Flexible German unions bend the Phillips curve

If applied in practice, concept proposals by German unions to demand shorter working weeks instead of asking more money will not make the ECB's life any easier

Wages: The lynchpin of the ECB's monetary policy

Recently, a lot has been written about the relationship between dropping unemployment rate and wages. ECB president Draghi even called wages the lynchpin of the ECB's monetary policy. As long as wages remain low, there does not seem to be a need for the ECB to tighten its monetary stance. Up to now, the ECB has been arguing that the Phillips curve, initially describing the inverse relationship between unemployment rates and inflation, was still intact, only flatter than traditionally. This thinking has been illustrated by the fact that the ECB's staff projections have constantly predicted an acceleration of wage growth at the end of the forecast horizon. Unfortunately, up to now, there is no evidence that these projections are any better than wishful thinking. The slack in labour markets (high number of people in low-wage jobs, involuntary part-time jobs or temporary jobs) is still too high to see a significant acceleration of wages any time soon. Today, this belief in a functioning Phillips curve got another hit.

Will wages ever pick up?

If there is one economy in the Eurozone, where wages should start to pick up, it is the German economy. However, since 2009, nominal wages have only increased by an average of roughly 2% YoY. In real terms, wages increased by around 1% every year. Better than nothing but not the wage growth one could expect in an economy which is in its ninth year of strong growth and in a labour market which produces record-low unemployment numbers and record-high employment numbers almost every single month. To paraphrase Frank Sinatra: if wage inflation does not pick up there, it will not pick up anywhere (else in the Eurozone).

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Hidden unemployment, a still huge low-wage sector and the influx of refugees are probably the main reasons for sluggish wage growth. Add to this latest problems in the automotive industry, the threat of automatization, globalization and downward pressure on wages and prices from digitalization (also in services) and it becomes increasingly unlikely to see German wages spike any time soon.

1% Real wage growth

YoY from 2009

A change in German preferences continuing the problem

The likelihood that German wages will do the ECB the favor to pick up this Autumn has clearly decreased. Today, German newssite "Spiegel Online" reported on the concept demands of IG Metall for the upcoming wage negotiations. According to this report, IG Metall will call for the possibility to reduce the current 35-hours-week to 28 hours, for a period of up to two years. Hourly wages should remain constant. It is an interesting trend, which in our view reflects the changing structure of the labour market and the changing preferences of employees. More leisure time and not more money.

If this is the new slogan of upcoming wage negotiations and settlements, don't expect Germany to take the lead when it comes to wage inflation that would make the ECB happy.

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