Chart 25 Sectoral labour cost developments

(annual percentage changes; quarterly data)

Sources: Eurostat and ECB calculations.
Note: CPE stands for compensation per employee and LCI stands for labour cost index.

Box 2

RECENT DEVELOPMENTS IN THE WAGE DRIFT IN THE EURO AREA

The adjustment of labour costs to changes in the economic situation can be gauged via different indicators. One such indicator is the wage drift, which measures the difference between the growth in the actual wages received by workers and that in negotiated wages. Since negotiated wages are typically fixed for some time ahead, short-run changes in economic conditions are most likely reflected in movements in the wage drift, driven by flexible wage elements, such as bonuses. This box presents an estimate of the wage drift in the euro area and explores its evolution since 2008.

Wage drift as a component of compensation per employee

The most frequently used indicator of labour cost developments at the aggregate level is growth in compensation per employee. In addition to growth in wages and salaries, it reflects changes in the employer part of social security contributions. Growth in compensation per employee can thus be broken down into negotiated wage growth, the wage drift and the impact of changes in employers’ social security contributions. Chart A shows this breakdown, defining the social security contribution component as the difference between the annual rate of growth in compensation per employee and that in gross wages and salaries per employee, and the wage drift as the difference between the annual rate of growth in gross wages and salaries per employee and that in negotiated wages.1 Using this approach, social security contributions will only have an

1 The wage drift is measured as the difference between the annual rate of growth in wages and salaries and that in negotiated wages rather than as the contribution that negotiated wages make to overall wage growth, owing to the data limitations applying to negotiated wages. In particular, this series is typically not available in levels, but only as the growth rate resulting from the wage bargaining process.
impact on growth in compensation per employee if they grow at a different rate to gross wages, and wage drift components will only have an impact if they grow at a different rate to negotiated wages.

The impact of changes in employers’ social security contributions has been relatively limited. Over the period since 1999 it has been neutral with regard to the annual average growth rate of compensation per employee of 2.1%. Measured in absolute terms, it has amounted to an average of 0.15 percentage point. Changes in social security contributions tend to be driven mainly by regulatory reforms and therefore do not normally exhibit a clear cyclical pattern. Hence, the longer the period for which wages are negotiated and the sharper the movements in the cyclical position of the economy, the greater a role wage drift should play in explaining the movements in overall labour cost growth over the economic cycle.

Assessing movements in the wage drift

The wage drift in the euro area, as shown in Chart A, is an aggregate measure, and its use as an indicator of cyclical adjustment is subject to a number of caveats. One caveat relates to the statistical and conceptual properties of the euro area indicator of negotiated wages, which, by contrast with compensation per employee, is aggregated from non-harmonised national data and does not cover all euro area countries. Moreover, wage indexation clauses that provide for adjustments to actual wage growth on the basis of past inflation outcomes are typically not reflected in negotiated wages and thus appear in the wage drift as a factor that is independent from the economic situation at the time.

A counter-cyclical impact of social security contributions on growth in compensation per employee can be explained by the fact that contribution rates are raised (lowered) in bad (good) times as revenues fall (rise) relative to expenditure. There may also be pro-cyclical effects if, for instance, employers’ social security contributions are reduced as a deliberate measure to lower labour costs in bad times.

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2 A counter-cyclical impact of social security contributions on growth in compensation per employee can be explained by the fact that contribution rates are raised (lowered) in bad (good) times as revenues fall (rise) relative to expenditure. There may also be pro-cyclical effects if, for instance, employers’ social security contributions are reduced as a deliberate measure to lower labour costs in bad times.

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Sources: Eurostat and ECB calculations.
3.4 THE OUTLOOK FOR INFLATION

According to Eurostat’s flash estimate, euro area annual HICP inflation was 2.2% in December 2012, unchanged from November and down from 2.5% in October and 2.6% in August and September. On the basis of current futures prices for oil, inflation rates are expected to decline further to below 2% this year. Over the policy-relevant horizon, in an environment of weak economic activity in the euro area and well-anchored long-term inflation expectations, underlying price pressures should remain contained.

Risks to the outlook for price developments are seen as broadly balanced over the medium term, with downside risks stemming from the impact of weaker than expected growth in the euro area and upside risks relating to higher administered prices and indirect taxes, as well as higher oil prices.