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Wages, labour costs and living standards

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SUMMARY

Ireland has one of the highest *median hourly earnings* in the EU. However, this indicator needs to be set in context with reference to labour costs faced by employers and living standards experienced by workers.

Compulsory social contributions of employers are low in Ireland in an EU context. When comparing standards of living a focus on median earnings ignores the benefits workers in many other EU countries receive from employers' social contributions. In terms of labour cost competitiveness (not to be confused with the wider concept of competitiveness), ignoring these contributions overstates the costs of Irish labour for employers relative to other member-states.

Ireland is actually below the UK and the EU-19 average in *business economy total labour costs*.

In addition, Ireland has a low standard of living as measured by '*Actual Individual Consumption*' relative to the EU28 average, sitting just above Portugal and Spain toward the bottom end of the table.

KEY POINTS

- *Median hourly earnings* in the *business economy* adjusted for purchasing power are almost €2 an hour higher in Ireland than the Eurozone average.
- The average of *total hourly labour costs* (the average cost per hour borne by an employer, including social contributions) in the *business economy* is lower than the Eurozone average and lower than in the UK.
- Ireland's *relative* position in terms of aggregate *nominal labour costs* has been improving against the UK and EU19 since the financial crisis of 2008-2012.
- Labour costs are just one consideration of many in a firms' cost-benefit analysis in deciding whether or where to invest.
- Irish living standards as measured by '*Actual Individual Consumption*' are in the bottom half of EU members and significantly behind other small open economies such as Belgium and Austria. Ireland is one of the only member-states where this is below 2008 levels (the EU19 average grew by over 10% in this period).

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Research for new economic policies

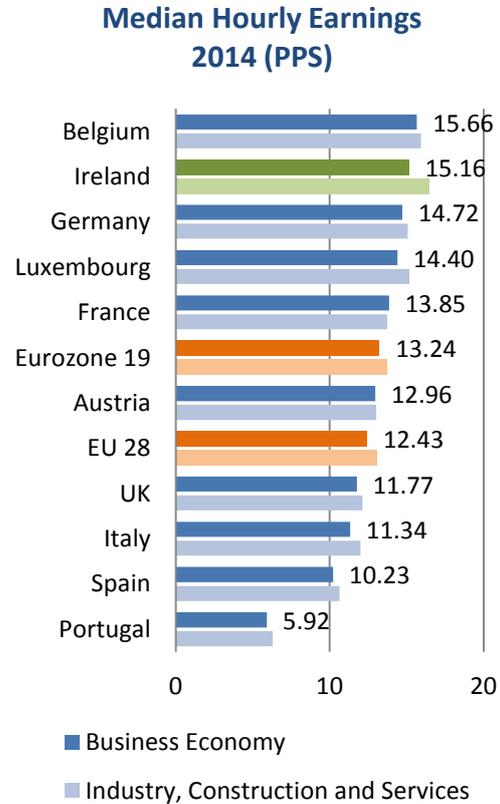
Median Hourly Earnings

Commentary on the level of wages in Ireland relative to those of other developed economies tends generally to be in the context of two separate debates; the standard of living Irish people enjoy relative to citizens in those countries and international cost competitiveness, which is particularly important for small open economies such as Ireland. Labour costs are one aspect of many in the decisions of multinationals on where to invest. Theoretically and holding all other considerations constant, cheaper inputs in the production of goods (labour in this case) translate into cheaper final products which can be sold in greater volumes. This impacts on GDP and should also impact on the standard of living in a country. It is important to note however that labour costs are not an appropriate proxy for the wider concept of international competitiveness though they are often presented as such, being just one facet of many. For instance, in two of the best performing traded sectors in Ireland, ICT and pharmaceuticals wages have consistently gone up post-crisis whilst they have stagnated or dropped elsewhere. Additionally, high labour cost economies such as Denmark and Japan are still considered competitive based on other metrics such as innovation and business culture. Labour costs are often a minor consideration in investment location decisions.

Median hourly earnings is the middle point of the hourly earnings distribution i.e. half of Irish wage earners fall below this rate and half sit above it. The rate as shown above is equalised with purchasing power, adjusting for the price of a typical 'basket' of goods in the respective country to compare international living standards. According to Eurostat's 2014 figures, Ireland has high *median hourly earnings* relative to our EU partners.

Median hourly earnings in *Industry, Construction and Services* (except public administration, defense and compulsory social security) in Ireland sit quite high in

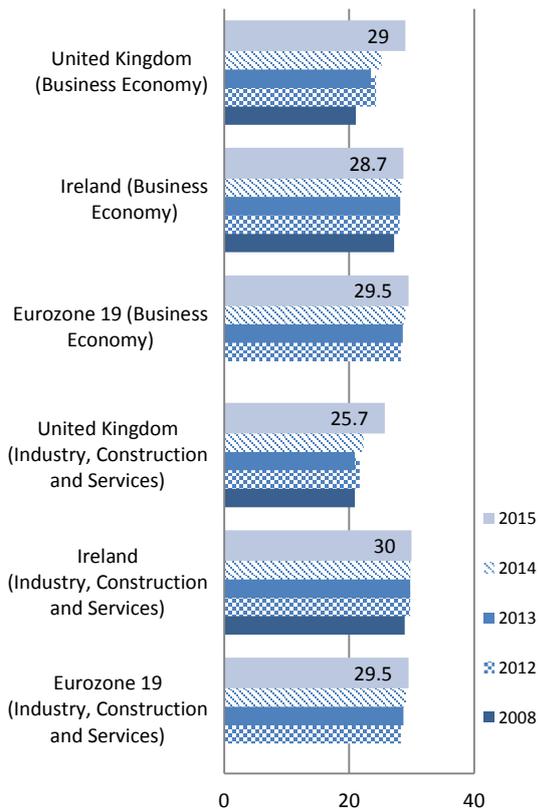
European rankings (2nd behind Denmark) at €16.49 an hour. This figure remained static from 2010-2014 whilst the Eurozone average rose by €1.20 an hour.



Irish workers *median hourly earnings* is lower relative to other member-states in the *Business Economy* which excludes earnings in areas like Education and Health sectors as well as in the arts and entertainment, coming in at 4th with 50% of Irish workers earning less than €15.16 an hour. In addition to Denmark, Sweden and Belgium also have a higher median hourly income in the *Business Economy*. Germany, Finland and Luxembourg have similar medians which are all within €1 an hour less than in Ireland. The Eurozone's average *median hourly earnings* is less than €2 below Ireland at €13.24. Between 2010 and 2014 the Irish median actually dropped by 20 cent an hour whilst the Eurozone average rose by €1.20.

In terms of international labour cost competitiveness *median hourly earnings* is not the measure multinationals would

Total Hourly Labour Costs



consider when weighing up the overall costs and benefits of investing in a given location as it does not include employers' compulsory social contributions (or available employee subsidies for that matter) which feed into the price of their products in international markets. Using this metric to compare labour costs with other countries overstates the relative costs of Irish employees to employers as social contributions are quite low in Ireland relative to other EU member-states. In addition, adjusting for purchasing power may be appropriate for some measures of living standards but it does not reflect the actual price a company has to pay for each hour of labour.

For the same reason that *median hourly earnings* is not the best proxy for labour cost competitiveness it is also lacking when it comes to measuring living standards; the measure ignores the higher social contributions most other member-states require employers to pay which fund social services for employees such as free GP

visits, supports in the case of being made unemployed or falling ill, for maternity benefit and pay-related old age pensions. The rate of *median hourly earnings* even when adjusted for purchasing power does not capture the higher price Irish workers have to pay for these services.

Labour Costs

A more appropriate measure of relative labour costs is *total hourly labour costs*. This measure adds the hourly employee compensation in wages/salaries to social security contributions and employment taxes subtracting any subsidies received for staff. It is calculated by dividing *total labour costs* in an economy by the number of hours worked in a year.

By some measures Ireland's average hourly labour costs rank around the middle of Eurozone members such as in *Industry, Construction and Services (except public admin, defense and compulsory social security)* which includes sectors such as Health and Education (€30 an hour compared to €29.50). In the *Business Economy*, Ireland is actually slightly lower than the Eurozone average (€29.50) and the UK (€29.00) in *total hourly labour costs* at €28.70 on average. This is significantly below other small open economies such as Belgium (€41.10) and Austria (€32.20).

In addition, Ireland's *relative* position in *total hourly labour costs* has been improving consistently against both the UK and Eurozone since the financial crisis. Whilst Ireland has kept these costs mostly static they have been growing in competing countries. Whilst in the *Business Economy* in the UK labour costs have increased by nearly €8 an hour since 2008 they have only risen by €1.50 in Ireland in the same period. Trends in *total hourly labour costs* in manufacturing (which includes the production of food; a labour intensive sector and key area in which Irish producers compete with the UK) have been similar between the two economies since 2012 where an almost €7 hourly gap has narrowed to just over €2 in that period. In 2015 the *total hourly labour costs* in

Actual Individual Consumption, Real Expenditure per capita (in PPS_EU28)

	2008	2009	2010	2011	2012	2013	2014	2015
Luxembourg	26,400	25,500	25,600	25,700	26,500	27,200	27,400	27,400
Germany	20,700	20,400	21,300	22,200	23,000	23,100	23,800	24,500
Austria	21,000	20,700	21,300	22,000	22,800	23,100	23,400	23,800
United Kingdom	21,600	20,200	20,600	20,800	21,400	21,300	22,000	22,800
Belgium	19,400	19,100	20,100	20,600	21,200	21,500	22,100	22,700
France	19,800	19,300	20,000	20,400	20,800	21,300	21,600	22,400
Eurozone 19	19,300	18,600	19,200	19,500	19,800	19,900	20,300	21,000
EU 28	18,000	17,400	18,000	18,300	18,700	18,800	19,200	20,000
Italy	19,300	18,600	19,500	19,600	19,300	18,800	18,900	19,700
Ireland	19,300	17,500	18,000	17,900	18,100	17,800	18,100	19,200
Spain	17,300	16,300	16,200	16,200	16,200	16,100	16,700	17,500
Portugal	15,800	14,900	15,500	15,000	14,800	15,200	15,600	16,500

manufacturing stood at €30.60 (Irl) to €28.20 (UK).

Actual Individual Consumption

Actual individual consumption is a measure (recently highlighted by Michael Taft in *Notes from the Front*) of all goods and services consumed by households (as opposed to purchased by households) including services provided by the government such as health and education and is converted to a common, technical currency ("Purchasing Power Standard" or PPS). According to Eurostat, 'AIC consists of goods and services actually consumed by individuals, irrespective of whether these goods and services are purchased and paid for by households, by government, or by non-profit institutions.....while GDP is mainly an indicator of the level of economic activity, (AIC) is an alternative indicator better adapted to describe the material welfare of households.'

Ireland is well below the Eurozone average in living standards according to this preferred measure and in fact is still below 2008 levels of individual consumption having been around the average for Eurozone members in 2008 (€19,200 down from €19,300 over seven years). The Eurozone average has risen significantly from €19,300 to €21,000 in this period. The figures for other small open economies such as Belgium and Austria have risen by

around 10% in this time whilst in the UK the level has risen by over 5%. *AIC* for the average German is now almost 20% higher than in 2008 (€24,500) and even other 'bailout' countries such as Spain and Portugal have seen slight rises in this period.

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