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Research

Labour "power gap" to hurt corporate margins

#PositiveImpact

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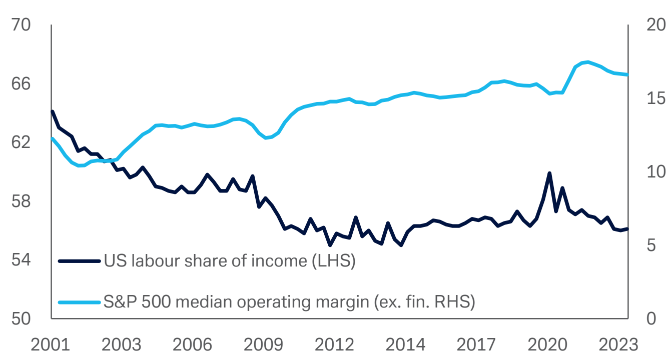
After Biden joined the UAW picket line last week and Trump spoke from a separate facility in Detroit, it is clear that labour power will impact corporates through the next presidential cycle. That is amplifying similar movements in Europe. The issue is the 'gap' between corporate and worker power. We believe the world is at a tipping point. The 'power gap' that has widened over the last few decades is beginning to shrink and will continue to do so for the rest of the decade.

The 'power gap' is still wide. It can be viewed in several ways and just one is in the following chart. This shows that company profit margins have risen much faster than wages.

Wages have underperformed company profits



Source: Haver Analytics, Factset, Deutsche Bank

Several factors that caused the 'power gap' are now reversing. Among them is that the integration of cheap labour from China into the world economy (which began in the 1980s) is largely complete. In fact, it is reversing in some cases. Higher Chinese wages reduce the incentive to outsource there. Meanwhile, some US and European companies are either decoupling from China or reconsidering investment in the country.

In the US and Europe, more demand for domestic workers will likely allow them to push for a greater share of the pie. We expect more industries to join the global industrial action, especially as workers see their peers from other firms making demands. Already we are seeing this happen. This year, the number of days lost to work stoppages in the US jumped to the highest level since 2000.

The corporates most likely to experience pressure from workers tend to be larger companies. These generally have larger workforces, more unionisation, and a greater history of industrial action. These factors are encapsulated in a more impactful 'labour management score'. Our analysis shows that companies with the highest potential labour impact also tend to have the least ability to absorb extra costs. In both the US and Europe, these firms generally have lower sales per employee and smaller profit margins. In other words, their bottom line may suffer greatly as wages increase. Particularly as one survey found that companies are struggling to pass on labour-related costs to customers.

If worker power grows, as we expect, corporate margins will come under further pressure into the medium term – especially for large-cap stocks. In turn, stock returns are likely to suffer. Consider that the stock of Ford and GM has fallen around 19% since the UAW contract negotiations began. The impact can also spread to other markets. Recent strike action at Chevron LNG plants caused natural gas prices to spike 35% at one point.

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