6 Wage Bargaining in the Share Economy

6.1 INTRODUCTION

In this chapter we consider a world in which the senior employees of a firm (insiders) differ from the new entrants or the unemployed (outsiders) in that, even though their ability and productivity is potentially the same as everybody else's, they enjoy a market power vis-à-vis the firm because of the existence of turnover costs (for example, hiring, firing, and training costs). Thanks to these costs the insiders are able to raise their wage above the minimal level required to induce workers to become entrants. For this reason the system may exhibit involuntary unemployment in long-run equilibrium, one that—unlike the type of unemployment considered in the previous chapters—is unaffected by cyclical fluctuations in demand. The existence of labour unions at firm level fits easily into this framework, further reinforcing the insiders' bargaining power, but is not a necessary condition for an equilibrium unemployment to arise.

We are here dropping, then, one of the competitive hypotheses on which the previous chapters were built. How will a share system fare in this new environment?

First of all, it can be shown that the share system is in general liable to be upset by local agreements between firms and incumbent workers to the effect of restricting employment. If such is the case, excess demand for labour vanishes and the share system will exhibit some positive level of involuntary unemployment—no difference in this regard with a fixed-wage system. This demonstration is provided in section 6.2.

All this does not allow us yet to draw a comparison between equilibrium levels of unemployment in the two systems, because a theory of wage determination is not yet provided. To this effect the bargaining process between firm and insiders must be specified: this is done by Weitzman (1987) by means of a Zeuthen–Nash bargaining model. Weitzman finds that the share system's equilibrium exhibits in general a lower level of unemployment (and also a lower wage level) than the wage system's. Section 6.3 below is devoted to explaining and discussing this result.
Lastly, it might be asked whether the results found in Section 6.3 are contingent on the rather special assumptions underlying the insider-outsider model. Section 6.4 examines the problem in the context of a monopoly union model à la MacDonald and Solow and summarises our general conclusions.

### 6.2 EMPLOYMENT-RESTRAINING AGREEMENTS UNDER REVENUE SHARING

We showed in Chapter 3, section 2, that a share system in short-run equilibrium with fixed compensation parameters will in general possess an inefficient allocation of labour among firms. This inefficiency would disappear in a long-run equilibrium in which firms were free to adjust compensation parameters to the optimal levels – but it is just such a tendency that could hardly be relied upon in a state of permanent excess demand for labour. Now we propose to show that in such a situation restrictive practices are bound to develop at the level of individual firms, and these practices will defeat the excess demand.

To place our argument in the conditions most favourable to the share system as described by Weitzman, in spite of what we have just stated, suppose that the system is indeed in efficient equilibrium: for example, imagine that conversion to the share system has taken place 'by night' starting from a wage system which was at rest in long-run equilibrium. This equilibrium is now upset by a sudden inflow of new job seekers: as we know, if Weitzman's expectations are fulfilled, these people will at once find employment at the going compensation parameters, and as a consequence the system will be thrown off the efficient equilibrium. A firm's incumbent workers, however, might 'purchase' from the firm its hiring rights for a stated period, paying a price (that is, accepting a wage cut) to compensate the firm for the profits forgone, provided it was in the workers' own interest to do so. If such a deal is carried out, the new job seekers will not be hired and – if similar agreements should spread across firms – the system will have lost full employment and preserved allocative efficiency; that is, it will have performed in fact like a wage system. Of course, given the parameters of the share contract, every new hiring will lower the pay of incumbent workers: the latter, therefore, will be willing to make the deal if the loss in their total pay from the new hirings is greater than the compensation that the firm will ask to refrain from hiring,