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# MINIMUM WAGES - REPORT FOR THE GERMAN MINIMUM WAGE COMMISSION 2025

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# Note

A slightly modified German version of the text was published as "Statements from the Written Hearing" in the "Supplement to the Fifth Report of the Minimum Wage Commission to the Federal Government Pursuant to Section 9 (4) of the Minimum Wage Act". I proposed an immediate increase in the minimum wage in Germany to 15 euros. In June 2025, the Minimum Wage Commission agreed to increase the minimum wage from 12.82 euros on 1 January 2026 to 13.90 euros and to 14.60 euros on 1 January 2027.

# Table of Contents

# 1. Introduction

Minimum wages are a very common phenomenon. The International Labour Organization (ILO) reports that 90 percent of ILO members have minimum wages[1]. A recent survey of 160 countries with minimum wages found that real minimum wages were raised in 70 per cent of the countries surveyed in 2023 (see ILO 2024: 23ff.). Minimum wages must therefore be counted as an integral element of market economies. And there are good reasons for this.

Firstly, without minimum wages, the wages of generally low-skilled workers or groups that are disadvantaged in the eyes of employers would fall to a level that would be socially unacceptable. Without minimum wages and in the absence of welfare state measures such as monetary transfers, wages in many countries would fall without limit in the face of unemployment, which is a normal state of affairs in many countries. There are only a few countries in which there is no statutory minimum wage and the trade unions are strong enough to prevent the emergence and expansion of a low-wage sector solely through collective bargaining. This group of countries includes Scandinavian countries such as Finland and Sweden; West-Germany also belonged to this group of countries after the Second World War. However, the introduction of a minimum wage in the united Germany in 2015 was made necessary by the partial deregulation and flexibilization of the labour market, the decline in trade union organising power and employers' resistance to declarations of general applicability of collective agreements[2].

Secondly, minimum wages not only have the function of preventing an explosion of the low-wage sector with socially not acceptable low wages, they also have the function of preventing the entire wage structure from slipping downwards in specific situations. For example, it cannot be ruled out that the nominal wage level will fall in the event of high unemployment and the economy will enter a catastrophic deflationary spiral. A deflationary process is triggered when nominal wages and thus unit labour costs fall. This implies that lower costs will force companies that are in competition to lower their prices. This increases the real debt burden of companies as well as that of private and public households, and there is a risk of a comprehensive over-indebtedness of the economy and deep financial crisis. An example of this is the Great Depression in the 1930s in the United States and Europe (cf. Fisher 1933). Japan after the 1990s is an example of how minimum wage policy was not used to establish an anchor against deflationary developments. Minimum wages in Japan followed the general wage trend, which was characterised by falling nominal unit labour costs and thus deflationary tendencies (cf. Herr 2015).

[1] Of the 195 countries in the world, 187 are members of the ILO.

[2] In 1998 (2023), 68% (44%) of employees in the old German federal states, that means the states before German unification, worked under industry level collective agreements, 8% (7%) under company level collective agreements and 24% (49%) under no collective agreements. In the new federal states, that means the states of the former German Democratic Republic which belonged before German unification in 1990 to the Soviet bloc, the figures were 50% (31%) for industry level collective agreements, 13% (14%) for company level collective agreements and 37% (56%) for no collective agreements (Statistisches Bundesamt 2025a).

In the debate about minimum wages, we see a paradox: almost all countries in the world have a minimum wage, yet the prevailing economic school, neoclassical economics in all its forms, considers a minimum wage to be detrimental to employment. Let us listen to Milton Friedman (1962: 148), probably one of the best-known neoclassical economists of the post-World War II era:

> …"The state can legislate a minimum wage rate. It can hardly require employers to hire at that minimum all who were formerly employed at wages below the minimum. It is clearly not in the interest of employers to do so. The effect of the minimum wage is therefore to make unemployment higher than it otherwise would be." Gregory Mankiw (2001: para 4), author of one of the most influential text books in economics, writes: "Like most other prices, wages are set by the market forces of supply and demand. The major difference between high-wage workers and low-wage workers is not that the former are better organised or better liked by their employers – it's that their higher productivity enhances the demand for their services. … The living wage campaign wants to repeal the law of supply and demand and raise wages by fiat. The goal is to help low-wage workers. Unfortunately, it wouldn't work out that way. One effect of a higher wage is a reduction in the amount of labour that employers demand."

In the simplest case, the negative employment effects are determined within the framework of neoclassical thinking by counting the number of employees who benefit from a minimum wage increase and are then, according to the logic, made redundant. However, there is a problem with the neoclassical argumentation. Despite many predictions about the negative effects of minimum wage increases, no negative employment effects have been empirically found at a macroeconomic level (for a comprehensive literature study, see Schmitt 2013) – also not in Germany. "The introduction of a statutory minimum wage was ultimately pushed through in Germany in 2015 against great resistance from politicians and academics. The employment losses unanimously predicted by standard economics did not materialise - fully in line with the empirical evidence of international minimum wage research." (Heise 2023: 143)[3] Traditional neoclassical labour economics was thus put in an explanatory crisis.

A way out of this dilemma was offered by a special case in the neoclassical model, the monopsony in the labour market (first discussed in Robinson 1933 and Stigler 1946, see section 2). However, it seems unconvincing to attribute the lack of negative employment effects of minimum wage increases to this special case alone.

This working paper takes a different approach. It counters the neoclassical argument with a fundamentally different theoretical approach in order to analyse the effects of minimum wages. It draws on the original works of John Maynard Keynes (1930 and 1936).[4]

The second section develops and demonstrates the effectiveness of this theoretical approach in explaining the empirical development in Germany. The third section draws conclusions.

[3] Own translation.

[4] It should be borne in mind that after the Second World War, the "Neoclassical Synthesis" became the dominant interpretation of Keynes, a mixture of neoclassical ideas that apply in the long term and Keynesian ideas that generate short-term disturbances. The New Keynesianism that emerged after the 1980s has even less to do with Keynes' ideas.

# 2. Effects of minimum wage increases

## 2.1 The macroeconomic effects of minimum wage increases

An increase in minimum wages received by a relevant group of employees, that is higher than the general wage increases, compresses the wage structure from below and thereby changes the distribution of income.[5] A generally accepted indicator for the relative level of the minimum wage is the Kaitz index, which indicates the relationship between the minimum wage and the median wage. Germany is one of the countries in which an increase in the minimum wage above the general wage increases compressed the wage structure from below and thus increases the Kaitz index.[6]

An increase in the minimum wage, which raises the Kaitz index, has a variety of macroeconomic effects. In order to understand the overall effect of minimum wage increases, we will first discuss the determination of the employment volume from a Keynesian perspective (see Figure 1).

Since at least Keynes (1936), there has been a macroeconomic paradigm that argues that in a situation of unused production capacities there is a close relationship between real aggregate demand and employment. In a typical economic expansion process, investment increases, generating income and production capacity, with a large proportion of income being consumed and creating demand that utilises the capacity created. Government demand and exports also play a role in capacity utilisation. There is a filter between the demand for goods and services and employment. This filter depends on various factors and determines the macroeconomic level of labour productivity. By definition, employment depends on aggregate output, which depends in most economic constellations on aggregate demand, and the level of macroeconomic productivity. The percentage change in

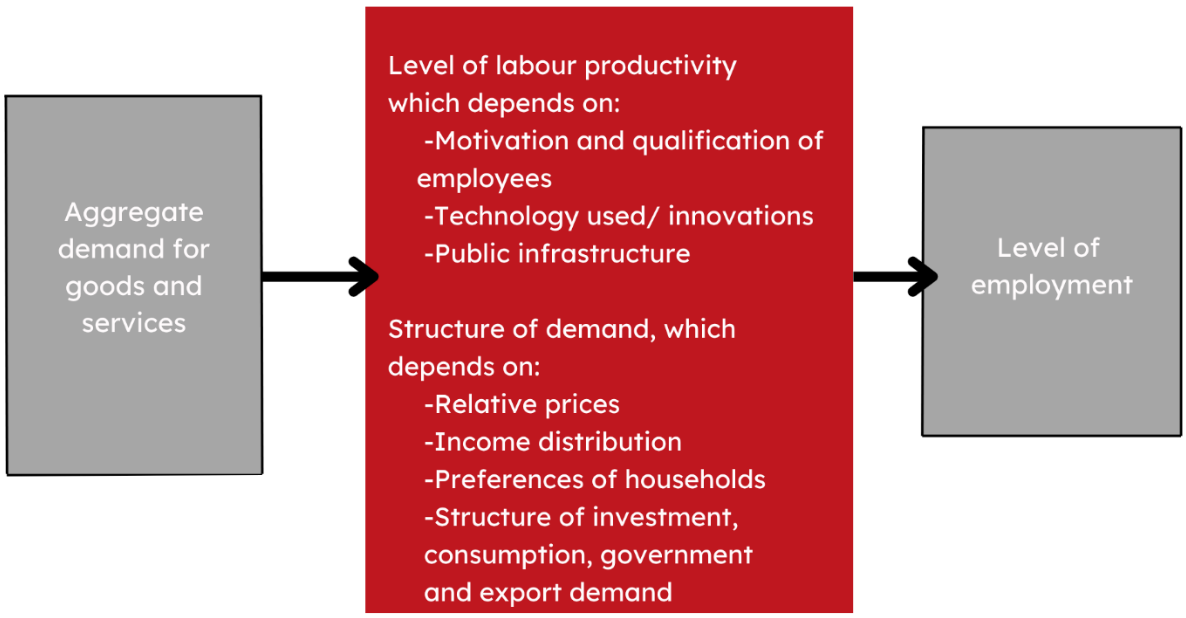
[5] Let's take Brazil as an extreme example, which we will return to below. Under the first presidency of Luiz Inácio Lula da Silva (Lula) from 2003 to 2011, minimum wages were increased by 62% in real terms between 2003 and 2012. The Kaitz index rose from 45% to 58% during this period. Inequality in the country decreased significantly, the GINI coefficient fell. Incidentally, employment in the formal sector rose from 80 million to 125 million during this period (Saltiel / Urzúa 2022: 879ff.; Leubolt 2014).

[6] There is a second group of countries in which minimum wage development largely or at least to a relevant extent replaces collective bargaining. In these countries, the trade unions are typically extremely weak and wage bargaining only exists in individual larger companies and in parts of the public sector. The minimum wage plays a dominant role in wage coordination in countries such as Estonia, Lithuania and the Czech Republic (Du Caju et al. 2008: 18). In many countries of the Global South, the development of minimum wages is the most important instrument for coordinating macroeconomic wage development. In a number of countries, there are minimum wage systems that determine even the wage structure for individual occupational groups (ILO 2020: 70ff.). A wage formation system that sets a fixed lower limit for the wage level through the minimum wage and in addition collective bargaining between trade unions and employers then determines the wage structure and general wage development is functional. Such a system exists for example in Germany. For the debate on functional macroeconomic wage development, see Heine / Herr (2024).

employment corresponds to the percentage increase in real output minus the percentage increase in the macroeconomic productivity level.[7]

First of all, the economic productivity level depends on the motivation and qualifications of the workforce as well as the technology and innovative strength of an economy, including the organisational performance of the management. Of course, the quality of the public infrastructure also plays an important role. If the level of productivity increases for the same aggregate demand, for example due to technological progress, then employment will fall.

*Figure 1: Determination of the employment level*




The macroeconomic productivity level also depends on the structure of demand and therefore the structure of production. If, for example, more labour-intensive services with a relatively low productivity level are in demand and fewer industrially produced goods with a high productivity level, then the macroeconomic productivity level falls and employment rises with the same aggregated demand. The structure of demand depends on a variety of factors, such as investment dynamics, government demand and the structure of exports. In the context of the minimum wage debate, however, we want to focus on the demand of private households.

Consumption demand depends on the level of income and preferences of households. However, it also depends fundamentally on the distribution of income. Wealth distribution also plays a role for consumption demand, However, minimum wages primarily affect income distribution and not distribution of wealth. If the Kaitz index

[7] By definition, GDP = (GDP/N)·N, where GDP stands for the real gross domestic product and N for the macroeconomic labour input. GDP/N expresses the macroeconomic labour productivity (π), so that GDP = π·N or N = GDP/π. Expressed in rates of change, employment changes correspond by definition to $\dot{N} = (\dot{GDP}) - \dot{\pi}$. If GDP grows by three per cent and productivity by two per cent, then employment increases by one per cent.

rises as a result of an increase in minimum wages, then there will be a redistribution in favour of minimum wage earners. If we assume that minimum wages affect the service sector in particular, as there are many jobs with low wages in this sector, then it must be assumed that the prices for services will rise after the minimum wage increase. There will be a shift in relative prices and a slight increase in the price level. Minimum wage earners can consume more in real terms, while the prices of specific goods have risen slightly for the remaining economic units, causing their real demand to fall marginally. Nevertheless, the change in income distribution is expected to lead to an overall increase in aggregate demand, as minimum wage earners are typically low-income earners who have a higher propensity to consume than higher income groups. A more equal income distribution not only stimulates capacity utilisation; it may even support high investment. “Moreover, experience suggests … that measures for the redistribution of income in a way likely to raise the propensity to consume may prove positively favourable to the growth of capital.” (Keynes 1936: 373)

If the Kaitz index rises, relative prices change, whereby it must be taken into account that the output of one industry is the input of other industries and therefore the entire system of relative prices can change as a result of substantial minimum wage increases. This can also have an impact on the level of productivity in an economy via a change in the demand structure.

Following these considerations, the overall effects of an increase in minimum wages, which increase the Kaitz index, can be discussed in detail (see Figure 2).[8]

**a) The increase in the minimum wage leads to higher aggregate demand via the effect of a more egalitarian income distribution.** This leads to a clear positive employment effect at the macroeconomic level. The fact that minimum wages have positive distributional effects is not disputed. The ILO (2020: 86) writes: “A growing body of literature has emerged over the past two decades examining the empirical evidence for the link between minimum wages and income inequality. Most analysts seem to agree that wage floors have the capacity to reduce both wage and income inequality in advanced economies and developing countries alike. The literature review … provides evidence that, for the most part, minimum wages can have an equality-enhancing effect by bolstering the relative earnings of low-paid employees, albeit to different degrees.” This was already stated in the classic text by Card and Krueger (1995) for the USA, and there are also a number of studies in Europe that come to the same conclusion (ILO 2020: 86ff.).

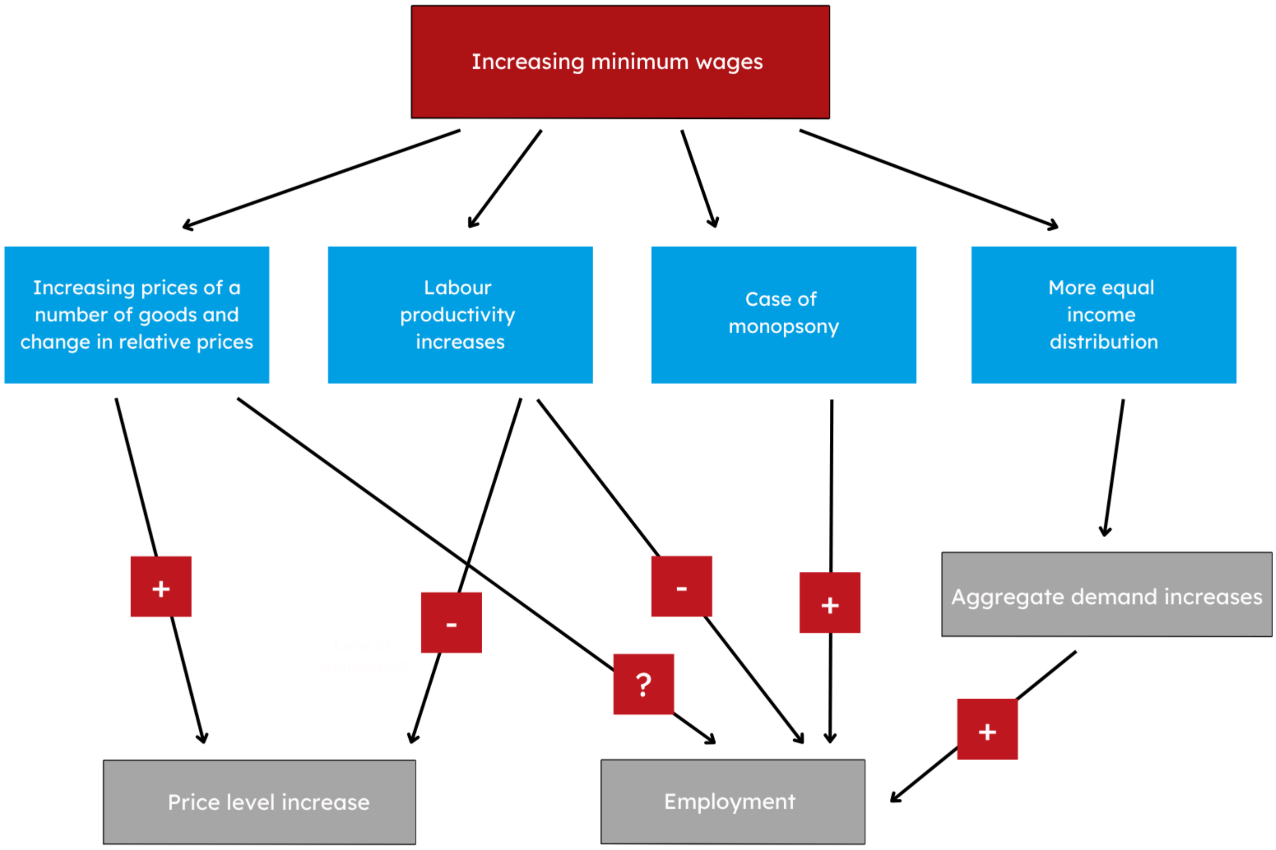
**b) Higher minimum wages increase the cost of labour in the sectors affected by minimum wage increases.** In the event of rising unit labour costs, companies will increase prices. They have the market power to do so, as all companies in an industry are affected by the cost increase. Higher unit labour costs, like higher energy costs or higher VAT, are therefore ultimately passed on to prices. Minimum wages can therefore lead to a limited increase in price levels. This is based on the view that the structure of relative prices depends primarily on the cost structure in the individual sectors, i.e. on unit labour costs, which depend on nominal wages and productivity in the various sectors, as well as other cost components such as intermediate inputs,

8 See also the expert report for the Minimum Wage Commission in 2017 (Herr et al. 2017)

raw materials, VAT, etc. The market power of companies in specific sectors, which determines the profit mark-up, also plays a role. In sectors with oligopolistic or monopoly profits, companies may not pass on all cost increases as this would reduce demand for their products too much.

Wage dispersion in a country, which depends on a variety of factors such as labour market institutions, minimum wages, the strength of trade unions, notions of fairness, etc., is therefore one of the factors that determine the structure of relative prices. The wage structure is not only determined by the various qualifications of the labour force and its productivity. Naturally, one would expect qualified workers to earn higher wages than less qualified workers. But how high the wage differences are is hardly determined by differences in productivity. Take, for example, the remuneration of DAX board members, who earned an average of 2.65 million euros in 2023, while the CEOs even earned a good 3.7 million euros (Wirtschaftswoche 2024). In contrast, the median salary of full-time employees in Germany in 2023 was 43,750 euros (Rush 2025).[9]

*Figure 2: Effects of minimum wage increases with the effect to compress the wage structure from below*




*+: positive effect, -: negative effect, ?: unclear effect*

[9] In neoclassical economics, the wage structure in equilibrium is determined by the marginal productivity of labour in the various segments of the labour market. If trade unions or the state intervene in the wage structure, employment falls and there is unemployment. In the approach advocated here, productivity and wages determine costs and become an element of the structure of relative prices.

| Most likely expected overall outcome |
|---|
| - Slight increase in employment<br>- Small increase in price levels<br>- Increase in labour productivity<br>- Long-term contribution to promoting productive, stable and socially cohesive societies |

**c) As minimum wages affect specific prices, as mentioned, the structure of relative prices changes.** It is quite possible that certain products or services that become more expensive as a result of minimum wage increases will be less in demand and therefore employment in these labour market segments will fall. However, this should not be viewed negatively. The change in the wage structure alters the price structure, which in turn affects the consumption structure. This shift in relative prices means that demand for some products decreases while demand for others increases.[10]

**d) A rising Kaitz index promotes productivity.** This is initially due to the fact that employees who receive a minimum wage increase feel more valued and are more motivated. Labour turnover decreases. Minimum wage increases can also lead to organisational improvements in companies and further training measures. And finally, companies can rely on improved technologies in case of higher wages (Riley / Bondibene 2017). If minimum wages rise, it is also to be expected that companies in an industry with very low productivity will have to leave the market or increase productivity, as they will no longer be "subsidised" by low wages. Minimum wages therefore lead to fair competition within an industry based on equal wages for all companies, and a positive reallocation of resources. The stronger the productivity effect, the smaller the price effect or the change in relative prices and the price level boost. However, the productivity effect leads to negative employment effects. Nevertheless, this is offset by positive employment effects due to the increase in aggregate demand as a result of redistribution.

In addition to the short- and medium-term positive effects on productivity, there is also a long-term positive effect in that an increase in the wages of the lowest wage groups increases this group's expenditure on education and training, promotes better career development for children and, overall, reduces the negative economic and social effects of inequality (Wilkinson / Pickett 2009).

**e) This leaves the case of the monopsony (or oligopsony), which plays such an important role in neoclassical economics (see Herr 2023).** In the monopsony, a company is in a position of power vis-à-vis employees - let's take a large steel factory as the main employer in a small town. Starting from an equilibrium wage, this company can reduce employment as part of its profit maximisation strategy and thus depress the wages of all those still employed. As long as lowering wages is more beneficial than reducing production and thus sales revenue, a company will reduce

[10] Let's take a look at Brazil. By increasing the minimum wage, the cost of domestic workers rose dramatically and the lower middle class could no longer afford domestic workers for the whole week. However, other and better paid jobs have been created - a positive development.

employment and wages. Employees of the company will not immediately change employers if wages fall due to relocation costs, preferences or a variety of other factors. However, the corporate strategy described above only works if there are weak trade unions that accept falling wages. The introduction of a minimum wage can now render this strategy null and void. This is because if the minimum wage is increased to the level of the equilibrium wage, the company will increase its employment and production again. However, if wages rise above the equilibrium wage, the usual negative employment effects occur in neoclassical economics. The relevance of the monopsony case on labour markets is difficult to determine in general terms (for an overview see Manning 2021). Therefore, it cannot be ruled out that monopsonies and oligopsonies play a certain role and increasing minimum wage in these cases have positive employment effects and at the same time reduce extra profits. However, it should be noted that, in the theoretical approach presented here, there is no equilibrium wage based on marginal labour productivity which would automatically result in unemployment if the wage level were exceeded.

To summarise, we can state that an increase in the minimum wage can be expected to have moderate positive employment effects overall - particularly via the income distribution effect. At the same time, an increase in productivity can be expected, which is positive for economic development in the long term. In addition, strong minimum wage increases will lead to a shift in relative prices with the associated effects and a moderate rise in price levels.

## 2.2 The macroeconomic effects of minimum wage increases

The model presented above fits very well with the empirical development in Germany following the introduction of the minimum wage in 2015.

From 2015 onwards, wages in the 5th, 10th and 20th percentiles in Germany rose significantly faster than the rest of the wages. This means that the minimum wages have led to a relatively broad increase in low wages (Bosch 2023: 7; Bachmann 2022). The low-wage sector (wages lower than two thirds of median gross hourly earnings) fell by 1.3 million employees in Germany between April 2014 and April 2024. In 2015, 21 per cent of employees belonged to the low-wage sector, in April 2024 it was 16 per cent, still high but lower (Statistisches Bundesamt 2025; Grabka 2024). This development led to a more egalitarian income distribution (Pusch 2024). This resulted in a correspondingly positive effect on aggregate demand

An increase in productivity was also observed in the sectors particularly affected by the minimum wage increases. The productivity effect is based on an increase in productivity in the companies directly affected by the minimum wage and / or on a shift of workers to more productive companies, usually in the same industry (Bosch 2023: 10). According to Dustmann et al. (2020), minimum wage increases in Germany led in particular to a reallocation of employment from very small and low-paying companies to larger and more productive companies. This has improved the quality of companies and working conditions overall.

Caliendo et al. (2022) compared between 2014 and 2021 a group of workers affected by minimum wage increases with a comparable group of workers who were not affected by minimum wages. The comparison found that there was a moderate contraction in a specific quantitatively overall small type of part-time employment, so called mini-jobs.[11] There was no change in employment subject to social insurance contributions, i.e. no negative employment effect However, this method does not take into account the fact that demand effects due to redistribution can lead to an increase in employment. Positive employment effects of minimum wage increase were obtained in an earlier study commissioned by the Minimum Wage Commission (Herr et al. 2017). In this study, the demand effect of rising minimum wages increased the growth of real gross domestic product and moderately increased employment. The number of hours worked in Germany rose from 60,460 million in 2015 to 61,372 million in 2024, while the minimum wage rose from €8.50 to €12.41 during the same period. The unemployment rate in Germany was 6.4 percent in 2015 and 6.0 percent in 2024. The minimum wage increases did not lead to high unemployment, as was often predicted, although macroeconomic development depends on many factors and this is not proof of the effects of minimum wages.

To summarise, we can state that minimum wage increases, which compress the wage structure from below, did not lead to any negative macroeconomic employment effects in Germany and increased productivity.

# 3. Conclusions for minimum wage development in Germany

In October 2022, the European Union Minimum Wage Directive was adopted, which was to be implemented by 2024. The directive recommends that minimum wages should not fall below 60% of median wages. For Germany, this would correspond to a minimum wage of €15.12 in 2025 (Schulten 2024). With a minimum wage of 12.82 euros at the beginning of 2025, the DGB (2025) also calls for a minimum wage of around 15 euros. In fact, there is absolutely nothing to be said against increasing the minimum wage to 15 euros in 2025. Germany would then reach the Minimum Wage Directive's target of a minimum wage of 60% of the median wage for the first time since the minimum wage was introduced in 2015. A minimum wage of 15 euros would not be expected to have a negative impact on employment. On the contrary, as in the past, a moderate positive macroeconomic employment effect could be expected. Positive effects on productivity could be expected as well. Last but not least, the gap between social transfers and labour income would be widened, which plays an important role in the perception of fairness in income distribution.

This leads us to conclude that the desired relationship between the minimum wage and the median wage is, in principle, a question that must be decided politically. It is

[11] Mini-jobs are marginal employment positions with a maximum monthly wage of €556 in 2025 or a maximum of 70 working days per calendar year. Employees in mini-jobs do not pay into unemployment insurance or health insurance and are therefore not insured in these areas. They can, if they want, be exempted from pension insurance. The minimum wage applies to mini-jobs.

part of the question what level of inequality a society is willing to accept in its wage structure. In the case of Germany, it is particularly important that a stable Kaitz index of 60% is realised. Further increases in the minimum wage compared to the median wage are of course possible. It should be noted that with an expected gross average salary for full-time employees of 59,094 euros in 2025, the median salary for full-time employees is only 45,800 euros (Rush 2025). Overall, Germany shows a relatively high level of inequality in the wage structure. The ratio between D9 and D1 (the lowest gross wage of the 10 per cent highest earners to the highest gross wage of the 10 per cent lowest earners) was 3.6 in Germany in 2021, the same value as in 2003. After 2003, the ratio rose to 4.0, only to fall again, not least due to the minimum wage. However, it should be noted that the ratio of D9 to D1 was 3.3 in 1995 (Grabka 2024: 73) and 3.18 in West-Germany in 1984 (Peters 2007: 9). In an international comparison, Germany ranks in the middle in terms of wage inequality. At the beginning of the 2020s, the D9-D1 ratio was 4.6 in the USA, 4.0 in Poland, 2.7 in France, 2.3 in Denmark and 2.1 in Sweden (ILO 2024: 41). There would therefore still be plenty of scope for a more equal wage structure in Germany. A significant increase in the minimum wage and a more equal wage structure are both economically possible. However, to achieve these objectives, society must engage in a broad debate on income equality.[12]

If the minimum wage is closely linked to wage growth, it can prevent or reduce the growth of a low-wage sector.. The minimum wage can reduce wage dispersion and thus income inequality overall. It is an anchor against deflationary nominal wage cuts. The minimum wage is an important element of an overall economic policy package. Other elements of such a package are a high level of collective bargaining coverage, which has unfortunately fallen significantly in Germany. Overall, inequality in Germany has risen, especially poverty.[13] This is detrimental to economic development. Research by the International Monetary Fund makes it clear that inequality, particularly at the lower end of the income scale, makes longer periods of growth less likely and prosperous development more difficult overall. This is supported by demand as well as productivity arguments (Ostry et al. 2014; Ostry 2015). Added to this is the fact that unequal societies lose their social coherence. This burdens the development of a country in many ways (Wilkinson / Pickett 2009). An increase in the minimum wage to a level of at least 60 per cent of the median wage — or even higher

[12] Let's come back to Brazil. Although the increase in the minimum wage in Brazil was an economic success, it led to a disastrous political backlash. After the minimum wage increases, the middle class, as mentioned, could no longer afford to hire domestic workers for the whole week as they used to. Going to restaurants or taking a taxi also became expensive, and new groups appeared in shopping centres that were unfamiliar. The result of the substantial increase of minimum wages was a profound change in society and lifestyle in Brazil. There was a middle-class revolt, the dismissal of Lula's successor and the election of right-wing radical President Jair Messias Bolsonaro in 2019. However, after Bolsonaro's presidency, however, Lula was re-elected.

[13] The WSI Distribution Report 2024 is based on disposable household income: The Gini coefficient rose from 0.282 to 0.310 between 2010 and 2021, the proportion of households below the poverty line (less than 60% of the median income) rose from 14.2% to 17.8% in the period, while the proportion below the severe poverty line (less than 50% of the median income) rose from 7.8% to 11.3%. In contrast, the proportion of rich households (more than twice the median income) rose from 7.7% to 8.0% and the proportion of very rich households (more than three times the median income) from 1.9% to 2.3% (Spannagel / Brülle 2024).

if there is a political consensus — is central to maintaining or creating a coherent society, as well as ensuring long-term economic and social prosperity.

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