

# Chapter 11: The Middle Class in Spain

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In Spain—as in other European countries—public debates have recently focused on the increasing levels of inequality and the constricted middle class. Concerns about the economic and social effects of the increased inequalities and the reduction of the middle class have taken on particular relevance during the last few years, especially since the onset of the economic and financial crisis in 2008. A growing number of academic studies have tackled these particular issues.

This chapter addresses these growing concerns surrounding the decline in the middle-class share in Spain, from two different points of view: the income perspective (providing an overview of the evolution of the median income growth rates registered since the start of the crisis almost ten years ago) and the non-income perspective (analysing other sociological and cultural aspects, such as education and labour market developments).

## 1. The income perspective

Before the crisis, the EU as a whole experienced slow progress in average income levels. However, that was not the case for peripheral countries, which managed to register a notable growth in real income levels. This resulted in a rapid process of income convergence between the EU core countries and the peripheral countries, mainly the Eastern European countries and Spain, which was the only Mediterranean country registering notable growth in real income levels during the period 2004-2008 (Eurofound, 2017).

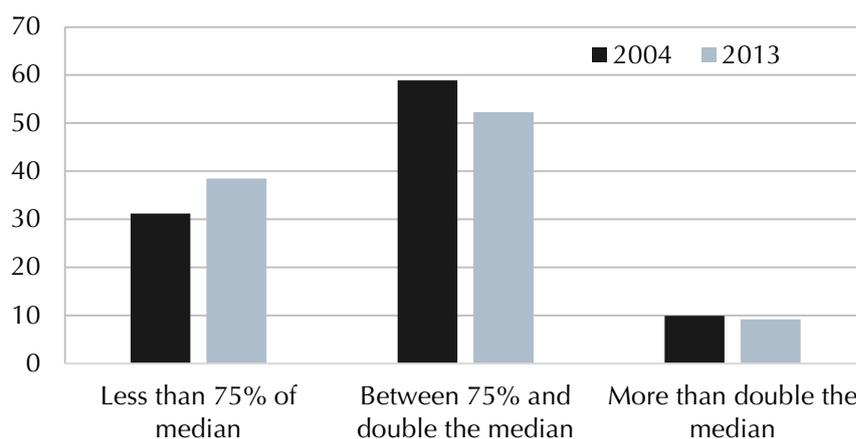
The crisis, however, marked a turning-point in the trends of income levels, which declined significantly from 2008 in most European countries (especially those in the periphery). Together with Ireland and Italy, Spain was one of the countries it hardest by the crisis. In particular, real household income levels in Spain decreased by more than 3% between 2007 and 2013. The lower income quintiles were especially worse-off, compared to their counterparts in the other countries.

Equivalisation, the process of accounting for household economies of scale, changes the pattern of real median income growth in Spain: over the 2007-2013 period it is close to 0. This could be interpreted as Spanish families staying together in households for a longer time, to absorb the shock to household income and employment. The stability in real household income then reflects a rational response to economic decline. On the other hand, the change in household size could also reflect a secular trend towards larger families, which coincides with a beneficial effect of

equivalisation. In any case, even after equivalisation the median equivalised net income in Spain remained one of the lowest in the set of countries in this book.

The income growth of the median household is a proxy for the income growth of the middle class. Among the other countries in this collection, the size of the middle class (56%) in Spain is among the smallest; see the overview in Chapter 2. Moreover, whereas in Ireland and Italy the middle class experienced a slight increase (Ireland) or remained constant (Italy) from the 1980s to 2013, the Spanish middle class contracted slightly in size.

The middle class declined particularly in the 2008-2013 period. Most of this decline is due to households now being designated as lower income. The increase in size of the bottom-income tier can also be observed in Figure 1. Following the crisis, the percentage of the population in the middle-income tier has diminished (since 2004, the Spanish middle class has declined by some 3.5 million people), while the population has clearly increased in the lower-income tier. Inequality has increased accordingly; see Figure 9 of the overview in Chapter 2.



**Figure 1: Household share per income class (2004 and 2013)**

Source: Fundación BBVA

In all, middle-class households, which were experiencing notable improvements before the crisis, are now moving backwards, feeling vulnerable and less confident in future opportunities (Fundación BBVA, 2016). Spain remains one of the economies with the highest levels of inequality among the countries considered in this study, due to the economic crisis and the ensuing loss of jobs (FAES Foundation, 2015 & 2016). These high inequalities suggest a worsening of the middle class and an increase in income polarisation.

As in other countries, social transfers have helped mitigate the increased income inequality in Spain during the crisis period; see Figure 9 in the overview chapter. However, as recent studies have found, the Spanish welfare system is relatively inefficient (compared to other European countries) in reducing inequalities (FAES

Foundation 2015 & 2016): the public spending components aiming to reduce inequality levels (education, for example) fail to achieve their purpose.

## 2. Non-income-related perspectives

### **The affordability of housing**

The crisis starting in 2008 led to difficulties in accessing housing in Spain. This was to a large extent a logical consequence of the incredibly high unemployment rates, the tightening of the mortgage conditions and the impossibility of selling one's own dwelling (Housing Europe, 2015). In this regard, recent studies point out that most Spaniards, from 2007 on, would only be able to access housing through tenancy. The policies launched by the government aiming to facilitate tenancies (such as the "Basic Emancipation Income", which consisted of a grant for young people who sign a tenancy contract) indicate the growing importance of tenancy in Spain (TENLAW, 2014).

Moreover, the 2017 Family Budget Survey conducted by the INE shows that middle-class households spend larger proportions of their budget (29.5% to 35.4%) on items related to dwelling, while this type of expenditure is clearly lower (26.6%) in households with greatest expenditure levels.

Furthermore, it is important to note that the strong bias towards homeownership is something that actually distorts inequality rates in Spain. In this regard, as some studies show (FAES Foundation, 2015), Spain is far from being one of the European economies with higher inequality levels when homeownership is taken into account; in that case, Spain is actually one of the EU countries registering relatively lower wealth inequality levels.

Finally, the indebtedness of the Spanish private sector has seen a significant reduction over the last few years. In particular, since 2010, when private indebtedness reached 216% of GDP (most of it coming from the mortgages that originated during the pre-crisis real estate boom), household indebtedness has fallen by 19 %-points of the GDP (Rallo, 2017). The rapid process of deleveraging of the last seven years has resulted in falling household consumption rates. This has obviously caused a loss of families' capacity to access housing, which was already hampered by the limited access to credit after the crisis.

### **Family stress**

Many scientific theories—such as the psychosocial stress theory (Nada Es Gratis, 2016)—hold that unemployment and economic difficulties generate situations of stress on individuals. Anxiety, depression, cardiovascular disease and pathologies are directly related to stress situations deriving from labour and financial problems (El País, 2010). In this regard, since the beginning of the crisis in 2008, Spain has seen a

notable increase in the number of persons suffering from anxiety and depression as a consequence of the weak economic environment (El País, 2009).

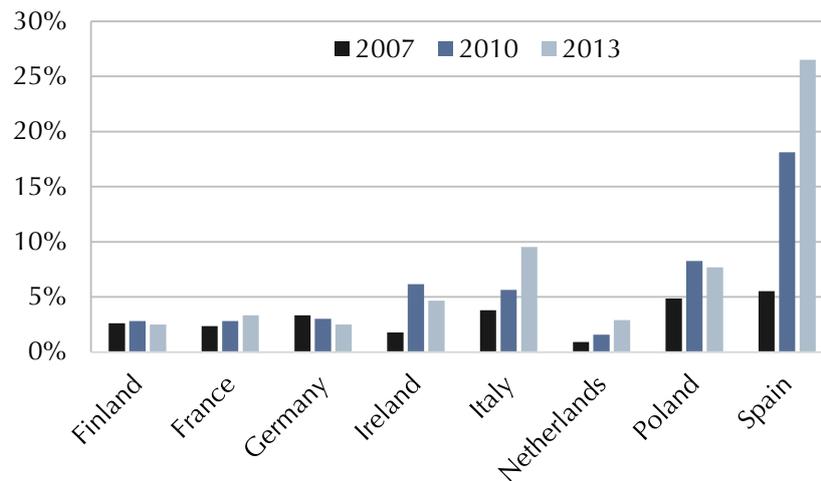
Moreover, the changes to the fiscal system introduced since the onset of the crisis have probably contributed to the increased anxiety and stress levels experienced by families. As experts maintain, the working (or middle) class has borne the brunt of the tax burden in Spain, thereby for many years providing for the sustainability of the social welfare system. Moreover, the middle-income class seems to suffer the most, and benefit the least, from the tax reforms adopted over the last few years. The reforms of 2014 reduced income tax rates, but mostly for the higher and lower incomes. As for the tax on capital, the general exemption applied on the first €1,500 of dividends, which was very important for the middle class, was eliminated in 2014 (El Economista, 2015; El País, 2014).

### **The labour market**

Spain has been one of the European countries affected the worst by the economic and financial crisis starting in 2008. As a result, unemployment rates increased greatly, as did job uncertainty and insecurity. The labour market situation has been one of the main determinants of the decline of the middle class in Spain.

During the period 2007-2013, the unemployment rate in Spain increased by around 18 %-points, reaching 26% of the active population in 2013—the highest unemployment rate in the countries in this collection; see Figure 5 of Chapter 2. The loss of employment opportunities, however, was felt particularly among young and low-skilled Spaniards. These are the type of employees that are also employed more often through partial and temporary labour contracts. This has led to a more pronounced decrease in their average income levels and a clear decline in their relative position in society.

In this regard, it is important to stress that the Spanish labour market is characterised by a strong duality between permanent and temporary workers (i.e., the typical insider-outsider problem). This has resulted in a pronounced volatility of the unemployment rate over the business cycle. The 2012 Labour Market Reform diminished the duality in the labour market to some extent (FEDEA, 2016), although the unemployment rate is still very high—at around 17% of the working population as of July 2017.



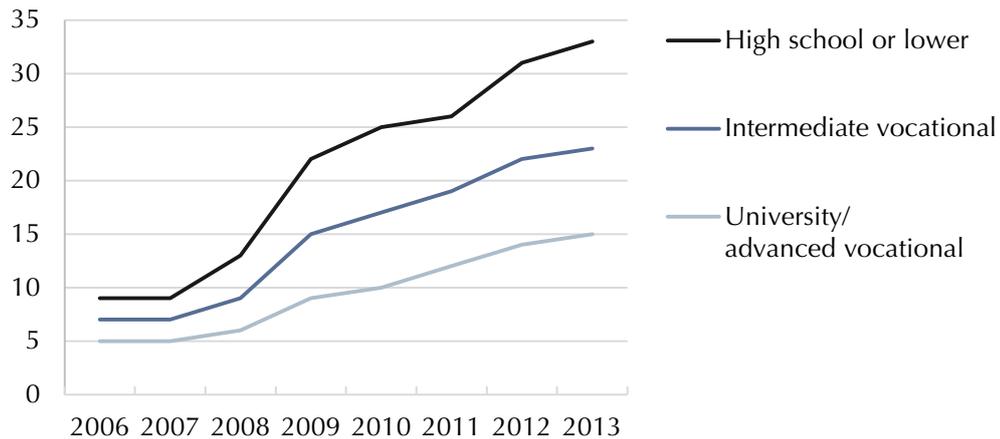
**Figure 2: Labour market insecurity over time**

Labour market insecurity is defined as the expected earnings loss associated with unemployment, a combination of unemployment risk, the expected duration of unemployment and the effective insurance against these losses through unemployment benefits. Source: OECD, Hijzen and Menyhert (2016).

In terms of labour market security, Spain also performed poorly during the crisis, compared to other EU countries; see Figure 2. It shows labour market insecurity defined as the expected earnings loss from unemployment for the countries in this book. From 2007 to 2013, the labour market insecurity rate worsened rapidly—from 5% to more than 25%. This rise in labour insecurity, which was mainly due to the increase in the risk of unemployment and its duration, particularly affected the most vulnerable groups, such as young people on temporary contracts and with low qualifications (Hijzen and Menyhert, 2016). Once again, young and low-skilled Spaniards were the most negatively affected.

### **Social mobility**

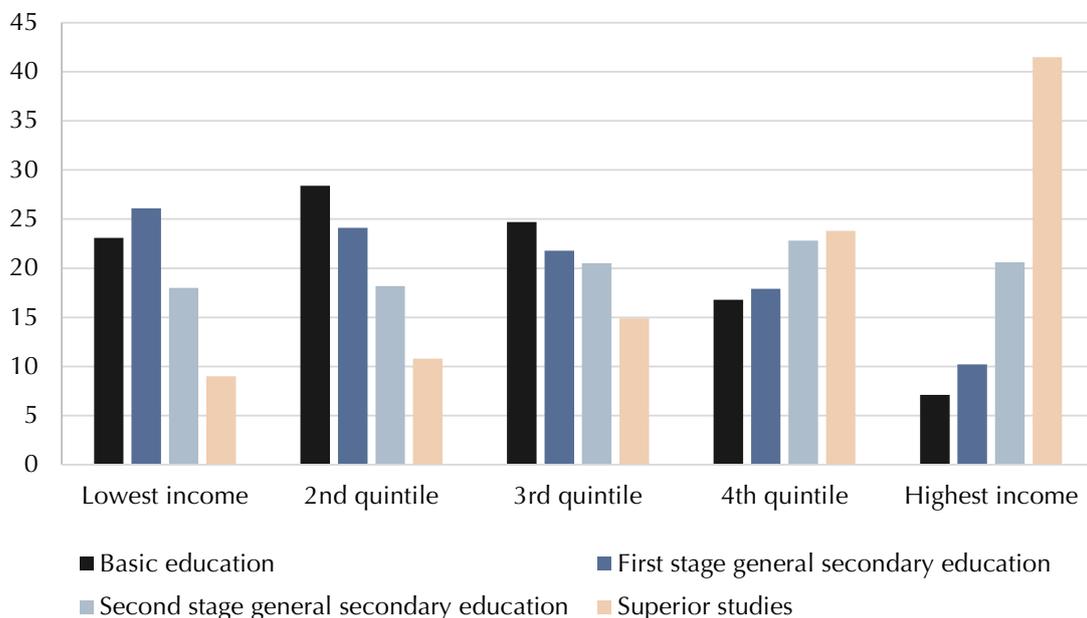
A good education system enables people to fully develop their knowledge and their personal and professional skills. Equal access to education and training systems therefore plays an important role in ensuring equal opportunities for everyone to find employment and succeed professionally. In that sense, Figure 3 shows that unemployment rates are higher among Spaniards who only have basic compulsory education, while for those who have completed secondary education and for university graduates the rates are clearly lower. Also, education plays a crucial role in people's opportunities of belonging to a wealthier income and social group; a good education is thus also correlated with higher wages. (FAES Foundation, 2015).



**Figure 3: Unemployment rates by education level in Spain**

Source: FAES Foundation (2015). The orange colour refers to University/advanced vocational training, black to intermediate vocational training/Baccalaureate, grey to high school or lower.

Figure 4 shows the population share per consumption unit. It shows that the 5<sup>th</sup> quintile of the consumption distribution is dominated by people with superior studies (that is, university studies or advanced vocational education), underscoring what an important factor education is in overcoming income differences across the Spanish population.



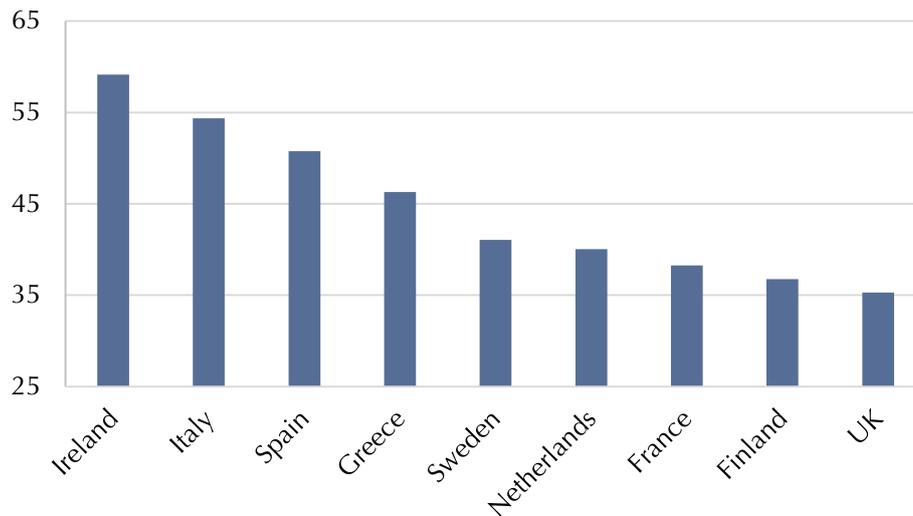
**Figure 4: Income distribution by education level—2017**

Source: Own calculations based on statistics from the INE.

In Spain, the education system is relatively ineffective in providing equal opportunities among all social- and income levels of society. To a large extent, this is due to the fact that educational success depends not only on the hard work and dedication of the young Spaniards, but also on the socio-economic and cultural status

of their parents. The number of children replicating their parents' educational level is relatively high in Spain, which means that intergenerational education mobility levels are low, compared to other EU countries; see Figure 5.

Furthermore, one of the structural defects in the Spanish educational system is the low proportion (compared to other EU countries) of young people with Intermediate Level Vocation Training studies. This accentuates the duality of the Spanish labour market and hampers the overall efficiency of the welfare system.



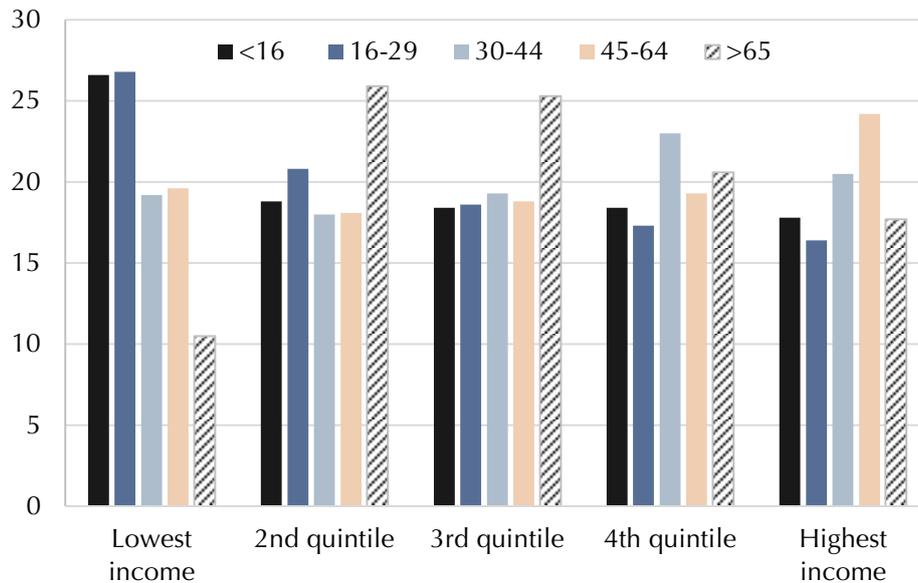
**Figure 5: Persistence in tertiary education for selected countries (2010)**

Persistence in education measured as the distance between the estimated probability (in %-points) to achieve tertiary education of an individual whose father had also achieved tertiary education and the probability to achieve tertiary education of an individual whose father had below upper secondary education. A larger number implies a larger gap, thus stronger persistence in tertiary education or a lower degree of education mobility across generations. The data shown is for the average persistence of men and women aged 35-44. Source: OECD (2010, Chapter 5).

Ultimately, these inefficiencies limit the scope of the potential positive outcomes of the education system and hinder its functioning as the 'social lift' that it should actually be. In fact, there seems to be a direct correlation between the size of the middle class and the efficiency of not only the education system, but also the welfare system as a whole (efficiency being measured as the capacity to reduce the Gini coefficient). The welfare systems of the Southern European countries (such as Spain or Italy) are characterised by their inefficiency in terms of redistributive capacity, compared to other EU countries (such as Sweden, Denmark or the United Kingdom; FAES Foundation, 2015).

### Generational issues

As shown in Figure 6, the middle-income tiers of society are mainly composed of households of people over 65 years of age, although younger people aged between 30 and 44 also represent an important part of the population in the 4<sup>th</sup> quintile. The lowest quintile has a specifically large share of young people (16 to 29 years old); the highest quintile has a large share of adults between 45 and 64.



**Figure 6: Distribution of age groups over income quintiles**

Source: own computations based on statistics from the Spanish National Statistical Institute (INE).

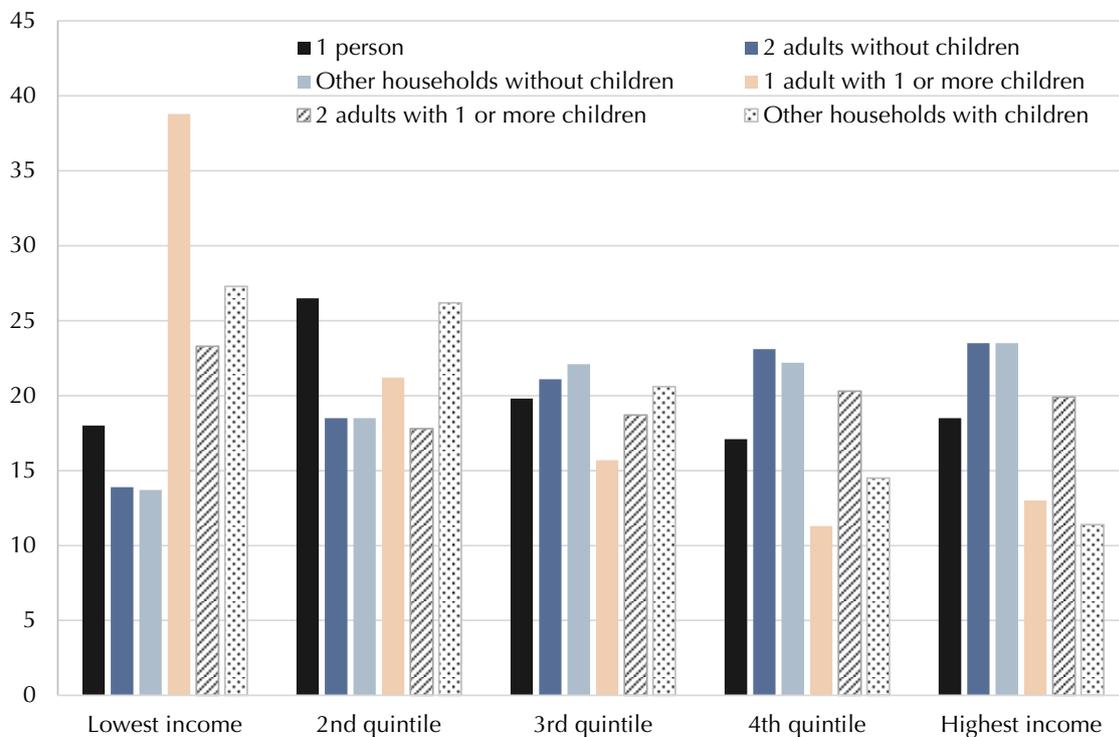
### Regional differences

According to data from the National Statistical Institute (INE), the median-income sectors of the Spanish society are concentrated in the autonomous regions of La Rioja, Comunitat Valenciana, Galicia, Cantabria, Navarra, Asturias and Aragón. The lower-income households tend to live in Andalucía, Extremadura, Murcia, Ceuta and Castilla-La Mancha. The upper-income families live in wealthier autonomous regions such as Madrid, País Vasco, Navarra and Cataluña. In this regard, it is important to note that the large differences in the living standards between the different Spanish regions make it difficult to accurately size the middle class. In other words, the median income levels vary significantly, depending on the region. In 2008, for example, the average income of Navarra was about 69% larger than that of Extremadura (Fundación FOESSA, 2014), which implies that belonging to the middle class differs greatly between regions (belonging to the middle class in Navarra is definitely not the same as belonging to the middle class in Extremadura). Ultimately, regional differences make it difficult to accurately measure the size of the middle class.

### Household composition

Figure 7 shows the composition of Spanish households, by income quintiles, according to household size. The INE calculates income quintiles by first ordering persons according to the income level per consumption unit. Subsequently, they divide these people into five groups, each group including 20% of the people. The first quintile corresponds to 20% of people with lower income levels, and the fifth quintile, to 20% of people with higher income levels per consumption unit. The 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> quintiles comprise the middle-income households.

This being so, household types seem to be evenly distributed over the income quintiles, except for households with a single adult and children. These households form a large share of households in the lowest quintile, while in the 4<sup>th</sup> and 5<sup>th</sup> quintiles they are far less important.



**Figure 7: Population by income quintile per consumption unit (2017)**

Population by income quintile per consumption unit according to household size.

### 3. Household perceptions

In most EU countries, the majority of people self-identify as belonging to the middle class. In Spain, according to data by the OECD (see OECD (2016b)), the proportion of the population considering themselves to be middle class (slightly above 50%) corresponds with the percentage of people that data would suggest as actually belonging to the middle class (50%). It is quite another story in other Mediterranean countries such as Portugal, where the proportion of the population self-identifying

with the middle class is lower than income data would suggest—or in Italy, where the proportion self-identifying with the middle class is much higher.

The Centre for Sociological Research (CIS, in Spanish), however, delivers different results. According to the December 2007 barometer, 37% of the Spanish population identified themselves as middle class; in June 2017, this percentage had fallen to 36%<sup>1</sup>. Although this is just a slight decrease, it is important to bear in mind, since it might reflect a lack of confidence in future labour market and economic prospects.

#### 4. Political representation

The two main political forces in Spain—the Popular Party (PP) and the Socialist Party (PSOE)—obtained almost 84% of the votes in the 2008 general elections, while in the 2016 elections their share fell to 56%. This is a reflection not only of the general disenchantment resulting from the crisis and its consequences (unemployment, increased inequality levels and so forth), but also of the undermining of confidence in the Spanish traditional politics, due to corruption scandals and lack of credibility of the traditional parties. Ultimately, this has provided a breeding ground for new political parties, such as Ciudadanos ('Citizens') or Podemos ('We can').

The case of Podemos is of particular interest. It is a populist formation which rapidly became very popular among Spaniards, especially the 'new middle class' and the middle-upper and upper classes (El Español, 2016 & CIS, 2016). The party has been able to fill the gap left by the traditional formations that have been losing popularity since 2013 (El País, 2015), as clearly demonstrated by their loss of votes in recent elections. As some studies note, there is a simple reason for this: the middle class has shown its discontent following the crisis and is looking for solutions from new political formations (El Mundo, 2016). Podemos obtained 21% of the votes in the 2016 general election. Ciudadanos ('Citizens'), seen by voters as a centre-right party, obtained 13% of the vote.

Ciudadanos has included the middle class in its political discourse—insisting on “the need for the middle class to be given back what they have lost” instead of “tightening its belt”, referring to the Government's proposal of decreasing the ceiling for expenditure back in 2016 (La Vanguardia, 2016). Curiously enough, Podemos stands for the opposite: the party (its leader, in particular) has disregarded the new and upper-middle classes that supported it, appealing, instead, to the working and lower-middle class identity as the driving force of Podemos (El Periódico, 2017).

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<sup>1</sup> The CIS distinguishes between 'new' and 'old' middle classes. The category 'new middle class' includes non-manual salaried employees, while the 'old middle class' comprises business owners, self-employed workers and farmers.

## 5. Globalisation, technology and migration

European societies and production models are forced to adapt to the demands imposed by the twenty-first century, marked by the globalisation process and the technological revolution. The digitalisation process we are now witnessing has brought about a job polarisation phenomenon (in skills and earnings) that is contributing to the decline of the middle class (OECD, 2016b). Indeed, new technologies have created high- and low-skilled jobs, while destroying semi-skilled employment.

Job polarisation and the reduction in semi-skilled employment will have a significant effect on the income distribution and social class structure in all countries, whatever their stage of development (FAES Foundation, 2015).

Several studies suggest that migration flows have a great impact on the economy (IMF, 2016), which is particularly important for countries such as Spain, which has historically been both a sender and receiver of migrants. Since the beginning of the 2008 crisis, migration flows have mostly taken the form of young and high-skilled people between the ages of 25 and 34 leaving the country in search of employment opportunities. Some studies estimate that 700,000 Spaniards left the country between 2008 and 2012 (Fundación Alternativas, 2013). As for immigration, Spain has traditionally been a net recipient of migrants. First, in the late 1990s, immigrants came from countries such as Morocco, France or Portugal. Later, it was Latin America and today, Romanian and Moroccan immigrants are the most numerous (El País, 2017).

Given the challenges of globalisation and digitalisation, the persistence of structural weaknesses threatens the standard of living of the middle class in Spain. The inefficiency of the labour market, the welfare state and education hinders the economic recovery of middle-class households. To help the middle class recover fully from the economic crisis, we propose several structural reforms:

- Spain needs a labour market reform that leads to a further recovery of employment and puts an end to duality and insecurity;
- Spain needs a fiscal reform that sweeps away the distortion of the economic activity and increases the country's tax collection capacity;
- Spain needs an educational reform that ensures equal opportunities and social mobility;
- Spain needs a reform of the worker's training scheme, which is weak and incapable of ensuring the human capital levels required to cover the needs of the companies;
- Spain needs a pension system reform in a context of increasing longevity and low birth rates;
- Spain needs to address the high public debt levels and the consequently high amount of resources assigned to debt payment.

## 6. Conclusion

As has been the case in other EU countries, Spain has recently seen a decline in the size of its middle class—so much so, that the Spanish middle class is actually the smallest among all the countries surveyed in this report. Overall, there are several factors underlying the worsening of the middle-income tiers of Spanish society.

The economic crisis and its severe consequences, mainly the high levels of unemployment and the ensuing rise in inequality, have been key factors determining the shrinking size of the middle class. But beyond that, Spain suffers from a structural weakness which, to a large extent, explains the constriction of the middle class: the inefficiency of the welfare system, which, as we have seen in this chapter, is not able to reduce the inequality levels and fails to facilitate social mobility.

Other sociological variables suggest the undermining of the middle class in Spain. These include lack of confidence not only in the labour market, but also in economic prospects, which is reflected in the loss of social class identity, together with the general disenchantment resulting from the crisis.

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