

Unit Labour Costs

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*The views expressed are those of the author and do not necessarily reflect
the views of the Ministry of Finance*

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Longstanding joke about economists is that they see something work in reality then go about figuring out whether it can also work in a model

Some do things the other way round: they see something work in a model, then ask whether it also works in reality

If it doesn't, the best economists revisit their model.

Others believe the model is right and the reality is wrong

And then there are those who don't even bother to check if it works in reality at all.

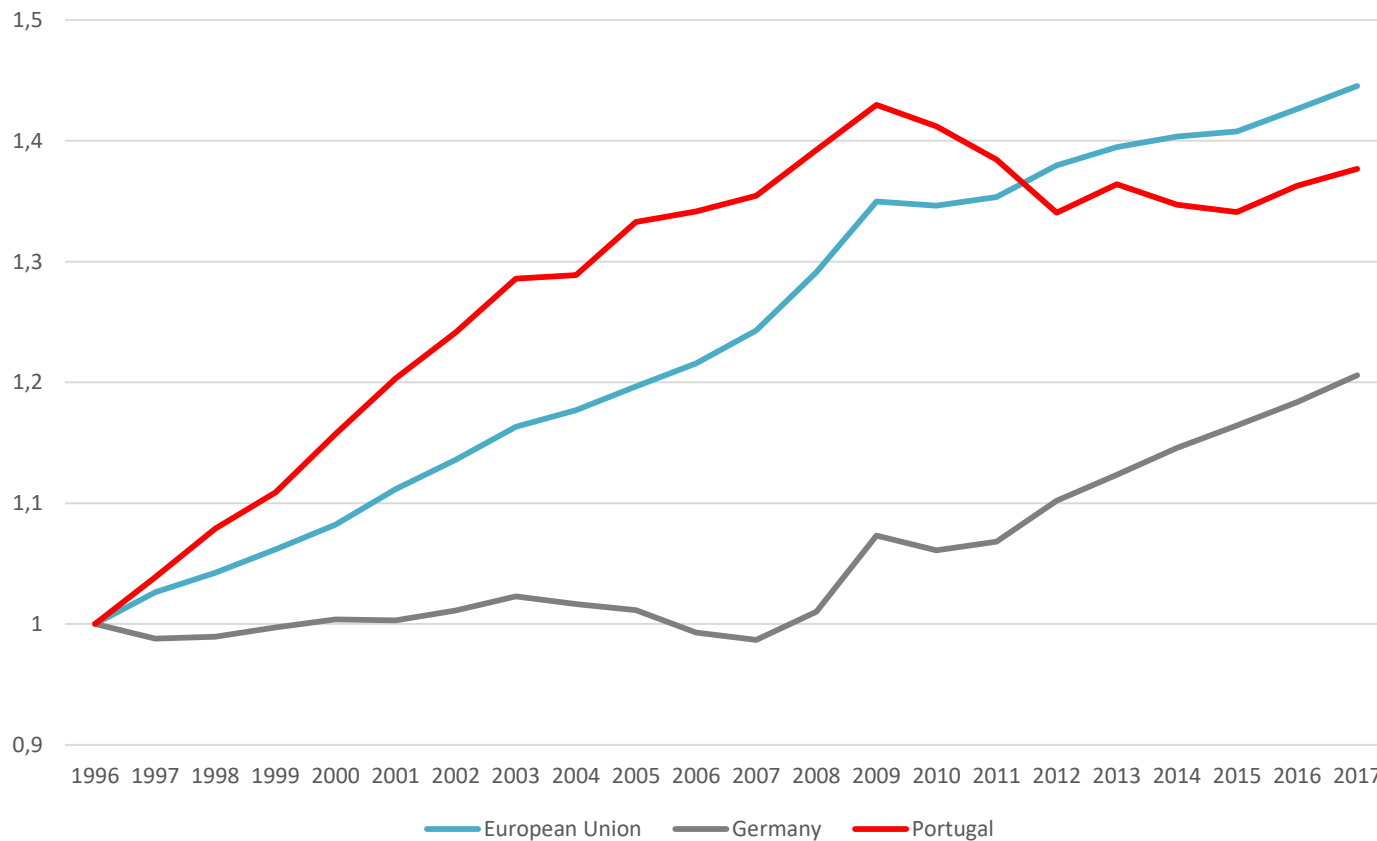
Martin Sandbu, Financial Times, August 15, 2016

Summary

- Widespread view that PT competitiveness deteriorated in the run up to the crisis
- Predicated on ULCs growing relative to EU average/northern creditor countries
- Yet, ULCs are based on conceptual errors
- PT ULCs, in recent years, little more than proxy for the GDP deflator
- There are better measures, portraying a very different picture

In a nutshell

Nominal unit labour costs: Ratio of compensation per employee to real GDP per person employed, 1996-2017



Source: AMECO, (PLCD)

The trouble is...

- Multiple goods and services
- Complex cost structures, labour costs only one part of the story
- Changing nominal exchange rates
- Conflating nominal and real figures

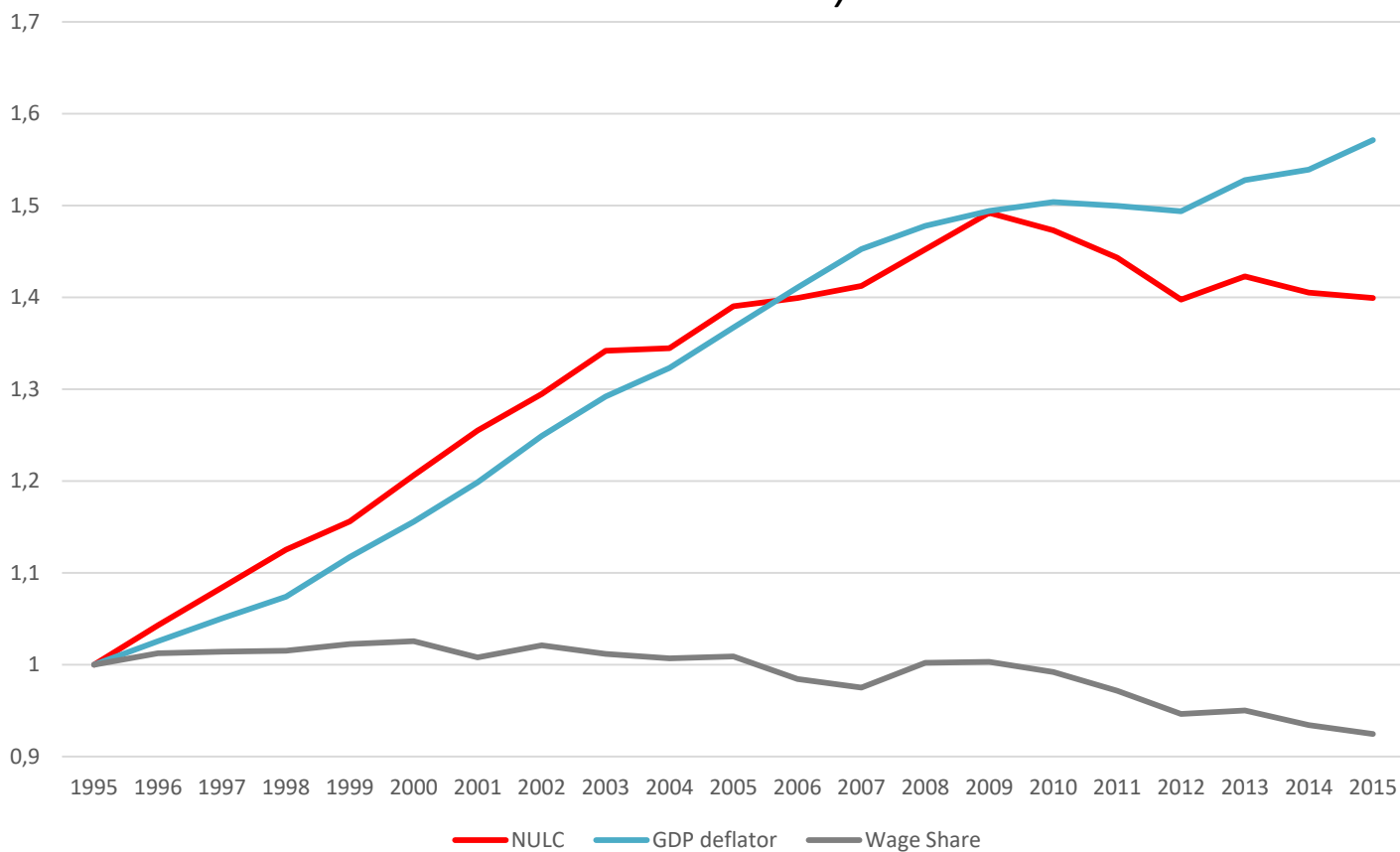
So what?

- $ULC = WL/Y$

W is nominal compensation per employee; L the number of employees; Y is real GDP

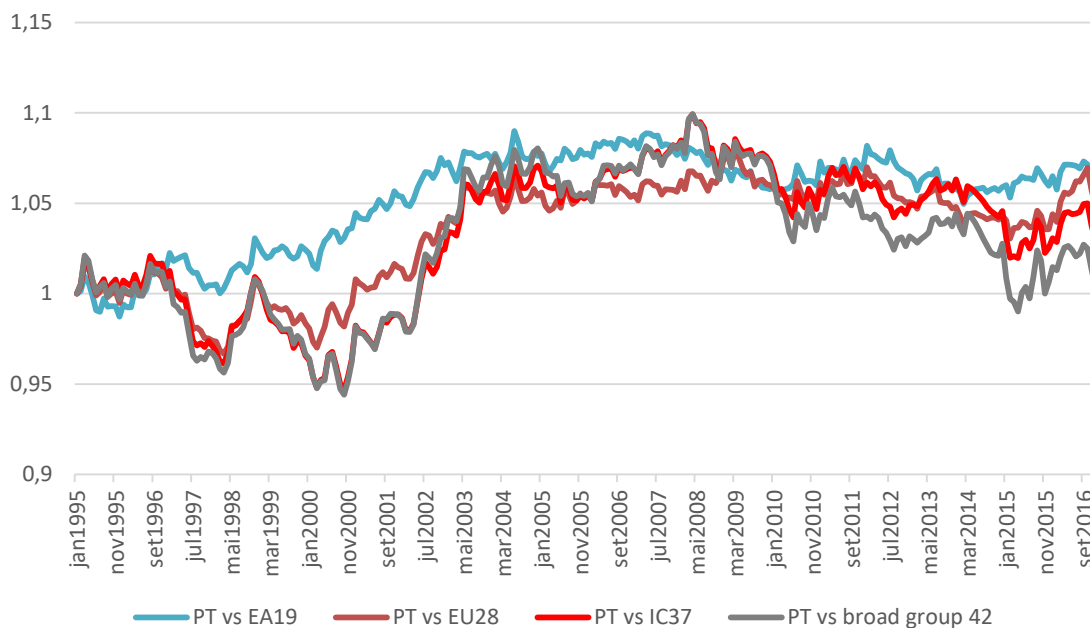
- What is the labour compensation involved in producing one unit of gross domestic product?
- “The theoretical abuse of applying the unit labour cost concept at the whole economy level”
- In practice: wage share * GDP deflator

Nominal Unit Labour Costs, Wage Share and GDP Deflator (Portugal, 1995=100)

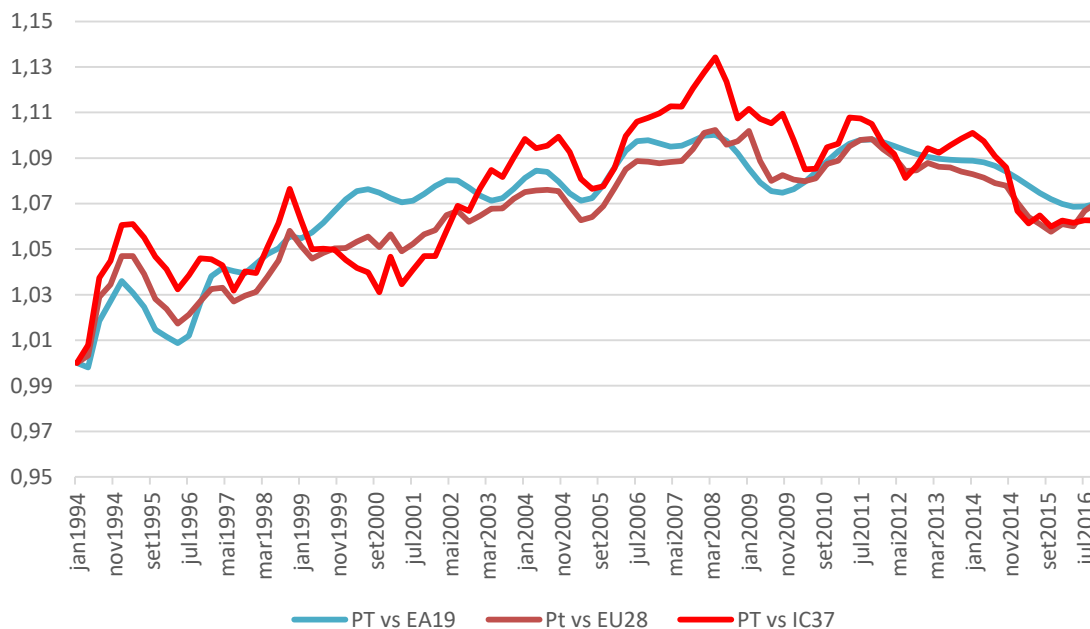


Source: Eurostat and Banco de Portugal

Real Effective Exchange Rates,
HICP Deflator (1995 = 100)

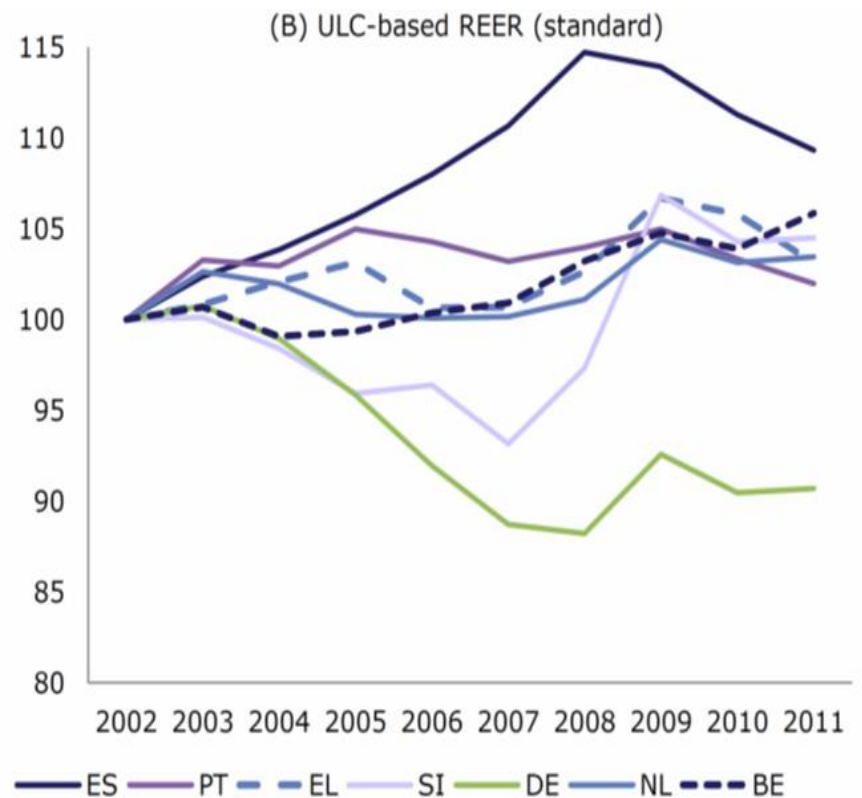
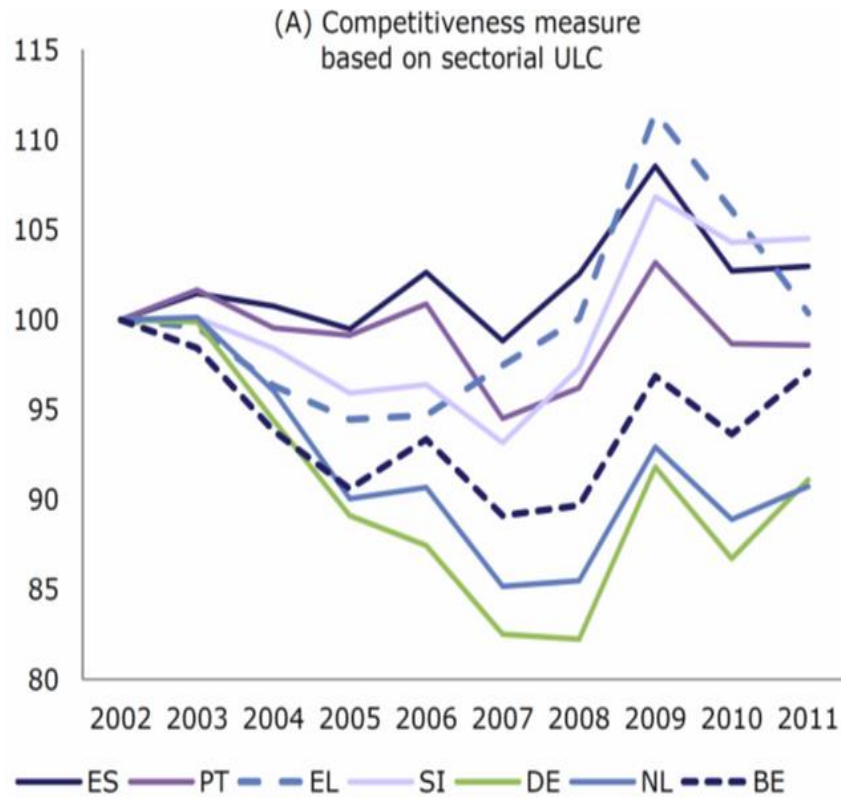


Real Effective Exchange Rates,
Export Prices Deflator
(1995=100)



Source: European Commission, Price and
Cost Competitiveness - Data Section
2016.

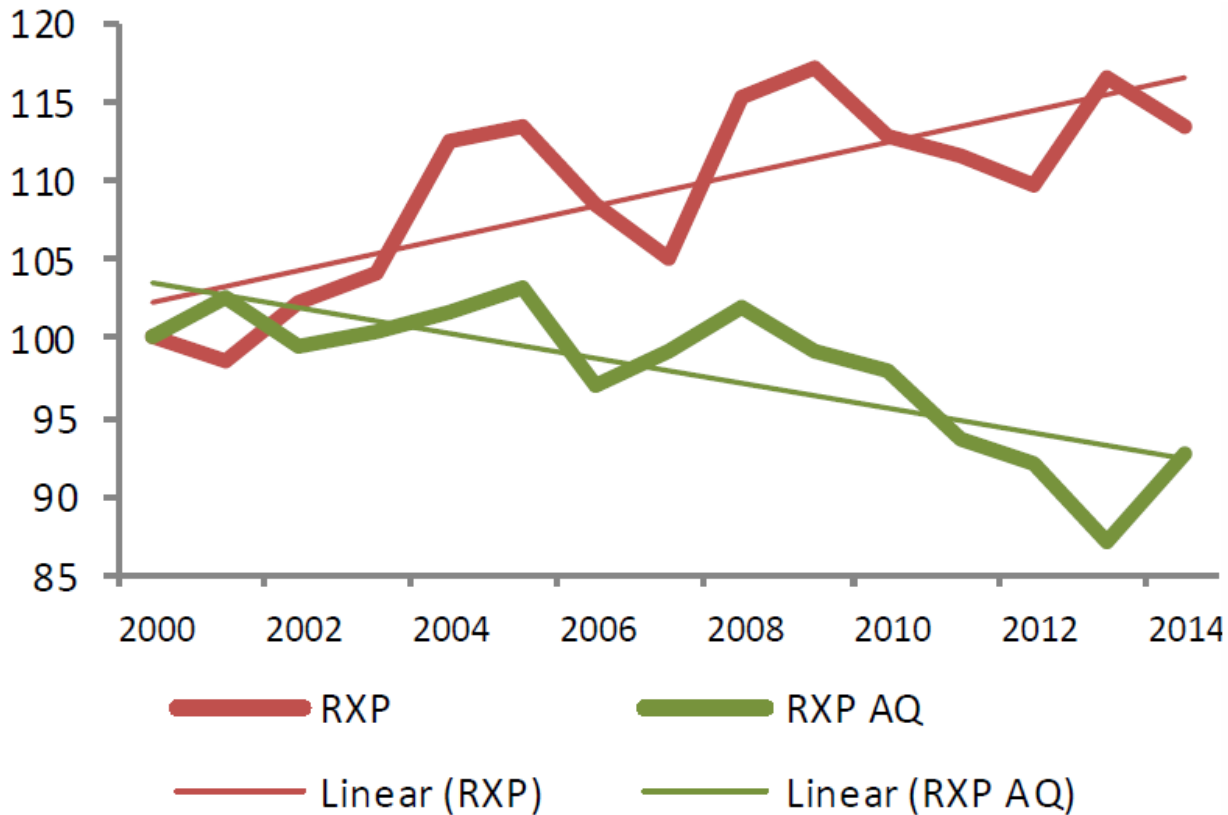
*ULC competitiveness measures (standard ULC vs sectoral ULC),
2002-2011, index: 2002=100*



(1) Competitiveness against (a) the rest of the EU (and Norway) and (b) against the rest of the EU.

Source: European Commission, "Quarterly Report on the Euro Area", 13(2), 2014

Relative export prices and relative export prices adjusted for quality (2000=100)



Source: CompNet Diagnostic Toolkit for Competitiveness. Note: An increase in the indicator reflects a loss in competitiveness

The Russian Bolsheviks have discovered that truth does not matter so long as there is reiteration. They have no difficulty whatever in countering a fact by a lie which, if repeated often enough and loudly enough, becomes accepted by the people.

Winston Churchill, Brighton, October 4, 1947

Thank you

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