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Labour markets at a crossroads: softening trends amid elevated uncertainty

Key takeaways

- *Labour market conditions in emerging market economies remain broadly stable, but unemployment in several advanced economies is edging up, and forward-looking indicators point to further weakening.*
- *Cyclical forces partly explain these developments, but longer-term structural forces are also at play, including deregulation and demographic pressures (ageing, migration, participation of older workers).*
- *Weaker labour markets may weigh on output, especially in the absence of productivity gains. In some emerging market economies, tighter conditions and stronger wage-price pass-through could raise the risk of de-anchoring inflation expectations.*

Introduction

After a prolonged period of tightness following the Covid-19 pandemic, labour markets in advanced economies (AEs) have come back into balance and show some signs of further cooling. Unemployment rates have edged up in many jurisdictions: hiring has slowed, (unfilled) vacancies are declining and standard measures of demand-supply imbalances have reverted to pre-pandemic levels. While this partly reflects normalisation, forward-looking labour market indicators indicate signs of further weakening in some countries. These developments contrast with emerging market economies (EMEs), where labour market conditions have remained broadly stable, albeit with some differences across economies.

This Bulletin reviews some of the recent trends in labour markets. After analysing cyclical factors, it delves into the structural drivers affecting supply and demand for labour. Finally, it explores implications for wage and price dynamics and for monetary policy.

Taking stock of recent trends

Unemployment rates remain low by historical standards in most jurisdictions (Graph 1.A), but trends are starting to diverge. In many AEs, the past two years have seen a broad increase in unemployment rates – by around 1 percentage point for the median jurisdiction – reflecting a gradual cooling of previously overheated labour markets (Graph 1.B). At the same time, cross-country dispersion has widened. Some economies are still near record low levels of unemployment, while unemployment has moved off its lows in others.[1] By contrast, unemployment in EMEs has remained stable on average, despite large heterogeneity.[2]

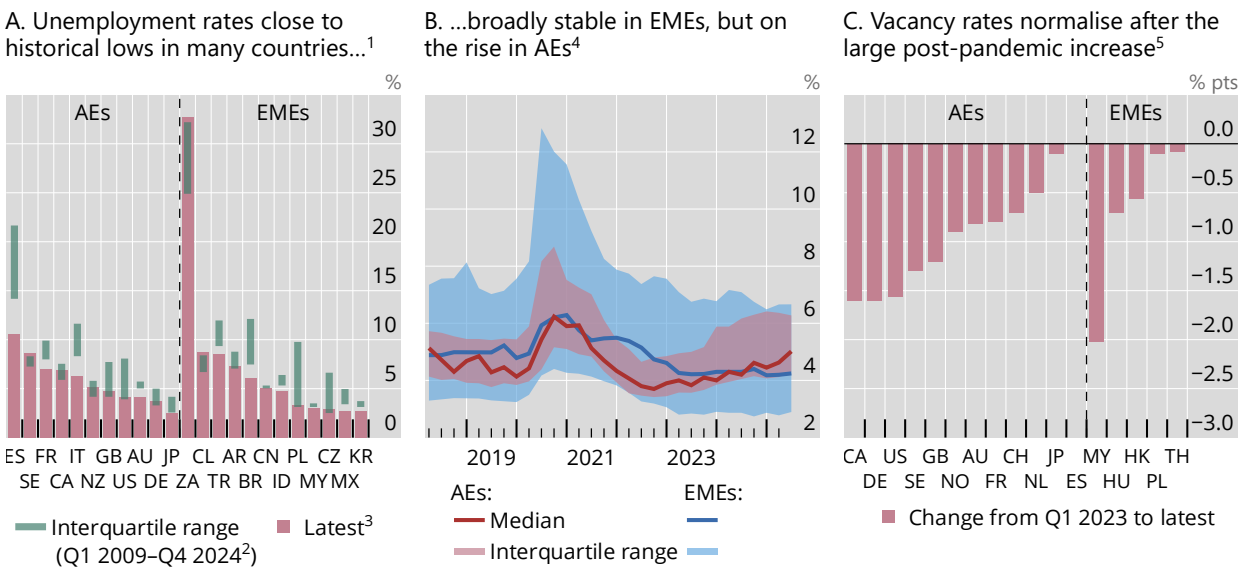
Moreover, sectoral drivers of employment growth also differ across AEs and EMEs. In many AEs, non-market services (such as education and healthcare) have been the main contributor. In contrast, in several EMEs (and some AEs) market services have been the dominant force (Graph A.2 in online Annex A). Finally,

[1] For instance, in Canada manufacturing, retail trade and accommodation and food services, which together account for about 26% of total employment, have recorded negative annual employment growth since March.

[2] Alternative measures of unemployment, like youth unemployment or underemployment, provide consistent signals. The former is now within historical ranges in several jurisdictions (Graph A.1.A in online Annex A), while the latter points to softening in the United States, unlike in the euro area, where it remains on a decreasing trend (Graph A.1.B in online Annex A).

Unemployment rates still low but on the rise in AEs

Graph 1



[1] Definitions differ among economies; seasonally adjusted series. Except for ID (semiannual). [2] For CN, Q1 2017–Q4 2024. [3] Q2 2025 except for: AR (Q1 2025); ID (H1 2025). [4] Data across 11 AEs and 25 EMEs. [5] Job vacancy rate computed as ((number of job vacancies) / (number of occupied posts + number of job vacancies))*100. For GB, job vacancy ratio computed as three-month rolling average ratio of vacancies per 100 employee jobs; for JP, new job openings. Varying national definitions, seasonally adjusted data. Latest = Q2 2025, except for CA, CH, ES, HK, HU, NO, PL and SE (Q1 2025), and MY and TH (Q4 2024).

Sources: International Labour Organization; OECD; LSEG Datastream; national data; BIS.

some EMEs, especially some Latin American economies and Türkiye, have achieved progress in reducing informal employment (Graph A.3 in online Annex A).

Job vacancy rates have declined markedly across both AEs and EMEs, signalling a broad-based slowdown in labour demand (Graph 1.C). In the United States, unfilled vacancies are now roughly on par with the number of unemployed workers – a normalisation after an extended period in which the vacancy to unemployment ratio was well above one. Moreover, developments in the US and UK Beveridge curves suggest that the phase of falling vacancy rates alongside stable unemployment is nearing its end. The latest data points align closely with the historical pattern, where lower vacancy rates are associated with higher unemployment rates (Graph A.4 in online Annex A).

Labour market flows point to further softening in some jurisdictions.[3] Since early 2023, several economies have shown rising separation rates and falling matching rates (upper left-hand quadrant in Graph 2.A). This includes Sweden, where unemployment has been rising, but also the United States, the United Kingdom and Switzerland, where unemployment has so far increased only marginally.

Additional insights, beyond matches and separations, come from the unemployment rate derived from the whole set of labour market flows.[4] During the post-pandemic recovery, this flow-based measure systematically undershot the actual (stock-based) unemployment rate, producing a negative flow/stock

[3] In contrast to conventional labour market indicators – such as unemployment, labour force and working age population – which adjust slowly and with significant lags, labour market flows between employment, unemployment and inactivity offer a complementary perspective on underlying labour market conditions.

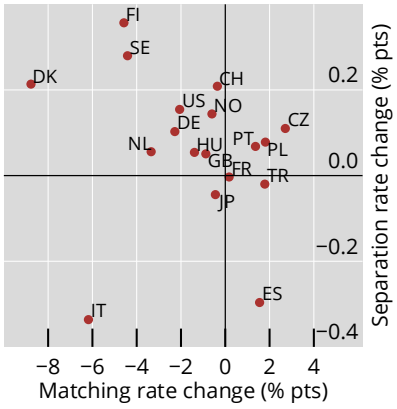
[4] This unemployment rate is the conditional steady-state unemployment rate implied by the matrix of labour market transitions between employment, unemployment and inactivity. It captures the direction of labour market dynamics. See Kharroubi and Koechlin (2025) for details.

unemployment gap (Graph 2.B).[5] This reflected strong labour market momentum, with flows signalling further reductions in unemployment down the road. Yet in several economies this gap has recently turned positive, implying that labour market flows have deteriorated more quickly than the modest rise in the observed unemployment rate would suggest. Indeed, the flow-stock unemployment gap has been a leading indicator of labour market conditions (Graph 2.C). Historically, a 1 percentage point increase in flow-based relative to actual unemployment tends to be followed by a similar rise in actual unemployment within the next year, suggesting that labour markets could further weaken, although to a limited degree, in the foreseeable future.

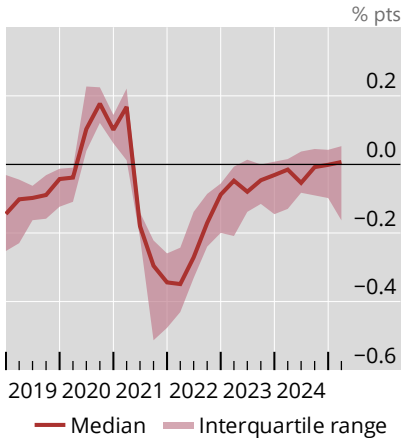
Labour market flows point towards additional labour market loosening

Graph 2

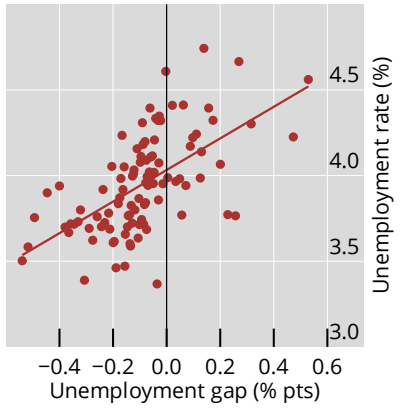
A. Rising separation and falling matching rates suggest loosening ahead[1]



B. Flow/stock unemployment gaps turning positive in several countries[2]



C. Current gap helps predict unemployment one year ahead[3]



[1] Dots show the change in the matching and separation rates between Q1 2023 and Q1 2025. The matching (separation) rate is the probability to switch from unemployment to employment (from employment to unemployment), averaged over the last four quarters. [2] The flow/stock unemployment gap is computed as the difference between the flow-based and actual unemployment rates. [3] Based on cross-country fixed effect panel regression, where the one-year-ahead unemployment rate is regressed on the current flow/stock unemployment gap and current unemployment rate.

Sources: OECD; national data; BIS.

Survey-based indicators of hiring and firing intentions (the so-called "soft data") also point to a cooling of the labour market in several key jurisdictions. In most AEs, firms expecting to cut employment in the near future have outnumbered those expecting to expand (Graph A.6.A in online Annex A). By contrast, in EMEs, except for Turkey and India, firms have grown more optimistic about employment prospects over the last year. Moreover, in addition to being somewhat noisy, soft data typically feed into hard data with a lag. In the United States, for example, shifts in firms' expectations about future employment growth start being reflected in actual private sector employment only after about 10 months, with the impact persisting for up to two years (Graph A.6.B in online Annex A). This suggests that the ongoing deterioration in several jurisdictions has yet to be fully reflected in the hard data (Bańbura et al (2023)). Indeed, while firms' expectations can shift rapidly – especially in periods of heightened uncertainty – actual hiring and firing decisions are typically much more gradual, partly reflecting adjustment costs.[6]

[5] Note that these unemployment measures, expressed as ratios of working age population, also depend on labour force participation. That said, labour force participation has changed little over the last two years (Graph A.5 in online Annex A), implying a limited contribution to changes in the unemployment gap.

[6] The delay in actual employment decisions may also be related to the risk of having to rehire dismissed workers if conditions improve. Such labour hoarding has weighed on productivity in several European economies in the post-pandemic period

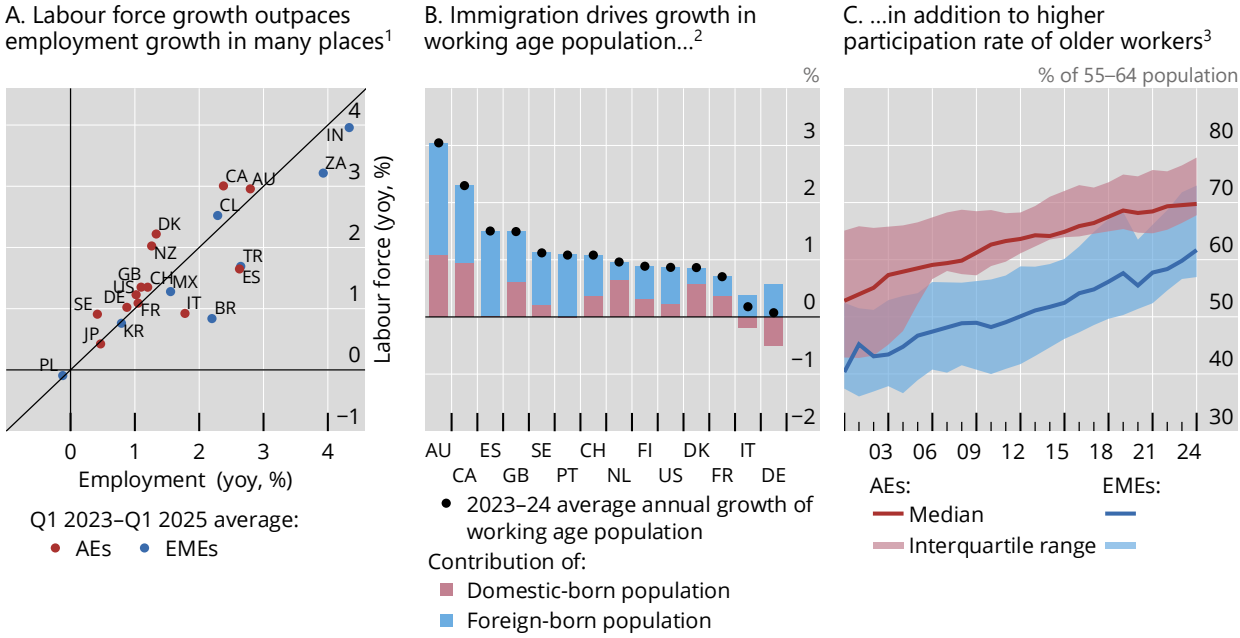
Structural forces continue to shape labour market dynamics

Beyond cyclical factors, structural forces continue to influence labour market outcomes, driving long-term trends but also weighing on short-term developments. Three structural trends seem particularly relevant at the current juncture.

The first is the broad trend towards deregulation. While laws governing labour markets differ widely across jurisdictions, many countries have moved to ease regulations (Graph A.8.A in online Annex A). This multifaceted deregulation policy, including measures such as cutting hiring and firing costs, decentralising wage bargaining and reducing unemployment benefits, has contributed to a fall in structural unemployment, ie the rate that is consistent with stable wage or price inflation (Graph A.8.B in online Annex A). Flexible labour markets and low structural unemployment matter for labour market dynamics, as they shape actual unemployment outcomes (Graph A.8.C in online Annex A).

Ageing pressures labour supply, amid rising immigration and participation of older workers[1]

Graph 3



[1] Based on quarterly seasonally adjusted data. [2] For CA, only 2023 growth rate. [3] Labour force participation rate of the 55–64 age cohort. Based on data for 13 AEs and 12 EMEs.

Sources: International Labour Organization; LSEG Datastream; national data; BIS.

The second trend relates to changes in labour supply. In several AEs, the labour force has expanded on par with, or at a faster pace than, employment (Graph 3.A). This has been the case even in countries where job creation proved strong, such as Australia and Canada.

Two important forces have supported growth of the labour force. The first is immigration (Graph 3.B). In many AEs, despite accounting for a relatively small fraction of the overall working age population, immigrants have contributed significantly – about 70% on average – to working age population growth (OECD (2024); IMF (2024)). This additional labour supply has eased shortages in key sectors such as healthcare, construction, logistics and personal services, containing cost pressures while supporting continued output growth.[7] The second is higher participation among older workers (aged 55–64), which

(Graph A.7 in online Annex A; Berson et al (2024)). This behaviour could lead to a stronger employment adjustment if firms perceive shocks as permanent rather than temporary.

[7] Immigration also affects wages and employment of native workers. While the impact can be positive in the long run, it is often negative in the short run, especially when the population inflow is large and unexpected. See Edo (2019).

has been on a rising trend (Graph 3.C), partly reflecting pension and retirement age reforms (Staubli and Zweimüller (2013)). Without this increase, overall labour force participation would have been considerably lower (Graph A.9.B in online Annex A).

However, demographic pressures are set to intensify (Graph A.9.A in online Annex A). The United Nations projects significant declines in the growth of the working age population worldwide by 2030 (Graph A.9.C in online Annex A).[8] In addition, the recent tightening of immigration policy across many AEs is likely to put further downward pressure on labour supply in these jurisdictions.

The third structural trend shaping labour markets is also the most uncertain and speculative: the rapid diffusion of new technologies. Advances in information and communication technologies and robotics have already transformed production processes in many sectors, with early-stage adoption often supporting job creation. Generative artificial intelligence (gen AI) adds a new layer, with estimates of potential productivity gains ranging from 10 to 55% across various occupations, although these remain subject to considerable uncertainty (see online Annex C for more details). Yet the employment impact could go both ways: gen AI can complement jobs by boosting productivity, particularly in IT and product development, or substitute them by automating routine tasks in clerical, administrative and operational roles. While no broad-based job losses have been observed so far, effects vary across sectors and depend on each country's level of digitalisation, AI capital and labour market policies.

Implications for monetary policy

While the current softening of labour markets has largely reflected normalisation, further weakening could weigh on growth. A notable feature in labour markets during the disinflation period has been the dominant contribution of employment to output growth. Except for the United States, Switzerland and Sweden, employment (as opposed to output per worker) has accounted for more than 90% of additional output in AEs over the past two years (Graph A.7.A in online Annex A). Hence, a loss of momentum in labour markets would probably have significant effects on output, especially in a scenario where labour productivity remained depressed.

Turning to wages, the decline in inflation rates over the past two years has supported a recovery in real compensation across many countries. Nominal wage growth is now outpacing inflation in most economies (Graph 4.A). Yet in many cases, real wage growth reflects a catch-up effect (Graph A.11 in online Annex A) – with nominal wages partly making up for past losses – rather than a genuine increase driven by strong productivity gains or labour market tightness. In turn, unit labour cost (ULC) growth has been slowing in most countries (Graph 4.B).

Risks of wages pressuring inflation thus appear limited in most AEs.[9] Not only are wage pressures expected to keep subsiding in line with labour market softening, but the pass-through from ULC increases to core inflation, despite some recent pickup, is still modest in AEs at around 20% (Graph 4.C). Therefore, even if wages were to retain some momentum, chances of a wage-driven inflation burst do not appear significant.

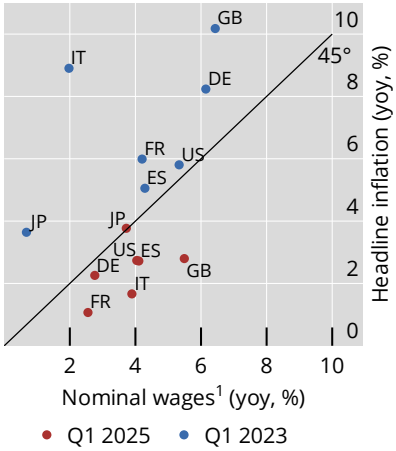
Higher trade tariffs and related adverse supply side developments, as well as fiscal deficits, are probably more important at this juncture. These factors are likely to push core goods inflation upwards in some countries, possibly reverberating on headline inflation and expectations (D'Acunto et al (2025)). They may further delay the convergence of inflation to targets in some jurisdictions and leave central banks in the difficult position of balancing looser labour markets against stronger price pressures.

[8] Beyond labour supply, ageing also influences labour demand and aggregate productivity. Older cohorts tend to consume relatively more services and fewer goods. In line with this, employment in sectors such as health services, where productivity is typically lower than other sectors, has grown faster than total employment (Graph A.10 in online Annex A).

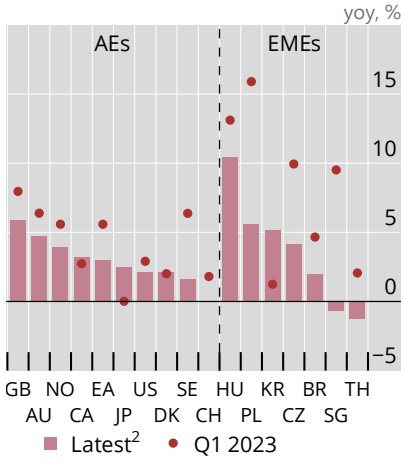
[9] Australia, Norway and the United Kingdom, where ULCs are still growing at 4% a year or more, are exceptions. Yet ULC growth is expected to continue decelerating in these jurisdictions.

Wage and cost pressures persist amid signs of labour market softening Graph 4

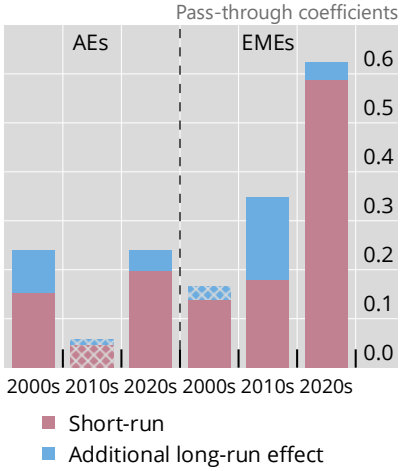
A. Nominal wage growth now outpaces inflation



B. Unit labour cost growth falls but remains elevated in several places



C. The pass-through from ULC to prices has increased[3]



[1] Definitions and sectoral coverage differ among economies. [2] Q1 2025, except for GB, KR and NO (Q4 2024). [3] Unit labour cost variation of pass-through to core inflation. Based on panel estimation of equation with core inflation as a function of lagged core inflation, domestic unit labour cost changes and country fixed effects. Short-run refers to pass-through within four quarters. Long-run refers to final pass-through, after several years. Based on a panel of 33 countries. Shaded bars for coefficients that are not statistically significant at 10%.

Sources: OECD; LSEG Datastream; national data; BIS.

By contrast, in EMEs the pass-through from ULC to prices has risen significantly relative to the pre-Covid period (Graph 4.C), partly reflecting the increased importance of labour in firms' total production costs. Moreover, given recent overshoots of inflation targets, some EMEs may face a risk of de-anchoring inflation expectations should inflation fail to converge to target sufficiently fast. Importantly, in some economies labour markets remain tight, adding to the risk of wage-driven inflation. Monitoring labour market developments and ensuring that wage growth remains consistent with central banks' ability to deliver on inflation targets should therefore remain a top priority.

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