With a weaker real economic trend, employment growth is expected to be somewhat slower than assumed earlier.

The somewhat weaker growth prospects for the Swedish economy imply that employment may rise a little more slowly than the Riksbank expected earlier. In the coming two years the labour force is expected to grow as unemployed persons return from various educational programmes.

To sum up, compared with the assessment in the September Report, unemployment at the end of the forecast period is now judged to be somewhat higher. This upward revision is primarily a consequence of weaker economic activity. Structural unemployment is judged to be unchanged.

WAGES AND PRODUCTIVITY

Wage increases across the economy in 1998 have averaged 2.5 per cent. However, the statistics do not yet include all the increases from the 1998 settlements. A number of local agreements for white-collar workers have still to be concluded.

In the forecast period the annual wage rise is judged to be around 3.5 per cent. This is somewhat lower than the figure in the September Report, mainly on account of the somewhat weaker growth prospects. Profitability is also expected to be somewhat lower for the same reason as well as successively falling inflation expectations. Wage drift is therefore judged to be somewhat lower, too.

The weaker real economic prospects imply that wages and productivity will both be somewhat weaker than assumed earlier.

The assessment of productivity is basically the same as in the September Report, with a continuation of the favourable trend. However, the productivity growth rate of 2.6 per cent that is reported for 1997 and the first half of 1998 must be regarded as unusually high. The path in the forecast period is expected to match the level in the period 1990–96, when the trend was 1.7 per cent, compared with around 1 per cent in the 1980s. The poorer economic prospects do, however, point to somewhat lower productivity growth.

The relatively positive outlook for wages and productivity is broadly unchanged since the September Report. A somewhat more subdued development of wages is balanced to some extent by weaker productivity growth.

THE 1998 WAGE AGREEMENTS

The general situation

New wage agreements have now been concluded for a large part of the labour market.[33] A high proportion of the agreements are for three years, in many cases with the option of cancelling the third year. A common feature of many agreements is provisions that support increased local wage flexibility. A number of agreements stipulate, for example, that the local wage allotment is to be distributed with reference to responsibilities, skill requirements and competence. Otherwise the structure of agreements varies considerably, for instance as regards shorter hours, enhancing competence and minimum wage increases. Comparisons between agreements are complicated by the fact that negotiated wage increases refer to different wage concepts; some apply to minimum increases, for example, and for others there is no central framework. This also blurs the concept of wage drift.

An approximate picture of the distribution by the duration of agreements is presented in Fig. B6 (p. 36), which covers agreements involving a total of about 2.5 million employees.[34] The proportion of agreements that expire before the end of 1999 is small; it includes the agreement for about 35,000 employees in the transport sector, which runs to the end of 1998. The great majority of the agreements run to 2001 Q1 and the larger share of them can be terminated earlier.

The 1995 round of wage agreements was negotiated at a time when employers as well as employees expected, on average, that the rate of inflation one to two years ahead would be about 3.5 per cent. This did not happen; instead, annual inflation in the period 1996–97 averaged around 0.9 per cent or about 2.5 percentage points less than expected.[35] As a result, real wage increases in the period 1996–97 were high, averaging about 4.5 per cent a year, which can be compared with a virtually unchanged real wage level in the 1980s.

The 1998 wage agreements suggest that the labour market organisations have realised that inflation will remain low. In the period from November 1997 to September 1998, expectations of inflation two years ahead averaged 1.9 per cent among employers and expectations among employees were about 0.1 percentage point lower.[36] This has probably been an important factor in the wage negotiations.

The institutional conditions for this year's wage negotiations may also have contributed to the comparatively restrained agreements. The argument for this view is contained in the so-called Calmfors-Driffill curve, which describes an inverted-U relationship between the degree of centralisation in wage negotiations and the increase in real wage costs.[37] What the curve illustrates is that agreements negotiated either centrally for the total labour market or locally for each firm result in lower increases in real wage costs than agreements concluded at an intermediate degree of centralisation. Central negotiations have the advantage that the parties have the motivation and force to consider macroeconomic consequences of the outcome, for example the effect of wage increases on employment, unemployment and tax revenue. Local negotiations have the advantage that the wage share is determined with reference to the situation of the firm in question and the wage increases are therefore likely to be more in line with production requirements. This year's negotiating round included elements of central as well as fully decentralised wage formation. The cooperation pact,[38] which covers about half a million employees and includes strong, impartial chairmen, for instance, is an example of the former and the increased allotment for local wage negotiations is an example of the latter. In this way the negotiating parties used both of the favourable positions on the Calmfors-Driffill curve.

Wage drift

Besides negotiated wage increases there is wage drift, which is more attuned to the economic situation of the individual firm because it can be adapted to local conditions such as the order inflow, local productivity, competition and standards of competence. In the period 1991–97 annual wage drift averaged about 1.5 per cent. In the forecast period, 1998–2000, there are several reasons why it may be lower.[39] For one thing, restraint may be promoted by the institutional frame of the cooperation pact, with elements of both central and local wage formation. For another, wage compensation for unexpectedly high inflation during the term of an agreement is no longer relevant; on the contrary, inflation to date has been lower than expected and expectations of inflation during the rest of the period have fallen since the agreements were concluded. Finally, corporate earnings may be affected by a weaker economic development and thereby leave less room for wage drift.

Option to terminate

Another consequence of a poorer economic development may be that employers exercise the right that both they and employees have to terminate agreements before they expire. As a rule, the agreements that include an option to terminate run for three years, up to the spring of 2001, and can be annulled about one year earlier. They involve at least 980,000 employees and include agreements for the engineering sector, commercial employees and some public sector salaried

33 For an analysis of the 1998 wage agreements, see Eurén, C. (1998), *Sammanställning av resultatet av 1998 års avtalsrörelse* (Compilation of the result of the 1998 round of wage negotiations), Annex to the report submitted by the Enquiry on Strengthening the Conciliation Institution.

34 This covers about 60 per cent of total employment. The agreements that are not included are mainly those with few employees.

35 Sources: Prospera Research AB and Statistics Sweden.

36 Source: Prospera Research AB.

37 See Calmfors, L. & Driffill, J. (1988), Bargaining structure, corporatism and macroeconomic performance, Economic Policy 6, pp. 13–61.

38 The pact is discussed by the impartial chairmen in Albåge, L-G. & Larsson, R. (1998), *Industriavtalet i 1998 års förhandlingar* (The Pact in Manufacturing in the 1998 Negotiations), a report to the Manufacturing Committee.

39 Wage drift will presumably remain high for employees in occupations for which there is a labour shortage.

employees.[40] For of a majority of these agreements, notice of termination has to be given not later than September 1999 and for some even earlier. The engineering agreement, which involves about 280,000 employees, has one of the earliest dates for notice of termination, 31 May 1999 at the latest. A termination may be an important signal of future wage outcomes.

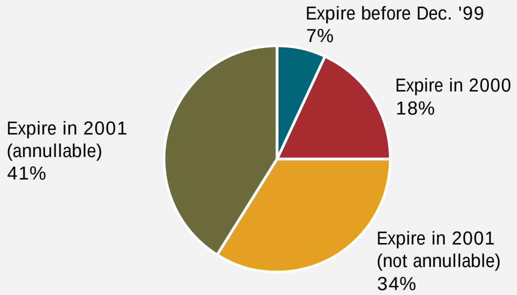
So what are the factors that point to early termination? One is the possibility that a less favourable economic development, for example in the wake of the Asian crisis, leads to poorer profitability than firms had counted on; the domestic upswing may be weaker than was foreseen at the time of agreements last spring. To compensate for lower profitability, firms in certain sectors could need to cut wages; as this is not feasible, they could resort to the alternative of terminating agreements. Another factor is the probability that inflation will be more subdued than was foreseen at the time of the agreements, in which case the increase in real wage costs will exceed what firms had envisaged and likewise motivate them to terminate agreements. Finally, it is conceivable that differences between occupational groups in the rate of wage increases, including wage drift, are such that certain unions decide to exercise their right to cancel agreements.

And what are the arguments against termination? The new institutional arrangements in the form of the cooperation pact may have helped to shorten the negotiating process and an early termination of agreements might lead to a loss of any goodwill that was earned in this way. Moreover, wage negotiations entail costs for all concerned and early termination brings forward the process of time-consuming negotiations with an uncertain outcome.

The relative weights of these factors are difficult to gauge. The negotiating parties have reasons for using the possibility of termination as a tactical weapon: employers are motivated to exaggerate the risk of termination in order to counter wage drift, just as employees have grounds for the opposite in order to achieve wage drift. A crucial factor for the value that labour market organisations attach to early termination of agreements will presumably be the course of economic development and inflation expectations during 1999. If no agreements are cancelled in advance, agreements for more than 420,000 employees will expire during 2000 and for more than 1.8 million in the spring of 2001. In the extreme case of early termination of all agreements for which this is possible, agreements for more than 1.4 million employees would end during 2000 and for more than 840,000 in 2001. The starting point for the inflation assessment in the main scenario is that neither party exercises the option to terminate their agreement.

40 E.g. unions affiliated to the Public Employees Negotiating Council (OFR), such as the Union of Civil Servants, the Police Union, the National Association of Military Officers and the central government section of the Confederation of Professional Associations. The agreements that expire in 2001 and cannot be terminated earlier include those for municipal workers, local government salaried employees, and hotel and restaurant workers.

Figure B6.
Duration distribution of wage agreements for 2.5 million employees.
Per cent



Source: Eurén, Christina (1998), Sammanställning av resultatet av 1998 års avtalsrörelse (Compilation of the result of the 1998 round of wage negotiations), Annex to a report from the Enquiry on Strengthening the Conciliation Institution.