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Article

"Germany needs stronger wage growth": Five questions to Karl Brenke

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Karl Brenke, research associate at DIW Berlin

FIVE QUESTIONS TO KARL BRENKE

»Germany Needs Stronger Wage Growth«

1. Mr. Brenke, how significant are the differences between industrial developments in Germany and France? German manufacturing managed to buck the trend successfully and contributes approximately 22 percent of value added, which is exactly the same percentage as ten years ago. However, development in France has been quite different; here, over the past decade, rapid deindustrialization has taken place and value added from manufacturing industry as a percentage of the overall economy is now barely ten percent, which is even lower than in eastern Germany. Industrial density in France has, therefore, suffered a great deal. However, product structure must also be taken into consideration. German manufacturing is traditionally geared towards capital goods and, thus, also research-intensive goods, the significance of which has increased dramatically over the last few years. France, on the other hand, tends to manufacture more consumer-oriented products and the significance of research-intensive goods has declined.
2. How can this divergence be explained? On the one hand, this stems from the country's capacity for innovation, i.e., differences in the development of research-intensive sectors. On the other hand, wage development is also of relevance here. In Germany, over the past decade, wage development in the manufacturing industry has been very weak. Wages have lagged behind the margin of distribution created by the increase in productivity. In France, the exact opposite has occurred: wages have overtaken productivity growth. As a result, France has experienced losses in competitiveness both in terms of price and product type.
3. Is this evidence that German manufacturing should continue to exercise restraint when it comes to wage development? No, quite the contrary. We are part of a currency union which requires disciplined behavior. This means that Germany needs stronger wage growth than in the past and the margin of distribution should be fully utilized. The French, on the other hand, can no longer afford to continue with the wage policy of the last few years and need much weaker wage growth. Although actual wage cuts in France would result in recession, any wage growth in the next few years should be very restrained.
4. Were both countries similarly affected by the 2007/2008 financial crisis? No, the financial crisis resulted in a decline in global demand, also for manufacturing goods. This had a much more significant impact on the German export-oriented manufacturing sector than on French industry. However, German manufacturing managed to recover from this shock relatively quickly. Industrial output in Germany is currently higher than it was before the financial crisis. France, on the other hand, experienced no recovery at all following the financial crisis. Although the slump was not as dramatic as it was in Germany, there was no recovery in France.
5. What do the differences in the industrial development of these two major European countries mean for the EU? These diverging developments obviously lead to tensions, i.e., one country is lagging behind when it comes to competitiveness while the other is forging ahead. This results in tensions which would have previously been mitigated by the exchange rate mechanism. As this mechanism no longer exists, care must be taken to ensure that uniform conditions are created within the currency union, particularly with regard to wage development. The introduction of the euro and the loss of the exchange rate mechanism have placed the onus on harmonized wage policies to alleviate such tensions.

Interview by Erich Wittenberg.

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