ECONOMIC VIEWPOINT

Is the Trend in Wages Different in Europe, the United States and Canada?

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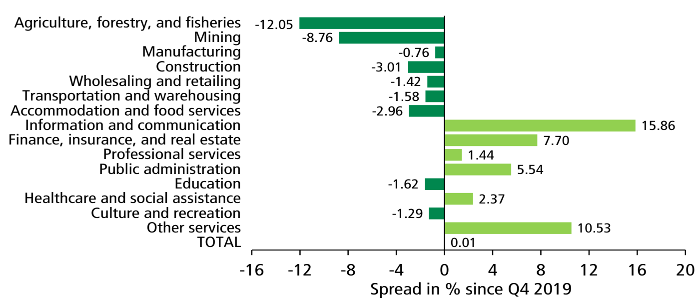
A growing number of economies have returned to pre-pandemic activity levels. However, the recovery continues to be uneven across countries and sectors, as the global economy has been hampered by new waves of COVID-19 and bottlenecks continue to disrupt the fluidity of supply chains. Coupled with a sustained demand for goods, these obstacles have fuelled inflationary pressures in many sectors, including energy, auto and manufacturing. As mentioned last fall in an *Economic Viewpoint*, the danger of sharp price increases is that they may cause an inflationary spiral in which inflation spreads across the entire economy and becomes self-sustaining, leading for example to wage inflation. The purpose of this document is to shed light on and compare the wage pressures observed in Europe, the United States and Canada. For the time being, the fastest acceleration in wage growth is occurring in the United States, due in part to a more serious worker severe than in the rest of the West.

The wage issue is a very important one in the current situation. In response to higher inflation, workers may demand bigger wage increases. This wage growth results in higher operating costs for companies, which may be partly or fully passed on to consumers through price increases. An inflationary spiral therefore sets in as price hikes drive up wages, which in turn worsen inflation. Major advanced economies are not yet showing that such a scenario is really taking shape and even less so that it is becoming widespread. However, interesting differences emerge in wage pressures among the main areas.

Partial and Uneven Labour Market Recoveries around the World

By the third quarter of 2021, the European Union (EU) had recovered to its pre-pandemic employment level, but some countries, such as Germany (-330,000 jobs), still have a significant shortfall. Even for the EU as a whole, the situation is very different when we look at the sectors. Some industries, such as agriculture, mining, and fishing, which were already struggling before the pandemic have a significant number of jobs to fill (graph 1). Other industries, such as food services and accommodation, have long struggled with public health measures restricting their activities and discouraging workers from returning. Support policies developed by the EU and its member countries have lessened the effects of the pandemic on employment, unlike in the United States and Canada.

GRAPH 1
The recovery in employment has been uneven across sectors in the EU

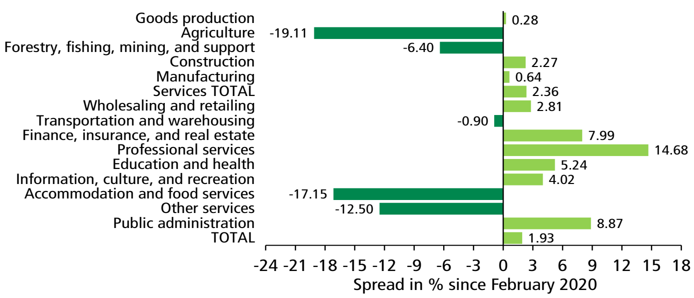


EU: European Union
Sources: Eurostat and Desjardins, Economic Studies

Europe's strategy was more focused on curbing job losses by allowing companies to reduce wages and employee hours, while making up the difference through government transfers. Industries able to better adapt to telework, such as information and communication, or even the financial sector saw their job numbers rise since the start of the pandemic.

In Canada, there are some similarities with the EU labour market situation. The agriculture industry was also hit hard due to poor harvests and a lack of foreign workers. Just like in Europe, the unfavourable circumstances of the pandemic hindered job recovery in food services and accommodation (graph 2). Since the Canadian government's strategy was aimed at supporting workers who had lost their jobs, a greater shortage than in the EU is noted in these sectors. Despite the challenges faced by some service industries, data for February 2022 show a 2.4% gain since February 2020 for all services owing to strong performance in financial and professional services and in education and health. In Canada, total employment therefore surpassed its pre-pandemic level by 1.9% in February, despite the decline caused by the Omicron wave.

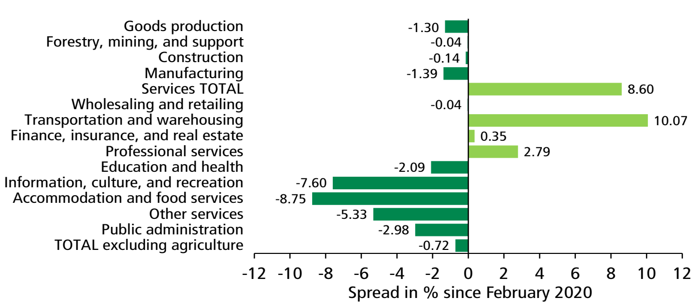
GRAPH 2
Overall, employment in Canada has recovered to its pre-pandemic level



Sources: Statistics Canada and Desjardins, Economic Studies

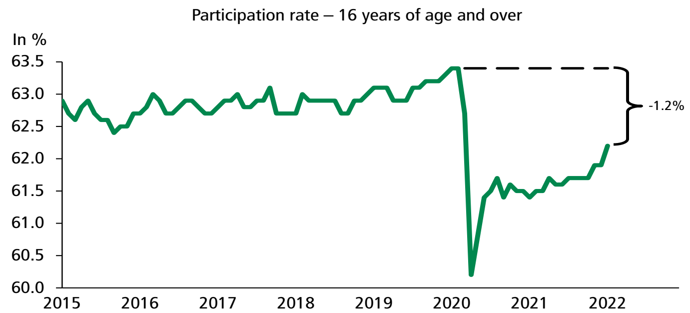
The United States, meanwhile, is dealing with a significant worker shortage. Only transportation and warehousing, the financial sector and professional services have had positive gains since February 2020 (graph 3). Service industries that involve human contact, such as food services and accommodation, are having the hardest time catching up. The decline in the participation rate in the United States reflects the magnitude of the labour shortage and the pandemic's repercussions on the job market. The latest data show that the participation rate is at 62.2%, compared to 63.4% before the pandemic (graph 4).

GRAPH 3
The U.S. job market still has a significant shortfall



Sources: Bureau of Labor Statistics and Desjardins, Economic Studies

GRAPH 4
Many Americans left the job market altogether

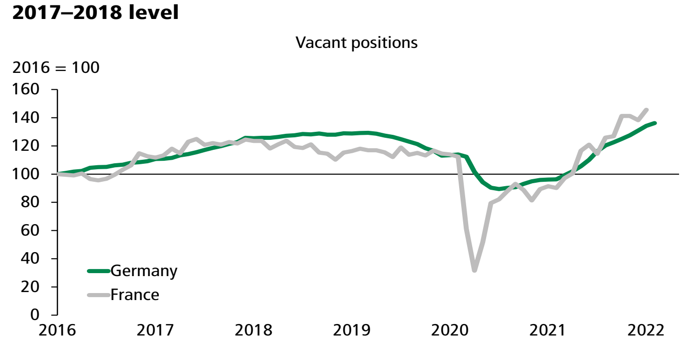


Sources: Bureau of Labor Statistics and Desjardins, Economic Studies

No Unusual Wage Growth in Europe for Now

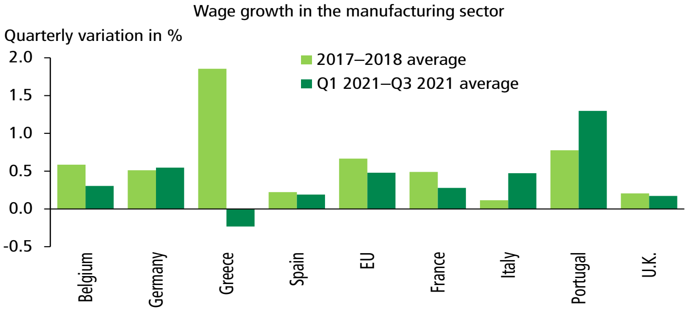
In Europe, the trend in manufacturing wages is generally a good leading indicator for wages in the entire economy. Since industrial unions are powerful, the outcomes of their wage negotiations usually set the tone for those in other sectors. For now, wage pressures have remained modest, even though the number of vacant positions has exceeded 2017–2018 highs (graph 5). Therefore, it seems that a large number of vacant positions is not necessarily putting upward pressure on European wages, including in manufacturing (graph 6 on page 3). For the time being, the demands of manufacturing unions continue to be reasonable, even though the economic activity has been very strong due to the demand for goods, which exploded during the pandemic. This is due to the retrospective nature of wage negotiations, in which it typically takes a few quarters for past inflation and labour shortages to be considered fully. Under these circumstances, wages in the European manufacturing sector could eventually react.

GRAPH 5
The number of vacant positions in Europe exceeds 2017–2018 level



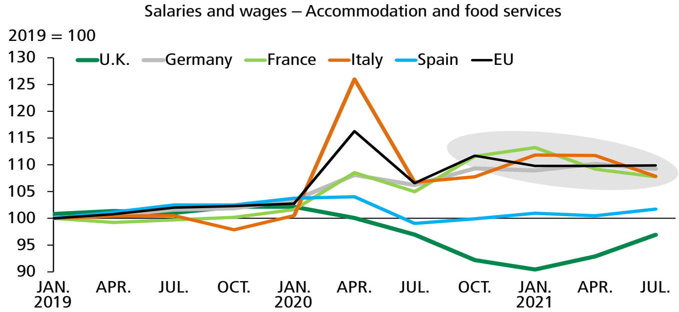
Sources: Datastream and Desjardins, Economic Studies

GRAPH 6
No acceleration in manufacturing wages in Europe



EU: European Union
Sources: Eurostat, Office for National Statistics and Desjardins, Economic Studies

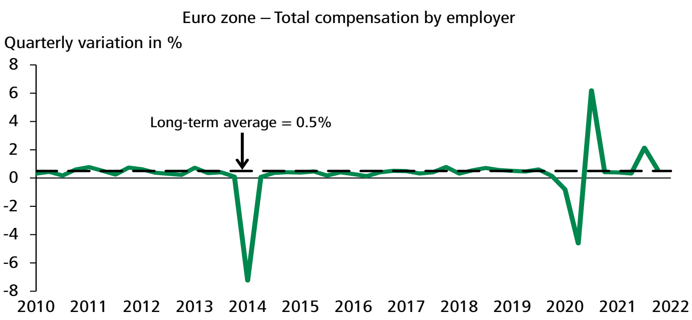
GRAPH 8
Lower European wages in accommodation and food services in 2021



EU: European Union
Sources: Eurostat and Desjardins, Economic Studies

A temporary acceleration has also been noted in the quarterly variation in total compensation per employee in the euro zone exceeding its long-term average (graph 7). It remains to be seen if it reflects a reaction to persistent inflationary pressures. Moreover, like the current U.S. situation, the wage push could instead be felt more not in manufacturing, but in the services sector, particularly accommodation, food services and recreation. An increase was already observed at the very beginning of the pandemic, but salaries and wages in accommodation and food services have been slightly falling since the end of 2020 in the EU (graph 8). The situation is the same for the arts, entertainment, and recreational activities, with a 5.0% drop over the past year. These are sectors whose profitability has been tremendously impacted by the public health measures and the absence of foreign tourists. The acceleration in demand for services could lead to upward pressure on wages in these industries, especially if they are faced with recruitment challenges.

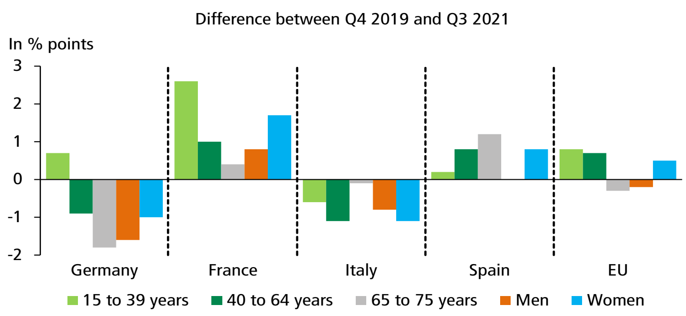
GRAPH 7
We are seeing a temporary acceleration of wage growth in Europe



Sources: European Central Bank and Desjardins, Economic Studies

In addition, the good recovery in the labour force in Europe may have been another factor that worked against steep wage increases. According to data for the third quarter of 2021, Germany and Italy have a participation rate lower than their pre-pandemic levels, whereas France and Spain have posted gains (graph 9). The differences between the recovery in the European and U.S. participation rates also help to explain the wage growth differences.

GRAPH 9
Good participation rate recovery in the EU

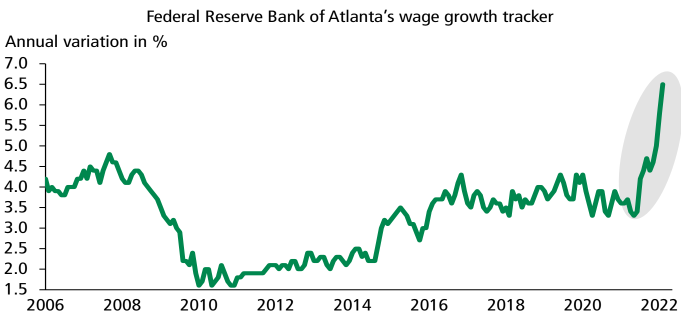


EU: European Union
Sources: Eurostat and Desjardins, Economic Studies

Wage Pressures in the United States

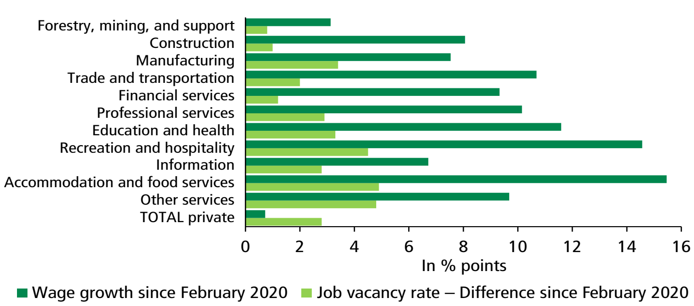
In the United States, the situation is more worrisome because the job market is facing two factors that are exacerbating the upward pressure on wages. First, the weak recovery in the participation rate results in a smaller pool of candidates for vacant positions. Then, a phenomenon called *The Great Resignation* has taken place in the United States, which is an acceleration in the number of workers voluntarily leaving their jobs for better ones or exiting the labour market altogether. As a result, U.S. companies are facing significant challenges in recruiting and retaining workers. Faced with this problem, they must raise wages to attract more workers and keep current employees. Consequently, a strong acceleration in hourly wages is being seen in the United States. The median wage tracker of the Federal Reserve Bank of Atlanta posted an annual variation of 6.5% in February, a level not seen since 2001 (graph 10). Hourly wages are rising even more remarkably in the services sector, particularly in recreation and hospitality (graph 11).

GRAPH 10
Strong acceleration in wage growth in the United States



Sources: Federal Reserve Bank of Atlanta and Desjardins, Economic Studies

GRAPH 11
Wage growth is stronger in services in the United States



Sources: Bureau of Labor Statistics and Desjardins, Economic Studies

While upward pressures on wages stem from a lack of workers, others could come from the high inflation currently observed in the United States. This worries U.S. companies (graph 12). The National Federation of Independent Business survey shows that inflation is the main problem for 22% of respondents, just below workforce quality, with 23%.

The labour shortage, however, could affect the U.S. job market for a long time to come. The participation rate might take up to eight years to recover, according to a Federal Reserve study. Since the beginning of the pandemic, participation has been declining among young people, unskilled workers, seniors, and family caregivers, particularly women. First, when younger people leave the labour force, they tend to return to school to eventually access better jobs or wait some time until the situation

GRAPH 12
Labour and inflation issues are worrying U.S. small enterprises

Sources: National Federation of Independent Business, Datastream and Desjardins, Economic Studies

is more favourable before re-entering the labour market. Although the first young people who went back to school should begin to re-enter the labour market, the positive effect on the participation rate may be offset by retirements due to the aging of the population.

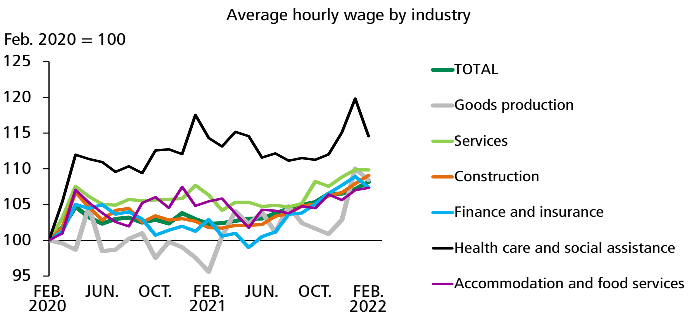
Rising Expectations in Canada

Just like its neighbour to the south and its European counterparts, Canada has seen strong growth in the number of vacant positions from pre-pandemic levels. The total number of job vacancies increased by 180,000 in the second and third quarters of 2021. Again, the food services and accommodation industry lead the group with a vacancy rate of 12.9% in the third quarter of 2021, compared to 4.4% in the fourth quarter of 2019. Labour shortage problems in Canada are nothing new and were already viewed as a major economic challenge before the pandemic.[1] In addition, inflation in Canada is not as bad as south of the border, at 5.7% in February 2022, compared to 7.9% in the United States. This could somewhat alleviate some of the upward pressure on wages. No strong average hourly wage acceleration has therefore been noted for the time being, except in health care and social assistance (graph 13 on page 5). Like in Europe, the good recovery in the participation rate does not seem to weigh in favour of steep wage increases. However, there is stronger growth in services than in goods production.

Although wage growth remains moderate, there has been an increase in wage growth expectations according to the Canadian Federation of Independent Business survey (graph 14 on page 5). In the last 12 months, the percentage of respondents expecting wage increases above 2% increased from 22.6% to 53.5%. The average expected increase in February 2022 was 2.9%, just under its record level of 3% in December 2021. These rising expectations are consistent with the higher prices

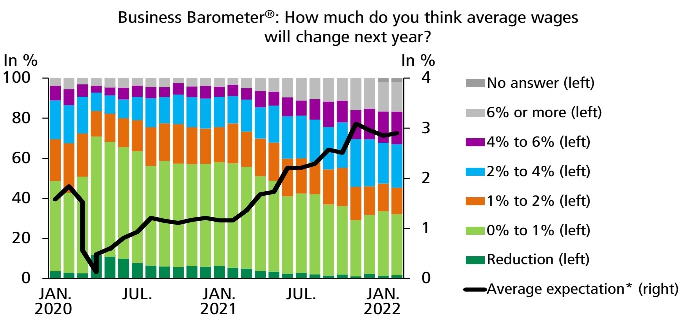
[1] For more details, see: Labour Shortages in Quebec and Ontario: Which Regions and Economic Sectors are Most Affected?, Desjardins, Economic Studies, *Economic Viewpoint*, March 13, 2019, 5 p.

GRAPH 13
Upward pressure on wages is still limited in Canada



Sources: Statistics Canada and Desjardins, Economic Studies

GRAPH 14
Sharp rise in wage growth expectations



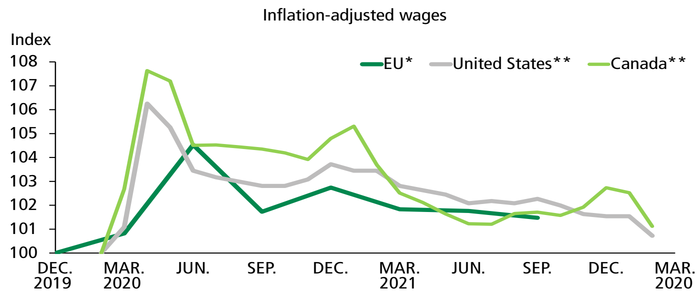
* Bimonthly data from March to May 2020.
Sources: Canadian Federation of Independent Business and Desjardins, Economic Studies

Canadians are seeing. This survey shows the current rigidity in wages and companies' willingness to raise them. Some acceleration in wage growth can therefore be expected. Lastly, the recurring problem of labour shortages coupled with rising consumer prices and the economic consequences of the pandemic could put more upward pressure on some sectors, particularly where the lack of workers is most acute.

Inflation Is Catching Up with Wages

In a context marked by high inflation, a sharp wage increase does not necessarily make workers better off. Nominal wage increases are offset by higher inflation (graph 16). Although real wages, that is inflation-adjusted wages, made some gains at the beginning of the pandemic, those have largely been wiped out. Consequently, real wages in Canada, the United States and the EU grew 1.1%, 0.7% and 1.5%, respectively, from their pre-pandemic levels. Workers' purchasing power has not improved much as a result but has not been completely eaten away by inflation either.

GRAPH 15
Real wage gains are limited by rising inflation



EU: European Union;
* Labour cost index: Q4 2019 = 100; ** Average hourly wage: February 2020 = 100.
Sources: Eurostat, Bureau of Labor Statistics, Statistics Canada and Desjardins, Economic Studies

A lower inflation and a less severe labour shortage than in the United States have led to slower growth in Canadian and European nominal wages. However, inflation continues to accelerate everywhere, a situation recently exacerbated by Russia's invasion of Ukraine and the economic sanctions that followed. Strong inflation should continue to drive wage increases. The reopening of the last sectors still under COVID-19 restrictions, such as food services, may further highlight the glaring lack of workers in these industries. Wages may therefore rise faster in these areas to attract labour. Other industries may also be impacted by the anticipated minimum wage increase in eight of the ten provinces. In addition, upcoming wage negotiations will take into account realized inflation and labour shortages, which could add to upward pressure on wages. In closing, we do not currently anticipate a true inflationary spiral, but the situation should be monitored as long as the labour market stays unbalanced, and inflationary pressures remain.