Moderate wage increases and flexible labour contracts to protect employment in Colombian manufacturing

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Based on conditional and unconditional demands for labour, we exploit the variations of real minimum wage across manufacturing subsectors to present evidence that this variable affects formal employment. *The long-term elasticity of labour demand to the minimum wage is around –0.7*. Accordingly, increases in the minimum wage lead to job losses for unskilled labour, mainly in plants with fewer than 100; thus, small increases in the minimum wage are desirable to protect employment. Labour demand is highly cyclical: the output elasticity is about 1.7. Thus, some flexibility in labour contracts is desirable to reduce the link between employment and variation of plants' sales. Open-ended labour contracts might allow reductions of the nominal wage rather than inducing job losses during periods of severe slumps, as has happened during the COVID-19 pandemic.