Wage Stagnation and Reinvigorating Wage Growth: The German experience

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Outline

1. German wage moderation – a European problem?
2. Stagnating ordinary living standards and increasing income inequality
3. Main drivers of change
4. Conclusions
1.1. German wage moderation – a European problem?

- Below average wage and unit costs increases in Germany
- In combination with declining public investments also below average increase of domestic demand and imports
- Increasing German export surpluses (2017 = 7.6% of GDP) contributing to European imbalances
- But German exports not very price-elastic: “Overall there is no evidence that wage developments are at the root of the development” (EC 2012: 91)
- reducing Germany’s current account surplus lies not solely in wages policy but also in an expansive national fiscal policy with an increase in public investment
- “However, Germany is not yet ready to take its financial policy in this direction” (Horn et al. 2017: 20).
1.1 Evolution of employee remuneration in the Eurozone and in selected EU member states 2000 - 2017

Employee remuneration per hour. Seasonally and working day adjusted. In national currency.

Quelle/ Source:
1.2 Increasing imbalances of payments in EU (in billion €)

1.3 Development of domestic demand 2000q1=100 (1)

2.1. Stagnating ordinary living standards and increasing income inequality
- Until 1990: Wages followed GDP growth – no increase in income inequality
- After unification until 1995 strong increase of low East German market incomes and pensions
- After 1995
  - decoupling of GDP and wages
  - increasing inequality of market wages and household incomes
  - stagnating living standards up to the 5th decile
- low wages important driver of increasing inequality of household incomes
2.1 Evolution of real hourly wages by decile in West Germany (all dependent employees) - With GDP per hour worked as comparison

Source: Source: Own calculations using the SOEP v32.1; GDP per hour worked, adjusted for prices, for West Germany up to 1991, for Germany as a whole from 1992 onwards: Statistisches Bundesamt, own calculations
2.2 Hourly gross wage of employees by Deciles 1995-2015

Source: Bundesregierung, Armuts- und Reichtumsbericht 2017 (based on SOEP v32)
2.3 Evolution of household real incomes before state redistribution by decile (working-age population 25 to 65 years of age) 1983 - 2014 and per capita GDP (until 1990 West-Germany, after 1990 Germany)

Source: Own calculations using SOEP v32.1; GDP: Statistisches Bundesamt, own calculations.
2.4 Household incomes after state redistribution - Households of older citizens (65 and over) compared with working-age households (25 to 65) - Deciles

Source: SOEP v32.1, own calculations
2.5 The low wage risk of dependent employees in households by income bracket (pre state redistribution) 1995 to 2014

Source: SOEP v32.1, own calculations. Low wage risk and household income in the various income brackets relate to the years as listed, not the previous years.
3.1 Main drivers of falling income standards

- **Erosion of the inclusive wage system:**
  - Privatization of public services (e.g. public transport, telecommunication)
  - Growth of atypical employment
  - Erosion of autonomous system of collective bargaining
  - Deregulation of labor law (Hartz-laws)

- **Increasing inequality of working hours**

- **Strengthening of old family model:** *strong financial incentives to work short hours*

- **Reduction of progressive income and corporate taxes:** *increased financial pressures on the welfare state*

- **Reduction of pension levels** *(effects will show up over the next 40 years)*
3.1 End of pattern agreements

3.2 Declining coverage by collective agreements

Source: WSI Tarifarchiv (based on IAB Establishment Panel data)
3.3 Rate of coverage by collective agreements and share of low-wage work (2014)

Source: Visser 2015, Eurostat, own calculations
3.5 Annual gross working time volumes by income bracket \((\text{pre-state-redistribution})\) - percentage change \\
\((\text{working households - Germany as a whole})\)

Source: Own calculations using the SOEP v32.1. Working households have a head of household between 25 and 65 years of age and income from gainful employment.
3.7 Main drivers of improving income standards

- Introduction of care insurance in the late 1990’s

- **New family model**: Expansion of child care and all-day schools, paid parental leave, new working time options (from FT to PT and vice versa) – less part-time penalties – longer hours

- **Job miracle in the financial crisis**: reduction of working hours not of jobs, recruitment of apprentices even in the crisis

- Introduction of **Minimum wage** and facilitation of extending collective agreements

- **Strong job growth since 2004**, especially skilled service jobs
Nominal growth in contractual hourly pay over two years by deciles 1998 - 2016
Conclusions

• Growing inequality of market and household incomes

• Main drivers:
  - Erosion of the inclusive wage system
  - Increasing inequality in the distribution of working hours

Main policy changes

- Reduction of inequality in the primary distribution by increasing coverage by collective agreements
- More equal distribution of working hours across income classes (also skill question!!)
- Abolition of incentives to work short hours linked with traditional family model
- Higher taxation of top earners

Quelle/ Source: