Inequality

The IFS Deaton Review

Inequalities in the French labour market: a mixed picture

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Introduction

The 'Labour market inequality' chapter by Giulia Giupponi and Stephen Machin in the IFS Deaton Review shows that the UK labour market has undergone important transformations since the 1980s, which have led to a significant increase in inequalities, and in particular in wage inequalities. They emphasise that inequality is the result of interactions between technical progress, globalisation and labour market institutions, with particular emphasis on the role of the minimum wage, collective bargaining and unionisation, and the regulation of the labour contract.

This commentary aims to compare the evolution of inequalities in the French and UK labour markets. This comparison is particularly interesting because the evolution of inequalities is very different in the two countries. While wage inequality has increased in the UK and most OECD countries, it has not increased in France. The commentary also draws on examples from other OECD countries.

I start by recalling that wage inequalities have remained stable in France in the last four decades but that the performance in terms of employment and unemployment is poor, compared with the majority of OECD countries, and in particular with the UK. Thus, although wage inequality has not increased in France, the poverty rate before taxes and transfers is much higher than in the UK because of the low integration into employment of a large part of the population. This indicates that the analysis of wage inequality only very partially sheds light on the impact of the functioning of the labour market on income inequality of the working-age population.

I then discuss the features of labour market regulation that have kept wage inequality in check in the face of the pressure of biased technical progress and globalisation, focusing, like Giupponi and Machin (2022), on the role of the minimum wage, collective bargaining, and regulation of the labour contract.

Evolution of inequality on the French labour market

In France, in the private sector, the D9/D1 interdecile ratio of net full-time equivalent wage first declined significantly from 1967 until the mid-1980s, from 4.0 to 3.0 (see Figure 1). It then fluctuated a bit around 3.0, its 2017 level. The sharp decline in wage inequality in the 1970s was due to a reduction in gaps at the bottom of the wage scale, linked in particular to increases in the minimum wage; the ratio of the ninth decile (D9) to the median (D5), which describes inequality at the top of the wage scale, remained much more stable, fluctuating around 2.0.

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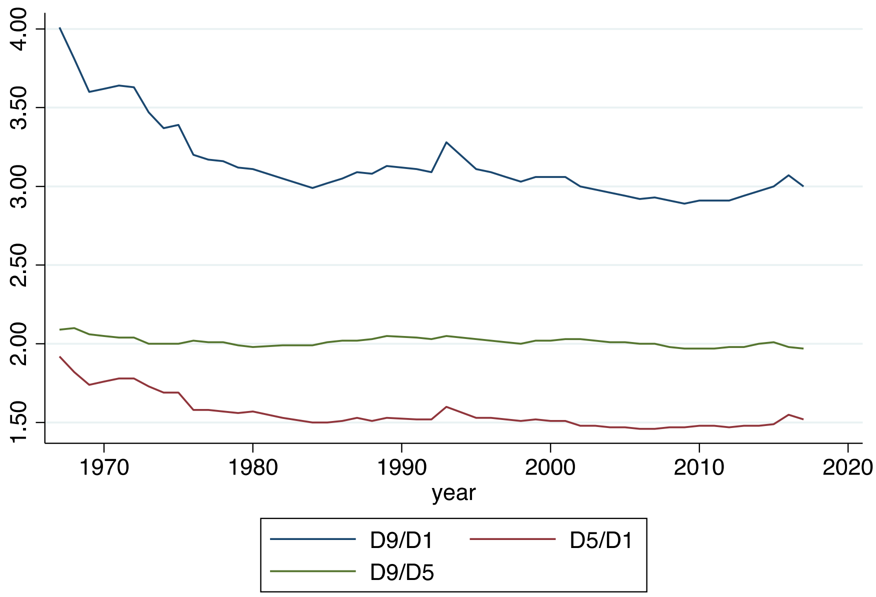
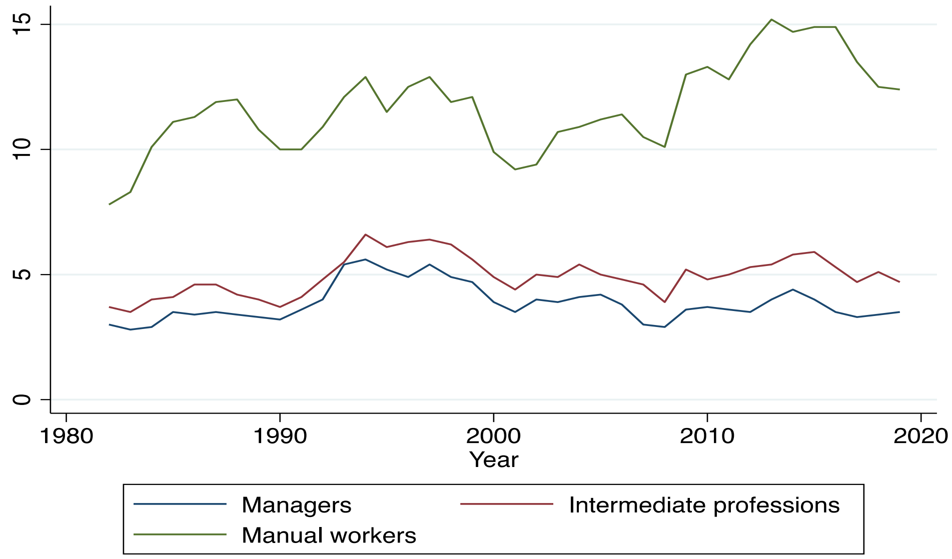
Figure 1. Distribution of private-sector full-time equivalent net wages in France, 1967–2017



Source: INSEE

Figure 2 shows that unemployment rates have increased overall since the early 1980s, but with a much larger increase for manual workers than for workers belonging to intermediate professions and managers, whose unemployment rates have remained at lower levels. This increase in inequality of unemployment risk is particularly marked for young people aged under 25, whose unemployment rate has been rising steadily over this period, fluctuating between 20% and 25% during the 2010 decade (Figure 3).

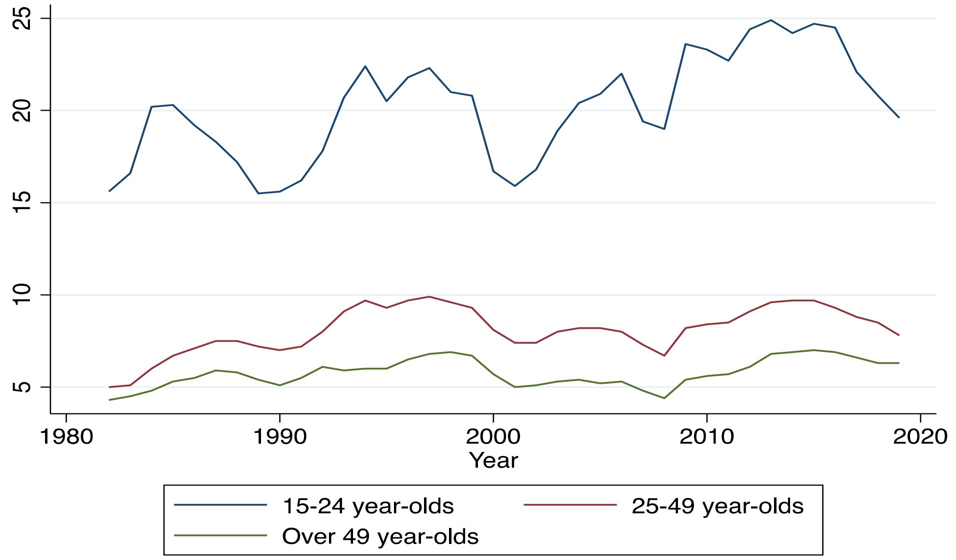
Figure 2. Unemployment rate by socio-professional category in France, 1982–2019



Source: INSEE

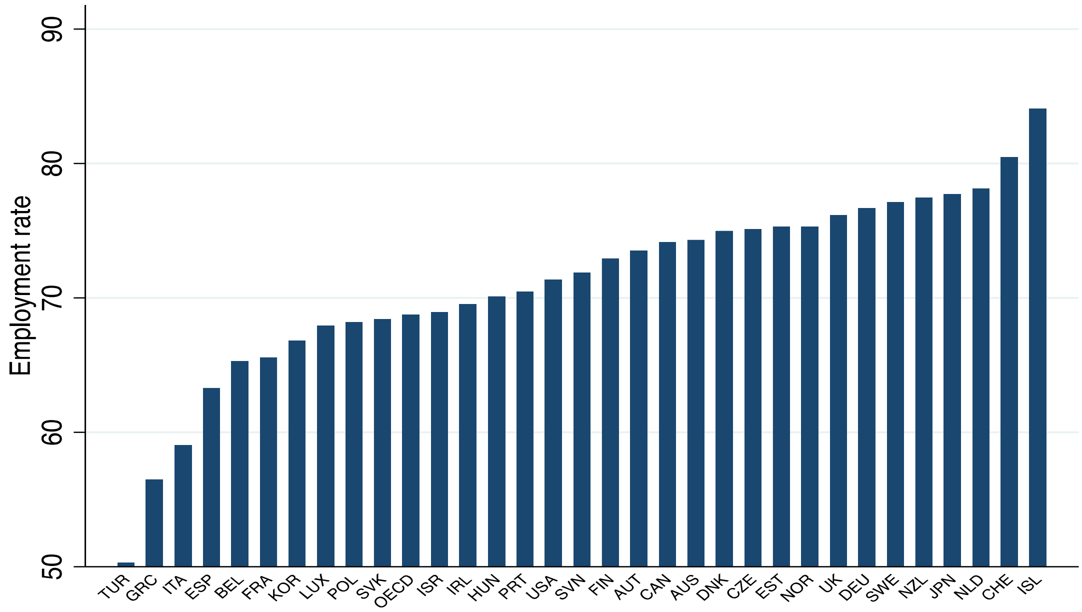
The high level of unemployment in France is concomitant with a low employment rate, which is below the OECD average not only for the working-age population as a whole (Figure 4), but also for all demographic groups, i.e., young people, older people and low-skilled workers (Blundell, Bozio and Laroque, 2013). The gap with the UK is significant: it reaches 10 points for the whole group of people aged 15–64 (Figure 4) and is lower for young people, older people, women and low-skilled workers.

Figure 3. Unemployment rate by age group in France, 1982–2019



Source: INSEE

Figure 4. Employment rates (people aged 15–64) in 2019



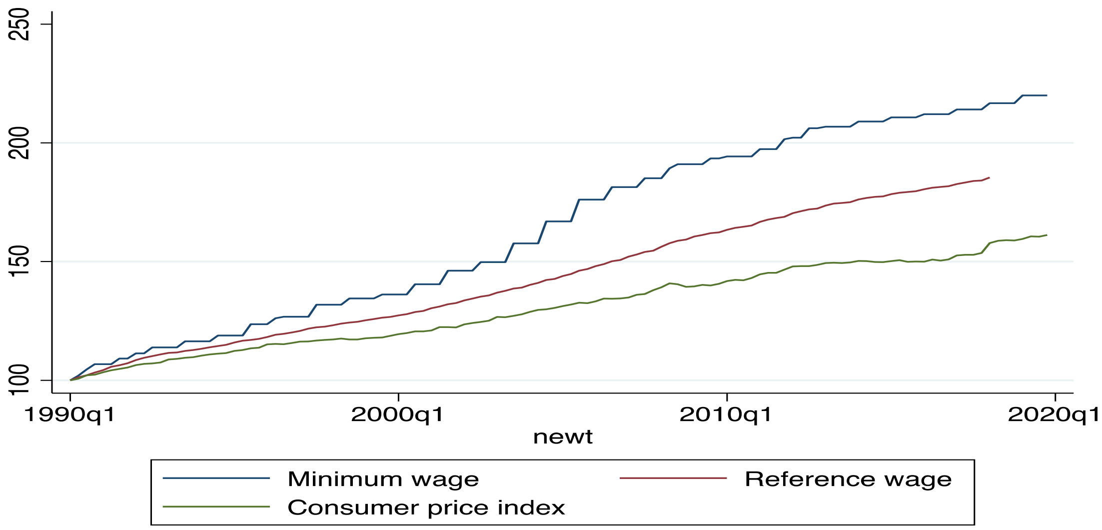
Source: OECD

Minimum wage

The minimum wage was introduced in France in 1950 and underwent major changes in 1970, as part of the Grenelle Agreements, which aimed to raise wages following the strikes of 1968. The minimum wage applies to all employees aged 18 and over. It is revised automatically according to the consumer price index and the change in purchasing power of the basic hourly wage for manual workers (and for manual workers and employees since 2017). In addition, the government has the option to increase the minimum wage at its discretion. Figure 5 shows that the minimum wage has grown faster than the average wage of blue-collar and white-collar workers since the 1990s, and especially during the 2000s when the legal reduction in working hours was offset by an increase in hourly wages to maintain the purchasing power of monthly wages.

As a result, as Figure 6 shows, the ratio of the minimum wage to the median wage is high in France. In 2019, it is 61% in France compared to 55% in the UK, and the share of employees affected by minimum wage increases is high. It has fallen since the mid-2000s but in 2019 is around 12% (Figure 7), a much higher level than in the UK, where it is less than 8%. This share is much higher for small companies, where it reached 28% in 2019 in France (INSEE, 2020).

Figure 5. Hourly nominal minimum wage, consumer price index and hourly wage for manual workers and employees in France from 1990q1 to 2019q4



Source: INSEE

Note: Consumer price index, including tobacco, for all households of employees excluding apprentices, trainees and temporary workers; all sectors excluding agriculture, public administration, household activities and extra-territorial activities. Reference wage refers to the base hourly wage for manual workers and employees.

Figure 6. Minimum–median wage ratio in OECD countries in 2020

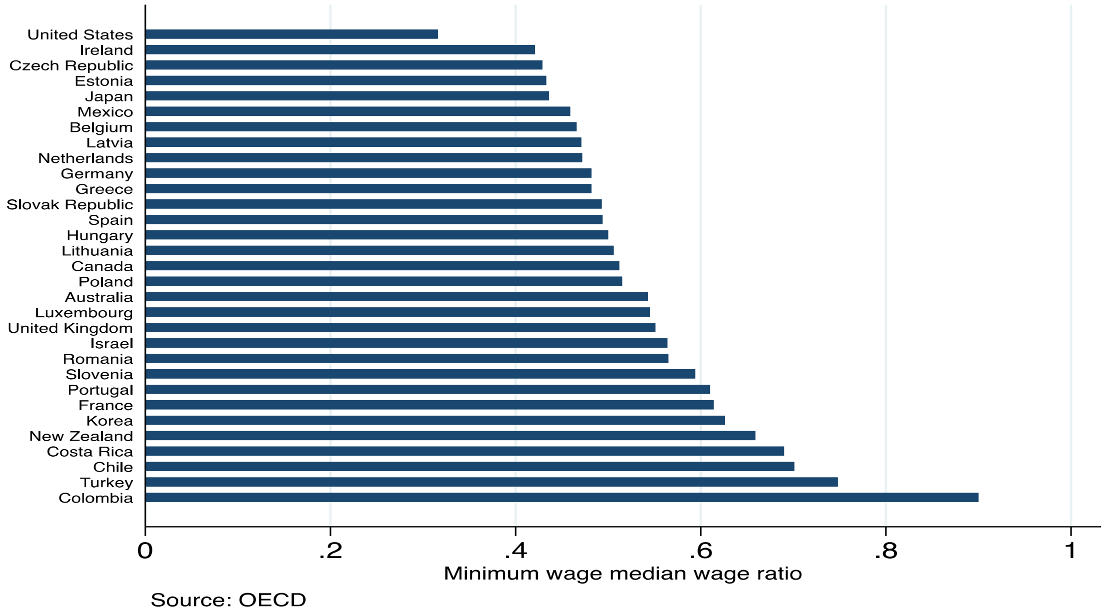
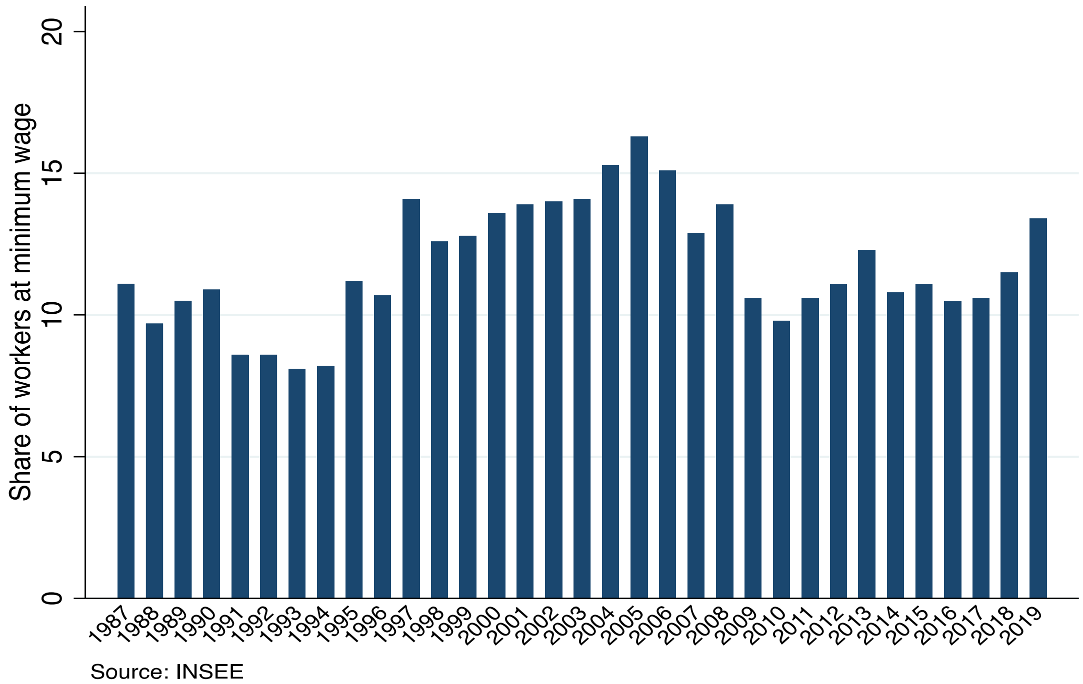


Figure 7. Percentage of employees affected by increases in the minimum wage from 1990 to 2019 in France



Since 1994, all governments have implemented policies to reduce employer social security contributions on low wages in order to limit the impact on employment of excessively high labour costs. These policies have grown in scale and the reductions in social security contributions on low wages, below 2.5 times the minimum wage, reached about 60 billion euros in 2019, or more than 2.5% of GDP (L'Horty, Martin and Mayer, 2019). Available evaluations show that these contribution reductions have a significant impact on employment when they are targeted at wages near the minimum wage. However, their effectiveness in terms of job creation decreases with the level of the wage, and disappears above about two times the minimum wage (L'Horty et al., 2019). Guillot, Bozio and Breda (2020) show that these reductions in employers' contributions significantly reduced the cost of low-skilled labour. However, Guillot et al. (2020) show that these reductions in contributions were not sufficient to counteract the drop of demand for low-skilled labour linked to technical progress and international competition.

In addition, to shed light on the impact of the minimum wage, a Committee of Experts was created in 2007. Composed of five independent academic experts renewed every five years, it writes a public report every year and issues a recommendation on whether the minimum wage should be increased beyond the increase induced by the rule of indexation to the consumer price index and to the wages of manual workers and employees. Since its creation, this committee has consistently recommended not to increase the minimum wage beyond the minimum statutory increase, based on the following justifications.

- The high level of the minimum wage relative to the median wage has an impact on the demand for labour.

- The increase in the minimum wage, which is costly for public finances because of the reductions in contributions on low wages, has a limited impact on the reduction of inequalities, because a significant proportion of those earning the minimum wage belong to households whose standard of living is not in the lowest deciles of the distribution of standards of living.

- Increases in the minimum wage are partly counteracted by reductions in social transfers, which mechanically diminish when the income from work increases.

For all of these reasons, the Committee of Experts systematically advocates using social transfers and taxes to reduce inequalities in living standards at the level of low wages rather than increases in the minimum wage.

These recommendations have been followed by all governments, with the exception of 2012, when François Hollande slightly increased the minimum wage after his election as president. Thus, Figure 5 shows that the minimum wage has been growing at the same rate as the basic wage of workers and employees since 2008, after growing significantly faster in previous years.

Collective bargaining

France is characterised by a very high rate of coverage of collective agreements, which amounted to 98% in 2018. This particularly high rate is not due to a high rate of unionisation, which is among the lowest in the OECD countries (see Figure 8), but to sectoral collective agreements negotiated by trade unions and employers' organisations and extended almost systematically to all employees by the Ministry of Labour. In principle, in the absence of an extension decision by the Ministry, collective agreements only apply in firms that are members of the employers' organisations that signed the collective agreements. But, since World War II, collective agreements have been gradually extended more and more frequently. These agreements are very numerous: each year, there are approximately 300 new sectoral agreements on remuneration and 600 new sectoral agreements on other various subjects, such as working conditions, gender equality, discrimination, the employment contract, forward-looking management of skills, employment of senior citizens, union right, financing of trade unions and employers' organisations, vocational training, etc. The legality of each of these agreements is examined by the Ministry of Labour and they are then extended at the request of the social partners. Once they have been extended, the agreements negotiated at sectoral level apply to all companies according to the principle of favourability, which stipulates that firms must apply the sectoral agreement unless the conditions are more favourable for employees. This principle, which admits rare exceptions, considerably limits the scope of negotiation at firm level. Extensions of sectoral agreements by various means are also common in continental European countries such as Belgium, Italy, Portugal and Spain (OECD, 2019).

This labour market regulation significantly limits wage inequalities insofar as wage agreements set wage floors according to occupation, diploma, seniority in the firm, work experience and the tasks the employee is capable of performing. In this context, the sectoral collective agreement defines a wage scale, the lowest level of which generally corresponds to the legal minimum wage. A large part of these wages is, in practice, indexed to the minimum wage (Avouyi-Dovi, Fougère and Gautier, 2013; Fougère, Gautier and Roux, 2018). As a result, increases in the minimum wage lead to a chain reaction of wage increases up to 1.7 times the minimum wage, which is above the median wage (Aeberhardt, Givord and Marbot, 2016).

Figure 8. Union density and bargaining coverage in OECD countries in 2016

Source: OECD

Several empirical studies find that the extension of industry agreements limits nominal wage inequality but results, in return, in a negative impact on employment and firm creation (e.g., Madruger, 2012; Murtin, de Serres and Hijzen, 2014; Hijzen and Martins, 2020; Martins, 2021). The conduct of industry-level bargaining, in which large, well-established firms have a decisive influence, leads to upward wage adjustments that are unfavourable to small firms, as well as to young firms with less financial capacity. However, these firms are more likely to employ new entrants to the labour market, especially young and low-skilled people. The almost systematic extension of sectoral agreements increases the downward rigidity of wages and creates barriers to entry (Haucap, Pauly and Wey, 2001). In addition, the homogeneity of nominal wages between regions with heterogeneous costs of living can translate into large differences in real wages between regions (Boeri et al., 2021).

Collective bargaining has an important impact on the functioning of the labour market beyond wage formation. Dustmann et al. (2014) argue that the transformation of the German economy from the 'sick man of Europe' to a lean and highly competitive economy within little more than a decade is rooted in the inherent flexibility of the German system of industrial relations. The flexibilisation of wage formation following the decentralisation of negotiations from the industry to the firm level has increased wage inequalities (Dustman et al., 2009) but has, in return, contributed considerably to reduce the unemployment rate and to increase the employment rate. In the same perspective, evidence on the decentralisation of collective bargaining in Portugal suggests that it has increased employment growth by up to 10 percentage points (Hijzen and Martins, 2020).

Boeri et al. (2021) highlight the importance of collective bargaining system by comparing Germany and Italy. Italy sets wages based on nationwide contracts that allow for limited local wage adjustments, while Germany has moved toward a more flexible system that allows for local bargaining. Boeri et al. show that Italy exhibits limited geographical wage differences in nominal terms and almost no relationship between local productivity and local nominal wages, while Germany has larger geographic wage differences and a tighter link between local wages and local productivity. As a consequence, in Italy, low productivity provinces have higher non-employment rates than high productivity provinces, because employers cannot lower wages, while in Germany the relationship between non-employment and productivity is significantly weaker. Boeri et al. estimate that if Italy adopted the German system, aggregate employment and earnings would increase by 11.04% and 7.45%, respectively. They stress that their findings are relevant for other European countries such as Belgium, Finland, France, Iceland, Portugal and Slovenia, which have a system similar to the Italian model, while Austria, Denmark, the Netherlands, Norway and Sweden are closer to the German model.

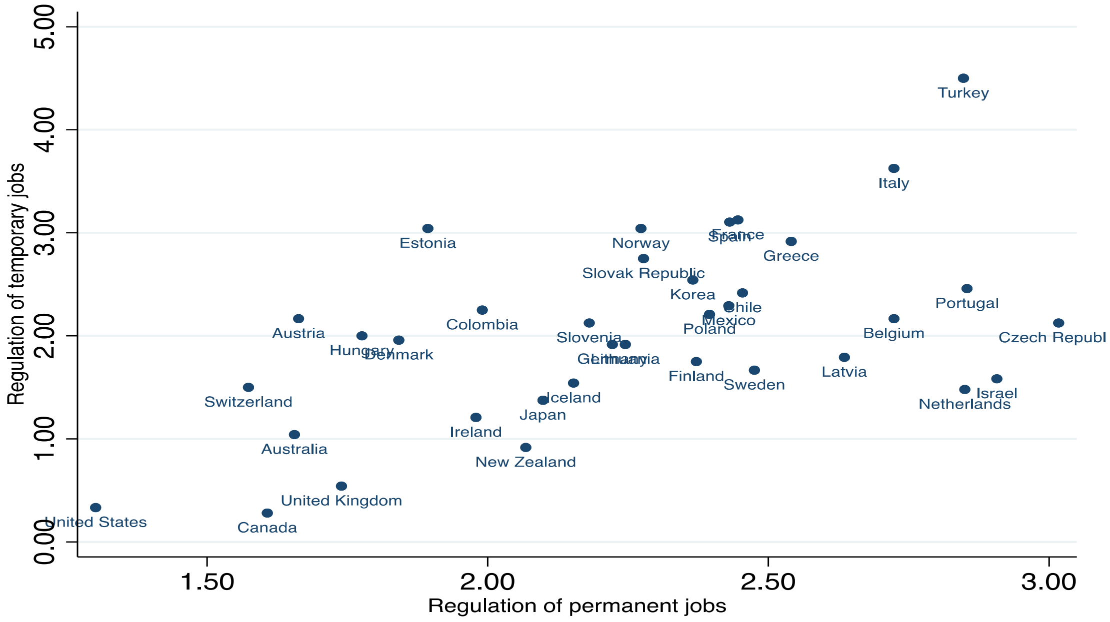
Taken together, these contributions show that economies that have adopted collective bargaining systems at the centralised or the industry level with little freedom for bargaining at the firm level have limited the growth of nominal wage inequalities in the face of the pressures of technical progress and international competition. Nevertheless, the lack of wage flexibility has resulted in significant costs in terms of job creation, productivity losses and the development of real wage inequalities between regions.

Contract regulation

Like several continental European countries (in particular Greece, Italy, Portugal and Spain), the French labour market is structured in a dual manner: on the one hand, holders of permanent contracts, protected by numerous and overly codified rules, which are a source of legal disputes that do not provide security for employees and are too uncertain for employers; and on the other hand, temporary contracts, whose term and cost are known in advance. This duality has been reinforced since the early 1990s (Behagel and Postel-Vinay, 2003). Today, temporary contracts account for more than 90% of hires and about 15% of employees.

In order to limit the possibility of substituting temporary contracts for permanent contracts, regulations generally impose stronger constraints on the use of temporary contracts or alternative forms of employment when permanent jobs are more protected. Thus, there is a positive correlation between the stringency of employment protection and the stringency of regulations that limits the use of temporary employment (Figure 9).

Figure 9. Regulation of temporary and permanent jobs in OECD countries in 2019



Source: OECD

Note: Range of indicator scores: 0–6. The indicator for dismissals of permanent jobs is for individual dismissals only, as the hiring indicator for temporary jobs is also based on hiring one worker.

The protection of permanent jobs, together with the regulation of temporary contracts, makes it possible to ensure job stability for employees whose salaries may be, to a large extent, disconnected from changes in their productivity due to sectoral collective agreements. Thus, there is complementarity between the regulation of employment protection and wage formation, which allows part of the workforce to hold stable jobs whose remuneration progresses regularly thanks to sectoral collective agreements. This complementarity ensures the coherence of the system, which limits the increase in wage inequalities when the economy is faced with external shocks such as biased technical progress and competition from low-wage countries. Wage inequality is further contained by the fact that labour laws and collective agreements impose equality of pay and working conditions between temporary and permanent employment contracts.

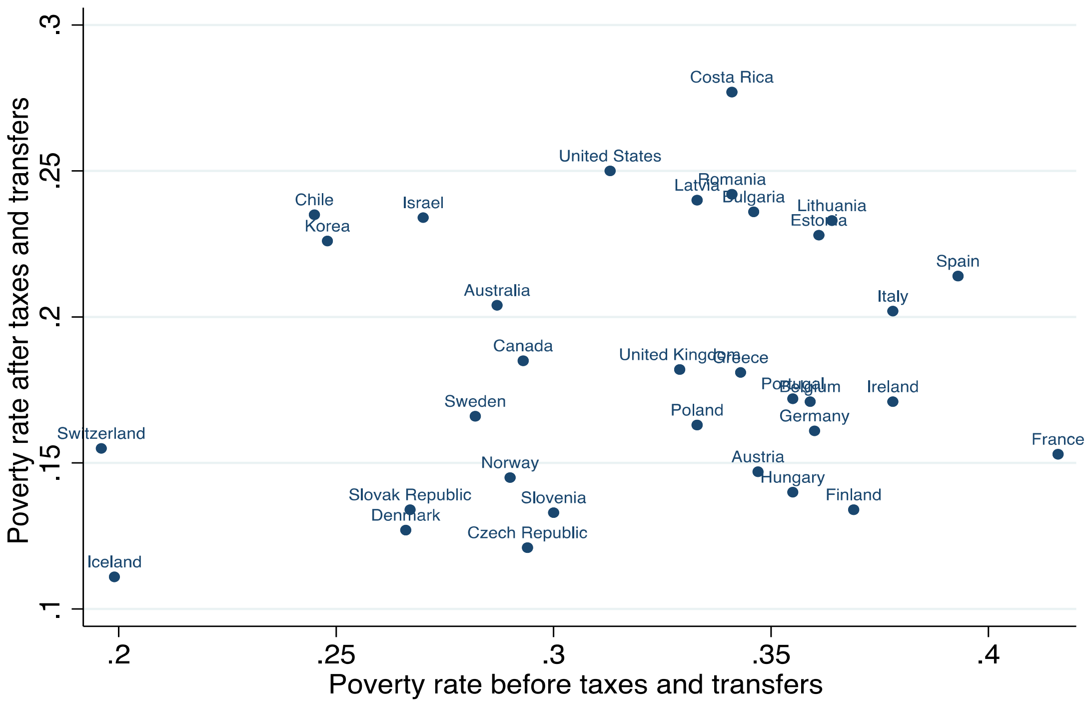
The fact that the counterpart of this system, which protects part of the workforce, creates inequalities in access to stable and well-paid jobs is well documented. In particular, the literature shows that youths, women and the low skilled tend to be the population groups for which temporary work relationships are particularly common, meaning that labour market duality is especially detrimental to these demographic groups (for a recent survey, see OECD, 2020).

Conclusion

A high minimum wage relative to the median wage, a rigid scale of centrally or sectorally negotiated minimum wages, and legislation to ensure job stability for employees on permanent contracts have enabled France to contain wage inequality, which has not increased for more than four decades. This strategy is very different from that adopted in the United Kingdom, where flexibility in wage formation and employment contracts has led to a significant increase in wage inequality, although the minimum wage has helped to limit this increase at the lower end of the wage distribution.

That said, the French strategy results in a low employment rate and a high unemployment rate that create significant inequalities in access to employment. Thus, the poverty rate before taxes and transfers is particularly high in France compared with the UK and all OECD countries (Figure 10). This suggests that imposing a wage structure co-administered by the social partners and the state to limit the growth of wage inequality is not necessarily an appropriate strategy to combat the growth of market income inequality. However, the poverty rate after taxes and transfers is much lower in France than in the UK because France is the country that reduces the poverty rate most through taxation and social transfers (Figure 11). But the high pre-tax and transfer poverty rate induced by labour market regulation implies that the relatively low post-tax and transfer poverty rate is achieved at a significant cost to public finances.

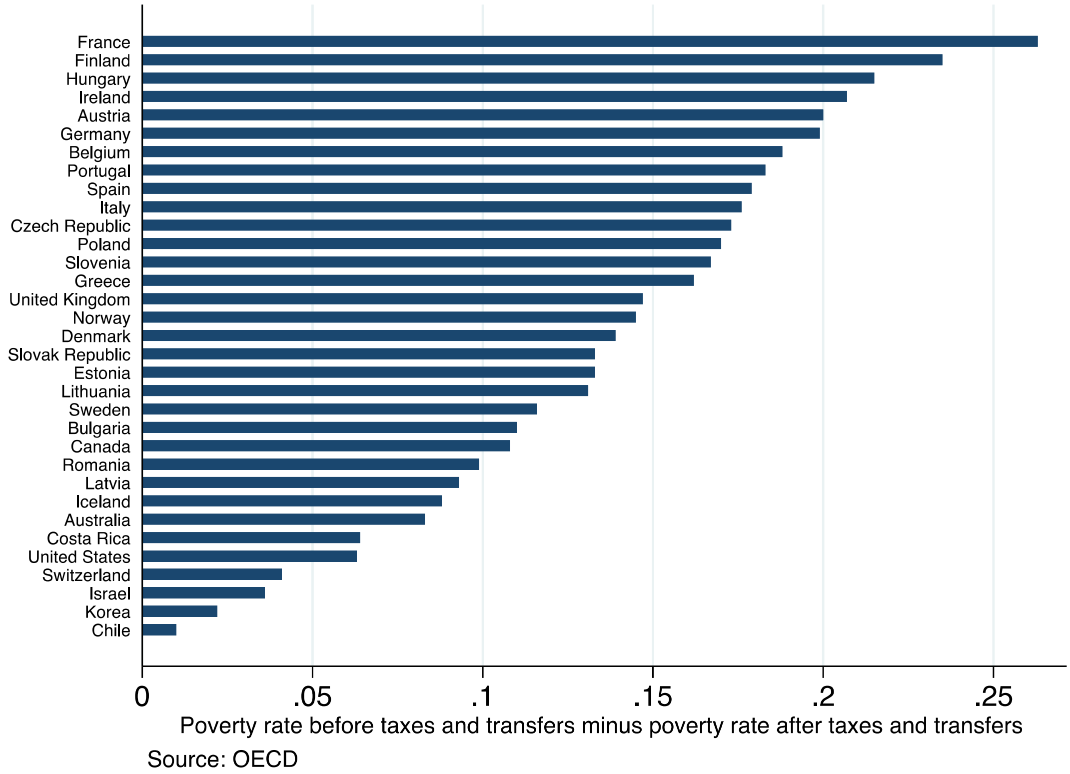
Figure 10. Poverty rates before and after taxes and transfers in OECD countries in 2017–18



Source: OECD

Note: Poverty rate = percentage of people living with less than 60% of median equivalised income.

Figure 11. Difference between before and after taxes and transfers poverty rate in OECD countries in 2017–18



Note: Poverty rate = percentage of people living with less than 60% of median equivalised income.

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