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Does the German social model support the convergence of living conditions in the EU?

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1.1 Convergence in the EU

- Two types of convergence in the EU:
 - Beta- convergence: catch-up process of poorer countries
 - Sigma-convergence: Reduction of social inequality within member states and the EU
- EU not conceived as merely economic union in which convergence is reached through factor mobility and market forces
- **Convergence will not happen spontaneously; there must be a political will to achieve it and it has to be actively managed**
- EU developed instruments to reach convergence (structural funds, EU directives ...)

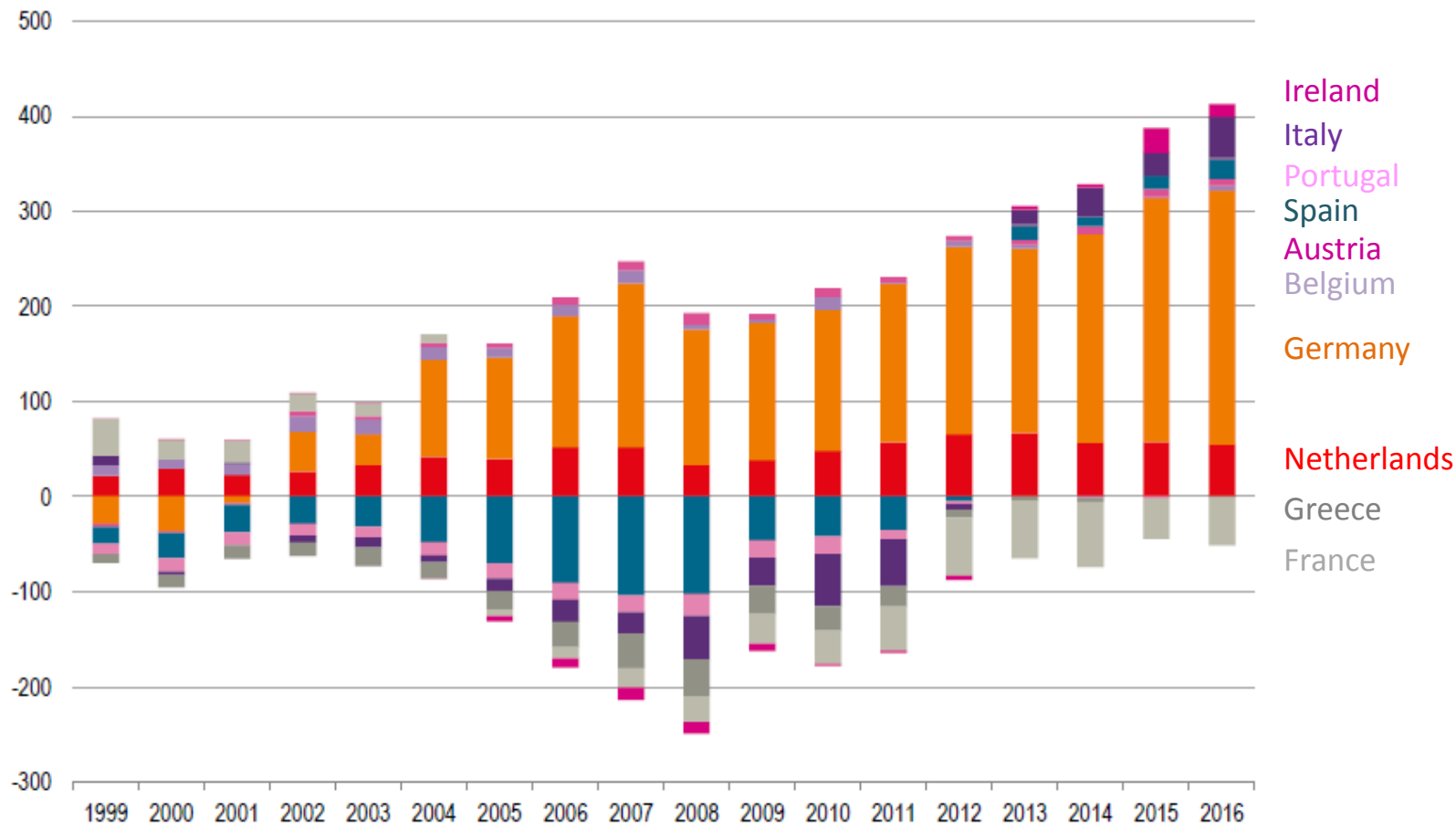
1.2 Convergence in the EU

- Convergence cannot be reached only through EU policy and convergence debate cannot be conducted on a country by country basis
- Common economic area – *and even more so in a monetary union* – a policy adopted by one country can have both positive and negative effects on the convergence processes in other countries
- Many examples of negative effects of national policy in tax, fiscal, social policy and other areas
- **My research question: Is the German social model setting model supporting convergence in the EU?**
- **This question became important because of extremely high trade surpluses of Germany**
- Very different answers to this question in and outside of Germany

2.1 Germany trade surpluses – are their roots in the German social model?

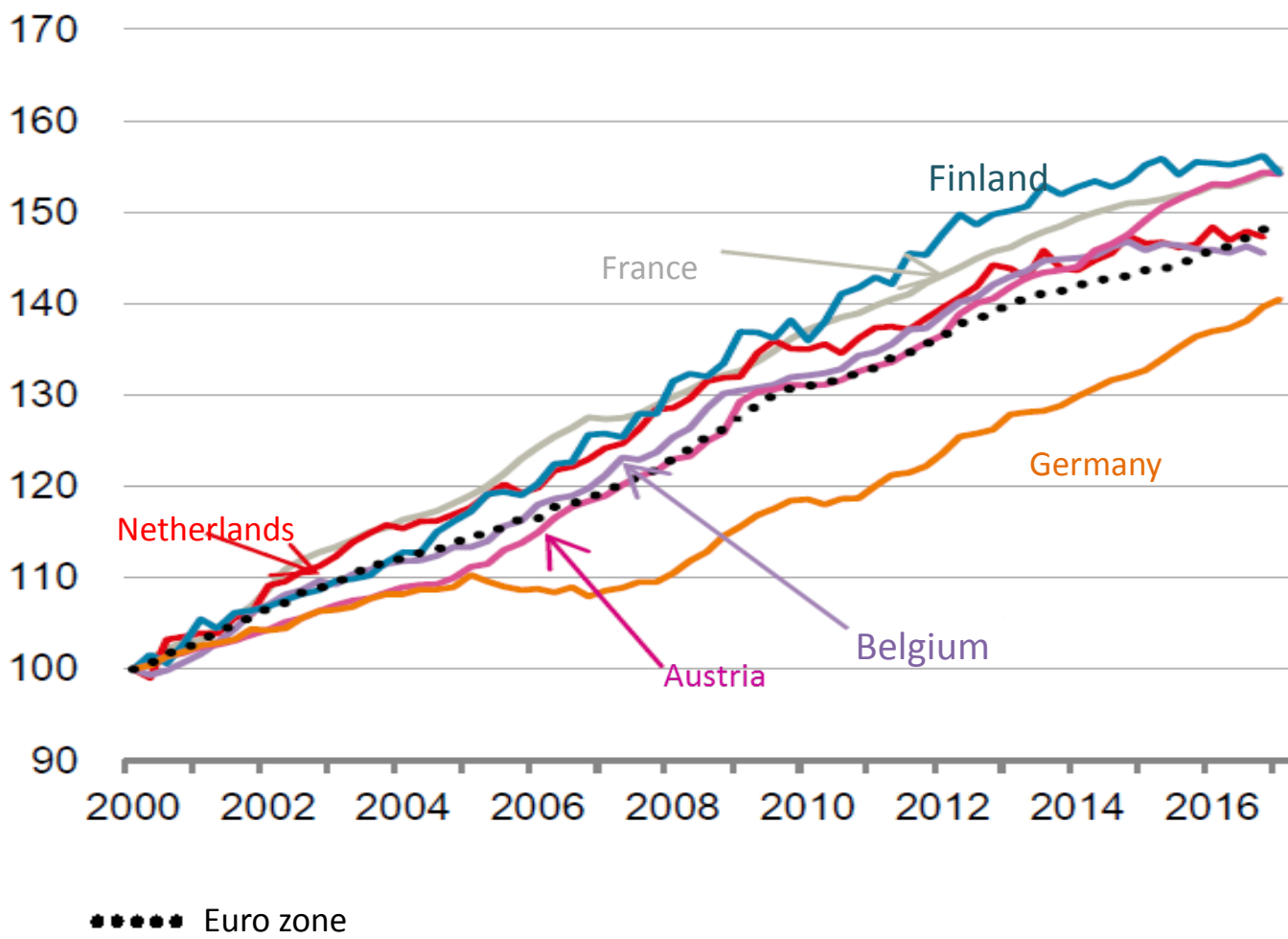
- German surplus in balance of payments in recent years around 8,5% of German GDP – mainly due to export surpluses
- **Surpluses exceeding the upper limit of 6 %** set by the EU – but no sanctions – sanctions easier when countries have to ask for credits
- Main stream view of trade surpluses and deficits: **price competitiveness and wages is the driver**
- **Recipe: If unit costs go down in South Europa and up in Germany everything is fine: wage setting therefore crucial - productivity neglected**

2.2 Balance of payments of Euro-countries in billion €



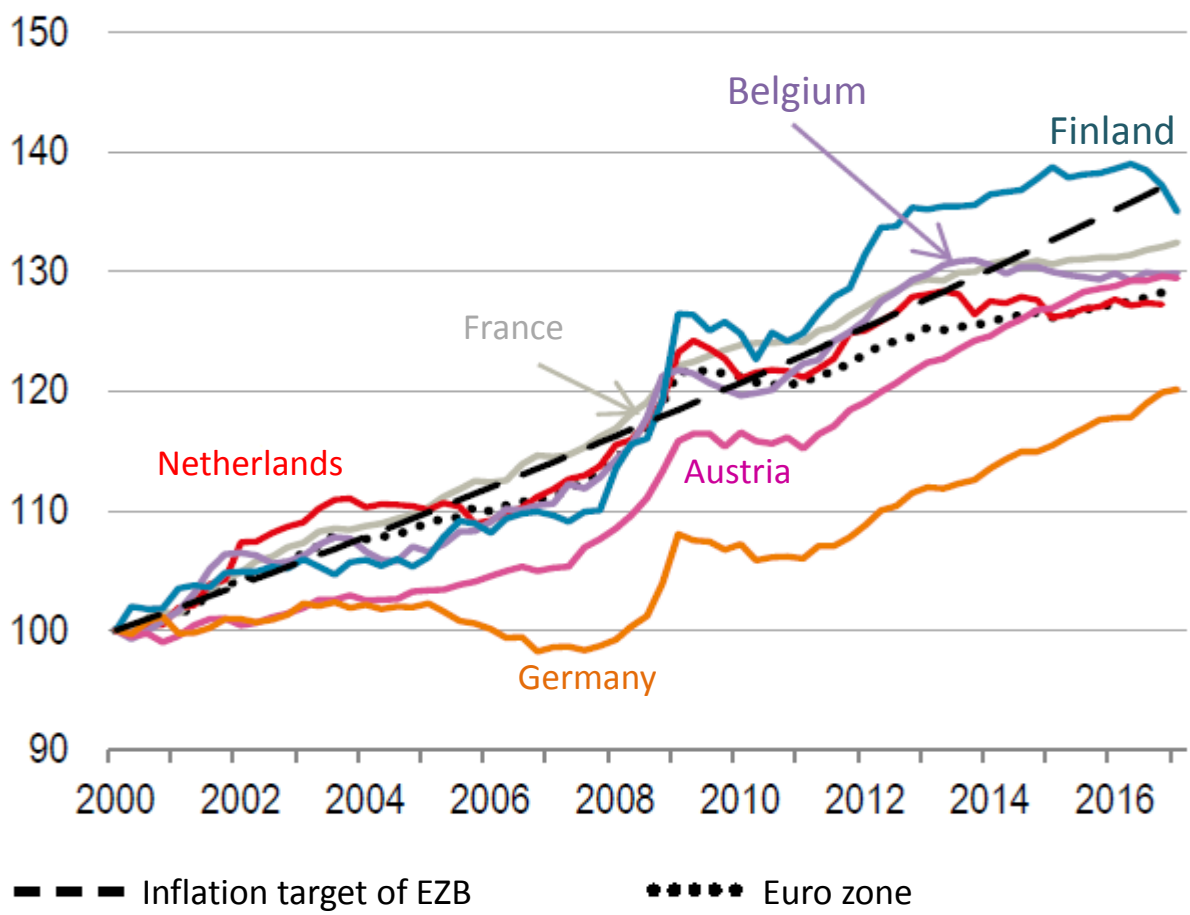
Source: Albu et al. (2017) IMK Report 128.

2.3 Development of hourly gross wages in selected countries - 2000q1=100 (1)



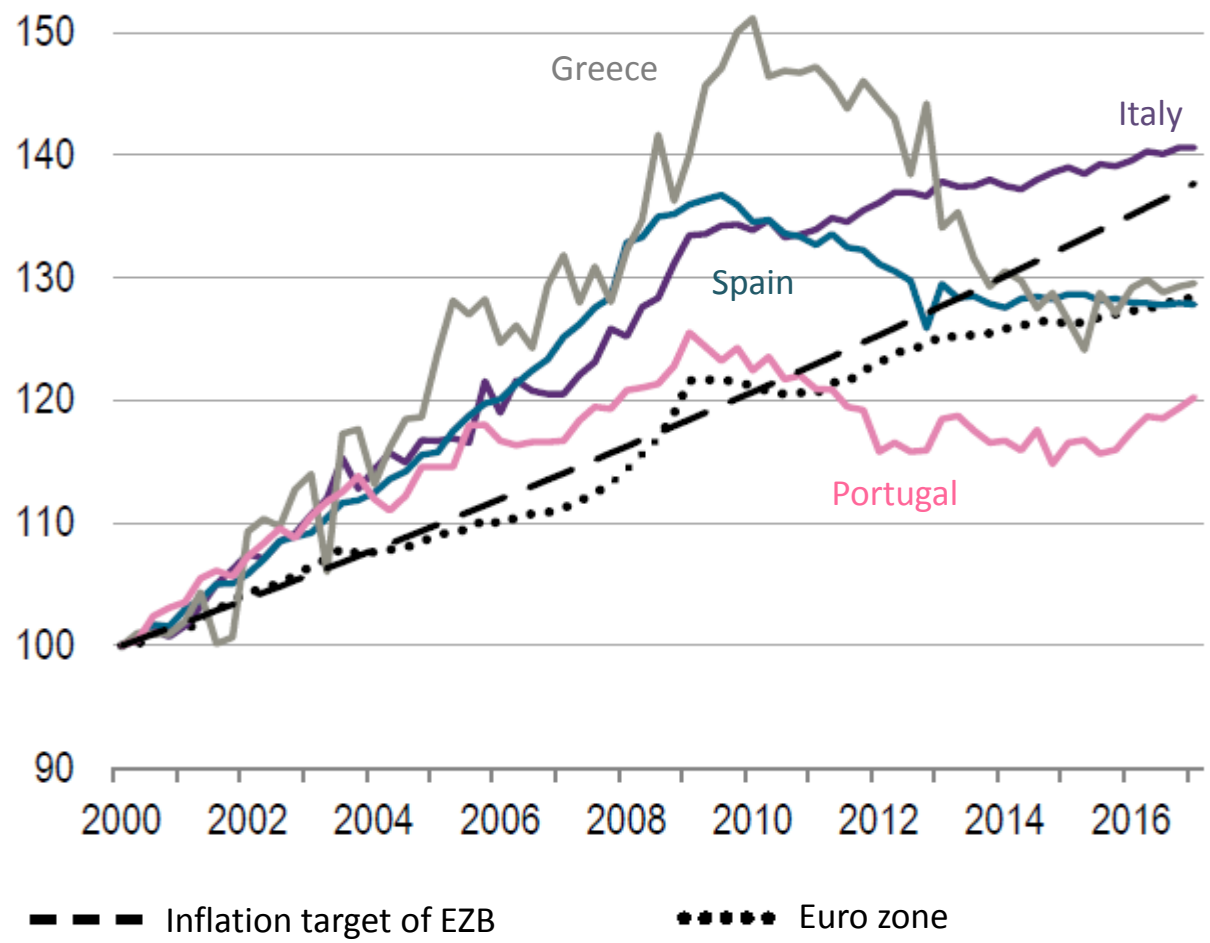
Source: Albu et al. (2017) IMK Report 128

2.4 Unit labor costs in the Euro zone 2000q1=100 (1)



Source: Albu et al. (2017) IMK Report 128.

2.4 Unit labor costs in the euro zone 2000q1=100 (2)



Source: Albu et al. (2017). IMK Report 128

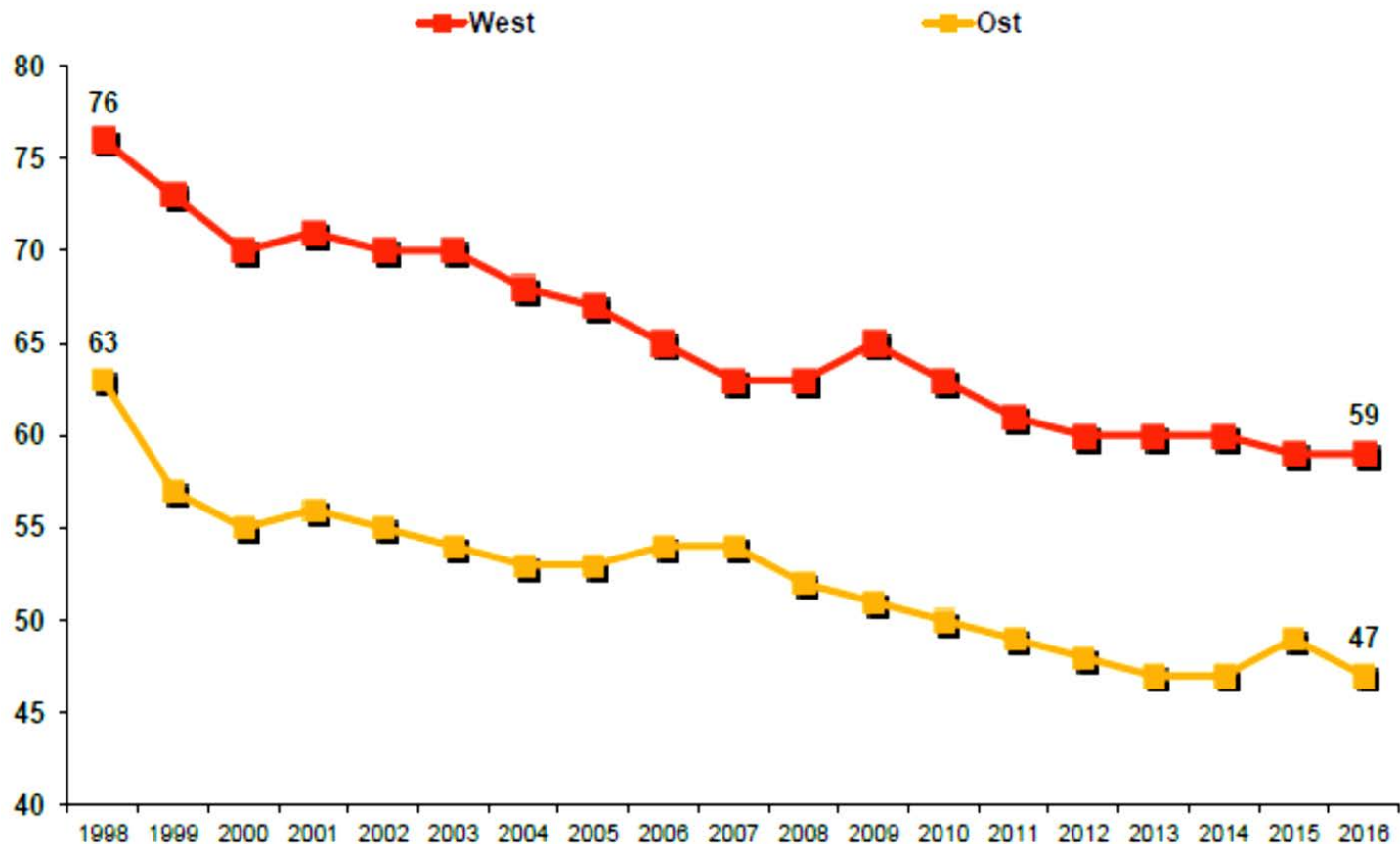
3.1 German wage setting system

German trade unions **under suspicion** to enforce wage restraint in order to encourage job growth in Germany at the expense of other EU member states

Some authors speak of **producer coalitions** in big companies in which unions and works councillors tolerate less favourable working conditions of peripheral workforces or suppliers and have campaigned against the introduction of the MW (Carlin/ Soskice 2009; Palier/Thelen 2010; Hassel 2014).

There are producer coalitions, but main reason for wage moderation declining coverage by collective agreements because of the **deregulation of product and labour markets and new employer strategies**

3.2 Evolution of coverage by collective agreement in Germany 1998 - 2016



Source: WSI Tarifarchiv (based on IAB Establishment Panel data)

3.3 Collectively agreed wages grew faster than actual wages – negative wage drift



Quelle: Statistisches Bundesamt, WSI-Tarifarchiv 2015 | © Hans-Böckler-Stiftung 2015

3.4 German wage setting system

Where unions are strong high wage increases and short working hours (example engineering industry)

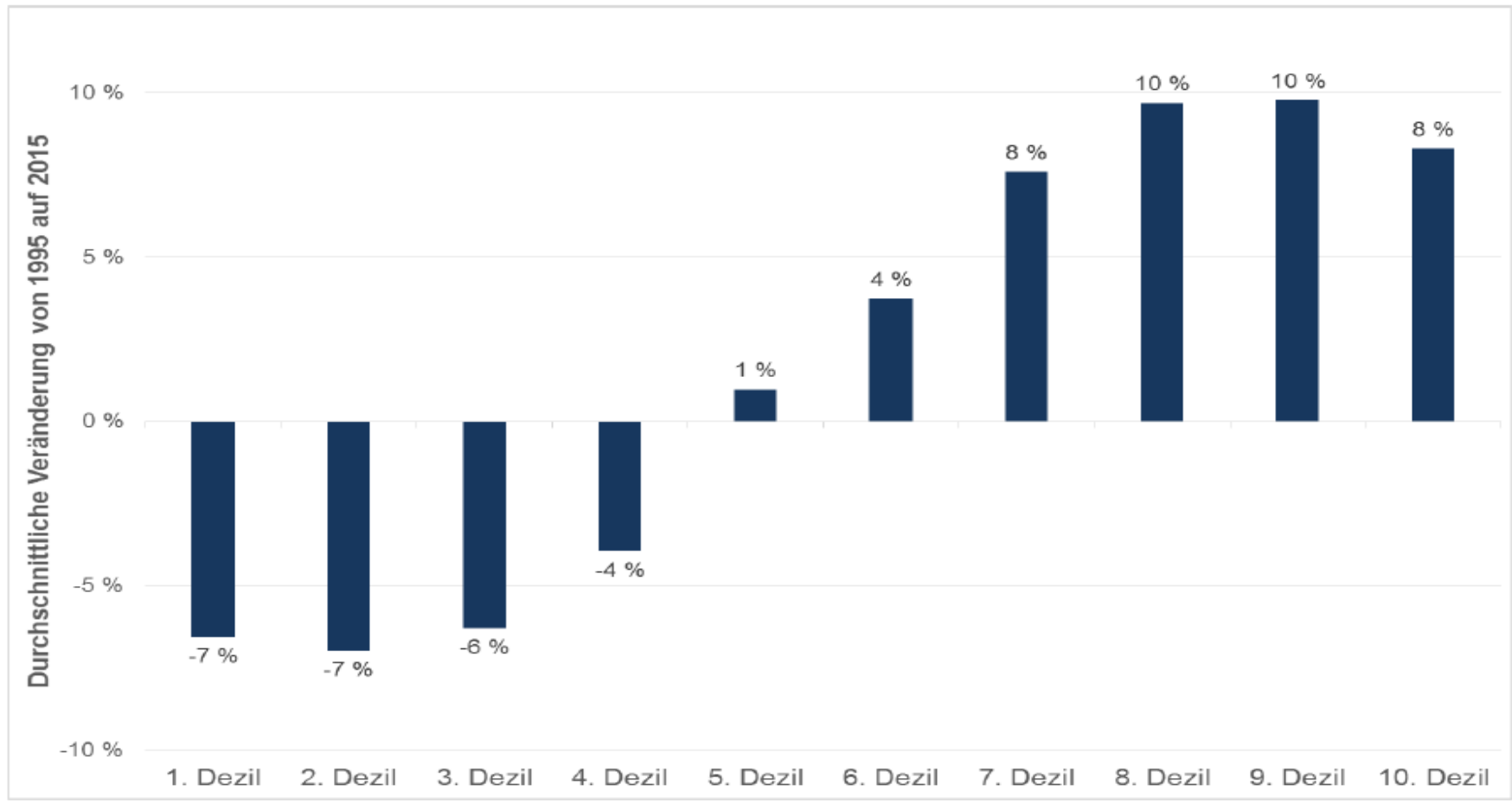
German wage setting system – vulnerable to outsider competition - most CA's not declared as generally binding

Main reasons for negative wage drift:

- Employer's leave of do not join the employer's association
- Fragmentation of companies / delocation of jobs to uncovered companies
- Deregulation of product market and privatization
- Deregulation of the Labour market through the Hartz-Acts

3.5 Result beside low average wage increases - increasing income inquequality

Hourly gross wage of employees by deciles 1995-2015



Source: Bundesregierung, Armuts- und Reichtumsbericht 2017 (SOEP v32)

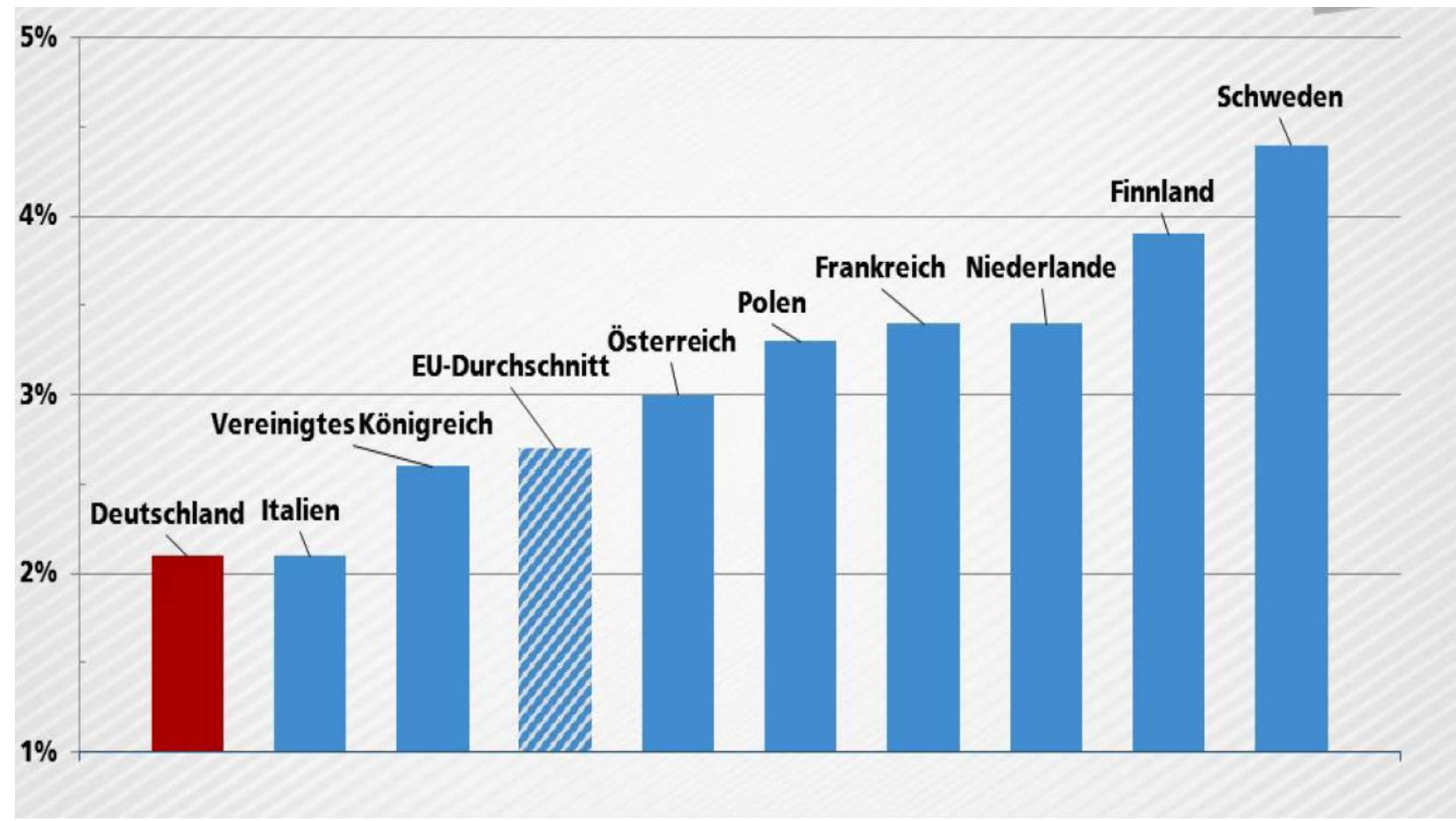
4.1 Would higher wage increases in Germany help?

Most non-German economists would agree

But different views

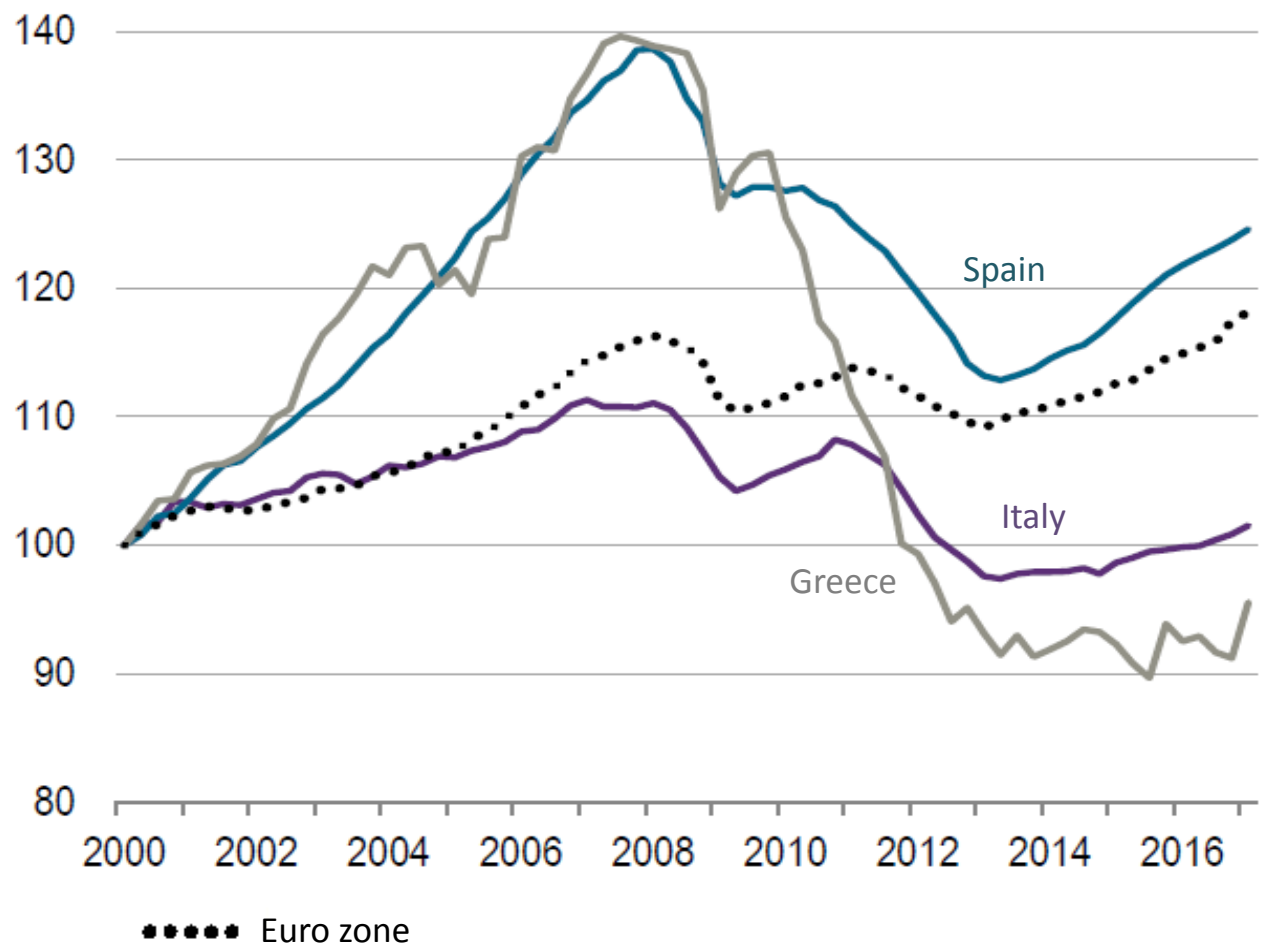
- *EU-Commission*: “Overall there is no evidence that wage developments are at the root of the development”
(European Economy 9/2012: 91) – Why then the dictates of the institutions in South European countries?
- *German government*: Low price elasticity of German exports, ageing society needs savings for the future...
- *IMK*: low price elasticity – but German wage restraint reduced domestic demand and therefore imports – **a combination of wage increases and investments programs would help**

4.2 Public investments in % of GDP 2016



Source: Eurostat

4.4 Development of domestic demand 2000q1=100 (2)



Source: Albu et al. (2017) IMK Report 128.

5. Conclusions

Low wage increases and growing income inequality in DE led to high trade imbalances in the EU – **negative impact** on

- **beta-convergence**: austerity policy in deficit countries stopped catch-up processes
- **sigma-convergence in EU**: increase of inequality in DE and EU

Driving force not producer coalitions – unions do not have the power anymore to negotiate higher wage increases across the economy

Higher wage increases and more investment in Germany needed to reduce trade imbalances

But **no political will** in DE to do so!