How to implement an ‘optimal wage regime’ for the euro zone

euprogressiveplatform.com/2019/05/10/how-to-implement-an-optimal-wage-regime-for-the-euro-zone

May 2019 [2014]

Michel Husson with Odile Chagny (*)

An optimum wage regime for the euro zone could be defined by three main objectives:

1. a stabilized macroeconomic wage share which allows for a fair distribution of productivity gains at the level of the national economy
2. homogeneous wage growth across economic sectors, in order to allow for the redistribution to all wage earners of the productivity gains obtained in the best performing sectors;
3. it must avoid a deterioration of some euro zone countries’ price competitiveness caused by a divergence among them in unit labour costs and/or inflation rates

We are very far from this optimum:

1. The first objective was very partially achieved before the crisis; since then, the wage share has declined in almost all countries of the euro zone.
2. The second objective has been achieved, since wages grew at roughly the same pace in the two major sectors (the “exposed” and the “sheltered” sectors), with the (notable) exception of Germany. But, since the crisis, the national models are converging on the “German model” where wages align with the specific productivity of each sector and no longer on average productivity gains.
3. The consequence of these partial achievements was a divergence in inflation rates that severely impaired the cost- and price-competitiveness of the vulnerable countries. Since the crisis, the adjustment of price competitiveness was obtained only by a restriction on demand[1] or by an internal devaluation[2], a devaluation of the exchange rate being by definition excluded inside the euro zone.

Every wage earner should benefit from the overall growth of the economy irrespective of the characteristics of the sector she is employed in. This was the “golden rule” of indexing wages on inflation and average productivity[3]. This rule should be re-established, because the systematic capture of productivity gains by the firms in the name of competitiveness – and often to the benefit of shareholders – is not economically and socially sustainable.

But the implementation of this golden rule was hampered by two factors. The first is the general drift in wage shares during the crisis period. The second is the imbalance caused by Germany, which significantly, and early, moved away from this wage rule. The introduction

of a minimum wage in Germany is a way to recognize that the drift was going too far.

It will be difficult to escape the “incompatibility triangle” that seems to exist between the three goals mentioned above, but we can sketch out three propositions that would at least loosen its constraints.

The first proposal is **the introduction of a European minimum wage system**, which would help to reduce the increasing wage gap across sectors and to prevent for deflation risks. It would offer an immediate answer and an essential tool to prevent a wage slippage in the so-called sheltered sector. Even Jean-Claude Juncker, the President of the European Commission, stated in 2013 that “we need a basis of social rights for workers, minimum social rights for workers, including of course one essential thing, a minimum wage, a legally compulsory minimum wage in the euro-zone member states”.

The concrete proposal could be that **an interprofessional minimum wage be set at 60% of the median wage in each country**. However, this proposal meets the opposition of some members of the European Trade Union Confederation, in particular Swedish and Italian unions which privilege the negotiations at the industry level. This blockage should be lifted, for example, by **establishing a floor wage as it is the case in Austria**.

A second condition should be also met to move towards the optimum wage regime. It concerns the **differentiation of inflation rates**, which reflects the structural characteristics of each country. Inflation is an indicator of a double conflict: between employees and employers for the distribution of productivity gains, on the one hand, between industries for productivity gains transfers, on the other hand. A **greater institutionalization of wage indexation rules and the homogenization in collective bargaining procedures could alleviate these tensions**.

More fundamentally, within a single currency area, an optimum wage regime requires a **convergence in productivity performances**. But it did not occur. The functioning of the European integration has instead led to an industrial specialization that accentuated polarization between countries and regions, while capital flows did not invest in the sectors with the highest potential productivity.

Only **transfers and investments directed towards sectors where productivity can be significantly raised in the catching-up countries would trigger the convergence of productivity gains**, which in turn constitutes the material basis underlying the homogenization of wage earners’ conditions of existence. These are the perspective proposed for example by the **European Trade Union Confederation with its plan for “investment, sustainable growth and quality employment”**, associated with its proposals for wages and collective bargaining.

Maybe the euro-system itself is far from optimal, and this the reason why such changes within the European economy may look very remote or even out of reach. But if they are not implemented, the polarization of Europe is likely to worsen, between the surplus countries and the others, condemned to a slower growth and a perpetual wage moderation, or, in other words to a "low-cost" development model.

Michel Husson is a French economist. He works at the French Institute of economic and social studies (IRES) and is known for his work on labour market policy.

(*) This contribution is based on research conducted with Odile Chagny at the Ires (Institut de recherches économiques et sociales). It was published by the European Trade Union Institute and by *La revue de l'Ires* (in French).

---

[1] The decrease in the aggregate demand for goods and services decreases the aggregate price level.

[2] Internal devaluation is one of the strategies used to increase one country's competitiveness in a situation of open economy with a fixed currency. It consists in a decrease of labour costs (e.g.: wages or labour taxation) to make the price of a good or a service more affordable both inside and outside the country. Internal devaluation is opposed to external devaluation, that is, the decrease in the relative price of a currency compared to other currencies.

[3] This was the "golden rule" during Fordism. The shift from Fordism to the service economy, together with the neo-liberal shift of the 1970s, broke this mechanism.