3 July 2025

Research Euro Area

Strong labour market amid cooling demand

- **The euro area labour market remains robust, while signs of cooling are evident. Amid record-low unemployment rates, recent survey data indicates moderating employment growth, and we expect aggregate employment growth to slow this year and the unemployment rate to decline marginally.**

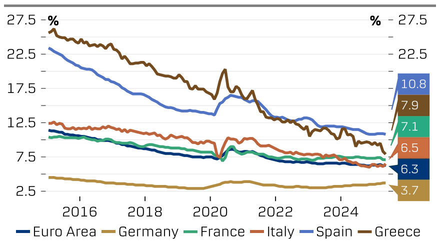
The labour market has shown remarkable resilience amidst slow economic growth and higher interest rates since 2022. By May 2025, the unemployment rate declined to 6.3% from 6.8% in May 2022 and employment continued to rise by 0.2% q/q in 2025Q1. However, employment growth is slowing compared to recent years and both Germany and France recorded job losses in the first quarter. The European Commission expects job losses in France and Germany to continue in 2025, with -0.2% y/y growth in both countries, while strong employment growth is expected to continue in Spain at 2.1% y/y. **We thus expect the convergence in unemployment rates between Southern and Central Europe to continue.**

Yet, labour demand is cooling. The job vacancy rate has declined from 2.9% in Q1 2024 to 2.4% in Q1 2025. The services sector vacancy rate is 2.7%, with the industrial sector weaker at 2.1%. Business surveys also show a reduction in firms citing labour as a production constraint. In April 2025, service-sector constraints fell to 22.9% from 34.1% in April 2024, while industrial constraints dropped to 18.2%, which showcases the relatively weaker labour demand in the industry. Finally, the EC's Employment Expectations Indicator (EEI) have remained below long-term average since 2024, indicating cautious hiring. However, actual employment data has been better, defying these signals**. Overall, the euro area labour market thus continues to show resilience, amid a gradual normalization of labour demand, which we expect to lead to an increase in employment of 0.5% y/y in 2025 and 2026, and a marginally lower unemployment rate over the coming 12 months.** Upside risks to the outlook includes the German fiscal package and defence spending, which increases hoarding motives. On the other hand, trade uncertainty and the declining profit share of firms, which now stands at the lowest level in 25 years when excluding the COVID period, are downside risks to the outlook.

Despite the strong labour market, wage growth is declining. The ECB wage tracker points to a reduction in negotiated wage growth to 3.1% y/y in Q4 2025 from 4.7% y/y in Q4 2024, and by Q1 2025, compensation per employee grew only 3.8% y/y. Wage growth is strongest in construction and services, while the industrial sector shows moderation. Easing labour cost pressures bolster ECB's disinflation efforts, but the tight labour market present upside risks to wage growth in the coming years.

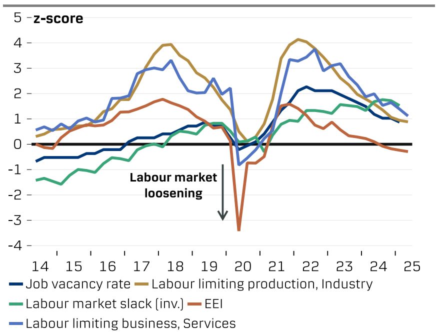
Finally, demographics will keep the unemployment rate low in coming years despite cooling employment growth as the labour force is expected to grow less than employment. Between 2022 and 2024, the working-age population grew around 0.4% annually which was largely driven by foreign labour compensating for the decline in the domestic working population that is especially pronounced in Germany.

Unemployment rates historically low



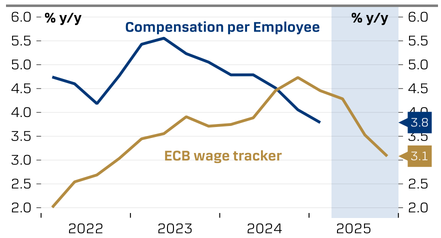
Source: European Commission, Eurostat, Macrobond

Labour market indicators cooling but are still strong



Source: European Commission, Eurostat, Macrobond

Wage growth declines from 2023 peak



Source: ECB, Macrobond

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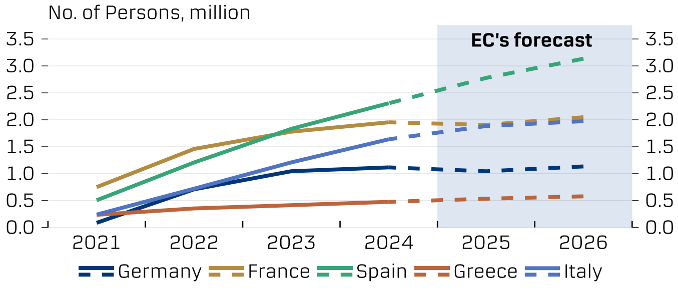
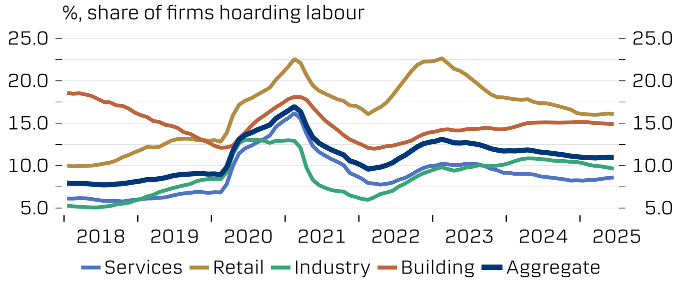
Appendix: Chart pack

Change in employment since 2020 across countries in euro area



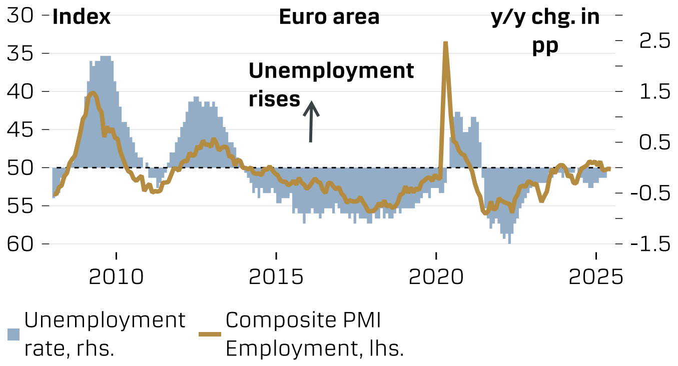
Source: European Commission, Macrobond

Labour hoarding remains above pre-pandemic levels



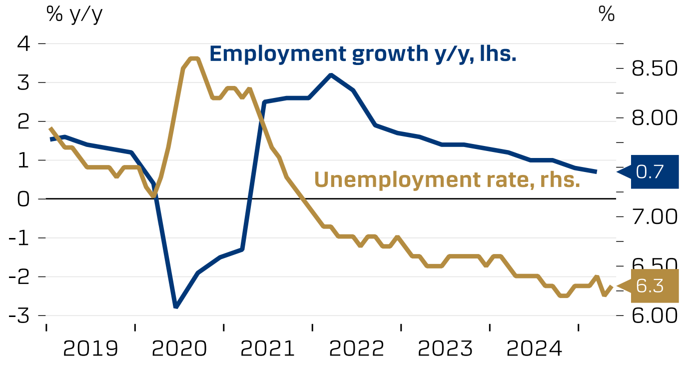
Note: The Indicator measures the percentage of managers who anticipate a decrease in their firm's output while maintaining or increasing employment.
Source: European Commission, Macrobond

PMI points to unchanged unemployment



Source: European Commission, Eurostat, Macrobond

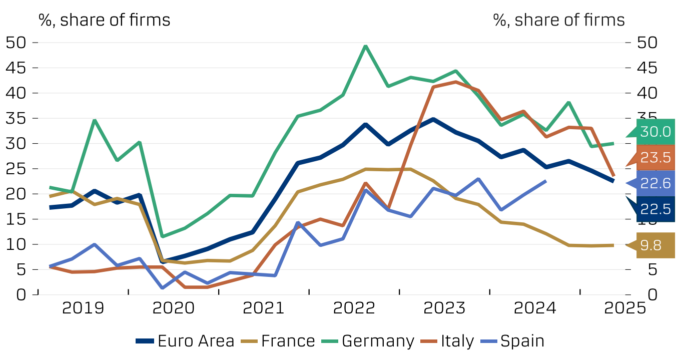
Unemployment at multi-year lows, but employment growth is slowing



Source: Eurostat, Macrobond

Service sector labour shortages remain elevated in Germany and Italy

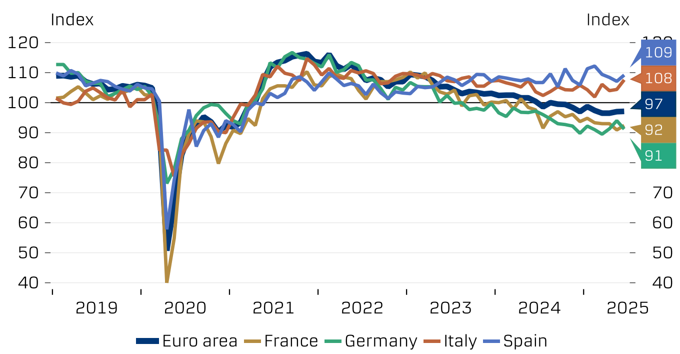
Factors limiting the business: shortage of labour (services)



Source: European Commission, Macrobond

Euro area employment expectations below long-term average

Employment expectations indicator



Source: European Commission, Macrobond

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None

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