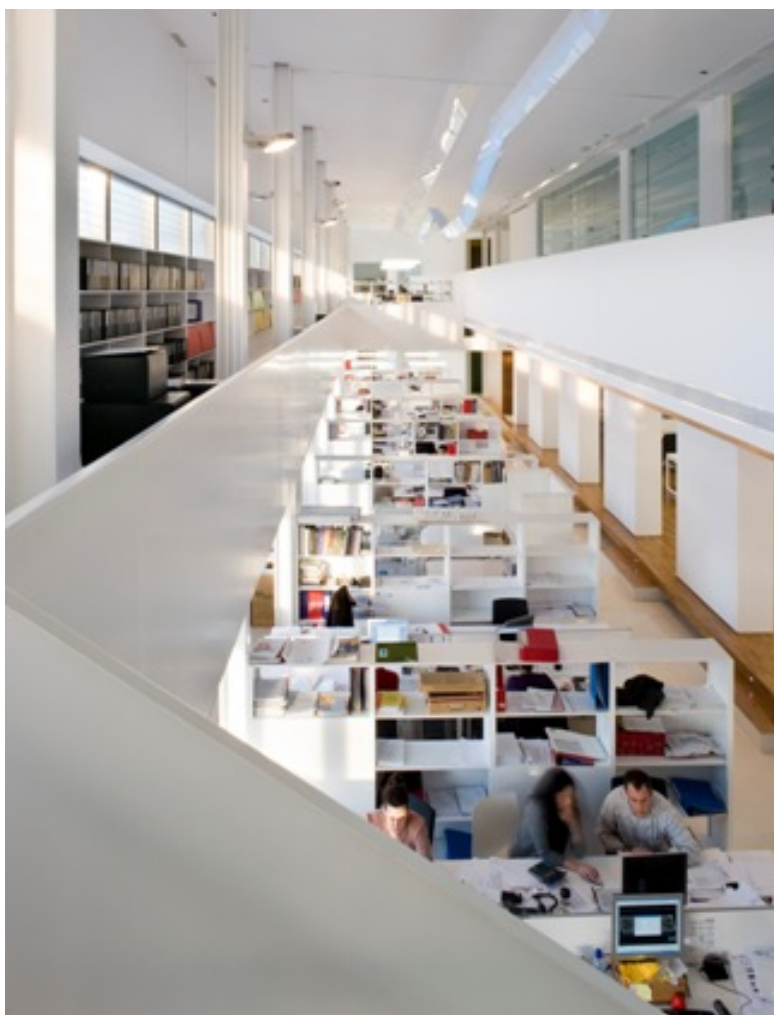


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Long term earnings inequality, earnings instability and temporary employment in Spain



Cross-sectional earnings inequality of male full-time employees falls over the second half of the nineties in Spain. A study finds that such decline was determined by a decrease in earnings instability and an increase in long term inequality. Given the marked decline in temporary employment

over the sample period, we also examine the effect of the type of contract on earnings variance components, and find that workers with fixed-term contract face on average more instability than workers with permanent contract. This evidence suggests that the decline in temporary employment is responsible for the decreasing earnings instability.

Earnings inequality is something that most citizens dislike, as they may perceive it as disproportionate or unfair. However, not all inequalities have the same consequences and are thus likely not to be deemed equally bad. More precisely, understanding the structure of earnings inequality is particularly interesting to judge the earnings distribution and to design better labour policies.

Earnings inequality over time may be driven by earnings differences that persist over time or rather reflect earnings instability. Long term earnings inequality captures differences that persist over a lifetime, so that individuals earning more earn systematically more, which leads to a rigid earnings structure where individuals do not move positions in the earnings distribution. Such persistent disparities may result from skill-biased technological change or demand shifts that benefit the highly paid.

Earnings instability instead measures disparities in earnings such that no individuals earn systematically more, which usually causes reshuffling and churning in the distribution. Large earnings instability are related to the decline of worker-firm attachment, possibly due to increased outsourcing or decreased employment protection legislation, EPL. The latter is especially relevant for our study since temporary employment in Spain has low EPL and accounts for over one third of overall employment, twice the European average.

Our study provides novel evidence on the relative importance of long-term earnings inequality and earnings instability in Spain, over a period (1993-2000) of decreasing inequality, and examines the influence of temporary employment on earnings instability. Understanding such relationship is important because, over the last three decades, many European countries relied on changing EPL provisions to combat the rise in unemployment. However, the often presumed positive association between lower EPL and earnings instability remains largely unexplored.

The study of the Spanish labour market over the second half of the nineties is compelling because during that period temporary employment fell substantially, from an all time high 35% in 1995 to 32% by the end of our sample period. Such a sharp decrease resulted from substantial changes in key EPL provisions with the aim of reducing the very large incidence of temporary employment. In particular, the 1997 reform substantially reduced firing costs and lowered payroll taxes for selected new hires.

Our findings suggest that the observed decline in earnings dispersion was mostly due to a fall in earnings instability. That is, over the sample period (1993-2000), earnings dispersion became more persistent and much less transitory. Our analysis also shows that such decline in earnings instability is mostly accounted for by the decline in temporary employment.

The study also concludes that the structure of earnings inequality changes over the life cycle. In particular, we show that relative earnings persistence increases over the life cycle, which implies lower instability for older cohorts. That is, earnings instability seems to fall over the life cycle, being especially high for younger age groups. These results are consistent with previous studies for some European countries.

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References

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