

Editorial

The papers published in this special issue of EMPIRICA result from an international workshop organized by the Oesterreichische Nationalbank in November 2000 on "*Wage bargaining within EMU*". The main aim of this effort to bring together a number of outstanding researchers studying labor markets, labor market institutions and wage formation was twofold: firstly to direct attention to future developments of wage setting under conditions of European Monetary Union (EMU) given the increased importance of wage policy on a macroeconomic level under the new economic policy conditions in Europe; and second to analyse the challenges for the interaction of wage bargaining institutions with other economic policy institutions, in particular with the European Central Bank (ECB).

Lars Calmfors introduces the subject with an extensive survey of labor market institutions. The paper distinguishes between the impact of the EMU on nominal wage flexibility and on equilibrium real wage and unemployment levels. A perceived need to increase nominal wage flexibility as a substitute for domestic monetary policy and a tendency toward less real wage moderation in the EMU are likely to promote informal bargaining co-ordination and social pacts in the medium run. But such co-ordination is not likely to be sustainable in the long run, as it conflicts with other forces pushing toward decentralization and deunionisation. This could induce an intensified need for government intervention in wage setting during a transitional period. Although monetary unification will strengthen the incentives for transnational co-ordination of wage bargaining, such a development is improbable in view of the co-ordination costs involved. If transnational co-ordination develops, it is most likely to occur within multinational firms.

Karl Pichelman complements this theoretical analysis by providing an in-depth review of aggregate wage developments in the EU member states. He discusses wage bargaining mechanisms and their impact on labour market outcomes and analyses nominal wage developments, focusing particularly on the evolution of cross-country patterns as an indicator of the synchronisation of wage developments. Finally, he discusses real wage growth in relation to productivity developments.

Alain de Serres, Stefano Scarpetta and Christine de la Maisonneuve note the importance of aggregation bias in the analysis of wage shares developments over time and across countries. They study five European countries and the United States and show that the trend decline in the aggregate wage share observed in these countries over much of the 1980s and 1990s partly reflects changes in the sectoral composition of the economy. The application of a fixed-weight aggregation method

changes the profile of the observed wage share in a significant way: namely, the overshooting of the wage share levels previously incorrectly seen in the early-1970s vanishes. Error-correction wage equations based on such adjusted wage shares generally have better regression fit and, importantly, show long-run elasticities of real wages to unemployment that vary less across countries and are substantially lower than those obtained with observed shares.

A central issue regarding the possible changes of wage bargaining institutions in Europe is how the commitment to price stability will affect labour market rigidities in the European Monetary Union. **Steinar Holden** investigates this question. In his model firms may choose between fixed wage contracts (where the employer cannot lay off the worker, and the wage can only be changed by mutual consent), or contracts where employment is at will, so that either party may terminate employment (with strong similarities to temporary jobs). He shows that a fixed wage contract provides better incentives for investment and training, while employment at will facilitates efficient mobility. Inflation erodes the real value of a fixed contract wage over time, and badly matched workers are more likely to quit for other jobs. Disinflation has opposing effects on labour market rigidity, as fixed wage contracts become more rigid in real terms, but fewer firms will choose fixed wage contracts.

Lilia Cavallari analyses, in a micro-founded model of a two-region monetary union, the macroeconomic impact of institutional reforms in labour markets and central banking that may occur as a result of monetary unification. The paper concludes that monopoly distortions in the labour market are a key factor in evaluating the effects of central bank's conservativeness and wage centralisation on inflation and unemployment. Wage restraint is favoured in a highly decentralised wage bargaining setup as well as under a liberal central bank, provided competition is high in the labour market.

Torben Iversen's paper pays further direct attention to this interaction between central bank monetary rules and systems of collective wage bargaining. He argues that the replacement of the Bundesbank, directly targeting German inflation, by the ECB targeting European inflation has removed a major institutional support of wage restraint in Germany. He elaborates the consequences of this for EMU under two scenarios: that inflation expectations will be generated by ECB monetary policy and that they will reflect German inflation outcomes. He then discusses possible institutional developments that may result, including government-union bargains.

Robert Franzese surveys the recent work on macroeconomic management with varying organization of wage/price bargaining and degrees of credible monetary conservatism. He stresses that the shared core implication of this work is that even

perfectly credible monetary conservatism has *long-run, equilibrium, on-average* real effects, even with fully rational expectations, and that these effects depend on the organization of wage/price bargaining. The emerging theory and evidence agree that a credibly conservative European monetary policy has nominal and real effects that depend on the Europe-wide institutional-structural organization of wage/price bargaining.

Finally, Peter Mooslechner and Martin Schürz analyse this increasingly popular literature on strategic interactions from a methodological viewpoint. As they clarify, these political economy approaches focusing on interactions between wage bargaining institutions and an independent central bank do not follow unified methodological rules and so cannot be categorised under a single particular paradigm. Moreover, the literature remains in a way circumscribed by the limits of our logical capacities and of mathematical tractability and therefore relates to the “real world” of wage bargaining and economic policy institutions in a very limited way only. A consideration of the vast complexity of institutional conditions that impact economic performance in EMU reminds and cautions one that actual economic policy research is able to cover only very few of a wide range of conditions responsible for the overall outcome.

In both economic research and policymaking, analysis of the interaction between wage bargaining, institutions and macroeconomic policy has gained much attention in recent years. The establishment of an European Monetary Union in 1999 has further increased the interest in this subject, especially from an economic policy coordination point of view. The collection of papers published in this issue tries to give a comprehensive and up-to-date overview of the subject. We hope the readership of EMPIRICA will enjoy our compilation and find it stimulating reading.

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Peter Mooslechner
Martin Schuerz