

## PREFACE

In no economy do all employees earn the same salary. Indeed pay variation is the norm rather than the exception. Some pay variation stems from innate worker heterogeneity, some from differential human capital investment, some from imperfect information, some from industry and occupation specific demand shocks, and some from asymmetric technological change; but there are many other reasons, as well. The ideal level of wage dispersion in any economy is a hotly debated topic. On the one hand, greater wage variation increases incentives to take risk often leading to hard work, innovation, and economic growth. On the other hand, too wide an earnings dispersion possibly instills resentment, perhaps leading workers to decrease cooperation, thus lowering output and stymying growth. At the extreme, too wide a dispersion could lead to political instability and even revolution. This volume contains eight articles, each dealing with an aspect of remuneration. Of these, one articles deals with competition, women's wages and employment, one articles deals with incentives to invest in human capital, four deal with compensation schemes, and finally two with unemployment and earnings.

One component of wage dispersion is the gender wage gap. Clearly government policy can affect what women earn relative to men. Most academic analyses concentrate on equal pay legislation. Few, if any, examine how broader government policies, such as those relating to international trade, affect pay for women. In the first article, Ernesto Aguayo-Tellez, Jim Airola, Chinhui Juhn, and Carolina Villegas-Sanchez examine the effects of NAFTA on the gender wage gap. They argue three forces are at work: First, greater competition, brought about by a free-trade policy, could force efficiency, which decreases a firm's ability to pay men higher wages than equally competent women. Second, industrial shifts might favor women. Third, tariff reductions possibly encourage technology upgrades, again favoring women workers. To test these hypotheses, Aguayo-Tellez, Airola, Juhn, and Villegas-Sanchez decompose the overall increase in female employment and wage bill shares into between and within industry components. They then link these changes to tariff changes across sectors. From this analysis, they find women's relative wages in Mexico increased,

employment shifted favoring women, and more women were hired in skilled blue-collar jobs. Thus, NAFTA benefited Mexican women relative to men, and probably narrowed the overall wage distribution in Mexico.

Earnings dispersion is currently rising in the United States and elsewhere. One reason is the rising proportion of students dropping out of high school. A higher dropout rate widens earnings variance nationwide and exacerbates concerns about poverty. Motivating an individual to do better in high school has important ramifications. It raises a person's chances of going to college and succeeding better in the labor market. However, determining the factors that prompt an individual to do better in school has been elusive. In November 2005, anonymous donors promised to pay between 65 and 100 percent of college tuition for any Kalamazoo, Michigan public school student who got into college and maintained a 2.0 average. Obviously, admission to more demanding colleges required students to have better academic performance. In the next article, Timothy J. Bartik and Marta Lachowska report on school performance outcomes emanating from this "Kalamazoo Promise" quasi-experiment. Using difference-in-differences regression techniques, they compare the change in secondary school student outcomes across time. They find significant increases in student performance and a lower number of days students spend in suspension. The results are most notable for African Americans.

Analyzing the impact of earnings dispersion nationwide is difficult because nations are widely heterogeneous and change is slow. However, investigating dispersion on a micro-level can be more manageable and still lead to global implications. In the next article, Laura Arranz-Aperte analyzes how wage dispersion affects worker productivity using plant data for Finland. She postulates two possible effects: First, higher wage dispersion motivates workers to put out more effort in hopes they will be rewarded adequately, thus raising output. Alternatively, too high a wage dispersion reduces comradery, thus decreasing worker cooperation, which results in lower plant productivity. To test the relative strengths of these hypotheses, Arranz-Aperte utilizes 1990–2002 Finnish matched employer–employee data. She finds a significant positive relationship between intra-firm wage dispersion and output (sales per capita). This validates incentive based approaches to enhance productivity rather than fairness-type arguments.

Another method of inducing greater employee productivity is for a firm to steepen the slope of the tenure-wage profile. In the next article, John G. Sessions and Nikolaos Theodoropoulos derived a two-period efficiency wage model in which firms face a trade-off between the level of monitoring and the wage-tenure gradient. Using two cross-sections of matched

employer–employee British data with an instrument that exploits variations in monitoring costs across establishments, they find that steeper tenure compensation schemes require less monitoring, thus providing evidence that firms increase output by deferring pay. They conclude that agency considerations are an important driver of the wage-tenure profile.

Sometimes firms are forced to pay more because markets must compensate workers in dangerous jobs. However, a large number of studies have had great difficulties detecting compensating wage differentials. In the next article, Nikolaos Georgantzis and Efi Vasileiou take another approach. Instead of looking simply at monetary aspects, they examine job satisfaction. Holding wage constant, one can conclude that job attributes other than safety cause utility to be equalized, should job satisfaction be comparable between safe and dangerous jobs. Georgantzis and Vasileiou test this proposition. They use a switching regression technique adjusted for selectivity applied to a unique data set on 3,030 workers from France, Greece, the United Kingdom, and the Netherlands. They find that overall job satisfaction is not affected by the wage differential for dangerous jobs. Thus they argue that job attributes other than money might be important in understanding compensating differentials.

Obviously getting workers to be more productive is crucial to becoming a more competitive firm. In a purely theoretical article, Marco Guerrazzi derives a game-theoretic model in a two firm economy. Each firm competes for labor by increasing its wage offers to screen for high-quality workers. He derives three theorems. First, each firm increases its wage offer to follow its competitor. Second, this dynamic leads to a stable equilibrium. Finally, high unemployment equilibria lead to greater levels of effort.

Some unemployment is voluntary. Clearly receiving a wage offer below one's reservation wage induces a person to remain unemployed because one could have accepted, but did not. Crucial to this decision is how one sets his or her reservation wage. In the next article, Núria Rodríguez-Planas examines how employees might signal high productivity by setting reservation wages sufficiently high to lead to longer unemployment spells. In short, she argues that because high productivity workers know they are more likely to be recalled than low-productivity laid-off workers, they so signal their productivity through higher reservation wages. As such they remain unemployed longer. To test this hypothesis, Rodríguez-Planas uses the 1988–2006 Displaced Workers Supplement of the Current Population Survey. She compares the post-displacement earnings of laid-off workers, some of whom may be recalled by their old employer, to workers who lose their jobs due to a plant closure, and therefore cannot be recalled. She finds that for white-

collar workers, post-displacement earnings fall less rapidly with layoffs than for plant closings, thus supporting her thesis that high productivity workers signal their productivity through their unemployment duration.

Long-term unemployment can be costly, but these costs are difficult to measure because of endogeneity. If lower quality workers are more prone to layoffs, then lower subsequent wages might be caused by innate lower quality, rather than layoff. Similarly, if poor health induces separations, then poor health might be a cause instead of an effect of job separation. Isolating the effects of long-term unemployment is important to understanding its effects on individuals and the economy. In the next article, Kenneth A. Couch, Gayle L. Reznik, Christopher R. Tamborini, and Howard M. Iams use the 1984 Survey of Income and Program Participation (SIPP) data linked to social security longitudinal earnings, disability, and mortality data to get at the costs of long-term unemployment. They examine changes in earnings, disability benefits, and mortality through the year 2000 for men who experienced prolonged joblessness lasting as long as three years around the time of the 1980–1982 recession, compared to changes for men who were employed during that time period. To get at endogeneity, they contrast these effects for involuntary and voluntary joblessness, as well as for those with and without preexisting health problems. Noteworthy is the magnitude of losses facing the long-term unemployed.

As with past volumes, we aim to focus on important issues and to maintain the highest levels of scholarship. We encourage readers who have prepared manuscripts that meet these stringent standards to submit them to Research in Labor Economics (RLE) via the IZA web site (<http://rle.iza.org>) for possible inclusion in future volumes. For insightful editorial advice, we thank Joan Brownell Anderson, Rodney J. Andrews, Keith A. Bender, David J. Berri, Petri Böckerman, Sylvie Démurger, Donghun Cho, Polona Domadenik, Robert Fairlie, Shuaizhang Feng, Alfonso Flores-Lagunes, Gaia Garino, John T. Gilles, Xiaodong Gong, Oecon Ola Honningdal Grytten, Björn Gustafsson, Luojia Hu, Mohamed Jellal, Peter Kuhn, Marc P. B. Klemp, Fidan Ana Kurtulus, Håkan Locking, Mauro Mastrogiacomo, Pierre-Carl Michaud, Dongshu Ou, Matloob Piracha, Nancy Qian, Ray Rees, Francois Rycx, Martin Salm, Pia Sophia Schober, Håkan Selin, Judith Scott-Clayton, Xinzheng Shi, Steven Stillman, James X. Sullivan, Laura Turner, Raymundo M. Campos Vazquez, Le Wang, Yaohui Zhao, Jeffrey Zax, Junfu Zhang, Zhong Zhao, and Thomas Zwick.

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