



4th World Conference on Business, Economics and Management, WCBEM

Wage share as a factor of income inequality in the context of the structure of national economy

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Abstract

This paper focuses on the quantitative examination of the wage share in the countries of the EU from 2008 to 2012, applying a division of national economy by three main sectors. The aim of the paper is to investigate the effect of employment structure and its changes, and the changes of the wage share inside the sectors on the aggregate wage share and its alterations during a short-term period. The conducted research showed that the levels of the weighted wage share, corresponding to the employment structure, were: the lowest – in agriculture, the highest – in the service sector. Furthermore, the shift of the aggregate wage share was mostly affected by the decline in the primary and secondary sectors, which was generally based on the decrease of employed people. The results also displayed that in several countries the wage shares declined because of the reduction of the wages and salaries rather than value-added.

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Peer-review under responsibility of Academic World Research and Education Center

Keywords: labour, income, wage share, employment, structure, national economy, sectors

1. Introduction

The world is slowly recovering from the recent crisis and prolonged recession, though economy and labour market are still far from sustainable positions. Nevertheless nowadays the world is also dealing with another major economic and social problem – inequality. There are three similar rates of economic imbalances: inequality of wealth, income and consumption. Income inequality is the most commonly used metric. The analysis of income inequality comprises studying disparities of income distribution among nations, as well as among social groups.

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Nowadays economists are more concerned about inequality within nations. A high response got Piketty's recent publication, where he argues that in every society three parts can be marked out in the income inequality: inequality in labour income; inequality in the ownership of capital and the income to which it gives rise; and the interaction between these two terms (Piketty, 2014). In economics there is such a factor as labour share, which is considered to be a highly informative macroeconomic factor to explore, when analysing income inequalities within and across countries.

In macroeconomics it is generally assumed that total value added is produced with two major input factors – capital and labour. Therefore, one part of value added is attributed to capital – capital share (it should be noted that in this case capital income includes corporate profit, net interest, rental income, and proprietor income), and another part is ascribed to labour input factor – labour share. The labour income share is considered to be a good indicator of the extent to which national income (or GDP, or gross value added) is distributed among capital owners and workers. Thus, the labour income share is defined as the share of GDP or value added, which is paid to workers.

The labour share is also frequently called the wage share; however, there is a difference. While labour share includes all compensation to employees, the wage share takes into account only wages and salaries paid to the employed people. To our concern, as wages and salaries represent a considerable part of labour income and, consequently, disposable income, it is particularly necessary to make assessment of wage share and its changes.

The invariability of the labour share has been named as a *stylized fact of growth* by David Ricardo (Krugger, 1999). However, nowadays, almost over the last three decades economists increasingly emphasize their attention to the widespread opinion of the decreasing labour as well as wage income share in the total value added (Gollin, 2002; Serres et al, 2002; Arpaia et al., 2009; Guerriero, 2012) in favour of capital share during a long- and mid-term period.

Moreover, nowadays economists are also concerned about the structure of national economy. In recent decades the structure of global and national economies has changed significantly. On the one hand, the dominant share of the tertiary sector becomes increasingly high, while share of the industrial sector continues to decrease. On the other hand, a necessity of more detailed structure of national economy appears in order to analyse the processes inside the sectors. The changes of national structure are reflected not only in the structure of GDP (or gross value-added), but in the structure of employment, too. As Stiglitz noted, structural transformation of national economy has a big effect on developing sustainable economic strategy (Stiglitz, 2011). Furthermore some researches argued that labour income share is highly correlated with the structure of value added of the national economy (Serres et al., 2002; Young, 2006).

Accordingly, this empirical paper focuses on the statistical examination of the wage share, as the factor of income distribution, across countries of the European Union (further, EU) from 2008 to 2012, applying a division of national economy by three main sectors. Consequently, the aim of the paper is to investigate the effect of employment structure and its changes, and the changes of the wage share inside the sectors on the aggregate wage share and its alterations during a short-term period. Methods applied – structure and dynamics analysis, cross-country statistical analysis, decomposition and variable-weights apportionment method.

2. Measurement of the wage share and its changes. Methodology

The labour income share can be calculated using the data from the national accounts. A widely used approach is to compute the labour income share as the share of employee compensation in GDP, while employee compensation incorporates the wages and salaries (in cash and in kind), all other bonuses and allowances, plus social contributions of the employer. Broadly speaking, the labour share measures the ratio of a total labour compensation to the gross domestic product. In this paper the authors used the wage share (*WS*) – the ratio of the wages and salaries (*W*) paid to employees to GDP or value added (*VA*). Accordingly, for the calculations of the wage share the following basic formula was used:

$$WS = \frac{W}{VA} \quad (1)$$

For almost two decades the debates about the labour share measurements and its improvements have been

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