Wage setting in Australia: Discussion of Joe Isaac’s AER article

Jeff Borland
University of Melbourne
Presentation to Fair Work Commission Workplace Relations Lecture, August 8 2018
1] Overview

• 1] What is the question about wage growth?
• 2] What is the timing of the divergence between growth in real wages and labour productivity?
• 3] Can institutions explain the divergence?
• 4] Are there other potential explanations?
2] What is the question about wage growth?

<table>
<thead>
<tr>
<th>Time horizon</th>
<th>Wage measure</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Nominal wages</td>
</tr>
<tr>
<td>Short-run</td>
<td></td>
</tr>
<tr>
<td>Long-run</td>
<td></td>
</tr>
</tbody>
</table>
2] What is the question about wage growth?

<table>
<thead>
<tr>
<th>Time horizon</th>
<th>Wage measure</th>
<th>Nominal wages</th>
<th>Real wages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Short-run</td>
<td></td>
<td>Why is wage growth so low in recent years?</td>
<td></td>
</tr>
<tr>
<td>Long-run</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
• Slow nominal wage growth in recent years
2] What is the question about wage growth?

<table>
<thead>
<tr>
<th>Time horizon</th>
<th>Wage measure</th>
<th>Nominal wages</th>
<th>Real wages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Short-run</td>
<td>Why is wage growth so low in recent years?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long-run</td>
<td>Joe Isaac’s topic: ‘Since 1983, both real AWE and AWOTE have risen well short of labour productivity increases.’ (p.175)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
• Real wages and labour productivity since the 1980s

Index = 100 in May 1982
3] The wage-productivity gap: What is the timing?

• Will use ‘Labour share’ approach to represent relation between hourly wage rate and labour productivity

• Labour share of income =
  
  \(\frac{\text{Real hourly compensation}}{\text{Labour productivity}}\)

• My main point: Important to be precise about timing
3] The wage-productivity gap: What is the timing?

Index = 100 in 1965-66

Lprody  Real product wage
3] The wage-productivity gap: What is the timing?

Labour share of income, 1965-66 to 2016-17
3] The wage-productivity gap: What is the timing?

Labour share of income, 1965-66 to 2016-17
3] The wage-productivity gap: What is the timing?

Labour share of income, 1965-66 to 2016-17
3] The wage-productivity gap: What is the timing?

Labour share of income, 1965-66 to 2016-17
2] The wage-productivity gap: What is the timing?

<table>
<thead>
<tr>
<th>Percent growth per annum</th>
<th>Labour productivity</th>
<th>Real hourly compensation (GDP deflator)</th>
<th>Real hourly compensation (CPI)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969-70 to 1982-83</td>
<td>2.1</td>
<td>3.2</td>
<td>3.4</td>
</tr>
<tr>
<td>1982-83 to 1988-89</td>
<td>0.9</td>
<td>-1.6</td>
<td>-1.7</td>
</tr>
<tr>
<td>1996-97 to 2016-17</td>
<td>1.55</td>
<td>1.2</td>
<td>1.4</td>
</tr>
</tbody>
</table>
3] The wage-productivity gap: What is the timing?

![Graph showing the wage-productivity gap](image-url)
3] The wage-productivity gap: What is the timing?
The impact of institutions on wage growth

- How might institutions matter?
- 1] Union (direct) effects on wages
- 2] The wage-setting process – Eg., pattern bargaining
- 3] The role of third parties in wage setting
- 4] Intra-firm norms for wage setting
4] The impact of institutions on wage growth

• (1) Unions?
4] The impact of institutions on wage growth

• (2) Pattern bargaining?

[Graph showing scatter plots comparing rate of increase in AWOTE (Full-time males) to rate of change in employment (4-quarter) for Mining states and Non-mining states in Early 1980s and Mid 2000s.]
5] Are there other explanations?

- Decline in quality-adjusted equipment prices
- International trade and offshoring
5] Are there other explanations?

• Decline in quality-adjusted equipment prices
• International trade and offshoring
• Theory of superstar firms:
• ‘If globalization or technological changes advantage the most productive firms in each industry, product market concentration will rise as industries become increasingly dominated by superstar firms with high profits and a low share of labor in firm value-added and sales. As the importance of superstar firms increases, the aggregate labor share will tend to fall.’ (Autor et al., 2017, Abstract)
• But in Australia:
• ‘The balance of evidence suggests that competitive pressure in Australia has not waned since the early 2000s... over the whole economy, concentration and profits appear remarkably steady.’ (Minifie et al., 2017, p.27)
References

• Autor, D., D. Dorn, L. Katz, C. Patterson and J. Van Reenen (2017), ‘The fall of the labor share and the rise of superstar firms’, mimeo.
