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Economic News

WAGE DEMANDS IN THE METAL AND ELECTRICAL INDUSTRY

“There’s more at stake”

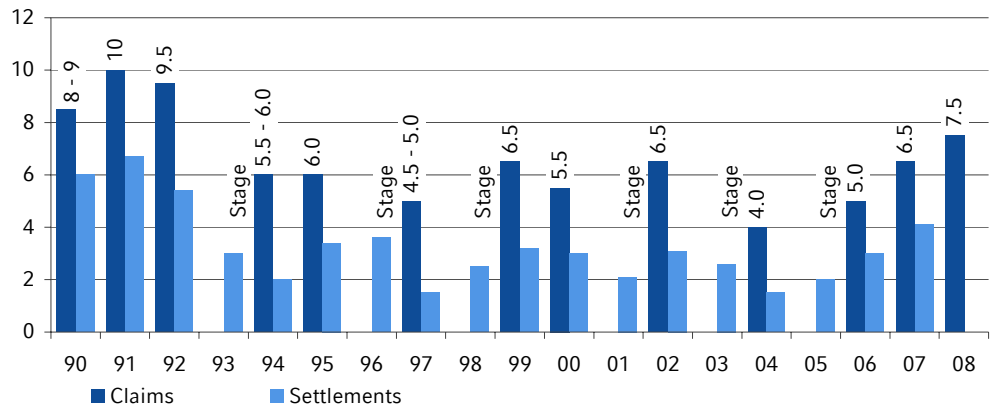
The German metalworkers’ trade union IG Metall is expected to go into collective bargaining negotiations beginning in October with the highest wage hike demand since 1992. We believe that the union’s pay increase demand for the 3.6 million employees in the metal and electrical industry will not exceed the 4.1% settlement agreed in the previous wage round. Despite the comparatively high wage agreement considering the gloomy economic outlook, risks to price stability are likely to be held in check. Consequently, inflation pressures should ease again as crude oil and commodities prices start declining.

- For the upcoming wage bargaining, the IG Metall executive board has called for a **7-8% wage increase** for the 3.6 million employees in the metal and electrical industry. Assuming the regional collective bargaining committees endorse this recommendation (which we do not doubt), this would constitute the highest wage demand since 1992. During the previous collective bargaining round, IG Metall demanded a 6.5% pay increase. The final pay demand for the wage negotiations beginning in early October will be set on 23 September.
- Rallying under the motto “There’s more at stake”, IG Metall has set itself the goal of exceeding the 2007 wage settlement, which provided a pay increase in two steps of 4.1% and 1.7%. According to IG Metall president Berthold Huber, there is an **urgent need** among employees in the metal and electrical industry **to make up for lost ground**. While corporate earnings have been rising strongly in recent years, employees’ wages have increased only marginally. At the same time, the trade union hopes that this wage demand will help to contribute to a more balanced overall economic growth, which has so far been powered by foreign trade alone. High inflation rates play a role inasmuch as the trade union, based on a room to manoeuvre in terms of wage calculations of 2.5%, expects inflation to exceed the 2% level. The argument related to inflation or purchasing power parity was not addressed explicitly, however.
- As expected, the wage demand came under **heavy criticism from employers**. In particular, employers claim that it is irresponsible to demand the highest wage increase in 16 years in the midst of an economic downturn. This would unnecessarily jeopardise not only the industry’s international competitiveness but also the more than 200,000 newly created jobs.

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- How is the union’s wage demand to be evaluated? First, it is always a case of “**pay hike demands are one thing but actual wage settlements are another**”. As a rule of thumb in the metal and electrical industry, the final settlement corresponds to slightly more than half of the initial demand. Historically, wage agreements are above this rule of thumb during more favourable economic periods and below during less favourable economic times.

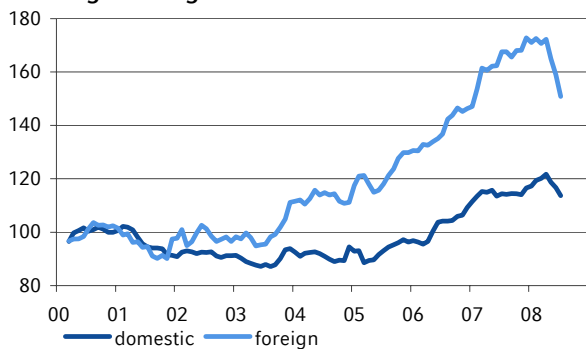
Metal industry: wage demands and settlements



Source WSI Collective Bargaining Archives, WestLB Research

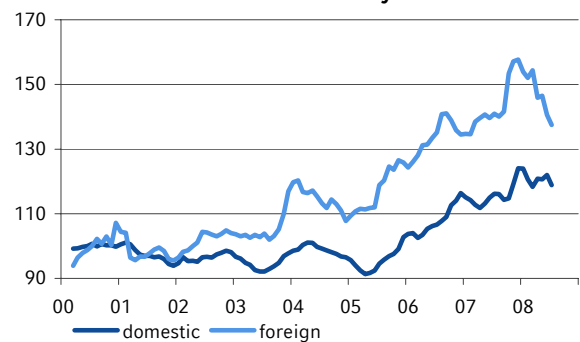
- It is beyond doubt that the German economy will face tougher times ahead. We expect an overall economic growth rate of merely 0.3% y/y for 2009. Nor does the **downturn** exempt the metal and electrical industry, especially as the very export-driven sector is particularly hard hit by the global slowdown. We have recently cut back our forecast for global economic growth to 3%, which is on the verge of a recession as defined by the IMF. Although the willingness of employees to strike should continue to be very high – according to the *Institut der deutschen Wirtschaft* (IW) there were as many strike days in 2007 as in 1993 – a strike would probably have less of an impact on companies than in the previous wage bargaining round given the lower level of demand and capacity utilisation. Accordingly, we believe that, despite the higher demand, the wage settlement will not exceed last year’s 4.1%, unless, however, agreements are reached beyond pure wage increases to curb higher company costs.

New engineering orders 2000 = 100



Source EcoWin, WestLB Research

New orders in the metal industry 2000 = 100



Source EcoWin, WestLB Research

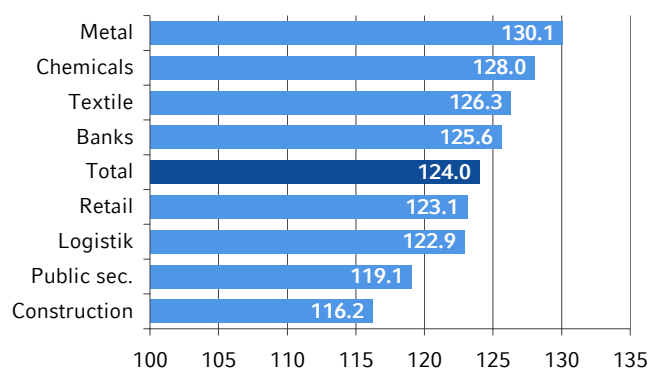
- Whether a settlement of this size is economically sustainable for companies will depend largely on **productivity growth**. The metal and electrical industry has achieved higher productivity growth in recent years than the overall economy so it has been able to absorb higher wage settlements. During a downturn, however, productivity growth typically tends to be lower, so that some companies will be able to compensate for labour cost increases only by means of cost cutting and job cuts. Hence, a substantial rise in labour unit costs in the metal and electrical industry is not on the cards.
- As a result, taken by itself the wage settlement that we forecast for the metal and electrical industry will **not constitute a serious risk to price stability**. There would be a serious risk to price stability only if other industries used this settlement as a basis for their own negotiations. We do not believe this will be the case, however, given the specific situation of the metal and electrical industry. On the contrary, wage agreements in other industries are likely – as in the past – to be struck at lower levels. Although at the overall economic level we expect unit labour costs to rise moderately, which tends to lead to higher inflation rates, given the slowdown in growth their impact on prices should be limited. Accordingly, we see the risk of a wage-price spiral as being very low. On the contrary, against the backdrop of lower crude oil and commodities prices, we expect inflation to ease towards 2% and even lower in the coming year.

Wage growth % y/y

	Basic collective bargaining increase	Overall collective bargaining increase	Effective wage increase
2000	2.1	1.9	1.5
2001	2.2	1.9	1.8
2002	2.3	2.7	1.3
2003	2.4	2.1	1.3
2004	1.7	1.3	0.6
2005	1.0	1.1	0.3
2006	0.9	1.3	0.9
2007	1.6	1.4	1.6
Q1 2008	3.1	2.7	2.3
Q2 2008	3.4	1.7	2.2

Source Deutsche Bundesbank, WestLB Research

Collective bargaining development, 1998 - 2007 1998 = 100



Source WSI Collective Bargaining Archives, WestLB Research

- With regard to the **labour market** and **overall economic growth**, a pay settlement in the metal and electrical industry of significantly below 4% would certainly be tantamount to more. The pressure to generate cost savings or cut jobs would be lower, which on balance would increase the likelihood of a stronger overall economic wage growth. At the same time, international corporate competitiveness would not be impacted, which at the very latest would be a plus when the global economy picks up again.

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