EZA 674/18Apr05: Germany Politics

Minimum wage; cross-party consensus ends as the debate heats up and parties look towards upcoming North-Rhine-Westphalia state election

- Increasing pressure on service sector wages due to the influx from low wage earners (“cheap labour”) from Eastern Europe has sparked the minimum wage debate.
- The recent debate was triggered by loose comments from Bavarian state premier Edmund Stoiber on this issue, seen as a general u-turn by the opposition.
- But mainstream CDU thinking – represented by Angela Merkel – is still opposed and would only accept some sector specific wage fixation.
- Chancellor Gerhard Schröder, who previously opposed minimum wages on economic grounds made a swift u-turn, trying to exploit the debate in the upcoming state elections in North-Rhine-Westphalia.

Minimum wages in Germany – debate highlights anxieties of German public

Until last week there appeared to be cross-party consensus that official minimum wages defied economic rationality and was not consistent with the German corporate culture. With unemployment levels at a record-high it seemed unlikely that there would be a significant swing in the opposite direction

Surprisingly it was Bavarian state premier Edmund Stoiber, who triggered the swing in the debate by remarking at a European conservative party reunion in Brussels that some measures against the influx of cheap labour from Eastern Europe should be considered. His remarks were seen as a blank cheque supporting legal provisions to secure a minimum wage level, a long-standing demand from the unions but, until this point, an anathema for the CDU/CSU. Within days chancellor Schröder supported demands from his party for a nationwide minimum wage, revising his former – economically motivated – reservations.

Although the CDU/CSU started to backtrack on this issue – notably economic spokesman Ronald Pofalla called for the application of current laws against low wages and social spokesman Karl-Joseph Laumann, demanded a list of “problematic sectors” – it has lost the lead in the debate. Now there appears to be a concession that the “wage adoption law” in the construction sector - establishing the sector wage contract as a minimum wage - could be extended.

The speed with which the debate swung behind the concept of minimum wages – despite the defiance to economic rationality – can only be explained by the current levels of economic and social uncertainty. The ill-sold Hartz-IV labour market reforms, introduced this year have been a contributing factor. The re-classification, for reporting purposes, of some beneficiaries of social aid as unemployed by the Hartz-IV laws, helped boost unemployment figures beyond the psychologically important threshold of five million. At the same time it led to a general perception that unemployment would lead to dramatic losses in income, an exaggerated fear, as only the long term unemployed will suffer a moderate cut in benefits.

Eastern European workers – clash of different social and economic cultures

More important is EU-enlargement, which has led to a swap of labour and capital between Germany (being the “frontline” economy between the old EU and the accession countries) and Eastern Europe: German direct investment to Poland in 2004 – the accession year – in-
creased by a net of € 100 million, equity investment rose by net more than € 0.5 bn. At the same time the inflow of low cost labour has seen a significant increase from last year, concentrated on specific low wage sectors like lodging, catering, construction and meat processing. This has forced the German government to act and after the March 17 job summit (see EZA668/29Mar05) it established a special workforce, which recently raided c300 firms for workers illegally employed on low wages. But the government has relatively little chance of stemming the flow - most of the migrant workers are freelance and thus circumvent the stipulation of the accession treaty only allowing a free flow of workers from 2011.

However, what the German government sees as “abuse of the (EU) freedom of services”, might simply be a difference in culture and work practices. While in Germany the vast majority of the workforce is employed (only 9% are self employed), in Poland, as in other accession countries, the employed are a minority of the total workforce. German labour regulations, based on the corporate culture, are therefore difficult to apply. This explains why the government sees limited merit in extending sector wage contracts to migrants – an option considered by the CDU – as most migrants are, by definition, not subject to wage contracts.

Alternative arrangements to curb downward pressure on wages

At the moment the debate is focussed on two main alternative approaches to curb this kind of wage pressure.

(1) The government – in contrast to its previous position – now prefers an official minimum wage similar to that in France, the UK and other EU economies. This would be applicable to all sectors and workers in Germany. It is not quite clear at which level it would be set; but is most likely to use the level of social assistance (€ 1,100 per month per household, including housing) as a reference point. This would be a clear change from the current practice of leaving the setting of wages to the unions and employers.

(2) The opposition by contrast wants to retain current practice but extend the “Entsendegesetz” (wage adoption law) to include other sectors. The law, which requires firms not to undercut official wage contracts, was initially devised in 1996 for three industries – construction, tile layers and painters – and tightened in 1999. Extending this law to other sectors such as meat processing, catering, hotel services would face a specific difficulty, since the German high court of labour stipulates that at least 50% of the employees of the industry must be subject to an official wage agreement. In particular in Eastern Germany this is not the case.

(3) Therefore the CDU, concerned about its own constituency of small craft firms, seems to favour minimum wages at a sector level. This would face the problem that – unlike a general minimum wage - it could not be linked directly to the level of social assistance – but both would make a lower level of remuneration illegal.

Firms have complained that any form of minimum wage – even the wage adoption law in the construction sector – would be extremely harmful for the German economy. It is argued that it would increase the incentive for German firms to shift their headquarters abroad, while boosting illegal work – which had been on the retreat last year for the first time since official statistics were available. At the same time putting a floor on wages would help to increase labour costs, dealing a further blow to the fledgling service sector. Acceptance of this rationale has been the guiding principle of the CDU.
Minimum wages and labour market reforms

The debate on the minimum wage was not particularly welcomed by the Government either. Minimum wages clearly go against the Hartz-IV reforms, which are based on the philosophy of more job creation in the non-regulated low-wage sector (see EZA656/28Jan05). This explains, why both Schröder and economics minister Wolfgang Clement reluctantly – under intra-party pressure – made a u-turn on this issue, announcing a government initiative by the beginning of May. How they solve this conflict with Hartz-IV should be indicative of their future priorities in terms of labour market reform. It is to be expected that they will come up with clear proposals on a band of minimum wages for a broad range of industries, but perhaps more influential on the final outcome will be the upcoming 22 May state elections in North-Rhine-Westphalia.

North-Rhine-Westphalia state elections influence the debate

These state elections have become of paramount importance. North-Rhine-Westphalia, the most populous state – covering more than 20% of the German population - has been a traditional stronghold of the SPD, which has run the state government since 1966. The fortunes of the SPD have taken a turn for the worse since the beginning of this year, and their rule is under serious threat – according to the opinion polls the opposition parties appear to have a clear overall majority of 52%.

The SPD sees the population of North-Rhine-Westphalia, with a large workforce, heavy industries and even mining, more left-leaning than the rest of Germany. At the same time it has to acknowledge that the one million unemployed in this state - who feel threatened by the Hartz-IV regulations - have become disenchanted with the party position. They are now attempting to rally traditional supporters by appealing to old socialist and anti-capitalist dogma.

The CDU - with its centrist wing rooted in this state - is trying to maintain a fine line between keeping its appeal to middle ground voters as caring conservatives and presenting themselves as a clear reformist alternative to the incumbent government.

In this respect the outcome of the vote might be indicative for the future direction of German politics. A defeat of the SPD – as currently indicated by the polls – may bring the SPD to a more market oriented position, and provide a more market oriented thrust to German politics in general.

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