Driving forces behind the wage costs differentials in Europe? Productivity is not the whole story.

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Abstract

In 2004 Eurostat began to publish new figures on hourly wage costs for all European countries. These figures are new in several dimensions: It is the first time comparable hourly figures on this schemes are available and they cover a quite important time period, 1995-2004/5, so that not only intra- and inter-countries-comparisons are possible but also a dynamic analysis. Secondly, they are fairly detailed at the sectoral level, so that inter-sectoral comparisons within and between countries are possible.

In a German context these statistics are of particular interest because it sheds new light on the ranking of Germany among other countries. Indeed until now it was a broadly accepted view that the German wage costs are of the highest in Europe. The new Eurostat figures but show a more balanced picture: Western European countries constitute a bulk of high wage costs, where Germany takes a rather middle-field position. The Southern and foremost new Eastern countries indeed have much lower wage costs.

The second interesting result is that one explanation for this is that the gap between wage costs in the manufacturing sectors and the (private & business) services is much larger in Germany than in other countries.

This study aims to explain why; along theories various explanations are possible. Firstly the neo-classical tradition forsees factors affecting or indicating the level of individual productivity, as well as the firm or sectoral-productivity. Indicators for this view are tested. Other departing theories see in the drop of perfect competition on both labour and goods markets a way for others factors (mark-up, market power) to influence wage costs levels. These factors are also tested here. And third, we think that demand plays a major role. Thus the structure of demand in a country explains a big share of the economic situation in different sectors. Thus the structure of demand (export-led or domestic-led) is also a major determinant of the wage difference between industry and services. Indeed, this factor seems to play a important role.

The paper is divided as follows: Firstly, the new Eurostat statistics is presented with some interesting descriptive results. In a second part, from theory a set of possible determinants of wage differentials between industry and services is listed. A bivariate analysis (correlation) is then performed and conclusions are drawn. In a third step, a multivariate analysis, a panel estimation, will be performed. The last part will conclude.

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