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Wages and Indirect Labour Costs in Western Industrialized Countries

by Heinz Salowsky, Cologne *

All Western industrialized countries have been passing through the same economic sequence since 1970: a boom followed by a recession which in turn gave way to a slow recovery. Economic and social policy focuses everywhere on the fight against inflation and unemployment. The success or failure of these efforts is reflected by the wage levels which are one of the most important economic efficiency indicators. The following article provides an international survey¹.

The industrialized countries of the West may be divided into three groups as far as wage levels are concerned: The highest wages, on an average of all industries, are paid in Denmark and Sweden. The USA has fallen back farther and farther since 1970 when it was still far ahead of all other countries. Four other countries (Switzerland, the Federal Republic of Germany, the Netherlands and Belgium), where wages were far below the US level, have drawn ever closer. Four great industrial nations (Great Britain, France, Italy and Japan) are following at quite a distance. Japan, once lagging far behind European wage rates, has linked up with the industrialized countries of Europe through large wage increases.

The highest rates of increase occurred in 1970-1975 in the last-mentioned group and in Ireland which brings up the rear: Ireland 160 p.c., Japan 158 p.c., Italy 144 p.c. and Great Britain 129 p.c. These countries however also recorded the largest price increases: Ireland 86.4 p.c., Japan 72.4 p.c., Italy 71.1 p.c. and Great Britain 84.4 p.c. Large wage increases are more often than not a reflection of inflationary developments in the national economy concerned. The relatively low rates of increase in some other countries, on the other hand, must be regarded as related to a very high starting level.

On the Comparability of Wage Levels

The picture changes profoundly if the wages expressed in national currencies are converted into a common monetary unit — the Deutschemark is used in the present survey — so as to make them comparable. Since business firms must compete in an international market and their competition

operates at the official rates of exchange, it seems reasonable to base the wage comparison on these official rates. The difference between the rates of increase in national currency and in German currency is a clear indication of the changes which have occurred in the rates of exchange. While the rise of hourly wages in national currency illustrates the domestic trend, especially if viewed in conjunction with the trend of prices, the rates of increase on a DM basis reflect the changes in the competitive position of individual countries in the international market.

In countries with currencies which have risen in value since 1970 compared with the DM wages show a higher rate of increase on a DM basis than in terms of their national currency. The only countries in which wages have in fact risen more in Deutschemark than in their national currencies are Switzerland — where the increase in wages in DM was 21.1 percentage points higher — and Austria — where the difference however was marginal.

For all other states the conversion into DM gives distinctly lower rates of wage increase because their currencies have depreciated significantly against the DM since 1970. In Ireland, Great Britain and Italy the wide margin between the wage movements as expressed in the national currency and in DM is truly striking. It reflects clearly the downslide of the pound sterling, the Irish pound and the Italian lira. Of the increase of gross hourly wages in the manufacturing industry

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¹ The article is based on Heinz Salowsky, Lohnentwicklung und Personalzusatzkosten in westlichen Industrieländern (The development of wages and the additional labour costs in Western industrialized countries). IW-Beiträge zur Wirtschafts- und Sozialpolitik Nos. 38/39 and 40/41, Cologne 1977.

LABOUR COSTS

Table 1
Average Labour Costs in the Industries
of Selected Countries in 1975

Country	Total in DM	Average Hourly Wages in DM	of which Additional Labour Costs	
			in DM	in p.c. of hourly wages
Sweden	17.77	12.71	5.06	(39.8)
Denmark	16.81	13.96	2.85	(20.4)
Netherlands	16.12	9.73	6.39	(65.7)
USA	16.10	11.83	4.27	(36.1)
Belgium	15.91	9.66	6.25	(64.7)
Switzerland	15.17	10.76	4.41	(41.0)
France	11.35	6.83	4.52	(66.2)
Italy	11.02	5.89	5.13	(87.2)
Austria	10.07	5.62	4.45	(79.1)
Great Britain	8.49	6.86	1.63	(23.7)
Japan	8.29	7.19	1.10	(15.3)
Ireland	7.34	6.01	1.33	(22.1)
For comparison: Federal Republic	15.66	9.80	5.86	(59.8)

Source: Heinz Salowsky, Personalzusatzkosten in westlichen Industrieländern (Additional labour costs in Western industrialized countries), Beiträge zur Wirtschafts- und Sozialpolitik Nos. 40/41, Institut der deutschen Wirtschaft, Cologne 1977, p. 10.

of Great Britain which in sterling terms amounted to 129 p.c. no more than 43 p.c. was left after the conversion into DM; of the 160 p.c. and 144 p.c. rise in national currency in Ireland and Italy 62 and 55 p.c. only were left on a DM basis.

The depreciation of the US dollar and the Japanese yen was less steep but still quite substantial. Conversion into DM turns the 43 p.c. rise of the dollar wages in the US industry – from \$ 3.36 an hour in 1970 to \$ 4.81 in 1975 – into a small decline: in 1970 the average hourly earnings in

US industry were still the equivalent of DM 12.26; by 1975 they were down to DM 11.83.

The Role of Fringe Benefit Costs

The level of hourly wages does not in itself say anything about the competitiveness or the labour costs of a country. The additional labour costs – the cost of fringe benefits – must be added to the direct wages in order to appraise its competitive strength. Among these is the expenditure for "working time" paid but not worked (vacations, legal holidays, absence due to sickness), employers' social insurance contributions and other employers' expenses whether under collective wage agreements or incurred voluntarily. Then there are special social welfare disbursements by employers, e.g., the Italian employers' contributions for the building of homes for workers, the transport levy in France which serves the purpose of holding down the fares of commuting employees, and a special Employment Levy in Great Britain.

There are great differences between the various countries in regard to both the level and the structure of these fringe benefit costs. The variations between them are also wider than between the direct wages; in 1975 they ranged from DM 1.10 an hour (in Japan) to DM 6.39 (in the Netherlands). Related to DM 100 of direct remuneration for the time actually worked the burden of "indirect" wage costs was highest in Italy (DM 87.30) and lowest in Japan (DM 15.28). The Federal Republic was third from the top in 1975 in regard to the absolute level of the additional wage costs per hour (DM 5.06); the cost of fringe benefits per DM 100 of direct remuneration amounted to DM

Table 2
Average Gross Hourly Earnings (of Men and Women) in the Manufacturing
Industries of Selected Countries

Country		in National Currency		in Deutschemark		Index in National Currency 1970 = 100		Index in Deutschemark 1970 = 100	
		1970	1975	1970	1975	1970	1975	1970	1975
France	ffr	5.92	11.99	3.91	6.83	100	202.5	100	174.7
Italy	lire	635	1,551	3.68	5.89	100	244.3	100	155.0
Netherlands	hfl	4.82	10.03	4.87	9.73	100	208.1	100	199.8
Belgium	bfr	66.2	144.3	4.86	9.66	100	218.1	100	198.8
Great Britain	p	54.9	125.8	4.80	6.86	100	229.0	100	142.9
Ireland	p	42.4	110.2	3.71	6.01	100	259.9	100	162.0
Denmark	dkr	15.25	32.57	7.42	13.96	100	213.6	100	188.1
Sweden	skr	12.17	21.44	8.56	12.71	100	176.2	100	148.5
Switzerland	sfr	6.56	12.30	5.55	10.76	100	172.2	100	193.9
Austria	S	20.9	39.8	2.94	5.62	100	190.5	100	191.2
USA	\$	3.36	4.81	12.26	11.83	100	143.1	100	96.5
Japan	yen	336	866	3.43	7.19	100	257.8	100	209.6
Federal Republic	DM	6.20	9.80	6.20	9.80	100	158.1	100	158.1

Source: Heinz Salowsky, Lohnentwicklung in westlichen Industrieländern (The development of the wages in Western industrialized countries), Beiträge zur Wirtschafts- und Sozialpolitik Nos. 38/39, Institut der deutschen Wirtschaft, Cologne 1976, p. 9.

LABOUR COSTS

59.80, placing the Federal Republic in the intermediate group as regards the relative weight of the additional labour costs.

The reason for the relatively low level of fringe benefit costs in some countries is to be found in the differences in the financing arrangements for the social security systems: in Denmark, Ireland and partly also in Great Britain these costs are for the most part met out of the tax revenue whereas in Japan contributions are relatively small.

There are also considerable structural differences between the fringe benefit costs in the various countries. Where the mandatory employers' contributions are relatively high, as in Italy and Belgium, the expenditure on a voluntary basis or by collective agreement is very low. It may be inferred that in these countries the legal arrangements are considered adequate and supplementary occupational schemes are either not needed or ruled out by lack of funds due to the high level of the mandatory contributions.

In any international comparison of labour costs it has finally to be borne in mind that relatively high additional labour costs do not necessarily imply a high level of the total labour costs. Austria and Italy are countries with relatively low direct wages but relatively high fringe benefit costs. In regard to total labour costs however they belong to the lower third of comparable industrialized countries. In contrast Denmark, a country with high direct wages but relatively low additional charges, is one of the states with the highest overall labour costs.

Sweden is undeniably holding the lead for total labour costs, i.e. gross hourly earnings plus fringe benefit costs, among all industrialized countries. The drawback of this is that, according to Swedish economic experts, high labour costs are the principal reason for the unsatisfactory course of the country's exports in the last two years. In 1975 and 1976 the Swedish exporters lost about one-sixth of their share of foreign markets while Sweden's investments abroad increased rapidly.

German Direct Investments Abroad

Characteristic of the changed situation is the influx on an increasing scale of foreign capital into the USA — especially from Great Britain, the Netherlands, Switzerland and the Federal Republic. From German investors the USA has by now attracted a total investment volume of nearly DM 5.5 bn, which makes it their favorite investment area. The improvement of the competitive position of US industry is due to the reversal of the trend of the US dollar's rate of exchange, as well as the more favourable course of labour costs. The US dollar has lost in value compared with most European currencies (except for the pound sterling and the Italian lira). Against the DM it has fallen from an average DM 3.65 (in 1970) to an average DM 2.46 (in 1975). The rise of US dollar wages by 43.1 p.c. coincided with a decline of the exchange rate by 32.6 p.c. Converted into DM, the hourly wages in the US manufacturing industry therefore receded from DM 12.26 in 1970 to DM 11.83 in 1975. "With little public notice, the

Table 3
Average Additional Labour Costs in p.c. of the Direct Remuneration
for Work Performed in the Industries of Selected Countries

Country	Total	Payments for Time Off	Mandatory Additional Labour Costs	Social Security Expenditure, Voluntary or by Collective Agreement	Other Expenditure of a Social Nature	Taxation of a Social Nature
France (1972)	66.15	13.85	32.09	7.14	12.75	0.33
Italy (1972)	87.23	18.57	48.21	1.05	18.52	0.90
Netherlands (1972)	65.66	19.61	23.42	9.74	12.87	—
Belgium (1972)	64.68	20.36	32.18	1.89	10.24	—
Great Britain (1973)	23.71	11.21	6.90	4.37	1.94	-0.71
Ireland (1975)	22.10	9.00	10.10	2.00	1.00	—
Denmark (1975)	20.40	12.50	4.40	1.00	2.50	—
Sweden (1975)	39.80	11.10	24.30	4.40	—	—
Switzerland (1975)	34.2-49.0	10.0-13.0	7.9-10.0	8.1-16.0	8.3-10.0	—
Austria (1975)	79.10	13.30	29.70	23.40	10.10	2.60
USA (1975)	36.10	13.80	8.80	11.60	1.90	—
Japan (1975)	15.28	3.22	6.19	1.00	4.87	—
For comparison:						
Federal Republic (1975)	59.80	17.30	25.10	4.90	12.50	—

Source: Heinz Salowsky, Personalzusatzkosten in westlichen Industrieländern (Additional labour costs in Western industrialized countries), Beiträge zur Wirtschafts- und Sozialpolitik Nos. 40/41, Institut der deutschen Wirtschaft, Cologne 1977, p. 9.

US has lost its long-time position as the country with the highest labour costs in the world" ².

The concentration of the German direct investments in a few countries is evidence of the high rating accorded by German investors to large domestic markets and well-developed infrastructures. The prospect of lower producing costs is an essential incentive for German investments in other countries, in addition to the motive of safeguarding and developing existing export markets (especially in the mechanical engineering and consumer goods industries) and taking advantage of vicinity to raw material sources (for basic and producer goods industries). Increasing use is evidently being made of the cost advantages accruing from transferring production activities abroad. It has been established not only by Institut der Deutschen Wirtschaft (Institute of the German Economy) but likewise by enquiries of the German Federal Bank that the German labour costs (wages plus fringe benefit costs) put the Federal Republic on the international scale in the highest group, at least in the industrial sector.

Labour Costs and Foreign Trade

The following figures indicate the position of the Federal Republic in comparison with its major world market competitors in regard to labour costs in 1975:

- In Japan and Great Britain the labour costs of industry were half of those of German industry (DM 8.29 and DM 8.48 per hour respectively as against DM 15.66);
- in the Italian industry (DM 11.02) and in the French industry (DM 11.35) the labour costs were a little less than three quarters of the German level;
- in the US industry the total labour costs per

hour were about 3 p.c. higher than in the German industry.

In 1976 the German labour costs rose further on an international scale although the wage settlements in that year were relatively moderate.

Overall averages for the whole of industry as necessarily used in this comparison have the advantage of greater general validity but also the disadvantage of inapplicability to important specific situations, i.e. to certain major industries. In some important US industries the direct hourly wages are still above the level of corresponding German wages while the additional labour costs in the Federal Republic of Germany are significantly higher than in the USA, with the result that these German industries may in the future show overall the higher labour costs if due allowance is made for exchange rate variations.

The level of economic activity and the economic growth in the Federal Republic are determined largely by external factors. The Federal Republic "earns" abroad about 37 p.c. of the national product; about one job in three depends upon the export trade. This high export ratio cannot be maintained in the long run unless the level of wages is kept more or less in line with those of the major competitors. In 1976 the German exports still increased by 15.6 p.c. to DM 256.2 bn although the German labour costs were high by international standards and the DM was upvalued by a significant margin. This export achievement was due to factors which are still given a high rating in international competition: high product quality, reliability of delivery, after-sales service. It must not be overlooked however that the imports into the Federal Republic last year increased even more strongly, by 20.2 p.c. to DM 221.6 bn, which, insofar as it is not due to higher raw material prices, proves that the competitiveness of foreign suppliers has definitely improved.

² US News and World Report, Feb. 9, 1976, p. 65.

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