What can we expect from Spain's ERTEs and similar furlough programmes? A European perspective

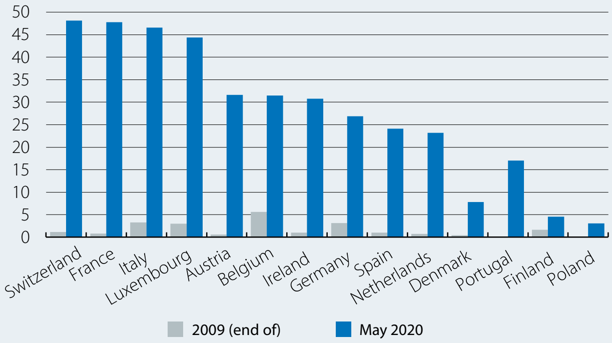
- **Temporary workforce reduction programmes (such as Spain's ERTEs) have become a widely used tool in Europe to prevent a sharp increase in unemployment following the COVID-19 outbreak.**
- **These programmes have a positive impact on the labour market in the event of temporary shocks affecting firms that are viable in the medium term. However, when a shock is of a more permanent nature, the destruction of jobs is not so much avoided as delayed.**

ERTEs have established their role as a key economic policy in Spain for cushioning the immense impact of the COVID-19 outbreak on the labour market. In June, they affected 1.83 million workers (3.4 million at the beginning of May) and represent the bulk of the exceptional expenses incurred in tackling the economic and social emergency we are currently experiencing. As we can see in the first chart, Spain is no exception: temporary workforce reduction programmes, which include ERTEs in Spain, are being widely used throughout Europe.

Although there are differences in the institutional design of the programmes implemented in most European economies, they share certain common features (see table): the procedures involved have been streamlined and the eligibility requirements eased, the state covers a fairly high fraction of the salary that workers affected by a total or partial reduction in their work no longer receive, and they are relatively long-lasting (especially in Germany and France).

Europe: percentage of workers in temporary workforce reduction programmes

(%)



***Note:** The data for Portugal correspond to mid-June and have been provided by the Government of Portugal.*
***Source:** CaixaBank Research, based on data from the European Trade Union Institute for 2020 and from the OECD for 2009.*

When analysing the impact of such furlough schemes, we must differentiate between the short and medium term. Their positive effects in the short term are widely documented, as they allow firms to retain their staff –

Europe: temporary workforce reduction programmes due to the COVID-19 outbreak

	Germany (*Kurzarbeit*)	Spain (ERTE)	France (*Chomâge Partiel*)	Italy (CIGS)	United Kingdom (*Job Retention Schemes*)
Eligibility	• More than 10% (33% in the 2008 financial crisis) of the company's workers have had their working hours reduced by more than 10%.	• Applies to companies which, due to force majeure (COVID-19), have either suspended their workers or reduced their working hours. A minimum period of Social Security registration is not required.	• Companies which want to temporarily suspend their workers or reduce their working hours.	• Companies can request it for either staff suspension or a reduction in working hours (the obligation to reach an agreement with the unions is eliminated).	• Workers with leave of absence. To qualify for the programme, working hour reductions were not previously permitted, although they are from 1 July.
Financial support	• Between 60% and 67% (67% for workers with dependent children) of the net salary lost + the Social Security contributions paid by the company are covered. This rises to 70% between the third and sixth months and to 80% from the seventh month.	• 70% of the net salary lost + full or partial coverage of the Social Security contributions paid by the company.	• 84% of the net salary lost (100% for workers on the minimum wage), with coverage of the Social Security contributions paid by the company.	• 80% of the gross salary lost.	• 80% of the gross salary (up to a maximum of 2,500 pounds per month) + coverage of both Social Security and pension plan contributions.
Duration	• Maximum of 21 months (normally 12 months).	• Until 30 September.	• Maximum of 12 months (6 weeks in the 2008 financial crisis).	• Under current conditions for COVID-19, until 31 October 2020.	• Until 31 October 2020.

***Notes:** Conditions of these programmes as of June 2020. Changes introduced after that month are not included.*
***Source:** CaixaBank Research, based on data from the national authorities.*

thus saving redundancy costs and the cost of searching for replacements when the economy is reactivated – as well as offering workers some certainty. In addition, they allow the aid to be tailored to reductions in working hours and have a lower public cost than alternatives such as wage subsidies or unemployment benefits.

In this regard, the *Kurzarbeit* in Germany was particularly effective during the Great Recession, saving an estimated 400,000 jobs. According to some estimates, the *Kurzarbeit* reduced Germany's unemployment rate in 2009 by 1.3 pps, and 4 out of 5 workers covered by this scheme were able to return to their usual job.[1] Furthermore, the positive effects on firms can be long-lasting: it has been documented that French companies that used this workforce reduction mechanism after the financial crisis fared better on average[2] than similar companies that did not use this type of programme.[3]

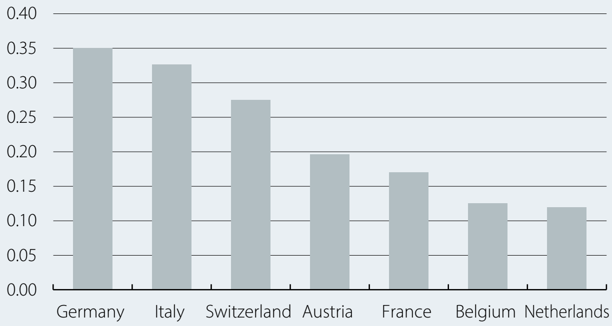
Various empirical studies have used sophisticated statistical techniques to identify the causal effects of these diverging paths and have corroborated the effectiveness of such programmes implemented during the Great Recession (2008-2009). It is estimated that in Germany, 0.35 jobs were saved for each worker enrolled in the programme.[4] This may seem a low figure, but in reality its level well below 1 is logical, since some jobs would have been preserved in the absence of these programmes as well. As an example, in France it is estimated that only 0.17 jobs were saved per worker covered by such schemes.[5]

One interesting element is the fact that, in the 2008 financial crisis, the positive effects were only observed among workers on permanent contracts, since firms are most interested in retaining them. In contrast, no beneficial effects were observed among temporary workers. This situation is very likely to be repeated in the current crisis, and it will have to be given particular consideration in economies with a high degree of labour market duality such as Spain or Italy.

However, experience with these programmes also shows that, while they are particularly effective for cushioning temporary shocks, they lose their effectiveness if the shocks persist in time. This explains why these programmes were especially effective for Germany, where the shock of the Great Recession had a temporary effect limited to 2009. In contrast, the effects on employment ended up being lost in Italy, where the shock was much more persistent as it continued through to 2012 due the sovereign-debt crisis. In fact, when the shock is temporary, firms that use temporary workforce reduction programmes manage to retain between 10% and 15% of the staff that they would have laid off if the shock were permanent.[6] Furthermore, as the last chart shows for the case of Italy, during the last financial crisis the positive effect of maintaining employment was only short-lived (during the year in which the programme was administered). Two years later, in contrast, the probability of being employed was exactly the same for a worker

Jobs saved in 2009 for each worker in a temporary workforce reduction programme with reduced working hours following the 2008 financial crisis

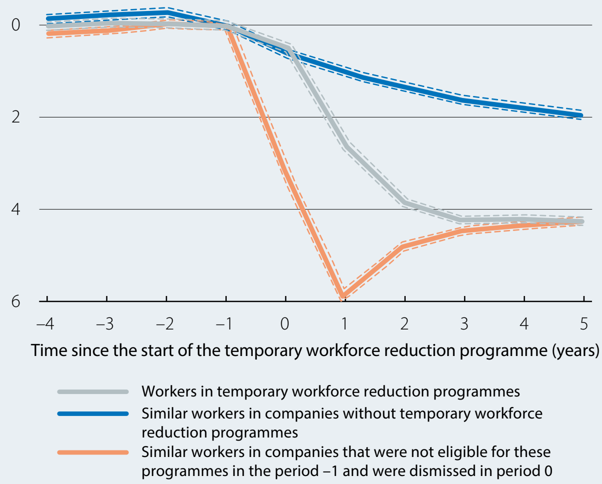
(Number)



Source: *CaixaBank Research, based on data collected from the main studies carried out in the various economies.*

Italy: probability of obtaining employment following temporary workforce reduction programmes in the 2008 financial crisis

Change in the probability of being employed compared to the period –1 (pps)



Note: *In most cases, period 0 corresponds to 2009, the year in which the Great Recession affected the Italian economy.*
Source: *G. Giupponi and C. Landais (2018). «Subsidizing labor hoarding in recessions: The employment & welfare effects of short time work». CEP Discussion Paper n° 1585.*

1. See J. Tilly and K. Niedermayer (2016). «Employment and welfare effects of short-time work». Working paper.
2. After 3 years, they were larger and had a lower probability of going bankrupt. In addition, they managed to recover their pre-crisis levels of profitability, as measured by ROE (return on equity) and ROA (return on assets).
3. See P. Cahuc and S. Carcillo (2011). «Is short-time work a good method to keep unemployment down?». Nordic Economic Policy Review, 1(1), 133-165.
4. See T. Boeri and H. Bruecker (2011). «Short-time work benefits revisited: some lessons from the Great Recession». Economic Policy, 26(68), 697-765.
5. *Op. cit.* note 3.
6. See G. Giupponi and C. Landais (2018). «Subsidizing labor hoarding in recessions: The employment & welfare effects of short time work». CEP Discussion Paper nº 1585.

who had been included in a furlough scheme and another with similar characteristics who had been fired at the time of the shock.

In addition, extending these programmes for longer than necessary slows down the reallocation of resources towards the most productive firms and can thus reduce aggregate productivity. Once again, Italy is an illustrative case: the empirical evidence shows that a 1-pp increase in the fraction of workers included in furlough schemes reduced employment in all other firms by 0.94% and cut productivity by 2%.

In short, subsidised furlough schemes are proving to be a key tool for cushioning the shock of the coronavirus outbreak on the labour market. However, looking ahead, we will have to tread very carefully in order to adapt such schemes to the new normal. In particular, their duration will have to be carefully fine-tuned. Withdrawing them too early could stifle some companies with a temporary drop in demand which therefore need them to survive until demand recovers. Keeping them in place for too long, however, may do nothing more than prolong the agony for some firms that will no longer be able to stay float, either because the decline in demand is more permanent or because the firms in question were starting from a position of relative weakness. In addition, furlough schemes covering workforce reductions triggered by force majeure will need to be quickly transformed into schemes covering those triggered by economic factors. On top of this, firms and workers will need to be properly incentivised to successfully return to work and to recommence productive activity. To this end, such schemes will need to be made more flexible and differentiated by sector – for example, being maintained in sectors affected by social distancing measures while a vaccine is still being sought –, while reducing working hours, rather than simply cutting staff numbers, will need to be encouraged.

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