SECTORAL REALLOCATION OF EURO AREA EMPLOYMENT AFTER THE COVID-19 SHOCK
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Abstract

The COVID-19 pandemic triggered an unprecedented labour market shock whose consequences are not yet fully understood. While labour demand suddenly froze as the pandemic hit, policy support in the form of job retention schemes helped to protect employment in many European countries but benefited more employees on permanent contracts. The COVID-19 shock had therefore very heterogeneous effects, hitting employed and job seekers with different intensities, and potentially inducing a significant process of labour reallocation. Furthermore, reflecting the larger direct impact of the pandemic on more contact-intensive work, the pandemic shock has been highly asymmetric in its employment effects across sectors.

In addition, pandemic-induced reallocations across occupations and sectors and the boost in the automation and digitalisation process has might increase the labour market mismatch and generate upward pressures on wages. However, the sharp, employment-intensive rebound in economic activity following the pandemic shock means that many workers may have been rehired before their work skills have depreciated. In any case, the question is whether, as the recovery progressed, demand returned to the same sectors where it had fallen, or whether there have been permanent job losses in those sectors. Overall, studying job flows is informative of the status of the labour market recovery post-Covid-19 pandemic and of the extent of perspective labour reallocation across sectors, as well as productivity and wage growth.

Indeed, reallocation may reflect efficient changes in employment following structural shifts caused by the pandemic – in that case job retention policies may hinder a
sustainable recovery. Labour reallocation is generally associated with a rise in productivity and growth, both determining innovation advancements and driving the business cycle. The dynamics of job-to-job transitions is also associated to earnings dynamics, though with country differences that depend on labour market institutions and structural features.

Regarding the extent of the COVID-19 reallocation shock, given its exogenous nature, it has might be lower than with the global financial crisis, whose origin was purely economic. However, Barrero et al. (2021) find evidence that the COVID-19 pandemic is largely a reallocation shock to the U.S. economy.¹ On the other hand, Anayi et al. (2021) find for the United Kingdom that during the COVID pandemic job reallocation rose less than during the Global Financial Crisis and point to the role of furlough schemes in reducing the extent of employment reallocation.²

This paper seeks first to assess the extent of the reallocation shock induced by the COVID-19 pandemic for the euro area economy, focusing on its four biggest countries (Germany, France, Italy and Spain). Then the aforementioned sectoral heterogeneity will be analysed. The hypotheses to be tested is that the COVID-19 pandemic has not been a major reallocation shock, in comparison with previous recessions.

Employment reallocation can be defined as the number of persons who currently have a different job or employment status than they had in the previous period. In this paper, those transitions are calculated from the EU-LFS data, that are available in a harmonized way for all 19 euro area countries. This survey provides population estimates for the main labour market characteristics, such as employment, unemployment, people outside the labour force, hours of work, occupation, economic activity and other labour related variables, as well as important socio-demographic characteristics, such as sex, age, education, household characteristics and regions of residence. The EU-LFS aggregated data on labour market transitions published by Eurostat do not provide a breakdown of employment flows by sector. Therefore, individual microdata are used, though they do not contain the information which

would allow tracking people across waves, so the paper mainly draws on the annual retrospective information, available since 2008.

Then, a standard measure of employment reallocation, namely, the excess reallocation rate will be computed. The sum of hiring and separations gives a measure for worker reallocation and the difference yields the net employment growth rate. Taking the difference between the gross worker reallocation rate and the absolute value of the net employment growth rate, a measure for excess worker reallocation is obtained. Such a measure indicates how much job churning is taking place after having accounted for the worker reallocation that is needed to accommodate a given aggregate employment growth rate. This measure will be analysed across sectors both from a time perspective and in terms of the contributions of the different types of flows that make up the indicator: hiring, separations and net flows.

The excess worker reallocation rate calculated from the EU-LFS microdata, available until 2020, for the aggregate of the four largest euro area economies decreased almost 2 pp in 2020, against the increases that firm-level data show for the United States and the United Kingdom. That development in the euro area was also very different to that observed in 2009, mainly due to a smaller increase in separations during the COVID-19 crisis. In the latter respect, the role played by the job retention schemes should be re-emphasised. Job-to-job transitions account for almost 60% of the excess allocation rate. Its reduction in 2020 was similar to that of 2009, but much more concentrated in their within sector component.

By sector, the largest declines in excess reallocation in 2020 took place in the accommodation and food services and arts and entertainment sectors, while just the non-market services, and the electricity and professional and scientific activities sectors increased their rates. Compared to the global financial crisis, just the construction sector experienced a lower drop in its excess reallocation rate in the COVID-19 crisis, due mainly to its slower acceleration in the fall in net employment.

Nevertheless, the aggregated data available for 2021 anticipate higher inflows and lower outflows. Overall, and coupled with expected higher job-to-job transitions, this

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3 EU-LFS microdata for 2021 are planned to be released in December 2022.
might have led to an increase in employment reallocation in 2021, as preliminary findings from national LFS microdata and administrative registers show for Italy and Spain.\textsuperscript{4}

**Keywords:** COVID-19, worker reallocation, job-to-job transitions