

Labour market and factor utilisation



Labour market

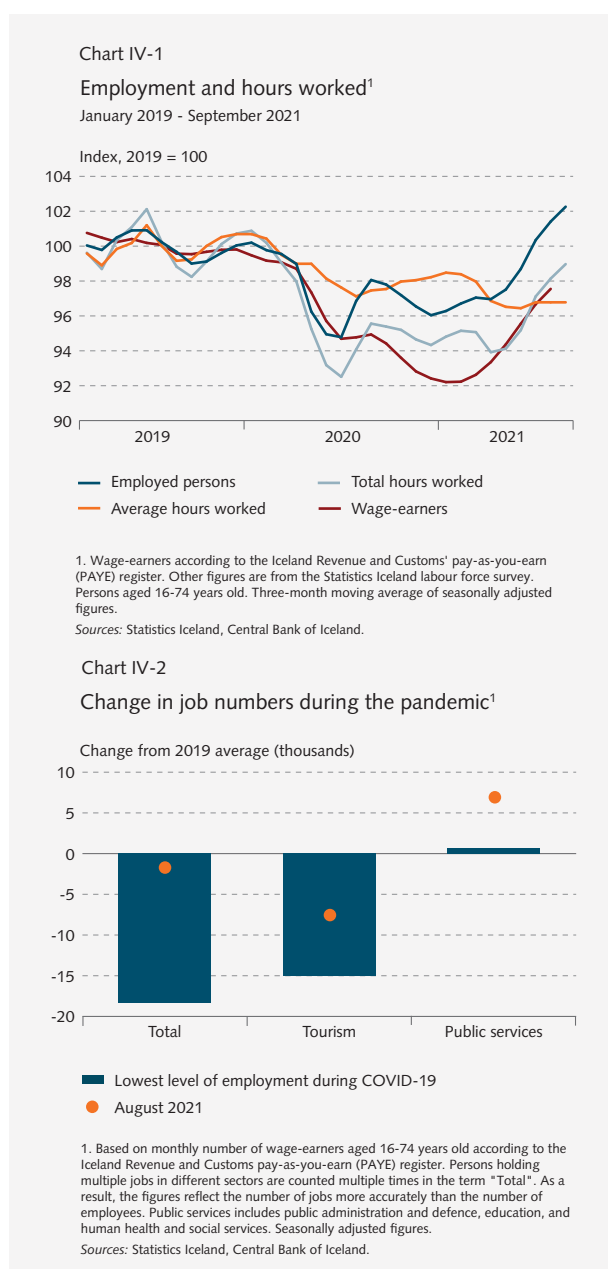
Jobs numbers rise swiftly, but average hours worked have fallen

According to the Statistics Iceland labour force survey (LFS), total hours worked increased by 3.5% year-on-year in Q3/2021, as the number of employed persons rose 4.3%, while the average work week was shorter by 0.8% (Chart 3 in Appendix 1). The number of employed persons has increased sharply since the beginning of 2021 and, in Q3, was a full 2% above the year-2019 average (Chart IV-1). Offsetting this is a more than 3% shorter work week. The shortening of the work week provided for in current wage agreements is estimated to account for nearly half of the change, according to estimates from Statistics Iceland of the impact the measure has had on the wage index. As a result, the rise in total hours worked has not kept pace with job growth, and in Q3/2021 total hours were 1% fewer than in 2019. However, total hours are somewhat greater than in 2019 once they are adjusted for Statistics Iceland's estimate of the effects of the contractual shortening of the work week.

The number of wage earners has also risen rapidly in 2021 to date. Data from the pay-as-you-earn (PAYE) register indicate that some 18,000 jobs were lost during the pandemic, but that around 16,700 jobs had been created by August 2021. Most of these jobs were in tourism, and the sector has reclaimed about half of those lost during the pandemic. Furthermore, in sectors that mainly reflect public services, there were nearly 7,000 more jobs than in 2019 (Chart IV-2).

Unemployment approaches its pre-pandemic level

Seasonally adjusted LFS findings show that the labour participation rate was slightly higher in Q3/2021 than



in 2019, after rising for three consecutive quarters. The employment rate rose considerably more, although it was still nearly 1 percentage point below its 2019 level (Chart 3 in Appendix 1). The unemployment rate therefore declined by about 2 percentage points quarter-on-quarter in Q3, measuring 4.6%. For comparison, it measured nearly 4% in 2019. According to the LFS, labour market slack also shrank during the quarter, albeit less than unemployment did.

The difference between LFS-based unemployment and registered unemployment has continued to narrow. Adjusted for seasonality, the latter measured 5.1% in October and was nearly ½ a percentage point higher than in February 2020. Long-term unemployment has also fallen rapidly, but it is still relatively high in historical terms.

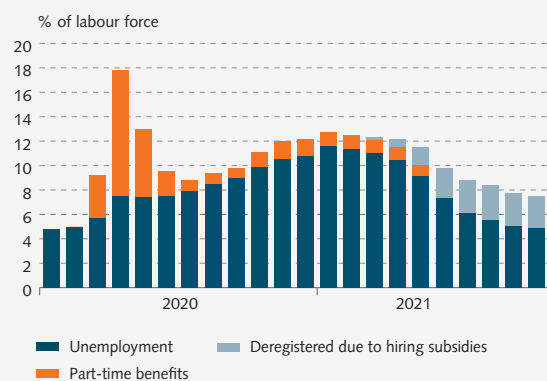
Government measures provide considerable support to the labour market

The recovery of the labour market has been supported in part by Government measures, particularly this past summer, when over 2,600 jobs were offered to students and a number of people benefited from hiring subsidies. It is estimated that if deregistration in connection with hiring subsidies is included, registered unemployment would have been roughly 2½ percentage points higher in October (Chart IV-3). This is probably the peak impact of the subsidies, however, as some of these workers would presumably have found jobs even without them. The level of Government support also declines as unemployment falls because the special job creation initiative will automatically expire when unemployment nationwide or in a given region falls to 6% or less. The initiative provides greater financial support and imposes more lenient requirements than conventional hiring subsidies do. In October, only the Suðurnes peninsula was above the 6% limit, whereas the capital area, where most job-seekers are located, fell below it last September.

Firms' recruitment plans reflect strong demand

Firms' recruitment plans turned sharply upwards in Q2 and remained strong in Q3. According to Statistics Iceland's corporate survey, there were nearly 8,400 job vacancies in Q3 – about 5,400 more than in Q3/2020 and over 3,700 more than in Q3/2019 (Chart IV-4). Furthermore, according to the seasonally adjusted results of the Gallup survey carried out this autumn among Iceland's 400 largest firms, the balance of opinion on staffing plans (i.e., firms planning to recruit net of those planning redundancies) was positive by 28 percentage points. Both surveys therefore indicate that job numbers

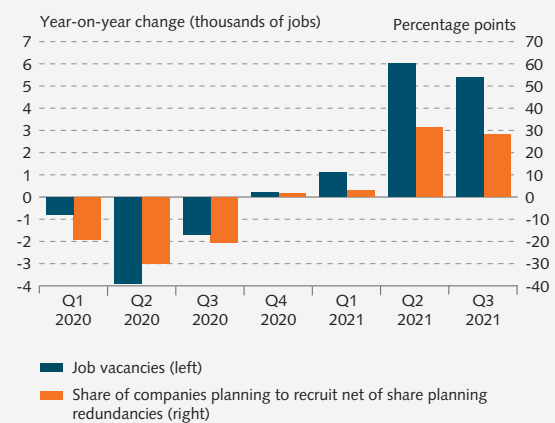
Chart IV-3
Registered unemployment¹
January 2020 - October 2021



1. "Deregistered due to hiring subsidies" is an estimate based on the number of approved subsidies and other information from the Directorate of Labour. Because applicants may submit their forms at the end of the application period, older figures may be revised.

Sources: Directorate of Labour, Central Bank of Iceland.

Chart IV-4
Firms' staffing plans¹
Q1/2020 - Q3/2021



1. Job vacancies according to Statistics Iceland company survey. Firms' recruiting plans in the coming 6 months according to Gallup survey of Iceland's 400 largest companies. The data are seasonally adjusted by the Central Bank of Iceland.

Sources: Gallup, Statistics Iceland, Central Bank of Iceland.

will continue rising in the coming term. It is uncertain, however, to what extent businesses' appetite for recruitment reflects hiring subsidies rather than an actual recovery of labour demand.

Labour importation on the rise

Iceland's population grew by 1.9% year-on-year in Q3, considerably more than in Q2 (Chart IV-5). The uptick in population growth is due mostly to immigration. It appears that importation of foreign workers will continue in tandem with the recovery of the domestic economy, owing to the large number of job vacancies that have not yet been filled.

Employment outlook ambiguous in the near term but set to improve over time

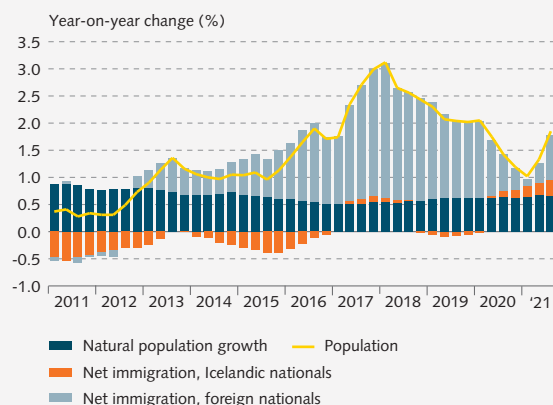
A large number of hiring subsidies will expire in Q4/2021, creating uncertainty about the short-term unemployment outlook. It is unclear how many subsidised employment relationships will remain intact thereafter, although the uncertainty is offset somewhat by firms' strong desire to add on staff and the overall shortage of workers. That said, the decline in unemployment could slow down or even reverse temporarily if a large number of people re-apply for unemployment benefits, as it can take some time to match job-seekers to vacancies. In the long run, however, the unemployment outlook is more favourable than in the Bank's August forecast. This is due to two factors: activity in the domestic economy has picked up more than was projected then, and estimates of the equilibrium unemployment rate have been updated. The baseline forecast assumes that job creation will continue and that LFS-based unemployment will measure 6% this year, falling to around 4% towards the end of the forecast horizon (Chart IV-6). Registered unemployment is estimated to be higher this year, at nearly 8%, but is also expected to fall to 4% by the end of the forecast horizon.

Indicators of factor utilisation

Labour productivity picks up again

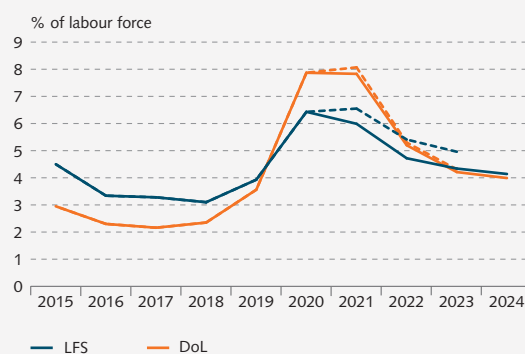
Labour productivity declined markedly in 2020. In terms of GDP per total hours worked according to the LFS, it fell by 1.7% year-on-year. Another measure published by Statistics Iceland, this one based on total hours worked according to the national accounts, showed a year-on-year increase of nearly 1%, however. In both instances, productivity growth declined by roughly the same amount between years, just over 3 percentage points. The latter measure indicates that because of dif-

Chart IV-5
Population
Q1/2011-Q3/2021



Source: Statistics Iceland.

Chart IV-6
Unemployment 2015-2024¹



1. Unemployment according to Statistics Iceland labour force survey (LFS) and registered unemployment, excluding part-time benefits, according to the Directorate of Labour (DoL). Central Bank baseline forecast 2021-2024. The broken lines show the forecast from MB 2021/3.

Sources: Directorate of Labour, Statistics Iceland, Central Bank of Iceland.

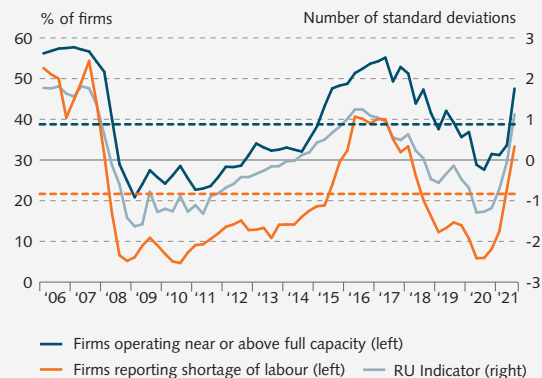
ferences in composition, labour productivity fell less in 2020 than it would have otherwise, as low-productivity sectors fared particularly poorly during the pandemic. To some extent, this reverses in 2021, but labour productivity is nevertheless expected to recover.

Output gap expected to turn positive in mid-2022

According to the seasonally adjusted results of Gallup's autumn survey of Iceland's 400 largest firms, a third of executives considered themselves short-staffed, and nearly half reported that their firm would have difficulty responding to an unexpected increase in demand (Chart IV-7). Both of these ratios are well above their historical average, and they are unusually high given the number of people on the unemployment register. Furthermore, the resource utilisation (RU) indicator, which combines various indicators of factor utilisation, rose steeply in Q3 and is now above its historical average for the first time since mid-2018.

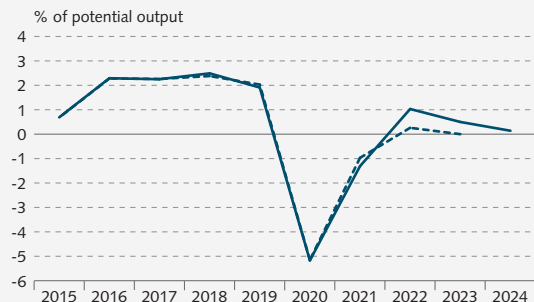
It therefore appears that the slack in output is narrowing quickly and may even have closed already. On the other hand, revised national accounts figures indicate that, for much of this year, the output slack was slightly larger than previously estimated. There is also considerable uncertainty about potential output, which could be overestimated, given the severe disruptions in production currently affecting the global economy. As a result, it is extremely difficult to estimate how much slack remains in the domestic economy or whether a positive output gap has already opened up. According to the Bank's baseline forecast, some slack still remains, but it is expected to disappear in H2/2022 and a positive output gap to open up thereafter, peaking in early 2023. Owing to stronger GDP growth in 2022, the output gap will be somewhat wider than was assumed in the August forecast (Chart IV-8).

Chart IV-7
Capacity utilisation¹
Q1/2006 - Q3/2021



1. Indicators of capacity utilisation are based on the Gallup Sentiment Survey conducted among Iceland's 400 largest companies. The resource utilisation indicator (RU indicator) is the first principal component of selected indicators of capacity utilisation; it is scaled so that its mean value is 0 and the standard deviation is 1. A more detailed description can be found in Box 3 in MB 2018/2. Seasonally adjusted figures. Broken lines show period averages.
Sources: Gallup, Central Bank of Iceland.

Chart IV-8
Output gap 2015-2024¹



1. Central Bank baseline forecast 2021-2024. The broken line shows the forecast from MB 2021/3.
Sources: Statistics Iceland, Central Bank of Iceland.