Policy Brief

The Political Economy of Income Distribution: Industry level evidence from Austria

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Year: 2016 No. PB13-2016

GREENWICH POLITICAL ECONOMY RESEARCH CENTRE (GPERC)

Abstract

Austria has experienced one of the steepest declines in the wage share in comparison to other European countries with a fall from 66.2% in its peak in 1978 to 52.8% in 2007 before the recession, and as of 2015 with a level of 55.5% it is 10.6%-point below its peak. We find that union density has had the strongest impact in Austria, explaining 85.1 percent of the average decline of the wage share (based on our estimations for the period of during 1996-2007). We also find a sizeable negative effect of intermediate imports (international outsourcing) and some negative effect of outward FDI as well as financialisation measured by household debt and financial payments (interest and dividend payments and income as a ratio to total resources of nonfinancial corporations). The negative impact of technology (measured by ICT capital intensity as a ratio to value added in the sector) is relatively smaller and not always significant. Results indicate that migration has had a very strong positive effect on the wage share. Increasing imports of capital and consumption goods have also had sizeable positive effects. The strategy of an equality-led development requires labour market policies aiming at pre-distribution as well as redistribution. These include strengthening the bargaining power of labour, ensuring higher collective bargaining coverage, enforcing gender equality, introducing and enforcing pay ratios to moderate wage inequality, and restoring the progressivity of the tax system.

Keywords: Austria, wage share, income distribution, labour unions, bargaining

JEL codes: E25, F66, J50

Acknowledgements: This policy brief is based on Guschanski and Onaran, The Political Economy of Income Distribution: Industry Level Evidence from Austria, supported by a research grant from the Vienna Chamber of Labour. The usual disclaimers apply.

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The political economy of income distribution: industry level evidence from Austria

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There has been a significant decline in the share of wages in GDP in both developed and developing countries since the 1980s. In a recent research paper (Guschanski and Onaran, 2016), we analyse the determinants of the wage share (adjusted labour compensation as a ratio to value added) for Austria and selected OECD countries.

We use sector-level data of nine OECD countries (Austria, Denmark, France, Germany, Italy, Spain, Sweden, the UK, the US) for the period of 1970 to 2011, which allows us to trace the developments in the wage share across high and low skilled sectors and within manufacturing and service industries.

Our findings lend strong support to the political economy approach to functional income distribution. The fall in the wage share is significantly driven by various variables reflecting the bargaining power of labour, in particular union density.

We find that globalisation had a strong impact on the wage share in all countries. In Austria, Germany, and to a lesser extent in the UK, the effect is due to outward FDI and intermediate import penetration which reflects the impact of international outsourcing practices.

Financialisation had the most pronounced effects in Austria, the UK and the US, while it appears to be also relevant in Germany.

We also find some evidence of a negative effect of personal income inequality on the wage share in Austria, Germany, the UK and the US.

Interestingly the impact of technological change, which has been the usual suspect of mainstream explanations of rising inequality, does not have a robust effect when other variables are controlled for. Whenever there is some evidence of a negative impact in some specifications in Austria, Italy, and the US, the effect is smaller than that of union density, globalisation or financialisation.

Austria has experienced one of the steepest declines in the wage share in comparison to other European countries with a fall from 66.2% in its peak in 1978 to 52.8% in 2007 before the recession, and as of 2015 with a level of 55.5% it is 10.6%-point below its peak. We find that union density has had the strongest impact in Austria, explaining 85.1 percent of the average decline of the wage share (based on our estimations for the period of during 1996-2007). We also find a sizeable negative effect of intermediate imports (international outsourcing) and some negative effect of outward FDI as well as financialization measured by household debt and financial payments (interest and dividend payments and income as a ratio to total resources of nonfinancial corporations). The negative impact of technology (measured by ICT capital intensity as a ratio to value added in the sector) is relatively smaller and not always significant. Results indicate that migration has had a very strong positive effect on the wage share. Increasing imports of capital and consumption goods have also had sizeable positive effects.

To sum up, our research shows that inequality in Austria increased because of the increased fallback options of capital related to increased capital mobility in the form of outsourcing, FDI and financialisation and declining fallback options of labour related to the decline in collective bargaining power rather than an unavoidable outcome of technological change. Labour mobility (the share of migrant workers in total employment) does not have a negative impact on the share of wages in total income even in the service sectors predominantly hiring low-skilled labour.

The fall in the wage share has been a deliberate outcome of policies which have led to the vicious circle of rising inequality, financialisation, chronically low demand, a slowdown in investment and growth both in Austria and Europe (Tori and Onaran, 2015; Onaran and Obst, 2015).

Negative effects of openness or global integration are not an unavoidable destiny, rather an outcome of the current domestic and international policies. Openness and regional integration can also be managed in a way to benefit both the richer and poorer partners if trade and investment flows are designed as part of an egalitarian and growth-oriented international economic policy. In an alternative economy where the balance of power shifts in favour of labour and unions have a strong voice, if migrants come to work, it is possible to set the terms and conditions under which they work by the local workforce. In the European context, progressive movements have more common ground than they currently exploit. There is scope for international cooperation, in case the coordination failure can be overcome.

The empirical evidence shows that to break this vicious circle we need alternative economic policies based on a coordinated policy mix of equality-led development and public investment. Onaran and Obst (2015) provide strong empirical evidence to reject the myth that we cannot have pro-labour policies in the age of globalisation. Austria as part of Europe as a whole is strong enough to pursue an egalitarian, wage-led growth strategy and would benefit from a coordinated boost to the wage share. As such, Austria and other countries in Europe could, and should, take a step forward in terms of radically reversing the fall in the wage share globally.

The strategy of a wage-led development requires labour market policies aiming at pre-distribution as well as redistribution. These include strengthening the bargaining power of labour, ensuring higher collective bargaining coverage, enforcing gender equality, introducing and enforcing pay ratios to moderate wage inequality, and restoring the progressivity of the tax system. Furthermore, income distribution policies need to be embedded into a broader macroeconomic and industrial policy mix targeting equality, full employment, and ecological sustainability. This requires regulating finance and the corporate governance of corporations, taming capital mobility, and implementing a public investment programme centred on substantial public investment in green physical infrastructure in renewable energy, public transport and housing and social infrastructure in care, education, and health.

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