Union wage formation and (un)employment

8 Concluding remarks

Abstract

This chapter summarizes and concludes the study. Furthermore, it discusses some policy implications and offers some suggestions for further research.

1 Summary and conclusions

The results of the study can be summarized as follows. Chapter 2 shows that trade unions are economic agents whose behaviour can be integrated in economic theory to explain wage formation and employment. The impact of trade unions on unemployment is less clear. This issue is taken up in the next chapter.

Chapter 3 presents an empirical model of union wage setting, employment and unemployment. The model is estimated with annual aggregate data for the Dutch private sector from 1965 until 1987. The results suggest that the increase of taxes and that of the discrepancy between consumer and producer prices (partially due to value added taxes) and the increase of benefits have caused an increase of the equilibrium unemployment rate in the Netherlands in this period.

Chapter 4 considers whether efficiency wage effects can explain unemployment. The efficiency wage theory argues that it may be profitable for the firm to pay more than the market clearing wage to increase the workers' productivity. A theoretical objection is that more complex contracts can be devised which provide incentives to workers without causing unemployment. There is some empirical evidence that high wages improve worker productivity; whether the effect is sufficiently strong and wide-spread to cause unemployment is questionable. Further, the chapter shows a new result with respect to the interaction between efficiency wage and insider-outsider effects. The insider-outsider theory argues that employed workers (insiders) have more market power than unemployed (outsiders). This market power enables the insiders to obtain wages above the market clearing level, while outsiders remain unemployed. The theoretical model shows that efficiency wage and insider-outsider effects reinforce one another if the insider has complete market power. Whether this result also holds in other situations remains to be assessed.

Chapter 5 presents an empirical application of the efficiency wage theory and the theory of union wage formation. The efficiency wage theory is used to explain wage drift, whereas the theory of union wage formation is used to explain contract wage changes. The estimates for the Netherlands (1972-1983) imply that there is an inverse relationship between contract wage changes and wage drift. In other words, wage drift reduces the impact of wage moderation by trade unions on employment.

The analysis of chapter 6 is also based on the theory of union wage formation. The central question is whether the probability for unemployed workers to get a job depends on the cause of their unemployment. Two possible causes of unemployment are distinguished. The first cause of unemployment is insider-outsider effects. In this situation the union does not care about unemployed. The second cause of unemployment is lack of human capital. This lack may be caused by the duration of unemployment. It appears that the probability for unemployed workers to get a job depends on the cause of their unemployment. Under monopoly unionism unprivileged workers (outsiders, untrained workers) are more likely to be hired if their unemployment was due to a lack of human capital than if the union does not care about them. Under efficient bargaining unprivileged workers prefer powerful unionism if their unemployment was due to a lack of human capital. If their unemployment is due to the fact that the union does not care about them, powerful unionism may hinder their employment.

Chapter 7 considers the empirical implications of insider-outsider effects on wages, employment and unemployment persistence. Furthermore, it provides a survey of empirical studies in this area. It appears that there is little evidence in favour of a lagged employment effect on the wage rate. It is clear that unemployment has a negative impact on wages. Long-term unemployment reduces wages as well, but perhaps at a lower rate than short-term unemployment. The insider-outsider and duration effects are not strong enough to cause full hysteresis.

2 Policy implications

The study has the following policy implications. The study of union wage formation, employment and unemployment of chapter 3 implies that pay-roll and income taxes, social security contributions, indirect taxes and benefits may increase equilibrium unemployment. It seems desirable to stabilize or decrease the tax burden, to reduce the number of workers on sick leave, etc. The analysis of contract wage changes and wage drift in chapter 5 suggests that the impact of wage moderation by trade unions is diminished by wage drift. It further indicates that wage control measures by the government are not very effective. The theoretical models in chapter 6 suggest that human capital matters in wage formation. The policy implication of the models is that a subsidy of training costs may enhance employment of untrained workers such as long-term unemployed. It is even better, but also more difficult, to prevent losses of human capital by eliminating long-term unemployment.

3 Suggestions for further research

The study is concluded by offering some suggestions for further research. The study of the determinants of equilibrium unemployment in chapter 3 concentrates on imperfect competition in the labour market. If the determination of wages and prices is considered as 'a battle of the mark-ups' (see Layard and Nickell (1986)), the analysis can be improved by including imperfect competition in the product market. An empirical study along these lines is provided by Nickell and Kong (1992) for 14 two-digit industrial sectors in Britain. Chapter 4 shows that insider-outsider and efficiency wage effects reinforce one another if the insider has complete market power. It would be interesting to generalize this result in case the insider has no complete market power. The empirical study of contract wage changes and wage drift in chapter 5 could be repeated on a larger data set, for example on panel data of several industries. Chapter 6 presents a static analysis of the impact of human capital or duration effects on wage formation and employment. The dynamic impact of human capital or duration effects on unemployment can be investigated by integrating wage formation theory and matching theory in a single model. The survey in chapter 7 shows that insider-outsider effects may cause unemployment persistence. An interesting subject for further research is whether wages and employment adjust symmetrically in booms and slumps.