Greenwich Political Economy Research Centre

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The working people of the UK are stronger in Europe

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Outline

- The working people in the UK have good reasons to vote to stay in the European Union,
- but not for the same reasons as the government or the reports from the financial sector and neoliberal think tanks suggest.
- The role of the UK in the EU for high road labour market policies
  - Onaran and Obst 2015
  - Onaran and Stockhammer 2016

Background

- Business reports, even when they endorse a "yes" vote, claim that Britain is better off without the EU directives, which protect workers' rights such as
  - the Working Time Directive
  - directives for paid leave, equal rights for part time, agency and full time
  - equal pay
  - maternity and paternity leave.
- TUC has demonstrated clearly the risks of Brexit for the rights of working people, especially women who constitute larger part of part time workers.

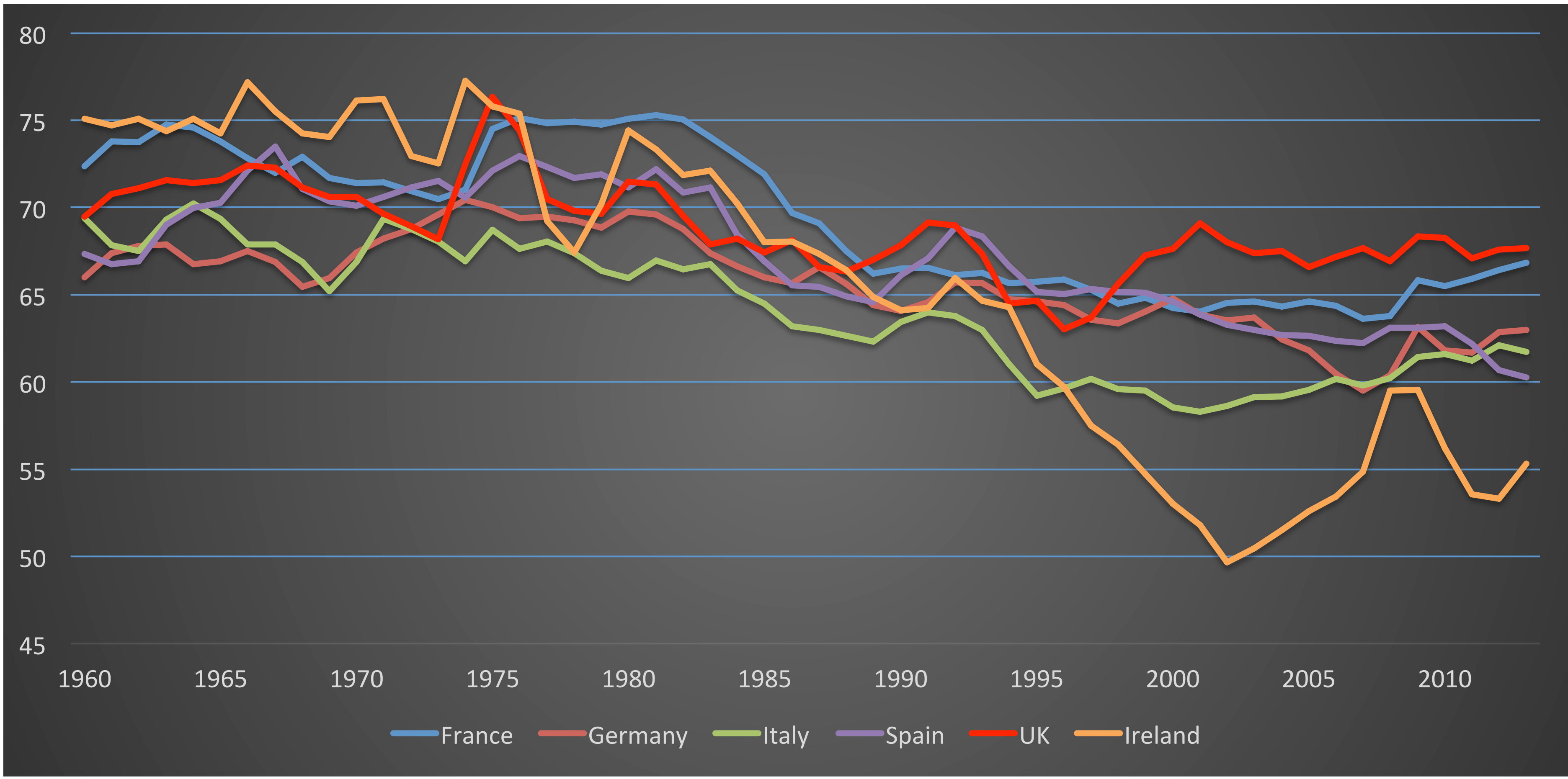
... Background

- However, despite these rights the labour market policies in the EU Member States (MS) has been far from a rosy picture.
- Individual EU MS and the European Commission (EC) have long encouraged wage moderation,
  - explicitly recommending real wage growth below productivity growth to increase the international competitiveness of the countries.
- This policy has resulted in three decades of
  - increasing inequality,
  - low road labour market policies,
  - fewer or worse quality jobs in the name of flexibility.

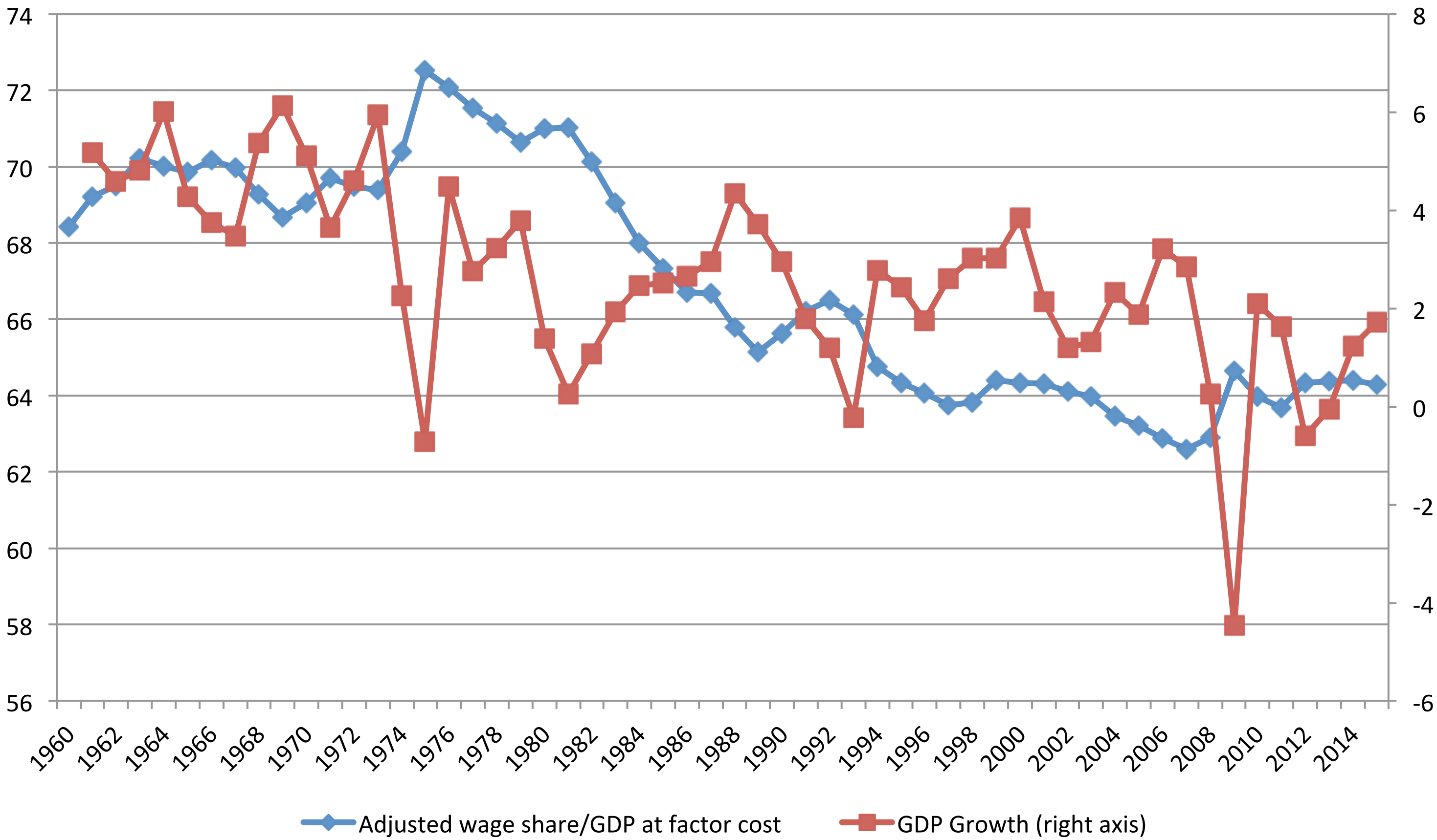
… Background

- Why should working people nevertheless vote to stay in?
- Because we have more chances of achieving a change towards high road labour market policies if we work together with the other progressive movements in the EU rather than in isolation in the UK.
- There is a rigorous macroeconomic rationale behind this argument

Wage share (adjusted, ratio to GDP, 1960-2015)



Wage share vs. growth, EU15, 1960-2015



Source: Ameco

What is the effect of a decline in the wage share on demand and growth?

- Mainstream : wage=cost
  - positive effect on investment & exports
- But wages have a dual role
  - Cost item
  - Source of domestic demand

Lower wages →

1. Lower domestic consumption
    - The poor consume more out of their income than the rich
    - Workers consume a higher proportion of their wages than the employers consume out of their profits

2. Positive effect on private investment offset by negative demand effect
    – Investment depends on profitability, but also demand

3. higher foreign demand (Net exports=Exports-Imports)
    – labour costs ↓ → higher international competitiveness

- if total effect is +: lower wage share → higher growth
  – the economy is profit-led (mainstream assumption)
- if total effect is -: lower wage share → lower growth, fewer jobs
  – the economy is wage-led

Empirical evidence

(Onaran & Galanis 2012, ILO; Onaran and Obst 2015, FEPS)

- Negative effect on consumption is larger than the positive effect on investment in the UK (as well as other EU15 or developed and developing countries)
  → Domestic economy (consumption + investment) is wage-led
- Net export effects on growth not too important in large economies, where exports and imports are only a small part of total demand
  → the UK, EU as a whole, and other large economies are wage-led
- Lower wages→ lower growth, fewer jobs
- Made worse with austerity
  - Lower demand
- → reliance on debt-led consumption
- "Britain and the EU need a pay rise and public investment in social and physical infrastructure"

The role of the UK in the EU

- UK is a wage-led economy→
- High road labour market policies can be implemented unilaterally
- Impact on trade deficit?
  - Negligible: wage share ↑1%-point → trade deficit /GDP ↑0.19%-point
  - trade imbalance → industrial policy
- What if other EU MS continue low road, ‘beggar thy neighbour’ policies?
  - There is still an area of manoeuvre in a wage-led economy, albeit narrower
- The EU membership is an opportunity.
- Improve cooperation among pro-labour forces, lead high road labour market policies in the EU as opposed to current position of promoting low road policies.

UK workers are stronger in the EU if it leads high road policies

- The effects of high road policies and public investment are a stronger if implemented at the EU level.
  - effect on GDP is almost doubled
  - negative impact on trade balance is more negligible when our trade partners allow their wages and demand increase.
- Globalization is not a barrier to these policies.
- international competitiveness based on wage competition in a highly integrated global economy is counter-productive.
- Europe and the UK is one of the main beneficiaries of coordinated wage-led growth and public investment .
  - Hence potentially global policy leader
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Policy Implications

- Aim of economic policy:
- full employment, ecological sustainability, and equality.
- mobilize all the tools of policy
- a comprehensive and coordinated mix of wage policy, industrial policy, public investment in social and physical infrastructure
- EU: Avoid beggar thy neighbour policies
- Coordination of wage bargaining systems to prevent a race to the bottom
- Productivity-oriented wage policy to stabilize effective demand

...Policy Implications

- 1.1. Pre-distributive policies
- policies targeting the top, middle, and bottom of the wage distribution.
  - Increase the bargaining power of labour via
    - reregulating the labour market
    - improving the union legislation,
    - increasing the coverage of collective bargaining
    - Eg: UK, if union density ↑ back to levels in 1980 (to 50% from 25%) →GDP pc ↑ by £440 (Onaran, Guschanski, Meadway, Martin 2015)
  - Close gender wage gaps (Onaran, Oyvat, Fotopoulou 2016)
  - sufficiently high minimum wages / living wage –national min wage relative to national average
  - regulating high/executive pay by enforcing pay ratios

... Policy Implications: Macro economic context

- Re-distribution: progressive taxation of income and wealth
- Reverse financialisation; reregulate finance and corporate governance
- Bring the welfare state back
- public investment in social and physical infrastructure
  - Physical infrastructure: **green** investment
  - Social infrastructure: **Purple** investment
    - create jobs in labour intensive services -education, child care, nursing homes, health, community and social services
    - improve pay and working conditions in these industries
    - socializing the invisible care
    - More jobs with lower Carbon emissions
- Shorter working time in parallel with the growth in productivity with wage compensation for the lower income groups.

Conclusion

- Working people in the UK are better off in the EU then outside the EU in coordinating
  - labour market policy
  - financial regulation,
  - tax coordination,
  - public investment policy
  - ecological sustainability

Sources:

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Appendices

FT on Onaran and Galanis, 2012 ILO

Capital gobbles labour's share, but victory is empty

The big picture

Steve Johnson looks at the wider negative implications of falling wages

In 1958, Walter Reuther, a powerful US union leader was taken on a tour of a newly automated Ford Motor plant. "Aren't you worried about how you're going to collect union dues from all these machines?" he was asked by a (no doubt smug) company manager.

"The thought that occurred to me," Mr Reuther replied, "was how are you going to sell cars to these machines?"

Fifty-five years on, such a debate may be even more pertinent. In the innocent days of 1958, wages accounted for half of America's gross domestic product. Today, thanks to the onward march of globalisation and technology, labour's share of the pie has fallen inexorably to 42 per cent, a trend that has been repeated in many

labour's share of the pie than the US or UK.

Richard Lewis, head of global equities at Fidelity Worldwide Investment, who has studied this trend, believes it to be structural rather than cyclical, and therefore unlikely to reverse.

Mr Lewis says globalisation has "lowered the power of labour to bargain," resulting in de-unionisation and the "emasculation" of workers.

Simultaneously, companies have been able to optimise their tax regimes and can engage in both "financial expense" arbitrage (borrowing in the cheapest countries) and regulatory arbitrage.

Most importantly, however, he says globalisation and a move towards supranational corporate entities has made it possible for companies to consolidate their industries more effectively.

What all this means for the investment community is perhaps a little less clear-cut. Özlem Onaran and Giorgos Galanis, the authors of the paper, found the impact varied widely between countries.

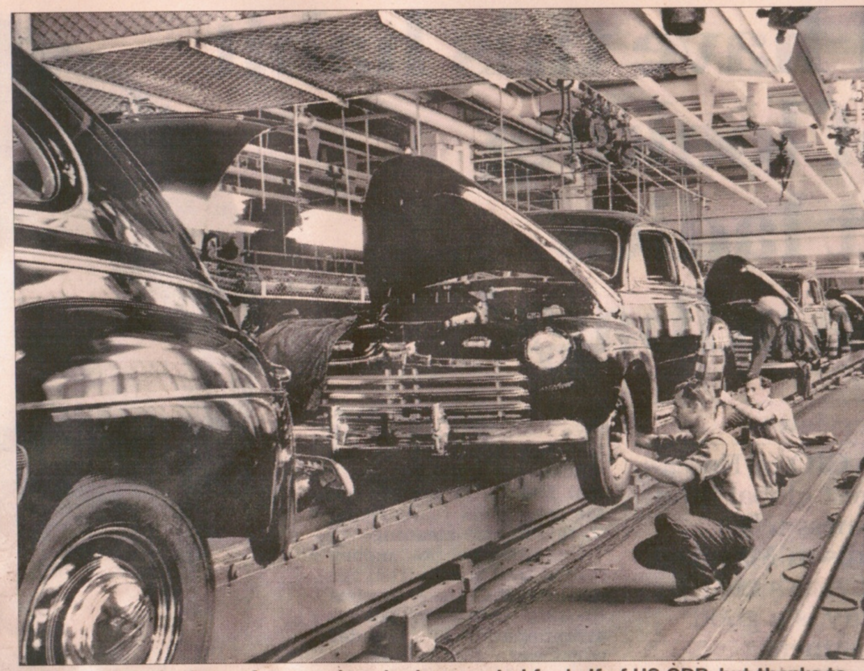
labour will continue to be squeezed.

Frances Hudson, global thematic strategist at Standard Life Investments, believes this geographic divide opens the way for relative value trades that favour companies in countries that are becoming more competitive.

To complicate matters further, the academics found the global effect of a squeeze on labour was negative, as the heightened export competitiveness enjoyed by countries with weak wage growth simply reduced the competitiveness of its trading partners – a form of "beggar thy neighbour". A one percentage point fall in labour's share was found to reduce global GDP by 0.36 points.

With this in mind, Mr Greenberg believes we may have to start thinking about a "post-growth" world. "The revenue numbers of the S&P 500 are basically stagnant. Is that going to reverse any time soon? I don't see how it can," he says.

Ms Hudson also wonders where growth will come from, given that the absence of wage inflation comes at a time of weak



In 1958, labour's share of economic output accounted for half of US GDP, but thanks to increasing globalisation and technology, this has fallen to 42%

right all along, and that capitalism ultimately sows the seeds of its own destruction, "when there is no consumer demand and it all falls over".

Mr Greenberg paints a picture of a bleak future

with, barring a "mass uprising", "McJobs" increasingly the norm.

"One thing that does need to change is the idea of shareholder value being the only responsibility of a company," he says, alluding

to the 19th century Q ers, "who took respons ity for their employees communities. There w sense that you ha responsibility for societ

Mr Reuther would doubt have concurred.

Impact of wage-led growth on investment and productivity

- Missing link between profits and private investment
- Increasing profits do not always lead to higher investment
  - Private investment is wage-led in the UK and 8 out of 15 EU MS
  - increasing demand → investment↑↑
- The non-financial companies' financial activities →private investment↓
  - Interest payments+dividends to shareholders as well as their financial revenues (Tori and Onaran, 2015)
- Inequality + Financialization →lower productivity & potential growth
- Higher productivity needs wage-led growth and regulating finance and corporate governance.

Impact of wage-led growth on inflation?

- a 1%-point rise in the wage share →2%↑in prices in the UK and 1.4% rise in the EU15, 0.6% in Ireland.
- The risk now is deflation not inflation
- Pay rise to defeat deflation
- Bank of England and the ECB need a pay rise!
  - a nominal wage increase of 4% in the UK, 2.7% in Ireland (assuming 0.7% rise in productivity)

The effects of a 1%-point decline in the wage share at the national level

	The effect of a 1%-point increase in the profit share in only one country on:					
	C/Y	I/Y	X/Y	M/Y	NX/Y	Private excess demand / Y
	A	*B*	*C*	*D*	*E(C-D)*	*F(A+B+E)*
Austria	-0.277	0.000	0.234	-0.161	0.396	0.119
Belgium	-0.151	0.206	0.000	-0.053	0.053	0.108
Denmark	-0.155	0.169	0.185	0.000	0.185	0.198
Finland	-0.243	0.000	0.074	0.000	0.074	-0.169
France	-0.324	0.101	0.062	-0.078	0.140	-0.083
Germany	-0.397	0.000	0.049	0.000	0.049	-0.348
Greece	-0.564	0.000	0.099	0.000	0.099	-0.465
Ireland	-0.229	0.161	0.000	-0.074	0.074	0.006
Italy	-0.410	0.156	0.050	-0.087	0.137	-0.117
Luxembourg	-0.153	0.000	0.000	0.000	0.000	-0.153
Netherlands	-0.322	0.078	0.000	-0.069	0.069	-0.175
Portugal	-0.402	0.000	0.000	-0.182	0.182	-0.219
Spain	-0.410	0.088	0.044	-0.068	0.113	-0.210
Sweden	-0.388	0.128	0.057	-0.056	0.113	-0.147
United Kingdom	-0.252	0.000	0.074	-0.066	0.140	-0.112

The effects of a 1%-point decline in the wage share at the European level

	Private excess demand / Y	Multiplier	% Change in aggregate demand (A*B)	The effect of a simultanous 1%-point increase in the profit share on % change in aggregate demand
	A	*B*	*C*	*D*
Austria	0.119	1.039	0.124	-0.185
Belgium	0.108	0.740	0.080	0.009
Denmark	0.198	1.246	0.247	0.107
Finland	-0.169	1.316	-0.222	-0.304
France	-0.083	1.559	-0.129	-0.228
Germany	-0.348	1.136	-0.395	-0.442
Greece	-0.465	1.984	-0.923	-1.027
Ireland	0.006	0.863	0.005	-0.066
Italy	-0.117	1.451	-0.170	-0.238
Luxembourg	-0.153	0.535	-0.082	-0.128
Netherlands	-0.175	0.820	-0.144	-0.191
Portugal	-0.219	1.546	-0.339	-0.477
Spain	-0.210	2.147	-0.450	-0.544
Sweden	-0.147	1.058	-0.155	-0.271
United Kingdom	-0.112	1.129	-0.126	-0.195
EU15*				**-0.298**

* Change in each country is multiplied by its share in EU15 GDP.

The effects of a differentiated increase in the wage share on growth, investment and net exports

	Change in profit share	% change in aggregate demand	Total effect on I /Y	Total effect on NX/Y
	A	B	C	D
A	-3.00	1.147	0.431	-0.419
B	-1.00	0.269	-0.138	0.202
DK	-1.00	0.443	0.020	0.153
FIN	-5.00	1.489	0.647	-0.758
F	-5.00	1.120	-0.053	-0.753
D	-5.00	2.195	0.684	-0.913
GR	-5.00	5.123	2.358	-1.404
IRL	-3.00	0.332	-0.379	-0.052
I	-5.00	1.181	-0.409	-0.842
L	-5.00	0.641	0.167	-0.355
NL	-5.00	0.953	-0.225	-0.641
P	-5.00	2.375	0.895	-1.004
E	-5.00	2.713	1.024	-1.303
S	-5.00	1.275	-0.095	-0.812
UK	-5.00	0.959	0.144	-0.756
*EU15**		*1.511*	*0.245*	*-0.794*

Notes: A = Austria, B = Belgium, DK = Denmark, FIN = Finland, F = France, D = Germany, GR = Greece, IRL = Ireland, I = Italy, L = Luxembourg, NL = Netherlands, P = Portugal, E = Spain, S = Sweden, UK = United Kingdom
* Change in each country is multiplied by its share in EU15 GDP.

Average Growth Rates of GDP in EU15 Countries (percent)

	France	Germany	Italy	Spain	The UK	Ireland
1961-69	5.7	4.4	5.8	7.7	2.9	4.4
1970-79	4.1	3.3	4.0	3.9	2.4	4.7
1980-89	2.4	2.0	2.6	2.7	2.5	3.1
1990-99	2.0	2.2	1.5	2.7	2.7	7.0
2000-07	2.1	1.6	1.5	3.8	3.0	5.5
2008-2013	0.3	0.6	-1.4	-1.1	0.2	-1.1