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Falling real wages and consumer recession

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Consumption will remain desolate in 2023, despite rising wages

The *annus horribilis* 2022 ended more conciliatory than many, including myself, had feared. At the beginning of the year, the stock markets blasted off price fireworks that had people rubbing their eyes. No one is talking about a gas crisis anymore. Inflation is currently falling faster than I would have dared to hope. Inflation-dampening discretionary interventions by governments help temporarily.

Might the German recession be avoided fail after all? It would be a bit premature to rejoice. The Achilles' heel of economic prospects remains household purchasing power. Real wages collapsed in 2022, rapidly deflated by inflation that had long raged out of control.

Households are financially very tight

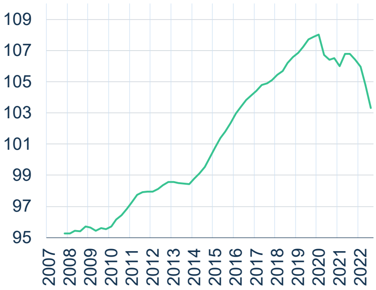
The adjacent chart shows the dramatic fall of purchasing power. In the third quarter of 2022 the seasonally adjusted real wage index crashed back to levels last seen in 2016. In Q4, the erosion of purchasing power will have intensified in view of double-digit price increases.

Government support measures such as the various energy brakes or tax-free one-off payments must be seen against this background. They cushion the profoundly antisocial distributional effects of inflation. Extra savings accumulated during lockdowns provide a further buffer, at least for the middle class.

But the bottom line remains: many citizens will feel the pinch and think twice before splashing out at the stores. Consumer sentiment (as measured by the GfK index, for example) is still deep in the red. This was also evident in the rather lukewarm Christmas sales, which ran under the motto "Silent Night".

Real wages slumped in 2022

Real Wage Index Germany (seasonally adjusted)



Source: Destatis, LBBW Research

State support cushions decline in purchasing power

2023 could be the year of the price-wage spiral

In addition to high inflation, relatively low wage settlements are responsible for the ailing real wages. The collective bargaining archive of the Hans Böckler Foundation, which is affiliated with the trade unions, reports an increase in nominal collective wages of just 2.7% for 2022. "Business as usual" despite double-digit inflation!

Presumably, it won't stop there. Despite the threat of recession, Germany enjoys full employment. In the euro zone as a whole, the situation looks almost as good. Wage demands are therefore just taking off. Last week, the service sector union ver.di put a demand of 15% on the table for logistics employees at Deutsche Post. For the 2.7 million federal and local government employees, unions aim at 10.5%. For railroad employees, double-digit demands are also likely to come into play in February.

Wage demands are taking off!

Real wages will rise again in the medium term

It would be utterly unrealistic to believe that wages will not rise strongly in the medium term. Rampant labor shortages and the high real wage losses will see to that. The tilted distribution of income will then also become somewhat more even again. However, it will certainly take a few years before the majority of households have compensated for the severe inflation shock.

Even if unions should succeed with their robust wage demands: a consumer-driven recession remains almost inevitable in 2023.