General Discussion of 'Wages Growth in Australia: Lessons from Longitudinal Microdata'

Much of the discussion centred on the interpretation of the results regarding the extent of rent sharing in Australia, and the methodology used by the authors to investigate it.

In terms of interpretation, one participant noted that the estimated rate of rent sharing made sense from the perspective of a firm that only partially passes on any rents (or windfalls) so as to insure themselves against rapid reversals of fortune. It was noted that the authors were only estimating a short-run sensitivity and that it would also be worth exploring the long-run sensitivity of wages to productivity changes; one would expect complete pass-through in the long run as it would make less sense for firms to be limiting rent sharing for insurance reasons. A comparison was made to the exchange rate pass-through literature in which sensitivity is different in the short run and the long run. To the extent that wage bargaining occurs over several years, the extent of pass-through beyond the one-year horizon would be particularly important to study.

Relatedly, the nature of the shocks identified by the authors was discussed. One participant suggested distinguishing between transitory and permanent shocks would facilitate the distinction between long- and short-run pass-through. Another point of discussion was the level at which the shock occurred. The paper investigated shocks at the firm-level. However, there was also an acknowledgement that industry-level shocks, such as changes to enterprise bargaining arrangements, could be relevant. Participants also questioned the implicit assumption of the authors that firm productivity shocks were exogenous and that all causality ran from changes in productivity to changes in wages. It was noted that causality could potentially also run in the other direction; for instance, the concept of an efficiency wage implies an ability to increase productivity by increasing employees' wages. The author agreed that this was a limitation of the approach, and there was some discussion of a number of possible methodological solutions though they also noted that instrumental variables approaches rarely overturned the key finding in the literature that firms share rents with their workers.

A final point of discussion on the interpretation focused on the translation of the microeconometric level estimates to the macroeconomic level. It was agreed that this translation was difficult to achieve, and the author noted that they had made only rough indicative calculations. One specific issue noted was that at the macroeconomic level, wages could be considered as jointly determined by labour productivity and the reservation wage, which complicates the relationship between productivity and wages.

In terms of methodology, there were two key areas of discussion. First, the discussant had raised a question of whether it was more appropriate to model the relationship between productivity and wages using the level or the growth in wages. The paper chooses wages growth as the dependent variable, which when coupled with individual fixed effects allows for permanent differences in wages growth across individuals. One participant suggested that there was recently published research on Australian wages (Freestone 2018) indicating that while there are substantial differences between individuals in wage levels, there is no support for an assumption of systematic differences in wages growth across individuals. The author noted that the growth specification was better suited to disentangling a change in the rent sharing relationship, as any such change seemed more likely to occur with respect to the pass through to wages growth rather than wages levels. Moreover, the author showed additional robustness tests which suggested that the results were generally robust to the choice of micro fixed effects structures and growth *versus* levels specifications when modelling the link between wages and productivity.

Second, there was some discussion of the method used by the authors to test for a difference in the estimated relationships since 2012/13. This date had been selected by the authors because much of the discussion about unusually low wages growth was centred on explaining the period since, and the intention was to compare it to the period prior. Suggestions were made to also explore the existence of a less sudden change in the relationships.

A number of other more specific issues were also discussed. A participant raised a concern that the estimates quoted in the paper on the effect of the rate of job-to-job transitions on wages growth were, if translated to the macroeconomy, too large to be credible. The author and others noted that the microeconometric estimates could not be easily translated into a macroeconomic effect in the way that the discussant suggested; the estimates were based on a model with many controls, including adjustments to remove the effect of the aggregate business cycle, so any macroeconomic effects were already controlled for. There was a brief separate discussion about how monetary policy should respond if labour market dynamism declines. Finally, there were two suggestions from participants for ways to expand the scope of the data in the authors' longitudinal employer–employee database. It was suggested that it would be useful to incorporate some data on relationships that firms have outside Australia – for instance, a firm's imports and exports – to allow for some investigation of the role of globalisation and the end of the mining boom on the Australian labour market. It was also suggested that some data be incorporated on the characteristics of jobs (in particular information on casual work arrangements) and employees' child care arrangements to better understand the interaction between working conditions and wages growth.

Reference

Freestone O (2018), 'The Drivers of Life-Cycle Wage Inequality in Australia', *Economic Record*, 94(307), pp 424–444.