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Minimum wage developments in 2022 - fighting the cost-of-living crisis

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Key points and policy recommendations

Despite substantial minimum wage increases, in almost half of the Member States with a statutory minimum wage, these were not sufficient to safeguard the purchasing power of minimum-wage earners in the current cost-of-living crisis. In order to better mitigate the negative effects of high inflation on the lives of workers and their families, Member States should take the following measures:

- Timely transposition of the European Minimum Wage Directive into national law to promote adequate minimum wages and adequate collective bargaining coverage as two important tools to deal with the cost-of-living crisis.
- Of the Directive's four criteria which Member States shall take into account when setting statutory minimum wages, the criterion "purchasing power taking into account the cost of living" should be given clear priority in times of high inflation – this would also help to adjust statutory minimum wages more regularly and timely in order to protect the most vulnerable workers from rising prices.
- Following the example of a range of countries, Member States should anticipate the effect of the Minimum Wage Directive by already applying its double decency threshold for adequate minimum wages of 60% of the median and 50% of the average wage as the benchmark for setting statutory minimum wages.
- Because high collective bargaining coverage ensures higher wage levels, Member States should also go early by taking the Directive's 80% threshold for adequate collective bargaining coverage as the benchmark for establishing action plans to gradually increase collective bargaining coverage.

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Introduction

In 2022, one of the main political challenges has been the need to address the cost-of-living crisis caused by an unprecedented increase in inflation. Prices had already started to increase in the second half of 2021 as a result of the combined effect of the economic recovery, supply-chain bottlenecks and a supply shortage of raw materials and basic inputs. In early 2022, the Russian invasion of Ukraine further exacerbated supply-chain tensions and increased inflationary pressures. The particularly high increase in energy and food prices eroded the purchasing power of a growing number of workers and their families, launching a cost-of-living crisis in which they found it difficult to make ends meet. Low-wage earners have been particularly hard hit by inflation because they tend to spend a higher share of their income on energy, food and other essential goods and services, where price rises are greater than for other, non-essential items (ILO 2022).

Against this background, minimum wages are currently a particularly important tool to safeguard the purchasing power of low-wage earners. The recently adopted European Directive on Adequate Minimum Wages in the European Union (European Parliament and Council of the European Union 2022), with its dual objective of ensuring minimum wage levels that enable a decent standard of living and of strengthening collective bargaining, can play an important role in supporting attempts to safeguard workers' purchasing power. This policy brief will assess the extent to which statutory minimum wages have been used as a tool to mitigate workers' loss of purchasing power, as well as the potential impact of the Minimum Wage Directive on minimum wage-setting in the Member States.

The Minimum Wage Directive and the cost-of-living crisis

Focusing on adequate minimum wages and strong collective bargaining, the Minimum Wage Directive promotes two important tools to address the cost-of-living crisis. As regards minimum wages, the Directive is explicitly not about setting a uniform minimum wage level across Europe, but about specifying certain criteria for adequate minimum wages that ensure a decent standard of living. Article 5(2) lists four criteria that Member States shall take into account when setting statutory minimum wages: (a) the purchasing power of statutory minimum wages, taking into account the cost of living; (b) the general level of wages and their distribution; (c) the growth rate of wages; and (d) long-term national productivity levels and developments. Member States are free to decide on the relative weight of these criteria. Of course, the purchasing power criterion is of particular relevance today, because it helps to ensure adequate minimum wages also in times of strongly increasing prices.

In addition to these more general criteria, Article 5(4) of the Directive provides a more concrete measure for adequate minimum wages, by referring to the value of minimum wages in relation to the overall wage distribution.

Article 5(4) states that Member States may be guided by indicative reference values when assessing the adequacy of statutory minimum wages, using internationally recognized indicators such as 60% of the gross median wage and 50% of the gross average wage. The Directive, thus, de facto establishes a ‘double decency threshold’. Although this threshold is not legally binding, it represents a strong normative benchmark for setting minimum wages at the national level. As will be shown, this double decency threshold already influences minimum wage-setting in a range of Member States.

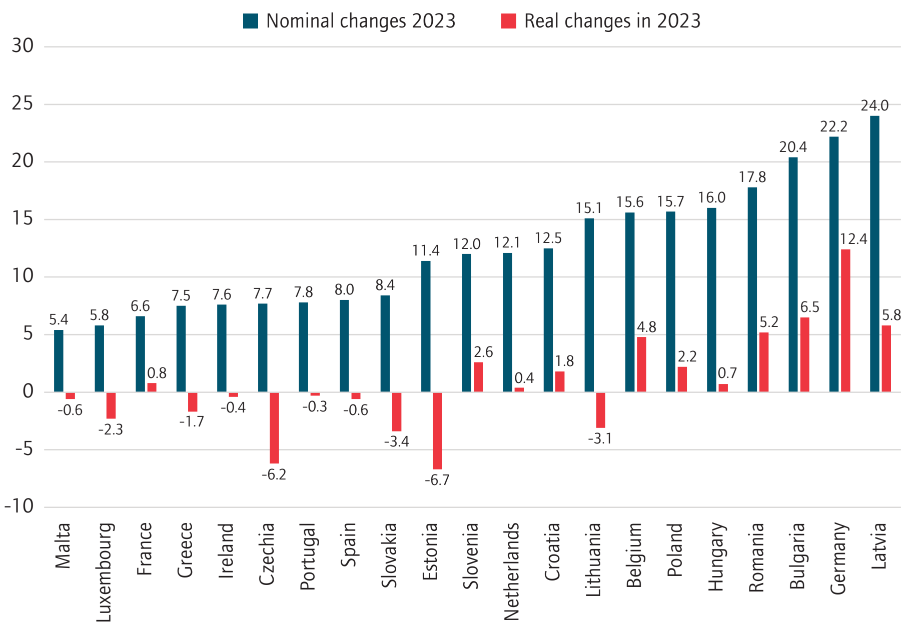
However, the double decency threshold may not be sufficient to ensure adequate minimum wages if the overall wage level is low because 60% of a low median or 50% of a low average wage is still not enough to ensure a decent living standard. This is where the Directive’s second key objective – strengthening collective bargaining – comes into play: Member States with less than 80% collective bargaining coverage are obliged to establish an action plan to gradually increase bargaining coverage. This requirement de facto defines a threshold for adequate bargaining coverage. Since higher bargaining coverage ensures higher overall wage levels for a larger proportion of the workforce (European Commission 2020), the Directive’s bargaining threshold is an important element to ensure a sufficiently high level of median and average wages so that minimum wages that fulfil the double decency threshold are adequate in the sense of ensuring a decent living standard. Since higher bargaining coverage usually correlates with significantly lower wage inequality (Keune 2021) and since, furthermore, economies characterized by lower wage inequality are less vulnerable to price shocks (ILO 2022), the Directive’s bargaining threshold also helps to fight the cost-of-living crisis by reducing wage inequality.

Development of statutory minimum wages in the EU

As Figure 1 illustrates, many countries used minimum wages as a tool to compensate the loss of purchasing power and substantially increased statutory minimum wages. In most EU countries, nominal minimum wages increased far beyond the nominal increase of overall wages (Müller et al. 2023) – taking into account the specific needs of low-wage workers in times of high inflation.

The development of nominal statutory hourly minimum wages in 2023 varies considerably across the EU. The nominal increases range from just above 5% in Malta (5.4%) and Luxembourg (5.8%) to very substantial increases of more than 20% in Germany (22.2%) and Latvia (24%). Nominal minimum wage increases were generally higher in central and eastern European (CEE) countries, continuing the long-standing trend of minimum wage convergence between CEE countries and western European countries. The exceptionally large increases in Belgium and Germany - the only two western European countries with an increase of more than 15% - can be attributed to specific factors. The substantial increase in Germany is the result of a government decision in June 2020 to gradually increase the minimum wage to EUR 12 by October 2022. In line with this government decision, the minimum wage in Germany was increased to EUR 10.45 on 1 July 2022 and to EUR 12 on 1 October 2022. Since this was an exceptional structural increase and since no changes were introduced to the process of minimum wage-setting, future increases will follow the usual procedure of recommendations of the minimum wage commission which are heavily determined by the development of collectively agreed wages. Future increases of the minimum wage will therefore most likely be more modest.

Figure 1 **Development of hourly nominal and real minimum wages in 2023* (in %; 1 January 2022 - 1 January 2023)**



* Note: Calculation based on national currencies. The development of real minimum wages refers to the development of nominal minimum wages deflated by the HICP annual average changes. Since real minimum wages represent the purchasing power of minimum wages; i.e. the ratio of nominal minimum wages to prices, real minimum wages have been calculated according to the following formula: Nominal minimum wage index X 100 divided by consumer price index (for more details see WSI Tarifarchiv 2023).
Source: WSI Minimum Wage Database (WSI 2023) and own data.

The substantial minimum wage increase in Belgium is a result of the wage indexation mechanism that links the development of minimum wages to the development of prices. Usually, there is an automatic adjustment of the minimum wage when the consumer price index has risen by more than 2% since the last increase. As a consequence of the sharp increase of inflation last year, there have been six minimum wage increases in 2022: from EUR 1691.40 per month on 1 January 2022 to EUR 1954.99 per month on 1 December 2022, when the last adjustment took place. The indexation mechanism in Belgium not only safeguarded the purchasing power of minimum wage earners; the six adjustments in 2022 also illustrate that it did so in a timely manner minimising the delay between price and minimum wage adjustments.

By contrast, in the majority of EU countries, minimum wages are usually adjusted annually on 1 January of each year. In the light of inflation developments, in 2022 additional adjustments of the minimum wage were also introduced in France (May and August) and Luxembourg (April), which both also have a minimum wage indexation system; and in the Netherlands where minimum wages are normally adjusted twice a year on 1 January and 1 July of each year.

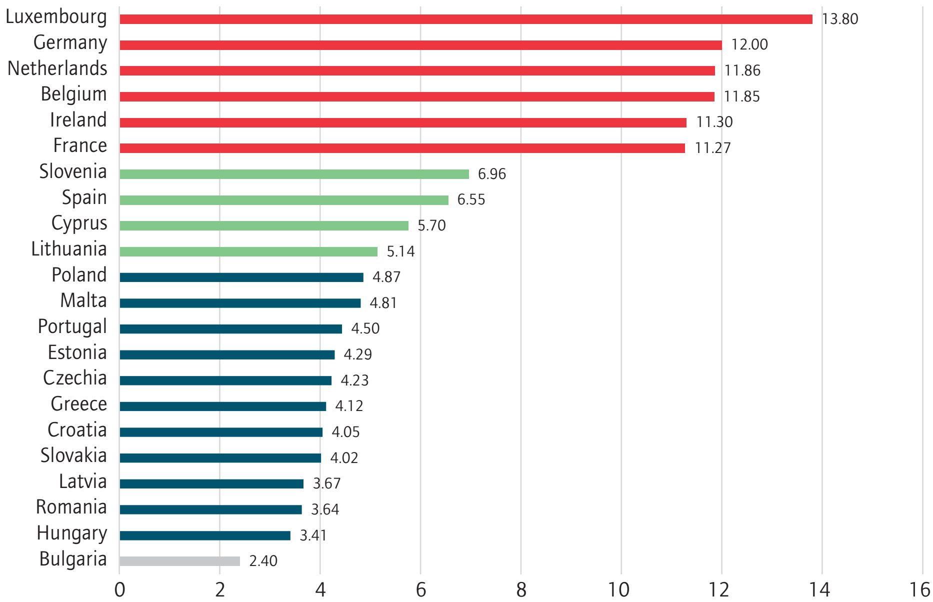
Drop in real minimum wages in many countries

However, in ten countries – almost half of all countries with a statutory minimum wage – the nominal minimum wage increases were not enough to safeguard the purchasing power of minimum wage earners. The drop in real hourly minimum wages ranges from marginal in Portugal (-0.3%), Ireland (-0.4%), Malta (-0.6%) and Spain (-0.6%) to very substantial in Czechia (-6.2%) and Estonia (-6.7%). By the same token, the increases in real hourly minimum wages range from less than one percent in the Netherlands (0.4%), Hungary (0.7%) and France (0.8%) to almost 6% and more in Latvia (5.8%), Bulgaria (6.5%) and in Germany which is the outlier with an increase in real minimum wages of 12.4%.

The substantial differences in the development of nominal minimum wages had an impact on the ranking of countries in terms of the absolute level of statutory minimum wages. Traditionally, three broad groups of countries can be distinguished in terms of the absolute level of minimum wages: a top group of six western European countries with the highest minimum wages, a small group of countries with minimum wages between EUR 5 and EUR 7 per hour, and a large group of exclusively southern European and CEE countries with minimum wages below EUR 5 per hour. The top group still consists of the same six western European countries, topped by Luxembourg with an hourly minimum wage of EUR 13.80; but due to its extraordinary nominal increase of 22.2% Germany made a big step from 6th to 2nd position with a minimum wage of EUR 12 per hour. At the bottom of this top group are France (EUR 11.27) and Ireland (EUR 11.30). In the middle group of countries where the minimum wage ranges between EUR 5 and EUR 7, Slovenia and Spain, which in 2021 were the only countries in this group, have been joined by Cyprus (EUR 5.70) and Lithuania (EUR 5.14). Cyprus is a notable case because Cyprus changed its minimum wage-setting mechanism from a system of negotiated minimum wages to a system of statutory minimum wages. Previously, statutory minimum wages only existed for a limited number of occupational groups (Schulten and Müller 2020). However, with effect from 1 January 2023, Cyprus introduced a general statutory minimum wage of EUR 940 per month, which on the basis of a 38-hour-week and 165 working hours per month amounts to an hourly minimum wage of EUR 5.70.

The group with the lowest hourly statutory minimum wages (below EUR 5) is still the largest group, ranging from Bulgaria (EUR 2.40), Hungary (EUR 3.41) and Romania (EUR 3.64) to Portugal (EUR 4.50), Malta (EUR 4.81) and Poland which is the new frontrunner of this group with EUR 4.87. In Greece, Portugal and Spain, the minimum wage is paid 14 times per year. In Figure 2 the minimum wage for these three countries has been converted to 12 payments. If 14 payments are taken into account the hourly minimum wage in the three countries amounts to EUR 7.64 in Spain, EUR 5.34 in Portugal and EUR 4.81 in Greece.

Figure 2 **Statutory national minimum wages in the EU (per hour, in Euros, January 2023)**



Notes: In those countries in which minimum wages are set on a monthly (or in the case of Malta weekly) basis, the amount has been converted into hourly rates based on the average collectively agreed number of working hours per month as provided by Eurofound's EurWORK's database. For non-Euro countries, the national currency has been converted based on the average annual exchange rate in 2022 provided by Eurostat. For Greece, Portugal and Spain where the minimum wage is usually paid 14 times a year; the figure calculates these as 12 payments a year for comparison purposes.
Source: Own compilation based on national sources.

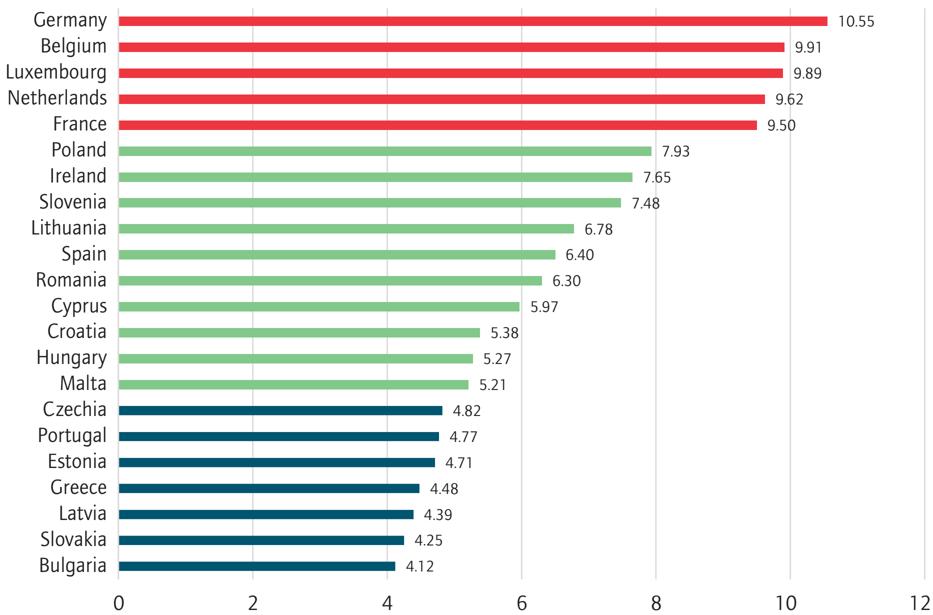
Statutory minimum wages in purchasing power standards

Measuring statutory minimum wages in purchasing power standards takes into account that the actual cost of living varies considerably among EU Member States. Against this background, the WSI minimum wage database also shows the value of minimum wages in purchasing power standards (PPS) on a euro basis (WSI 2023). Since there is always a time lag in calculating the PPS conversion factors, the data in Figure 3 is based on PPS for private consumption in 2021.

Figure 3 illustrates that measuring statutory minimum wages in PPSs considerably reduces the gap between EU Member States – and in particular between western European countries and CEE countries. Whereas the ratio between the highest and lowest nominal minimum wages is 1 to 5.73, this ratio is more than halved to 1 to 2.56 when minimum wages are measured in PPSs. Expressing the value of statutory minimum wages in PPSs demonstrates that minimum wages in the EU not only converged nominally but also when taking into account the actual cost of living. In 2015, for instance, the ratio between the highest and the lowest statutory minimum wage in the EU measured in PPSs was 1 to 3.93 (Schulten 2015).

Figure 3 furthermore shows that taking into account the actual cost of living considerably changes the order of countries as regards the value of minimum wages. For example, Bulgaria (4.12 PPS), Hungary (5.27 PPS) and Croatia (5.38 PPS) have significantly higher minimum wages on a PPS basis, while in countries such as Luxembourg (9.89 PPS) and Ireland (7.65 PPS), the comparatively higher cost of living negatively affects the value of the minimum wage. As a consequence of the comparatively lower cost of living, Germany replaces Luxembourg at the top of the ranking even though the nominal minimum wage in Germany is considerably lower than in Luxembourg.

Figure 3 **Purchasing power of statutory minimum wages (per hour, PPS based on Euros*, 1 January 2023)**

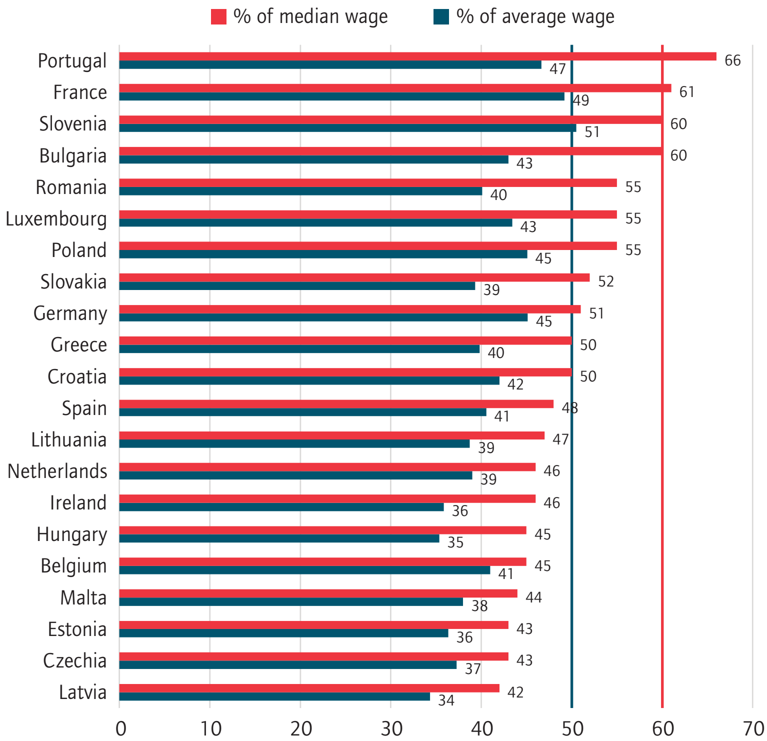


Notes: Conversion to PPS on a euro basis based on the purchasing power parities for private consumption reported by the World Bank for 2021.
Source: WSI Minimum Wage Database and Lübker and Schulten 2023.

The normative force of the Directive

The absolute level of minimum wages says little about whether minimum wages are adequate in the sense of being sufficient to ensure a decent living. Measured against the double decency threshold of 60% of the median and 50% of the average wage set out in the European Minimum Wage Directive, Figure 4 demonstrates that according to data from the OECD earnings database (OECD 2022), in 2021 only Slovenia fulfilled the criteria for adequate minimum wages. In all the other countries more or less substantial minimum wage increases are needed to ensure adequate minimum wages. It should be emphasised that the OECD database only provides data until 2021 so that the substantial minimum wage increases in 2022 are not yet taken into account for the measurement of the relative value of minimum wages.

Figure 4 **Minimum wage as % of full-time median and average wages (2021)**



Source: OECD earnings database (OECD 2022). For Bulgaria, Croatia and Malta, data for 2018: European Commission (2020).

Even though the EU Member States still have two years to transpose the Directive into national law, already today, the double decency threshold has an impact on national developments. In Germany, for instance, the increase to EUR 12 was also justified by the fact that this would bring the minimum wage significantly closer to a level of 60% of the national median wage (Müller and Schulten 2022). In Cyprus, the level of the newly introduced statutory minimum corresponds to 60% of the national median wage (European Commission 2022); and in Ireland, the government has announced that over the next four years it will gradually raise the minimum wage to a living wage level equivalent to 60% of the Irish median wage (Government of Ireland 2022). The double decency threshold was furthermore referred to in the debates in Belgium, where the labour minister announced that the Belgian minimum wage did not meet European standards and would have to be raised to EUR 12 per hour in order to reach the target of 60% of the median wage; and in the Netherlands, where the trade union federation FNV called on the government to raise the minimum wage to EUR 14 per hour in order to meet the targets of the European Minimum Wage Directive.

The example of Austria, where minimum wages are set by collective agreements, illustrates that the impact of the Directive may also influence discussions in countries without a statutory minimum wage; even though the Directive's provisions on the adequacy of minimum wages does not apply to them. In order to safeguard the purchasing power of employees across all sectors, the trade unions agreed on a new minimum wage target of EUR

2,000 per month for the bargaining round in autumn 2022. This target roughly corresponds to what the Directive suggests as adequate minimum wages (Müller and Schulten 2022).

Conclusion

Despite the dynamic developments of minimum wages between 1 January 2022 and 1 January 2023, the nominal increases have not been sufficient to safeguard the purchasing power of minimum wage earners in almost half the countries with a statutory minimum wage. Thus, regular and timely minimum wage adjustments taking into account the purchasing power of minimum wages are key to protect the most vulnerable workers from high inflation. The fact that all but one Member States with a statutory minimum wage do not fulfil the Directive's double decency threshold for adequate minimum wages illustrates not only the need but also the scope for minimum wage increases. Research into the impact of minimum wage increases on inflation illustrates that these are negligible because of the relatively low share of minimum wage earners (Dullien et al. 2022; Cazes et al. 2022).

The adoption of the European Minimum Wage Directive in October 2022 has the potential to be a gamechanger. With its dual objective of ensuring adequate minimum wages and strengthening collective bargaining, the Directive promotes two key tools to mitigate the negative effects of high inflation on the lives of workers and their families.

The Directive's double decency threshold for adequate minimum wages provides a strong normative benchmark which already influences minimum wage setting at national level, even though the Directive has not yet been implemented into national law.

The Directive's requirement to establish national action plans in those countries with a collective bargaining coverage of less than 80% is another important measure to fight the cost-of-living crisis. High bargaining coverage not only directly supports workers' wages by ensuring a higher general wage level, but it also helps to ensure sufficiently high median and average wages so that minimum wages that fulfil the double decency threshold are high enough to ensure a decent standard of living. The two objectives need to be seen in combination.

Thus, timely implementation of the European Minimum Wage Directive would be a key measure to address the cost-of-living crisis. However, policy-makers at national level could – and should – already act now by using the Directive's benchmarks for adequate minimum wages and adequate collective bargaining coverage as a reference to safeguard the purchasing power of workers in their respective country as the cost-of-living crisis continues to unfold.

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