

World Economic Trends II

<The 2017 Autumn/Winter Report>

- Study of Possible Factors Weighing Down on Wage Growth in Major Developed Economies in Europe and the U.S. -

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Cabinet Office
Government of Japan

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About "The Trend of the World Economy"

In place of the White Paper on the World Economy (Annual Report on the World Economy), published on an annual basis from 1958, the semi-annual report has been issued since 2002. This is the 32nd issue.

Chapter 1 Slow wage growth in major developed economies in Europe and the U.S.

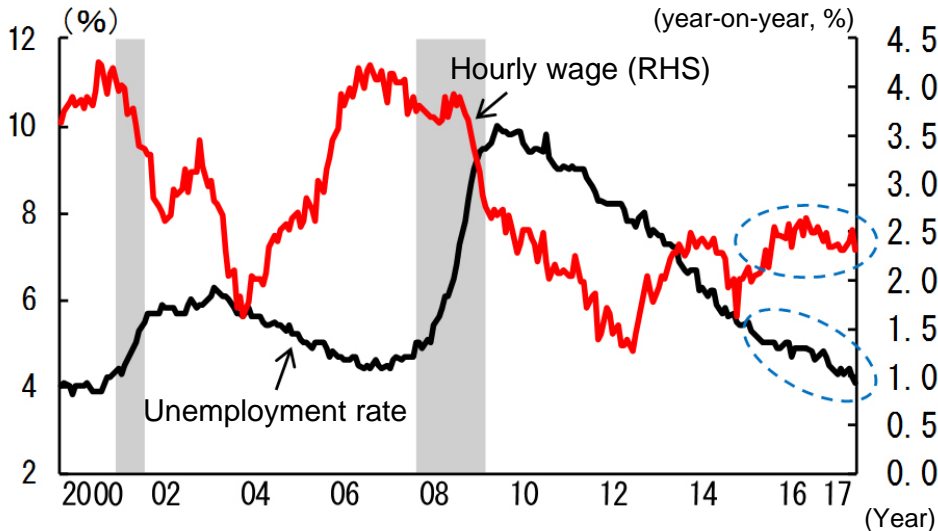
(Trends of unemployment rate and wage in the U.S. and the Eurozone)

- In the U.S., the unemployment rate has been falling steadily and it's a historic low level. In the past phases of economic expansion, the nominal wage made some 3 or 4% growth on a year-on-year basis, while it is growing by a mere 2.5% in the current phase (Figure 1).
- In the Eurozone, the unemployment rate has been above the level immediately before the Financial Crisis, though falling down steadily. In the phases of expansion before the Crisis, the nominal wage made some 2 to 4% growth on a year-on-year basis, while it is growing by 1 to slightly more than 2% at most in the current phase (Figure 2).

(Factors weighing down on wage growth)

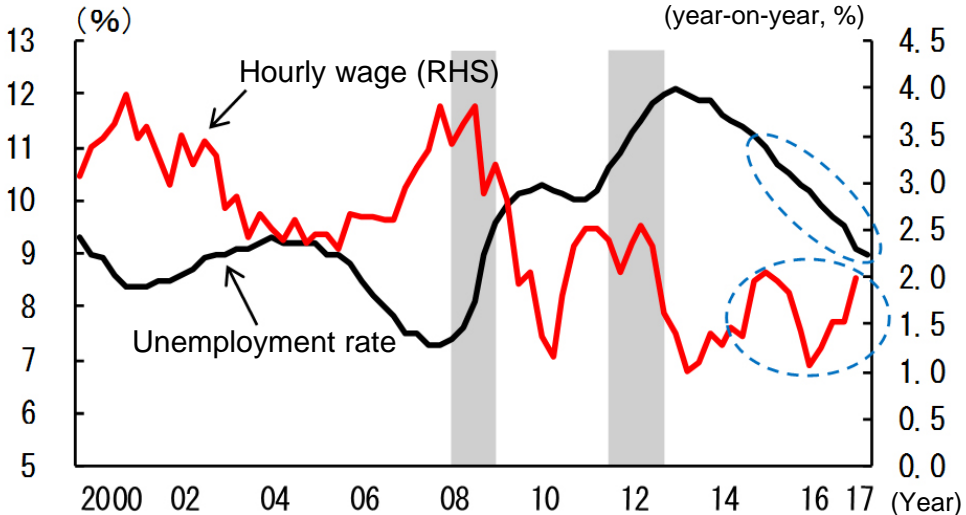
- Among possible factors weighing down on wage growth in major developed economies in Europe and the U.S. are: (1) Labor market slack (Looser balance between supply & demand for labor); (2) Slower growth rate of labor productivity; (3) Weaker bargaining power of workers for wage increase; and (4) Lower inflation expectations.

Figure 1 Changes in unemployment rate and nominal wage growth in the U.S.



(Note) 1. Adapted from U.S. Department of Labor
 2. Shaded are phases of recession & depression.

Figure 2 Changes in unemployment rate and nominal wage growth in the Eurozone

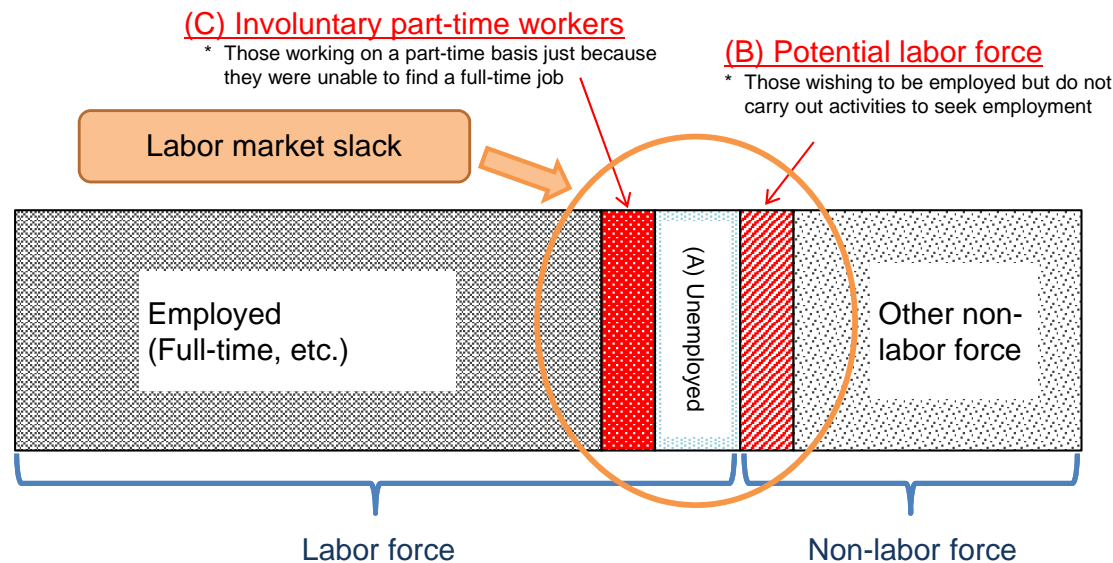


(Note) 1. Adapted from Eurostat & OECD. Stat.
 2. Shaded are phases of recession & depression.

(Factors weighing down on wage growth: 1. Labor market slack)

- Any slack in the labor market cannot be fully detected solely on the basis of the unemployment rate. This is because, in addition to (A) unemployed people (those out of employment who are carrying out active job search), there are other types of underutilized labor force, such as (B) potential labor force (those wishing to be employed but do not carry out activities to seek employment) and (C) involuntary part-time workers (those working on a part-time basis just because they were unable to find a full-time job) (Figure 3).
- Any greater slack than assumed solely on the basis of the unemployment rate which is caused by these types of underutilized labor force would hinder wage growth.

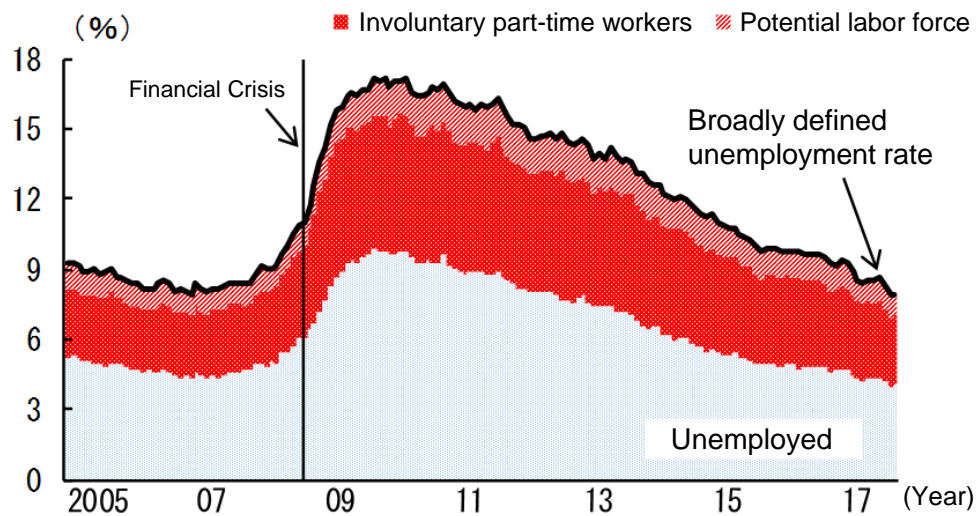
Figure 3 Labor market slack



(Factors weighing down on wage growth: 1. Labor market slack - 1)

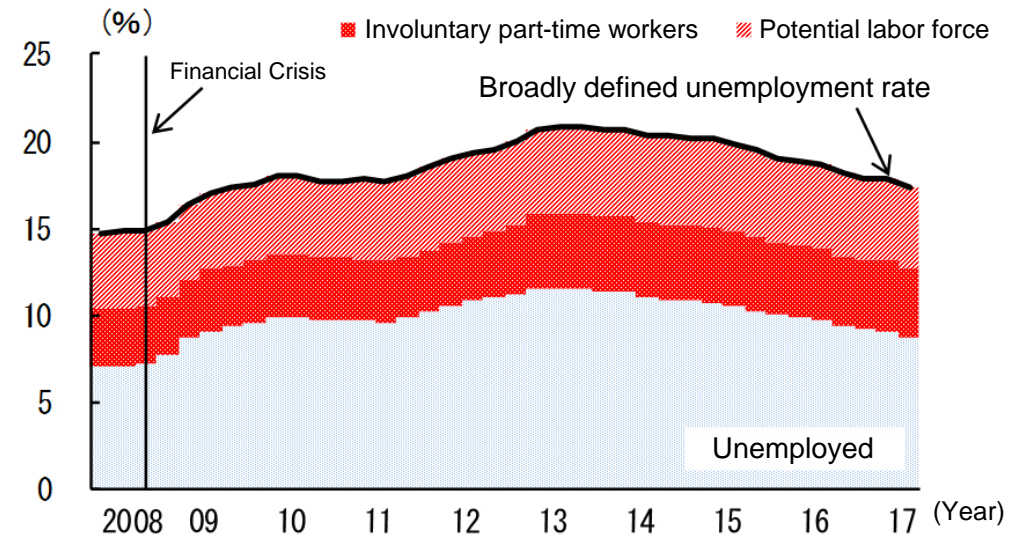
- In the U.S., the current level of broadly defined unemployment rate (8.0%) is almost the same as the lowest level immediately before the Financial Crisis (7.9%) (Figure 4).
⇒ The slack in the labor market is shrinking.
- In the Eurozone, the current level of broadly defined unemployment rate (17.3%) is higher than the lowest level immediately before the Financial Crisis (14.7%) (Figure 5).
⇒ The slack in the labor market remains.

Figure 4 Broadly defined unemployment rate in the U.S.



(Note) Adapted from U.S. Department of Labor

Figure 5 Broadly defined unemployment rate in the Eurozone

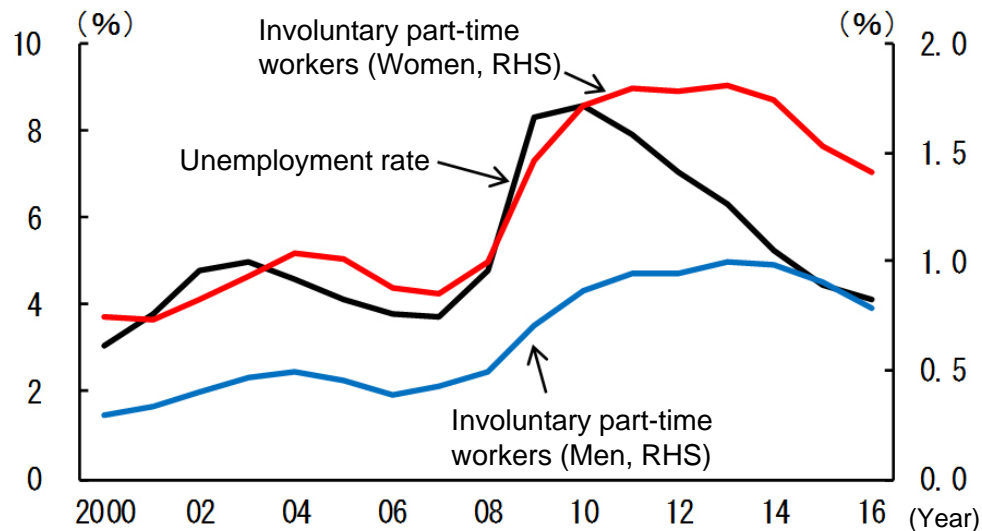


(Note) Adapted from Eurostat

(Factors weighing down on wage growth: 1. Labor market slack - 2)

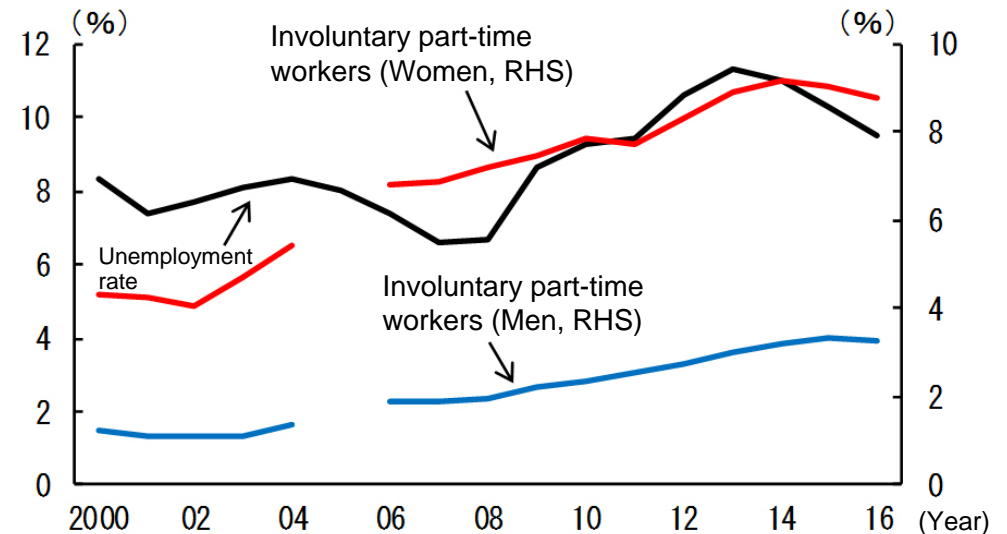
- After the Global Financial Crisis, the unemployment rate and the share of involuntary part-time workers among the labor force (ratio of involuntary part-time workers) rose sharply.
- In the U.S., the unemployment rate started to fall in 2011, before the ratio of involuntary part-time workers declined in 2014, both among the men and women (Figure 6). In the Eurozone, the unemployment rate started to fall in 2014, and so did the ratio of involuntary part-time workers in 2015 and 2016 among the women and men, respectively (Figure 7).
- The ratio of involuntary part-time workers tends to start falling several years after a decline in the unemployment rate, leaving some slack in the labor market for the time being.
- The slack seems to be shrinking in the U.S. while it seems to remain in the Eurozone.

Figure 6 U.S.: Unemployment rate and the ratio of involuntary part-time workers (prime-age)



(Note) 1. Adapted from U.S. Department of Labor and OECD.Stat
 2. Rates of unemployment and involuntary part-timers aged 25 - 54

Figure 7 Eurozone: Unemployment rate and the ratio of involuntary part-time workers (prime-age)



(Note) 1. Adapted from Eurostat
 2. The data of the ratio of involuntary part-timers for 2005 is missing.
 3. Rate of unemployment aged 25 - 54, and ratio of involuntary part-timers aged 25 - 59

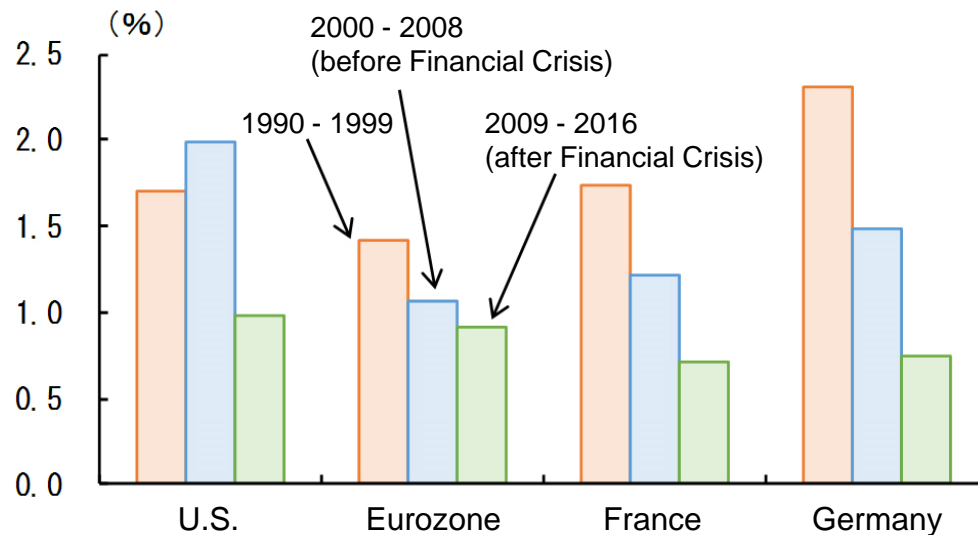
(Factors weighing down on wage growth: 2. Growth rate of labor productivity growth)

- Higher labor productivity would enable companies to raise wages. But in major developed economies in Europe and the U.S., the labor productivity growth rate is on a long-term downward trend (Figure 8).

(Factors weighing down on wage growth: 3. Weaker bargaining power of workers for wage increase)

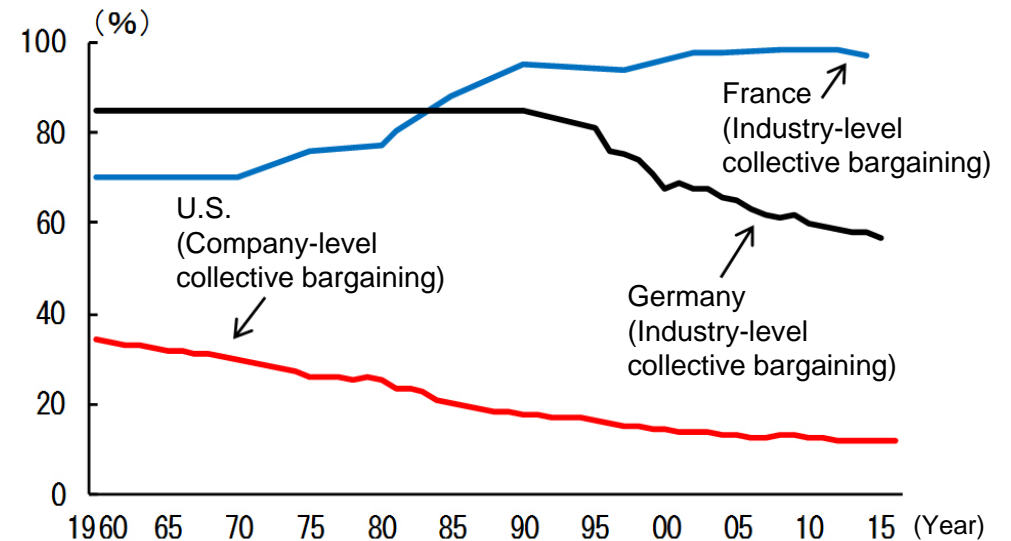
- The collective bargaining coverage rate, the ratio of workers covered by a labor agreement concluded through collective bargaining, is low in the U.S., where collective bargaining is conducted primarily at the company level while it is high in Germany and France, where they are mainly conducted at the industry level (Figure 9). In the U.S., workers are losing bargaining power on wages while labor unions in Germany and France maintain greater influence.

Figure 8 Growth rate of labor productivity



- (Note) 1. Adapted from OECD.Stat.
2. The figure for the Eurozone between 1990 and 1999 is the mean between 1996 and 1999.

Figure 9 Collective bargaining coverage rate

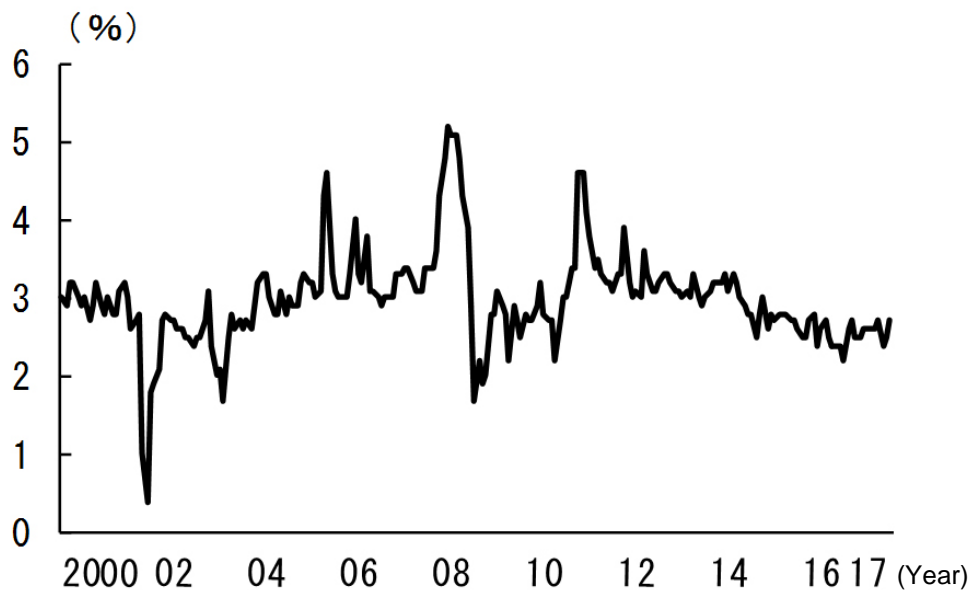


- (Note) 1. Adapted from OECD.Stat.
2. The collective bargaining coverage rate refers to the number of workers covered by a labor agreement concluded through collective bargaining divided by the total number of workers.

(Factors weighing down on wage growth: 4. Lower inflation expectations)

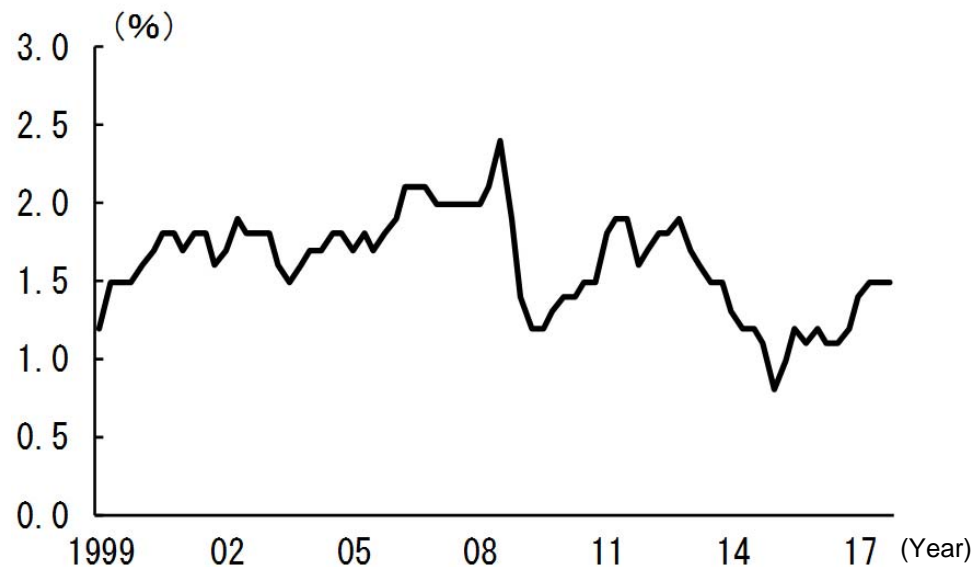
- In the U.S., inflation expectations indicate a long-term downward trend, as the expected rate of inflation remains below 3% in late 2017 (Figure 10).
- Also in the Eurozone, inflation expectations tend to fall in the long term. Despite picking up from 2015, the expected rate of inflation remains around 1.5% in 2017 (Figure 11).

Figure 10 Expected rate of inflation in the U.S. (one year)



(Note) Adapted from Michigan University

Figure 11 Expected rate of inflation in the Eurozone (one year)



(Note) Adapted from the ECB Survey of Professional Forecasters.

(Factors weighing down on wage growth: What are common and different factors between Europe and the U.S.)

- In major developed economies in Europe and the U.S., wage growth rate has recently been weighed down on by a combination of factors, the degree of influence by each factor differs between countries and regions (Figure 12).
- Common to the U.S. and Eurozone are slower growth of labor productivity and lower inflation expectations. In addition, weaker bargaining power of workers for wage increase in the U.S. and slack in the labor market in the Eurozone have some influence.
- What is required for wage increases include:
 - (1) Policy measures for raising labor productivity; and
 - (2) For countries and regions with the slack, active labor market policies (support for job seekers, vocational training, etc.)

Figure 12 Factors weighing down on wage growth (Summary)

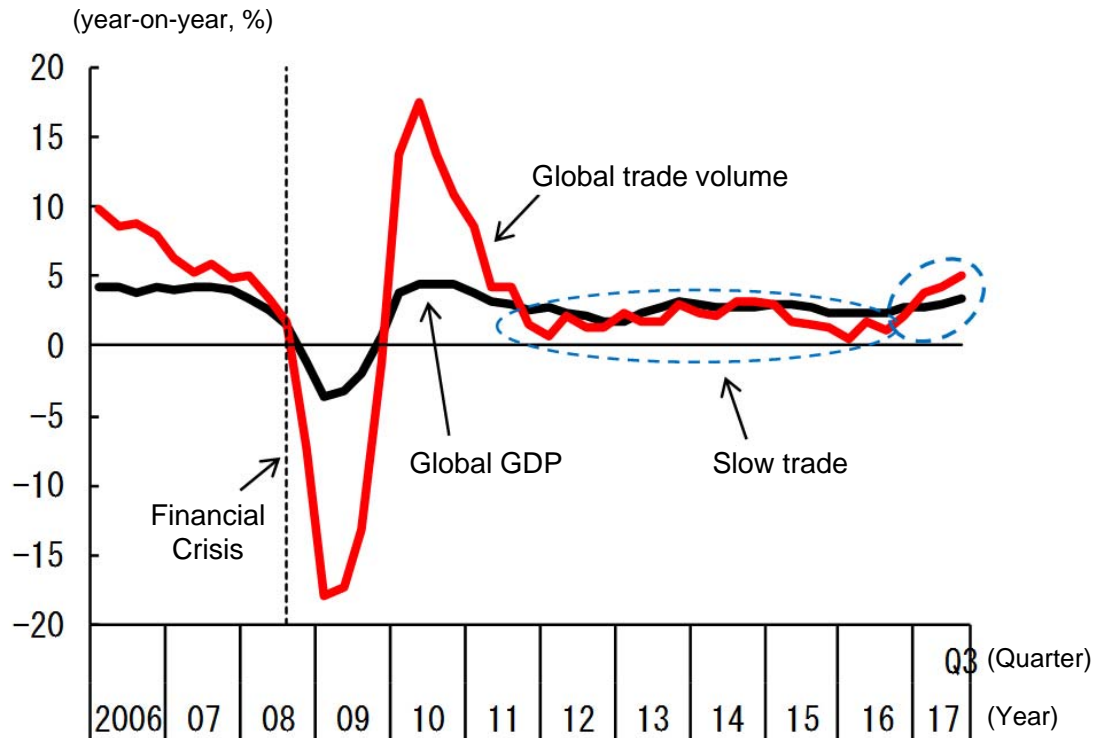
	U.S.	Eurozone	
(1) Labor market slack	Slightly influential	Influential to a degree	
Broadly defined unemployment rate Ratio of Involuntary part-time workers	Almost same as in 2007 Slightly higher than in 2007 Declining recently	Higher than in 2008 Higher than in 2007 Slightly declining recently	
(2) Slower growth rate of labor productivity	Influential to a degree	Influential to a degree	
Labor productivity growth rate (1971 -)	Declining	Declining	
(3) Weaker bargaining power of workers for wage increase	Influential to a degree	Germany: Slightly influential	France: Not influential
Coverage of collective bargaining (1960 -)	Declining	Declining	Increasing
(4) Lower inflation expectations	Influential to a degree	Influential to a degree	
	Long-term downward trend	Long-term downward trend	

Chapter 2 Economic Trends and Structural Changes in Major Regions

(World economy: Economies around the globe are recovering simultaneously.)

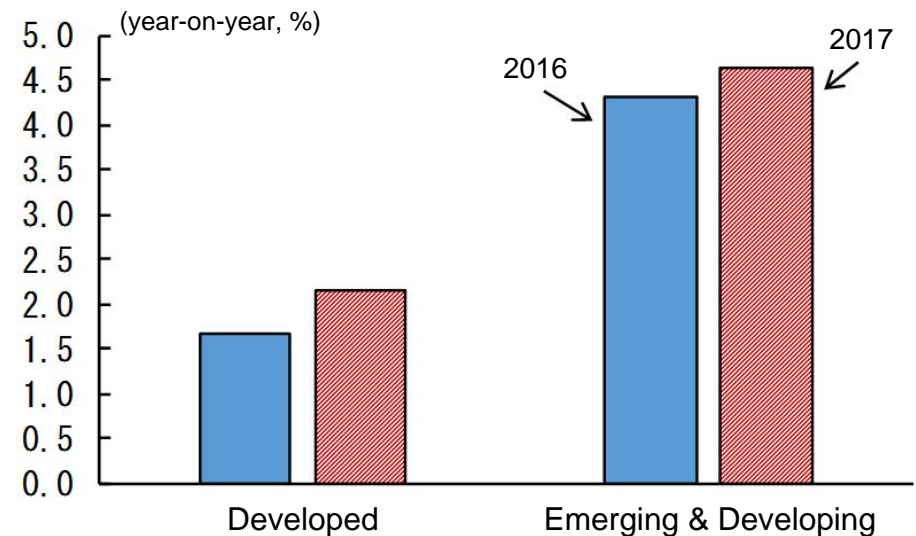
- The world economy has been recovering moderately, with expansion of trade volume (Figure 13). Since 2011, a few years after the Financial Crisis, global trade volume had been growing at lower rate than that of the world economy (so-called "slow trade"). In 2017, trade volume grew faster than global GDP.
- Behind this reversal lies faster growth in 2017 than in 2016 both in developed and emerging & developing countries, a synchronised recovery of global economies (Figure 14).

Figure 13 Global trade and production volume



(Note) Adapted from World Bank, and Netherlands Bureau for Economic Policy Analysis (CPB)

Figure 14 Growth rate of developed and emerging & developing economies



(Note) Adapted from IMF "World Economic Outlook Database, October 2017"

(European economy: Factors behind the difference in economic growth between Spain and Italy)

- Spain, hit as heavily as Italy by the Global Financial Crisis and the European debt crisis, sees its current economic growth faster than Italy's. One of the factors that caused the difference is their capital spending.
- Italy's slower actions to deal with bad debt of banks, and their consequent lending conditions, held back capital spending (Figure 15).
- Another factor that discouraged Italian companies from capital spending is their larger indebtedness than Spanish (Figure 16).
- Differences were also observed between the two countries in quality of labor, capital spending in IT for higher productivity, competitiveness in export, and composition of companies (the number of small companies, businesses allowed to operate with lower productivity, etc.), likely to reflect different growth potentials between them.

Figure 15 Supply & demand of funds in major Eurozone economies: Lending conditions of banks

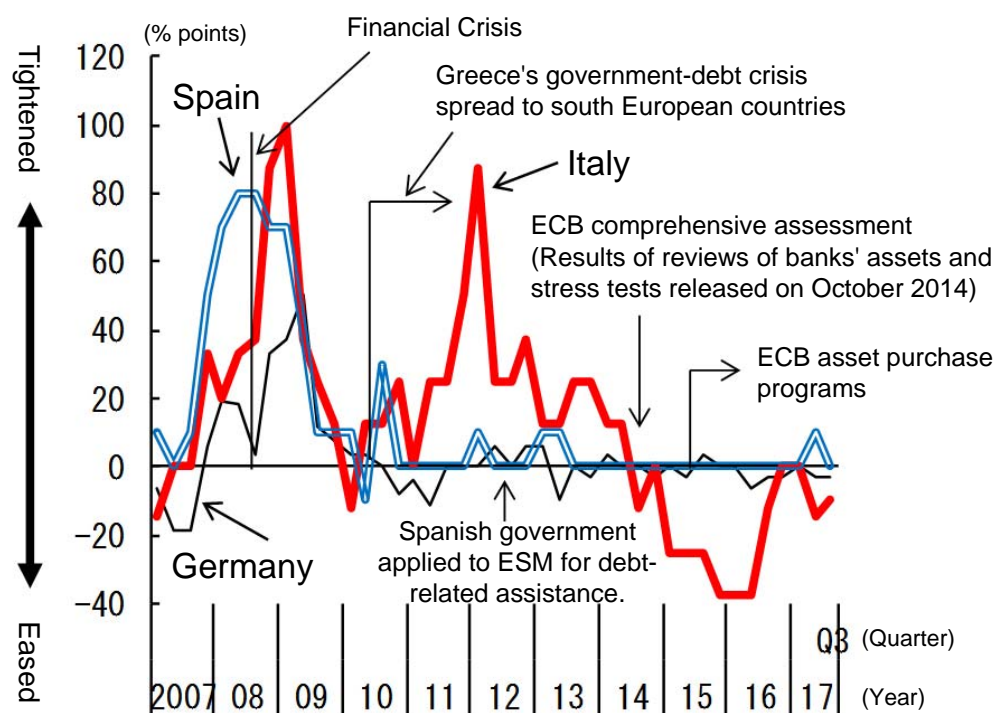
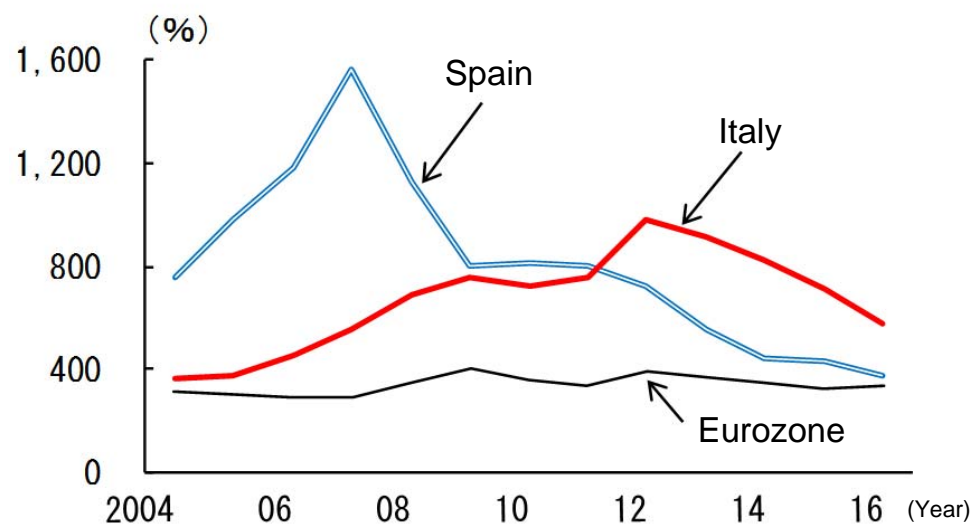


Figure 16 Debt / income ratio of non-financial companies in the Eurozone and selected economies



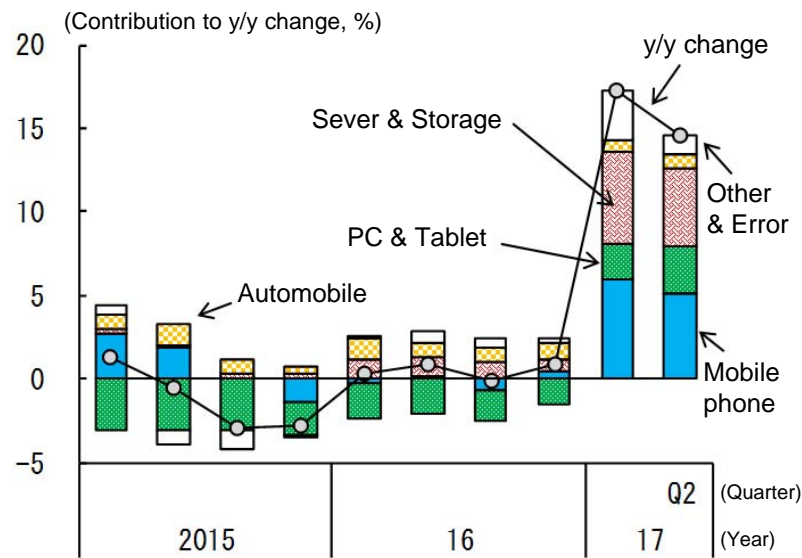
(Note) Adapted from Eurostat

- (Note)
1. Adapted from the European Central Bank
 2. To calculate lending conditions, companies were asked about changes in standards for approval of loans and credit lines for them over past three months. The percentages of those responding "Tightened significantly," "Tightened somewhat," "Eased considerably" and "Eased somewhat" are multiplied by 1, 0.5, -1, and -0.5, respectively, before totaled up.
 3. The latest survey was conducted between September 15 and October 2, 2017. It covered 134 banks (99% of which responded).

(Asian economy: Export and production of electric components in Korea and Taiwan)

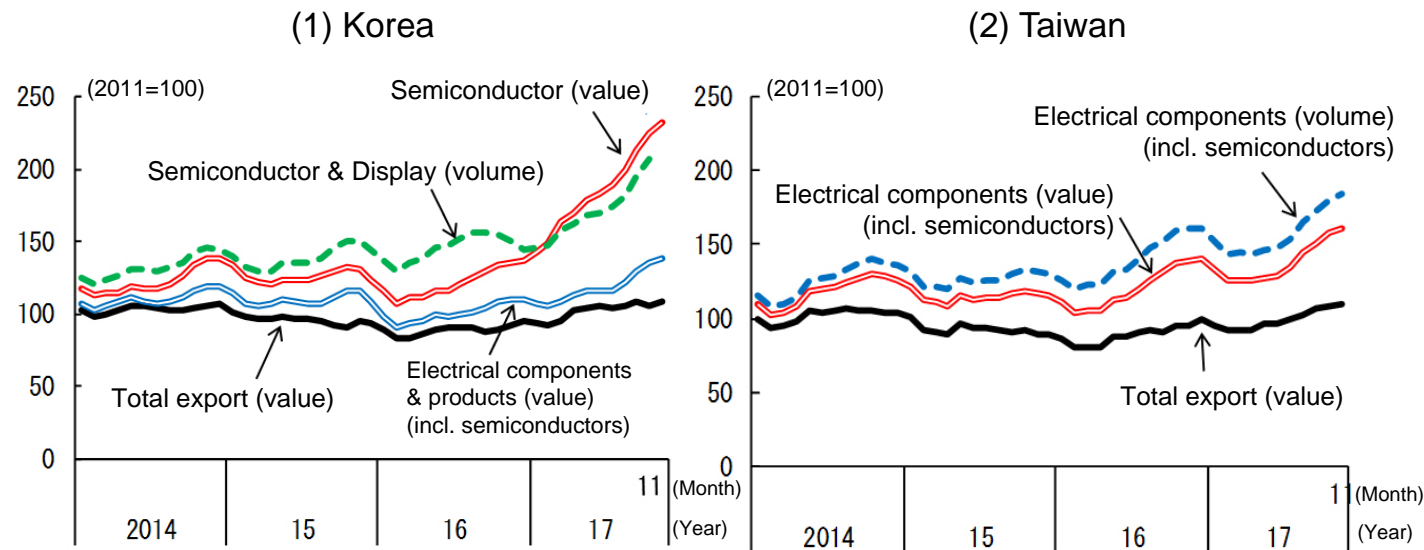
- Global sales of semiconductor exhibited a sharp increase in 2017, led mainly by growing demand for semiconductors used for mobile phones and servers as they are getting larger in storage and more sophisticated in functionality (Figure 17).
- Semiconductors and other electronic component industries make up an important part of the economy in Korea and Taiwan. With the growth of global semiconductor market, exports has increased mainly for electronic components and industrial production also has picked up in both economies. Especially in Korea, major supplier of memory ICs, exports of semiconductors has increased remarkably amid growing demand for memory ICs used for mobile phone and servers and rising its price due to the tight supply and demand balance (Figure 18).

Figure 17 Sales of semiconductors by final product



(Note) Adapted from Bloomberg

Figure 18 Exports of semiconductors and other electric components in value and volume



(Note) 1. Adapted from The Korea Customs Service and The Bank of Korea
2. 3-month moving average

(Note) 1. Adapted from the Taiwanese Ministry of Finance
2. 3-month moving average