

Global Inequality & Growth:

Inequality and the role of institutions

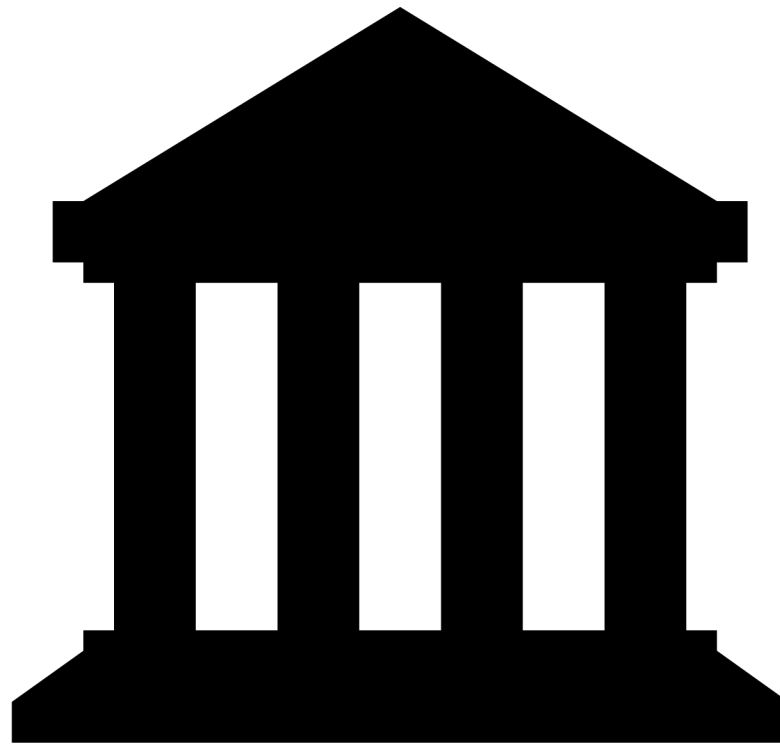
Ludvig Wier



Last lecture

- Skills premium in many advanced countries in recent decades
- US: earnings gap between college and high school graduates has more than doubled over the past three decades
- Increase in the skill wage premium explains 60–70% of the rise of US wage inequ. between 1980 and 2005 (Goldin and Katz 2010)
- The US skill premium has increased more than most other developing countries

This lecture: how does institutions impact inequality?



Roadmap



The limits of the supply-demand framework



Minimum wage



Unions



Market power

Limits of the supply-demand framework



Limits of the supply-demand framework

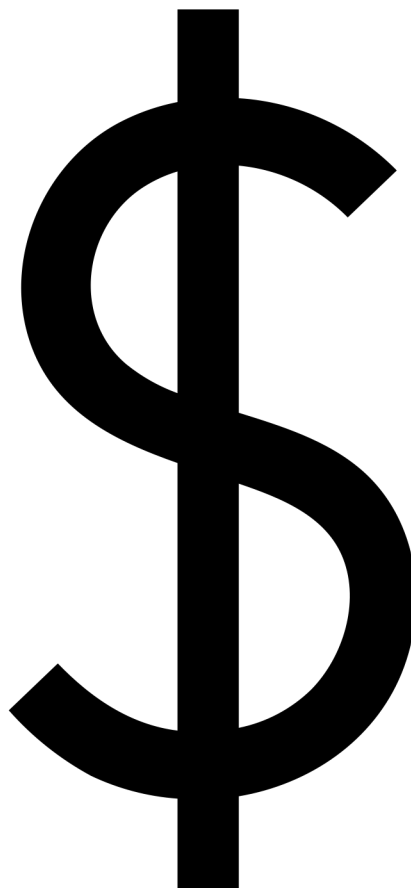
The supply/demand framework (“race between education and technology” story) cannot explain key facts:

- Sharper inequality increase in the US than elsewhere
- Rise in inequality concentrated at the top

Four main other forces also play a role:

1. **Changes in minimum wages**
2. **Change in the role and power of unions**
3. **Changes in market power**
4. Changes in top marginal income tax rates (not covered today)

Minimum wage

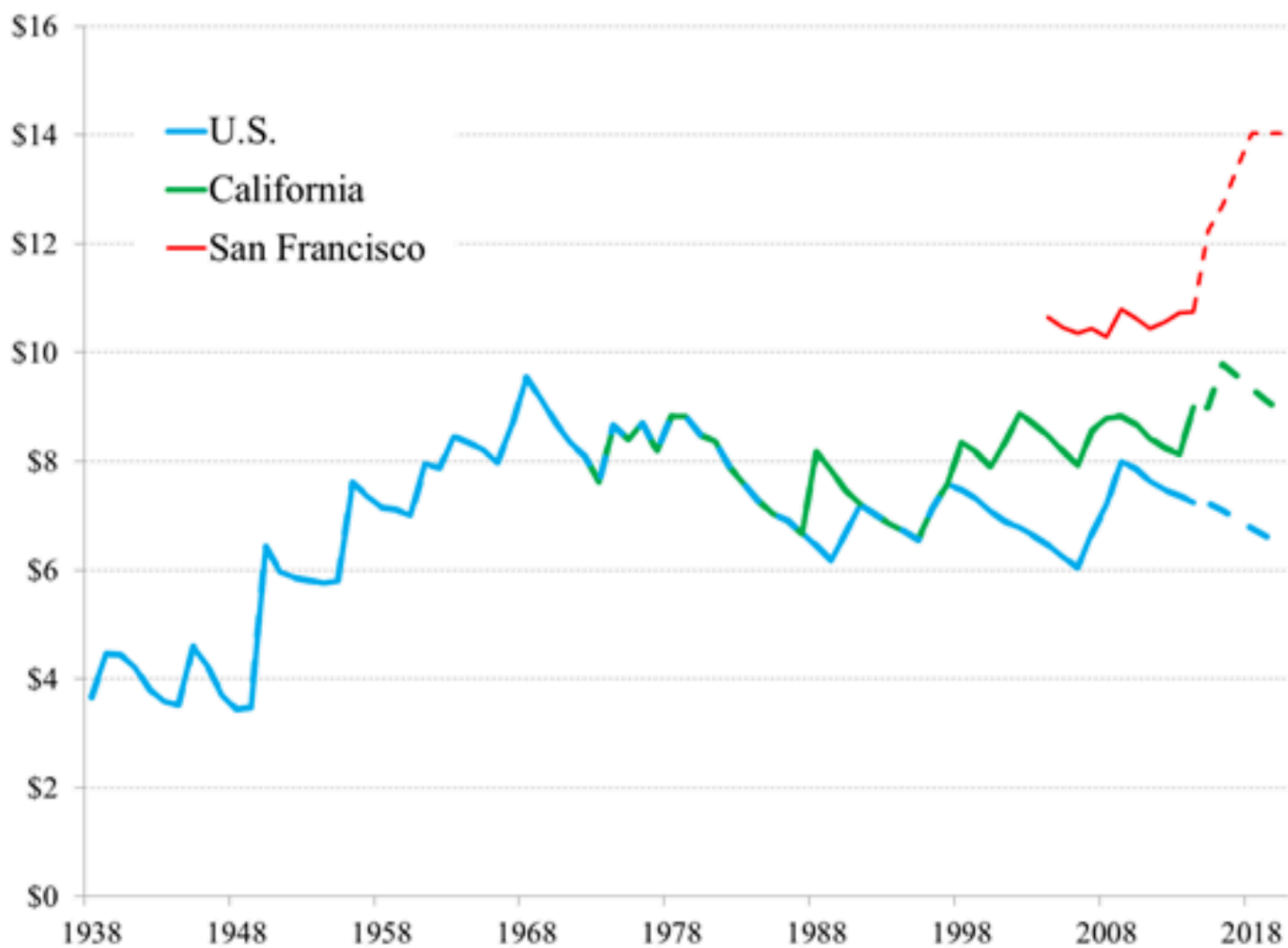


The evolution of the minimum wage

- Federal min. wage introduced in US in 1933; now equal to 7.25\$/h = lower in real terms than in 1960
- Northern and Western States tend to have min. wages $>$ fed. min.
- Different history and evolution of labor market across countries

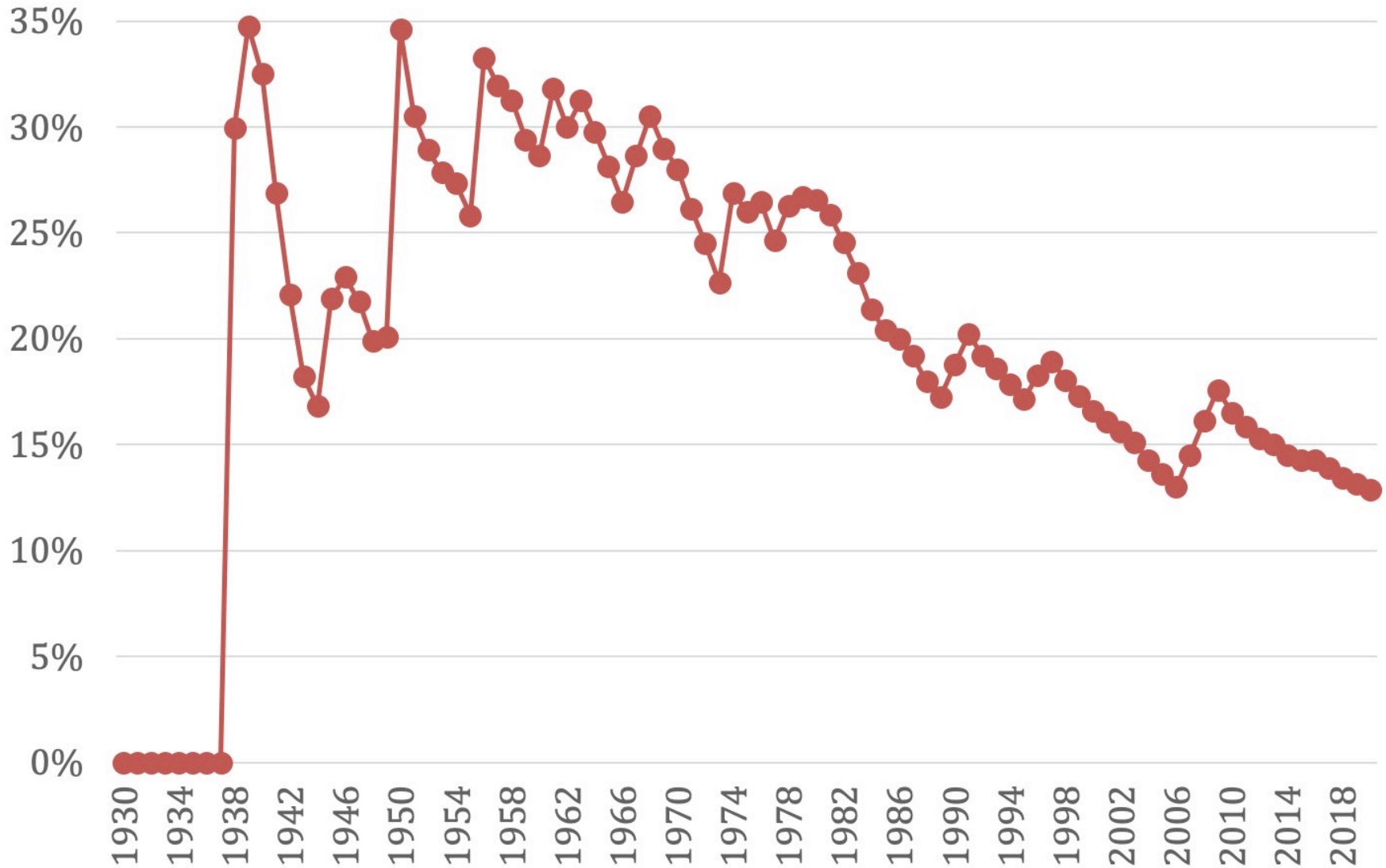
Minimum wages across countries

- In France, min. wage introduced in 1950; now equal to 9.5 euro/h
- Introduced in UK in 1999
- Introduced in Germany in 2015 (8.84 euros per hour)
- No government set min. wage in Nordic countries, but binding salary scales negotiated by unions and employers
- Denmark = 15 dollars/h

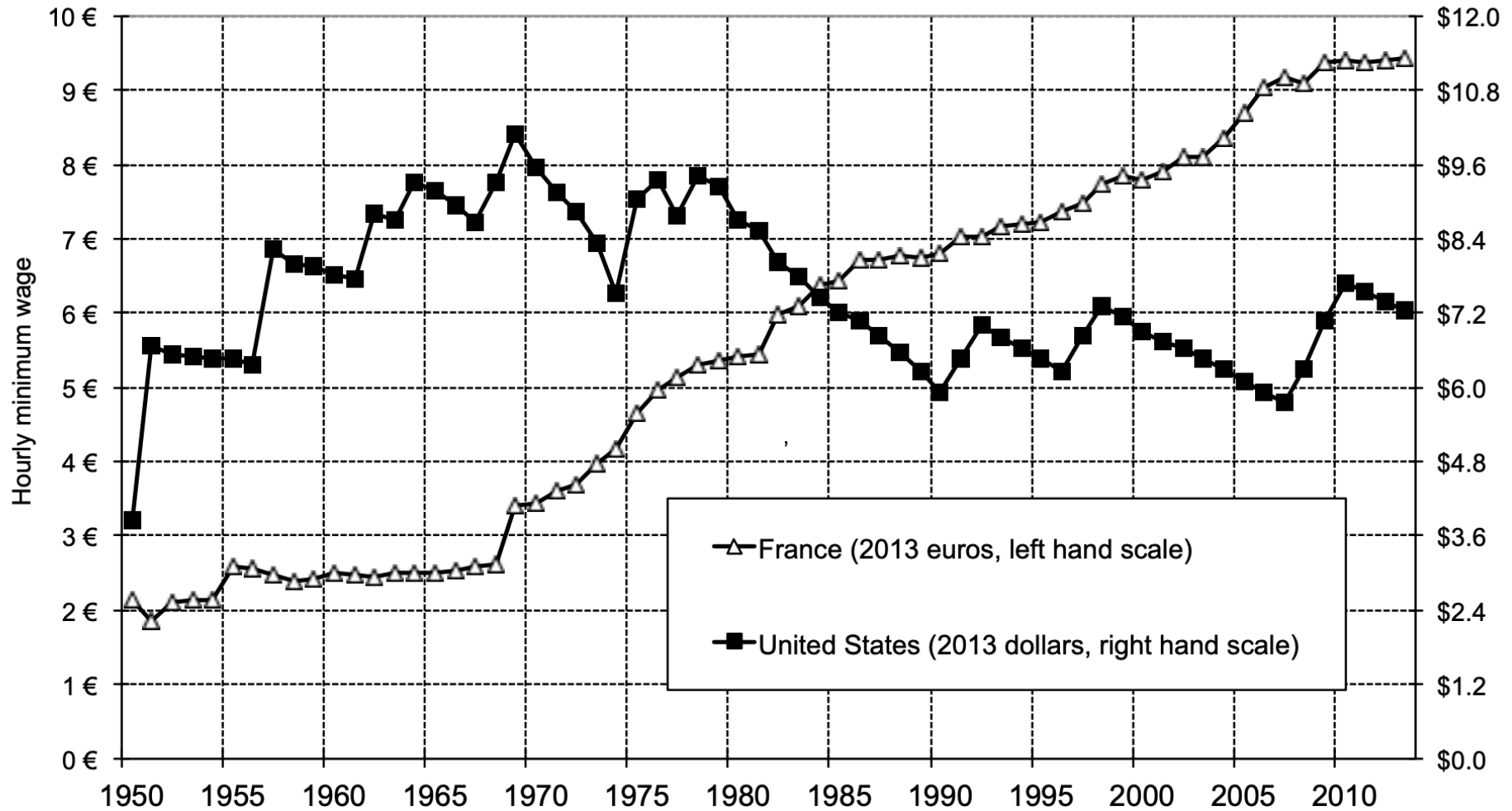


Note: minimum wage in constant 2014\$. Source: Montialoux and Reich (2016)

Annual federal minimum wage in the US, as a % of the average national income per worker

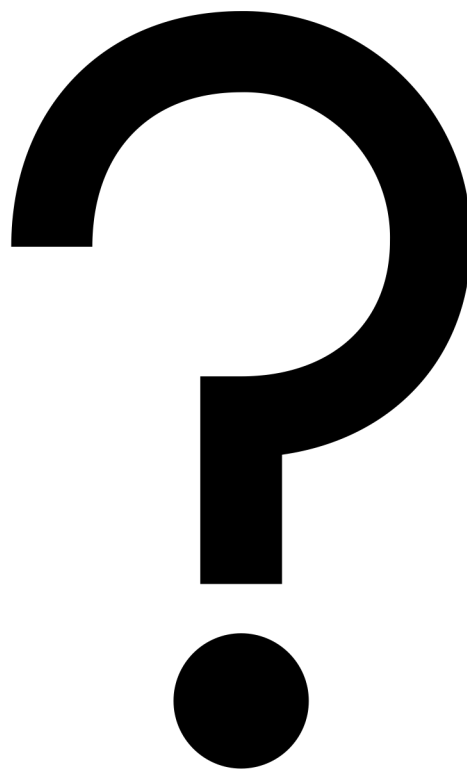


Minimum wage in France and the U.S., 1950-2013



Expressed in 2013 purchasing power, the hourly minimum wage rose from \$3.8 to \$7.3 between 1950 and 2013 in the U.S., and from €2.1 to €9.4 in France. Sources and series: see piketty.pse.ens.fr/capital21c.

How does minimum wages impact inequality?



How does minimum wages impact inequality?

- Minimum wage reduces lower tail inequality (DiNardo, Fortin and Lemieux 1996; Autor et al. 2016)
- Decline in the real value of the minimum wage explains 30-40% of the rise in P10/P50 wage inequality in the 1980s
- Effect due to spillovers: minimum wage must have raised the wages of workers earning above the minimum

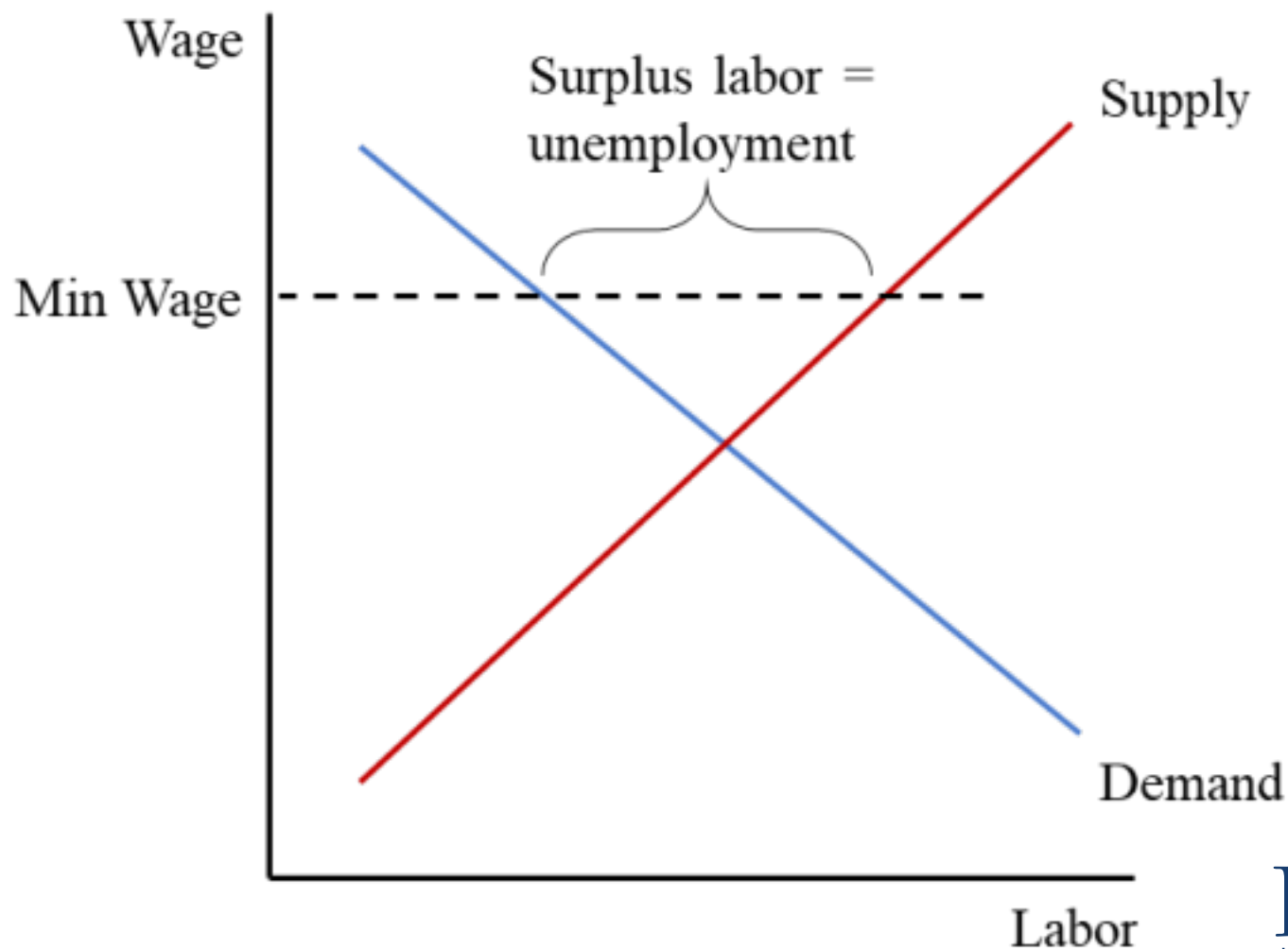
Kahoot! Effect on employment

- How does a minimum wage affect employment and incomes?

Effect of minimum wage on employment

- Conventional supply and demand analysis suggests negative effect on employment
- However, in a number of controlled experiments (State minimum wage hikes), show little effect found on employment

Econ 101 on minimum wage



Challenges to Econ 101

- If workers are currently paid *below* their marginal product → you can raise the minimum wage with no or positive employment effects
 - Why would that be the case?
- What if highly productive workers are currently not supplying their labor? → you can raise the minimum wage with no or positive employment effects

Teaching the Minimum Wage in Econ 101 in Light of the New Economics of the Minimum Wage

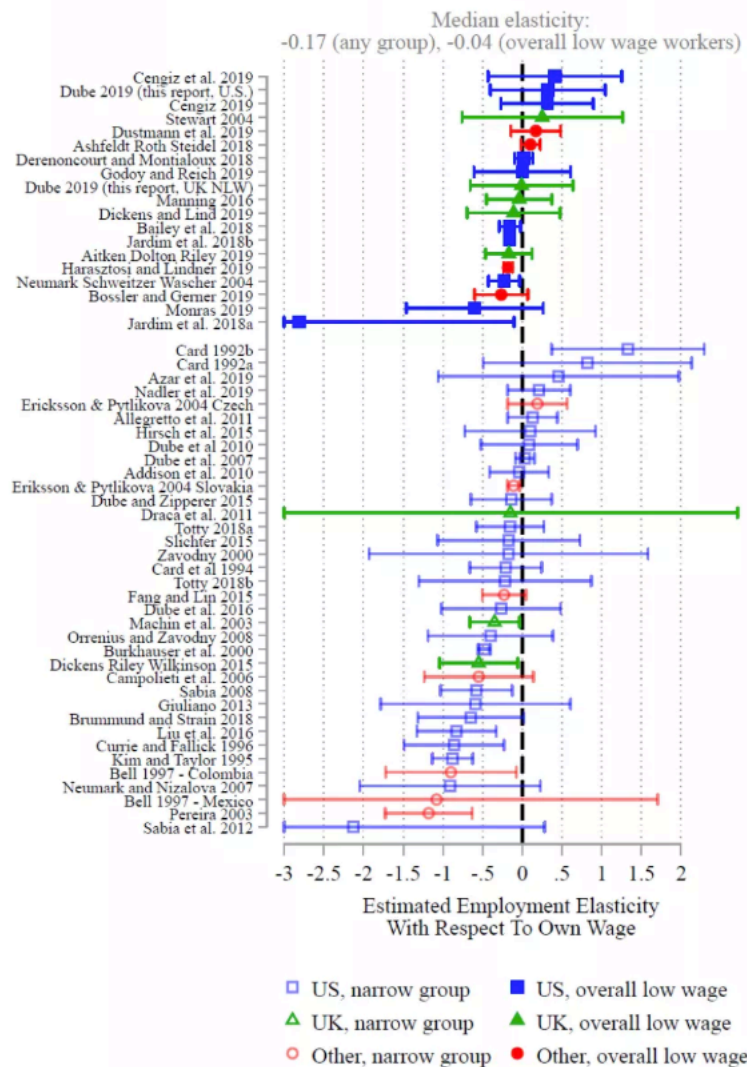
Alan B. Krueger

Abstract: The author argues that the recent controversy over the effect of the minimum wage on employment offers an opportunity for teaching introductory economics. Research findings on the minimum wage could be used to motivate alternative models of the labor market, such as monopsony and search models, and to teach students how economists test hypotheses with data.

Key words: minimum wage, monopsony, natural experiment

JEL codes: J3, A2

Chart 4.B: Own-wage employment elasticities from the minimum wage literature



Arindrajit Dube, University of Massachusetts Amherst, National Bureau of Economic Research and IZA Institute of Labor Economics

The economic debate over the minimum wage, explained

There's still disagreement. But it looks like in many cases, pay raises swamp any lost jobs.

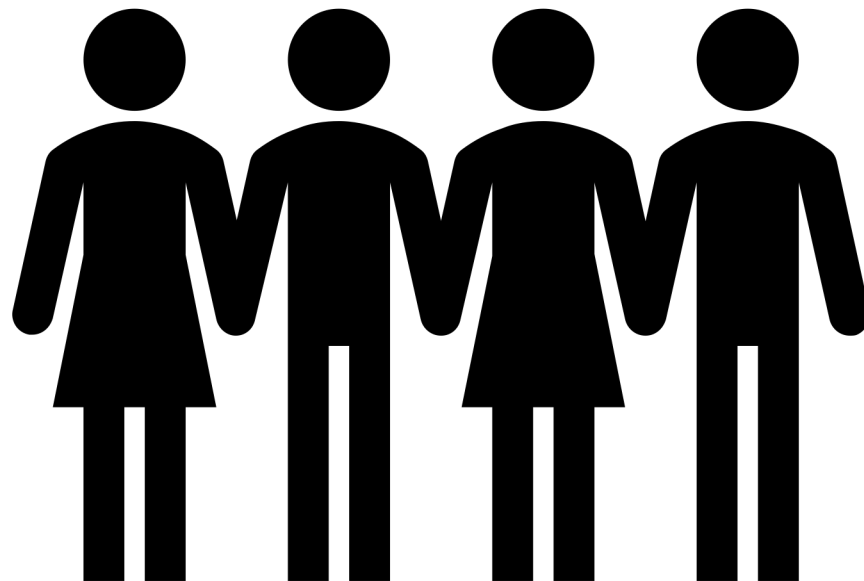
By Dylan Matthews | [@dylanmatt](#) | dylan@vox.com | Nov 20, 2019, 8:00am EST

“The median study looking at a broad group of low-wage workers estimates an “elasticity” of -0.04; that is, a 25-percent increase in average wages for a given group due to a minimum wage increase should lead to a 1 percent decline in employment for that group. That’s a really small effect, and one that suggests the benefits of a modest minimum wage hike should swamp the costs.”

Remember the context when setting min. wages

- Minimum wage effects are a matter of degree:
 - – If high low-wage payroll tax & poor training system for low- skill workers, then cost of high minimum wages can be large
 - – If min wage low (such as US today), raising it can actually raise employment by raising labor supply (Card and Krueger 1994)
 - – The right level also depends on the tax system and the education system

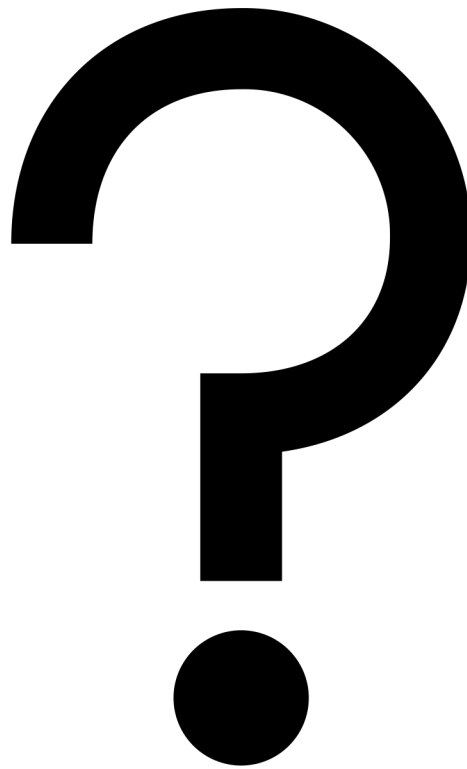
Unions



Unions

- Big decline in unionization in advanced economies
- But with different trends: US vs. Canada
- Strong correlation btw & union and % of top 10% income share

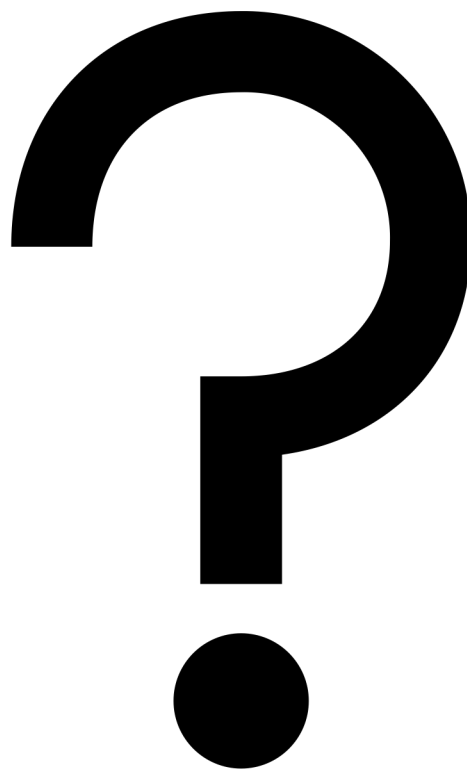
How do unions work?



How do unions work?

- Very differently across countries:
- Scandinavia: Unions set floor wages which are specific to occupation but covers essentially the whole workforce (Sweden enacts the bargaining agreements as law)
 - Flexible and powerful
- US: Unions limited to individual firms (low power) and set the entire wage scale (not just floor)
 - Inflexible and not powerful

How does a good union work?



How does a good union work?

- A good union tries to extract economic rents from employees (i.e. pays close attention to the bottom-line) but never asks for more than what is viable in the long/short run

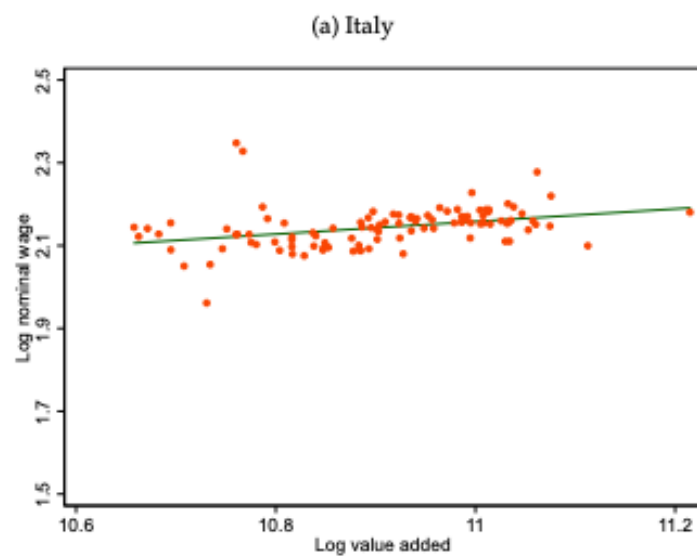


SAS opfordrer alle ansatte til at gå ned i løn

Corona-krisen har foreløbig ført til, at direktionen er gået 20 procent ned i løn.



Figure 4: Nominal wage and value added



(b) Germany

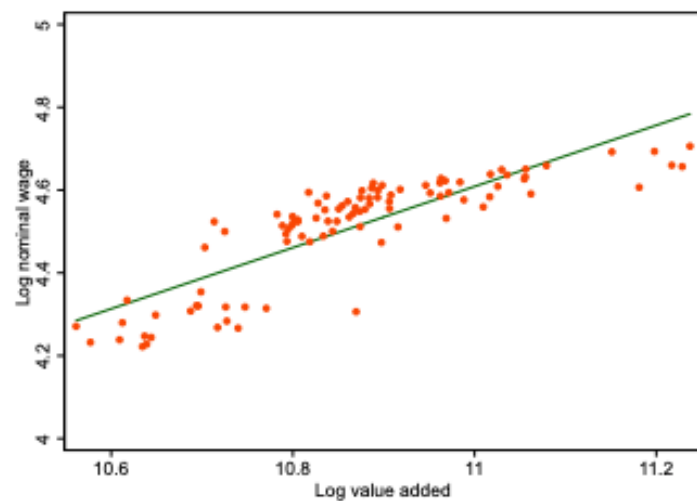
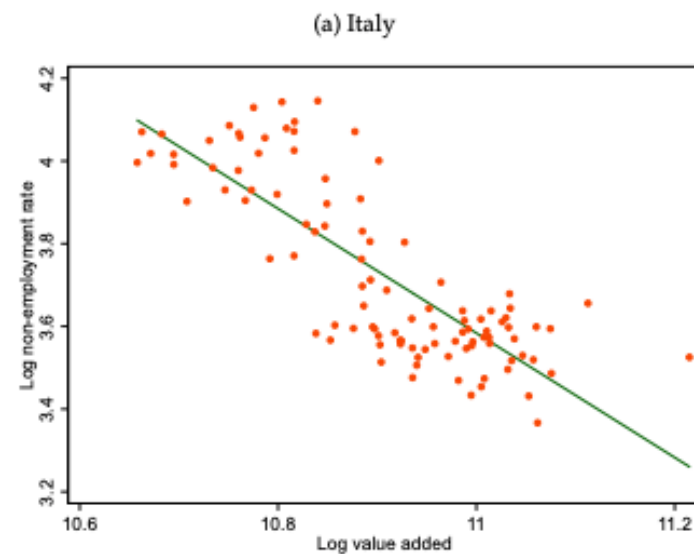
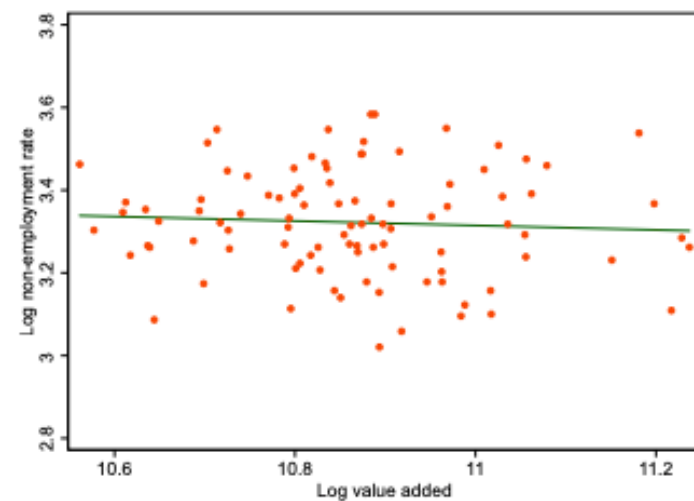


Figure 6: Non-employment and value added



(b) Germany



A Film by STEVEN BOGNAR and JULIA REICHERT

AMERICAN FACTORY

美国工厂





Fuyao exec challenges
'American Factory'
scene translation
regarding unionization



BUSINESS | Aug 20, 2019

By **Thomas Gnau**, Staff Writer

Filmmakers stand by the accuracy of the subtitled translations.

Fired 'American Factory' Workers Successfully Fought Back



Lisette Voytko Forbes Staff

[Business](#)

Breaking News Reporter

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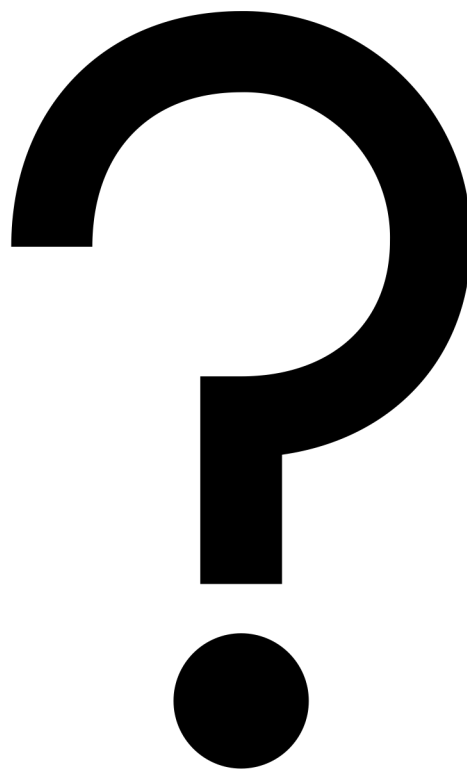
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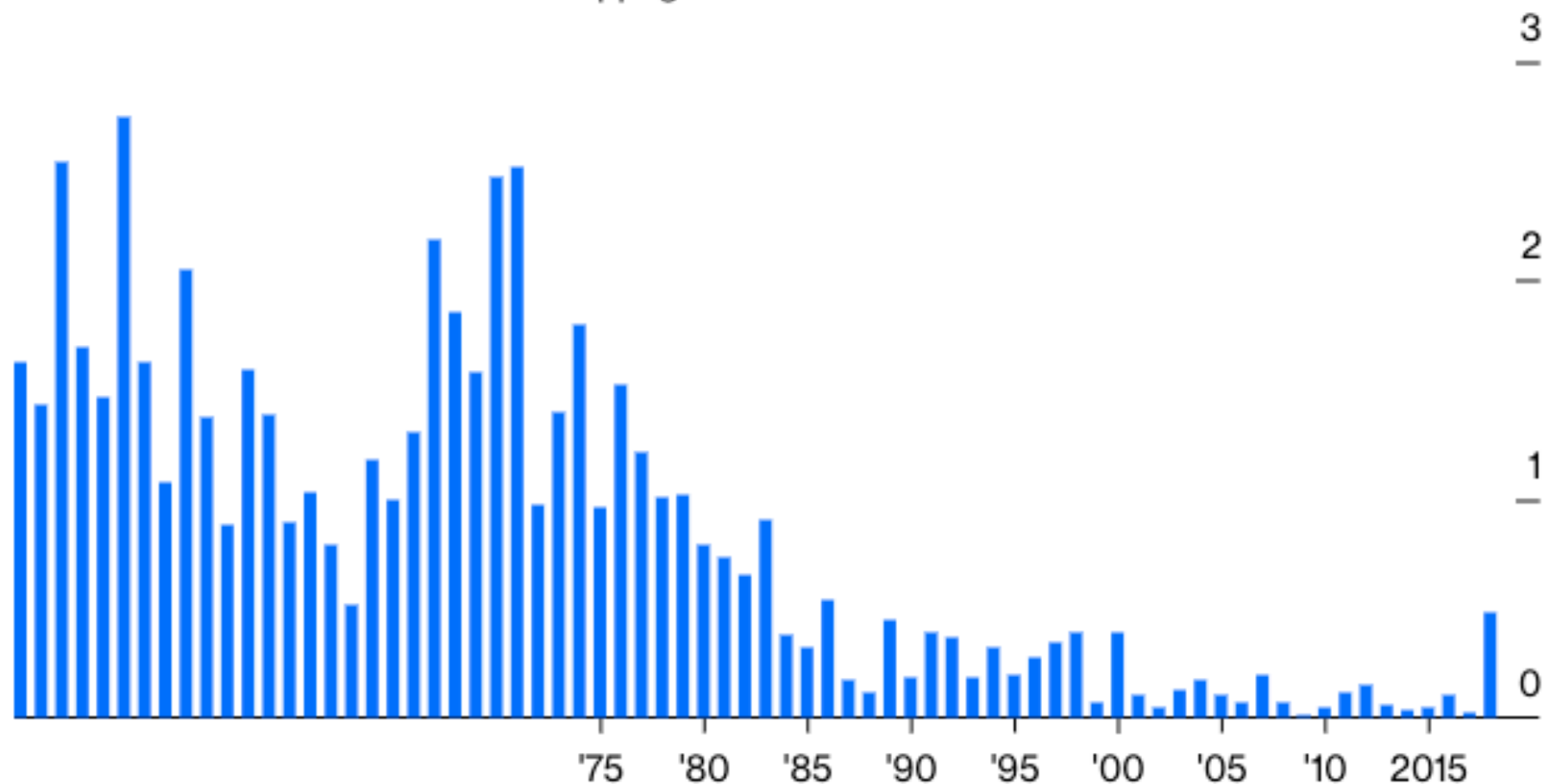
Jill Lamantia, left, and Fuyao chairman Cao Dewang, right. STEVEN BOGNAR AND BLOOMBERG

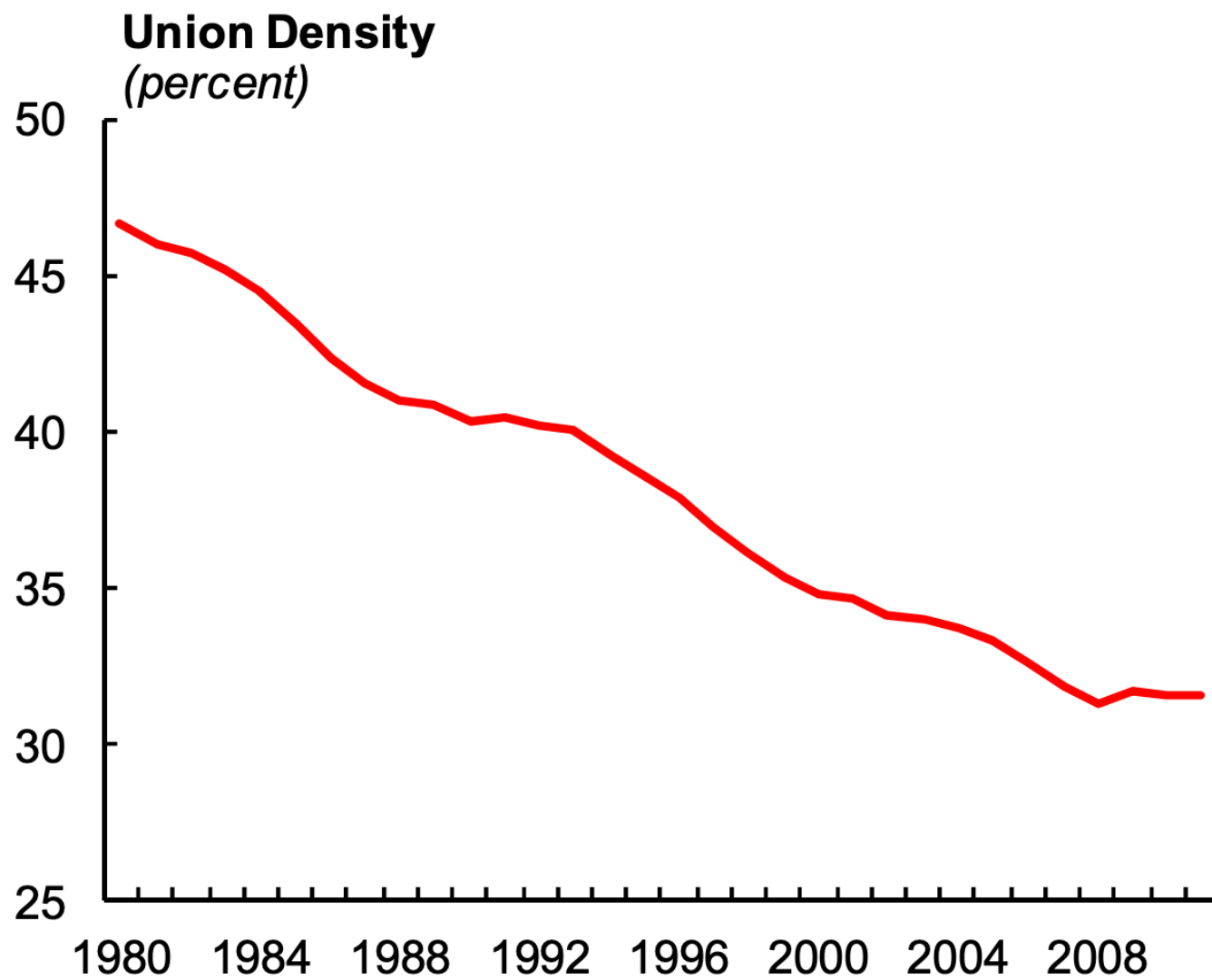
What are the advantageous/disadvantageous of union bargaining versus minimum wages? Kahoot!



U.S. Workers Are Striking Like It's the 1980s

■ Millions of workers involved in stoppages

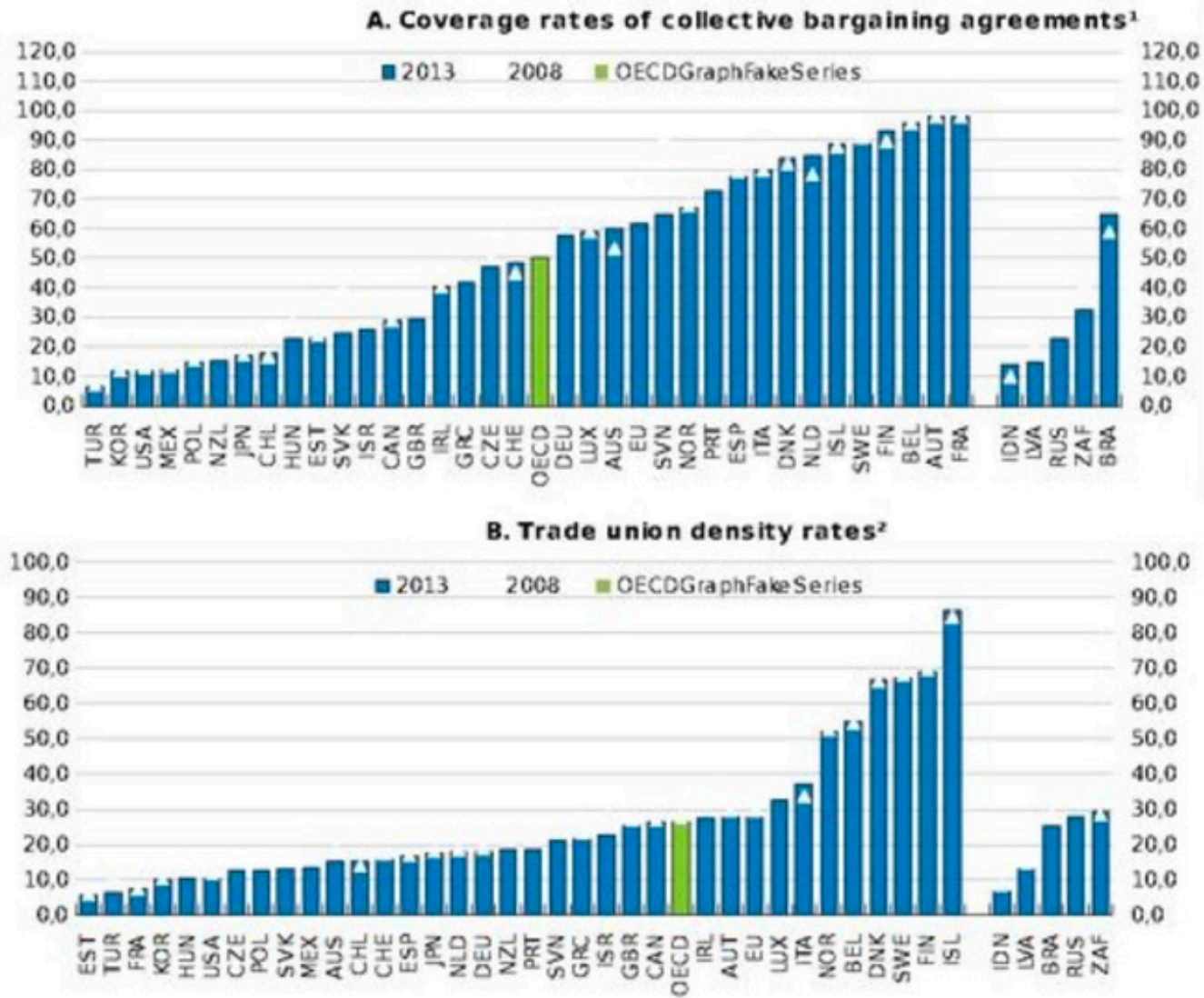


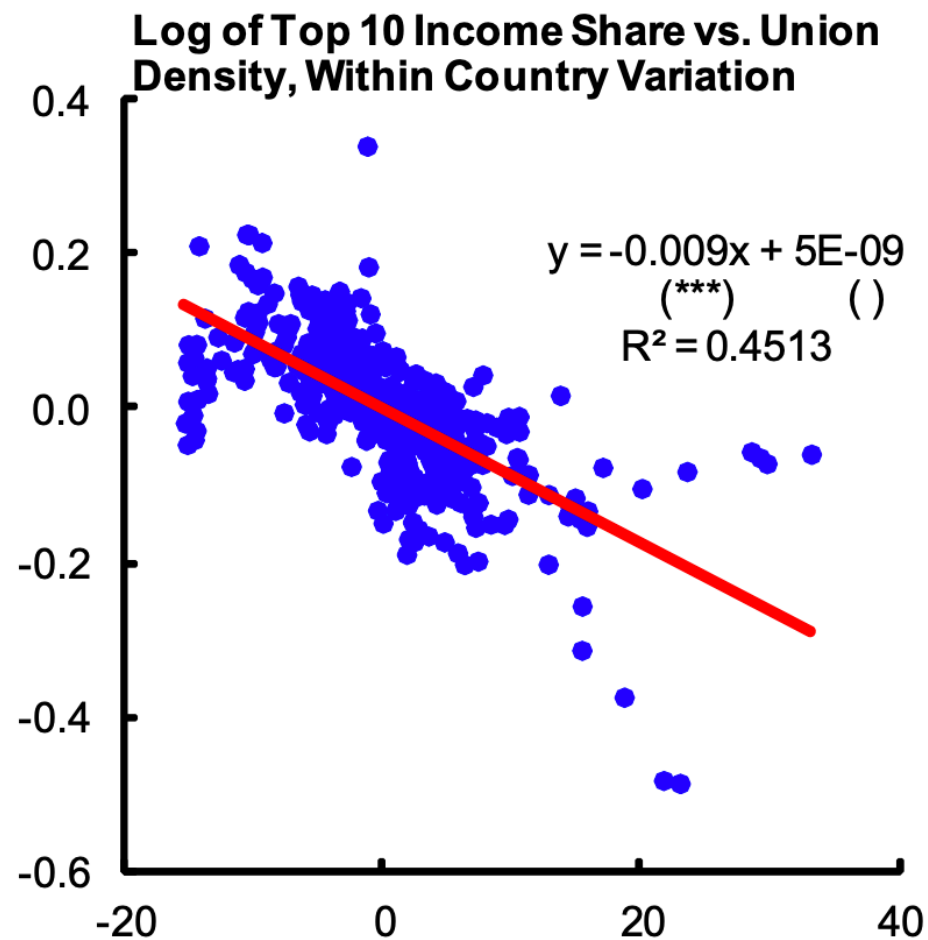
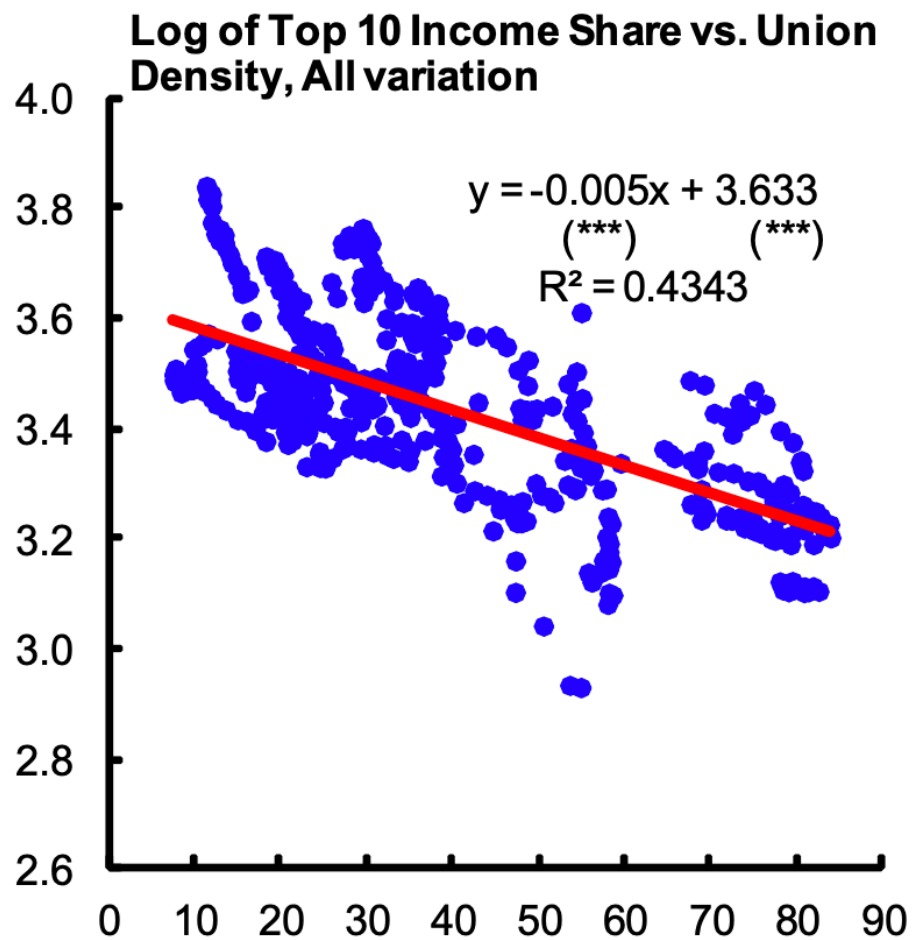


Source: Jaumotte and Buitron (2015)

Figure 4.14. Coverage rates of collective bargaining agreements and trade union density rates

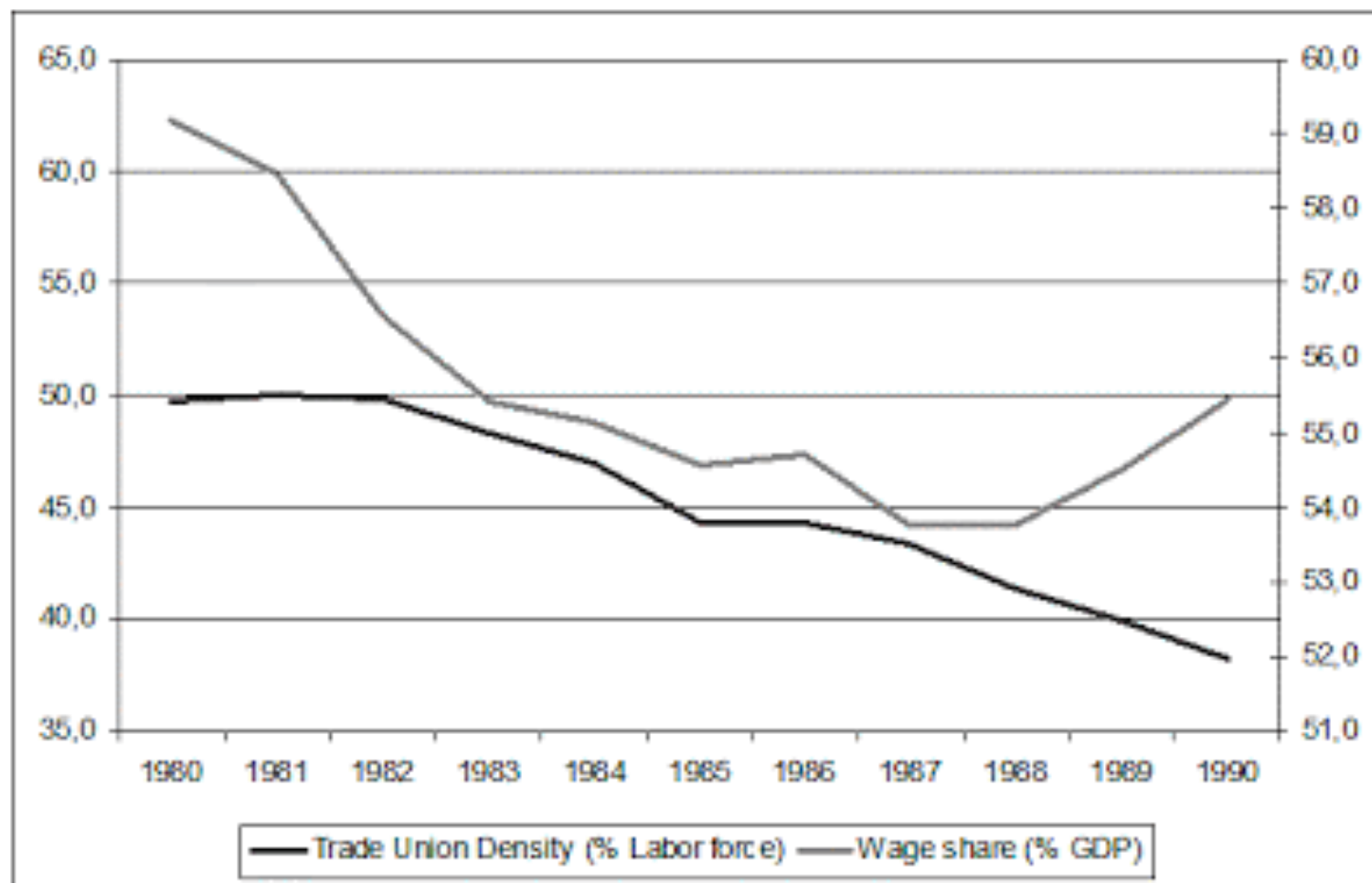
Percentage



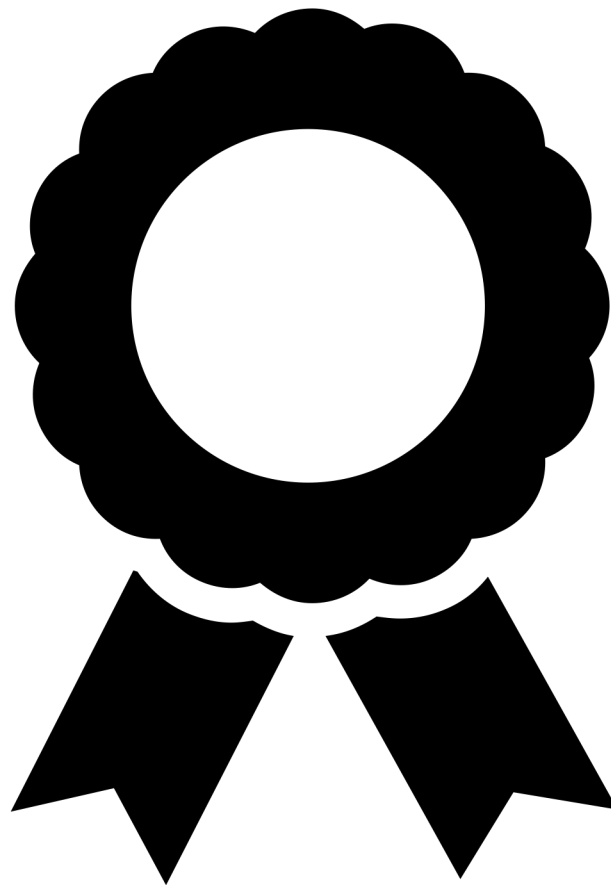


Source: Jaumotte and Buitron (2015)

Margaret Thatcher's Battle for Britain



Market power



Market power

- Market power: deviation from perfect competition pricing
- Monopoly: producer sets the price of what they sell:
 - Ex: Monsanto = sole supplier of GMO soybeans and corn
 - Ex: Internet access = local monopolies of cable companies
 - In these cases, price $>$ marginal cost

Table 1

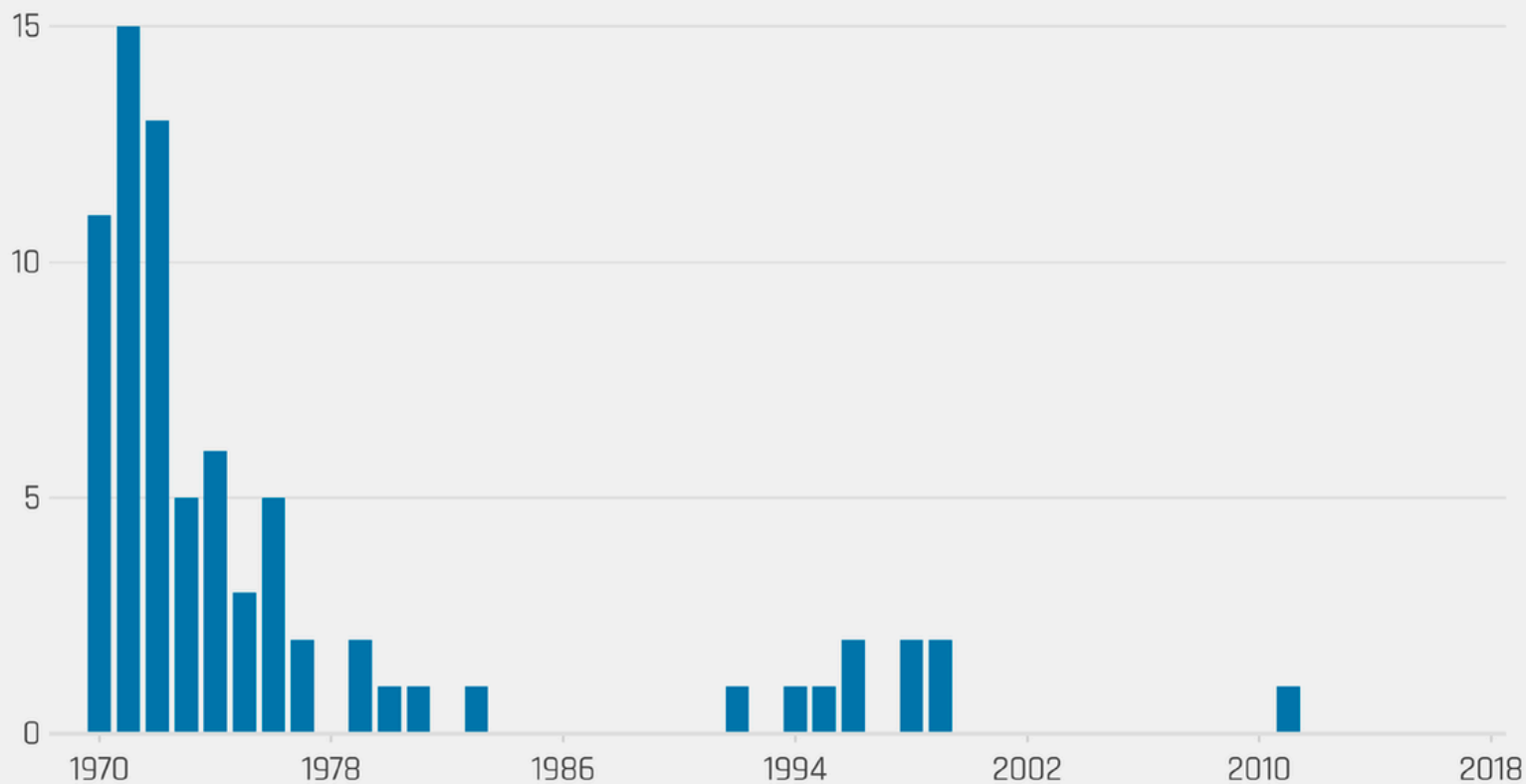
**Percentage Point Change in Revenue Share Earned
by 50 Largest Firms, 1997-2007**

Industry	
Transportation and Warehousing	12.0
Retail Trade	7.6
Finance and Insurance	7.4
Real Estate Rental and Leasing	6.6
Utilities	5.6
Wholesale Trade	4.6
Educational Services	2.7
Accommodation and Food Services	2.6
Professional, Scientific and Technical Services	2.1
Administrative/Support	0.9
Other Services, Non-Public Admin	-1.5
Arts, Entertainment and Recreation	-2.3
Health Care and Social Assistance	-3.7

Source: Furman and Orszag (2015)

The decline of anti-monopoly enforcement in the United States

U.S. Department of Justice, 1970-2016



Source: "Workload Statistics," available at <https://www.justice.gov/atr/division-operations> [last accessed May 23, 2019].



The New York Times

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Opinion

It's Time to Break Up Facebook

By Chris Hughes

May 9, 2019

Monopsony

- Monopsony: purchasers set the price of what they buy:
 - Ex: Walmart = main purchaser of products for retail
 - Ex: fast-food chains = main employer in small towns
 - Consequences on labor market: $\text{wage} < \text{marginal product}$
- Can explain worsening of inequality
 - Strong rationale for min. wage (protect low-wage workers from lack of negotiating power)

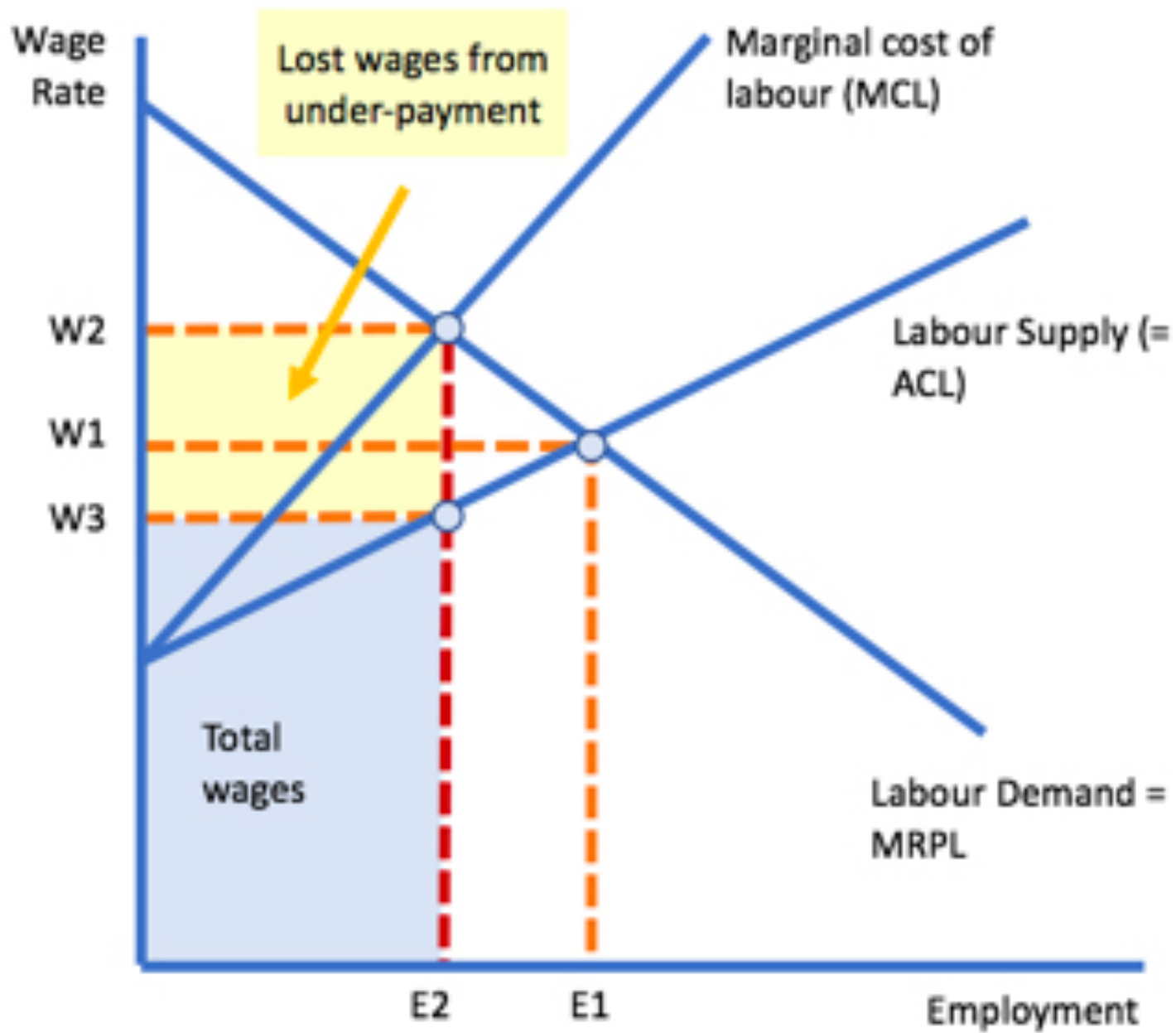
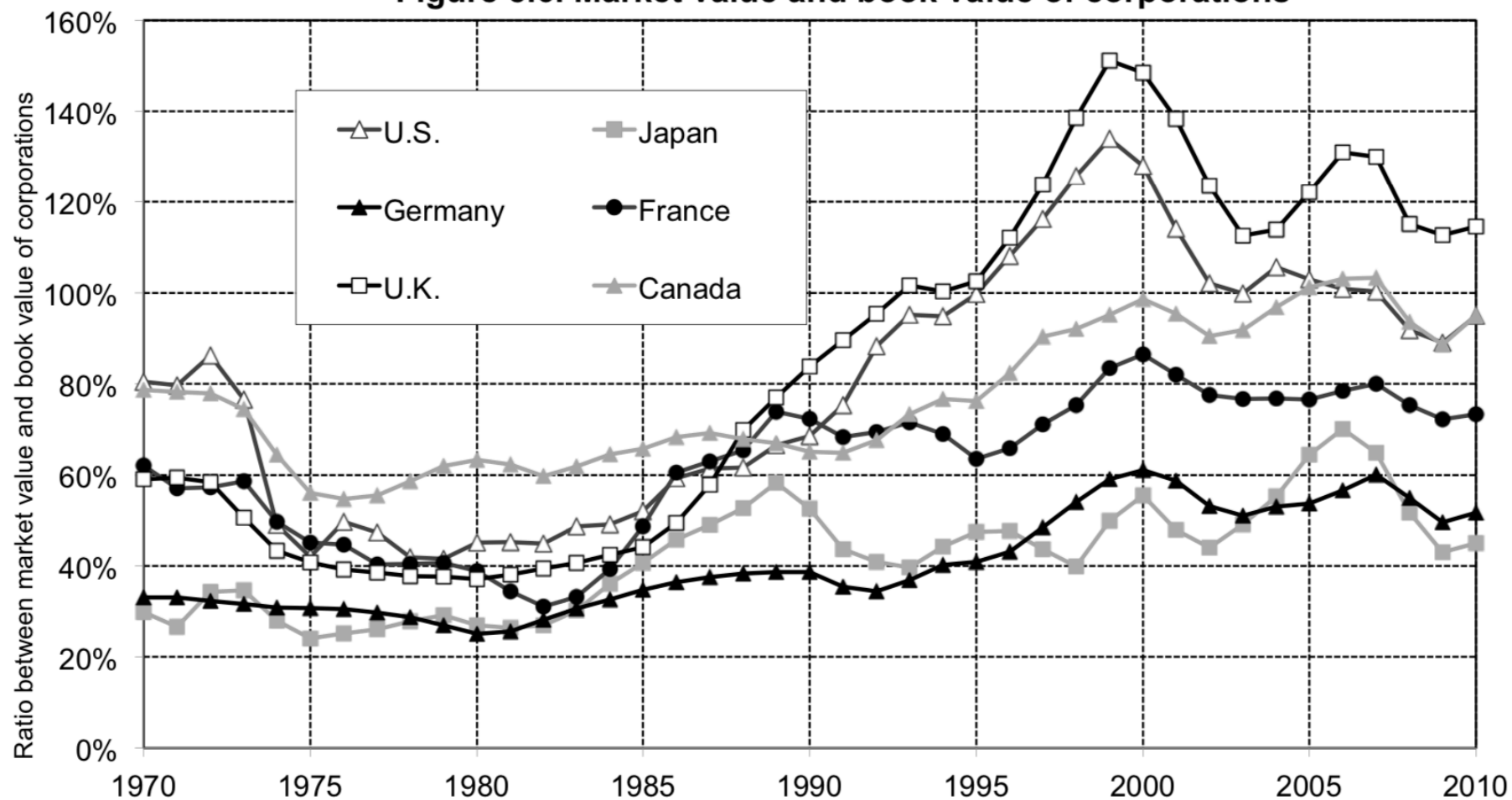


Figure 5.6. Market value and book value of corporations



Tobin's Q (i.e. the ratio between market value and book value of corporations) has risen in rich countries since the 1970s-1980s. Sources and series: see piketty.pse.ens.fr/capital21c.

Policy implications

- Market power largely determined by political decisions → antitrust laws, laws on revolving door & lobbying, campaign finance laws
- Minimum wage: key local policy issue
- Unions work very differently across countries – some with greater success than others
- Changes in labor law and contract law can empower workers to take action against employers and to assert their interests

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