

## *Research Fellowship Programme - Future of the EMU*

### **Essay on Macroeconomic Adjustment in EMU: The Role of Wage Bargaining Systems**

#### **Background**

EMU entails a fundamental shift in the nature of the macroeconomic adjustment and, consequently, adds a new dimension to the role of wage bargaining. With a single currency and a common inflation target for monetary policy, divergent price dynamics linked, *inter alia*, to different wage-setting frameworks, may translate into persistent real exchange rate divergences and the accumulation of current account imbalances. Within this framework, the macroeconomic adjustment could be enhanced by collective bargaining institutions that help preventing similar harmful dynamics and promoting a rapid adjustment.

Some authors have stressed the role of centralisation for wage outcomes. Differences in how wage setters internalise the costs of their settlement translate into different wage outcomes. Calmfors and Driffill (1988) emphasised a hump-shaped relation between wage outcomes and the extent of centralisation of wage bargaining.<sup>1</sup> The empirical evidence is however not conclusive on the effect of decentralised wage setting on aggregate wage outcomes, including in light of the difficulty in disentangling the role played by wage centralisation and that played by wage coordination. Other relevant aspects of the wage setting framework include the mode of coordination, *inter alia* the role played by government and social partners to achieve coordinated objectives, the role played by certain sector in setting the pace for other sectors in sectoral wage bargaining (horizontal coordination), the presence of a hierarchical order across bargaining levels (vertical coordination).

Regarding the debate on the endogenous adaptation of bargaining frameworks before EMU, some scholars expected that after monetary unification there would have been a loosening of the wage discipline that characterised the run up to the EMU, while others claimed that the loss of monetary autonomy would have led countries to introduce reforms enhancing wage flexibility. With hindsight, none of these expectations fully materialised as wage moderation continued in some countries but not in others. Nonetheless, a trend towards more decentralised wage setting was observed in a number of euro area countries, including via the introduction of opening clauses in sectoral agreements and reforms in the operation of extension mechanism of collective contracts.

#### **Aims of the essay and key questions to be tackled**

The overall aim of this essay is twofold: (i) collect and describe information on the evolution of bargaining frameworks in EU countries regarding especially the aspect of wage decentralisation and wage coordination; (ii) from a normative viewpoint, evaluate the desirability and feasibility of wage setting reforms at national and super-national level that are supportive of macroeconomic adjustment in EMU.

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<sup>1</sup> Calmfors, L. and J. Driffill (1988), " Bargaining structure, corporatism and macroeconomic performance", *Economic Policy*, Vol. 3, No. 6 (Apr.), pp. 13-61.

- (i). Collect and describe information on:
  - a) wage setting centralisation / de-centralisation including for what concerns:
    - presence and characteristics of opening clauses in collective agreements and other ways for firm-level contracts to derogate from sectoral contracts;
    - functioning of mechanism for extending collective agreements to parties not participating in wage negotiations;
    - measures favouring the spreading of firm-level collective agreements;
  - b) wage coordination, including for what concerns presence of wage leadership and by which sectors

The information should span the longest possible time horizon and should be codified in such a way to be easily treated statistically (the end result should ideally be a database of variables representing bargaining characteristics for each country in each year). A description of the information collected should be provided.

- (ii). Identify the type of collective bargaining structures and institutional arrangements that may facilitate the adjustment of the real exchange rate in countries members of a monetary union? What forms of wage-setting coordination frameworks could be desirable and feasible? What feasible supportive reforms are needed at national level?