

## **Extended Abstract:** “Inequality, Labor Share, and Wage Contracts.”

Since the mid-1970s Germany and other developed countries have experienced an increasing income inequality (Card, Heining and Kline, 2013; Lemieux, 2008) and a decreasing share of output paid as labor compensation (Karabarbounis and Neiman, 2014; Elsby, Hobijn and Şahin, 2013). Figure 1 plots these trends for Germany in the past four decades. Various economic theories have been put forward in order to explain these shifts: substitution of capital for labor, globalization, economic dynamism, unionization, minimum wage. This paper suggests an additional frame of analysis: the evolving nature of labor contracting.

In order to test this hypothesis, I construct a proxy for the propensity of a labor contract to be updated using the Sample of Integrated Labor Market Biographies (SIAB), a two percent random sample of labor market histories for German workers from 1975-2009 constructed from administrative records and distributed by the German Federal Employment Agency. These data contain the exact beginning and ending date of each employment spell. In a typical ongoing employment relationship these are the first and last day of the year; however, a small portion of ongoing employment relationships contain a mid-year reregistration. Further, the year-on-year pay change for an employee who experiences a reregistration more closely matches that of a worker who experiences a job-to-job transition than one who experiences neither reregistration nor mobility: the distribution for movers and reregistrants is higher on average and more positively skewed.

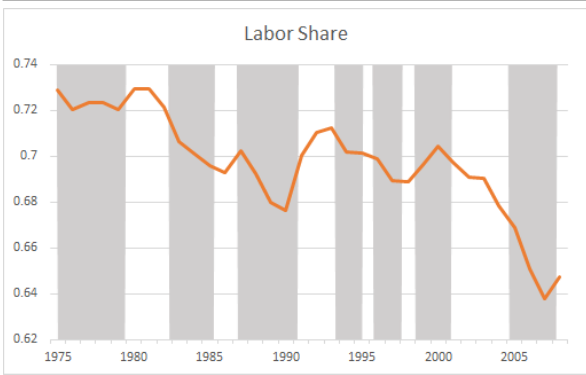
I further document that the share of ongoing employment spells which experience a reregistration has increased since 1975 (Figure 2) while probability of job loss and job-to-job transition remain relatively stable. Further the premium associated with reregistration has also remained relatively stable. Finally, I show that an increase in the propensity for reregistration within an industry predicts an increase in both upper and lower tail inequality, controlling for changes in the job finding and losing rates within the same industry.<sup>1</sup> I also show that, increase in the propensity for reregistration within an industry predicts an decrease in labor share, controlling for changes in the job finding and losing rates within the same industry.

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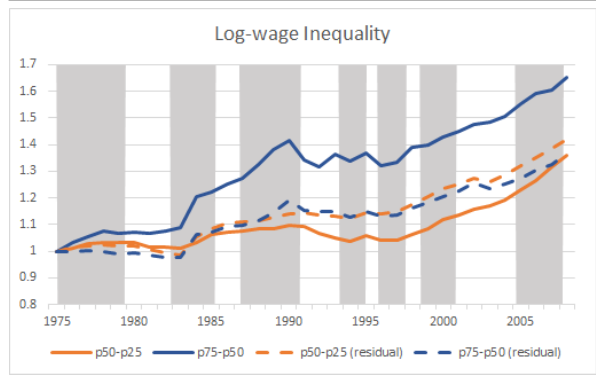
<sup>1</sup>Note, the SIAB data are top-censored at the social security limit. Following Card, Heining and Kline (2013) and Dustmann, Ludsteck and Schnberg (2009) I impute censored wages using a series of Tobit fit separately by gender, year, age range, and education level. I then consider the residual wage dispersion which is not accounted for by age, schooling, sex, industry or occupation. The results hold when restricting the sample to workers with apprenticeship training, which constitute about 60 percent of the sample and for whom typically less than 10 percent of observations are censored.

I consider these trends in the context of an on-the-job search model with heterogeneous wage contracts. In particular, I consider a model in which firms select between posting a non-negotiable wage contract, as in Burdett and Mortensen (1998), and posting a renegotiable wage contract that updates to reflect the worker's evolving outside options, as in Postel-Vinay and Robin (2002). When posting a vacancy featuring a renegotiable contract is comparatively costly only the more productive firms renegotiate (Doniger, 2014). I show that in the context of this model, a secular shift toward employment contracts with upwardly-renegotiable wages predicts an increase in inequality and a decrease in labor share. The remainder of this project aims to structurally estimate the change in contracting costs necessary to account for the observed trends in reregistration, labor share, and inequality. I also aim to address how these costs are modulated by contemporaneous changes in institutional features, particularly social insurance and minimum wages.

Figure 1: Trending Inequality and Labor Share in Germany (1975–2008)

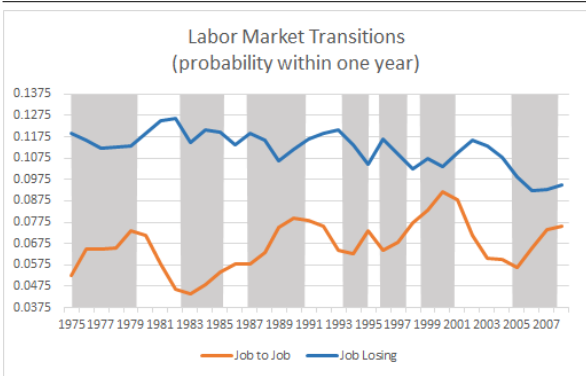


Source: EU-KLEMS, OECD and author's calculations. Recession dates are taken from the OECD and are were downloaded from FRED.

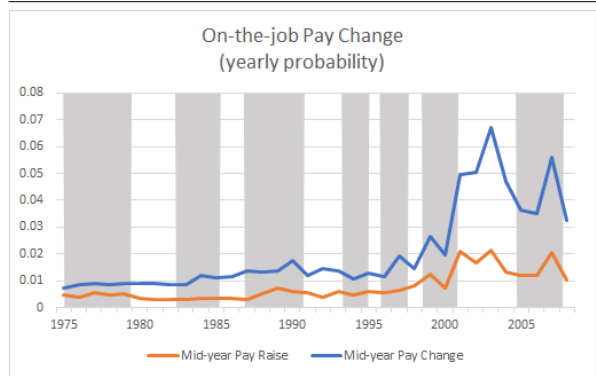


Source: SIAB and author's calculations. Trends in residual inequality display only the rise in inequality not accounted for by age (five year bins), education, sex, industry, and occupation. Note: the SIAB data contains a trend break in 1984 when bonuses began being counted in yearly income.

Figure 2: Job Mobility and Changes in Compensation (1975–2008)



Source: SIAB and author's calculations. Transitions are counted as job-to-job if fewer than 15 days elapse between employment spells.



Source: SIAB and author's calculations. Note: the SIAB data contains a trend break in 1984 when bonuses began being counted in yearly income.

## References

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