



The Labour Income Share in the European Union





- “Labour income share” measures the ratio of total labour compensation to value added
- Synonyms: labour share, wage share
- functional income distribution
NOT personal income distribution





- Motivation
- Definition – measurement issues
- The facts : 1960-2006
- Drivers: theory
- Drivers: empirics
- Conclusions





- **Equity:**
LIS affects personal income distribution
- **Efficiency:**
If LIS above its equilibrium, and real wages not flexible enough downwards, then higher employment and output volatility and higher equilibrium unemployment
- **Macro-economic stability:**
LIS affects the different components of aggregate demand and the composition of the tax base





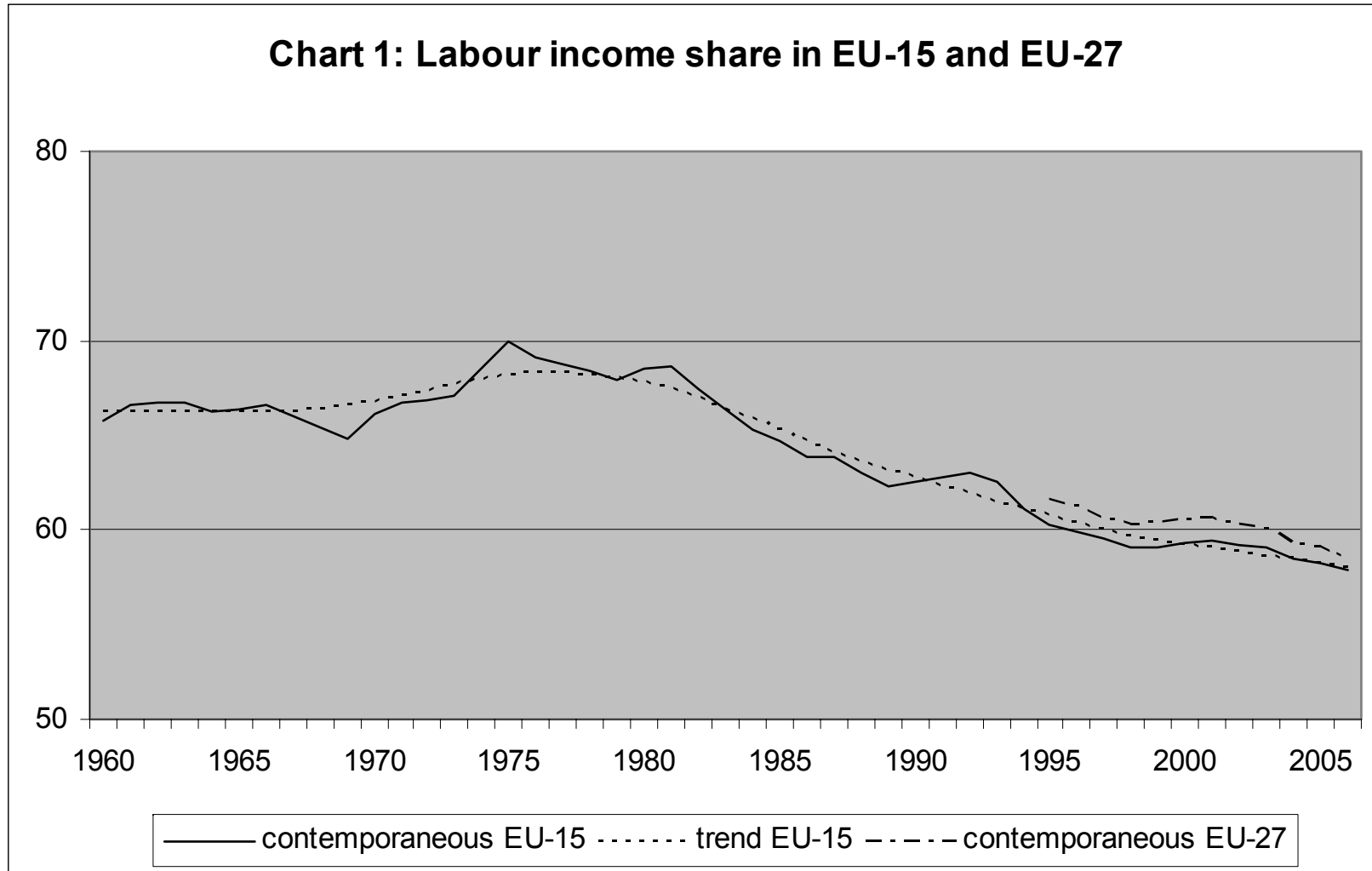
- LIS = total labour compensation divided by gross domestic product

- Measurement issues
 - wage rate of self-employed





Chart 1: Labour income share in EU-15 and EU-27



The labour income share in the EU, US and Japan: 1960-2006



Chart 1: Labour income share in EU-15 and EU-27

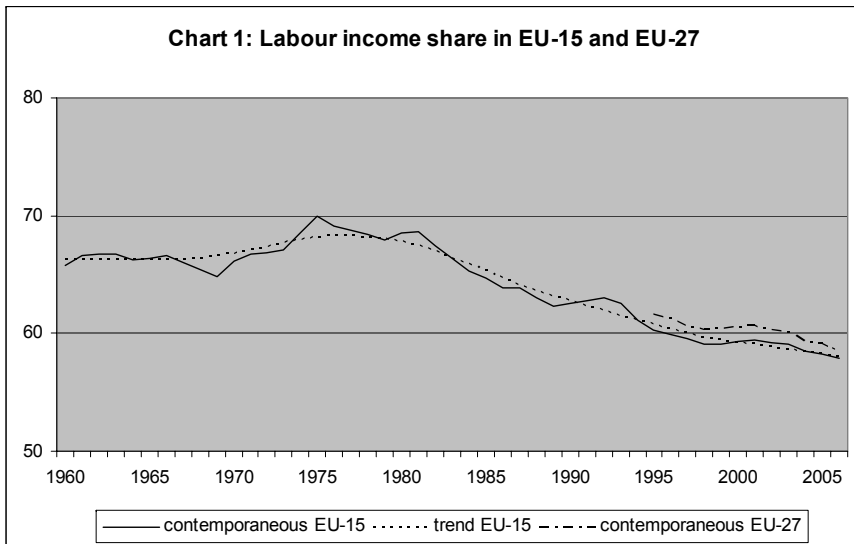


Chart 2: Labour income share in United States

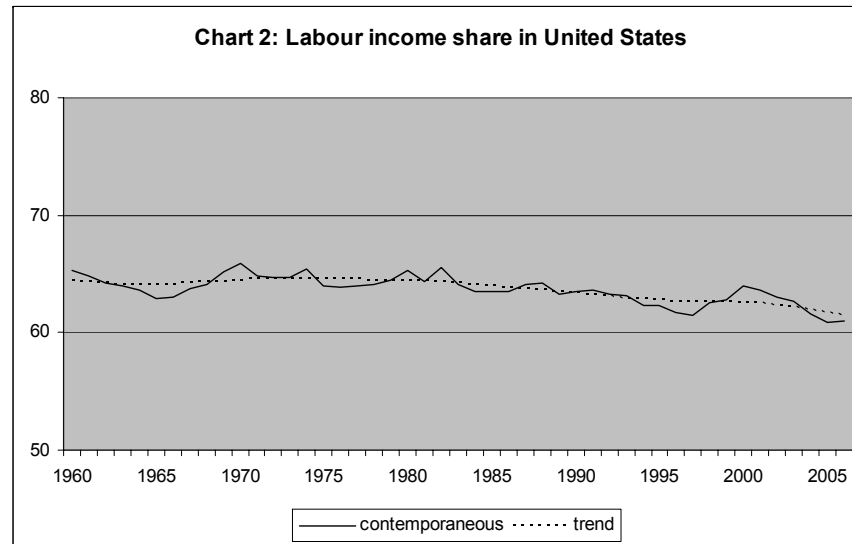
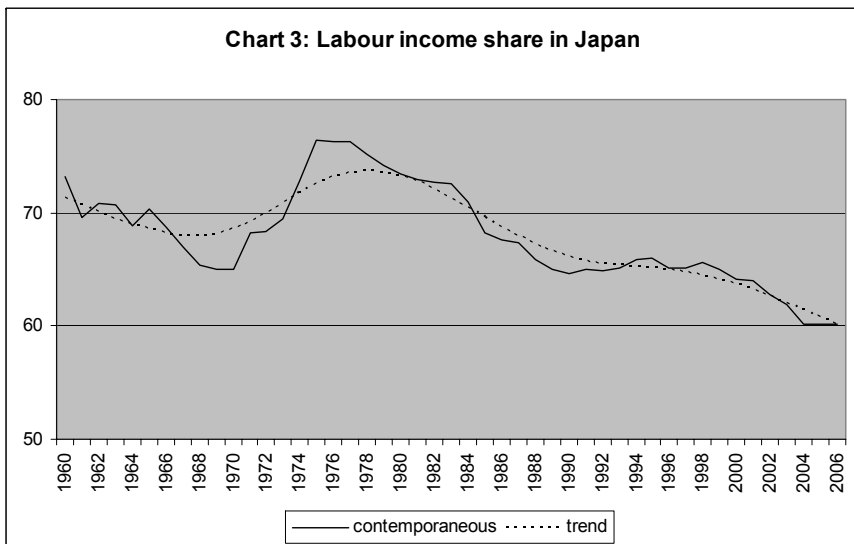


Chart 3: Labour income share in Japan





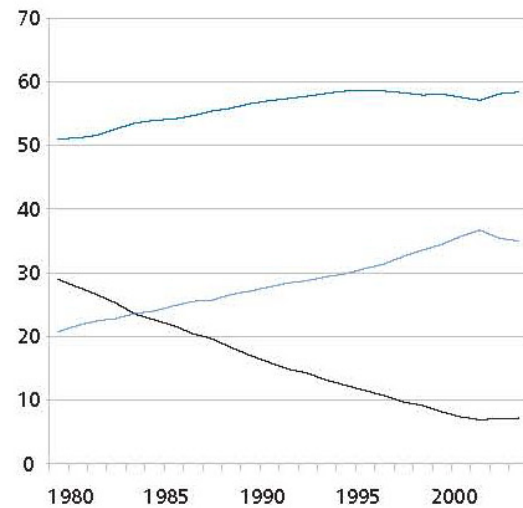
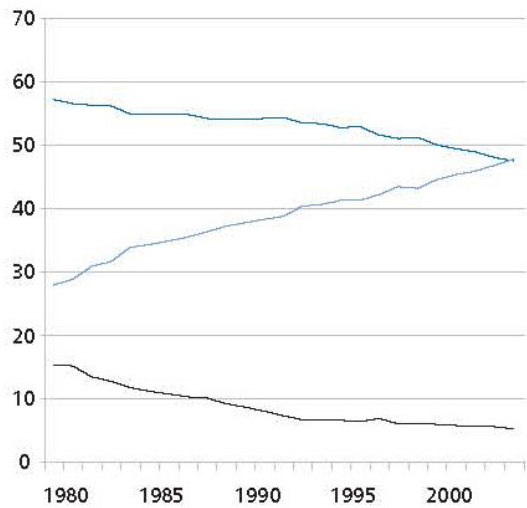
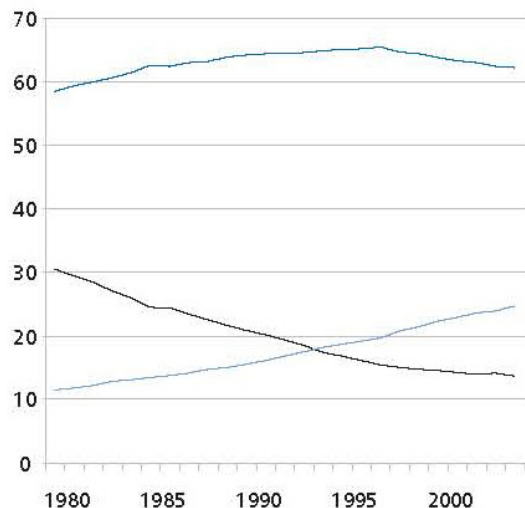
Share in total labour compensation

Chart 5: 10 Member States

Chart 6: The United States

Chart 7: Japan

— low-skilled — medium-skilled — high-skilled



Source: EU KLEMS database and own calculations.



- Production technology
- Institutions/policies
- Globalisation



- Elasticity of substitution between labour and capital
 - Unitary: constant labour income share
 - non-unitary:
 - relative factor endowments matters
 - order of magnitude ($<$ or >1)



- Empirical research indicates that new technologies substitute for unskilled labour and complement skilled workers
- Different degrees of substitution imply that changes in the capital intensities of the production process can have different effects on the income shares of the various skill types





- Imperfect competition in the product market creates rents, which are to be distributed between capital and labour as a function of their relative bargaining power



- In the case of a binding minimum wage, the wage will tend to be higher than the marginal productivity of labour, and labour will be able to extract a higher share from total revenues.
- The effect of active labour market policies depends to a large extent on the elasticity of substitution and on the effectiveness of these policies to allow workers to progress in their job and skill level





- traditional trade theory:
LIS will fall in case of further trade liberalisation if a country is capital-abundant
- globalisation adversely affects the bargaining position of labour
- outsourcing of activities





- A system of income share equations for low, medium, & high skilled workers
- Regressors per equation:
 - capital-to-labour ratio
 - ICT-intensity of production process
 - rents in goods market
 - bargaining power in labour market
 - active labour market policies
- Data:
 - Ameco
 - EUKLEMS
 - Bassanini-Duval





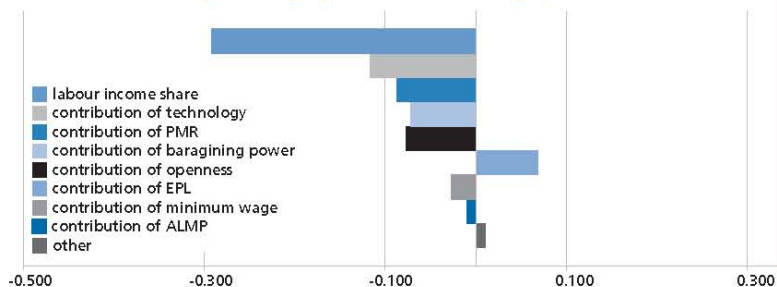
Table 5: Estimation results of a system of equations¹

	skill composition of labour			total labour
	low-skilled	medium-skilled	high-skilled	
capital-labour ratio (in log)	-4.770*** (1.655)	8.900*** (1.862)	5.788*** (0.870)	9.917*** (1.728)
ICT use (in log)	-4.140*** (0.355)	1.587*** (0.399)	2.104*** (0.186)	-0.449 (0.370)
PMR (in log)	3.752*** (0.917)	0.111 (1.032)	-2.587*** (0.482)	1.276 (0.958)
openness	0.003 (0.014)	-0.059*** (0.016)	0.004 (0.007)	-0.052*** (0.014)
union density	-0.232*** (0.039)	0.190*** (0.044)	0.090*** (0.021)	0.048 (0.041)
UBenefit	-0.103*** (0.028)	-0.197*** (0.031)	-0.013 (0.015)	-0.312*** (0.029)
EPL (in log)	-2.071* (1.057)	-5.584*** (1.190)	3.060*** (0.556)	-4.595*** (1.104)
labour tax wedge	-0.289*** (0.046)	0.042 (0.052)	-0.084*** (0.024)	-0.330*** (0.048)
minimum wage	0.439*** (0.075)	-0.241*** (0.085)	-0.045 (0.040)	0.153* (0.079)
ALMP	0.056*** (0.010)	-0.057*** (0.011)	-0.005 (0.005)	-0.006 (0.010)

Change in the labour income share: total and per skill type

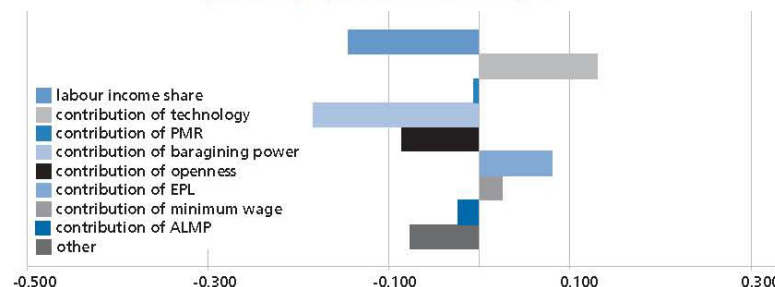


Chart 15: Change in labour income share in EU-11: total (percentage points, annual averages)



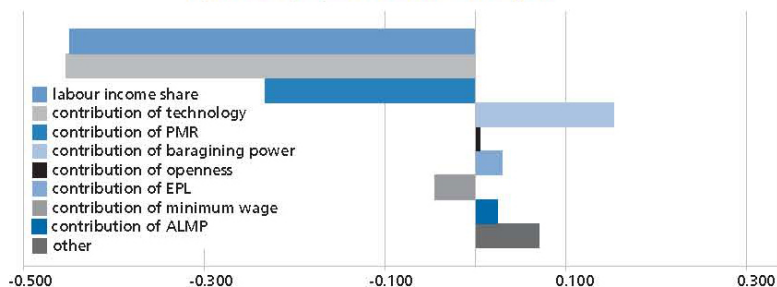
Note: EU-11 includes Belgium, Denmark, Germany, Spain, France, Italy, the Netherlands, Austria, Finland, Sweden and the United Kingdom.

Chart 17: Change in labour income share in EU-11: medium-skilled (percentage points, annual averages)



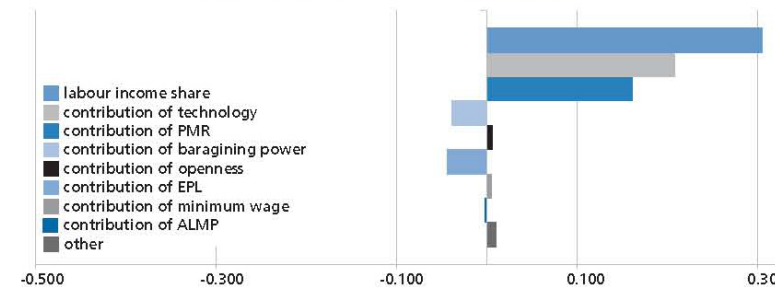
Note: EU-11 includes Belgium, Denmark, Germany, Spain, France, Italy, the Netherlands, Austria, Finland, Sweden and the United Kingdom.

Chart 16: Change in labour income share in EU-11: low-skilled (percentage points, annual averages)



Note: EU-11 includes Belgium, Denmark, Germany, Spain, France, Italy, the Netherlands, Austria, Finland, Sweden and the United Kingdom.

Chart 18: Change in labour income share in EU-11: high-skilled (percentage points, annual averages)



Note: EU-11 includes Belgium, Denmark, Germany, Spain, France, Italy, the Netherlands, Austria, Finland, Sweden and the United Kingdom.



- the labour income share is not invariant
- drivers can have a significant different impact on the income share of different skill types
- technological progress (including changes in the capital-to-labour ratio) made the largest contribution to the fall in the aggregate labour income share, but this loss was unevenly spread





- Avoid adverse developments in LIS through a well-balanced policy package.
- Pursue labour market policies that:
 - a) allow the low-skilled to progress
 - b) address the social needs of the low-skilled during this adjustment period.





- Policies based on flexicurity principles should facilitate the swift progression of low-skilled workers to better jobs

