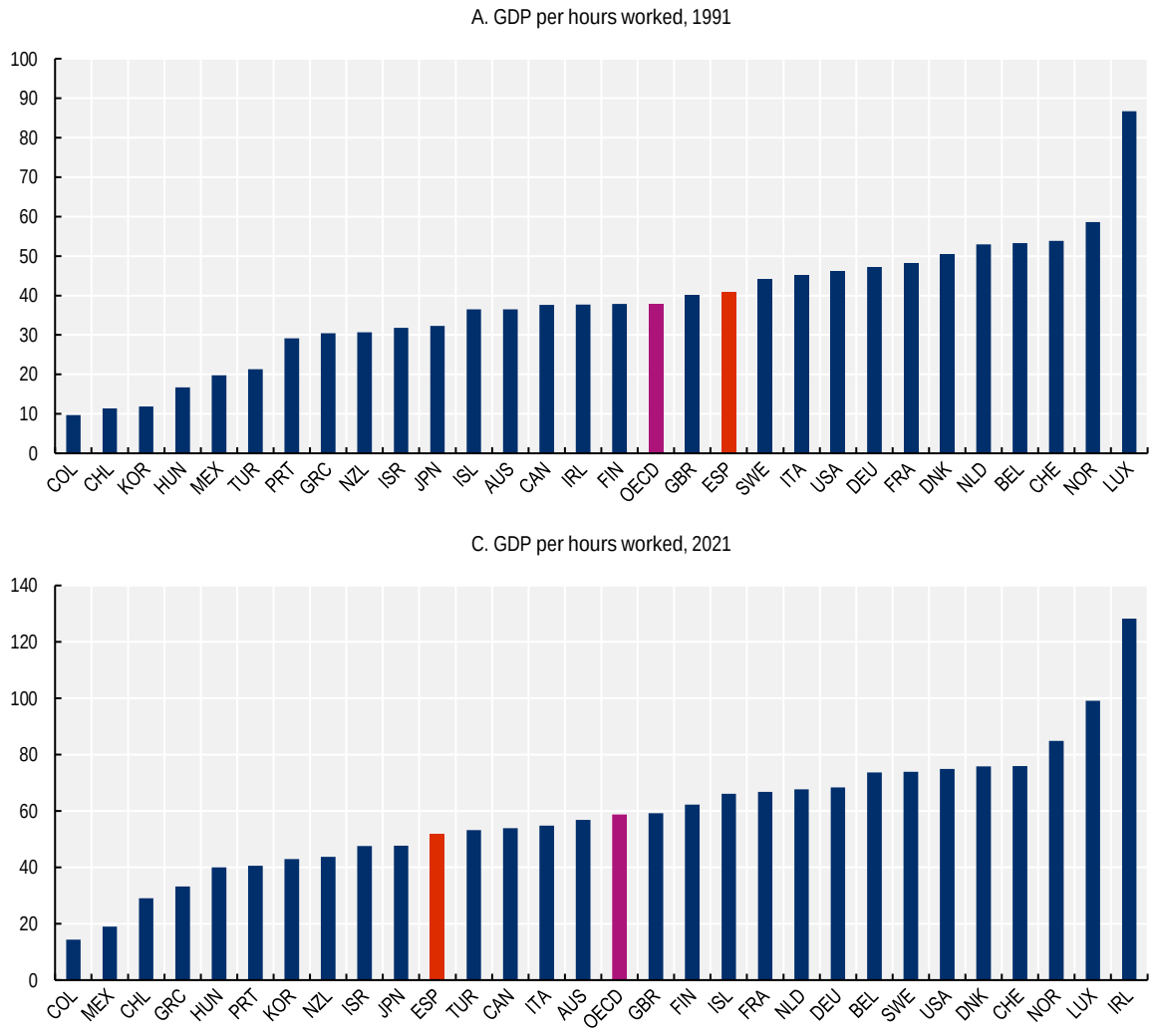
Spaniards has tended to decline over the last couple of decades (OECD, 2023[3]). The increase in wage inequality is similar to the pattern observed in many other OECD countries and is consistent with the secular increase in the relative demand for skilled workers, as a result of the integration of low-wage countries in the world economy (e.g. China) and skill-biased technological change.

Figure 2.1. **Spain's labour productivity growth has fallen sharply since the 1990s**



Note: Panel A: Data are measured in constant prices USD 2015 purchasing power parities. OECD is the unweighted average among the countries analysed. Panel B: Productivity is GDP per hour worked. Wage are average annual wages per full-time and full-year equivalent employee in the total economy. OECD unweighted average for Australia, Belgium, Canada, Denmark, Finland, France, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, the Netherlands, New Zealand, Norway, Spain, Sweden, Switzerland, the United Kingdom, the United States.
Source: OECD Productivity Statistics Database.

Figure 2.2. **Spain's labour productivity performance has deteriorated considerably in recent decades**



Note: Data are measured in constant prices 2015 USD purchasing power parities. OECD is the unweighted average among the countries analysed.
Source: OECD Productivity Statistics Database.

Box 2.1. Measuring labour productivity and its components

Labour productivity measures the total volume of output produced, in terms of the real gross domestic product (GDP) per unit of labour. Total hours worked is generally the preferred measure of labour input, as it accounts for differences in total working hours per person across countries. In practice, the number of persons employed is often used as a proxy for labour input, as data on total hours worked are not always available or readily comparable across countries (OECD, 2018[4]).

Cross-country comparisons of hourly labour productivity need to be considered carefully. One particular issue is that information on total hours workers and information on production is gathered from different sources, which may result in slight differences in the range of economic activities covered. As a result, productivity estimates that rely on information on total hours workers from labour force surveys without correcting for differences in coverage tend to be biased downwards. The hourly labour productivity figures presented in this chapter use the adjustment procedure proposed by Ward, Zinni and Marianna (2018[5]).

Some analysts have pointed to the possibility that productivity growth might be underestimated due to the difficulty of fully accounting for the growing importance of the digital economy (the "mismeasurement hypothesis"). For example, intangible assets (e.g. brand recognition, intellectual property, software and computerised information) may not be fully captured, which can lead to underestimating output growth, and therefore productivity growth (Brynjolfsson, Rock and Syverson, 2021[6]). Most researchers, however, concur that these potential mismeasurements – while deserving more attention – are not sufficient to explain the productivity slowdown (Ahmad, Ribarsky and Reinsdorf, 2017[7]).

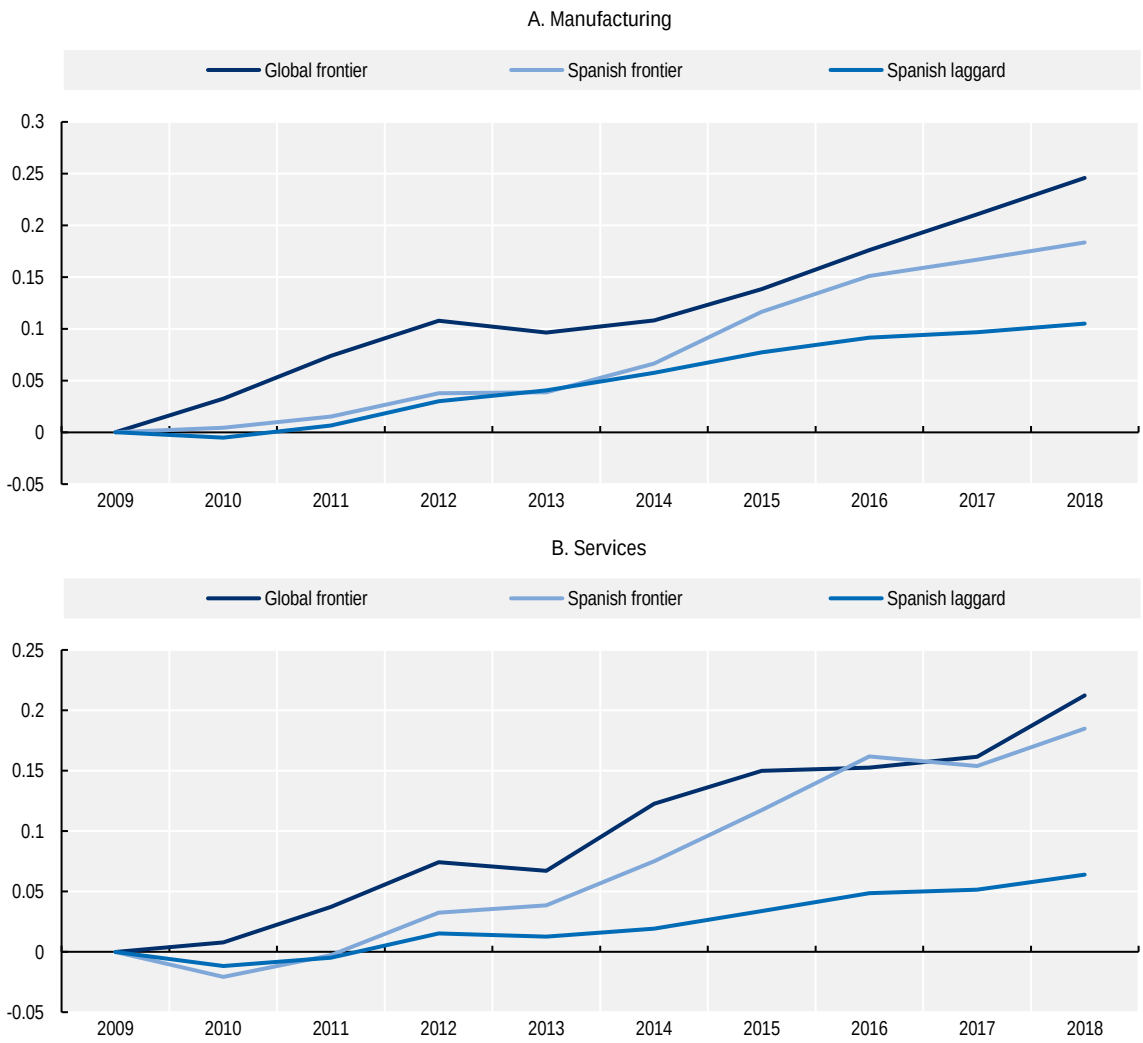
2.2.2. Disparities in productivity between firms and regions are widening

In Spain, as in many other OECD countries, the slowdown in labour productivity growth reflects to an important extent slow growth among low productivity firms, while growth in high productivity firms has remained robust (Figure 2.3). The top 5% of most productive firms in Spain, so-called frontier firms, exhibit healthy labour productivity growth (about 2% per year on average), comparable to that of their counterparts in other OECD countries. Labour productivity growth among other less productive firms, so-called lagging firms, however, has fallen considerably behind, particularly in services (1% per year in manufacturing, 0.5% in services). As a result, disparities in productivity between firms have been widening.

The slowdown in productivity growth among lagging firms is likely to reflect a combination of factors. It could reflect the growing difficulty for lagging firms to move from an economy based on production to one based on ideas. As technologies become more complex and their use increasingly hinges on the availability of human and organisational capital, this may have slowed the diffusion of new technologies from frontier to lagging firms (Berlingieri et al., 2020[8]; Gal et al., 2019[9]). But it could also reflect rising entry barriers and a decline in the contestability of markets. This is supported by evidence that suggests that the divergence in productivity growth is more pronounced in more strictly regulated product markets (Andrews, Criscuolo and Gal, 2016[10]).

Figure 2.3. The labour productivity slowdown has been more marked among laggard firms

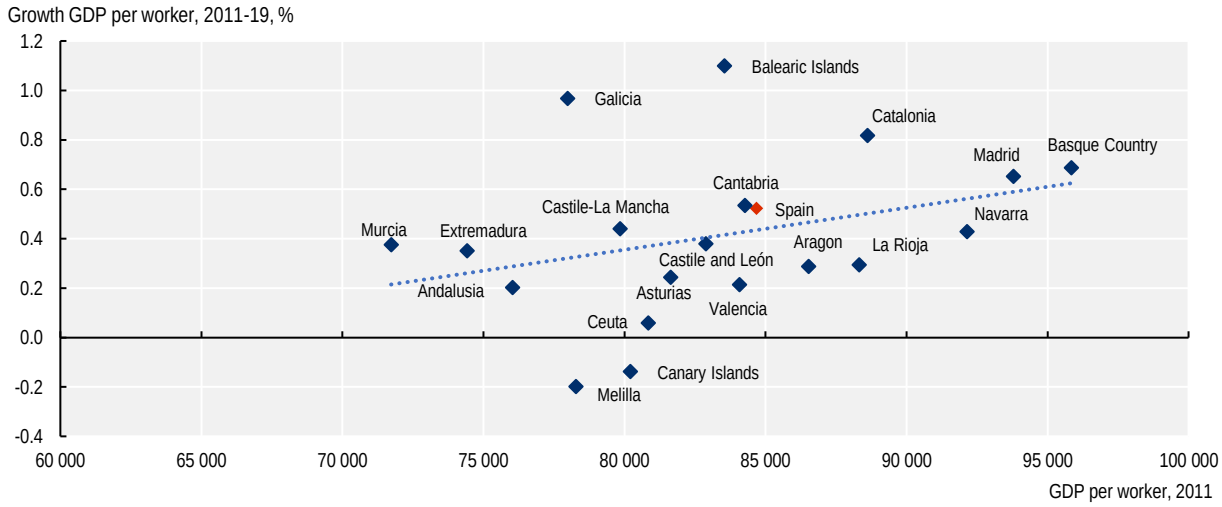
Log value added per person employed (2009 = 100)



Note: Average across detailed manufacturing and services industries using firm-level data. 3-year moving average. Labour productivity is defined as value added per employee. Productivity frontier is defined as the average of the productivity for the top 5% firms in the productivity distribution.
Source: Preliminary calculations following the methodology in Andrews, Criscuolo and Gal (2016[10]) using the 2021 vintage of the Orbis firm-level financial accounts database by Moody's/BvD, with acknowledgments to Natia Mosiashvili for carrying out the calculations.

Disparities in productivity growth across Spanish regions (autonomous communities) are significant and have tended to widen (Figure 2.4). Over the period 2000-19, average annual productivity growth was the strongest in the Balearic Islands and Galicia, about twice the nation-wide growth rate. In contrast, productivity declined somewhat in the Canary Islands and Melilla. There is no indication that lagging regions are catching up with higher productivity ones. On the contrary, productivity growth tends to be lower in regions with low levels of productivity, so that regional disparities are widening.[2] For example, the Canary Islands exhibit both low levels of productivity and strong declines in productivity, while regions in the North-East tend to exhibit high productivity levels and high growth.

Figure 2.4. Regional disparities in productivity are large and have tended to widen further



Note: GDP per worker is measured in constant prices, with 2015 as the base year. Region is the autonomous community of work (not residence).
Source: OECD Regional Statistics Database.

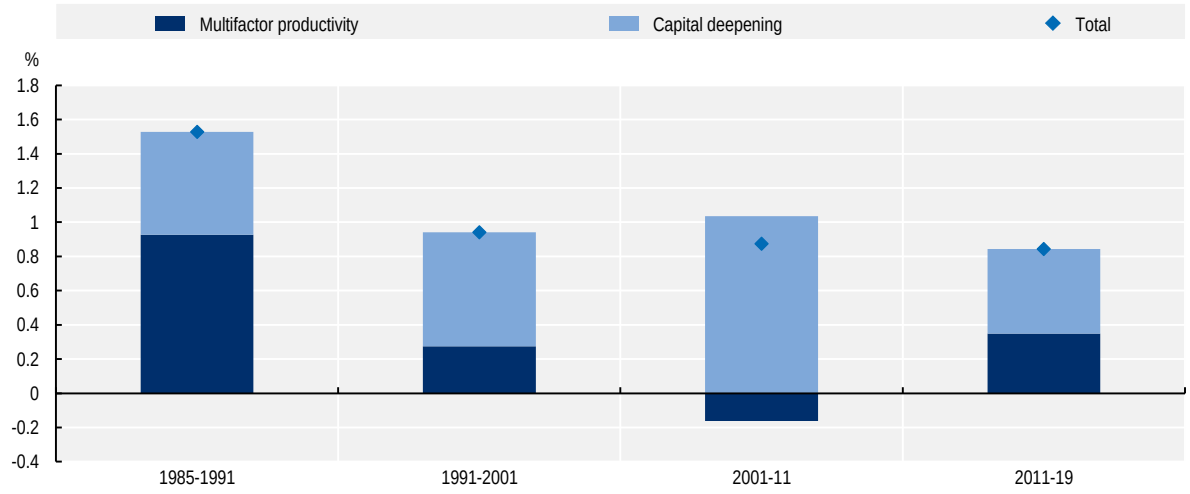
2.2.3. The productivity slowdown reflects both lower MFP growth and lower capital deepening

In theory, labour productivity growth can be promoted either by increasing the amount of capital per hour worked, i.e. capital deepening, or by improving the efficiency with which labour and capital are used in the production process, i.e. multifactor productivity (MFP). Aggregate MFP is primarily intended to reflect the efficiency of the production process (management practices, economies of scale and scope) and the efficiency of the allocation of resources across firms (including through firm entry and exit). However, since labour quality is not taken into account in the estimation of MFP, it may also capture the role of worker skills in practice.

The slowdown in labour productivity growth since the 1990s in Spain was largely driven by slower MFP growth. MFP growth fell from about 1% in the late 1980s to about 0.25% in the 1990s and even turned slightly negative to -0.2% in the 2000s. (Figure 2.5). During the 1990s and 2000s, labour productivity growth remained broadly constant as lower MFP growth was offset by increased capital deepening. Since the early 2010s, labour productivity growth remained low as capital deepening slowed following the global financial crisis despite the return to positive, although still weak, MFP growth.

Figure 2.5. The productivity slowdown was due to a weakening of MFP growth and, more recently also slower capital deepening

Average annual growth in Spain, percentage



Note: Data are measured in constant prices.
Source: OECD estimates based on OECD Productivity Statistics Database.

2.2.4. The slowdown in capital deepening reflects a sharp and persistent reduction in investment due to the global financial crisis

The reduction in capital deepening can be attributed to a significant and persistent decline in investment following the global financial crisis. Spain was highly susceptible to the crisis due to the presence of a housing and real estate bubble, as well as the banking sector's exposure to the housing sector. Before the global financial crisis, investment as a share of GDP was well above that of the OECD average, partly fuelled by the boom in construction (Figure 2.6). When the global financial crisis hit, investment declined sharply across the OECD, but particularly in Spain, bringing investment down to a level well below the OECD average. The recovery in investment has been weak and incomplete across the OECD, including Spain. Investment in Spain remains below its level at the onset of the global financial crisis as well as its historical average.

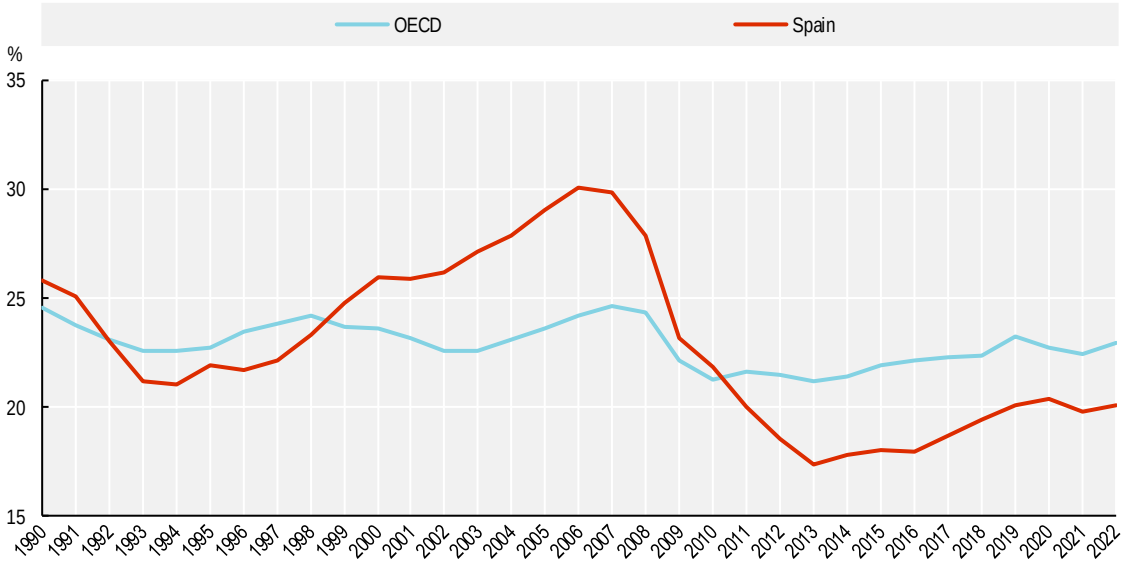
In contrast to the global financial crisis, most firms were able to preserve their investment capacity during the COVID-19 crisis. This reflected in part the fact that the financial system remained in good health during the COVID-19 crisis and in part the exceptional financial-support measures that were adopted by governments in response to the crisis (e.g. bank loan guarantees, deferrals of taxes and social-security contributions, and wage bill subsidies including through job retention schemes (OECD, 2020[11]). As the situation evolved, crisis-support measures were increasingly replaced by recovery measures under the National Recovery, Transformation and Resilience Plan (RTRP) and the EUs Next Generation programme (OECD, 2023[3]). These often take the form of public investment through public-private partnerships in strategic sectors where private investment is deemed insufficient.

Going forward, there is considerable uncertainty about the investment outlook given the tightening of monetary policy in the context of still high inflation and geopolitical instability as a result of Russia's war of aggression in Ukraine (OECD, 2023[12]). While investment in Spain has held up well since the COVID-19 crisis up until 2022, thanks in part to the role of crisis-support and recovery packages put in place by governments, it remains well below the average level in the OECD or nearby countries such as France and Italy. According to the government, the RTRP and associated reforms will boost GDP by about

3 percentage point in 2023 and 2024 (Ministerio de Asuntos Económicos y Transformación Digital, 2023[13]).

Figure 2.6. Investment has remained weak since the global financial crisis

Gross fixed capital formation, total economy, percentage of GDP



Source: OECD Annual National Accounts database.

2.2.5. Seizing upon new opportunities requires addressing structural factors that have weighted on MFP growth for a long time

The slowdown in MFP growth is largely structural in nature and reflects a combination of long-standing challenges:

- The difficulty of workers to adapt to changing work practices and the use of new technologies, including those requiring digital skills.
- The difficulty of firms to innovate, adopt new technology and introduce more efficient management and working practices.
- Large and growing disparities in productivity between regions.

Each of these challenges is likely to be affected by the transformative processes that were triggered or reinforced by the COVID-19 crisis. The pandemic accelerated the use of digital technologies in the workplace (e.g. video conferencing, cloud computing, and team-working tools) and the adoption of remote working practices. This shift allowed for greater flexibility and reduced commuting time, leading to improved productivity. The pandemic also expedited the adoption of automation and generative artificial intelligence (AI). The automation of routine tasks and increasingly also non-routine tasks enable employees to focus on more complex and value-added activities, increasing their productivity.

While these developments are likely to support stronger productivity growth, there is considerable uncertainty about the size of these effects and the extent to which the new opportunities provided by digitalisation, automation and generative AI can be effectively seized upon without first addressing the deeper structural challenges that have held back productivity growth during the past three decades. This further highlights the importance of addressing long-standing structural challenges for reviving productivity growth.

2.3. Reviving productivity growth

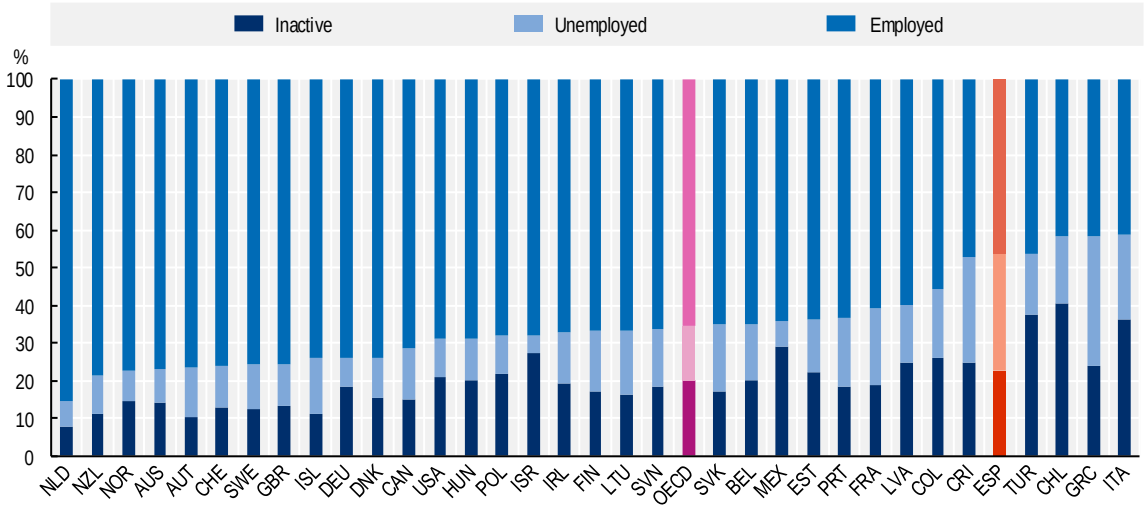
Weak productivity growth in Spain reflects a combination of long-standing structural challenges, mostly specific to Spain, and more recent challenges related to the broader global economic context. This section, however, will mainly focus on the deeper structural factors that were already holding back productivity growth in Spain before the global financial crisis. These are: i) the scarcity of skills needed to fully exploit the potential of new technologies, ii) structural barriers to productivity gains and innovation for firms, and iii) large and growing disparities in productivity between regions. This section describes these challenges and discusses a number of policy measures that could help address them. The specific role of labour market policies will be discussed separately in Chapter 3.

2.3.1. Significant skill imbalances prevent the full use of new technologies

In Spain, a significant skills mismatch between the skills provided by workers and those required by employers hamper productivity growth. Compared with other OECD countries, skill shortages are particularly marked in a number of areas important for innovation and the use of technology, such as engineering, computers and electronics, and may have contributed to underskilling, i.e. the share of workers reporting that they lack some of the qualifications required to perform their job (OECD, 2021[14]). These shortages have become more pronounced in recent years, as the demand for labour rose sharply during the economic recovery from the COVID-19 crisis (Salvatori, 2022[15]). At the same time, new labour market entrants continue to have difficulty finding a job despite progress in recent years (Figure 2.7). In 2021, among young Spaniards aged 18-24 who are not in education or training, more than half are unemployed or inactive, compared with about a third for the OECD average. This may reflect having low qualifications in general, but also and perhaps more importantly, not having the right skills for the jobs that are available. The latter may contribute to overskilling, i.e. the share over workers reporting that they have higher qualifications than required for their job. Addressing skills imbalances requires i) preventing early school leaving; ii) building stronger linkages between the worlds of work and education; and iii) promoting adult education and training.

Figure 2.7. Spanish youth face a difficult transition from school to work

Labour market status of youth aged 18-24 not in education or training, 2021, percentage



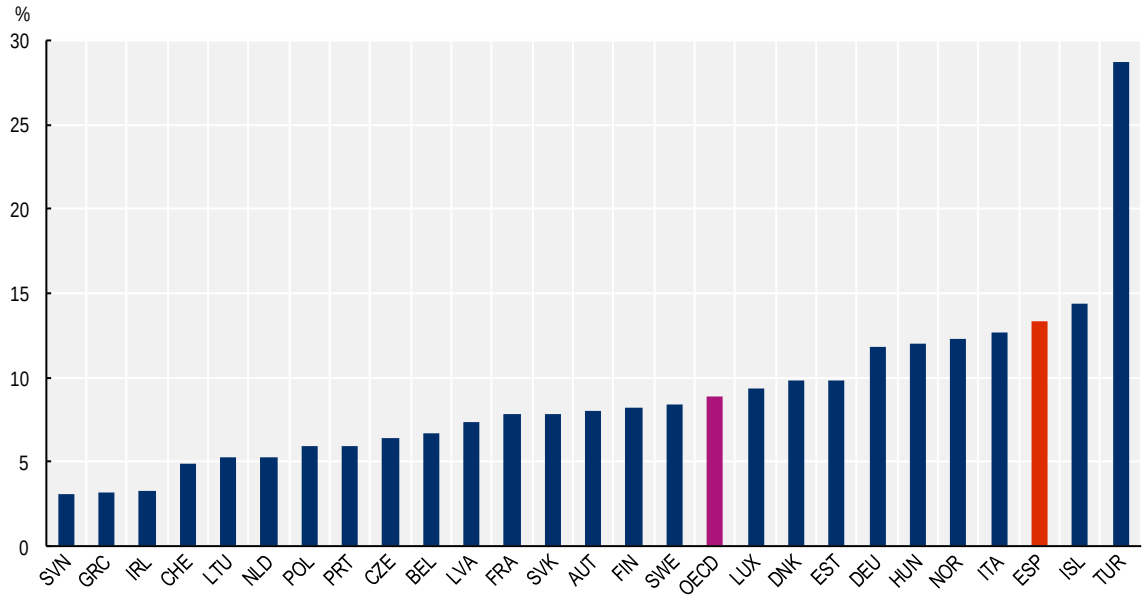
Note: OECD unweighted average.
Source: OECD (2024), "Education at a glance: Transition from school to work", *OECD Education Statistics (database)*, https://doi.org/10.1787/58d44170-en.

Preventing early school leaving

Many early school leavers are not well equipped to take advantage of new technologies. Spain continues to have one of the highest early school leaving rates in the OECD despite significant progress in recent years: in 2021, 13% of the 18-24 year-olds leave school without having gone beyond lower secondary education, almost half the level a decade earlier, but still considerably higher than the OECD average of 9% (Figure 2.8). Early school leaving is particularly an issue for boys and young persons from poor households. Early school leaving significantly reduces the chances of making a smooth transition from school to work. It is associated with a higher risk of unemployment, and fewer job opportunities based on the use of new technologies. In particular, many early school leavers will remain poorly educated later in life (OECD, 2023[3]). Moreover, low skills are more likely to become obsolete as automation progresses, while high skills can make work more productive by complementing new technologies (Autor, Levy and Murnane, 2003[16]; Nedelkoska and Quintini, 2018[17]; Georgieff and Hyee, 2021[18]).

Figure 2.8. Many young Spaniards leave the education system early

Early school leavers, share of 18-24 year-olds, 2021 or latest, percentage



Note: OECD is the unweighted average among the countries analysed.
Source: OECD (2023[3]), *OECD Economic Surveys: Spain 2023*.

Tackling early school leaving starts early in life and continues into older age

Early childhood education and care (ECEC) can influence learning dispositions later in life and is particularly important for children from disadvantaged backgrounds (OECD, 2006[19]). Expanding access to early childhood education has been a government priority since 2021. Participation in early childhood education is now above the OECD average. However, access to early childhood education for poor families remains a challenge (OECD, 2023[3]). Early warning indicators and tailored support for students at risk of dropping out via specific programmes could lower early school leaving further. Spain's Territorial Co-operation Programmes, such as the Educational Guidance, Advancement and Enrichment Programme (PROA+), which provides support to students with educational problems, and the Programme of Accompaniment Units, which provides guidance to students and families from disadvantaged

backgrounds, are welcome. For those who have already left school, adult learning programmes can offer a second chance, provided that they are sufficiently comprehensive and offer recognised training. A recent example of Vocational education and training (VET) reform going in the right direction is the 2020 *Plan for the Modernisation of Vocational Training.* It allows students from upper-secondary vocational education to move on to higher education and provides accreditation for skills acquired outside the formal education system. In 2022/23, about 100.000 students were enrolled in Centres for Adult Teaching geared towards obtaining a degree.

Building stronger linkages between the worlds of work and education

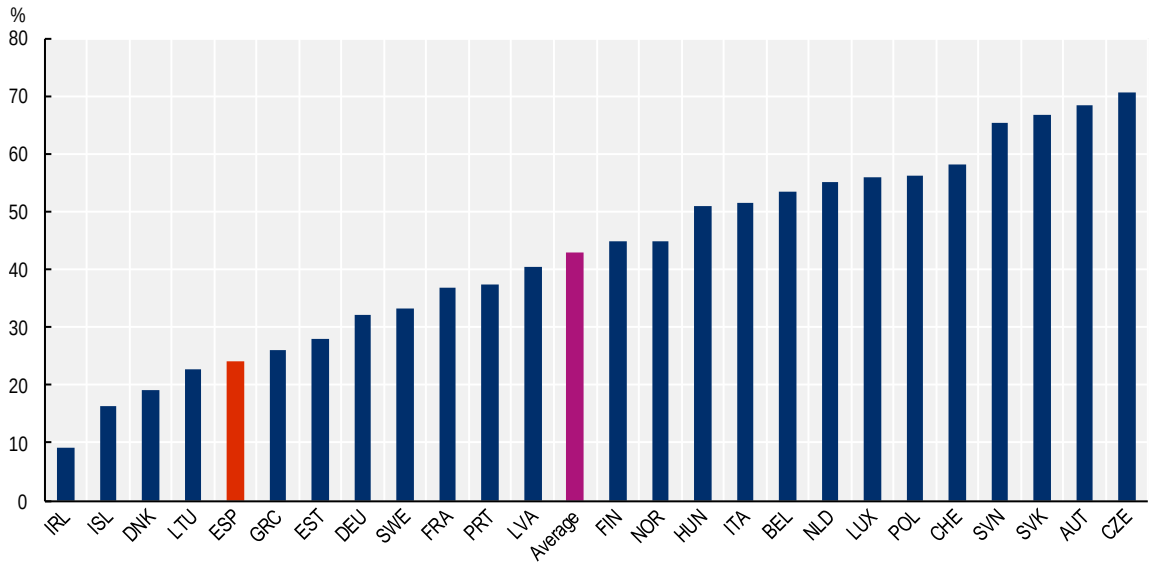
For those who have completed higher education, a significant mismatch between the skills acquired at school and those required by firms may prevent them from making full use of their abilities and hence result in overskilling. Tertiary education in Spain is not well aligned with firms' needs: only a small share of university graduates are enrolled in Science, Technology, Engineering and Math (STEM) courses, and the incidence of over-qualification remains relatively high compared to other OECD countries (OECD, 2023[3]).

VET could be effective in providing specific technical skills that are lacking (Boto-García and Escalonilla, 2022[20]). However, in 2021, only 24% of Spanish students in upper-secondary education were enrolled in VET, compared to an OECD average of 43% (Figure 2.9). The Organic Law on Vocational Education of March 2022 aims at promoting, modernising and making vocational training more appealing. Moreover, it seeks to make all vocational training dual by combing school-based learning with learning in the workplace. The effectiveness of the reform hinges crucially on its implementation and in particular its ability to induce firms to offer more training places and to attract more students into the system. To increase the number of training places, it is essential to involve small firms (OECD, 2023[3]). This can be achieved by ensuring that vocational programmes cater to the needs of small firms and by reducing the financial and administrative costs of participating. This could take the form of direct financial incentives or the pooling of administrative and educational processes across firms. For example, the *Tknika* centre in the Basque Country gives firms, especially SMEs, access to specific services and infrastructure (OECD, 2021[14]). The attractiveness of VET programmes for students hinges mainly on their ability to improve career prospects and working conditions, but also on the conditions of the training contract. The new training contract introduced as part of the 2021 Labour Market Reform guarantees minimum wage levels for VET students.[3] Moreover, the Organic Law on Vocational Education foresees more attention for career guidance in the education and validation processes.

Involving businesses in the design of vocational and university degrees can also help improve the match between the skills acquired in education and labour market needs (OECD, 2023[3]). In line with this objective, the Organic Law on Vocational Education will involve companies in the process of accrediting skills acquired through professional experience. The Basque *University+Business Strategy* provides an example of such an initiative at the regional level. It integrates business training, as well as joint education and knowledge-transfer projects, into university programmes. Regular evaluations of the relevance of study programmes could also help ensure that curricula evolve in line with changing labour market needs. For example, the Catalan quality assurance agency (AQU Catalunya) provides regular information on the relevance of educational programmes for the labour market, taking into account the labour market outcomes of graduates and the views of employers on the skills of recent graduates.

Figure 2.9. VET enrolment is low in Spain

Share of students enrolled in upper secondary vocational education, 15-19 year-olds, 2021, percentage



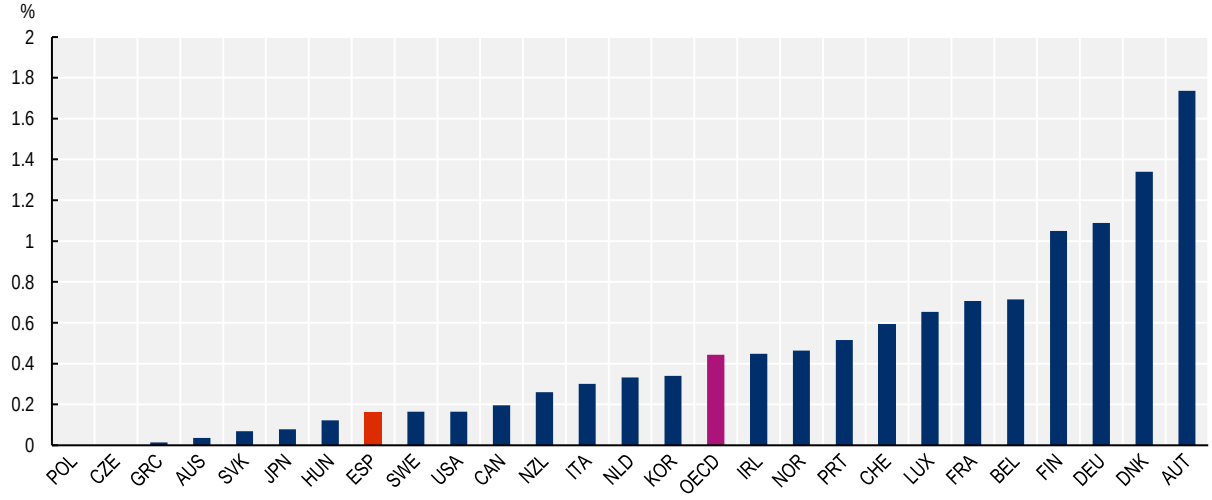
Note: Average is the unweighted average among the countries analysed.
Source: OECD (2023[3]), *OECD Economic Surveys: Spain 2023*.

Promoting adult learning

Later in life, adult learning programmes (e.g. reskilling and upskilling) can equip individuals with the skills in demand on the labour market. However, adult training opportunities for the unemployed are limited in Spain: public expenditures on training per unemployed worker only amount to 0.16% of GDP per capita worker, compared with an average of 0.44% in the OECD countries analysed (Figure 2.10).[4] There is therefore scope for increasing public spending on adult learning in Spain. If carefully designed, individual learnings accounts can help to assign individuals training rights and reinforce individual choice by tying these rights to the individual rather than to the job (see Box 2.2).

Figure 2.10. Training opportunities for the unemployed are limited in Spain

Public expenditures on training, per unemployed, as a share of GDP per capita, 2019



Source: Calculations from OECD data on Labour Market Programmes, National Accounts, OECD Labour Force Statistics.

Box 2.2. Individual learning schemes

There has been a renewed interest by policy makers in individual learning accounts as a way of tying training rights to the individual rather than to the job. While in principle individual learning accounts present attractive features (e.g. empowering individual choice), their effectiveness depends critically on their design. In particular, there is a risk that, if badly designed, they may widen participation gaps between over- and underrepresented groups. The features of a well-designed individual learning account include: simplicity; adequate and predictable funding; greater generosity for those most in need; provision of effective information, advice and guidance; a guarantee of access to quality training; and an explicit accounting of the links with employer-provided training.

Three types of individual learning schemes can provide an individual entitlement to training:

- Individual Learning Accounts are virtual individual accounts in which training rights are accumulated over time. They are virtual in the sense that resources are only mobilised if training is actually undertaken. The only real example of an Individual Learning Account is the French Compte Personnel de Formation (CPF).
- Individual Savings Accounts for Training are real, physical accounts in which individuals accumulate resources over time for the purpose of training. Unused resources remain the property of the individual and, depending on the scheme, may be used for other purposes (e.g. retirement). A few such schemes have been implemented in the past, generally as a pilot scale (e.g. learn$ave in Canada or the Lifelong learning accounts in the United States)
- Training vouchers provide individuals with direct subsidies for training purposes, often with co-financing from the individual. They do not allow for any accumulation of rights or resources over time. This is the form of individual learning scheme most frequently implemented. While many individual learning schemes are called “individual learning accounts”, most of these schemes actually function as vouchers.

Source: OECD (2019[21]), “Individual Learning Accounts: Design is key for success”, Policy Brief on the Future of Work, OECD, Paris, www.oecd.org/employment/individual-learningaccounts.pdf

2.3.2. Firms face structural barriers to productivity gains

Low productivity growth in Spain mainly reflects low growth among low-productivity firms whereas growth among frontier firms has remained robust. This section therefore mainly focuses on policies to support the diffusion of new technologies to lagging firms and the reallocation of resources from less to more productive firms. It also discusses avenues for ensuring that productivity growth among frontier firms remains robust.

Supporting the diffusion of new technologies to lagging firms

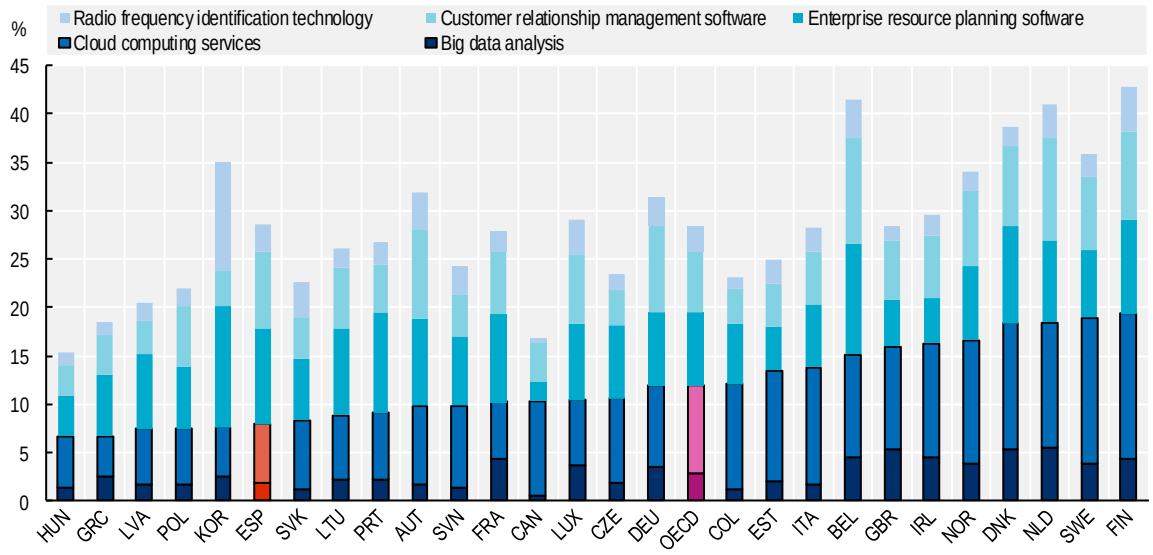
A key challenge for Spain is to promote the diffusion of advanced technologies to lagging firms. Consistent with a slow diffusion of technologies across firms, the adoption rate of advanced digital technologies is among the lowest in the OECD. Adoption rates for Big Data analysis (1.8%) and cloud computing services (6.2%) are one-third lower than the OECD average (Figure 2.11). This suggests that the adoption of such technologies is largely limited to frontier firms. Spain performs relatively well in the adoption of basic digital technologies (IMF, 2023[22]), including enterprise resource planning and customer relationship management software. A key challenge is therefore to promote the adoption rate of advanced digital technologies across firms.

Direct support measures for lagging firms could help with the adoption of advanced technologies by reducing financial frictions and market distortions (Arregui and Shi, 2023[23]; Berlingieri et al., 2020[8]; Pisu et al., 2021[24]). This could, for example, take the form of better access to finance (e.g. via the development of equity markets), targeted support for intangible investment (e.g. training for managers, software and R&D), or increased non-monetary support (e.g. access to data, less stringent regulation). R&D support has a particular role to play in providing lagging firms with the managerial and organisational capital that is needed for the adoption of advanced digital technologies, including efficient management practices (Berlingieri et al., 2020[8]). By engaging in R&D, lagging firms not only innovate, but also accumulate tacit knowledge that enables managers to understand and assimilate advanced technologies. Grants, loans and credit guarantee schemes are particularly suitable for reducing the cost of R&D and improving access to finance in lagging firms.

The development of digital infrastructure is also key to foster the adoption and diffusion of advanced digital technologies in lagging firms (Pisu et al., 2021[24]). Fiscal incentives can encourage private investment in underserved areas. Direct public investment is essential where private investment is not commercially viable. Regulatory restrictions on the deployment of technology could be reduced, as was done by the 2022 *Telecommunications Act*, which relaxes public domain use rights and the requirement for public authorities to provide a local urban planning (OECD, 2023[3]).

Figure 2.11. Spain lags behind in the adoption of advanced digital technologies

Adoption rate of digital technologies among firms, 2020 or latest, percentage



Note: The height of the bar gives the average adoption rate across the five technologies. The five components give the contribution of the adoption of each technology to the overall average. Only enterprises with ten or more employees are considered. OECD is the unweighted average among the countries analysed.
Source: OECD ICT Access and Usage by Businesses Database.

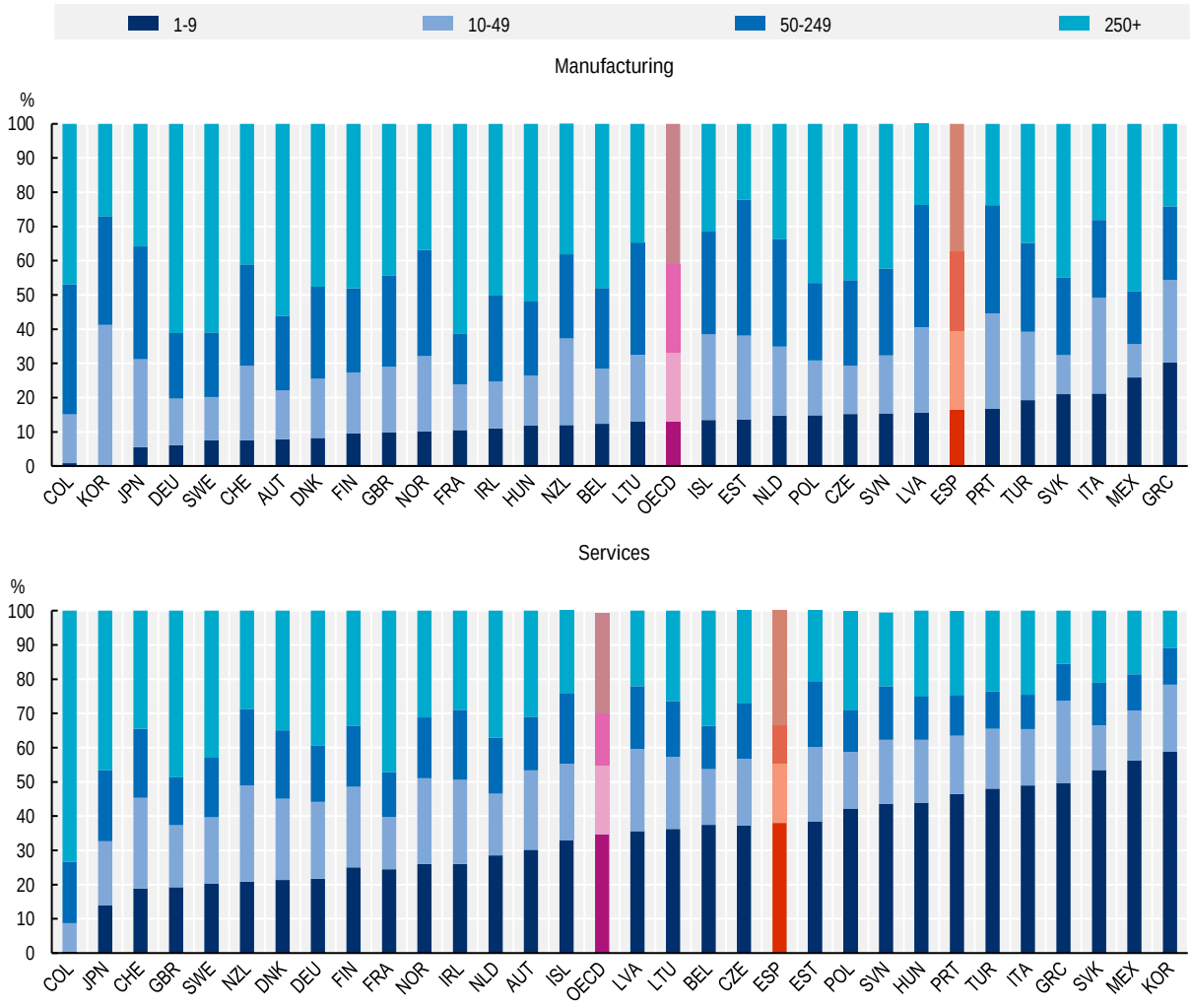
Provide stronger incentives for small firms to grow and flourish

One important factor that is holding back productivity growth among lagging firms and the adoption of advanced digital technologies is the high incidence of small and micro firms in Spain. Firms with less than ten employees account for 16% of employment in manufacturing and 38% in services compared with 13% and 35% on average across the OECD (Figure 2.12). Small firms tend to be less productive (OECD, 2023[25]) and tend to exhibit lower productivity growth than larger firms (Berlingieri et al., 2020[8]). Low productivity growth in small firms is likely to reflect a variety of factors, including access to credit for investment and the capacity to invest in training, adopt new technologies and innovate (Lopez-Garcia and Montero, 2012[26]). There are several factors that could limit the growth of firms, including access to finance, regulatory barriers, and inadequate managerial skills.

Regulatory barriers mainly relate to size-contingent regulations, differences in regulations between regions and direct support measures targeted at small firms. Size-contingent regulations are used in many different areas including taxation, labour, accounting and finance (Arregui, 2023[27]). They weaken incentives for small firms to grow their business and provide an unfair competitive advantage to small firms (González Pandiella, 2014[28]). Differences in regulations across regions constrain firm growth by limiting market size. Harmonising regulations across regions, in line with the *Market Unity Law,* could help to promote business growth, by increasing effective market size, supporting economies of scale, and strengthening competition between firms (Adalet McGowan and San Millán, 2019[29]; OECD, 2023[3]). Finally, direct support measures should be targeted primarily at young firms rather than small firms as this has been shown to increase the effectiveness of public spending (OECD, 2018[30]). Depending on their precise implementation, size-based measures also carry the risk of further weakening incentives for small firms to grow.

Figure 2.12. Employment in Spain is over-represented in small firms

Distribution of employment by firm-size group, 2020 or latest



Note: Services include non-financial market services. OECD is the unweighted average among the countries analysed.
Source: OECD Database on Structural and Demographic Business Statistics (SDBS).

Promote the reallocation of resources from less to more productive firms

Apart from supporting the productivity in less productive firms, there is also a need to allocate resources more efficiently between less productive firms with structural difficulties to more productive firms with healthy growth prospects.

Indeed, there are signs that the process of job reallocation from less to more productive firms has become less effective over time in Spain as well as in many other OECD countries. Across the OECD, there has been a secular decline in firm entry and exit rates and the speed of job reallocation from less to more productive firms over the past couple of decades (Adalet McGowan, Andrews and Millot, 2017[31]; Calvino, Criscuolo and Verlhac, 2020[32]). Moreover, in almost all major OECD countries, and in particular in Spain, employment has shifted from manufacturing to service sectors (e.g. restaurants, health and residential care activities), where productivity tends to be lower (Sorbe, Gal and Millot, 2018[33]; OECD, 2018[4]). This has been a moderate but persistent drag on labour productivity growth.

An issue that is particularly relevant for Spain is the relatively high share of firms that are no longer competitive but remain active (OECD, 2019[34]). Since these firms typically exhibit low levels of productivity, their continued survival prevents resources from flowing to more productive firms, holding back productivity growth (Banerjee and Hofmann, 2018[35]). Indeed, in a well-functioning market, insolvent firms, sometimes called “zombie firms”, exit the market, encouraging business creation and entrepreneurship. One reason why this may not happen sufficiently in Spain may be its insolvency regime. An efficient insolvency regime encourages entrepreneurs to take the risk to start a new business and is positively associated with entrepreneurship and productivity growth. As an important step in this direction, Spain has reformed its insolvency regime in 2022 by facilitating pre-insolvency actions and out-of-court negotiations (OECD, 2023[3]).

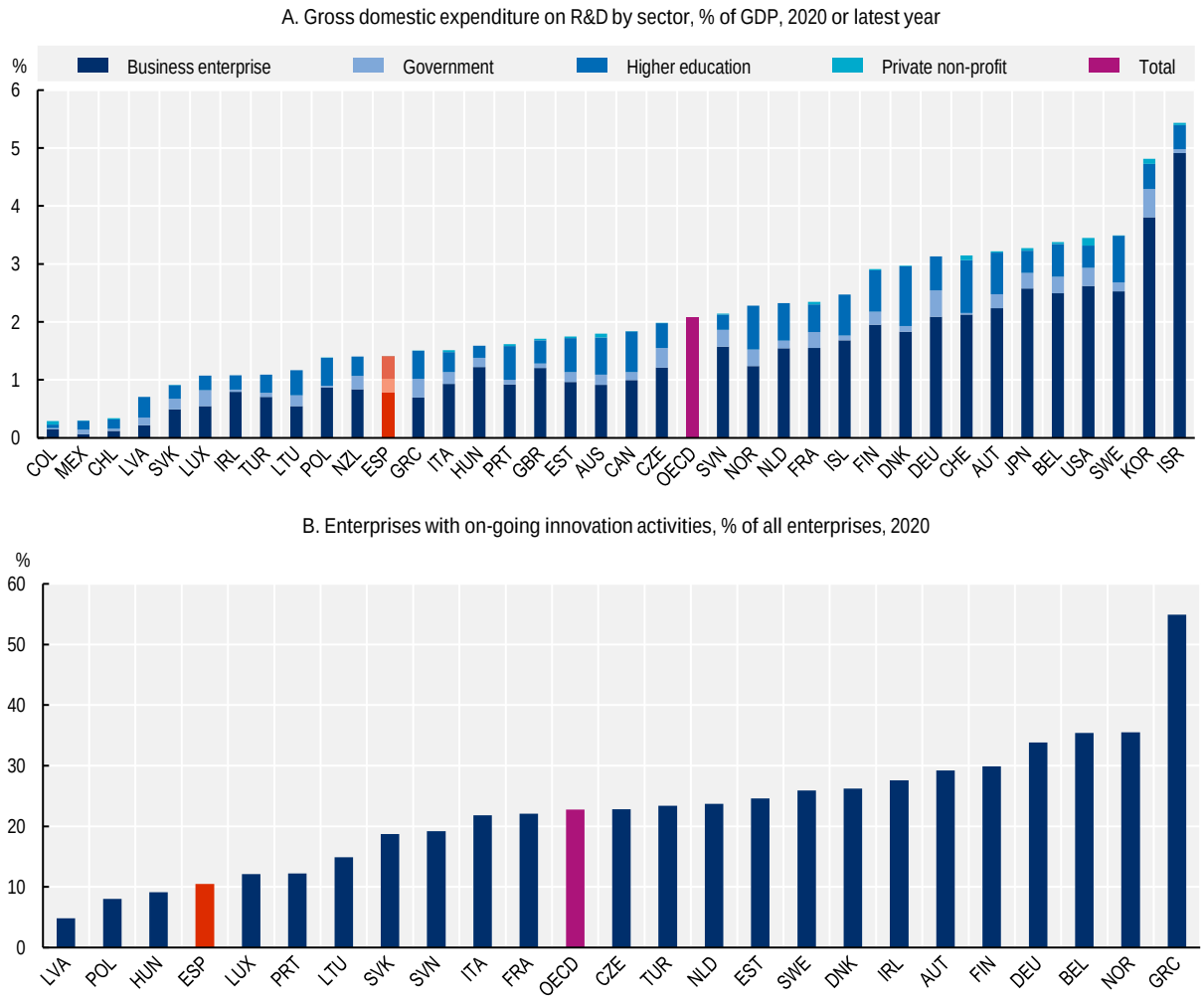
Employment protection regulation, which is relatively strict in Spain (see Chapter 3), may also slow the process of efficient job reallocation and hence productivity growth (OECD, 2020[36]). It can do so by reducing the ease with which firms can adjust employment in response to changing business conditions and by weakening the incentives of workers to move to more productive firms (for example because they would lose accumulated entitlements to severance pay). Yet, employment protection can also support productivity growth by strengthening incentives for the accumulation and preservation of firm-specific human capital in the workplace and by promoting the use of high-performance work and management practices based on long-term employer-employee relationships. In the end, therefore, the key question is whether employment protection strikes the right balance between supporting job reallocation and providing incentives for learning and innovation in the workplace. The role of employment protection for productivity growth, including the 2021 reform, is discussed in detail in Chapter 3.

Support innovation activity in the private sector

While productivity growth among frontier firms has remained robust, there are concerns about their ability to do so in the future since innovation is rather low. Indeed, Spain is among the OECD countries that spend the least on innovation. Only 1.4% of GDP is spent on R&D, two-thirds of the OECD average (Figure 2.13, Panel A). Spanish firms also lag behind in terms of public-private partnerships (OECD, 2021[14]), process innovations and non-R&D innovative spending (Arregui and Shi, 2023[23]). In addition, Spain is among the OECD countries with the lowest share of innovative firms. In 2020, 11% of firms had ongoing innovation activities, half the OECD average (Figure 2.13, Panel B).

Collaboration between private firms and public research institutions in particular can be an effective approach to promote innovation (OECD, 2023[3]). In this spirit, the new public-private partnerships implemented under the Recovery, Transformation and Resilience Plan have been created to bring together various actors, including SMEs in technology clusters. Industry and civil society could play a stronger role in the university governance system, and firms should be encouraged to hire PhDs. To enhance the effectiveness of measures to support innovation their rigorous assessment is crucial. The reformed *Law on Science, Technology and Innovation* goes in the right direction by giving a *Science, Technology and Innovation Advisory Board* the responsibility to promote the introduction of evaluation mechanisms. A strengthened evaluation framework in turn could facilitate performance-based funding. Given the major role played by regions in the design and implementation of innovation policy, improving co-operation between regions, but also with central government, could increase the effectiveness of innovation policies through synergies and knowledge spillovers (Adalet McGowan and San Millán, 2019[29]).

Figure 2.13. Spending on R&D is low and there are few innovative firms in Spain



Note: OECD is the unweighted average among the countries analysed.
Source: OECD (2023[3]), *OECD Economic Surveys: Spain 2023*.

2.3.3. Tackling disparities in productivity between regions

Tackling disparities in productivity requires place-based policies to support disadvantaged regions and policies that can promote geographical mobility from disadvantaged regions to high-performing regions.

Supporting lagging regions

Public investment in public employment services, education and infrastructure is key to support disadvantaged regions and facilitate the diffusion of innovation and good practice between regions. To effectively administer and implement large-scale investment projects, education and employment programmes, a good co-operation between national, regional and local governments is essential. To ensure efforts are focused on the most promising projects, it is important to have well-established and transparent procedures for their selection and the way they are awarded to private contractors (OECD, 2018[1]).

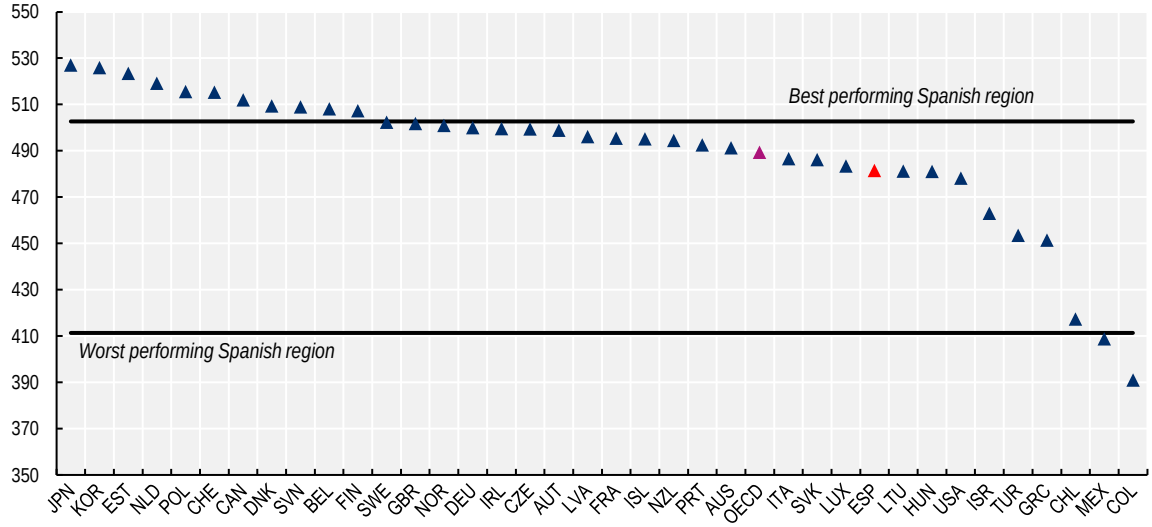
Supporting skills development in disadvantaged regions is particularly important. The supply of skills in some regions may be as low as in some of the lowest-performing OECD countries, as shown in Figure 2.14

focusing on mathematical skills. Redirecting resources for education, training and employment policies towards lagging regions would enhance the career opportunities of workers in these regions and enable firms to find the skills they need in the local workforce and develop new opportunities for investment.

Apart from mobilising more resources, it is also important to increase policy effectiveness. Benchmarking services and evaluating polices at the regional level are crucial in this regard (Adalet McGowan and San Millán, 2019[29]). Greater interregional co-operation could help to enable regions with insufficient resources to carry out high-quality evaluations. This co-operation could take the form of an independent National Evaluation Agency responsible for regularly evaluating regional policies. It could build on the existing sectoral conferences, which aim to co-ordinate policies between regional authorities and central government. Evaluations can be used to identify best practices as well as cases where improvements are needed. Policy guidance and funding could be provided to promote the adoption of best practices in lagging regions, in line with the recent *Programa de Aprendizaje Mutuo* (Adalet McGowan and San Millán, 2019[29]) or the 2023 Employment Law that seeks to modernise active labour market policies, by standardising basic services and promoting impact analysis.

Figure 2.14. Skills supply in some regions is as low as in some of the lowest-performing OECD countries

Mean PISA scores in mathematics, 2018



Note: In 2018, some regions in Spain conducted their high-stakes exams for tenth-grade students earlier in the year than in the past, which resulted in the testing period for these exams coinciding with the end of the PISA testing window. Because of this overlap, a number of students were negatively disposed towards the PISA test and did not try their best to demonstrate their proficiency. Although the data of only a minority of students show clear signs of lack of engagement (see PISA 2018 Results Volume I, Annex A9), the comparability of PISA 2018 data for Spain with those from earlier PISA assessments cannot be fully ensured. OECD is the unweighted average among the countries analysed.
Source: OECD (2019[37]), *PISA 2018 Results (Volume I): What Students Know and Can Do*, https://doi.org/10.1787/5f07c754-en.

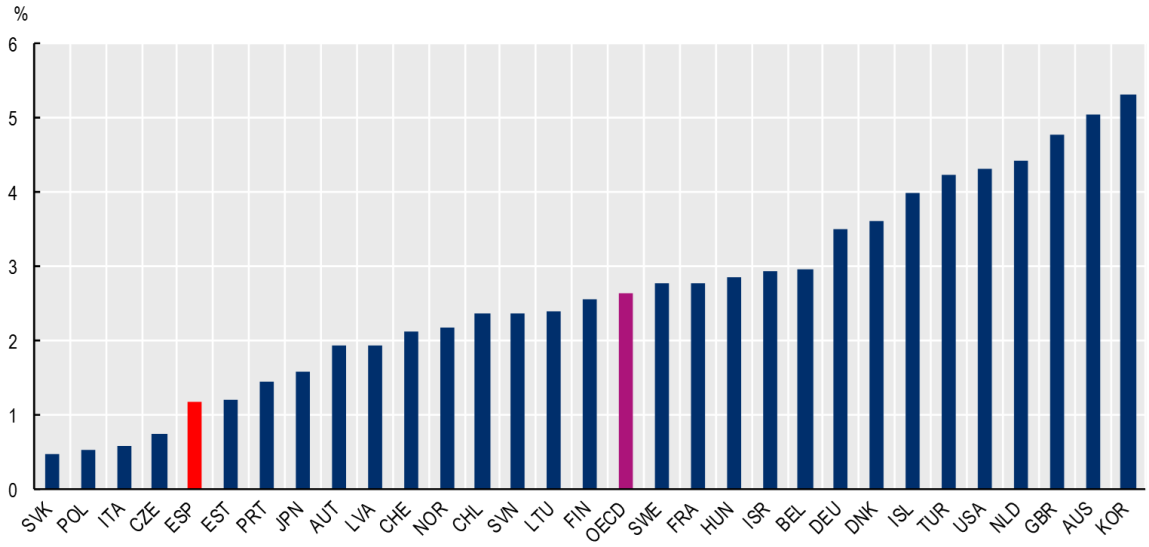
Low job mobility between regions hampers the efficient reallocation of labour

Spain's high degree of decentralisation and large regional disparities can hamper the efficient allocation of labour (Adalet McGowan and San Millán, 2019[29]), as workers and jobseekers may find it difficult to move from one region to another: the annual regional migration rate in Spain was only 1.2% during 2017-21, less than half the OECD average (2.6%) (Figure 2.15).

Policy measures to promote labour mobility are those that limit the potential losses of workers and jobseekers moving from one region to another. First, one can ensure that social assistance and ALMP entitlements are transferable between regions. A recent example is the “social card”, which centralises all non-contributory benefits received, regardless of their source (national, regional or local) (Adalet McGowan and San Millán, 2019[29]). Second, ensuring availability of affordable housing also can help to promote geographical mobility. Housing allowances, rent ceilings or social housing, targeted to those most in need are useful tools. For example, the *2018-21 National Housing Plan* includes a housing allowance for low-income youth and families (Adalet McGowan and San Millán, 2019[29]).

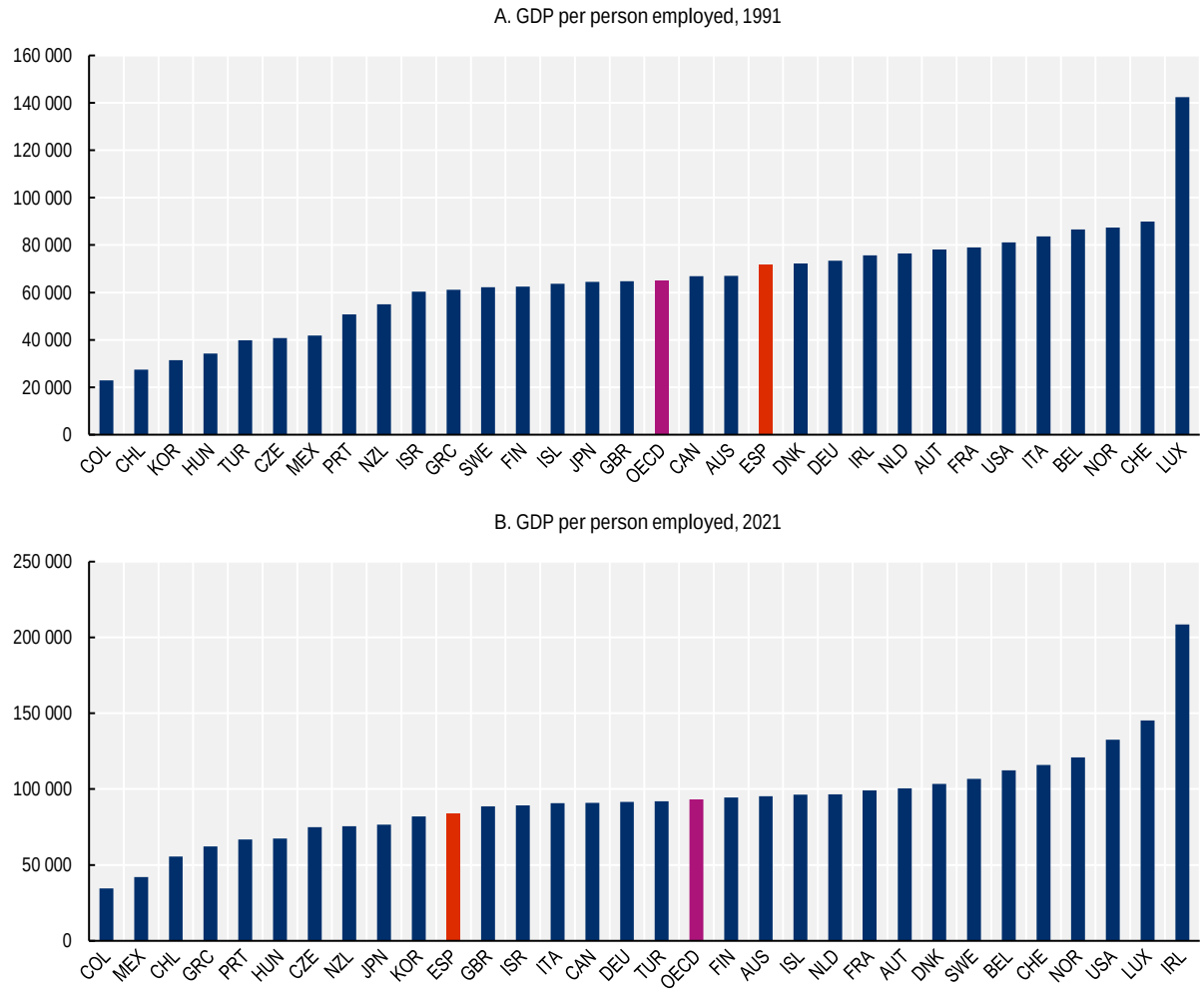
Figure 2.15. Regional mobility is low in Spain

Annual regional migration rate (Flows across TL3 regions, average 2017-21, percentage of total population)



Note: Average 2017-21, otherwise available years: 2017 for Chile, Poland and the United States; 2017-18 for Australia and Italy; 2019-21 for France and Latvia. OECD is the unweighted average among the countries analysed.
Source: OECD Regional Database.

Figure 2.16. **Spain's labour productivity performance has** deteriorated considerably in recent decades



Note: Data are measured in constant prices 2015 USD purchasing power parities. OECD is the unweighted average among the countries analysed.
Source: OECD Productivity Statistics Database.

Main insights

Productivity growth in Spain has been persistently weak for several decades. Productivity growth started slowing in the mid-1990s, earlier than in most other OECD countries, and its slowdown has been particularly pronounced. In recent years, it averaged just 0.5% per year, compared with 1.2% for the OECD as whole. As a result, productivity performance has fallen below the OECD average, with important implications for real wage growth and the standard of living. In fact, real wage growth since the 1990s has been close to zero, as it failed to keep up even with weak productivity growth.

The slowdown in productivity growth in Spain

The slowdown in productivity growth reflects three key challenges. While many OECD countries have been confronted with similar challenges, they have tended to be more pronounced in Spain.

- *Lower multi-factor productivity (MFP) growth*. Low MFP growth is in part due to difficulties with adapting to technological change and globalisation. This reflects barriers to the adoption of more efficient technologies and work practices in firms and a mismatch between the skills of workers and those required by employers.
- *Lower capital deepening*. Lower capital deepening is largely due the persistent decline in investment following the global financial crisis. The decline in investment was particularly sharp in Spain due to the collapse of the housing bubble and the ensuing banking crisis. It has failed to fully recover due to low MFP growth, high economic uncertainty and enduring financial weaknesses.
- *Growing disparities in productivity*. Growing disparities mainly reflect lagging productivity growth in low productivity firms and regions. This reflects the slow diffusion of new technologies from frontier firms to other firms and inefficiencies in the allocation of resources from low to high productivity firms. Productivity growth has remained robust in frontier firms.

The recent acceleration in the importance of digital technologies and the development of generative artificial intelligence (AI) creates important new opportunities for productivity growth. However, if history is a guide, seizing upon them may be a challenge unless the causes of weak productivity growth are effectively addressed.

Reviving productivity growth in Spain

To revive productivity growth, it will be important to address persistent skill imbalances that limit the adoption of new technologies, promote the development of more efficient technologies and their diffusion to less productive firms, reduce regulatory barriers for firms to grow and flourish, and tackle regional disparities in productivity.

- *Investing in education and training*. The education and training system could become more inclusive by continuing efforts to reduce early school leaving and remedying skills gaps through second-chance schools, and more responsive to evolving labour market needs by expanding enrolment in vocational education and training based on a combination of school and work-based learning, reinforcing the culture of life-long learning, and involving employers more strongly in the education and training system.
- *Supporting productivity growth in firms*. This requires promoting the adoption of advanced digital technologies in lagging firms by increasing access to digital infrastructure and access to credit to promote investment in intangible assets, including managerial and organisational capital

(e.g. management practices). It also requires supporting the reallocation of resources from low-productivity firms with structural difficulties to more productive firms with healthy growth prospects.

- *Tackling regional disparities in productivity*. This requires public investments in the quality of education, employment services and infrastructure in lagging regions, including by identifying best practices and providing technical and financial support to local providers, and supporting regional mobility by ensuring social entitlements are portable across regions and promoting the availability of affordable housing in more advanced regions.

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Notes

[1] This is true when measuring labour productivity in terms of total hours worked or the number of persons employed (see Figure 2.16).

[2] The correlation coefficient between productivity levels and productivity growth across regions is positive but relatively weak (0.3).

[3] The minimum wage level is 60% of the wage for the equivalent category of employee in the first year of education and 75% in the second year, subject to the interprofessional minimum wage.

[4] Spain is above average in terms of total expenditure on training as a percentage of GDP. This may suggest that the challenge is mainly one of targeting resources to those who need training the most rather than the overall level of spending.

3 The role of labour market policies in broadly shared productivity growth

Andrea Garnero, Alexandre Georgieff and Alexander Hijzen

This chapter discusses the role of labour market policies in supporting broadly shared productivity gains. Particular emphasis is placed on the recent labour market reforms in relation to wage-setting institutions, employment protection and job retention support. It provides three key insights. Wage-setting institutions in the form of minimum wages and collective bargaining have been significantly strengthened to promote a broader sharing of productivity gains with workers, particularly those with low wages. The use of temporary contracts has been significantly restricted to combat labour market duality. This has resulted in a sharp decline in the number of temporary contracts and an equally sharp increase in the number of permanent contracts in the year following the reform. Job retention support in the form of ERTE has been reformed, defining the parameters of the permanent scheme, while introducing an innovative mechanism for scaling up support in emergency situations (the so-called "RED mechanism").

3.1. Introduction

The objective of this chapter is to discuss the role of labour market policies in reviving productivity growth and ensuring that productivity gains are broadly shared through higher wages and better employment opportunities, particularly for groups with a weak position in the labour market.

The labour market policies considered in this chapter are primarily designed to promote working conditions in terms of wages (minimum wage and collective bargaining), job security (employment protection and job retention schemes) as well as other work arrangements (working time), consistent with the OECD framework for the measurement and assessment of job quality (Cazes, Hijzen and Saint-Martin, 2015[1]). These policies primarily seek to promote a broader sharing of productivity gains by setting legal minima for wages or non-wage working conditions or indirectly by supporting the bargaining position of workers. However, they also can have important implications for productivity as well as employment.

The OECD Jobs Strategy of 2018 argues that good working conditions can contribute to raising productivity within firms by fostering long-term employer-employee relationships, and by doing so, strengthen incentives to invest in skills, technologies and innovation and the adoption of high-performance work and management practices (OECD, 2018[2]). The challenge for policy is to provide the conditions for learning and innovation in the workplace while, at the same time, provide sufficient flexibility to allow for the efficient reallocation of workers between firms that differ in their productivity.

3.2. Wage-setting institutions

Relatively little is known about the productivity effects of wage-setting institutions (e.g. minimum wages, collective bargaining). In the OECD Jobs Study of 1994, wage-setting institutions were regarded with considerable skepticism due to the risk of pricing low-skilled workers out of the market, and hence further increasing unemployment at a time when this was a primary policy concern, and the risk of undermining the efficient allocation of workers across firms by mitigating incentives for job mobility and investing in human capital (OECD, 1994[3]). The contrast with the new OECD Jobs Strategy of 2018 is striking (OECD, 2018[2]). Because of the greater emphasis on job quality, wage-setting institutions are seen as an integral part of the toolkit to promote good jobs for all workers by ensuring that productivity gains are broadly shared. Indeed, the focus is on how the effectiveness of wage-setting institutions can be enhanced and any potentially adverse consequences mitigated. The more positive view on wage-setting institutions also reflects a stronger recognition of the role of firms in wage-setting. Whereas according to the traditional view wages are fully determined by the demand and supply for skills, it is now widely recognised that wages also depend on the firm for which one works, as firms have some power to set wages due to the presence of labour market frictions (OECD, 2021[4]).

The main insight provided in this section is that wage-setting institutions, in the form of both statutory minimum wages and collective bargaining, have been significantly strengthened in Spain in recent years. The minimum wage was increased from a relatively low level in 2018, well below the OECD average, to a level well above the OECD average in 2023. Similarly, the 2021 labour market reform significantly strengthened collective bargaining, notably at the sectoral level. These reforms are likely to contribute to a broader sharing of productivity gains with workers, particularly those with low wages and as such counter the decoupling of wage growth from productivity growth since the global financial crisis (see Chapter 2). It is too early to provide a full assessment of their effects reforms for employment and productivity. An early assessment of the 2019 minimum wage reform suggests that it significantly boosted the wages of directly affected workers, without significantly reducing their employment (Hijzen, Pessoa and Montenegro, 2023[5]). The section concludes with a number of considerations that may help to further improve the role of wage-setting institutions in promoting broadly shared productivity gains in Spain.

3.2.1. Minimum wages

The minimum wage has increased rapidly in recent years

The statutory minimum wage was introduced in Spain in 1964. Initially, the minimum wage was differentiated across regions and sub-minima existed for teenagers below 18. Since 1998, there has been a unique national minimum wage for all workers, irrespective of their age or region where they work. The minimum wage is set each year by the Spanish Government by Royal Decree. Decisions are made on a discretionary basis in consultation with the social partners, taking account of past and predicted inflation as well as general economic conditions. Since 2021, an advisory commission provides independent recommendations on the desired future evolution of the minimum wage.

The minimum wage has gained significantly in importance as a policy tool in recent years in Spain (Figure 3.1, Panel A), in line with a more general global trend.[1] Until 2018, it played only a modest role as it was set at a relatively low level by OECD standards, around 45% of the median wage in the private sector. However, it has increased rapidly since to 58% of the median wage in 2022, with most of the increase taking place in 2019 when it was increased by 22% in a single step. In 2020, an advisory commission (*Comisión asesora para el análisis del salario mínimo,* CASSMI) was created by the government. It consists of experts from academia, social partners and the Ministry of Labour and Social Economy, the Ministry of Finance and the Ministry of Economic Affairs and Digital Transformation. Its first main task was to define a path towards reaching a MW at 60% of the average *net* wage by 2023, which corresponds to about 62% of the gross median wage.

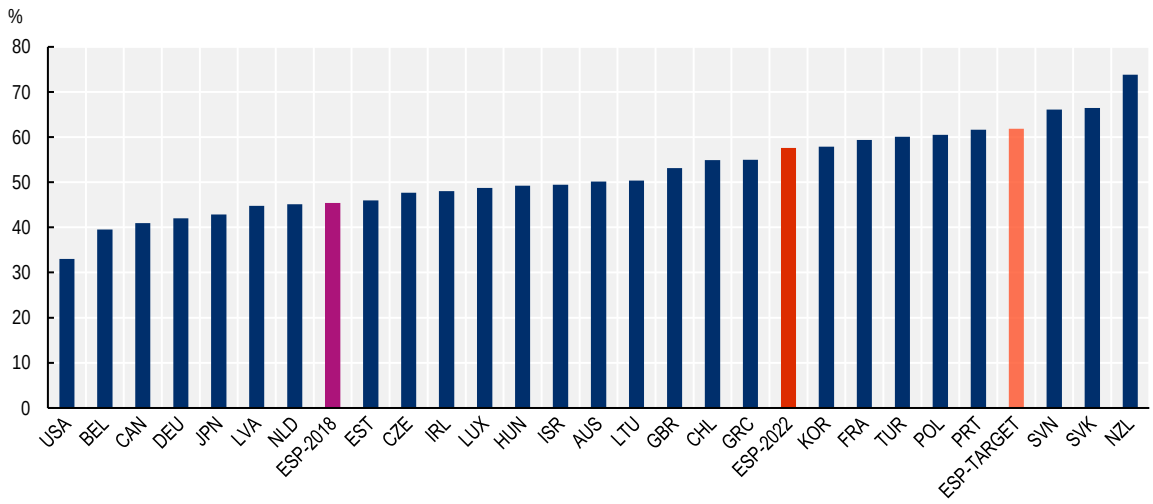
With the sharp rise in prices in most OECD countries, minimum wages have become an even more important tool to protect the standard of living of low-paid workers. The recent increases in 2022 and 2023 in Spain have allowed the minimum wage to keep up with inflation (OECD, 2023[6]). While such upratings of the minimum wage have been crucial to protect the standard of living of low-wage workers, they have also raised concerns in some OECD countries, notably those where inflation remains high.

In an inflationary context, one concern is that minimum-wage increases could contribute to a wage-price spiral. Most empirical studies agree that part of minimum-wage increases is passed onto consumers – see e.g. Harasztosi and Lindner (2019[7]). However, the extent to which this is the case depends on the bite of the minimum wage as well as on the way it is set.[2] ECB (2022[8]) and OECD (2023[6]) show that in most countries the effects of minimum-wage increases on aggregate wage growth are quite limited. This is even the case for major increases due to the limited number of workers directly affected by them. While there is no direct evidence for Spain, given the bite of the minimum wage and the current level of inflation, the risk of a wage-price spiral driven by increases in the minimum wage appears very limited. Moreover, in Spain like in other OECD countries, profits have increased more than labour costs, which suggests that there is room for profits to absorb some further increases in wages to mitigate the loss of purchasing power, at least for the low paid, without generating significant additional price pressures.

Another potential concern relates to the consequences of wage compression for employment and productivity growth. Increases in the minimum wage without similarly sized increases in wages higher up in the distribution induce wage compression. In principle, a squeezing of the wage distribution could reduce employment among low-wage workers, while weakening incentives to move to better firms, slowing efficiency-enhancing job reallocation. It could also reduce incentives of higher-wage workers to provide effort. That said, there is limited empirical evidence on the importance of these mechanisms and the effects of wage compression on employment and productivity more generally. This is an important area for future research.

Figure 3.1. The minimum wage in Spain is being revalued

Minimum wage as a share of median wage, 2022 unless indicated otherwise



Notes: The figure represents the minimum gross wage in 1 January 2022 as a share of the 2022 gross median wage in the private sector (unless stated otherwise). ESP-2018 refers to the 2018 minimum gross wage as a share of the gross median wage for 2018. ESP-target refers to the target minimum gross wage equivalent to 60% of the average net wage as a share of the median gross wage in 2022.
Source: OECD Tax-Benefit model.

The economic and labour market effects of the minimum wage

An intensive debate on the labour market effects of minimum wages

Despite the growing interest in minimum wages as a policy instrument to promote fair wages and broadly shared productivity gains, some controversies remain about their alleged employment effects. A traditionally influential view based on the competitive-market paradigm holds that minimum wages reduce employment by pricing low-skilled workers out of the market. This view was however challenged in the ground-breaking study by Card and Krueger (1994[9]) that showed that minimum wages may have positive rather than negative employment effects. This is consistent with the presence of labour market frictions that confer wage-setting power to employers. Subsequent studies have sought to improve on data and research designs, while shedding light on the underlying mechanisms. While the majority of studies does not show large negative employment effects, the issue continues to be debated (see, among others, Manning (2021[10]), Dube (2019[11]) and Neumark et al. (2021[12]) for recent surveys).

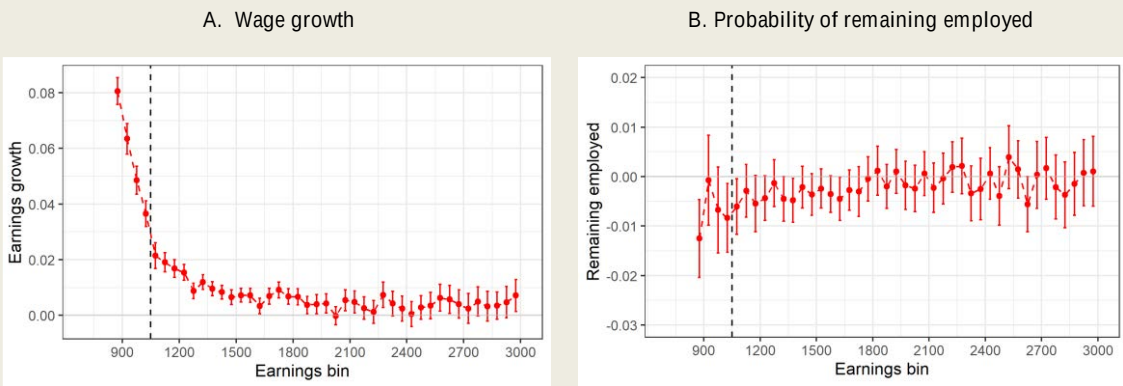
A number of recent studies have analysed the 2019 minimum wage hike in Spain. There is a broad consensus that the increase in the minimum wage significantly increased the wages of low-wage workers, reduced wage inequality and alleviated in-work poverty (Arranz and García, 2022[13]; Cárdenas et al., 2022[14]; Granell, Fuenmayor and Savall, 2022[15]). At the same time, there is little indication that the increase in minimum wages has significantly reduced employment among low-wage workers. While a number of ex ante studies, including one by the Bank of Spain (2017[16]), raised significant concerns about job losses, these concerns have not materialised to the expected extent. Ex post studies by Gorjon et al. (2022[17]) and Hijzen at al (2023[5]) point to small negative employment effects (see Box 1.1), while larger negative estimates are reported in Barcelo et al. (2021[18]). All in all, the emerging evidence for the 2019 minimum wage hike suggests that the minimum wage increase of 2019 boosted the wages of low-wage workers and reduced wage inequality, without significantly undermining job opportunities for low-wage workers.

Box 3.1. An assessment of the 2019 minimum wage hike in Spain

In recent OECD work, Hijzen et al (2023[5]) provide an assessment of the 2019 minimum-wage hike in Spain. This increased the minimum wage by 22% in a single step and directly affected about 7-8% of dependent employees. The assessment is based on an individual-level analysis that follows the outcomes of workers that were employed in the year before the reform over time. Among directly affected workers, the hike in the minimum wage increased full-time equivalent monthly earnings by on average 5.8% and reduced employment by 0.6% (about 7 000 jobs), which implies a small own-wage labour-demand elasticity of -0.1. Further analysis suggests that estimated job losses tended to be concentrated among workers on fixed-term contracts. In sum, the hike in the minimum wage significantly increased the wages of low-wage workers, but only resulted in a very limited reduction in the probability of remaining employed.

Figure 3.2. The wage and employment effects of the minimum wage hike in Spain

Change in outcome between 2018 and 2019 relative to that between 2017 and 2018



Notes: Estimated coefficients plus 95% confidence intervals based on clustered standard errors by province, industry and wage bin.
Source: (Hijzen, Pessoa and Montenegro, 2023[5]), "Minimum wages in a dual labour market: Evidence from the 2019 minimum-wage hike in Spain", *OECD Social, Employment and Migration Working Papers*, No. 298, https://doi.org/10.1787/7ff44848-en.

Productivity effects at the firm and aggregate level

The minimum wages may affect aggregate productivity directly through their effect on the productivity of firms (upgrading) and indirectly through changes in the structure of employment across firms that differ in their productivity (efficiency-enhancing job reallocation).[3]

Productivity effects within firms due to the minimum wage may arise for different reasons, and if they arise, are most likely to be positive. A higher wage may induce workers to exert more effort as implied by efficiency-wage theory (Akerlof, 1982[19]; Georgiadis, 2013[20]). Higher labour costs may also induce firms to invest in capital or to adopt more efficient working practices, based on for example long-term contracting and investment in firm-specific training, to boost the productivity of workers. There is some empirical evidence that the introduction of the minimum wage in the United Kingdom increased firm productivity through the adoption of more efficient work practices (Riley and Rosazza Bondibene, 2017[21]). From a policy perspective, the key challenge is to support firms employing minimum-wage workers with raising their productivity. As discussed in Chapter 2, this includes, amongst others, policies that support

investment in human capital and other intangible assets, promote framework conditions for the digital age and improve access to digital infrastructures (OECD, 2021[22]).[4]

Aggregate productivity effects may also reflect the impact of the minimum wage on job reallocation between less and more productivity firms. Such reallocation effects will be positive and more pronounced when i) firms that make intensive use of minimum-wage workers are less productive, ii) firms that make intensive use of minimum-wage workers are more negatively affected by a minimum wage increase in terms of profitability (Draca, Machin and Van Reenen, 2011[23]; Bell and Machin, 2018[24]), employment and firm survival (Luca et al., 2019[25]); and iii) more productive firms respond by creating more jobs (Drucker, Mazirov and Neumark, 2019[26]; Dustmann et al., 2021[27]). Such "firm-driven" reallocation may, however, be mitigated by slower "worker-driven reallocation" as the minimum wage compresses wage differences between firms, weakening incentives for voluntary job mobility from less to more productive firms (OECD, 2018[2]).

The cost and benefits of changes in job reallocation driven by an increase in the minimum wage are likely to depend on the ease with which displaced workers can find new jobs. Finding a new job following displacement is likely to be easier in market-reliant countries that emphasise flexible product and labour markets as well as in countries with a strong emphasis on public policies to support job transitions. Among a sample of European countries, Bertheau et al. (2022[28]) point in particular to the importance of comprehensive activation policies in limiting the earnings losses of job displacement due to time spent out of work. To promote worker-driven job mobility between firms, activation services should also be made available to workers who are stuck in low-quality jobs and would like to make a career change.

The design of the minimum wage

The effectiveness of the minimum wage in boosting the incomes of workers and their families and its consequences for employment and productivity depend importantly on the way it is designed.

Continue to support the work of the minimum wage commission

The process for adjusting minimum wage rates varies across OECD countries. In most OECD countries, the minimum wage tends to be adjusted annually with a short delay between the decision and the application. In other countries, the minimum wage is adjusted annually or biannually but with a slightly longer delay which may make a difference in times of high and/or rising inflation. In some countries, there is no regular adjustment, which may result in long delays and major losses in purchasing power. In the United States, for instance, the federal minimum wage has not been increased since 2009 (while minimum wages at state and local level have been updated much more regularly). In years of high inflation, multiple increases in minimum wages can take place during the year in comes countries (e.g. Belgium, France and Luxembourg).

The revision of minimum wages may be subject to government discretion or can take place automatically in the case of indexation. In some OECD countries – notably, Belgium, Canada (since April 2022), Costa Rica, France, Israel, Luxembourg, the Netherlands and Poland – there is a form of automatic indexation of the minimum wage to the nation-wide level of wages or prices. Minimum wages are for instance indexed to negotiated wages (i.e. wages defined in collective agreements) in the Netherlands, and to actual wages in Israel. Indexation to (past) prices occurs in countries such as Belgium, Canada, France[5] and Luxembourg.[6] Poland links its minimum wage to future price developments and corrects it *ex post* in case of differences between the forecasts and the realised rates. A few countries have a form of indexation that kicks in only if social partners fail to find an agreement (Colombia and the Slovak Republic).

In several OECD countries, minimum wage commissions provide advice (more or less binding) in setting the level the minimum wage (including Australia, France, Germany, Greece, Korea, Ireland, Mexico, the United Kingdom). The operation of these bodies varies from country to country in terms of the advisory

(e.g. France) or legally binding (e.g. Australia) nature of their recommendations, the extent to which the view of the social partners are taken into account and their independence. In France, for instance, the commission has only an advisory role on the discretionary increase that the government can add to the automatic increase due to price and productivity increases. In Ireland and the United Kingdom, the commissions are composed of experts and representatives of the social partners and the governments can deviate from the recommendations but have to justify the deviation in parliament. In Germany, the government can refuse the recommendation of the minimum wage commission, which is composed by social partners and two experts without voting rights but cannot change it. In Australia, the Fair Work Commission is entirely independent, and its decisions are legally binding.

The experience of minimum wage commissions in OECD countries shows that they are particularly well placed to give objective recommendations, based on a wide range of economic and social factors. The work of the Spanish CASSMI should continue to be supported. Its contribution to produce and commission independent research on a range of issues related to the minimum wage has enriched the public debate and provided a useful evidence base for the government. Social partners, including the employers' organisations, which decided not to take part to the latest deliberations, should continue to be closely involved in the process and the government should commit to respect the advice of the commissions, or in the alternative, explain in a public statement why it disagrees. The resources available to CASSMI should be strengthened to monitor and evaluate the effects of the minimum wage on the labour market. This also requires mobilising administrative data that allow tracking the wages of individual workers in a timely manner (the social security data provide the ideal source for this in the case of Spain).

Table 3.1. Uprating procedures of the minimum wage (timing and frequency of adjustments)

	Delay between the decision and application lower or equal to two months	Delay between the decision and application higher than two months
Regular adjustment on a fixed date	Australia Canada (Federal) Colombia Costa Rica France Hungary Japan Luxembourg Mexico Poland Portugal Slovenia Switzerland (5 Cantons) Türkiye	Estonia Germany Ireland Korea Lithuania Netherlands New Zealand Slovak Republic Spain United Kingdom
No regular adjustment	Belgium Chile Czech Republic (Czechia) Greece United States (Federal)	Latvia

Note: Switzerland (5 Cantons) refers to the five cantons with a statutory minimum wage: Canton of Basel-Stadt, Canton of Geneva, Canton of Jura, Canton of Neuchâtel, and Canton of Ticino.
Source: OECD (2023[6]), *OECD Employment Outlook 2023: Artificial Intelligence and the Labour Market*, https://doi.org/10.1787/08785bba-en.

Table 3.2. Automatic minimum wage indexation in OECD countries, 2022

Country	Indexation mechanism
Belgium	The minimum wage is indexed to the so-called "health index", i.e. past CPI excluding alcohol and tobacco and petrol but including heating fuel, gas, and electricity (every time the index increases by 2% or more since last increase)
Canada	The minimum wage at the federal level is indexed to the Consumer Price Index for the previous calendar year. Also, nine provinces and territories have a form of indexation.
Costa Rica	The minimum wage is indexed on the living cost; and the Gross Domestic Product (GDP) growth.
France	The minimum wage is indexed to past CPI for the bottom quintile and revised annually or as soon as the CPI increases by 2% or more since last minimum wage increase). Annual revisions also incorporate half real salary increase of blue-collar workers (only if positive).
Israel	The minimum wage is anchored to 47.5% of the average wage.
Luxembourg	All wages are indexed to past CPI (every time CPI increases by 2.5% or more since the last semester)
Netherlands	The minimum wage is indexed to the predicted wage developments for the next six months using a basket of collectively agreed wages.
Poland	The minimum wage is indexed to future inflation + 2/3 of future GDP growth if, in the first quarter of the year, the amount of the minimum wage is lower than half of the average wage. If the inflation forecasts differ from the realised evolution of the price index, a correction takes place in the following year.
Switzerland	In the canton of Neuchâtel, the cantonal minimum wage is automatically adjusted each year to the consumer price index. In the canton of Basel-Stadt, the minimum wage is adjusted (only upwards) according to a mixed index (average of nominal wage and consumer price index). In the canton of Geneva, the minimum wage is indexed to the consumer price index (only upwards). In the canton of Ticino, the government adjusts the lower and upper limits of the cantonal minimum wage annually according to the development of the national price index.
United States	The federal minimum wage is not indexed. Currently, 13 states and the District of Columbia index state minimum wages to a measure of inflation. In addition, another 6 states are scheduled in a future year to index state minimum wage rates to a measure of inflation.

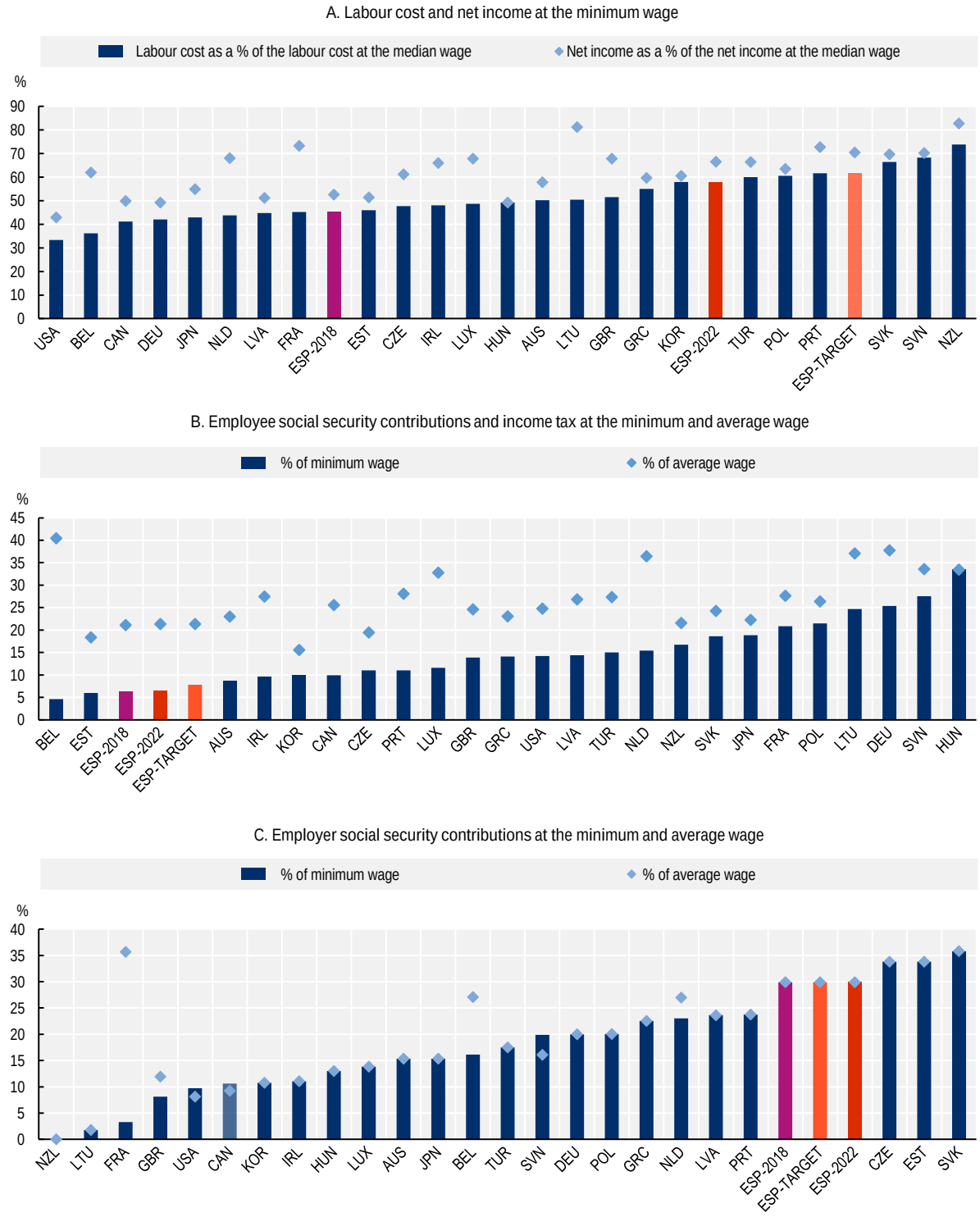
Note: In Belgium, it is important to note that all wages are indexed but rules may vary across sectors depending on the collective agreement. Moreover, wage increases in general are capped by a "wage norm" (a ceiling which takes into account weighted wage developments in France, Germany and the Netherlands). In addition, in Colombia, the minimum wage is indexed to prices if social partners fail to find an agreement. In the Slovak Republic, the minimum wage is set at 57% of the average wage of two years before if social partners fail to find an agreement.
Source: OECD (2023[6]), *OECD Employment Outlook 2023: Artificial Intelligence and the Labour Market*, https://doi.org/10.1787/08785bba-en.

Explore ways to further enhance the role of the minimum wage by leveraging its co-ordination with the tax-and-benefits system

Co-ordination with the tax-benefits system can help to increase the effectiveness of the minimum wage to make work pay, while mitigating its effects on labour costs and competitiveness. In principle, this can take the form of targeted reductions in employer social security contributions for low-wage workers (e.g. France) or make-work pay measures targeted at low-wage workers (e.g. France, Ireland, the United Kingdom), including targeted reductions in income taxes or employee social security contributions or the use of tax credits and in-work benefits. France is an example of country with a relatively high gross minimum wage by OECD standards and relatively important tax-benefit measures targeted at low-wage workers. It uses targeted reductions in employer social security contributions to contain the impact of the minimum wage on labour costs and competitiveness and in-work benefits to enhance the effectiveness of the minimum wage in terms of take-home-pay.[7] As a result, there is a large difference in the labour costs of minimum wage workers for employers and the take-home pay for minimum wage workers relative to the median (Figure 3.3, Panel A).

Figure 3.3. The role of personal incomes taxes and social security contributions for the labour costs and take-home pay of minimum-wage workers

2022 unless stated otherwise



Source: OECD Tax-Benefits model.

At present, there is little co-ordination between the minimum wage and the tax-benefits system in Spain, likely reflecting the fact that, until recently, the need for co-ordination was limited given the low minimum wage. In Spain, there is currently a small difference between the labour costs for employers and the take-home pay for workers at the minimum wage relative to the median. As in most OECD countries, minimum wage workers in Spain are exempt from personal income taxes, resulting in somewhat smaller tax wedge for minimum wage workers than those at the median. However, employer and employee social security contribution rates are the same for low and median-wage workers. Moreover, no specific benefits complement take-home pay for minimum wage workers. With the recent revaluation of the minimum wage, the case for co-ordination may have become stronger and the different ways in which this could be done deserve to be explored and analysed.

In principle, one option could be to introduce targeted reductions in employer social security contributions, to promote job opportunities for low-skilled workers. While in Spain, employer social security contributions at the minimum wage are among the highest in the OECD, its employment-incentive model already provides an important set of temporary exemptions from employer social security contributions for the hiring of low wage workers, not taken into account by the OECD Tax-Benefits model (Panel C). The pros and cons of permanent exemptions for low-wage workers as in France relative to temporary exemptions for the recruitment of low-wage workers as in Spain are not obvious. While permanent incentives in principle may be more effective in creating job opportunities for low-wage workers, they also come at a significantly higher fiscal cost and carry a larger risk of distorting employment towards low-wage and low-productivity firms, with potentially adverse effects for aggregate productivity growth.

Another option would be to explore how the effectiveness of the minimum wage in reducing in-work poverty could be enhanced further. While employee social security contributions and personal income taxes at the minimum wage are already quite low (Panel B), it may be possible to complement the minimum wage with an in-work benefit for workers in low-income households. In-work benefits represent a more direct tool for addressing in-work poverty than the minimum wage (OECD, 2009[29]), but one that does not carry the risk of pricing low-workers out of the market and supports efficiency-enhancing job reallocation by preserving incentives for job mobility across firms. The recent revaluation of the minimum wage, moreover, may further increase the effectiveness of in-work benefits as a policy tool by reducing the risk that employers use their bargaining position to appropriate in-work benefits intended for workers by lowering their wages. Indeed, this is why the OECD advocates the use of in-work benefits in combination with a moderate minimum wage (OECD, 2018[2]).

Box 3.2. The system of in-work benefits (***Prime d'activité***) in France

In-work benefit (IWB) schemes are designed to create a significant gap between the incomes of people in work as compared with the income that they would get if they were out of work, thereby making work pay, while supporting the incomes of the most vulnerable in or out of work. They pursue, therefore, the twin goal of, on the one hand, enhancing employment and the movement of workers up the earnings ladder and, on the other hand, ensuring a greater inclusiveness of the labour market. In order to avoid creating new disincentives higher up the earnings ladder, IWB must avoid threshold effects by maintaining a sufficiently large phase-out region over which benefits are withdrawn gradually.

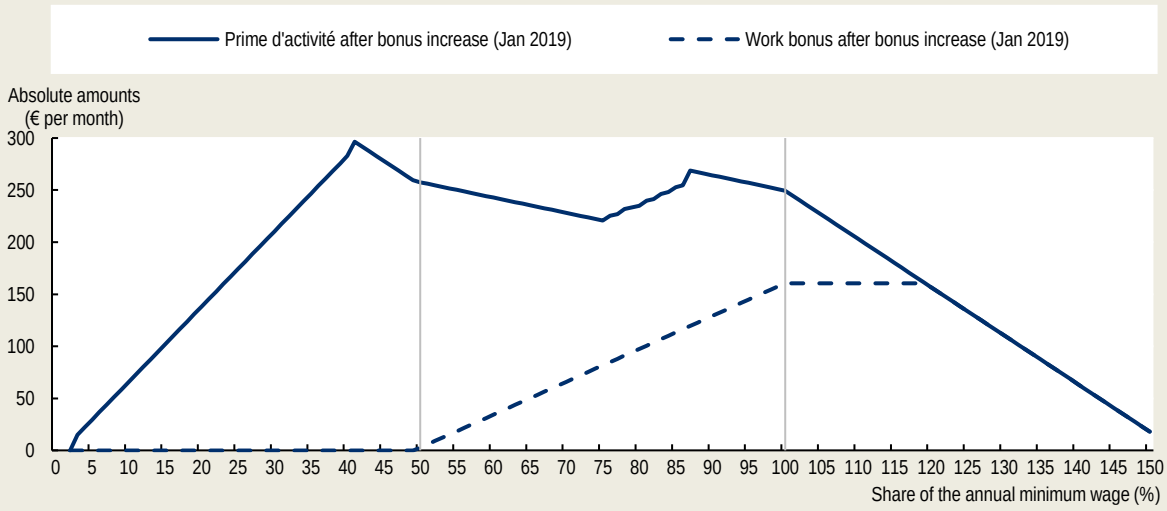
The effectiveness of IWB depends on their targeting, the duration for which they are provided and the way they are operated. First, the effects of in-work benefits on work incentives are more pronounced when targeted at groups that are more sensitive to financial incentives such as lone parents (Immervoll and Scarpetta, 2012[30]). Moreover, in-work benefits are more effective when they are provided permanently, i.e. as long as needed, rather than for a limited maximum duration. The evidence suggests that temporary in-work benefits have limited effects on poverty in the longer-term (Van der Linden, 2016[31]). Finally, IWB systems tend to be more effective when they are operated in a simple

and transparent way. If potential beneficiaries do not understand the IWB system, the desired labour-supply response tends to be smaller (Chetty, Friedman and Saez, 2013[32]). This is more likely when the interaction with other taxes and benefits is complex.

As an illustrative example, Figure 3.4 documents the level of in-work benefits along the wage distribution (expressed as a share of the minimum wage) for the Prime d'Activité in France. As in most other countries, the Prime d'Activité is characterised by a phase-in region, a plateau and a phase-out region. The benefit consists of two components: a lump-sum amount that varies by family composition and a work bonus based on individual earnings that phases in at 0.5 times the full-time minimum wage level, from which household income is deducted.

Figure 3.4. The ***Prime d'activité*** in France

Monthly benefit in euros, 2019



Note: Simulations refer to single household without children after taking account of other taxes and benefits.
Source: Carcillo et al. (2019[33]), "Assessing recent reforms and policy directions in France: Implementing the OECD Jobs Strategy", https://doi.org/10.1787/657a0b54-en.

3.2.2. Collective bargaining and social dialogue

Evidence on the link between collective bargaining and social dialogue on the one hand and productivity is relatively scarce. In principle, their impact on productivity may go in different ways (Freeman and Medoff, 1984[34]). By strengthening the bargaining power of workers, collective bargaining tends to increase wages at the expense of profits, and when conducted at the sector-level, also induces a more compressed wage structure across firms ("monopoly" channel). This has sometimes raised concerns about its potentially adverse effects on investment and resource allocation. These concerns may be more pronounced when collective bargaining is centralised and wage co-ordination is weak. But by providing a voice for workers and better outcomes, social dialogue and collective bargaining can also help overcome common challenges (e.g. adoption of new technologies or the prevention of work-related health problems), while strengthening the commitment of workers to their firms, which may raise productivity ("voice" channel). This is more likely when social partners are well-organised and benefit from broad memberships (OECD (2018[35]). This allows social dialogue and collective bargaining to be widespread at the firm-level and social partners to be representative also at higher levels (e.g. sector, country).

The discussion below focuses on two aspects of collective bargaining that have received considerable attention in the discussion on productivity: i) the degree decentralisation of collective bargaining systems, which refers the scope for negotiations at the firm-level, for reallocation and innovation; ii) the degree of wage co-ordination across collective wage agreements for macroeconomic performance and international competitiveness. It also discusses how collective bargaining can help to enhance a fair sharing of the burden of inflation between firms and workers.

The degree of decentralisation of collective bargaining

Decentralised collective bargaining has often been linked with better productivity performance (OECD, 2019[36]). Decentralised systems can take two different forms. Collective bargaining may take place predominantly at the firm-level, as in "fully or largely decentralised systems" (e.g. Central and Eastern Europea countries as well as OECD countries outside Europe). While this typically provides more flexibility to firms and may support productivity, it tends to be associated with low and declining collective bargaining coverage. Alternatively, decentralisation can take place within sector-level bargaining by allowing substantial scope for further negotiation at the firm-level (upwards and downwards), as in "organised decentralised systems" (e.g. Nordic countries, Germany and the Netherlands). This also provides some flexibility to firms but does not result in lower collective bargaining coverage. In centralised systems, sector-level agreements do not leave (significant) scope for deviations downward at the firm-level (the terms of conditions can only be more favourable). While following the global financial crisis, Spain introduced more decentralisation in its system of sector-level bargaining, this has been partially reversed by the latest labour market reform of 2021 (see Box 3.3).

Box 3.3. Recent developments in collective bargaining in Spain

Until 2012, collective bargaining in Spain was largely centralised. Collective bargaining took predominantly place at the sector-level through either nation-wide or regional agreements. Firm-level agreements were rare and could only be used to top up sector-level agreements (favourability principle).

In 2012, a controversial labour market reform was undertaken, without the support of the social partners, to embark on a process of organised decentralisation of collective bargaining by allowing firm-level agreements to deviate downwards from higher-order agreements and introducing opt out clauses. Moreover, the validity of collective bargaining agreements beyond their formal end date in the absence of a new agreement was reduced to one year (ultra-activity). The hope was that by providing more wage flexibility this would promote labour market resilience and support a job-rich recovery from the global financial crisis (OECD, 2014[37]). It is not clear to what extent these expectations have materialised. While the reform does not appear to have led to a significant increase in the use of firm-level agreements, possibly due to the absence of recognised worker representatives in most firms, the use of opt-out clauses was relatively common among firms (about 20% in 2019), particularly large firms and firms in the hospitality and arts sectors (OECD, 2021[38]). While the latter may have enhanced the alignment of wages and productivity across firms, it may also have weakened sector-level bargaining and have contributed to the decoupling of wage from productivity growth (see Chapter 2).

In a major labour market reform in 2021, based on a broad-based agreement between the social partners, these changes were partially reversed by restoring the principle of favourability with respect to base pay, allowances and bonuses and bringing back ultra-activity. The reform also specified that in the case of sub-contracting the sector-level collective agreement of the activity in question prevails. However, some room to derogate from sector-level agreements was preserved as working time and other non-wage working conditions continue to be governed by the principle of favourability of firm-level agreements and the use of opt out clauses – arguably the key element of the 2012 reform – was

not affected. Apart from increasing the centralisation of collective bargaining, an important aim of the reform was to strengthen bargaining position of trade unions and in doing so, promote a broader sharing of productivity gains.

The importance of decentralisation for productivity mainly resides in its ability to provide wage flexibility to firms. This can help to enhance the allocation of resources across firms that differ in their productivity. Indeed, in a frictional labour market, wage differences between firms tend to reflect differences in productivity and act as an allocative device by providing incentives for workers to move to more productive firms.[8] Wage flexibility can also contribute to the adaptability of firms to changes in business conditions (including idiosyncratic shocks). As a result, average firm wages in decentralised systems tend to be more strongly aligned with differences in productivity across firms and over time (Berlinghieri, Criscuolo and Blancenay, 2019[39]; OECD, 2021[4]). Other reasons why decentralised collective bargaining may be associated with better productivity performance are that it requires the presence of worker representatives within the firm, which also enables social dialogue in the workplace, and that it tends to be associated with a higher prevalence of performance pay (see Box 3.4)

Empirically, it is difficult to analyse the importance of decentralised collective bargaining systems for productivity. However, there is some indication that countries with more decentralised collective bargaining systems – including those with organised decentralised systems – tend to have better productivity outcomes (OECD, 2019[36]; OECD, 2018[2]). Garnero et al. (2020[40]) study the effects of firm-level bargaining on wages and productivity in Belgium, whose collective bargaining system shares several features with the Spanish one.[9] They show that firm bargaining increases both wage costs and productivity (with respect to sector-level agreements). In the case of Belgium, the productivity premium associated with firm-level agreements is smaller than the corresponding wage premium. This suggests that firm-level agreements help to redistribute income from capital to wages, particularly when product market competition is low and the rents to be shared between workers and firms are relatively high.

The empirical evidence on social dialogue and collective bargaining in the workplace tentatively suggests either no or small positive net effects on firm productivity, with considerable heterogeneity across workplaces, industries and countries – e.g. Hirsch (2004[41]), Addison (2016[42]), Doucouliagos et al. (2018[43]). The effects are likely to be more positive the better the quality of labour relations (Krueger and Mas, 2004[44]; OECD, 2016[45]), the higher the degree of product market competition (Freeman and Medoff, 1984[34])and when collective worker representation in the workplace is present (OECD, 2018[35]). It may also help if the voice and monopoly channels are clearly separated as is the case in dual systems that combine sector-level collective bargaining with works councils in the workplace (Marsden, 2015[46]; Freeman and Lazear, 1995[47]).

The 2021 labour market reform moved towards more centralised collective bargaining, restoring the principle of favourability with respect to base pay, allowances and bonuses. This means that firm-level agreements can no longer deviate downwards from high-order collective agreements with respect to pay. The practical importance of this may be modest since firm-level agreements remain relatively rare and, overall, its use does not appear to have significantly increased since the reform of 2012 when favourability was removed (although this may be different in specific sectors and companies, particularly in multi-service companies). This may be because firm-level agreements require having a trade union or recognised worker representative in the firm which is not always the case. At the same time, some room to derogate from sector-level agreements was preserved as non-wage working conditions continued to be under the principle of favourability of firm-level agreements and the use of opt out clauses – arguably the key element of the 2012 reform – was not affected. Given the alleged importance of decentralised collective bargaining and social dialogue in the workplace for productivity, an *ex post* assessment of the impact of the recent labour market reform would be useful.

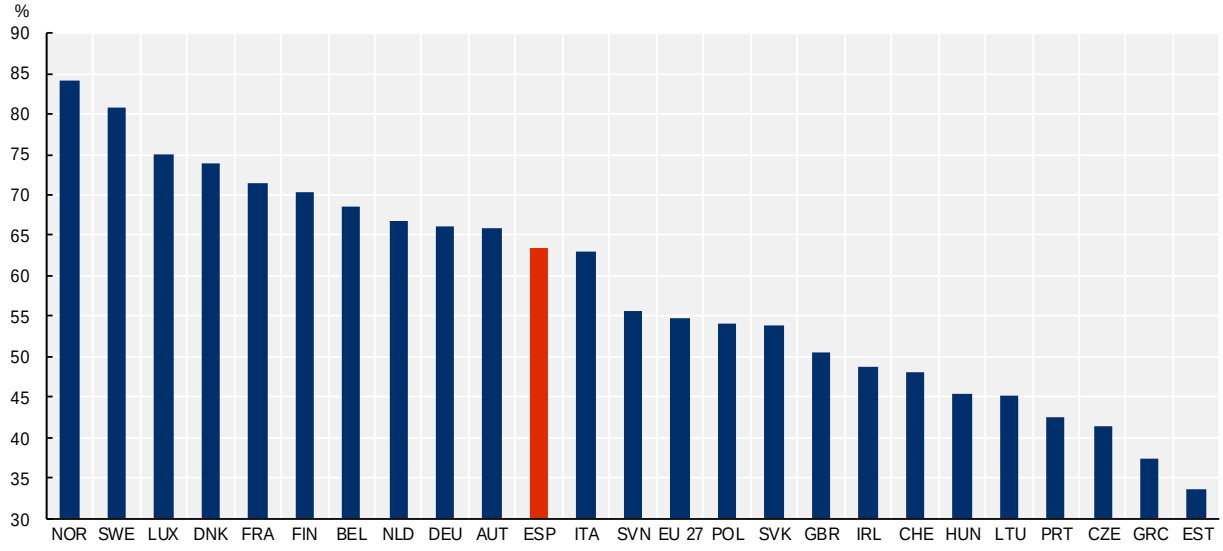
To support social dialogue and firm-level bargaining further promote the representation of workers in the workplace

Collective bargaining systems that leave scope for firms to tailor the conditions set in higher-level agreements tend to be associated with higher productivity growth. In other words, some degree of flexibility at the firm level is required to ensure productivity growth. However, a pre-condition for this to happen is to have representative forms of worker representation at the firm-level, including in SMEs.[10]

There are large differences in the degree of workplace representation across countries (Figure 3.5). Interestingly, the coverage of firm-level representation is not particularly high in EU countries where firm-level bargaining dominates, although institutions of workers representation are indispensable pillars of collective bargaining in single-employer systems. Worker representation at the firm-level tends to be relatively high in multi-level bargaining systems, where sectoral bargaining is complemented by firm-level bargaining levels (notably in the Nordic countries, Germany or the Netherlands). By contrast, firm-level representation is low in countries characterised by sector-level bargaining with only limited bargaining at the firm-level, such as Greece or Portugal (OECD, 2019[36]). In Spain, workplace representation is about 60%, lower than in most other countries with multi-level bargaining, but higher than the EU average. In order to support social dialogue and organised decentralisation, local representation of workers in firms could be promoted further, particularly in SMEs.

Figure 3.5. Workplace representation in EU countries

Employees represented at workplace by trade union, works council or similar body as a percentage of employees



Source: OECD calculations based on the European Working Conditions Telephone Survey 2021.

To extend social dialogue to all segments of the economy, some governments have tried to promote social dialogue in SMEs. For instance, in Italy, the government in 2017 increased tax incentives to promote negotiations on performance-related pay and welfare provisions at the firm level with the stated aim of extending firm-level bargaining to medium and small firms and strengthen the link between productivity and wages at the firm level (D'Amuri and Nizzi, 2017[48]). The evidence discussed in Box 3.4 suggests that this may have contributed to increased labour productivity at the firm level.

Box 3.4. Performance pay, collective bargaining and productivity

Performance pay can positively contribute to labour productivity (Lazear, 2000[49]). In principle, performance pay can help to attract more capable employees, encourage higher effort and quality of work, increase investment in employee training, reduce turnover and absenteeism, and improve teamwork and co-operation. Moreover, performance pay also provides wage flexibility in firms, which may be important in countries where flexibility in base pay and employment is limited (Stokes et al., 2017[50]). However, performance pay also can have drawbacks, such as the incentive to skimp on quality and other difficult to observe aspects of performance. Pay based on individual performance may also weaken incentives for co-operation. Empirical studies suggest that performance pay is usually associated with improved employee productivity (Damiani, Pompei and Ricci, 2022[51]).

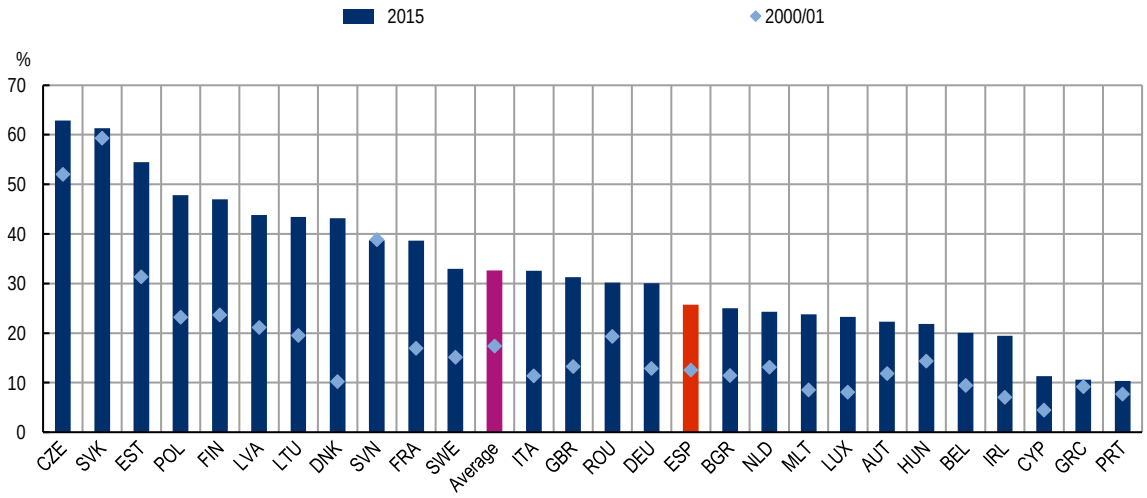
In almost all EU countries, the use of performance pay has increased in recent last decades (Figure 3.6). This has gone hand-in-hand with a decline in the coverage of collective pay agreements. Trade unions have often been reluctant to agree on the use of performance pay as they undermine the goal of more uniform and egalitarian pay policies. In fact, Zwysen (2021[52]) find that in firms where employee representation is present, performance pay is more equally divided. The use of performance pay also tends to be more prevalent in countries in which collective bargaining coverage is low or it is more decentralised.

Like in most other EU countries, the share of workers receiving some form of performance pay in Spain doubled from 13 to 26% during the period 2000 to 2015. However, the use of performance pay remains below the EU average (32.6%) and below nearby countries such as France (38.6%) and Italy (32.6%). The increased use in performance pay reflects the growing use of bonuses linked to individual performance, that of the team or the firm as a whole. By contrast, the share of workers who receive their entire salary based on their own performance pay has declined.

The restoration in the 2021 reform of the principle of favourability with respect to bonuses might slow the increasing trend in the use of performance pay and a specific monitoring could be put in place. In addition, the Spanish Government can promote the use of bonuses through information dissemination and advice on best practices as well as by providing direct fiscal incentives. Italy introduced a tax break for performance pay in 2015. The evidence shows that this increased labour productivity (Damiani, Pompei and Ricci, 2022[51]).

Figure 3.6. Performance pay has become more prevalent

Percentage of employment, 2000/01-2015



Note: The figure shows the share of any type of performance pay (financial participation, team performance, individual performance, piece-rate) over time by country.
Source: Zwysen (2021[52]), *Performance pay across Europe*.

The degree of wage co-ordination across sectors

The effective co-ordination of negotiated wages across bargaining units can help to enhance macroeconomic performance, including productivity. First, wage co-ordination can help align wages with productivity at the aggregate level, consistent with full employment, similar to centralised bargaining (OECD, 2006[53]; Aidt and Tzannatos, 2008[54]). When unemployment is high, the main focus tends to be on wage moderation. In the context of high price inflation and labour shortages that characterises most OECD countries, co-ordination may also support stronger wage growth, depending on the way it is done. Second, wage co-ordination can play an important role in promoting labour market resilience by facilitating adjustments in wages and working time in response to macroeconomic shocks and thereby mitigate the unemployment impact of recessions (OECD, 2012[55]; OECD, 2017[56]). Third, wage co-ordination can help to promote international competitiveness and balanced growth by ensuring that wages remain well aligned with productivity in exporting sectors while preventing wages in other sectors, notably non-tradables, from diverging too much and undermining international competitiveness.[11] Fourth, wage co-ordination necessarily implies some degree of wage compression across sectors and this, in combination with wage moderation, could strengthen incentives for investment in sectors that are highly profitable and support aggregate productivity growth (Barth, Moene and Willumsen, 2014[57]).[12]

Wage co-ordination takes different forms in different countries. Co-ordination is strongest when it is based on strict statutory controls (state-imposed co-ordination). This is the case in Belgium where wages are indexed to increases in living costs but capped by an explicit wage norm based on wage developments in neighbouring countries.[13] In Nordic countries, as well as Austria, Germany and the Netherlands, a lead sector sets the wage norm, usually the manufacturing sector, and others follow (pattern bargaining). (Fougère, Gautier and Roux, 2018[58])[14] In several other countries, peak-level organisations set guidelines that should be followed when bargaining at lower levels (peak-level bargaining). The way wage co-ordination is organised could have important implications for the way it affects macroeconomic performance, including productivity. For example, pattern bargaining is more likely to be associated with wage moderation even when inflation is high, whereas this is less obvious in the case of peak-level bargaining.

In Spain, wage co-ordination tends to be relatively weak. While peak-level organisations play an important role in developing shared responses to key challenges, their role in wage co-ordination across industries is generally limited. Wages are more strongly aligned with productivity across sectors than in countries where wage co-ordination is important (OECD, 2019[36]). Guidelines for wage-setting are not binding and have little impact in practice due to the fragmented nature of employer and employee organisations, the low quality of labour relations and the lack of trust between the social partners. Whether measured in terms of the number of days lost due to strikes, the perceived quality of labour relations by senior executives or the degree of trust by the population in trade unions, Spain is well below the OECD average (OECD, 2019[36]). That said, with the revaluation of the statutory minimum wage, the minimum wage is likely to have become a more important reference point for wage negotiations, potentially increasing the effective degree of wage co-ordination between sectors (similar to France).

Collective bargaining in times of high inflation

The sudden and surprise increase in inflation since the second half of 2021 represents a new and significant challenge for collective bargaining systems in all OECD countries. Negotiated real wages have plummeted in all OECD countries where data are available (OECD, 2023[6]). Several factors can explain why negotiated nominal wages, on average, have not managed to keep up with inflation. Most importantly, the staggered and rather infrequent nature of wage agreements implies that negotiated wages do not adjust immediately to unexpected price inflation.

Spain is one of the few OECD countries where collective agreements can include indexation clauses Table 3.3). According to the Bank of Spain (Banco de España, 2022[59]), in 2022 among the workers covered by a collective agreement, 45% had their negotiated wages indexed to inflation, up from 17% on average in 2014-21, but still lower than at the beginning of the 2000s, when 70% of workers with a collective agreement had such clause. Collective agreements are typically indexed to headline inflation, which includes energy prices. Most workers are covered by annual indexation clauses, but in some cases, there are multi-year indexation clauses. In this case, possible wage adjustments would be determined based on how inflation behaves over the full term of the collective agreement (which can help smoothing the impact of a temporary spike in inflation). Most indexation clauses (75%) include caps, which limit the extent to which inflation is reflected into higher wages.

Wage indexation ensures that employees' salaries keep pace with the cost of living, which can help maintain their purchasing power and provide a sense of security. Additionally, it can help reduce conflicts between employers and employees over wage increases. In 2022, there were relatively few strikes in Spain, in comparison with the historical pattern as well as other OECD countries (OECD, 2023[6]). However, wage indexation can lead to higher labour costs for employers, which can negatively impact their profitability and competitiveness. Moreover, wage indexation can contribute to an inflationary spiral, where prices rise in response to wage increases. For now, it seems that nominal wage adjustments to higher inflation have not fuelled a wage-price spiral. In Spain, like in most of other OECD countries, unit profits have increased by more than unit labour costs between 2021 and 2022 (OECD, 2023[6]). This suggests that many firms were able to increase prices by more than the increase in costs (e.g. higher energy prices, wages), contributing to domestic price pressures. It also means, as mentioned above, that there is some room for profits to absorb further adjustments in wages – at least for the most vulnerable workers – without generating significant price pressures or resulting in a fall in labour demand.

Table 3.3. Automatic wage indexation in collective agreements, 2022

Country	Inflation-indexed (or other indicator) pay scales	Formula	Automatic correction
Belgium	Yes, in all sectors.	"Health index", i.e. past CPI excluding alcohol and tobacco and petrol but including heating fuel, gas, and electricity	No
Germany	Yes, but only in few sectors	The agreement is renegotiated if inflation exceeds a specific rate.	No
Italy	Yes, in all sectors	Forecast HICP index without imported energy goods.	Yes, both upwards and (but rarely or never applied) downwards
Luxembourg	Yes, in all sectors	Past CPI	No
Netherlands	Yes, but only about 5% of the agreements	Past CPI in period t-1	n.a.
Spain	Yes, but only in some sectors	No general rule, but usually CPI in past	Yes, but only upwards (if realised inflation is higher than the indicator of reference) with a maximum cap.
Switzerland	Yes, but only in few sectors	It varies depending on the agreement	Yes, but only upwards (if realised inflation is higher than the indicator of reference)

Note: n.a.: information not available.
Source: OECD Questionnaire on recent measures to deal with inflation pressure on wages (February 2023).

Continue supporting the efforts of social partners to reach broad and forward-looking agreements

As discussed in the OECD Jobs Strategy of 2018, the involvement of the social partners is essential for building consensus, maintaining social peace, and ensuring the legitimacy of policy decisions (OECD, 2018[2]). It allows for the representation of diverse perspectives and helps to balance the interests of different stakeholders. The involvement of the social partners can also help to make policy more forward-looking. This requires identifying potential challenges and opportunities ahead of time, rather than firefighting problems when they arise. Anticipating future challenges and opportunities, finding solutions, and managing change proactively, can be achieved more easily and effectively if employers, workers and their representatives work closely together with the government in a spirit of co-operation and mutual trust. This has been crucial for the 2021 labour market reform and the co-ordination of collective bargaining through the social pact in May 2023. The government needs to continue supporting the efforts of social partners to reach broad and forward-looking agreements and involving them in the development and implementation of future reforms.

This is particularly relevant in times of high inflation. Blanchard and Pisani-Ferry (2022[60]) have argued that a forum in which trade unions, employers' organisations and the government agree on how to share the burden of inflation would likely allow a fairer outcome and lower risk of second-round inflation (e.g. a pass-through of inflationary shocks through wages on prices, thereby triggering a price-wage spiral), making the job of monetary policy easier. Tripartite agreements, including on wages, were relatively common in the heydays of collective bargaining, but they are now very rare. However, the 2022 tripartite agreement on wages and competitiveness in Portugal as well as the May 2023 bipartite agreement in Spain show how social dialogue can help ensuring a fair share of the costs of high inflation and promote broadly shared productivity gains more generally.[15]

3.3. Employment protection and job retention

Job security provisions, whether in the form of employment protection or job retention schemes, can have important implications for broadly shared productivity growth. They can contribute to stronger productivity growth by strengthening incentives for the accumulation and preservation of firm-specific human capital in the workplace by promoting long-term employer-employee relationships and the use of high-performance work and management practices. However, they can also undermine productivity growth. By reducing the tendency of firms to adjust employment in line with changing business conditions and weakening the incentives of workers to move to more productive firms, they may undermine efficiency-enhancing job reallocation across firms. Evidence for OECD countries suggests that strict employment protection may also strengthen incentives for the use of flexible work arrangements, resulting in labour market duality. While a limited use of flexible work arrangements can support labour market efficiency by enhancing the matching process between workers and firms, an excessive use risks undermining incentives for on-the-job learning and hence productivity growth. From a productivity perspective, it is therefore crucial that job security provisions strike the right balance between supporting job reallocation across firms and providing incentives for learning and innovation.

The main insight of this section is that the recent labour market reform of 2021 significantly reduced labour duality and supported labour market resilience through the enhanced design of job retention support (ERTE). More specifically, by restricting the use of temporary contracts, there has been a remarkable shift from temporary contracts to permanent contracts, without any apparent effects on overall employment so far. While these initial outcomes are encouraging, the increase in the use of permanent contracts has to some extent taken the form of intermittent open-ended contracts, which provide more job security than temporary contracts, but not necessarily more income security, since working hours vary, depending on the length of the period of activity and the season, within the limits established in the applicable sectoral collective agreement. The massive use of job retention support during the COVID-19 crisis has prevented a surge in unemployment and stands in sharp contrast with the experience during the global financial crisis when the use of job retention support was negligeable, and unemployment increased massively. The 2021 labour market reform builds on the recent experience with ERTE during the COVID-19 crisis by defining the parameters of the permanent scheme and introducing an innovative mechanism for scaling up support in emergency situations (the so-called RED mechanism).

3.3.1. Employment protection

Employment protection legislation defines the rules that govern the hiring and firing of workers. It is generally justified by the need to protect workers against unfair behaviour on the part of their employers and the need to induce employers to internalise the negative consequences of dismissals on society in terms of higher expenditures on unemployment benefits and the destruction of human capital following job loss and joblessness (Pissarides, 2010[61]). This sub-section starts by benchmarking employment protection rules for permanent and temporary contracts in Spain before the recent labour market reform, then proceeds by discussing the 2021 labour market reform and its effects and concludes with some considerations for the future.

Employment protection is relatively strict in Spain

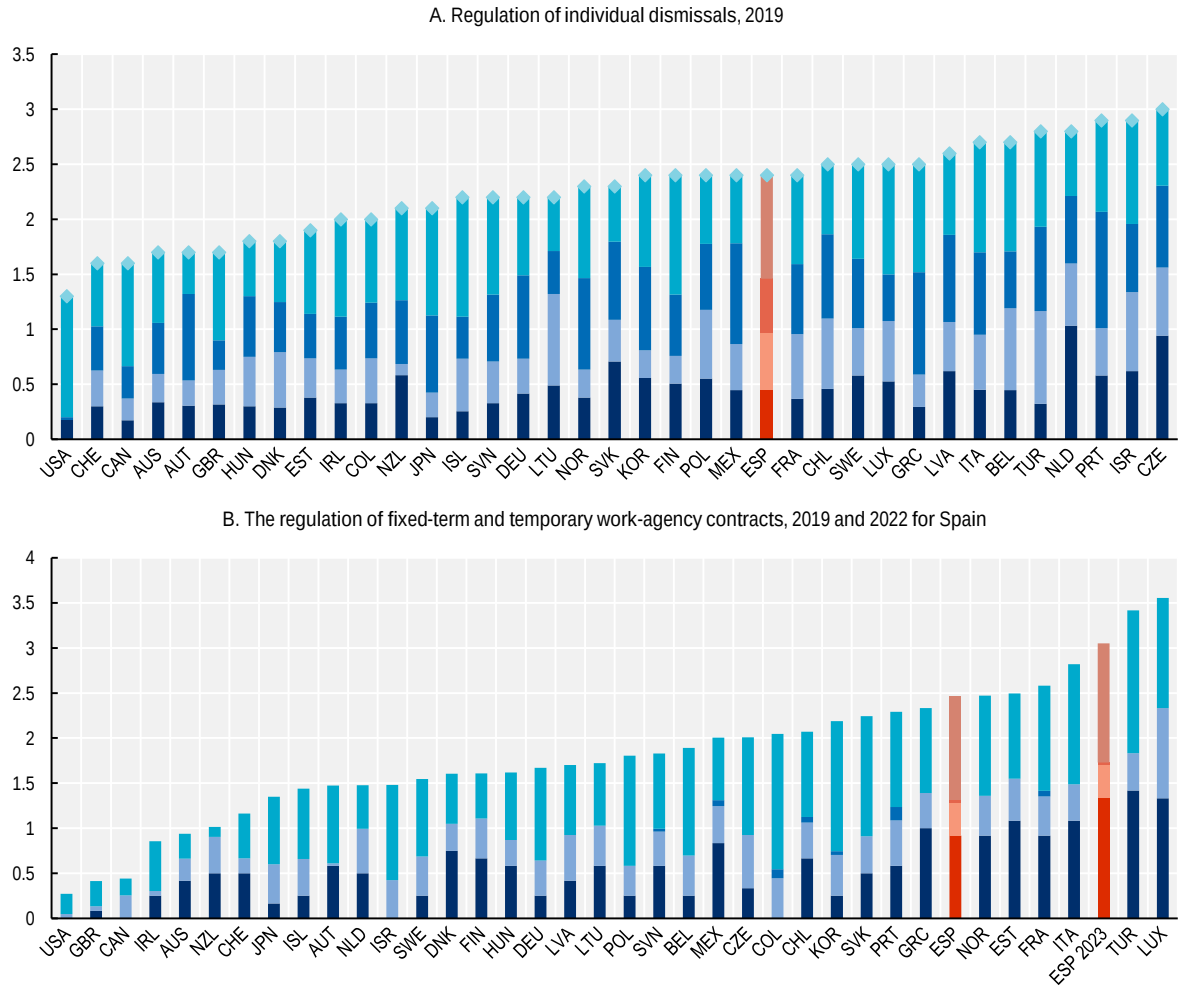
According to the OECD employment protection index of the stringency of individual dismissals of workers on open-ended contracts, Spain is among the top third of countries where regulation is the strictest (Figure 1.6, Panel A). This mainly reflects the high level of severance pay that is due in the case of fair dismissal and the strict enforcement of unfair dismissal regulation. The latter relates to provisions that limit the scope for challenging dismissals in court or which facilitate the termination of employment contracts by mutual consent. Procedural inconveniences for employers engaging in a dismissal process, such as

notification and consultation requirements, do not stand out as being particularly strict. Similarly, the framework for unfair dismissals, which relates to the permissible grounds for fair dismissals and the repercussions for the employer if a dismissal is found to be unfair, is not particularly strict. The rules for collective dismissal are broadly similar as those for individual dismissal.[16]

Similarly, according to the OECD employment protection index on the stringency of regulations on the use of temporary contracts, Spain was among the top fifth of countries with the strictest rules, even before the recent labour market reform (Panel B). The regulation of fixed-term and temporary work-agency contracts (temporary contracts in short) relates to the circumstances where they can be used, the number of times they can be renewed and their cumulative duration. In Spain, fixed-term contracts can only be used for "objective" reasons, such as a temporary task or a temporary increase in workload, while in most other countries, no justification is required for hiring a worker on a temporary contract or specific exemptions apply. The maximum cumulative duration of fixed-term contracts varies according to the reasons for using them from 90 days per year in the case of foreseeable temporary increases in workload to 6 months in the case of an unforeseeable increase in workload or 12 months if specified in the sectoral collective agreement or in the case of training contract (2 years maximum in case of *contrato de formación en alternancia* which combines training with work). Fixed-term contracts can usually be renewed only once within the maximum cumulative duration. Similar rules apply to temporary work-agency employment.

Figure 3.7. The regulation of employment contracts is relatively strict in Spain

Index, 0-6, 2019



Note: Range of indicator scores: 0-6. Panel A: The four broad categories of dismissal regulation determine with equal weight the aggregate score. Panel B: The aggregate indicators assign the same weight to hiring regulation for fixed-term contracts, hiring regulation for temporary work agency contracts and termination of fixed-term contracts. The two indicators for terminating fixed-term contracts before and at the end date contribute in equal shares to the indicator.
Source: OECD EPL database.

Strict employment protection and the excessive use of temporary contracts have raised concerns about their implications for productivity

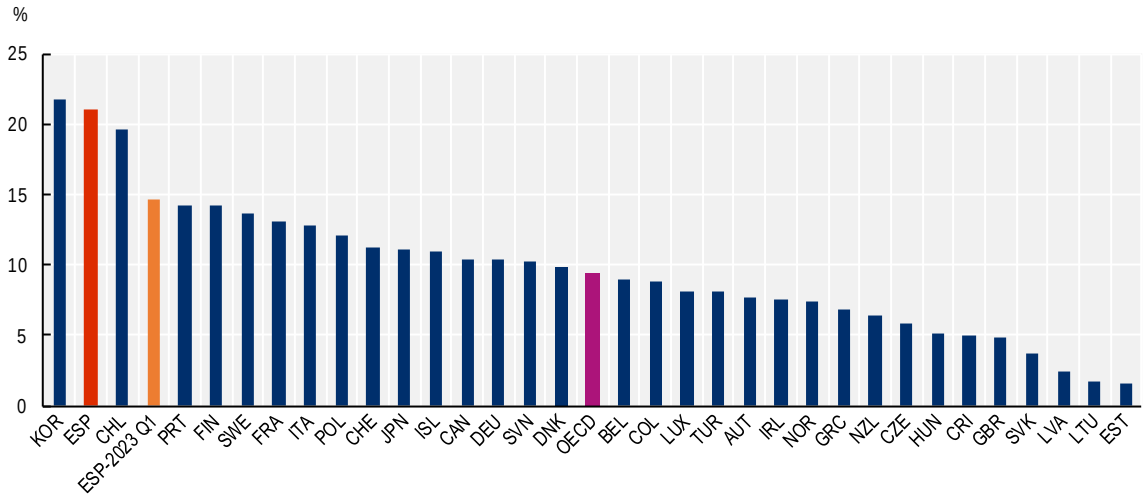
Strict employment protection for permanent workers has sometimes raised concerns about its implications for aggregate productivity growth for two reasons. First, strict employment protection tends to reduce job mobility among permanent workers, with potentially adverse consequences for the efficiency of job reallocation between firms that differ in their productivity. Employment protection of permanent workers not just reduces job dismissals as envisioned, but also incentives for hiring workers on permanent contracts, and hence overall labour market fluidity (Micco and Pagés, 2006[62]; OECD, 2010[63]; Bartelsman, Haltiwanger and Scarpetta, 2013[64]).[17] While the reduction in worker flows is intended to some extent, if it is reduced beyond its optimal level, it can have adverse implications for aggregate productivity growth

(Bassanini, Nunziata and Venn, 2009[65]), by undermining the efficiency of job reallocation across firms (Andrews and Cingano, 2014[66]; Bottasso, Conti and Sulis, 2017[67]). Second, employment protection rules may influence the use of temporary contracts. Evidence for OECD countries suggests that strict rules for permanent workers can strengthen incentives for the use of temporary contracts (OECD, 2018[2]).[18]

The strict regulation of fixed-term contracts has not always been found to have a significant impact on their use. Indeed, before the labour market reform of 2021, Spain had relatively strict rules for the use of temporary contracts, but its incidence in employment was the second highest in the OECD (Figure 3.8). This most likely reflects non-compliance. This is an issue in many OECD countries since workers typically face weak incentives to challenge the inappropriate use of temporary contracts in court, given their weak position in the labour market and the short duration of their contract.[19] That said, a very high use of temporary contracts raises important concerns about productivity growth as well as inclusiveness. While in principle temporary contracts can help promote labour market efficiency by making permanent jobs more accessible for unemployed workers, when their use is too widespread, as was the case in Spain before the 2021 reform, they no longer provide effective stepping stones to permanent jobs but rather tend to replace them, with adverse consequences for average job quality, skill development and productivity growth (OECD, 2018[2]).

Figure 3.8. The use of temporary contracts in Spain was excessively high

Percentage of total employment, 2021 for all countries and Q1 2023 for Spain



Source: OECD Employment database, http://stats.oecd.org/Index.aspx?DataSetCode=TEMP_D and Instituto Nacional de Estadística.

To tackle labour market duality and revive productivity growth, a more balanced approach to employment protection is needed. In principle, this could be achieved through a number of different approaches (OECD, 2018[2]):

- Restricting further the use of temporary contracts (see Box 3.5);
- Easing the employment protection of permanent workers;
- Aligning termination costs across contracts.

The 2021 labour market reform in Spain represents an important step in this direction by restricting the use of temporary contracts, while preserving the changes that were made as part of the 2012 labour market reform that eased the employment protection of permanent workers.

Box 3.5. Recent reforms that increased restrictions to temporary employment

In recent years, a number of OECD countries have conducted labour market reforms that restrict the use of temporary contracts by limiting the circumstance in which they can be used and their maximum cumulative duration.

These reforms in many cases reversed labour market reforms in the 1980s and 1990s that sought to tackle persistent unemployment by liberalising the use of temporary contracts. Today's evidence suggests that these reforms did little to promote overall employment or reduce unemployment, but instead resulted in the substitutions of permanent contracts by temporary ones (Kahn, 2010[68]; Daruich, Di Addario and Saggio, 2023[69]), with adverse consequences for job quality, inclusiveness and productivity growth. Consequently, one would expect the reforms that go in the opposite direction by restricting the use of temporary contracts to have positive outcomes in terms of labour market performance.

Examples of countries that restricted the scope for use temporary contracts:

- **Denmark** introduced the obligation to make temporary employment conditional on objective reasons in 2013.
- **Italy** introduced the obligation to provide a rationale when using a fixed-term contract for more than 12 months in 2018. The reform reversed the 2014 Poletti decree that abolished the obligation to provide a rationale when using fixed-term contracts and allowed for five successive renewals.
- **Slovenia** outlawed the recruitment of different workers in the same position using temporary contracts for more than two years in 2013. In addition, a maximum limit was imposed on the use of temporary agency work in a firm.

Examples of countries that introduced legal limits for the cumulative duration of temporary contracts:

- **Poland** reduced the maximum cumulative duration of temporary contracts to 33 months in 2016.
- **Germany** reduced the maximum cumulative duration of temporary work agency assignments to 18 months in 2017.
- **Slovak Republic** reduced the maximum cumulative duration for temporary work agency assignments to 2 years in 2015.
- **The Netherlands** reduced the maximum cumulative duration of successive temporary contracts from three to two years in 2014.
- **Japan** made it possible for workers who have had a fixed-term contract for at least five years to have their contract automatically converted into a permanent one in 2013.

Source: OECD (2020[70]), "Recent trends in employment protection legislation", in *OECD Employment Outlook 2020: Worker Security and the COVID-19 Crisis*, https://doi.org/10.1787/af9c7d85-en.

The scope for using temporary contracts has been restricted further

In an effort to reduce contractual segmentation, the 2021 labour market reform restricted the use of temporary contracts. From its entry into force in February 2022, permanent contracts became the default contract, while the use of temporary contracts has been strictly limited to temporary staff needs. More specifically, i) the very flexible and widely used *contract for work and service* (*Contrato por obra o servicio*) has been abolished, ii) the duration of the existing training contracts (*contrato de trabajo en prácticas* and

contrato para la formación y el aprendizaje), which had a maximum cumulative duration of 2 and 3 years respectively, has been reduced to one year (*contrato para la obtención de la práctica profesional)* and two years respectively *(contrato de formación en alternancia*); and iii) the requirements to justify the temporary nature of needs have been strengthened. As a result, Spain has become the country with the third strictest rules in the OECD (Figure 1.6).

Another important part of the reform, but one that is not reflected the OECD Employment Protection indicators, is the increased scope for the use of *open-ended intermittent contracts* (*Contrato fijo-discontinuo*). Whereas before the reform their use was strictly limited to seasonal work, the reform extended its scope to all intermittent activities, temporary agency work, and contract work. Consequently, open-ended intermittent contracts can be used for many of the activities that were previously conducted with temporary contracts. In principle, such contracts are preferable to workers since they provide more stability and a stronger protection against the risk of dismissal. That said, their implications for income security are not entirely clear. While the law requires that open-ended intermittent contracts specify in advance the expected period and hours of work, it does not guarantee a minimum amount of activity. The regulation of a minimum guaranteed number of working hours and several other aspects of these contracts is left to collective agreements.[20]

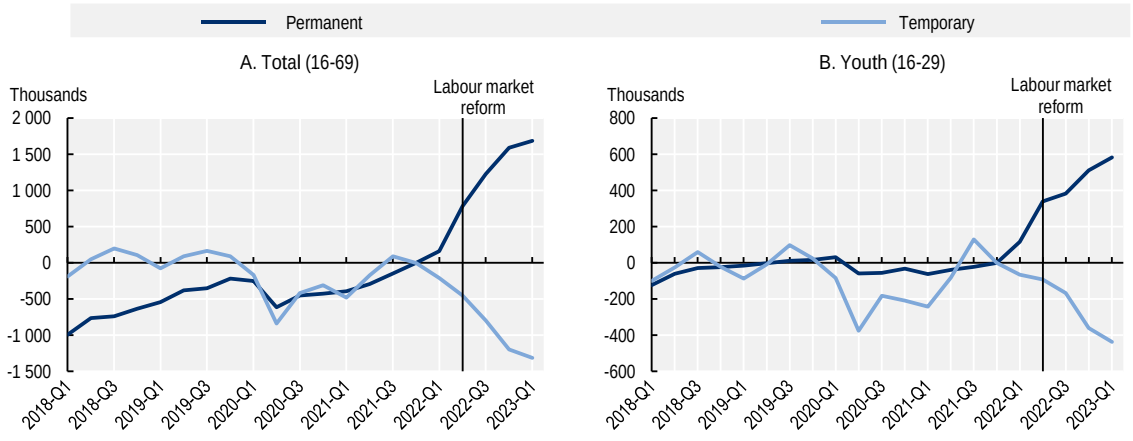
The reform has already resulted in a sharp reduction in the use of temporary contracts

At first glance, the reform seems to have achieved its objective, as it has been followed by a sharp reduction in temporary employment and a surge in permanent employment, particularly among young people (Figure 3.9). The reduction in the incidence of temporary work is sizeable. It declined from more than 20% in 2021, more than double the OECD average, to a less than 15% in Q1 2023, but still about 1.5 times the OECD average. Since the reform has only just been implemented, it is too early to say anything about its implications for productivity growth in the medium and longer term. Consequently, the effects of the reform will need to be monitored closely.

Recent evidence on a similar reform in Portugal indicates a limited impact on employment and a reduction in the incidence of temporary employment (Cahuc et al., 2023[71]) – with positive consequences for job security and job quality, but also for productivity (OECD, 2018[2]; OECD, 2020[70]).[21] One reason is that limited opportunities for career advancement in the firm for people in temporary jobs tend to reduce their commitment to the job and thus their incentives to invest in firm-specific knowledge and skills.

Figure 3.9. The 2022 reform has been followed by a surge in permanent employment and a sharp reduction in temporary employment

Number of permanent and temporary employees (thousands), difference compared to Q4 2021



Source: Instituto Nacional de Estadística, www.ine.es/jaxiT3/Tabla.htm?t=4238&L=0

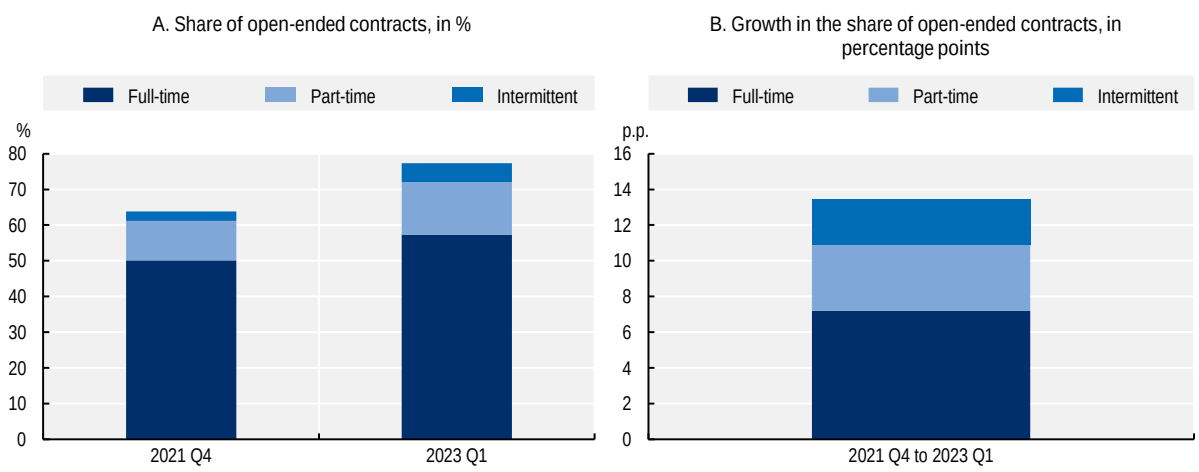
Closely monitor the appropriate use of all contracts and support transitions to regular open-ended contracts

It should be noted, however, that the rise in permanent employment at least to some extent reflects the increased use of *open-ended intermittent contracts* (Muñoz de Bustillo Llorente, 2022[72]). The share of open-ended contracts increased from 64% to 77% on average between 2021Q4 and 2023Q1, with about 20% of this increase due to *open-ended intermittent contracts* (Figure 3.10). Its incidence in employment doubled, from 2.7% in 2021Q4 to 5.3% in 2023Q1, but still remains modest in proportion to the total number of jobs.

As mentioned above, such contracts offer more employment stability than temporary contracts, but not necessarily more income security. Although working hours are known in advance, they might vary depending on the length of the period of activity and the season, within the limits of the applicable sectoral collective agreement. There is also a potential risk that it could increase unemployment benefit expenditures since suspended workers do not need to actively look for another job in contrast to unemployed workers whose temporary contract expired or was terminated. Depending on how firms will use open-ended intermitted contracts, there may be a need to regulate the minimum number of hours in a given period for all sectors, which for now is mostly left to sectoral collective agreements, and for measures that require firms to internalise some of the fiscal costs incurred by the use of these contracts. For example, employers' social security contributions could be linked to a firm's past use of unemployment benefits by workers on *open-ended intermittent* contracts on their payroll. See Box 3.7 for a description of experience-rated unemployment benefits systems in France and the United States.

Promoting transitions from open-ended intermittent contracts (as well as from temporary contracts) to regular open-ended contracts is particularly important. The reform already pays considerable attention to this issue by obliging companies to inform workers on intermittent contracts and their legal representatives of any vacancies for regular open-ended contracts. In addition, workers on intermittent contracts have priority access to vocational training opportunities in the workplace during periods of inactivity. These actions are very much welcomed, and indeed it may be possible to go further. For example, it may be possible to give workers on open-ended intermittent contracts access to career guidance and develop flexible courses that can be combined with variable work schedules.

Figure 3.10. The rise in open-ended employment reflects to a large extent the increased use of open-ended intermittent contracts



Source: Spanish Ministry of Inclusion, Social Security and Migration.

Employment protection for permanent workers could further enhance the better balance between security for workers and flexibility for firms

While the initial effects of the recent labour market reform are promising, it may be possible to go further by reforming the employment protection of workers on permanent contracts. Such reforms are notoriously difficult to implement given their large distributional implications. Indeed, this is the reason why many countries in the 1980s and 1990s, including Spain, opted for partial labour market reforms that liberalised the use of temporary contracts. However, this does not mean that the regulation of permanent contracts cannot be enhanced to provide a better balance between flexibility for firms and security for workers. The Italian Jobs Act provides a nice example. Amongst others, this introduced severance pay for economic dismissal which previously did not exist, increasing the *de jure* level of employment protection. This was expected to reduce incentives to challenge dismissals in court, reducing legal uncertainty for employers. Consequently, workers were better protected against the risk of economic dismissal, while at the same time, the effective dismissal costs for firms were reduced by reducing legal uncertainty. The remainder of this section considers a number of reforms for the regulation of open-ended contracts that do not reduce the effective protection of workers but may help to reduce its effective costs for employers. The next sub-section discusses how internal flexibility, as provided by job retention support, can help to share the costs of economic downturns more evenly across the workforce.

Increase the scope for terminating permanent contracts by mutual consent

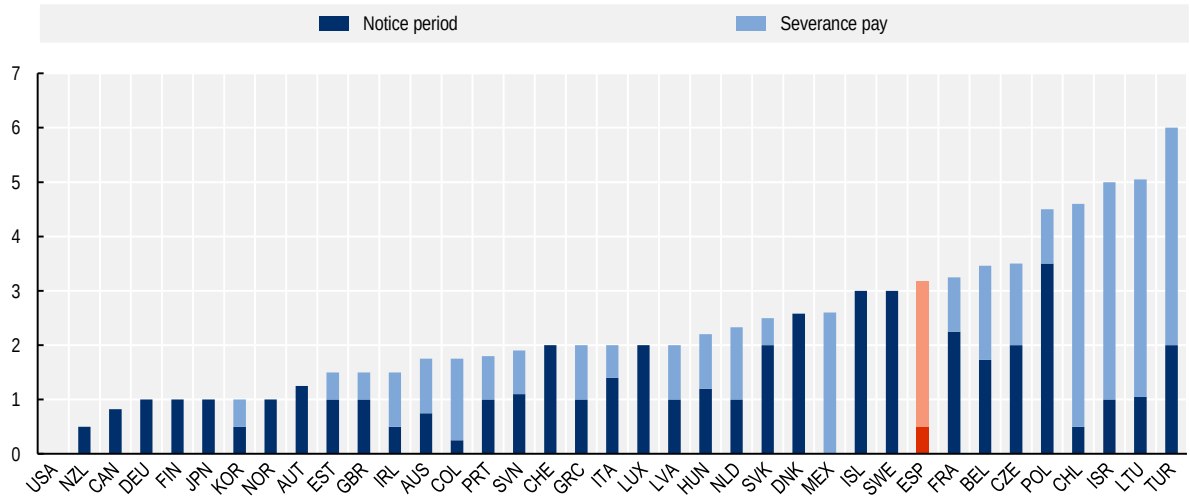
A first possibility could be to make it easier to terminate permanent contracts by mutual consent, as it is rather difficult in Spain in comparison with other OECD countries. Unlike in many other OECD countries, workers who end their contract by mutual consent are not entitled to unemployment benefits in Spain and cannot easily access public employment services related to job-search assistance, career counselling and training. This could reduce the willingness to terminate contracts by mutual consent and increase uncertainty about the cost of dismissal for firms. A number of countries have established specific pre-termination resolution mechanisms to secure job termination for employers (OECD, 2013[73]). For example, France introduced a formalised scheme of termination by mutual agreement in 2008 (*rupture conventionnelle*). The agreement must be approved by the Labour Ministry and is subject to a cooling-off period, after which the employee is entitled to standard severance pay (or more) and unemployment benefits. Strengthening activation services can further help to alleviate concerns that workers who become unemployed do not actively engage in job search (Box 3.6).

Adjust the balance between length of notice period and other aspects of employment protection

A second possibility could be to adjust the balance between the length of notice period and other aspects of employment protection such as severance pay (Figure 3.11). Severance pay for permanent workers is relatively high in Spain in international comparison. It amounts to 20 days of pay per year service up to a maximum of 12 months.[22] At the same time, notification periods are relatively short. Compared with severance pay, notice periods tend to be less costly for employers since the worker is in principle required to continue working during the notice period whereas it can be more protective for workers, by allowing the public employment services to intervene before the dismissal takes place, thereby facilitating the transition to another job (OECD, 2018[74]). Spain may therefore be able to strike a better balance between the costs and benefits of employment protection for regular workers by increasing the length of notification periods, while adjusting other aspects of employment protection to keep the overall stringency of employment protection constant (OECD, 2020[70]). This would also increase the scope for offering employment services to workers during the notice period before the contract ends. It has been shown that this can be particularly effective in reducing the costs of job displacement (Box 3.6).

Figure 3.11. Notice periods are short while severance pay is quite high

Workers on permanent contracts, four years of job tenure, measured in months of pay after dismissal notice, 2019



Note: These values are for individual (not collective) dismissals. They take the average of dismissals for personal and economic reasons.
Source: OECD (2020[75]), *OECD Employment Outlook 2020: Worker Security and the COVID-19 Crisis*, https://doi.org/10.1787/1686c758-en.

Box 3.6. Policies to support displaced workers or workers at risk of job displacement

Employment policies to support displaced workers or workers at risk of displacement (e.g. workers on ERTE in restructuring firms) include early intervention measures and effective activation polices.

Early intervention measures have proved particularly effective

A crucial difference between displaced workers and most other groups served by the public employment service (PES) is that it is often possible to initiate re-employment services during the notice period prior to displacement. Rapid response services, for example by setting up a temporary PES office in factories that will soon close, facilitate the timely delivery of re-employment services. Such early interventions can speed up the adjustment process and achieve better outcomes by starting the process before workers become unemployed. Employers typically view job applications from workers who are still employed more favourably and labour market prospects tend to deteriorate the longer a worker is unemployed. Although such early interventions can be effective, they are not used as widely as would be desirable, as they are often limited to workers affected by mass layoffs or firm closures (OECD, 2018[2]).

The extent to which employers and unions are actively involved in the planning and provision of re-employment services to displaced workers can be important for the effectiveness of early interventions. In Sweden, job security councils, which are operated by the social partners, demonstrate the feasibility of offering early intervention measures to all displaced workers, when employers and unions are actively engaged (OECD, 2013[76]). In Spain, there have been a number of cases, particularly in the context of the green transition, where the social partners have played an active role in the reallocation of workers during mass layoffs. As discussed in the main text, employment protection rules can also help establish an appropriate level of employer engagement by requiring employers to respect a minimum period of advance notice for layoffs. Governments can then ensure that notified workers are the focus of outreach activities by the PES or that workers are required to register with the PES as soon as they are notified.

An effective activation strategy is essential

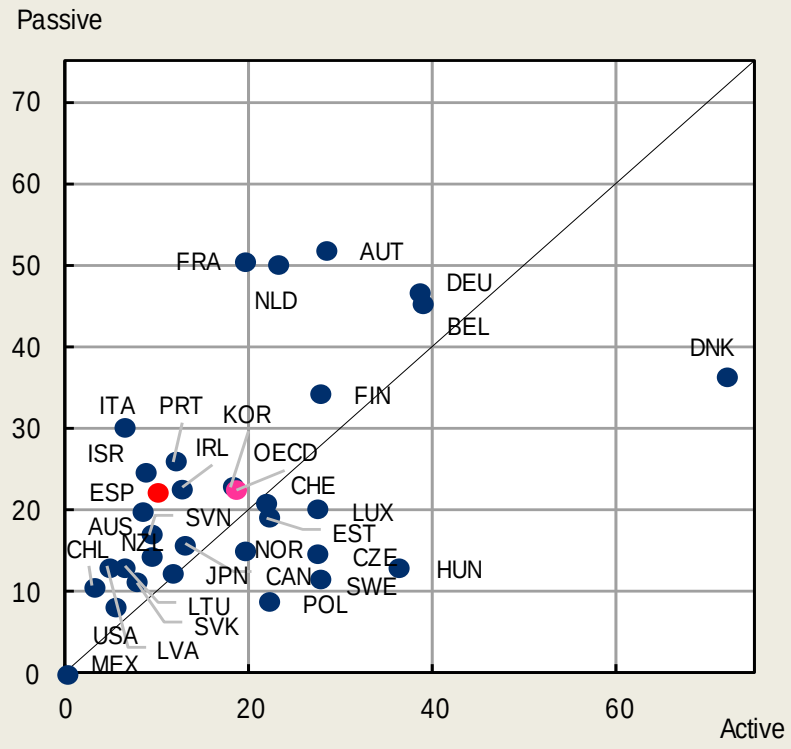
An effective national activation strategy to get people into work provides a solid foundation for promoting the rapid re-employment of displaced workers. In Spain, the share of jobseekers who regularly contact PES is among the lowest in the OECD. This partly reflects the fact that spending on active labour market policies (ALMPs) per unemployed person is significantly lower than in other OECD countries (Figure 3.12). At the same time, spending on income-support measures per unemployed person tends to be significantly higher than elsewhere. Moreover, spending on ALMPs should be better targeted. At present, it is heavily skewed towards hiring subsidies (around 40% of the total), which often are not well targeted to groups with low employability. A better targeting of resources would increase policy effectiveness while at the same time free up of resources for other programmes. The recent of Law of Employment of February 2023 provides an important step in the right direction by modernising active labour market policies through the development of more efficient tools to promote employability, an enhanced co-ordination and planification of the system and the allocation of additional resources.

But policy also needs to take into account the specific barriers to re-employment confronting displaced workers (e.g. obsolete skills and the lack of recent job-search experience), specific advantages (e.g. a history of stable employment and strong labour force attachment) as well as the specific local circumstances (e.g. displacement frequently concentrated in economically declining regions). While all displaced workers should benefit from prompt access to basic job search services, some will require more intensive re-employment services or retraining. One key challenge is to identify this smaller group rapidly and offer them intensive services when these are most effective rather than after a long period

of unemployment as is commonly the case. Displaced workers at risk of long-term unemployment and their support needs can be identified using profiling tools. A promising initiative is SEND@, a digital tool for employment counsellors developed by the Spanish public employment service (SEPE) (OECD, 2022[77]).

Figure 3.12. Spending on active labour market policies per unemployed workers is relatively low in Spain

Active and passive labour market programme spending per unemployed as a percentage of GDP per capita, 2019



Note: 2018/19 for Australia, New Zealand and the United States.
Source: OECD Database on Labour Market Programmes, OECD (2018[2]), *Good jobs for all in a changing world of work: The OECD Jobs Strategy*, https://doi.org/10.1787/9789264308817-en and OECD (2022[78]), *Impact evaluation of the digital tool for employment counsellors in Spain: SEND@*, https://www.oecd.org/els/emp/FinalReport-EvaluationOfSEND.pdf

3.3.2. Job retention schemes

Since the global financial crisis Spain has made several efforts to strengthen job retention support and support labour market resilience. The main idea of job retention schemes is to preserve jobs that are temporarily at risk by allowing firms to reduce their labour inputs in line with the decline in economic activity, while supporting the incomes of workers who have been suspended or whose working hours have been reduced. From a productivity perspective, the main value of job retention scheme is to preserve the match-specific human capital in jobs that have become temporarily unviable but remain viable in the longer term. The main risk is that job retention support is used to prop up jobs in firms with structural difficulties and

hence slows down the process of efficiency-enhancing job reallocation across firms. The design of job retention support is key in determining its costs and benefits (Hijzen, Salvatori and Puymoyen, 2021[79]).

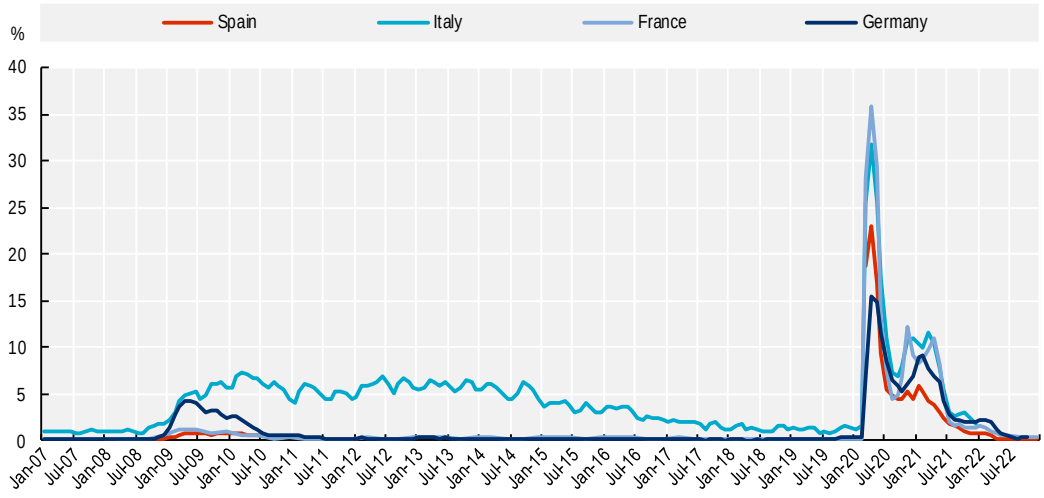
Job retention support during the COVID-19 crisis was a major success

The use of STW as a policy measure to promote labour market resilience is relatively recent in Spain. While a STW mechanism has existed since 1980, it was originally designed as a measure to limit the social impact of collective dismissals with an emphasis on work-sharing. The procedure for application was similar to that for collective dismissals, requiring an initial petition, a consultation period with worker representatives and the approval of the labour authority. This lengthy process meant that the scheme was not well suited for addressing emergencies in the context of a sharp economic downturn. This was illustrated by its limited use during the global financial crisis when take-up peaked at 0.8% of the workforce, well below the average of OECD with STW schemes. The 2012 labour market reform simplified the procedure for both collective dismissal and short-time work. The need for an administrative authorisation was removed and the delays for before giving notice or engaging in short-time work were reduced. In response to the COVID-19 crisis its use was further simplified and its generosity was increased.

During the COVID-19 crisis job retention support was provided promptly, resulting in unprecedented levels of take-up, and its use was phased out gradually as economic activity resumed. In April 2020, just one month after the outbreak of the pandemic, almost one in four workers were covered by job retention support (Figure 3.13). The timeliness of support is likely to have played a crucial role in preventing a surge in unemployment due to the lockdown measures that were put in place to contain the spread the of the virus. As economic restrictions were gradually withdrawn and economic activity resumed, the demand for STW support declined. This was reinforced by adjustments to ERTE that gradually increased the costs of using it for firms. As a result of these factors, the use of ERTE had declined to negligible levels by mid-2022. The fact that take-up did not persist long into the recovery is reassuring and suggests that ERTE is unlikely to have had a major impact on slowing job reallocation from low-productivity firms with structural difficulties to high-productivity ones with healthy growth prospects.[23]

Figure 3.13. The use of STW in historical perspective

Percentage of dependent employment, January 2007 – December 2022



Note: Italy: Data before 2018 are based on the number of authorised hours (estimated number of employees using the ratio of the total hours authorised under the quarterly average hours worked by employee) and spliced using the actual number of participants from January 2018. Spain: Data are not available from October 2010 to February 2020.
Source: OECD (Forthcoming[80]), *Preparing ERTE for the Future: An Evaluation of Job Retention Support During the COVID-19 Crisis*.

Short-time work played a major role in limiting job losses

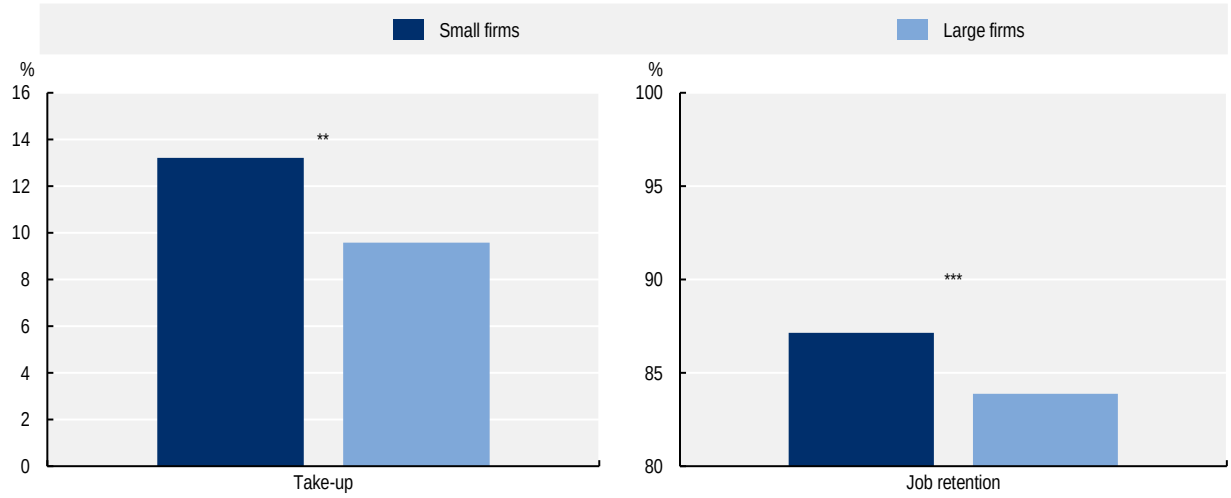
A first indication of this is that the increase in unemployment in response to the decline in economic activity was several times smaller during the COVID-19 crisis when the use of STW was unprecedented than during the global financial crisis when its use was negligeable. The relatively small unemployment response to the decline in economic activity does not just reflect that the COVID-19 crisis was different. If that were to be the only reason, we should see a similar difference in other OECD countries. While there are important differences in some countries, the case of Spain stands out. During the global financial crisis, the Spanish labour market adjusted to the economic downturn by shedding more jobs than any other OECD country. This reflected in part the excessive reliance on temporary contracts which made it easier for firms to shed workers, but also the underdeveloped nature of STW to support broad-based reductions in working time. By the time the COVID-19 crisis struck, there was still a strong reliance on temporary workers, but STW had become available as a tool to support job retention on a massive scale. Consequently, it is likely that STW played a role in limiting the rise in unemployment following the COVID-19 crisis.

In order to more formally evaluate the effectiveness of ERTE in saving jobs during the COVID-19 crisis, OECD (Forthcoming[80]) provides quasi-experimental evidence based on the difference in co-financing rules for hours not worked for small and large firms. During the first 18 months of the COVID-19 crisis, firms with less than 50 employees were fully exempted from paying social security contributions over hours not worked, whereas firms with 50 or more employees were only partially exempted. As a result, firms with slightly less than 50 employees not only used ERTE more intensively than slightly larger firms, but also recorded smaller reductions in employment (Figure 3.14). Moreover, the number of jobs saved relative to the number of jobs supported was sizable, suggesting that efficiency losses were modest. Efficiency losses arise when supporting jobs that do not need support and would have been retained anyway or when supporting jobs that have become permanently unviable and would eventually have been terminated. The positive employment effects of ERTE are largely driven by permanent workers. This is in line with evidence for the global financial crisis that short-time work schemes have a tendency to reinforce labour market segmentation (Hijzen and Venn, 2011[81]).

The effects of ERTE on productivity are more difficult to assess. On the one hand, ERTE is likely to have preserved valuable firm-specific human capital by preventing the destruction of permanent jobs that were temporarily suspended. But on the other, ERTE could also have slowed the job reallocation between firms by supporting jobs that had become permanently unviable in low productivity firms. Cross-country evidence for a number of OECD countries suggests that job retention schemes did not distort the efficiency of job reallocation from less to more productive firms during the COVID-19 crisis (Demmou et al., 2023[82]).

Figure 3.14. The lower the cost of using ERTE for firms the higher is its use and the higher the rate of job retention

Percentage change in employment from February 2020



Note: The figure displays the mean in take-up and employment of ERTE during the first 18 months of the pandemic from March 2020 to August 2021 in firms with 50 or more employees (large firms) and those with less than 50 employees (small firms) on 29 February 2020. During this period the use of ERTE was less costly for small firms as they benefited from larger exemptions from social security contributions over hours not worked. Take-up in Panel A refers to the share of workers employed on February 2020 that spent at least one day on ERTE during the period from March 2020 to August 2021. Job retention in Panel B refers to the share of workers employed in small (large) firms in February 2020 that were still employed in the same firm on average in each month during the period from March 2020 to August 2021. **, *** statistically significant at the 5 and 1 percent level respectively

Source: OECD (Forthcoming[80]), *Preparing ERTE for the Future: An evaluation of Job Retention Support During the COVID-19 Crisis*.

To promote future resilience Spain has enhanced the design of job retention support in 2021

The labour market reform of 2021 also affected the regulation of ERTE (Real Decreto-ley 32/2021): it established the parameters for the permanent scheme; and ii) introduced an explicit framework for scaling up support in times of exceptional need (the "RED mechanism") (OECD, Forthcoming[80]).

As before the pandemic, regular ERTEs could be declared on the basis of either (i) economic, technical, organisational or productive reasons (ETOP), or (ii) force majeure. Firms can reduce hours worked by employees between 10% and 70% of their normal hours or fully suspend workers. Governmental actions that limit or prevent normal economic activities (such as the stay-at-home orders used in the pandemic) were added as legitimate reasons for the use of the force majeure modality of ERTE. As established during the pandemic, firms can benefit from social security exonerations conditional on preserving workers for at least six months after ending their use of ERTE. In the case of ETOP, an interesting innovation is that social security exonerations are only applied if firms undertake training activities for their workers. Replacement rates were kept at 70% for workers on ERTE, irrespective of the modality used.

The reform also created two new types of ERTEs that could be "activated" by the government in the case of either (i) macroeconomic cyclical downturns, or (ii) sectoral transformations that require substantial labour reallocation. The activation of the sectoral one might be requested by a tripartite agreement between the social partners and the government. This possibility is referred to as the "RED Mechanism". Once this mechanism is activated, firms can apply for the use of ERTE under a simplified procedure while benefiting from favourable exoneration rates to social security. A one-year cap on the use of ERTE was set for both types of ERTE, but the sectoral one can be extended for two additional semesters upon approval. In the

case of sectoral ERTE, firms are required to submit a requalification plan for their workers and must provide training in order to obtain social security exonerations.

Spain is now one of the few OECD countries with an explicit framework for scaling up support in times of exceptional need (RED Mechanism). It does so by striking a subtle compromise between allowing for discretion in the modulation of support and the use of automatic rules. The risk of not having an explicit framework for scaling up support is that too much time is needed to reach a political consensus at a time when expediency is of the essence. Automatic rules bypass this issue by scaling up support once a given threshold is reached (e.g. unemployment rate). Such rules are currently used in several OECD countries to extend the maximum duration of unemployment benefits during economic downturns. However, this approach does not work for STW. Since the threshold for triggering additional support is necessarily backward looking, there is a risk that additional support is only made available after the first wave of job losses has taken place. The RED mechanism instead, relies on a tripartite agreement by the social partners validated by the government to trigger additional support.

Considerations for further reflection

While ERTE has been a major success and the 2021 labour market reform already introduced the most important changes to further enhance the effectiveness of ERTE in supporting labour market resilience, it would be useful to continue thinking how it can be fine-tuned further in the future. Below a number of considerations that could be relevant for such a reflection.

Promote the effectiveness of training while on short-time work

Training while on short-time work is actively promoted through the use of financial incentives in the form of additional exemptions from social security contributions. The purpose of training should generally be work-related (in the regular ERTE scheme as well as under the RED mechanism for cyclical reasons). The idea of work-related training is to enhance the viability of the job of the worker and, in doing so, support job retention. While the use of training while on short-time work appears to have been relatively high, it is not always clear whether training is meaningful and effective. In particular, there is a concern that training is done to extract additional exemptions from social security rather to address a specific skill gap. This risk is more pronounced when training is provided informally within the firm. One way to allay such concerns would be to require training to be provided externally by certified suppliers of education services as in the case of France and to conduct regular evaluations of training courses provided in the context of short-time work. Individual learning accounts could further help to promote training that is more directly focused on the career development of workers themselves (see Chapter 2).

Replace co-financing with experience-rated employer contributions

One potential concern with short-time work is that it slows the reallocation of jobs from less to more productivity firms and hence aggregate productivity growth by supporting jobs that have no future beyond the programme. The idea of requiring employers to co-finance part of the cost of hours not worked is that it provides incentives for firms to only use short-time work to support jobs that are at risk but remain viable in the medium term. A potential problem with co-financing however is that it also makes short-time work less effective as a tool to support firms with liquidity constraints, that is, the very firms it is supposed to help. This may be a consequence of the way co-financing is implemented. In Spain as in most other countries, co-financing takes the form of a direct and contemporary contribution to the cost of hours not worked and hence has a tendency of increasing the financial difficulties of firms. To address this issue, Spain could consider a shift from direct co-financing to experience-rating, whereby the current use of ERTE affects social security contributions in the future. This could be part of a broader reform that introduces a bonus-malus system for the financing of unemployment insurance, following the examples of France and

the United States. See Box 3.7 for a description of experience-rated unemployment benefits in France and the United States.

Box 3.7. Experience rating unemployment insurance in France and the United States

Only few countries operate experience-rated employer contributions for unemployment insurance. The United States had such as a system for a long time, while it was introduced in 2022 in France. One reason why few countries operate such systems may be that they tend to be difficult to implement. With the advancement of digital technologies, this argument has become less important. Experience-rating mainly serves to reduce the termination of jobs that are temporarily under pressure as in the case of temporary layoffs, intermittent contracts and short-time work.

United States

Unemployment insurance benefits in the United States are primarily financed through experience-rated employer contributions for unemployment insurance. Each employer has a fictional account that is credited with their contributions and debited with claims from its ex-employees. The balance relative to the wage bill of the employer (highest over the past three to five years) determines the level of contributions subject to a floor and a ceiling. The actual rates vary across states and time. According to the Department of Labor, about 60% of unemployment claims is individualised such that the employer pays for the fiscal cost of layoffs of its own workers, while the other 40% is shared evenly across firms due to the role of floors and ceilings.

France

France introduced a “bonus-malus” system for unemployment insurance in selected sectors in September 2022. The main rationale of the reform was to limit the excessive use of short-term contracts. This bonus-malus modulates the rate of the employer’s unemployment insurance contributions, depending on the number of workers in a firm whose contract is terminated and subsequently registered with the public employment services as a share of its workforce. Firms with a separation rate above the median will see an increase in their contributions up to a ceiling of 5.05% of the wage bill, while firms with a lower rate will experience a reduction down to a floor of 3%. The bonus-malus system applies to firms with more than ten employees in sectors with an average separation rate of more than 150% of the national rate and is calculated based on the separation rate during the previous year.

Source: https://oui.doleta.gov/unemploy/pdf/uilaws_exper_rating.pdf, https://travail-emploi.gouv.fr/emploi-et-insertion/bonus-malus/

3.4. The quality of the work environment

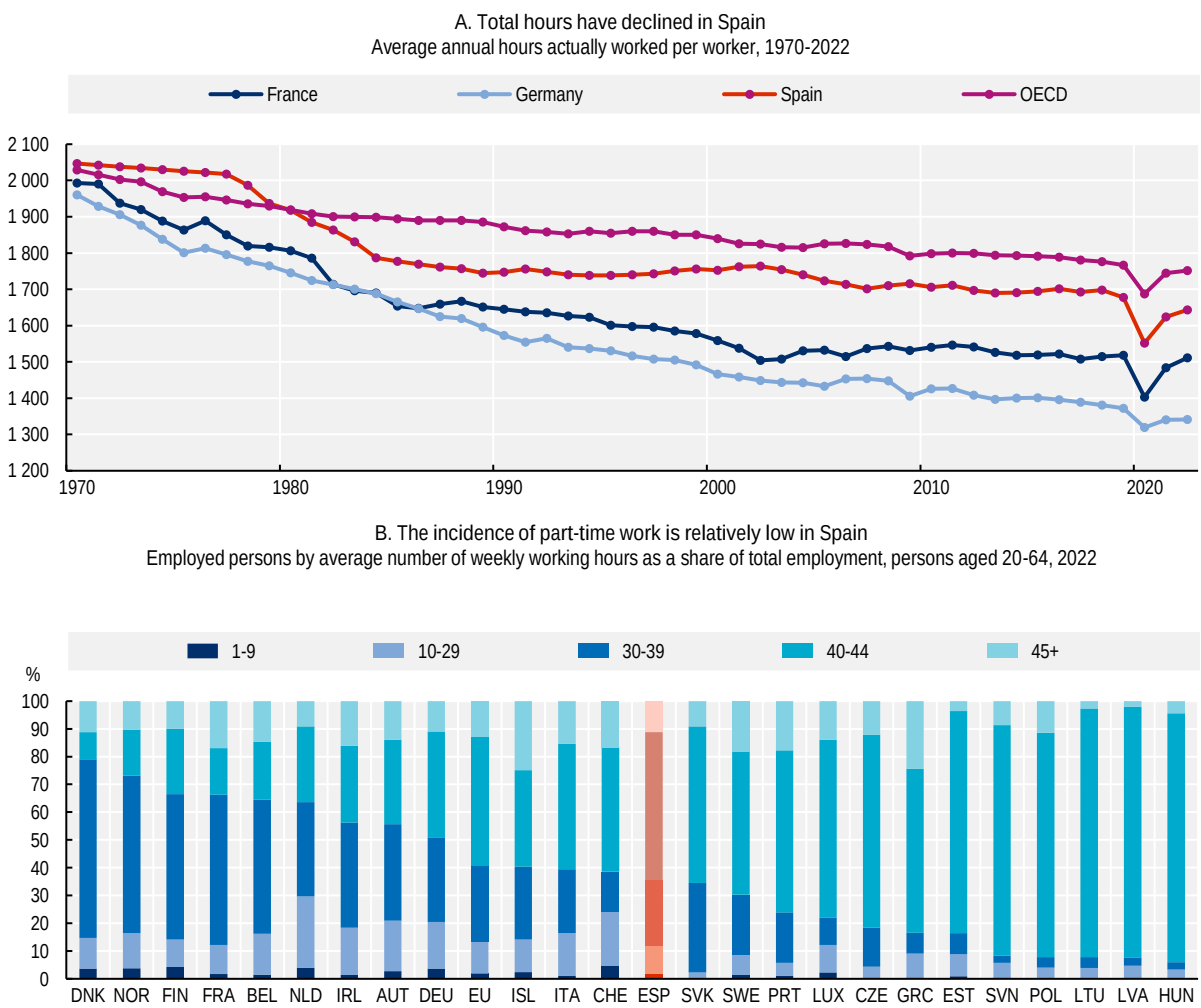
The quality of jobs not only depends on their pay and job security but also on the quality of the working environment (Cazes, Hijzen and Saint-Martin, 2015[1]). A crucial aspect of the working environment is how well workers can combine responsibilities at work with care responsibilities for family members (e.g. children, parents). By allowing for a better work-life balance, working-time regulations not only can play an important role in supporting worker well-being, but also raise productivity. This section therefore zooms in on working time and, more specifically, the possibility of reducing weekly working hours to boost productivity.

3.4.1. Working time

Long working hours lower productivity

It is well established that working long hours is correlated with poorer health outcomes, especially when workers have little control over their time use (OECD, 2021[83]). The link with productivity is less clear cut. At the industry level, there is some evidence of diminishing returns to hours worked, i.e. hourly productivity decreases when working hours are longer – see for example, DeBeaumont et Singell (1999[84]); Shepard et Clifton (2000[85]). At the company level, total worker productivity tends to be proportional to the number of hours worked, i.e. no negative effect (Schank, 2005[86]; Kramarz et al., 2008[87]; Gianella and Lagarde, 1999[88]). Some studies, however, have found threshold effects with regards to part-time work – see Künn-Nelen et al. (2013[89]) and Garnero et al. (2014[90]). At the individual level, some studies have found diminishing returns to working hours in specific professions, such as paramedical staff (Brachet, David and Drechsler, 2012[91]), ammunition workers (Pencavel, 2014[92]), and call centre employees (Collewet and Sauermann, 2017[93]).

Figure 3.15. Total hours worked in Spain remain high compared with other Western European countries



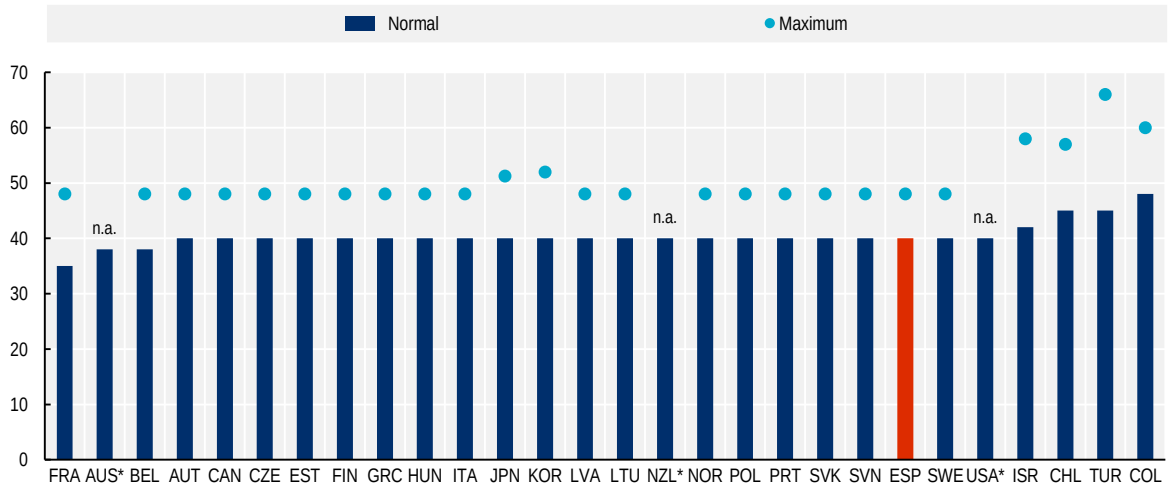
Source: Panel A: OECD (2023[94]), "Hours Worked: Average annual hours actually worked", *OECD Employment and Labour Market Statistics (database)*, https://doi.org/10.1787/data-00303-en. Panel B: Eurostat, Weekly working hours by sex, age, professional status and occupation.

Only few countries have normal working weeks of less than 40 hours

The regulation of working time still displays limited differences across OECD countries, but remains an issue of heated and recurrent debate. Working time regulations typically focus on three main aspects: (i) rules setting maximum weekly working hours, (ii) rules on the use of overtime (level and remuneration), and (iii) the conditions and modalities of these rules (e.g. overtime premia). Compared to other OECD countries, Spain is a country which allows for relatively significant variation in both normal and maximum hours rules alongside Germany, the Netherlands, and Switzerland (OECD, 2021[83]). In Spain like in most OECD countries, the statutory limit for normal weekly hours is set at 40 hours a week, based on a five-day working week and eight-hour working days, but collectively agreed derogations are possible in certain sectors and activities (Figure 3.16). Only three countries have shorter statutory normal weekly working hours: these are France where weekly working hours are capped to 35 and Australia and Belgium where they are capped at 38. Maximum weekly hours including overtime tend to be stricter than the 48-hour limit specified in the EU Working Time Directive since in addition overtime hours cannot exceed 80 within a given year. As in the case of normal weekly hours, the rules allow again for flexibility through the use of collectively agreed derogations in certain sectors and activities.

Figure 3.16. Only few countries operate working time limits on normal weekly hours below 40

Statutory normal and maximum weekly working hours, 2021



Note: * Overtime limits do not exist in Australia, New Zealand and the United States, although in Australia overtime has to be "reasonable" based on a number of defined factors.
Source: OECD (2021[83]), "Working time and its regulation in OECD countries: How much do we work and how?", in *OECD Employment Outlook 2021: Navigating the COVID-19 Crisis and Recovery*, https://doi.org/10.1787/c18a4378-en.

Approaches to reduce weekly working hours

This section briefly discusses a number of approaches that can be used to shorten the working week for full-time workers and hence promote better productivity. While in principle promoting part-time work could be an alternative way of reducing weekly workers worked, the evidence of the positive link between productivity and working time tends to get stronger beyond a certain level (Pencavel, 2018[95]). Since the incidence of overtime does not stand out internationally, the discussion here focuses on ways to reduce the normal working week for full-time workers.

Reducing normal weekly working hours

A number of countries reduced normal weekly working hours for full-time workers, typically without a reduction in monthly earnings (see Box 3.8). A prominent example is that of France which reduced the normal working week for full-time employees from 39 to 35 in 1998/2000 (the "Aubry laws"). Its main objective was to promote employment by sharing the same amount of work across a larger number of workers. A recent study by Batut et al. (2022[96]) provides a cross-country evaluation of a number of similar reforms that took place between 1995 and 2007 in selected European countries. The evaluation exploits industry differences in the initial share of workers directly affected by the reform in combination with the timing of the reform. It finds that hourly wages and productivity in more affected sectors rose, while employment did not increase.

Box 3.8. Working time reforms in selected OECD countries

This box describes examples of reforms that reduced normal weekly hours for full-time workers.

- In 1996, **Portugal** reduced standard weekly working time from 44 to 40 hours while keeping monthly wages constant – hence with an increase in hourly wages – without any specific compensation for firms. While in principle the scope of the reform was wide ranging, in practice it was more limited as around half the workforce was already at or below the new limit before the reform entered into force, due to the stricter constraints imposed by sectoral and regional collective agreements.
- In 1997, **Italy** reduced the standard weekly working hours from 48 to 40 hours. While very large on paper, the Italian reform essentially adapted the labour code to the provisions already foreseen by most collective agreements where standard working hours were already well below 48 h/week. Only 18% of Italian employees were affected by the reform. The Italian reform did not foresee any specific adjustment to monthly wages nor any compensation for firms.
- Following the election of a Socialist Government in 1997, **France** cut standard working time from 39 to 35 hours with no change to the net monthly wages of workers. In exchange, firms received a reduction in social security contributions, targeted to low-skilled workers. The French law was passed in 1998 (Loi Aubry I), but it mainly worked through economic incentives and collective agreements between employers and unions. It was only in 2000 that the reduction in working time was uniformly enforced by law throughout the territory (Loi Aubry II). Overall, 80% of French employees were affected by the reform.
- In 2001, **Belgium** reduced standard working hours to 38. As in France, the reduction was initially voluntary. In order to encourage employers to reduce working time, a one-off reduction in employers' social security contributions was granted. In 2003, all companies were mandated by law to reduce standard working hours to 38 hours with no compensation. Overall, 33% of Belgian employees were affected by the reform.
- In 2002, **Slovenia** reduced standard weekly working time from 42 to 40. The law did not specify anything with respect to wages, but the pay policy agreement for 2002-03 ensured that workers did not get a cut in their wage. At the same time, companies did not receive any compensation or subsidy. Overall, 21% of Slovenian employees were affected by the reform.

Source: Batut et al. (2022[96]), *The employment effects of working time reductions: Sector-level evidence from European reforms*, https://doi.org/ 10.1111/irel.12323.

Shortening the working week

In recent years, there has been a prominent debate in Spain and other OECD countries about the possibility of a four-day work week. In principle, different models can be adopted to implement a shorter work week, with potentially different effects on productivity. A first model involves a reduction in the number of workdays as well as a reduction in weekly working hours at equal wage. A second model involves compressing the 40 hours working week into four days at equal salary, resulting in longer working hours per day, but with no reduction in total weekly or monthly working hours. This was the approach adopted by Belgium in 2022, where the 38-hour workweek was spread over four days, resulting in a 9.5-hour workday. In other cases, hybrid forms between these two models have been adopted. It is likely that different models will have different impacts on productivity. While a reduction in working time is likely to increase productivity and enhance work-life balance, the same may not be true for a reform that reduces the number of working days but at the same time increases their intensity by increasing daily hours.[24]

There is only limited evidence on the impact of a reductions in the working week on productivity. To assess the role of reducing the number of working days, a number of trials have taken place recently, notably spearheaded by the 4 Day Week Global advocacy group (Autonomy, 2023[97]).[25] While the emerging results are encouraging, they should be interpreted with caution since the number of firms involved was typically small and participation in the trial was voluntary, potentially giving rise to selection bias. Moreover, there is likely to be significant heterogeneity across sectors, firms, and occupation in their capacity to adopt the four-day week and its effects on productivity.

Going forward, a key question is to what extent a shorter working week can generate sufficiently large productivity effects to compensate employers for the increase in hourly labour costs and/or workers for the loss in earnings (depending on the way the shorter working week is implemented). Another is the extent to which any productivity effects depend on the way the shorter working is organised (more compressed worker schedules over fewer days or fewer hours per day) and the economic activity of the firm. To better understand these issues, there is a need for policy experimentation and more empirical evidence.

Box 3.9. Recommendations

Minimum wages, working time and collective bargaining.

- Continue supporting the work of the minimum wage commission, by ensuring that both trade unions and employers take part to it and strengthening its resources to monitor and evaluate the effects of the minimum wage on the labour market.
- Explore ways to further enhance the role of the minimum wage by leveraging its co-ordination with the tax-and-benefits system.
- Support social dialogue and organised decentralisation by further promoting the local representation of workers in firms.
- Continue supporting the efforts of social partners to reach broad and forward-looking agreements such as that that led to the 2021 reform or the 2023 social pact on wages.
- Build on the strong involvement of the social partners in the area of working time to promote a better understanding of the effects of a shorter working week by facilitating policy experimentation and expanding the evidence base.

Employment protection and job retention support.

- Continue monitoring the appropriate use of all types of contract and further support transitions to regular open-ended contracts.

- Establish procedures to promote termination by mutual consent while maintaining access to unemployment benefits.
- Increase the length of the notification period to allow providing early support to dismissed workers, while adjusting other aspects of employment protection to keep the overall stringency of employment protection constant.
- Promote the effectiveness of training while on short-time work by requiring work-related training to be provided externally by certified suppliers and conduct regular evaluations to assess the effectiveness of training courses.

Unemployment benefits and activation policies.

- Experience-rate employer social security contributions for unemployment insurance, including in the case of open-ended intermittent contracts and short-time work.
- Provide employment services to workers who are at risk of dismissal, by intervening early during the notice period for dismissal or reaching out to workers on short-time work for structural reasons.

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Notes

[1] Recent years have seen renewed interest at international level in statutory minimum wages. Germany introduced a statutory minimum wage in 2015, and South Africa did so in 2019. In 2022, the European Union passed a new Directive to promote adequate statutory minimum wages and enhance the effective access of workers to minimum wage protection. A number of countries significantly increased the minimum wage (e.g. Portugal, Korea, Mexico, the United Kingdom).

[2] In the United Kingdom, where about 5% of workers are paid at the minimum wage, even an increase in the minimum wage of 20% would only lead to an increase in inflation of 0.2% (which compared to current inflation rates is very small). In France, due its greater bite (about 14% of workers benefitted from the increase of the minimum wage in January 2022), the way it is set (indexed on both inflation and average wage), and its influence on collective wage agreements, the consequences of minimum-wage increases for inflation may be more important (OECD, 2023[6]).

[3] Positive productivity effects in firms using minimum-wage workers mitigate adverse employment effects. Positive reallocation effects by contrast derive from job destruction in firms using minimum-wage workers, but job creation in other firms with higher productivity. As a result, significant reallocation can be consistent with small aggregate employment effects (Dustmann et al., 2021[27]).

[4] See Chapter 2 for further details.

[5] In France, the formula also adds half of past increases in real wages among blue collar workers.

[6] In Belgium and Luxembourg, the indexation mechanism for the minimum wage is the same as the one for collectively agreed wages.

[7] Note that the co-ordination works both ways since the minimum wage also helps ensure that in-work benefits are effective in boosting the incomes of low-wage earners by limiting the scope for "capturing" by employers who lower the wage of workers receiving benefits.

[8] This may be more effective when combined with wage co-ordination (discussed separately in the next sub-section).

[9] In both countries, sectoral agreements play a strong role, extensions are relatively widely used, derogations from higher level agreements are possible but usually limited or not often used. The main difference is that in Belgium, wage co-ordination is strong while it is relatively weak in Spain.

[10] In OECD countries, representative institutions at the firm-level can be local trade union representatives (either appointed by the trade union or elected by the employees), works councils (established bodies elected or appointed by all employees in a firm, irrespective of their membership of a trade union), or workers representatives (either union members or independent). In most OECD countries, several representative institutions can cohabit in one workplace. This often depends on the firm's size and related legal thresholds above which representation is mandatory. In several OECD countries bodies/councils dedicated to occupational health and safety issues are also present in the workplace.

[11] To the extent that the loss of competitiveness can trigger a balance-of-payments crisis, it may also help promote more balanced growth and contribute to macroeconomic stability.

[12] While this may help to explain how Scandinavian countries have been able to marry wage compression with robust productivity growth in principle, our understanding of the role of wage compression for productivity growth remains quite limited. This therefore represents an important topic for future research.

[13] Until 2015, Finland was the country closest to Belgium since central agreements played an important role in guiding what lower-level agreements could negotiate (state-induced co-ordination). In France, the relatively high minimum wage also severely restricts the room of manoeuvre of social partners and renders many wage floors irrelevant (Fougère, Gautier and Roux, 2018[58]).

[14] A concrete example of pattern bargaining is Sweden, where the tradable sector (mainly manufacturing) sets the "cost mark" (an increase in the wage bill for that year), looking at productivity and wage developments in other countries. The cost mark represents a reference ceiling for the other sectors. In this case, the role of firm-level bargaining is mainly called to decide on the distribution of wage increases within the firm (with exceptions).

[15] In October 2022, the Portuguese Government, four employer associations and the trade union UGT signed a tripartite agreement on wages and competitiveness with the goal to both increase the labour share (i.e. the part of national income allocated to wages) and to raise productivity growth. To achieve these objectives, the government, unions and employers agreed to increase the minimum wage, boost workers' income using the tax and benefit system, support to companies' R&D expenditure and on-the-job training and simplify the tax system and the licensing process – see OECD (2023[6]) for more details.

[16] The main difference is that collective dismissals require a consultation period with worker representatives as well as establishing a reallocation plan in companies over 50 employees, which is monitored by the competent labour authority. This plan should be designed for a minimum period of 6 months and should cover job-search support, training and career counselling.

[17] The rules for unfair dismissals, including reinstatement rules, have been shown to be particularly important in this regard (Bassanini and Garnero, 2013[100]).

[18] This is consistent with econometric findings in Bassanini and Garnero (2013[100]) for a large number of OECD countries as well as Hijzen et al. (2017[98]) for Italy and Centeno and Novo (2012[99]) for Portugal.

[19] Nevertheless, there is some indication that in countries where the enforcement of regulations is strict this also matters for employment protection provisions (Bassanini and Garnero, 2013[100]).

[20] Only for contractors and subcontractors, the maximum period between two calls is set at 3 months or that established by sectoral collective agreement.

[21] The reform limited the scope of valid cases for the use of fixed-term contracts (FTCs) in firms with 750 employees or more. Before the reform, FTCs were allowed without any restrictions in new establishments (younger than 2 years). Since February 2009, large firms can no longer benefit from these exemptions.

[22] As a result, permanent workers dismissed after 4 years of services are entitled to 80 days of pay, the fifth highest in the OECD, and those dismissed after 20 years to 360 days, the third highest in the OECD.

[23] This stands in contrast to the experience during the global financial crisis when the use of STW tended to be more persistent in a number of countries (e.g. Italy). This both reflects the protracted nature of the global financial crisis and subsequent reforms that enhanced the design of STW.

[24] Perhaps not surprisingly, the unions in Belgium fiercely opposed the reform in 2022. Similarly indicative, the take-up for a trial experimenting the compressed work week in a public service in one region in France in 2023 was very low.

[25] The Spanish Ministry of Industry, Commerce and Tourism also recently launched a pilot project to enhance productivity in SMEs in manufacturing by reducing weekly working hours.

Reviving Broadly Shared Productivity Growth in Spain

Spain has been confronted with weak wage and productivity growth for several decades. This report provides an overview of the role that labour market policies as well as other policies can play in reviving broadly shared productivity growth in Spain. To set the scene, it starts with documenting the decline in broadly shared productivity growth and its underlying mechanisms. It then provides a discussion of how policies can enhance the adaptability of the economy and labour market to structural change. It concludes with a discussion of the role of selected labour market policies for promoting broadly shared productivity gains. The emphasis is on wage-setting institutions, employment protection and job retention support, consistent with the focus of recent reforms.

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