Raise Wages/Reduce Inequality Without Strong Labor Market Institutions? No Way, Jose!

1- Stagnation and Inequality

2. Analysis of Institutions: global evidence

3- Shrinking US Unionism

4- Informalization, Minimum Wages, Exec Pay, Etc.

5- Spreading Capital Ownership and Profit-sharing

6- Conclusion on Policy

Richard B. Freeman, Harvard and NBER
Berkeley, Aug 26, 2016

1.The Stagnant Real Wage/Inequality Problem

1-- Real wage increases for normal workers can come from productivity **growth** or **redistribution** of income from other income recipients (capital or high wage workers)

2- If you accept that “long term” productivity growth slackened then real wage growth at rate of productivity will not get much wage gain and will lock in high inequality.

3- Inequality creates big space for redistribution – measured capital share up, and up more if include capital income paid to execs and counted as labor earnings.

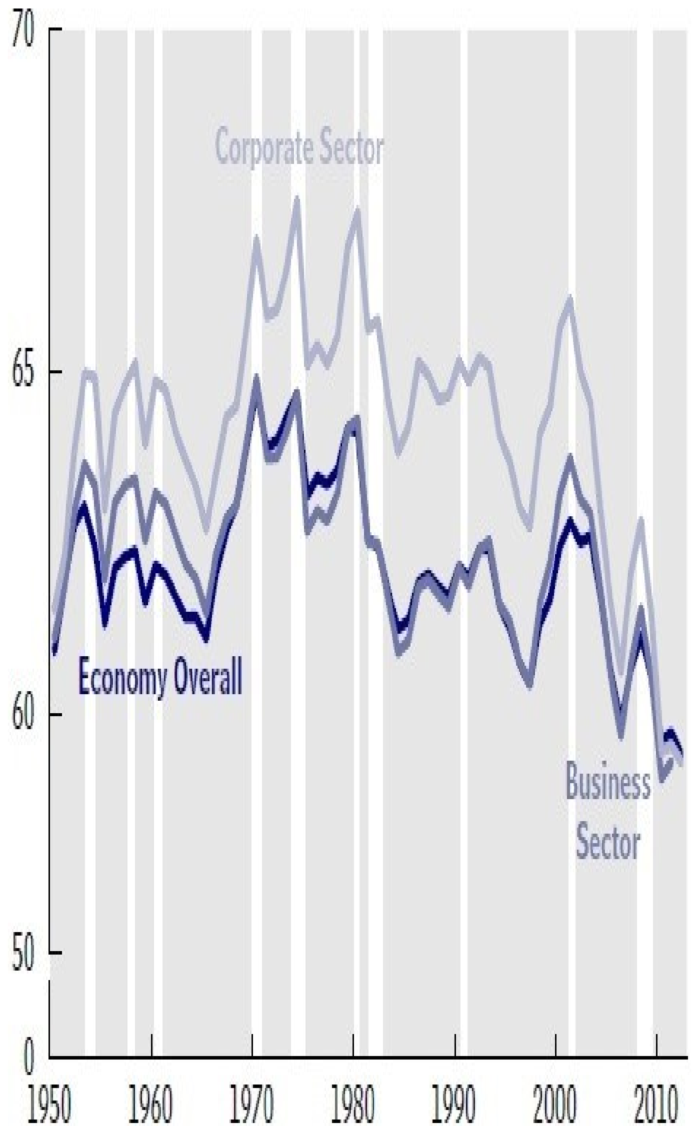
Fractiles of Inequality

1) Occupiers focused on **upper 1%** (22.5% of income in 2012), but share of income to **upper 0.1%** increased from 3.1% (1972) to 11.3% (2012) (half of upper 1%) so maybe focus on 0.1%
within upper 0.1%, 48% of income goes to **upper 0.01%** whose share rose from 1.2% (1972) to 5.5% (2012)
within upper 0.01%, 49% of income goes to **upper 0.001%.**

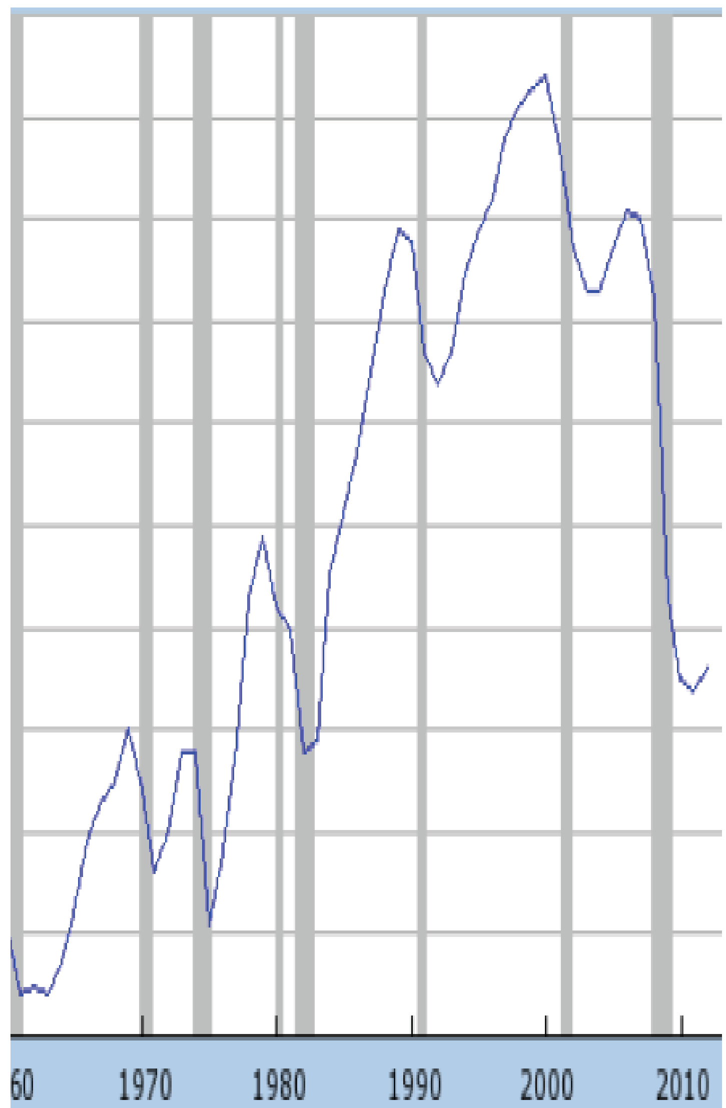
2) Top 400 taxpayers –**upper 0.00028%** of 145m returns –earned
1.5% of 2012 adjusted growth income (0.52% in 1992),
8.3% of dividends (1.4% in 1992); 5.3% of interest (0.9% in 1992)
12.3% of capital gains (5.7% in 1992)
(http://www.irs.gov/pub/irs-soi/12intop400.pdf)

Evidence that Inequality is New Normal for USA

Labor's Share of National Income



Employment/ Population



Gini Coefficient of all Households

2. Analysis of Institutions

What to include? CB but with low unionism, must consider other institutions as well: labor contracts – Weil's fissured labor markets; min wage; exec comp; corp governance ...

What is counter-factual?

1) If labor institutions remained as in 1970s, what would have happened to real wages and inequality? If unions, key issue is spillovers – to nonunion workers; to politics; etc – GE

2) If institutions were stronger/reacted more? I thought 2008 finance implosion change system greatly. Looking forward simulation.

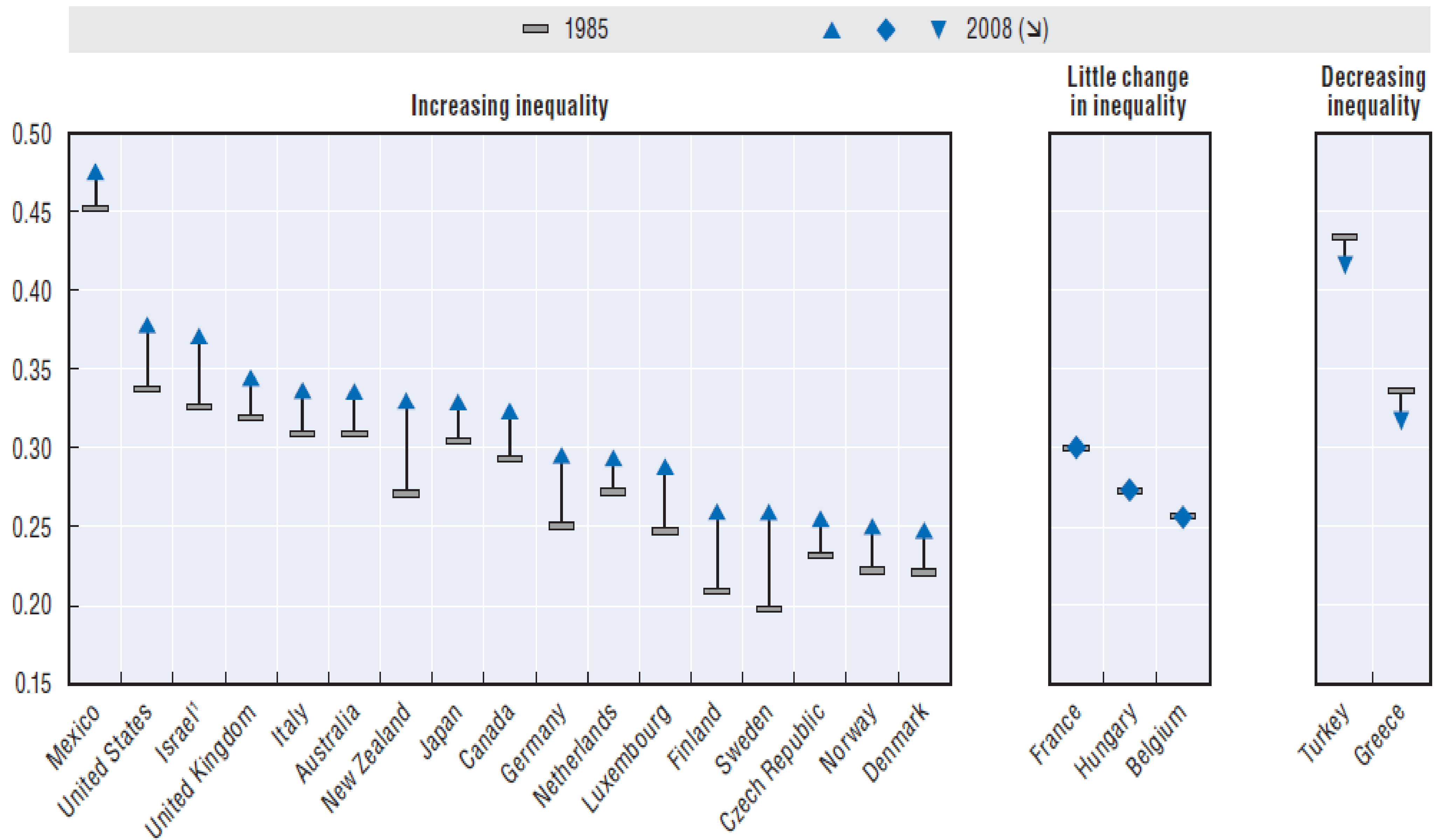
What if institutions are Cantillon's cock? Cock-a-doodle-do and sun rises. Endogenous institutions.

If all else was same, analysis at level of countries with different institutions would be ideal but the French is weird, Dutch are tall, Germans precise, Swedes into sharing; Canadians too civil ...

Three insights from Cross-Country

Figure 1. **Income inequality increased in most, but not all OECD countries**

Gini coefficients of income inequality, mid-1980s and late 2000s

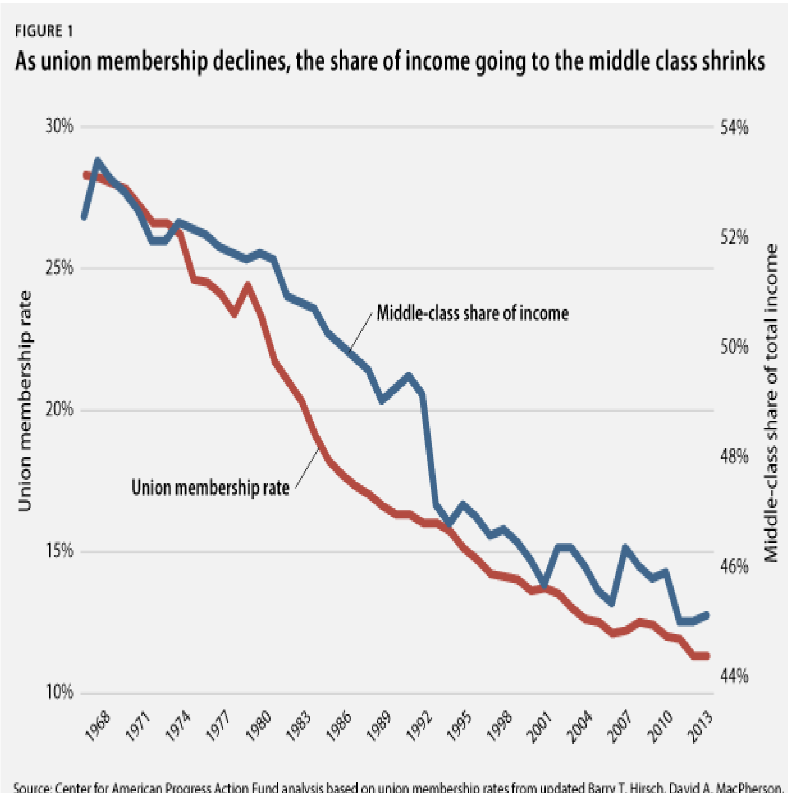


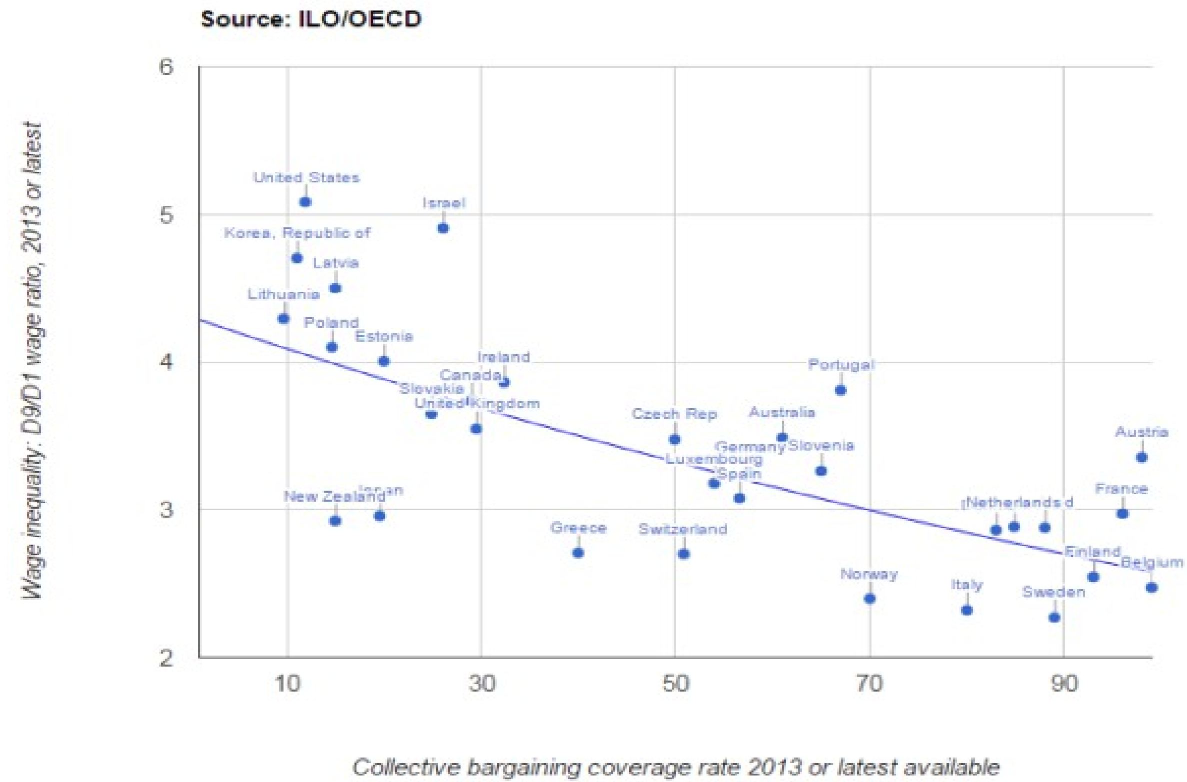
Changes in bargaining coverage, 2008 to 2012/13

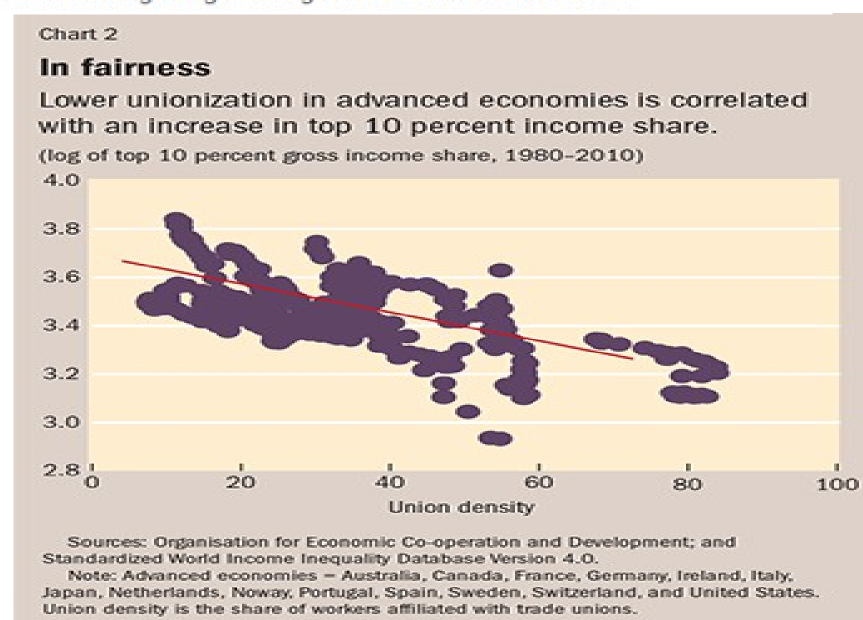
Campos & Nugent "Labor Market Reforms, Growth and Inequality: Evidence from a New Dataset" (July 2016)

"a dynamic analysis of the determinants of changes in employment protection legislation rigidity across countries and over time … based on more than 140 countries, (from 1960 to 2004) … to examine the "Freeman conjecture" that labor laws rigidity may decrease inequality without negatively affecting economic growth ... We find that the rigidity of employment protection legislation reduces income inequality but its effects on economic growth are ambiguous." This comes from regressions of Gini coefficients on index of labor market regulations and stuff and of per capita growth rates on index and stuff. The inequality result holds no matter what. The per capita growth result comes from adding investment and ethnic fragmentation and other stuff.

3. Unions/Labor Organizations







Unions reduce inequality.

Lower pay differentials within workplace

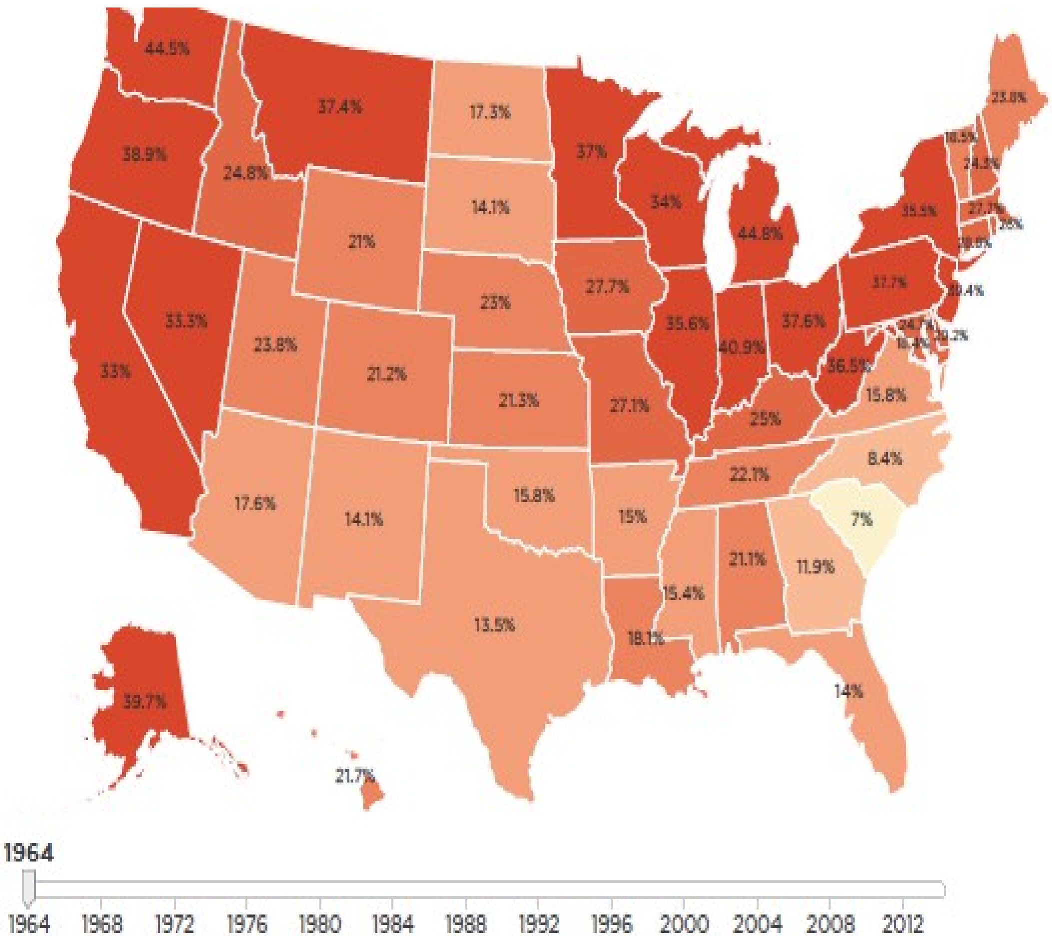
Reduce pay differentials across workplaces

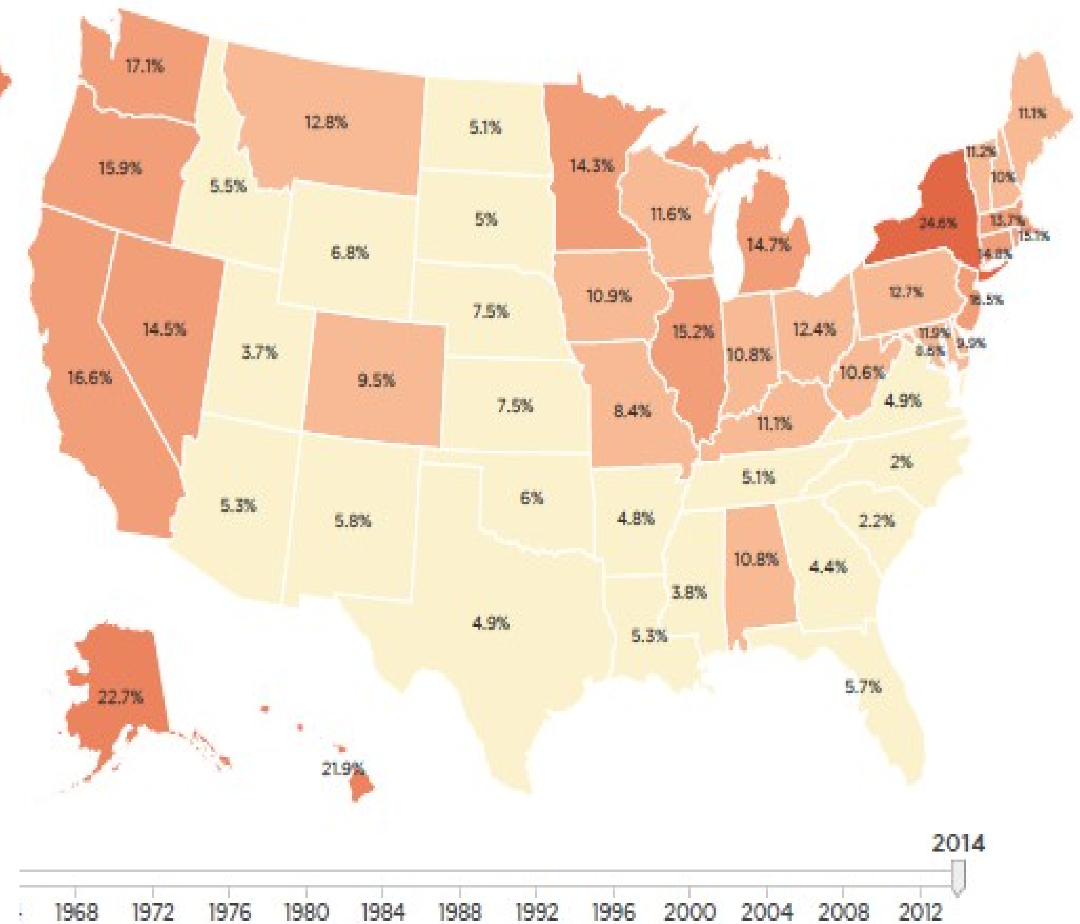
Establish procedures for promotions

Support minimum wages/social spending

Inter-generational transmission of education, income)

But where are US unions?





Pvt Sector Union Members (2015), 7.6 Million

Workers in ESOPs/ESOP-like plans, (2015) 15.0 Million

Total Union Members, (2015) 14.8 Million

Meta-Analysis of What do Unions Do
(Doucouliagos, Freeman, Laroche (2017)

Transforms 1,912 estimates of union effects from 306 studies into partial correlation coefficients through 2015 and finds

1- No union effect on growth of productivity

2-Varying relation to productivity by country and industry around average of 0, with US positive in education, construction, and recent studies for nursing homes.

3- Reduces turnover, raises wages/cuts profits; negatively associated with investment in physical capital/R&D. (But wage and turnover meta are older)

4- Union effects seem to diminish over time.

Assessing union decline in increased inequality/wage stagnation

Shift-share: lower inequality/union premium x Δ union share estimates contribution of Δ unionism. These are "conservative" estimates. But inequality/wage stagnation among union workers moved similarly to that among nonunion workers. It *could be* that changes for both groups reflect Δ density, but difficult to prove. So assume *could be* is and we get:

Rosenfeld et al (2016) analysis. Regresses nonunion wages on union density in 72 region-industry cells over time with other stuff and uses coefficient on density to estimate that less educated nonunion private-sector men would earn 8% more in 2013 if density was at 1979 level. With 0.67 ln point increase in productivity from 1979-2013 this would be 12% of the real wage/productivity gap , but coefficient on "spillover" declines over time.

Concerns over this advocacy modeling: does not "attack" result with other time varying region-industry competitor: trade; population; regional income; so we can see robustness. Not consistent with international experience. Increased inequality/stagnant wages in EU countries with CB suggests this overstates impact. German unions negotiated wage freezes and accepted secondary jobs so that inequality has gone up. Now gone to minimum wage.

4. Other institutional changes

At lower part of labor market, growth of informal labor market David Weil, Fissured Labor Market; Katz and Krueger estimates

Table 2
Alternative Work Arrangements

(Percent of Employed Who Also Worked During Survey Week)	CPS Feb-1995	CPS Feb-2005	RAND Oct/Nov-2015 Weighted	RAND Oct/Nov-2015 Alt. Weight
Alternative Work Arrangements	9.3	10.1	17.2	15.8
Independent Contractors	6.4	6.9	9.6	8.4
On-Call Workers	1.6	1.7	2.8	2.6
Temporary Help Agency Workers	1.0	0.9	1.6	1.6
Workers Provided by Contract Firms	0.5	0.6	3.3	3.1
Note:				
Workers Provided by Contract Firms (Single Jobholders)	0.5	0.6	2.1	2.0
Number of Observations	61,752	63,437	2,194	2,194

Source: Current Population Survey; Katz and Krueger (2015).

At top of market, failure of Clinton-Gore's “no tax deductions for executive pay above $1M” by performance pay 162m exemption that pushed exec pay to capital income. No company level analysis of how much this contributed to shift increased CEO/worker pay, But if apply ERISA principle that firms must make tax-privileged fringes available to all, would force some to rethink huge capital incomes paid to top five executives. Other tax breaks to pvt equity.

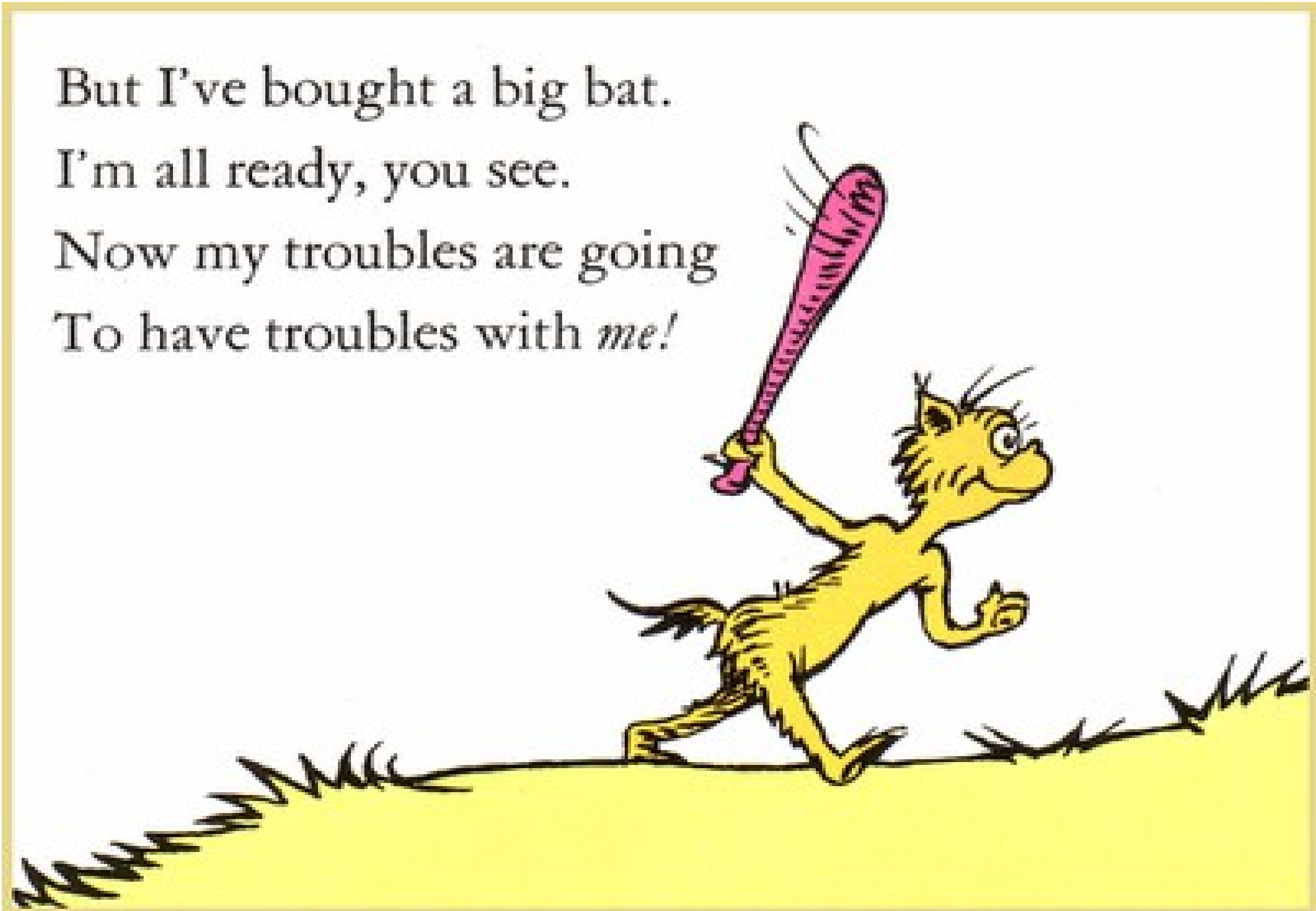
Minimum Wage

Three determinants of effects: elasticity – if <1 get redistribution to lower paid; and "el farol" spillover, where increased minimum spills over to many persons above minimum or uncovered by law; and for policy increases, how elasticity and spillover change with increases.

On elasticity, Doucouglias and Stanley 2009 BJIR meta-analysis reports no effect on employment in 64 US minimum wage studies after correction for publication bias – funnel graphs showing selection for negative minimum-wage effects. Belman and Wolfson examine hours and employment in 23 studies and get median elasticity of -0.05. Giotis, Georgios; Chletsos, Michael, 2015 find no publication bias and small negative in 45 studies 2010-2014.

On spillover, Harris and Kearney 2014 estimate that "minimum wage increase could raise the wages of up to 35 million workers—that's 29.4 percent of the workforce" based on simulation assumption that people within 150% would be affected, excluding self-employed. The el faro data that is convincing is for informal sector workers. No compelling evidence on spillover.

5. Road to More Equal Economy: Institutions to Change Labor's Capital?



“Preponderance of Evidence” says ownership raises productivity and earnings

Meta-analysis reports that “two thirds of 129 studies... found favourable effects while one tenth found negative effects”. “Research ... overwhelmingly positive and largely credible.”

2007 UK Treasury Oxera study of tax breaks for *individual* employee stock ownership in 16,844 corporations found ownership increased value added per worker by ~ 2.5% in the long run.

Kruse, Freeman, Blasi NBER study of 41,000 worker reports in 14 firms found worker co-monitoring helps overcome free riding. Increased employee attachment, lower turnover, more employee suggestions for improvements; works best with other “high performance” labor practices and policies.

Blasi, Kruse, Freeman, Great Places to Work study reports that of the 100 Top, 17% have ESOPs, 10% majority employee owned, 16% give options to most employees; applicants with more inclusive capitalism --> high performance work practices; higher ‘Tobin’s Q’.

Critics Worry about non-diversified investment in own firm.

But ...Privately-held ESOPs half as likely to go bankrupt/close as controls; four times more likely to have defined benefit plan. Pension assets/ employee higher in ESOPs. ESOP default on company stock acquisition loans 1-2% lower annually than LBO and pvt equity portfolios.

But … BLS rates of return in 1991-2011 show ESOPs outperform 401k plans in most years, were less volatile, and mean performance is > all plans

And GSS2014 (Kruse and Kurtulus) shows that ownership/profit sharing firms have low layoff rates and that shares via firm grants, not purchase:

	Layoff Rates	
	Yes	No
Employee Owned	1.6%	4.6%
Profit sharing	2.7%	4.2%

	Granted	Purchased
%Own Stock	69.00%	31.00%
Mean Value	$36,800	$11,900
Median value	$4,500	$300

Strong base

	2002 (1)	2006 (2)	2010 (3)	2014 (4)
All private sector				
Percent of employees covered				
Own company stock	20.1%	17.1%	17.8%	19.5%
Hold stock options	12.3%	9.1%	9.0%	7.2%
Profit sharing	33.2%	38.1%	^	35.8%
Gainsharing	23.0%	26.5%	^	25.3%
Any of above	42.1%	46.2%	^	44.7%
Number of employees covered (millions)				
Total employees in economy^^	109.0	114.5	107.8	117.3
Own company stock	21.9	19.6	19.2	22.9
Hold stock options	13.4	10.4	9.7	8.5
Profit sharing	36.2	43.6	^	42.0
Gainsharing	25.1	30.4	^	29.7
Any of above	45.9	52.9	^	52.4

But limited depth

		2002 (3)	2006 (4)	2014 (5)
Size of financial stakes				
Company stock value if own stock				
Dollar value	Mean	$41,972	$32,691	$45,342
	Median	$8,000	$10,000	$10,000
Percent of salary	Mean	80%	57%	95%
	Median	21%	25%	23%
Bonus size if received profit sharing				
Dollar value	Mean	$6,652	$6,846	$8,347
	Median	$1,250	$2,000	$2,000
Percent of salary	Mean	10%	10%	11%
	Median	4%	5%	5%

6. No way Jose Conclusion

1) Problem is not whether economists/policy-makers can devise policies/ policy experiments to strengthen labor institutions in desirable ways but whether society acts on them. Financial implosion did not produce great reforms in capitalism and inequality/stagnant wages seems to have opened door to more negative than positive social responses.

2) No capitalist economy has low inequality/reduced inequality outside of war or disasters without strong labor movement; and no organization beyond unions has produced change that lowers inequality for most workers.

3)Unions have grown in spurts in crisis, but they failed to expand in Great Recession/Sluggish Recovery as they did in 1930s and, with some exceptions, are establishment bureaucracies incapable of acting out of CB/Dem Party box. What will get unions/workers to respond?

4) Luckily for the health of universe, economists almost always fail to see big change, so a pessimistic analysis that change does not seem imminent means it is likely to happen, often set off by some small change. Who knows what will happen if/when the Harvard Grad students vote union?