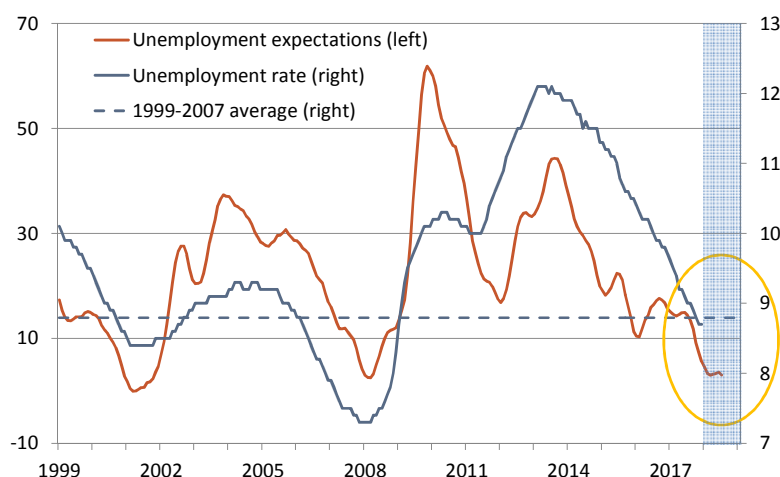


2 February 2018

The Eurozone labour market: nice job

Eurozone unemployment rate (%) versus expectations over next 12 months



Consumers' unemployment expectations over the next 12 months, six-month average, advanced by six months (left). Unemployment rate in % (right). Average unemployment rate from 1999-2007 is 8.8%. Sources: European Commission, Eurostat.

- Jobs, jobs, jobs:** During the double whammy of the financial and euro crisis, 5.5m workers lost their jobs in the Eurozone. The unemployment rate shot up from 7.3% in early 2008 to a peak of 12.1% in early 2013. Since then, the labour market has turned around. Over the last five years, 7.5m jobs were created.
- Back to normal:** In January 2018, the unemployment rate fell below its 1999-2007 average (8.8%) for the first time in nine years to 8.7%. According to job openings data, labour demand in the Eurozone is at a record high. Unlike the US, where participation has fallen in recent years, Eurozone participation is rising. Surveys show that labour shortages are starting to replace a lack of demand as the number one limitation on production and business expansion.
- Recovery-turned expansion:** The labour-market-driven Eurozone recovery has broadened across all countries and sectors. All major pillars of demand are contributing to growth. More recently, the synchronised, investment-led pick-up in global growth has provided an extra boost to Eurozone confidence and exports. So far at least, there have been no major negative shocks (think Trump-led tit-for-tat protectionism). Meanwhile, French President Emmanuel Macron has reduced the cloud of political uncertainty over the Eurozone. His labour market reforms for the French economy have helped turn the initial Eurozone recovery into a fully fledged expansion that can last.
- Still more room for growth:** There is still spare capacity in the Eurozone labour market. The Eurozone economy can, therefore, sustain above-trend growth (c2.5%) for a while without overheating. According to survey data by the European Commission, consumer expectations for further falls in the unemployment rate over the next 12 months are at their highest in 16 years. Can unemployment fall below the pre-crisis low? Probably, yes. Other economies that are at a more advanced stage of the cycle, such as Germany and the UK, enjoy unemployment rates well below pre-crisis levels with participation – unlike in the US – rising to record highs.
- The ECB can go slow:** Eurozone demand growth is healthy and self-sustaining, and measures of spare capacity are falling. But the Eurozone is not quite close enough to full capacity yet for the ECB to be confident enough to tighten policy soon. Until the unemployment rate falls further, wage growth will remain subdued and inflation will remain below the ECB's "below, but close to 2%" target. Although real GDP is growing well-above trend, the low risk of an inflation overshoot means the ECB can go slow when it finally decides to remove some stimulus. We expect the ECB to stop growing its balance sheet in September 2018 and begin its rate hike cycle in Q1 2019. If core inflation were to remain sticky at the current below-target level of c1%, the ECB may feel the need to go even slower in order to let the labour market run a bit hot.

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