Private Sector Wages: Trends, Prospects and Issues

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1. Economic Trends

Global Trends

Global economic growth has weakened over the last year with slowdowns in the euro area, the United Kingdom (UK) and the United States (US). The OECD has downgraded its forecasts for 2020 and 2021 to just 3%. The advanced economies of the G7 are generally experiencing sluggish growth (see Table 1) with a particularly weak performance in Italy. The advanced economies are all characterised by low inflation but exhibit greater variation in terms of labour market performance. The unemployment rates in Germany, the UK and the US are all close to historic lows, whereas France and Italy have stubbornly high levels of unemployment.

Table 1: Snapshot of the major economies (G7 and China), %

	GDP (annual growth in real terms, Q3)	**Consumer prices** (annual growth in October)	**Unemployment rate** (October)
USA	2.1	1.8	3.6
China	6.0	3.8	3.6
Japan	1.3	0.2	2.4 (Sep)
Germany	0.5	1.1	3.1
UK	1.0	1.5	3.8
France	1.3	0.8	8.5
Canada	1.6	1.9	5.5
Italy	0.3	0.2	9.7

The slowdown is partially a natural function of a maturing business cycle. The global upswing must eventually peter out. The slowdown also reflects a number of specific factors. Most notable is the unusually elevated levels of policy uncertainty related to Brexit and to future global trading conditions. This policy uncertainty, in conjunction with rising trade barriers, remains a constraint on private investment and on traded goods. In addition, the Chinese economy is transitioning to a more mature phase of development, which will be characterised by lower rates of growth.

Of even greater concern is that advanced economies are enduring a sustained period of low productivity at a time of ageing demographics. Recent years have seen persistently low levels of investment in the productive capital stock in many advanced economies. This has negative implications for productivity growth over the medium-term.

Republic of Ireland Trends

The Republic of Ireland's headline real GDP grew by 6.6% per cent annually in the first half of 2019. The outsize impact of a small number of large multinationals continues to distort the headline GDP data. The more useful 'modified domestic demand' indicator which strips out intellectual property investment and purchases of aircraft by leasing companies grew by a more modest 2.3% in the first half of 2019.

The domestic Irish economy's long cyclical upswing appears to be slowing down somewhat, although labour market conditions continue to improve. The CSO estimate that the unemployment rate fell to 4.8% in November, with unemployment down over 17,600 compared to the previous year. Long-term unemployment is down to 1.4%, while annual employment growth was a healthy 2.4% in the third quarter of this year. Despite the labour market improvements there is only limited evidence that the economy is overheating (see Table 2).

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While there are notable downside risks to the economy - including Brexit and a possible deterioration in global trading conditions – we project a continuation of growth in economic output and employment in 2020. The tightening labour market should support robust growth in real wages next year. Indeed real average hourly wage growth should comfortably exceed 2% in 2020. Inflation will remain subdued despite upward pressure from wage growth and aggregate demand.

Table 2: Is the economy overheating? – A simple dashboard

Indicator	Question	Comment
Unemployment rate (UR)	Is it falling and below the long-term average?	Yes but the UR is higher than in the UK, Germany and US. Ireland ranks just 13th in the EU
Employment rate (ER)	Is it rising and above the long-term average	Yes but employment rate (20-64) was just 16th in the EU in 2018, 8.5pp behind Sweden (74.1 vs. 82.6) – job vacancy rate is 5th weakest of 25 EU countries
Consumer prices	Is it rising and above the long-term average?	No – CPI has increased by an annual average of 0.3% over nine years and is currently 0.7%
Property prices	Is the growth rate faster than the long-run average?	No - Annual property price increases softened to 1.1% in September and are just 83% of peak
Wage inflation	Is the growth rate faster than the long-run average?	Yes. Hourly earnings are up 4.0% annually (weekly wages were up 3.4%). However, this follows a long period of stagnation
Growth in underlying investment	Is it growing faster than the long-run average?	No – 0.5% decline in first half of 2019 and housing completions are well below the level of household formation
Underlying investment rate	Is it rising and above the long-run rate as a percentage of modified output?	Mixed. Rate was a sustainable 20.5% in 2018

Private consumption	Is it growing faster than the long-run average?	Yes – real annual growth of 2.8% in first half of 2019 follows four consecutive years of over 3% growth
Growth in private sector credit	Is it growing faster than the long-run average?	Mixed – lending to the private sector is growing at 1.2% on an annual basis - lending for house purchases was up 1.5% annually in July
Current account balance (CA)	Is it negative and deteriorating?	No – modified current account balance was in surplus in 2018. CA has moved sharply negative in 2019 reflecting on-shoring of IP assets
Savings rate (SR)	Is it falling and below the long-run average?	No – SR of households is rising and well above the long-run average at 10.1% in the second quarter

2. Trends in Employment and Unemployment

Employment rose by 17,000 (0.8%) in the third quarter of 2019 (Q3) and was up 54,000 (2.4%) over the previous year. The rate of expansion is slowing but remains well above long-term norms. Sectoral job trends are shown in Table 3.

Even so, the employment rate is below the EU average. The total employment rate for the core 20 to 64 years cohort in 2018 was 74.1% in the Republic of Ireland. This rate ranked 16th in the EU. The rate peaked at 75.1% in 2007 before falling to 64.5% by 2012. The best performer in the EU is Sweden at 82.6% (Iceland is at 86.5%), while the worst performer in the EU was Greece at 57.8%. The UK, at 78.7%, also outperformed the Republic. Achieving Swedish employment rates would mean employment growth of 11.5% assuming no increase in the size of the labour force. This may suggest significant potential slack in the Irish labour market.

The seasonally adjusted unemployment rate was 4.9% in Q3. The long-term unemployment rate halved between the third quarter of 2017 and the third quarter of 2019, both in percentage terms (2.7% to 1.4%) and in raw numbers (64,800 to 34,900). However, the youth unemployment rate was 14.8% in September. The South-East is the poorest performing region with an unemployment rate of 7.3%. Dublin has the lowest unemployment rate at 4.5%. Regions with tighter labour markets can expect faster wage growth in 2020.

The long term unemployment rate halved between the third quarter of 2017 and the third quarter of 2019

The Republic's seasonally adjusted rate of 4.8% in October ranked just 13th in the EU. There is a wide spectrum of national labour market performances performance in the EU ranging from lows of 2.2% unemployment in Czechia and 3.1% in Germany, to a high of 16.7% in Greece.

The sheer range of national employment and unemployment rates suggests there may not be natural or 'normal' rates. Rather, equilibrium employment and unemployment rates are likely to reflect the underlying labour market structures, barriers and constraints within national economies. This implies a role for activist policy. It also implies that traditional rules of thumb about full employment lying at some threshold like 4% may be fundamentally misguided. The generalised strengthening of the labour market since 2012 is consistent with sectoral and regional specific tightness, for example in the ICT sector and in the Dublin region. Even so, the Republic's relatively low job vacancy rate suggests there is some remaining slack.

Table 3: Sectoral job trends – A heat map

	2008Q3	2018Q3	2019Q3	19/08 (% change)	19/18 (% change)
Agri, forestry, fishing	111.2	104.8	99.6	-10.4	-5.0
Industry	306.9	279.6	289.0	-5.8	3.4
Construction	201.7	145.8	149.3	-26.0	2.4
Wholesale/retail	323.7	301.5	301.8	-6.8	0.1
Transport/storage	92.4	101.8	104.4	13.0	2.6
Accommodation/food	139.2	178.8	174.6	25.4	-2.3
ICT	87.6	122.1	128.4	46.6	5.2
Financial, insurance and real estate	109.7	100.2	113.1	3.1	12.9
Professional/sci/tech	124.9	135.9	134.3	7.5	-1.2
Admin and support	93.9	105.6	109.6	16.7	3.8
Public admin and defence	99.0	104.9	115.2	16.4	9.8
Education	143.1	173.7	186.8	30.5	7.5
Health/social work	238.5	281.5	290.8	21.9	3.3
Other	112.6	122.0	119.0	5.7	-2.5
All sectors	2191.1	2263.4	2317.0	5.8	2.4

3. Private sector wage and labour cost trends

Table 4 and Table 5 show private sector (business economy) wage and labour cost trends in the Republic and in comparator economies. Wage growth trailed that of the UK in each of the five years from 2013 to 2017 and trailed the EU in four of those years. However, Irish wage growth exceeded the comparators in 2018 and the faster wage growth is likely to have continued in 2019. The Irish economy recovered more slowly in the wake of the 2008 economic crash and is now experiencing catch-up growth in output, employment and wages.

Table 4: Labour cost index, % change, business economy

Labour Costs	2013	2014	2015	2016	**2017**	**2018**
EU	1.0	1.6	2.0	1.5	2.6	2.7
Ireland	0.9	0.6	0.8	1.8	2.2	3.1
UK	1.1	1.5	4.2	1.5	3.1	3.3
Germany	0.4	2.5	2.5	2.2	3.4	2.1

Table 5: Wages, % change, business economy

Wages	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
EU	1.3	1.6	2.3	1.6	2.6	2.8
Ireland	0.6	1.0	0.8	1.7	2.2	3.4
UK	1.0	1.6	3.8	1.8	2.7	3.0
Germany	1.1	2.2	2.5	2.1	3.2	2.4

Table 6 and Table 7 compare labour costs and wage rates in the business economy for a selection of countries. Average Irish hourly labour costs (€30.50) are below the EU15 average and significantly trail a number of high-income peer countries including Denmark (€44.70), Sweden (€39.30) and Germany (€35.00). The UK is the only high-income (i.e. GDP per capita greater than €30,000) EU country with cheaper labour costs than the Republic. The Republic is above the EU15 average in terms of hourly wages but does have lower average wages than Germany, Sweden and Denmark.

Table 6: Labour costs in the EU15 and selected countries, €

Labour costs	2016	2017	2018
EU 15	29.9	30.6	31.4
Ireland	29.0	29.6	30.5
UK	26.7	25.7	26.3
Germany	33.1	34.2	35.0
Denmark	42.8	43.9	44.7
Sweden	40.8	41.2	39.3

Table 7: Wages in the EU15 and selected countries, €

Wages	2016	2017	2018
EU 15	23.0	23.5	24.0
Ireland	24.5	25.1	25.9
UK	22.4	21.5	21.9
Germany	26.0	26.8	27.5
Denmark	37.2	38.0	38.8
Sweden	27.6	27.7	26.5

Average weekly wages in the private sector stagnated in the private sector between 2008 and 2015 but have been increasing by an annual average of 3% since the third quarter of 2015. Average weekly earnings were €708.24 in the third quarter of 2019 and were up 3.9% over the previous year. Average hourly wages also began to accelerate in 2015 and have increased 10.5% in the last four years including 4.7% between third quarter 2018 and third quarter 2019. Average hourly wages are now €21.69 in the private sector.

At the same time, inflation has remained subdued. The Consumer Price Index (CPI) has increased just 1.8% over the last five years and was up 0.7% in October. As such, real average hourly earnings in the private sector are now increasing by close to 4% over the previous year and real average weekly earnings are in excess of 3% (see Table 8).

Table 8: Wage data, third quarter 2019, €

	Weekly Earnings	Annual Growth, %	Hourly Earnings	Annual Growth, %	CPI, Annual Growth, %
All	768.14	3.4	23.53	4.0	0.7
Private Sector	708.24	3.9	21.69	4.7	0.7

Average private sector earnings are below the average for the public sector. However, the private sector has had faster earnings growth in recent years. The top seven performing sectors over the last five years from a wage growth perspective are all in the private sector (see Table 9).

Table 9: Average hourly earnings by economic sector (seasonally adjusted), €

	2014Q3	2018Q3	2019Q3	14-19 %	18-19 %
All NACE economic sectors	**21.69**	**23.16**	**24.05**	**10.9**	**3.8**
Mining and quarrying (B)	23.23	24.52	23.25	**0.1**	**-5.2**
Manufacturing (C)	21.79	22.78	23.11	**6.1**	**1.4**
Construction (F)	19.15	21.16	21.83	**14.0**	**3.2**
Wholesale and retail (G)	17.21	18.54	20.01	**16.3**	**7.9**
Transportation and storage (H)	20.32	22.92	23.18	**11.4**	**1.1**
Accommodation and food (I)	12.12	13.00	13.57	**12.0**	**4.4**
ICT (J)	28.33	32.50	34.37	**21.3**	**5.8**
Financial and insurance (K)	29.52	33.02	33.89	**14.8**	**2.6**
Real estate activities (L)	17.81	23.21	23.33	**31.0**	**0.5**
Professional, sci & technical (M)	24.38	26.91	27.31	**12.0**	**1.5**
Admin and support service (N)	16.32	18.16	19.17	**17.5**	**5.6**
Public admin and defence (O)	25.51	25.87	26.12	**2.4**	**1.0**
Education (P)	32.62	35.81	36.76	**12.7**	**2.7**
Human health (Q)	22.18	22.88	23.59	**6.4**	**3.1**
Electricity, water and waste (D,E)	27.58	29.13	29.30	**6.2**	**0.6**
Arts, entertainment (R)	17.08	17.94	19.32	**13.1**	6.7

Pay Comparison

€13.57
per hour

Accommodation and food

€20.01
per hour

Wholesale & Retail

€36.76
per hour

Education

There are significant differences in pay between the various occupational categories. The managerial and professionals category earned €1,297.89 per week in the second quarter of 2019. This was more than double the weekly earnings for clerical, sales and service employees (€519.01) and production, transport, craft and other manual workers (€556.13). The professional category has also had the fastest growth in wages (15.1%) over the last five years.

An important point is that the average worker does not earn the 'average' or mean level of earnings. It is the median level of earnings that actually represents the wage of the average worker. This is important because median weekly earnings in 2018 were just €592.60, or 80% of mean earnings (€740.72). Indeed 63.5% of workers earn less than the mean.

The private sector median was even lower at €523.25. Thus the average private sector worker has annual earnings of just €27,209. The median for 18-24 year olds was just €294.15 per week. Overall, 28.7% of workers earn less than €400 per week – a percentage that rises to 68.7% in accommodation and food services and 43.9% in wholesale/retail. Finally, the economy-wide median for women (€517.62) is just 78% of male earnings (€659.58), while 25.7% of women earn less than €300 per week.

4. Prospects for wages

Wages are determined as part of a bargaining process and a number of factors feed into this process. These include A) output prices, B) consumer prices, C) the tax wedge, D) the unemployment rate (and other indicators of labour market tightness), E) labour productivity and F) a range of other factors including trade union density and collective bargaining coverage.

The most recent collection of institutional forecasts for wage growth in 2020 is ranging from a low of 3% to a high of 4.5%. The low of 3% is a Department of Finance estimate of compensation per employee based on an assumption of a no-deal Brexit. The European Commission projects growth in compensation per employee of 3.7% while the Central Bank projects 4.2% on the assumption of a Brexit deal. The ESRI projects growth in average hourly earnings of 4.5%, while the NERI projects growth of 3.9%.

The strong outlook for wage growth reflects the increasing tightness of the labour market

The strong outlook for wage growth reflects the increasing tightness of the labour market although in practice the often significantly different regional, sectoral and firm specific contexts will mean significant differences in regional and sectoral wage growth.

The long-run sustainable path for wage growth will depend on future developments in price inflation and labour productivity. Historically labour productivity ranges between 1% and 1.5% over the medium-term. The European Central Bank has an inflation target of just below 2% (though actual inflation has been consistently below the official target in recent years). This suggests sustainable medium-term wage rises of between 2.9% and 3.4%.

However, this assumes that the labour share adequately compensates the economic contribution of labour. Labour shares have been declining in many advanced economies over the last forty years. This phenomenon has also occurred in the Republic of Ireland. Falling labour shares drive inequality. To reverse this trend of declining labour share and rising market inequality it will be necessary for labour compensation per hour to exceed the medium-term average sum of inflation and labour productivity. This suggests a medium-term wage target of 3.5% or higher.

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