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Spain's central bank urges government to stick with labour reforms
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Interview with Pablo Hernández de Cos, Governor of the Banco de España

Spain's central bank chief has warned its new leftwing government not to scrap a landmark labour reform that economists say is crucial to the country's recovery.

Pablo Hernández de Cos told the Financial Times that Spain's competitiveness could be hit by moves such as a shift from company-level to sector-wide bargaining over wages and conditions — a priority for the ruling coalition.

"The Spanish economy still needs to keep its competitiveness at a high level," Mr Hernández de Cos said in an interview.

He also put down a marker in the debate on eurozone monetary policy, calling on the European Central Bank to adopt a clear inflation target of 2 per cent, rather than its current, more complicated formulation.

Spain's creation of more than 2m jobs between 2014 and 2018 was one of the recent economic success stories of the eurozone, accounting for about a quarter of all jobs created in the single currency area over the period.

Mr Hernández de Cos noted that a labour market reform pushed through by the previous centre-right government in 2012 gave companies more flexibility to cut costs after the financial crisis. The reform cut severance pay for workers as well as reorienting negotiations on pay and conditions towards individual companies.

"Since it is so difficult from an empirical analysis to disentangle all these changes [put into place by the labour reform] . . . if you just touch one, you do not know what the consequences will be," Mr Hernández de Cos said.

The plan to repeal the reform is a centrepiece of the coalition agreement between the Socialists and the radical left Podemos party, who formed a government last month. They want to ban sackings due to absenteeism caused by illness and limit the use of subcontracting. They also want to end the priority given to company specific rather than sector wide negotiations.

Mr Hernández de Cos argued that it would be better to focus on issues such as reducing the high proportion of people on temporary contracts — more than a quarter of the workforce, one of the highest levels in the eurozone — and cracking down on Spain's perennially high unemployment, now roughly 14 per cent.

The central bank chief sounded an alarm about the government's moves to increase Spain's minimum wage, which rose by 22 per cent in 2019 and 5.5 per cent this year. He suggested it could deny employment to people with lower productivity — such as some younger workers and over 50s.

He also called on the government to take greater steps towards reducing its structural budget deficit of about 2.5 per cent of gross domestic product, and its debt, which is just below 100 per cent.

The fiscal consolidation of the last four years [a period of both centre right and Socialist governments] in terms of the reduction of the structural deficit has been very, very small, almost negligible," he said. "That is a fact."

Mr Hernández de Cos' proposal that the ECB should shift to a straightforward 2 per cent inflation target would bring the bank in line with the US Federal Reserve and the Bank of England. Since 2003 the ECB's objective has been less precise — inflation of "below but close to 2 per cent" — but the target is under discussion as part of the central bank's first strategic review of its policies for 16 years.

The Spanish central bank boss, who worked as an adviser at the ECB from 2004 to 2007 and now sits on its governing council, said such a shift would "provide clarity" at a time when "even people working in financial markets have different interpretations" of the ECB's inflation target.

"I think it is crucial for monetary policy to anchor inflation expectations of agents: you need to be able to transmit what your target is and for them to know what it is," he said, adding that such a move would clarify that the ECB was as concerned about inflation undershooting its target as overshooting it.

"A point target, a simple one that has been used by other institutions — that is good for me," he said.

Mr Hernández de Cos is seen as one of the more dovish members of the ECB governing council who supported its recent cuts to interest rates. Hawkish members are likely to press for it to target a range of inflation — say between 1.5 per cent and 2 per cent — which may make rate rises more likely at a lower level of inflation.