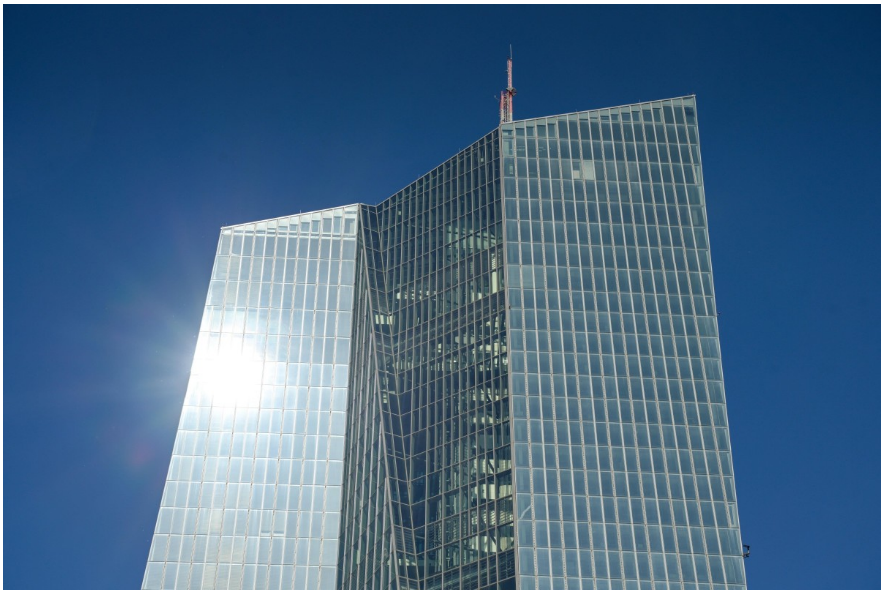
Drop in eurozone negotiated wage growth brings relief to ECB

The decline in negotiated wage growth from 4.7 to 4.5% year-on-year confirms expectations that wage growth is no longer accelerating. But it is too small to open the door to an ECB rate cut in March. With wage growth expected to trend down carefully from here, we expect modest ECB cuts starting in June



Wage growth is the number one worry for the ECB at the moment, as has been stressed by European Central Bank President Christine Lagarde time and again in recent speeches. While we anticipate that wage growth will moderate significantly over the course of 2024 on the back of abated inflation and weakened economic conditions, it must come as a relief in Frankfurt that negotiated wage growth fell from 4.7 to 4.5% in the fourth quarter.

Sure, it's only a small tick down, but broadly in line with expectations that negotiated wage growth will start to trend down over the course of 2024. That also follows from the ECB's own wage tracker, which monitors wage growth agreed in collective bargaining agreements for the 12 months ahead. This has plateaued for some time now and most recent agreements have trended lower. We expect to see a more meaningful decline in nominal wage growth before the summer. Other measures of wage growth have already cautiously started to move down earlier, but negotiated wages make up the bulk of wage developments in the eurozone.

Still, the fourth quarter drop is a small decline and therefore we don't expect the ECB to be particularly hasty in deciding on first rate cuts. The June meeting – after another quarter of wage data is released – looks like a good moment for a first 0.25% rate cut to us.

While nominal wage growth declined, today's release did mark the first quarter of real wage growth (so wage growth – inflation) since the start of the energy crisis in the eurozone. The deep fall of real wages has therefore only just bottomed out and for now, the rebound is not expected to be particularly strong. The expected declining trend of nominal wage growth over the course of 2024 makes the upside to consumption rather limited.

Yet, elevated nominal wage growth does add to cost pressures for businesses and if recovering purchasing power leads to continued consumption, then this could result in a slower than hoped for return to the 2% target for the ECB. While those concerns shouldn't be overdrawn in the current environment of lackluster economic activity, it is an important reason for us to expect the ECB to adjust monetary policy only carefully in 2024. We expect 0.75% of cuts in total for the year.

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