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Research in Brief

Columbia Business School

Economy & Policy

My Work Is My Bond? A Financial-Asset Approach to Wage Contracts Could Lessen Inequality

Key Takeaways

- Inequality is a significant problem in America, and it's worsened over time
- A key contributor may be a declining sense of corporate paternalism toward workers
- Securitizing workers' wages over a long period could smooth out the vagaries of short-term business cycles and tie workers and firm owners more closely together
- This would be a purely private endeavor that could help avoid government interference in redistribution of wealth

Adapted from "The Macroeconomics of Stakeholder Equilibria" by John B. Donaldson of Columbia Business School and Hyung Seok E. Kim of the Korea Advanced Institute of Science and Technology.

The paper from Columbia Business School, "The Macroeconomics of Stakeholder Equilibria," proposes a model for a purely private, mutually beneficial financial agreement between worker and firm that keeps decision-making in the hands of stockholders while improving the employment contract for employees.

The study was co-authored by John B. Donaldson of Columbia Business School and Hyung Seok E. Kim of the Korea Advanced Institute of Science and Technology.

Research

When companies make decisions that prioritize value for stockholders, workers often lose out. As many observers have noted, the rise of a shareholder-centric economy over the past few decades has coincided with a rise in inequality in America.

Recent research suggests that simply implementing a mutually agreeable contract between workers and management may eliminate as much as 60% of the negative side effects of (investment) decisions made by stockholders without the need for stronger measures, such as government intervention for wealth redistribution. That's essentially what was achieved in the economy of the U.S. between 1970 and 2015, the authors say. But as wealth inequality has become more entrenched due to the increasing "centralization" of capital ownership, the researchers' analysis suggests that share has fallen to 50%.

"In this paper we propose one route to a more inclusive society," Donaldson and Kim say. They start from empirical evidence that companies took a more paternalistic approach to negotiating with their workers in the 1950s and 1960s than they do now.

Stockholders account for just 10% of society, the researchers note, so in the spirit of a society working for the benefit of all stakeholders, the researchers propose what they call "egalitarian wage bargaining." Negotiations over wages should consider factors that affect worker's employment circumstances such as differing levels of risk that workers face relative to stockholders such as job loss, and, potentially, differences in working conditions, they say.

Research (continued)

The researchers' key contribution is the idea that once a salary has been negotiated, firms might securitize the wages – turning them from a series of ongoing, possibly unsteady, paychecks into a "fixed-income-like wage asset." That way, an ongoing stream of income can be made more stable for the worker, smoothing out the ups and downs of the business cycle.

The asset would be tradable, and workers could use them to borrow against their future income streams to finance the purchase of a house, say, or to tide them over during recessionary periods.

Without some intervention, such as the adoption of this model, even greater inequality is likely, the researchers suggest. We'd likely see a more stagnant economy, "with the value of the wage asset becoming progressively disassociated from labor productivity," and workers cautious about spending. "The latter phenomenon surprisingly resembles key features of the 2008-2015 financial crisis where U.S. wealth inequality was historically high and the economy's real interest rate was unambiguously negative," they write.

Conclusion

Building a more inclusive society may start with a few small steps. More egalitarian contracts between firms and workers could be fairer and more productive for everyone, and have ripple effects through to the broader economy. If firms were even more proactive and established a proposed financial instrument in place of traditional weekly wages, workers could share in the benefits – and risks – of the stockholders of the firm, without the need for existing stockholders to give up their ownership.

Columbia Business School Faculty

John Donaldson
Mario J. Gabelli Professor of Finance
Economics Division

Connect with Columbia Business School

Email
communications@gsb.columbia.edu

CBS Insights
leading.business.columbia.edu

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