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IG METALL PAY AGREEMENT MAY 2007: WAGE GROWTH IN THE GERMAN METAL SECTOR BASICALLY REMAINS STABLE

With IG-Metall opening the 2007 bargaining round by demanding a 6.5% wage increase, many policy makers in Europe have been focussing on the possible outcome of this wage negotiation. In particular, the IG-Metall's wage demand has most probably been at the basis of the ECB's repeated warnings that 'wage growth might be higher than expected' because of the economic recovery handing back more bargaining power to trade unions.

On the 4th of May, IG-Metall concluded a new collective agreement for the region of Baden-Württemberg. The agreement is covering a period of 19 months (April 2007-31st of May 2008) and it recommends other regions to conclude a similar agreement in their metal sector.

Contents of the agreement

What stands out in the agreement is a 4.1% increase in wages from 1st June 2007 on. This structural wage increase is supplemented in 2007 by a lump sum payment of 400 euro covering April and May 2007.

Another, but substantially more limited, structural pay increase of 1.7% will be paid out in June 2008. This structural wage increase will be complemented in 2008 with a 0.7% one-off payment for five months in a row from June until October 2008. Depending on the economic situation of the company, the payment of this 0.7% one-off payment can be delayed until the 1st of October 2008, provided management and the works council strike an agreement on this.

Impact on wage growth

The interaction of structural wage increases with one-off payments does not make it so straightforward to estimate the impact of the agreement on total wage growth. To do so, IG-Metall developed a methodology to calculate the value of the agreement over the calendar years as well as over the period the agreement is covering. Using this methodology, we estimate that:

- The average monthly wage increase over 2007 implied by this agreement is 3.8%, up from 3.1% in the previous calendar year.
- This certainly represents an acceleration of wage growth. However, with 10 months of collectively bargained wage increases already fixed for 2008, the average wage increase over the first ten months of 2008 can be calculated as well. Agreed monthly wage growth over the first ten months of 2008 would be limited to 2% only. Of course, the total average wage outcome for 2008 will

depend on the collective agreement to be negotiated at the end of 2008. But even if, for arguments' sake, we assume that this would involve a pay raise of 5%, then the average wage outcome for 2008 would still be limited to 2.5% (with the impact of the wage increase on 2009 again depending on the length of the agreement, what is happening with one-off payments and so on).

- **In other words, the acceleration in wage growth in 2007 is temporary and provisions are already taken in the agreement to return over 2008 to a relatively modest pace of collectively bargained wage growth.**

Another of looking at this is to focus on the value of the whole agreement and comparing it to the previously concluded agreement, irrespective of calendar years. Comparing the average wage increase over the 19 months of the May 2007 agreement with the wage increase concluded in the previous 13 months' agreement concluded early last year and covering March 2006 to March 2007 reveals that the acceleration of the average monthly wage increase from one agreement to the other agreement is very limited: It was 3.05% in the old agreement and 3.17% in the recently concluded agreement.

	Average wage increase over the calendar year		Value of the whole agreement
2006	3.1%	2006 agreement March06-March07	3.05%*
2007	3.8%	2007 agreement April 07- October 08	3.17%
2008 (10 months)	2% (10 months figure) to a max of 2,5%		

Source: ETUC calculations except *: IG-Metall estimate

Evaluation: ECB concerns over inflationary wage developments are misplaced

It appears that there's an implicit trade-off in the German metal agreement: A bigger and more tangible pay increase for the coming months is traded off against a substantially lower wage increase over 2008. This pattern of a temporary acceleration in wages might also reflect the policy on non-wage costs in Germany. Indeed, one third of the extra revenue generated by the VAT-increase is being recycled to employers, lowering their social security contributions. So, a one-off windfall profit for employers is being taken up by collective bargainers in the form of a temporary acceleration of wage growth.

This implies that the ECB's fear of wages spiralling out of control are totally misplaced. If wages in what is now probably one of the most competitive and most profitable sectors in Europe are only engineering a temporary acceleration of wage growth in 2007 (which is moreover being neutralised to a certain extent by cuts in employer social security contributions) and then returning to a substantially more moderate stance in 2008, then the danger of inflationary wage developments in the euro area is not real but imaginary.

At the same time, with inflation in Germany running around or even below 2% and probably falling substantially below 2% in 2008¹, the 3.8% average wage increase over 2007 does result in a sizeable boost in the purchasing power of wages of German metal workers of around 2% this year and probably at least 1% in 2008. Provided the trend of negative wage drift coming from opening clauses at enterprise level is kept under control, the German metal agreement is delivering real growth in wages without endangering the objective of price stability or the profitability of firms².

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¹ Commission forecasts table on 1.2% inflation in Germany in 2008.

² Given the fact that hourly productivity in the entire German economy is now growing at around 1.8%.