

Wages, demand and the economy

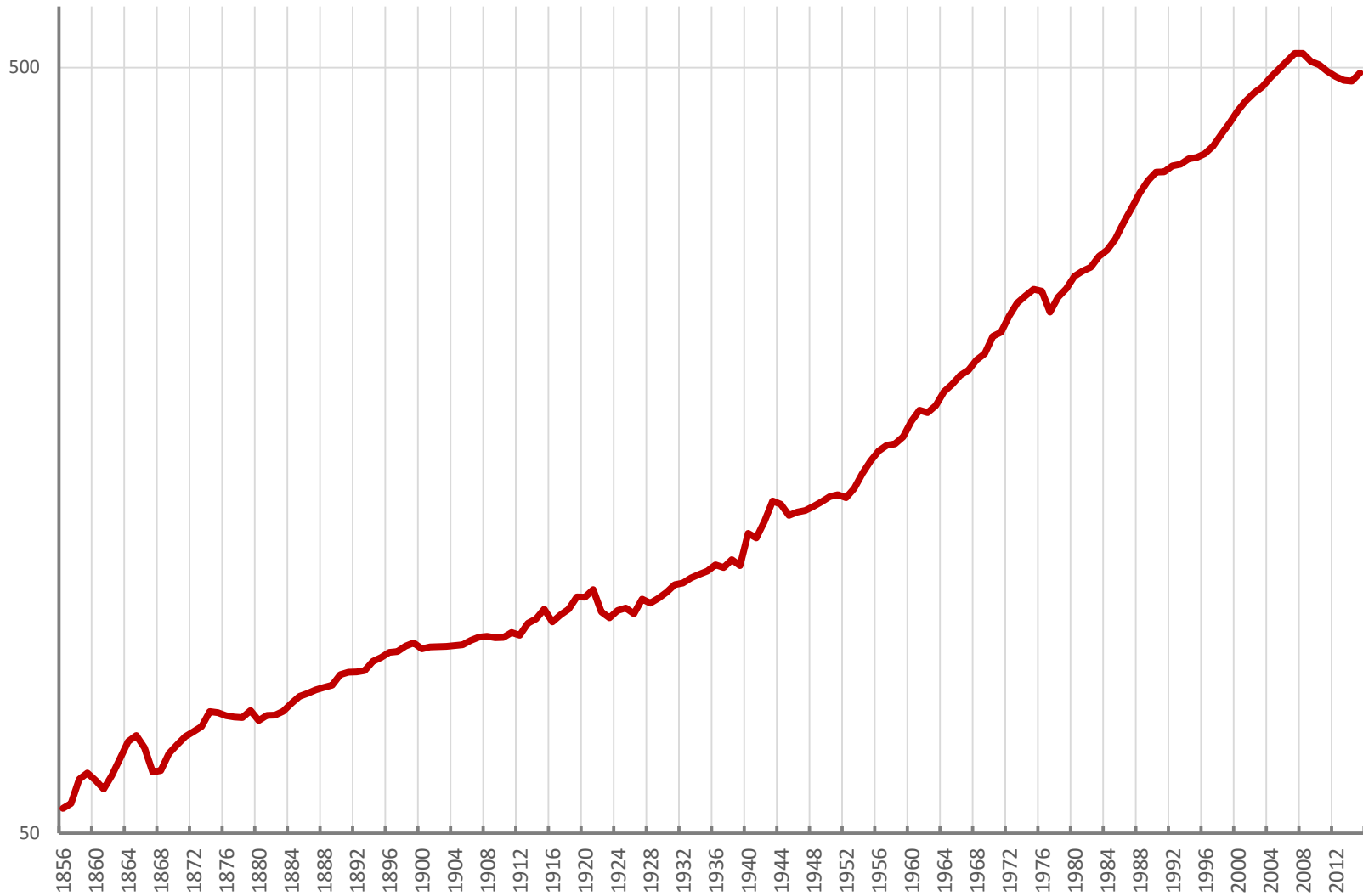
Geoff Tily, TUC

Outline

- 'Great stagnation' in real earnings
- Earnings v employment v GDP
- Government cuts and aggregate demand
- The productivity fallacy
- Wider failure of consolidation

'Great stagnation'

Level of real average weekly earnings, 2015 prices (log scale)



Real earnings in downturns, indices peak=100

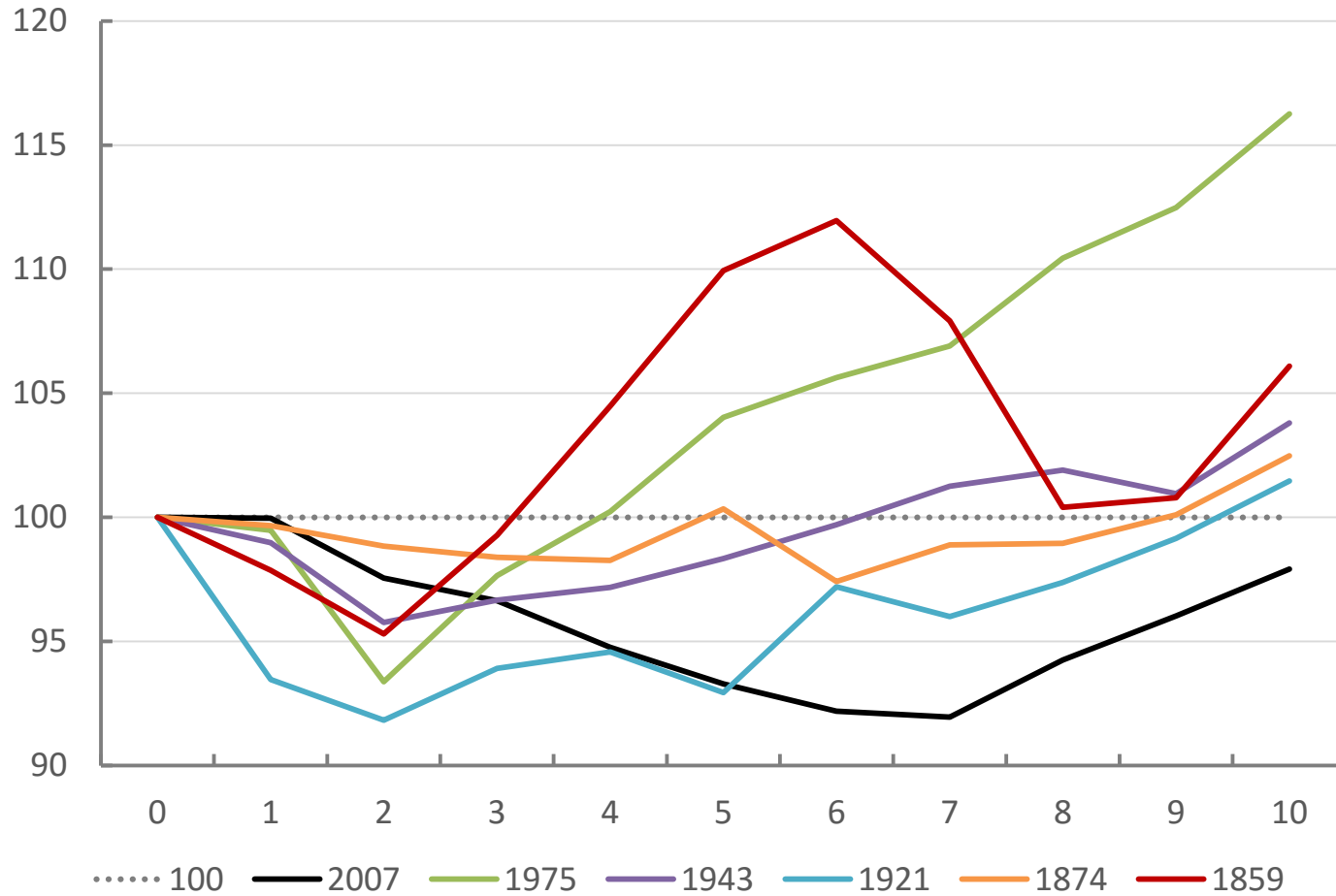
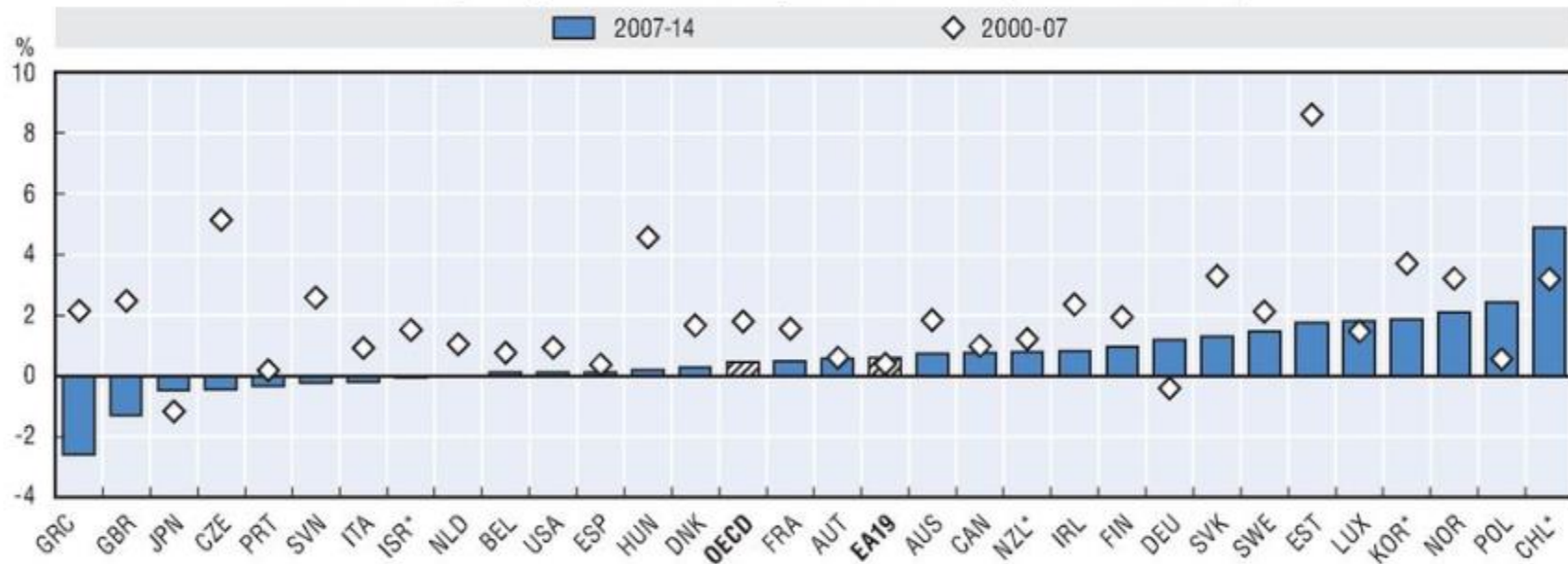


Figure 1.10. **Real hourly wage growth in OECD countries**

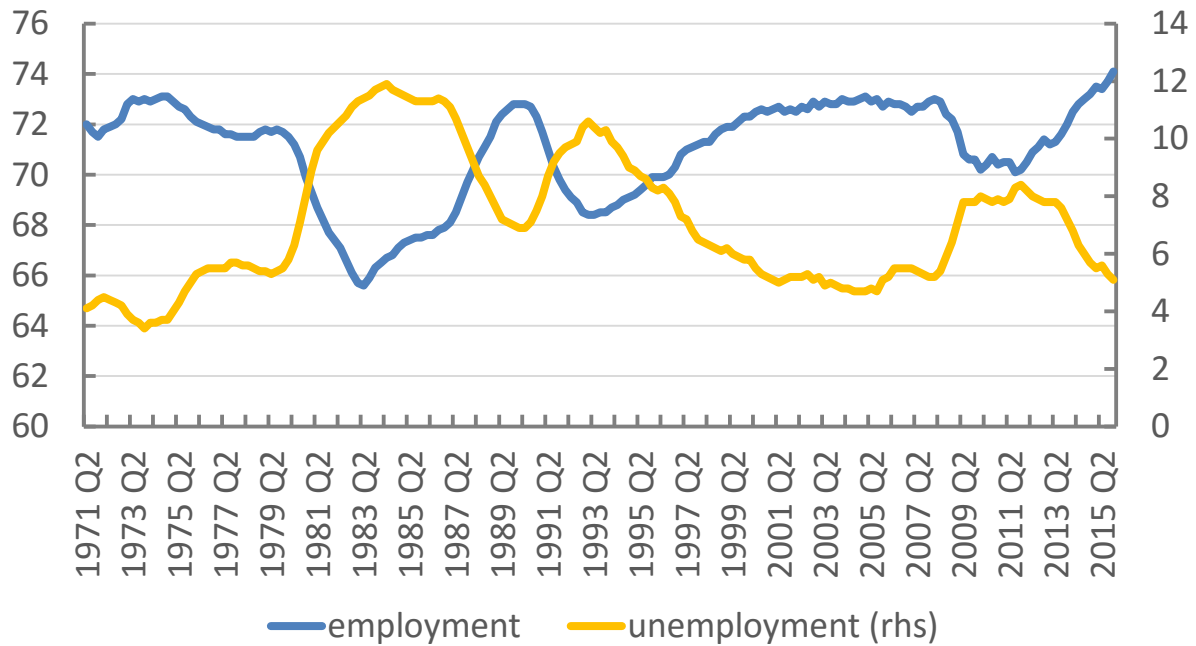
A. Annual average change before and after the global financial crisis (2000-07 and 2007-14)^a



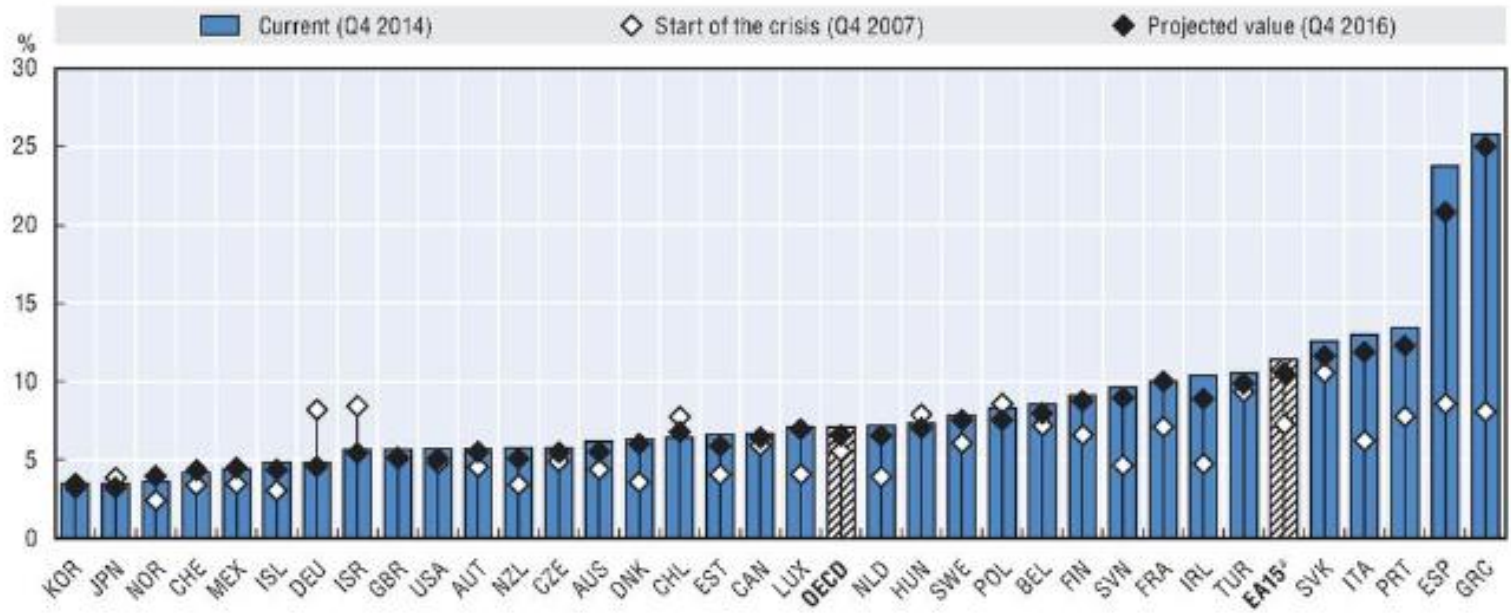
B. Percentage-point change in annual real hourly wage growth between 2000-07 and 2007-14^a



Strong employment headlines



A. Unemployment rate
Percentage of the labour force



B. Unemployment gap
Percentage-points change in the unemployment rate since the onset of the crisis (Q4 2007)

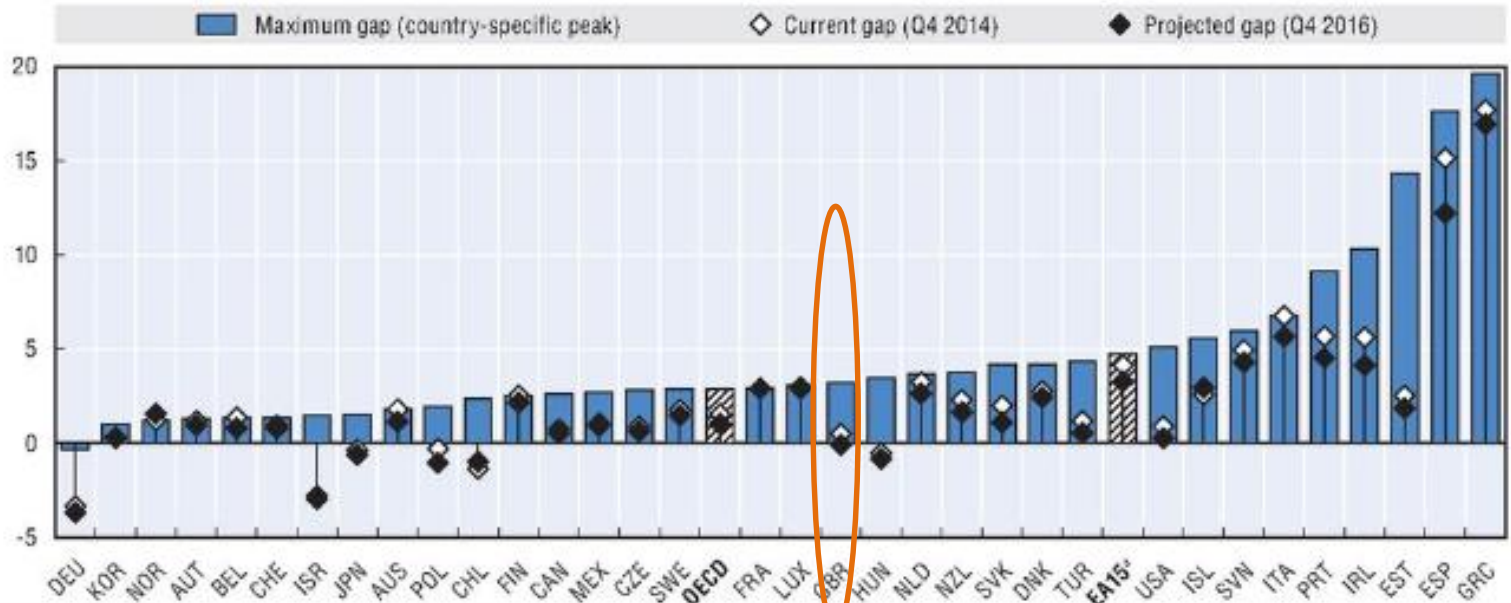
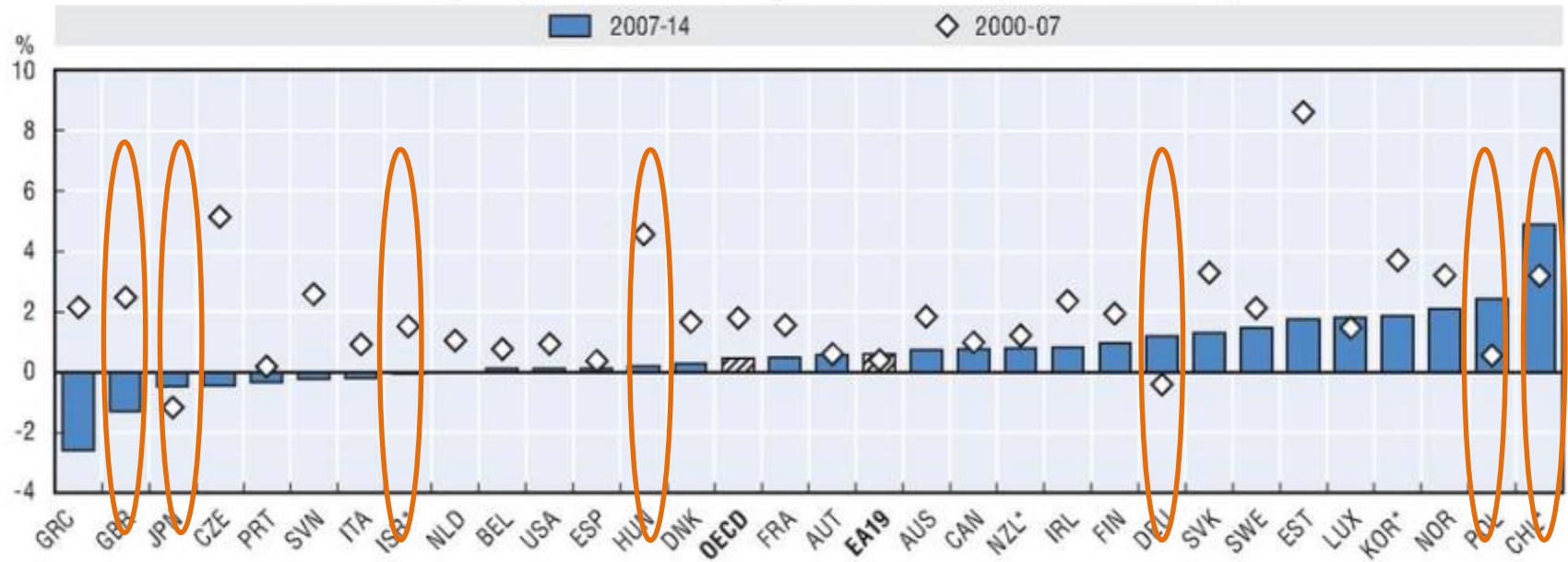


Figure 1.10. Real hourly wage growth in OECD countries

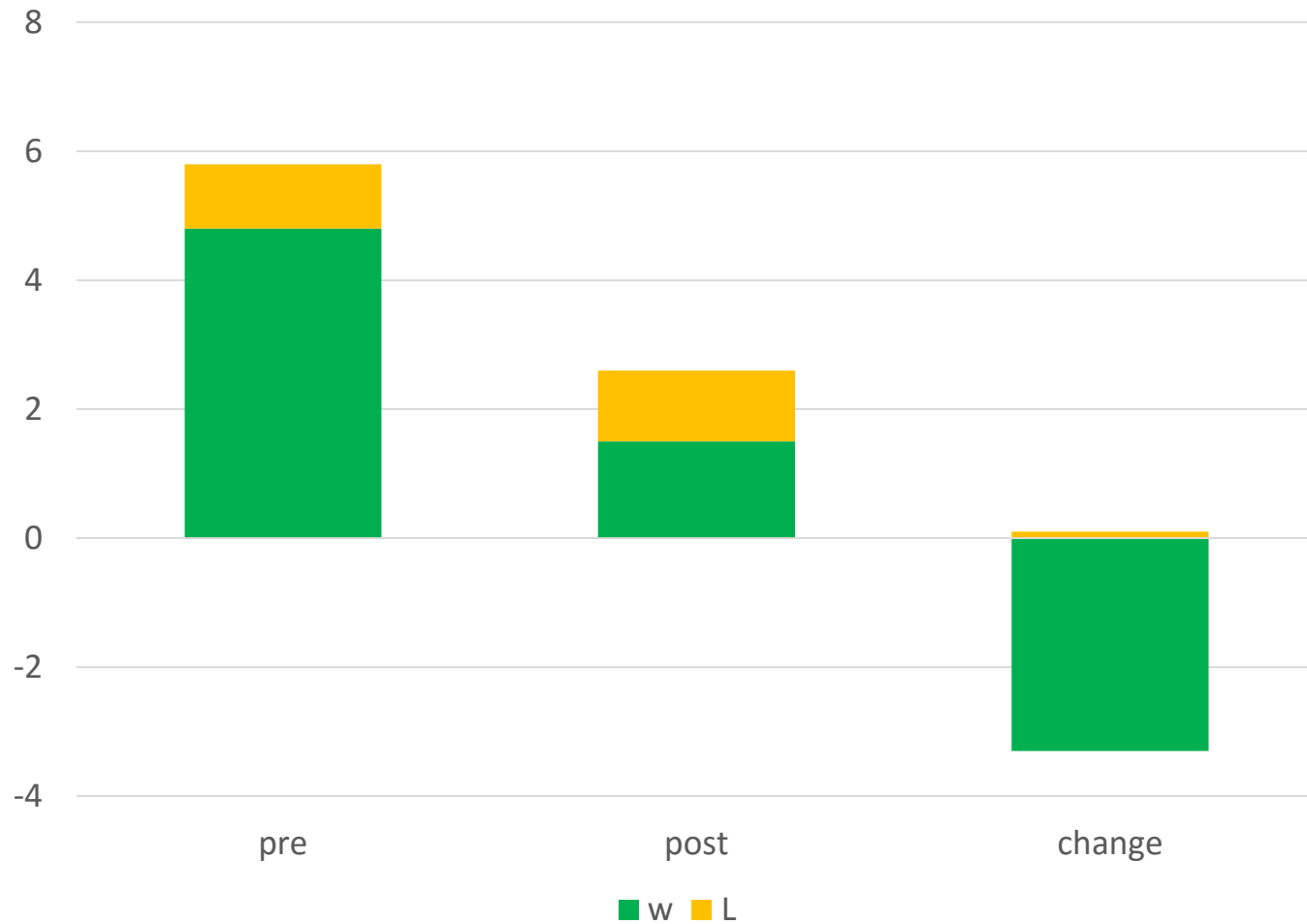
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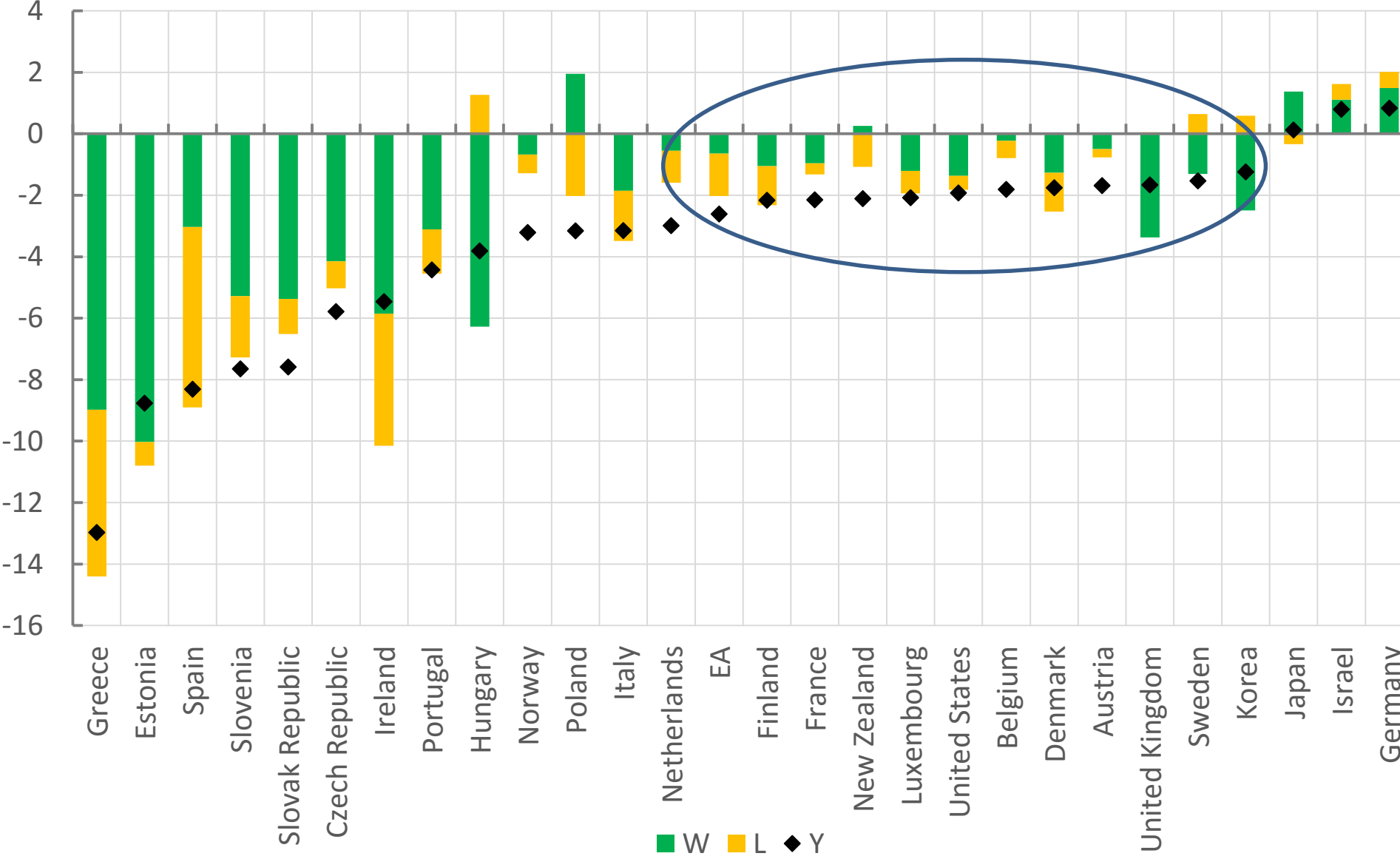


UK labour income growth



Labour market adjustment v GDP by country

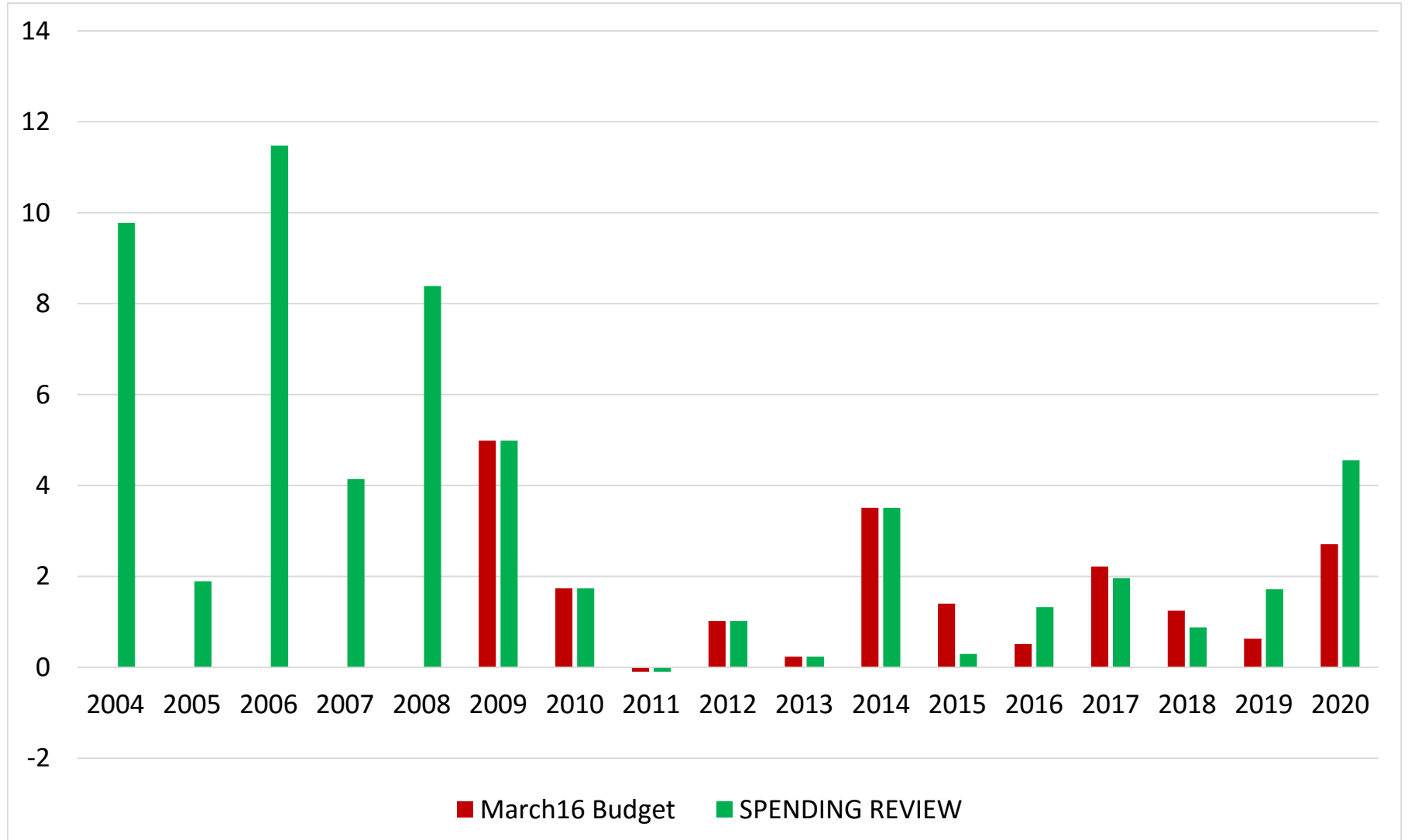
(change in annual average growth, post minus pre crisis)



Techniques

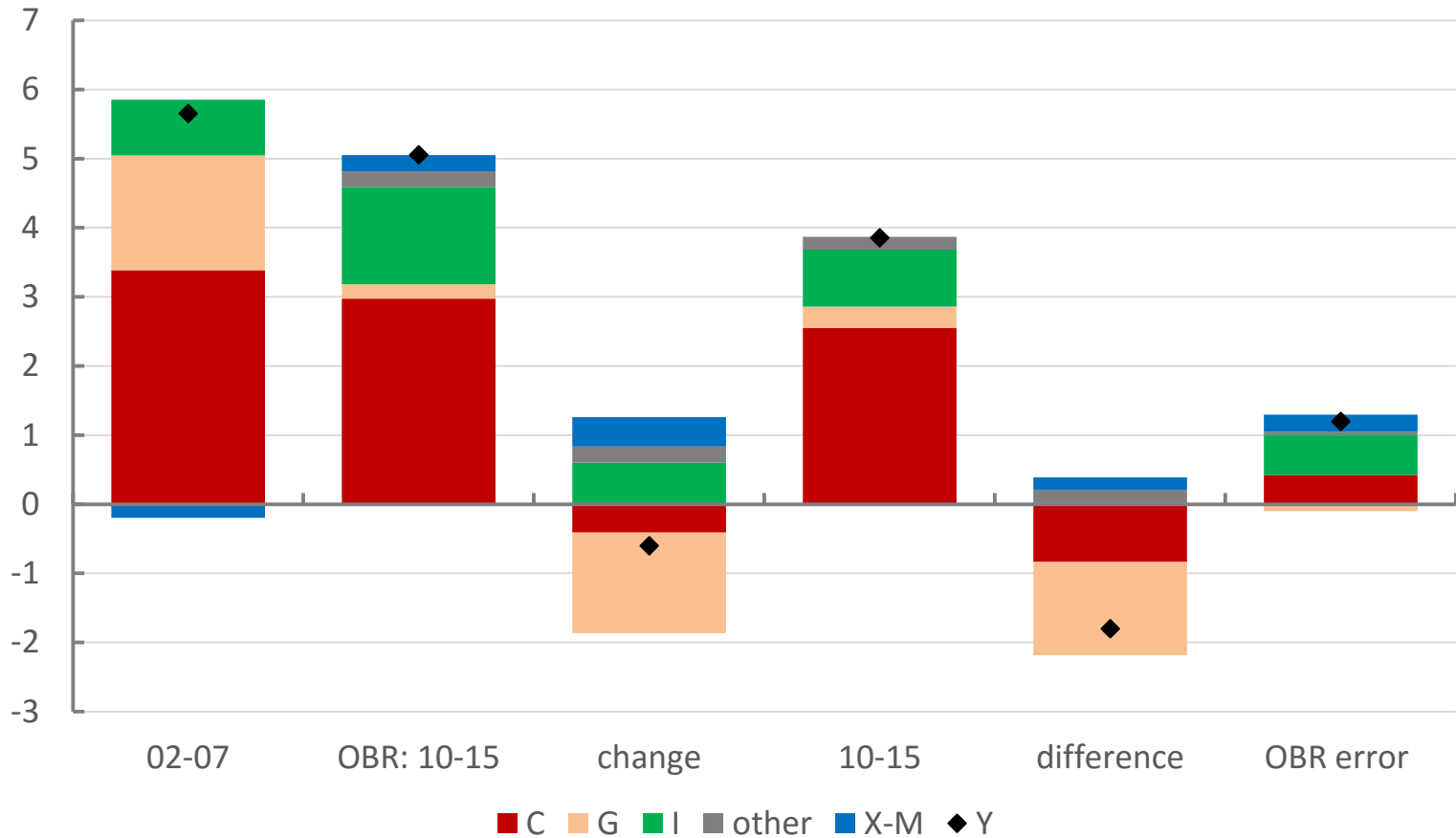
- Nominal figures
- General government final consumption + fixed capital expenditure (GGFCE + GGFCF)
- GDP expenditure and income
- Derive growth rates and contributions to growth
- Compare pre and post crisis
- (see what the OBR said too)

Government expenditure growth, per cent

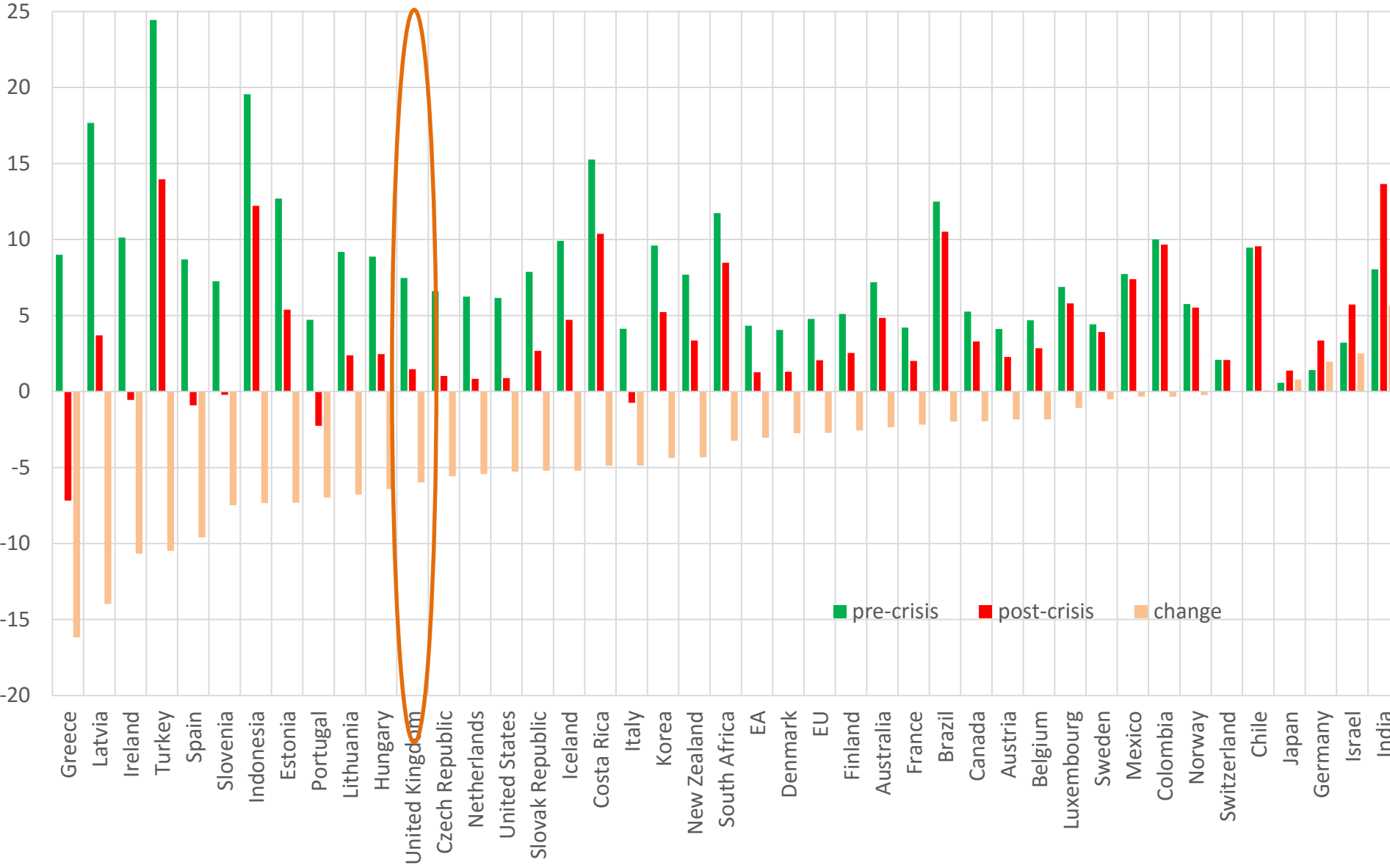


Low government spending growth reduced GDP growth

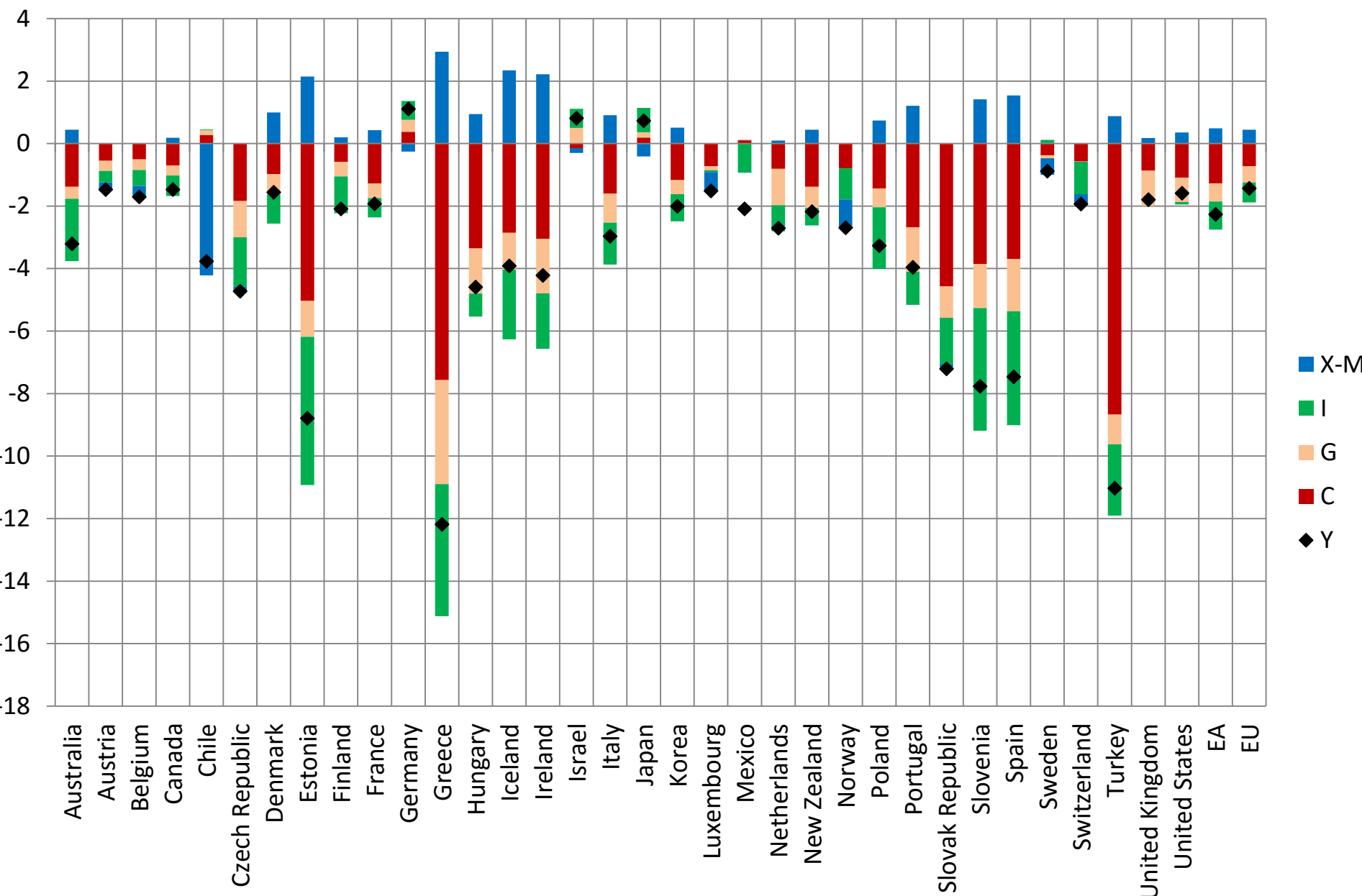
Contributions to GDP(E) annual average growth, percentage points



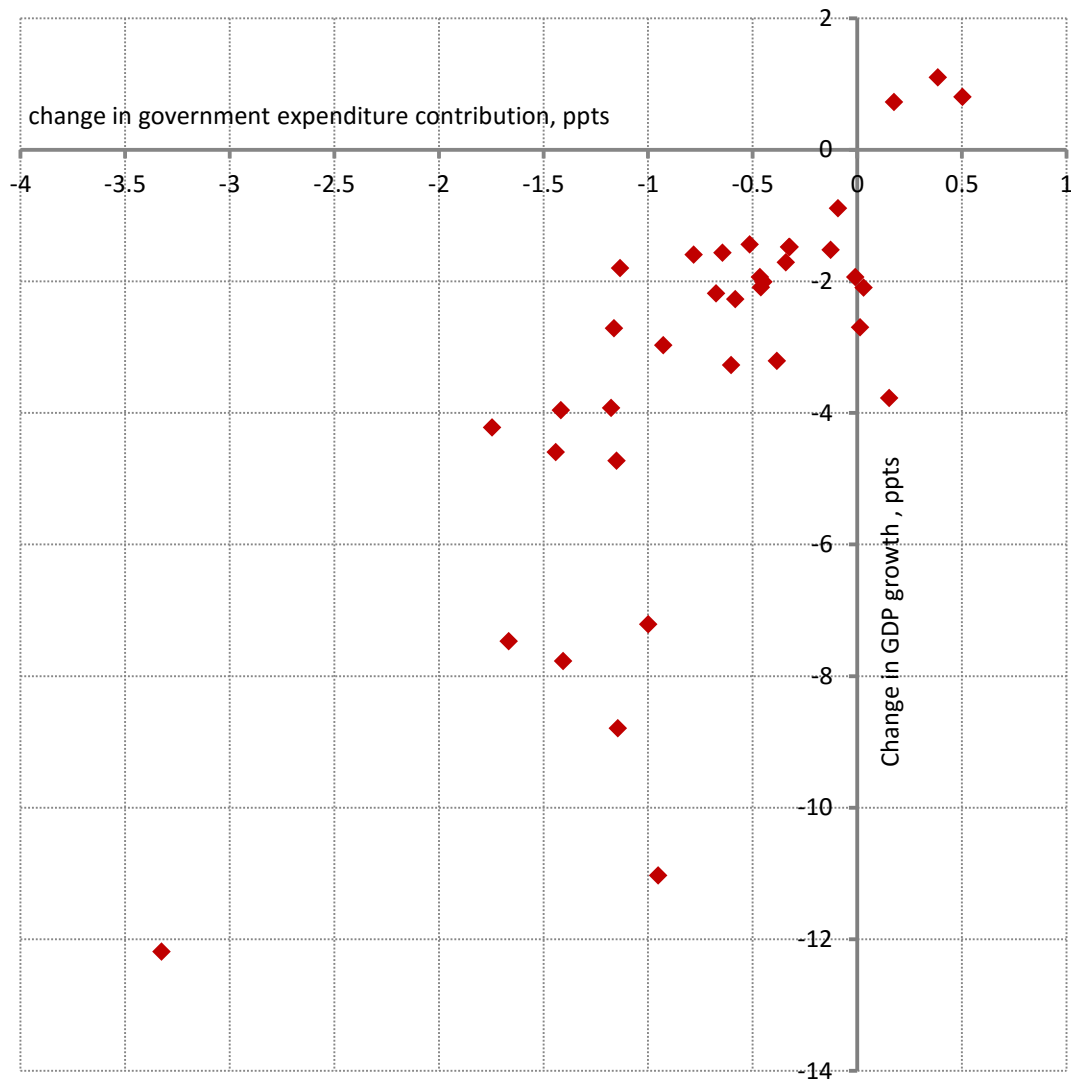
Government expenditure, annual average growth, %



GDP(E): change in contributions to growth, ppts



Regression of change in GDP growth against change in government expenditure contribution to GDP, percentage points

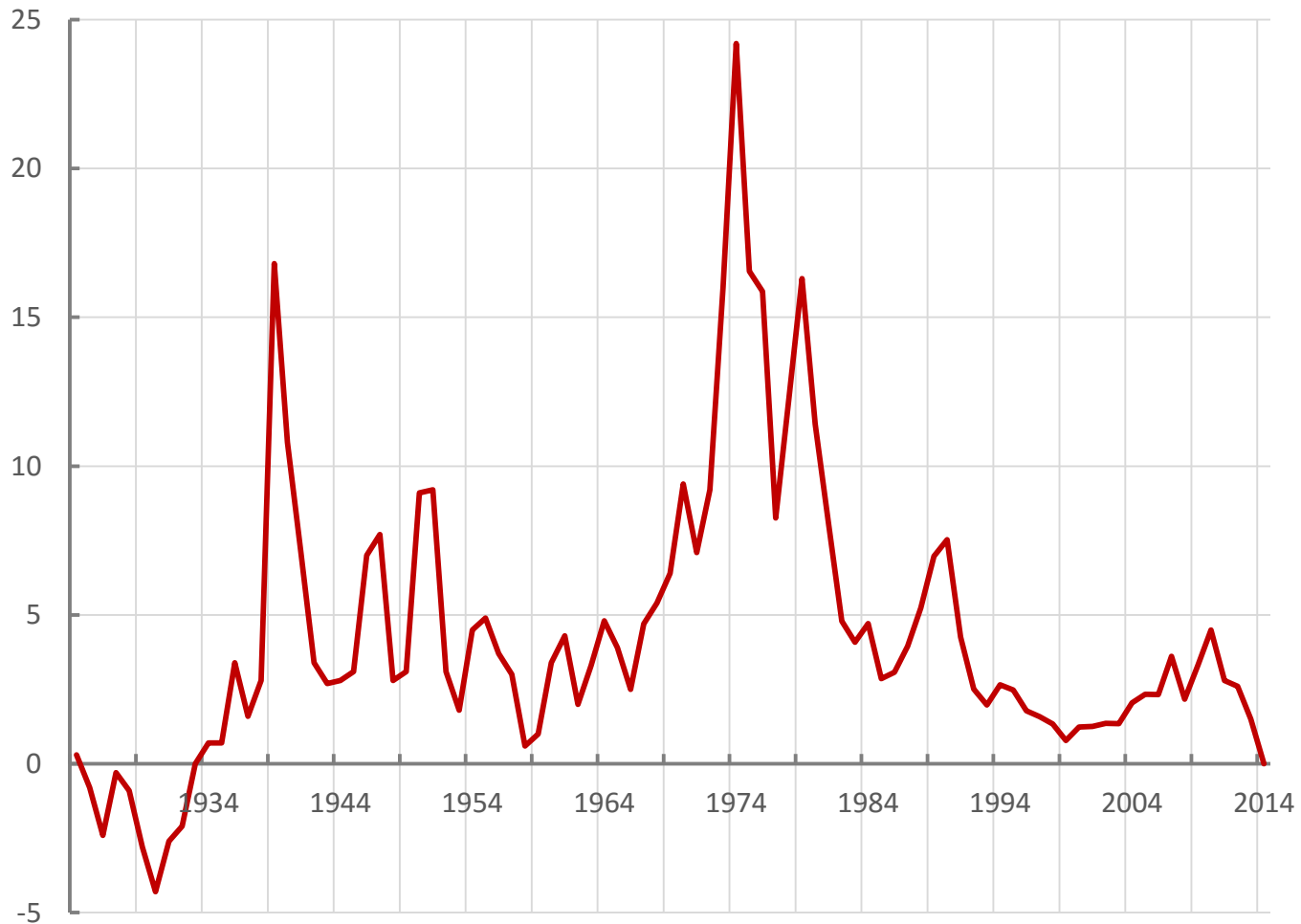


Productivity fallacy

- Tendency to read directly from low productivity to supply failure. Fallacy.
- Alternative: simply the way the labour market has adjusted to meet (demand driven) lower GDP growth through wages (P) rather than employment (Q)
- Productivity calculation compares low GDP growth with disproportionately high employment growth
- Causality reversed: the adjustment in the labour market is causing low measured productivity. Weak economy causing weak productivity.
- Not to deny fundamental importance of structural issues: financialisation, industrial policy, infrastructure etc.
- But in meantime, danger of missing scale of demand failure

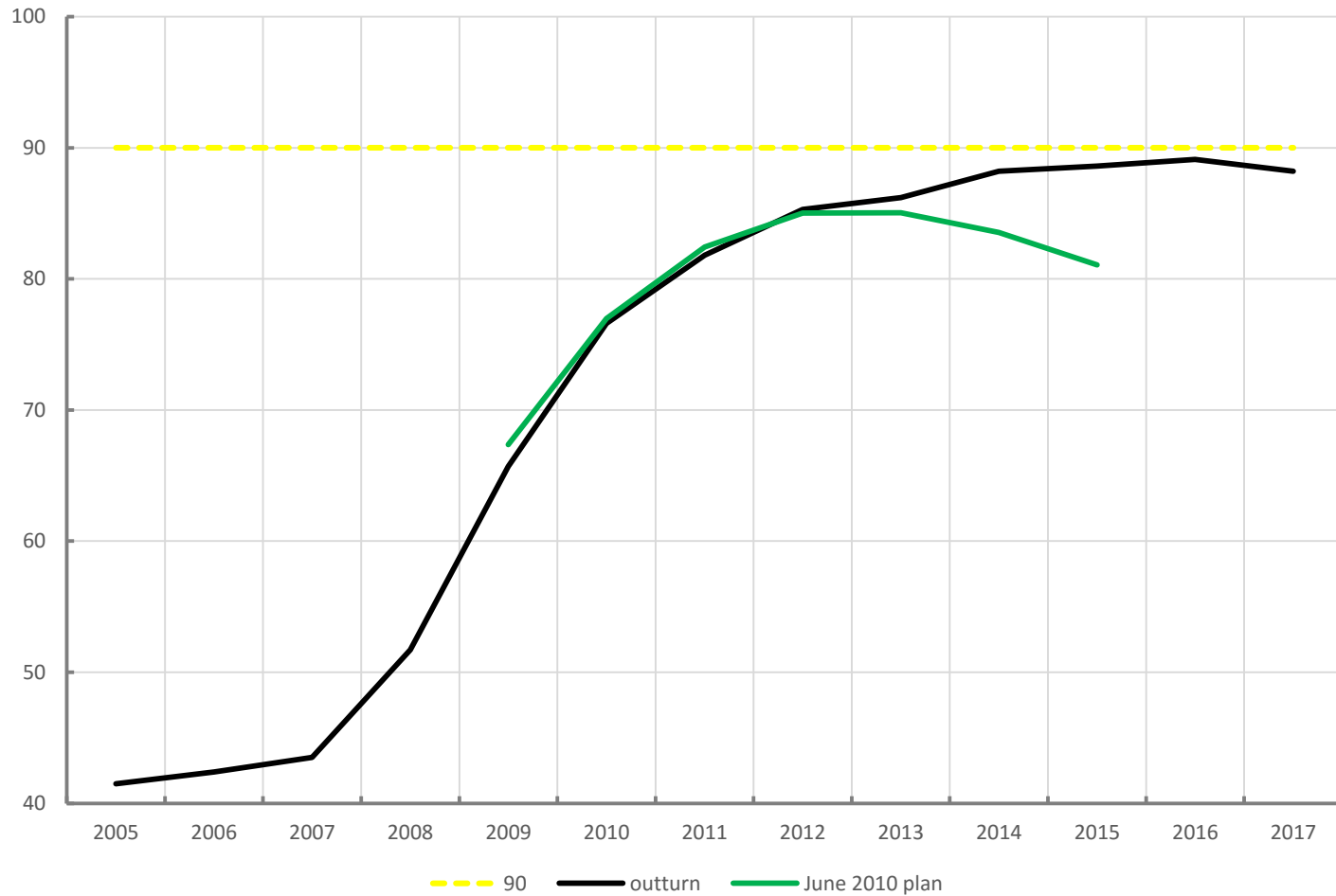
In 2015: lowest inflation since the Great Depression

CPI annual inflation, %



Sum of the parts, weak economy, weak wages, low revenues = 'consolidation' failed

Public debt, % GDP



Conclusion

- Great stagnation in earnings
- Reflects weakness of economy
- And demand deficiency
- Leads also to disinflation and failed government revenues
- Policy: expand demand

End

<http://touchstoneblog.org.uk/>

[@geofftily](#)

94 years of UK productivity growth

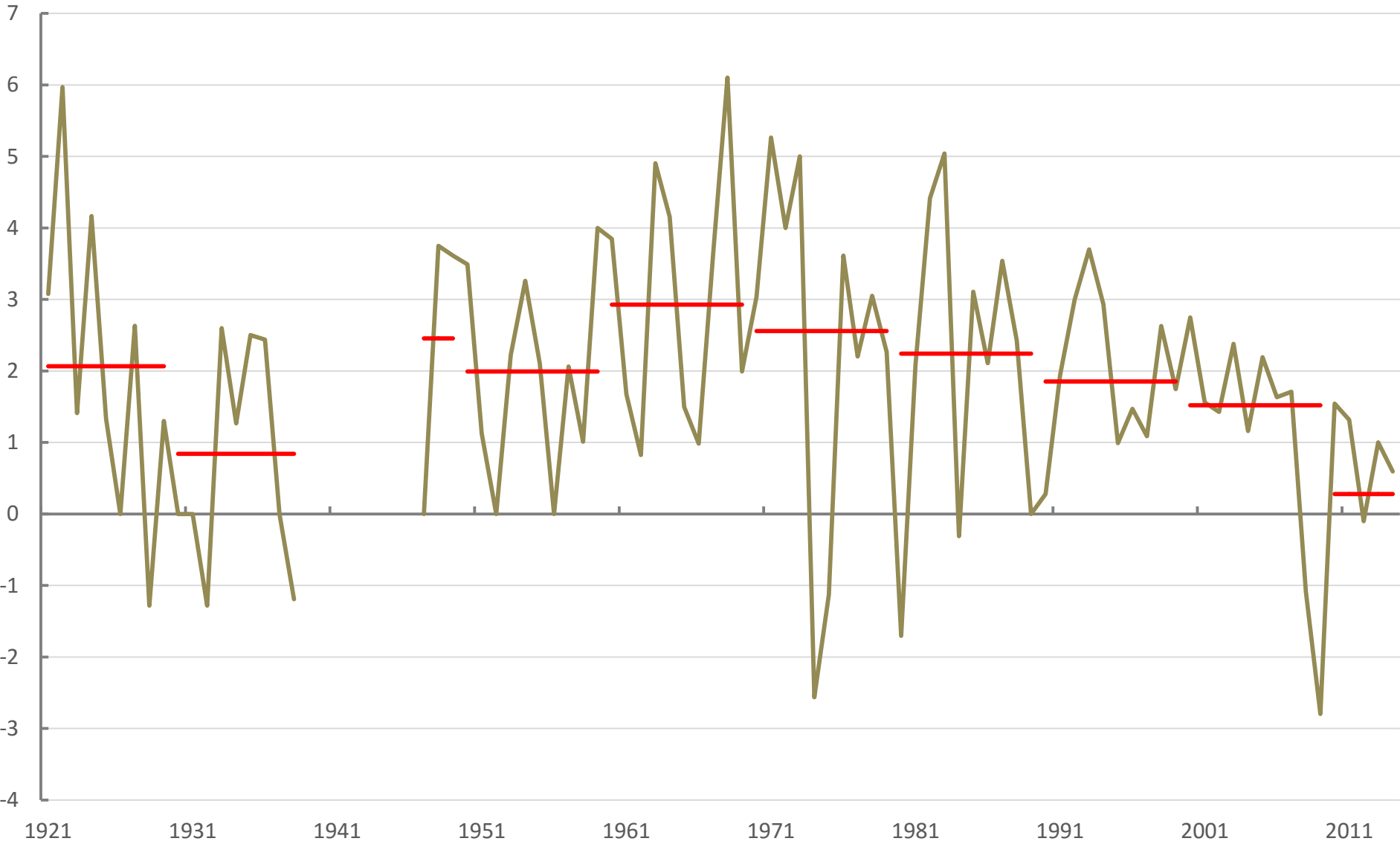
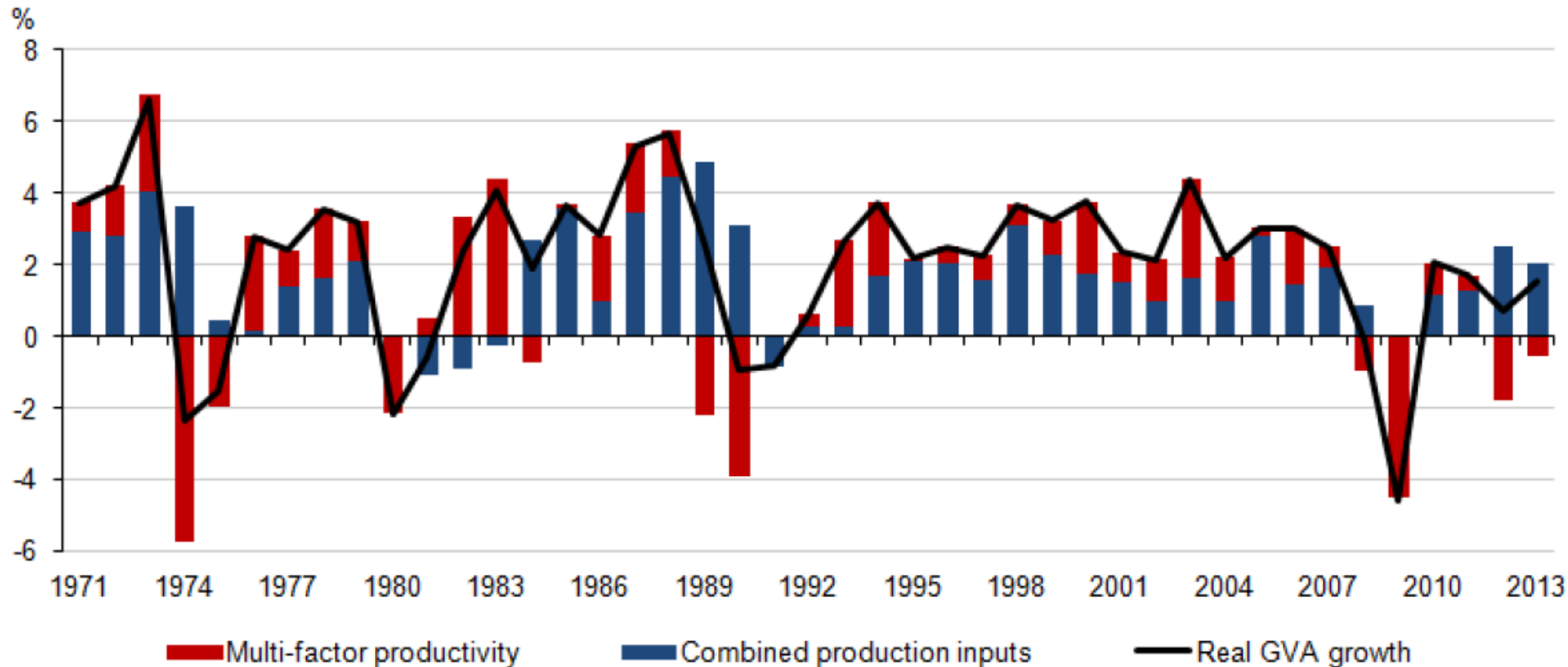
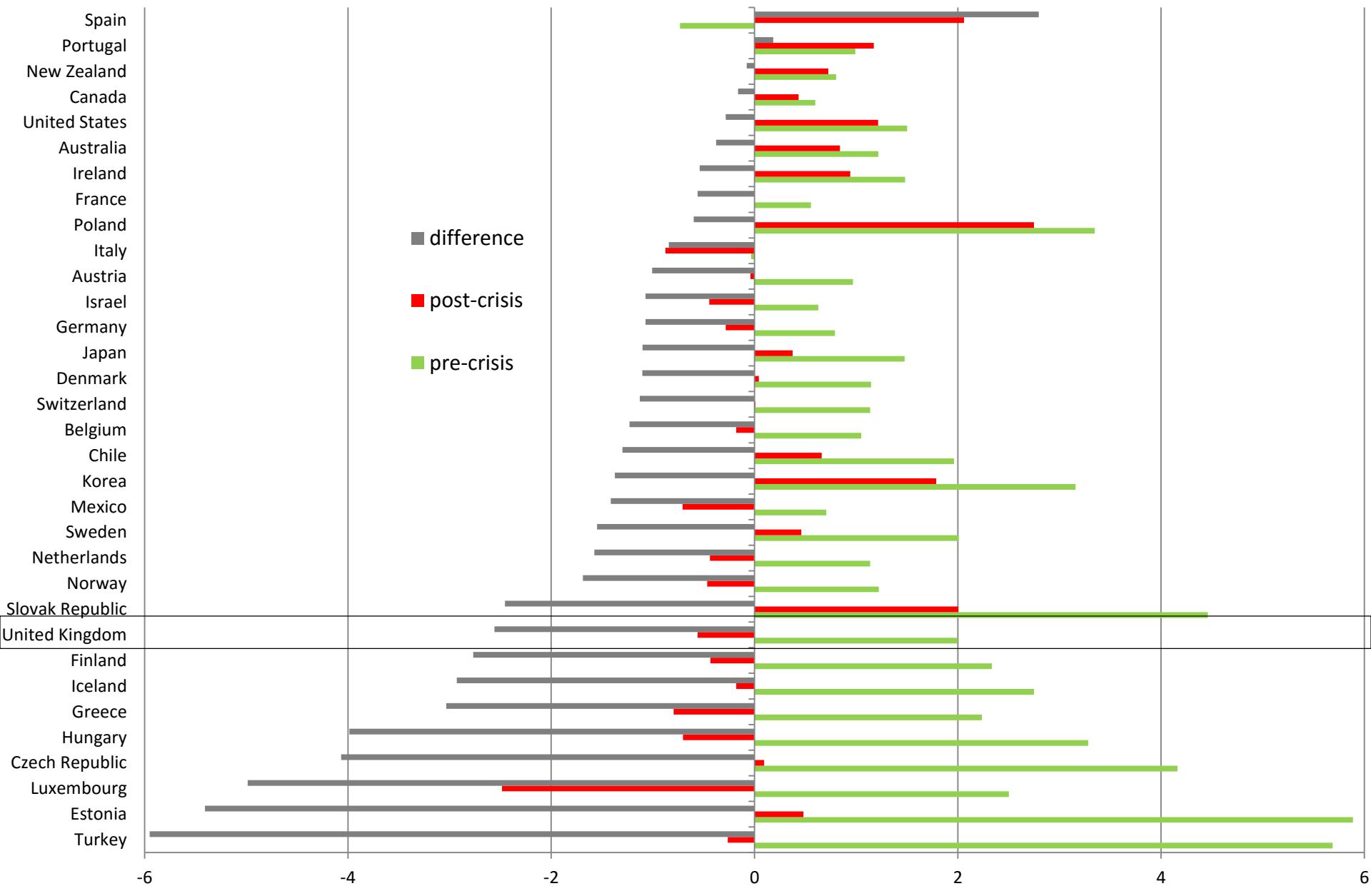


Figure 12: Contributions of factor inputs and Multi-Factor Productivity (MFP) to real Gross Value Added (GVA) growth: %



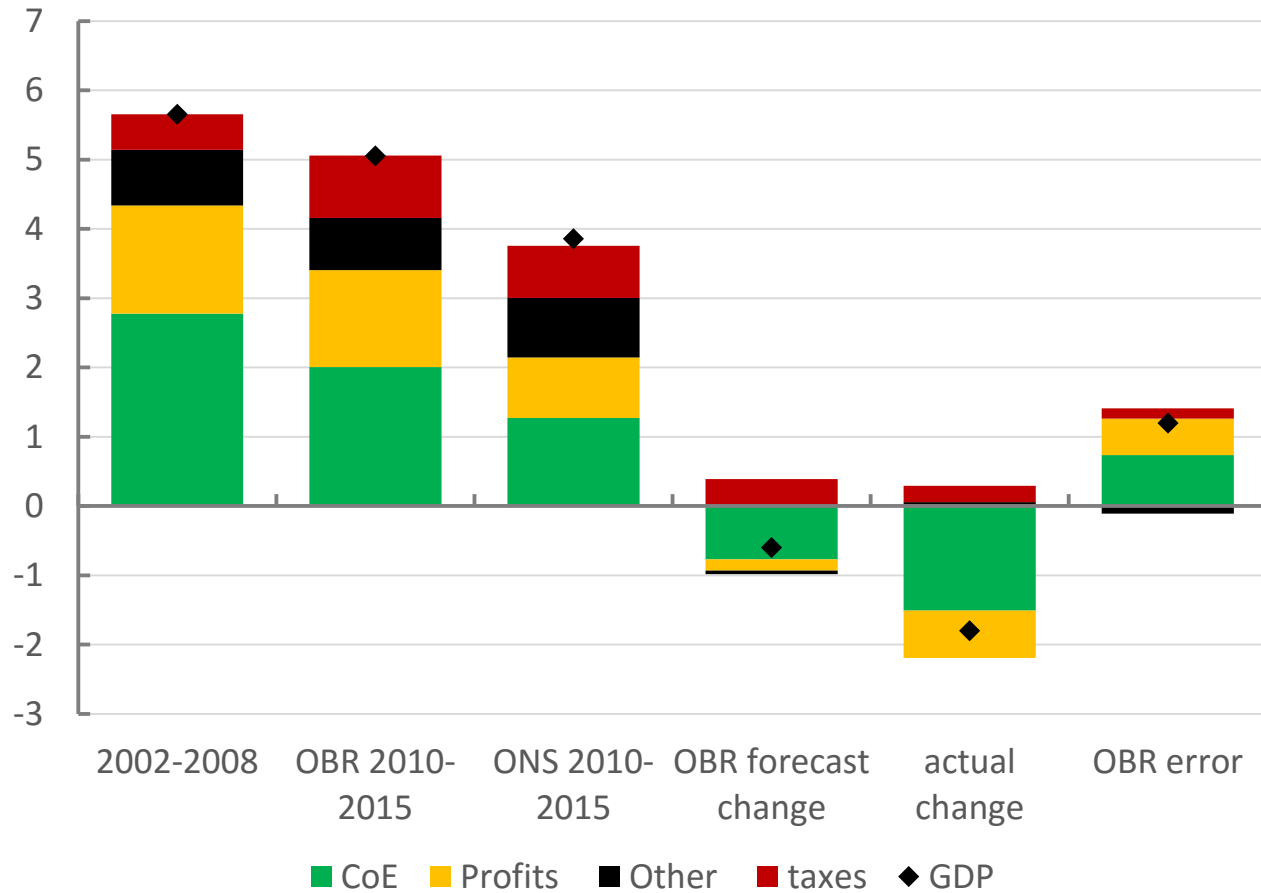
Source: ONS *Economic Review*, February 2015

Average annual growth in productivity pre and post crisis



Labour takes a bigger hit of the weaker growth

Contributions to GDP(I) growth, percentage points



Disproportionately met through reduced wages

Contributions to labour income growth (approx.)



When is productivity relevant?

- Outside full employment

$$\text{Productivity} = \text{GDP} / f(\text{GDP}(I))$$

- E.g. profits ...
- A relevant diagnostic, but not as causal
- If we are below capacity, demand is key factor
- Under spare capacity, economic 'growth' potentially misleading: rate of utilisation of spare capacity
- One cause of inflation is excessive speed
- IMHO, there has always been spare capacity