Raising Wages through Sectoral Bargaining

Alí R. Bustamante

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About the Author

Alí R. Bustamante is the deputy director of the worker power and economic security program at the Roosevelt Institute, where he focuses on how public policy can structure markets around both economic and social value and empower Americans through the provision of public goods and stronger labor protections. Prior to joining Roosevelt, he served as chief economist at the Louisiana Workforce Commission, senior research associate at the Southern Economic Advancement Project, and as faculty at Florida International University, the University of New Orleans, and Loyola University New Orleans. Dr. Bustamante earned a BA and PhD from the University of Miami, where he specialized in political economy.

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Introduction:
The Need for Progressive Wage-Setting Mechanisms

The erosion of the real value of the minimum wage in the United States was a problem before the pandemic and has only gotten worse during recent years. Despite high rates of wage growth over the past two years, the stagnant federal minimum wage and declining rates of union density have contributed to the suppression of average real wages for many Americans. In light of these trends, policymakers should look to sectoral bargaining as a critical tool in raising wage floors and ensuring that workers are fairly compensated.

American workers' compensation is fundamentally shaped by two legal frameworks: minimum wage laws and collective bargaining rights. The inadequacies and limitations of existing labor laws have played a crucial role in depressing wage growth. The failure to regularly adjust the federal minimum wage, coupled with the inadequate expansion of state-level minimum wages, has led to a substantial erosion of real wage floors. At the same time, low levels of union membership have taken collective bargaining off the table for most workers. Without the collective power of unions, individual workers face significant challenges in negotiating for better pay and conditions, exacerbating the wage stagnation problem.

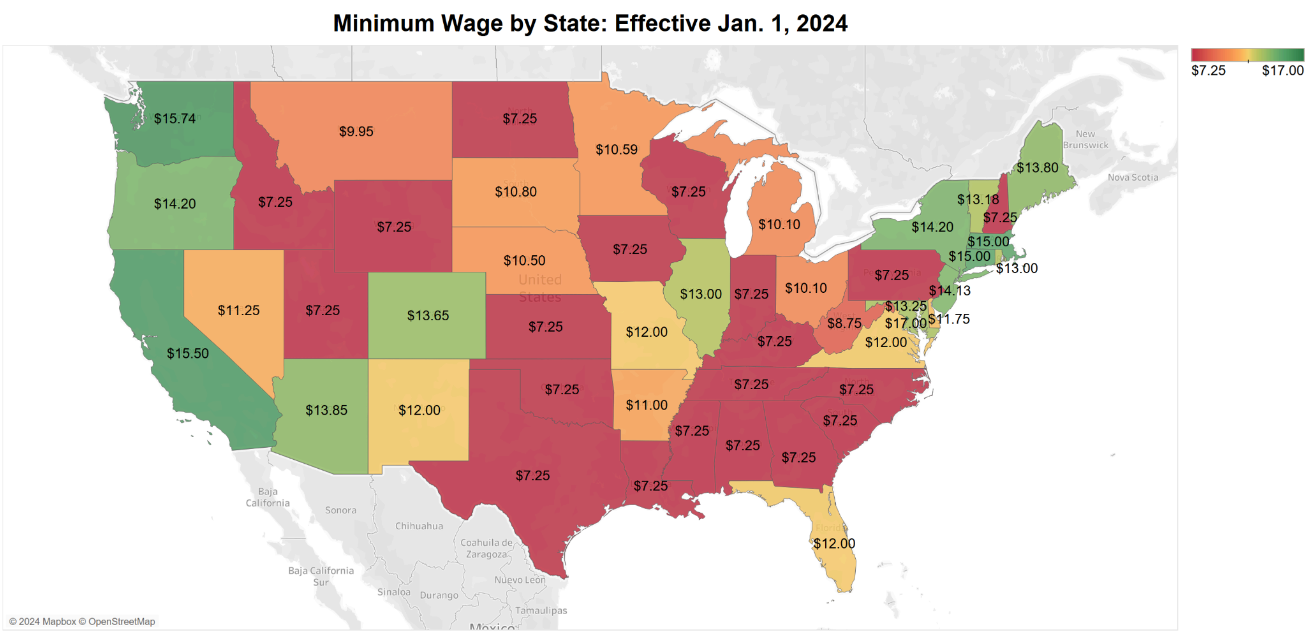
To reverse this trend, there is a pressing need for reforms that include regular adjustments to the federal minimum wage and stronger support for collective bargaining. In addition, sectoral bargaining legislation can offer a nuanced and targeted approach to wage setting where wages have eroded the most.

Stagnant Minimum Wage and Weakened Unions Depress Wage Growth

Minimum wage laws establish the wage floors for the majority of American workers, dictating the lowest wage rate employers can legally pay. The federal minimum wage, set by the Fair Labor Standards Act of 1938, currently stands at $7.25 per hour. This rate, which was established in July 2009, has not kept pace with inflation or productivity gains, leading to a significant real wage erosion (Baker 2020).

Since 2009, the value of the $7.25 federal minimum wage has eroded by 29.6 percent to $5.10 because of inflation. The majority of the federal minimum wage's erosion (16.1 percent) occurred prior to the pandemic, but the inflation triggered by pandemic supply shocks—peaking in July 2022—deepened the rate of erosion. Despite the decline in the purchasing power of the federal minimum wage, in 2022, 1 million workers were reported to earn wages at or below the federal minimum—about 1.3 percent of all hourly paid workers (BLS 2023b). The wage floor set by the federal government is salient because 20 states adhere to the federal standard in setting their own minimum wages (figure 1).

Figure 1: Minimum Wage by State



US Department of Labor. Author's calculations. Alí R. Bustamante, PhD. Roosevelt Institute.

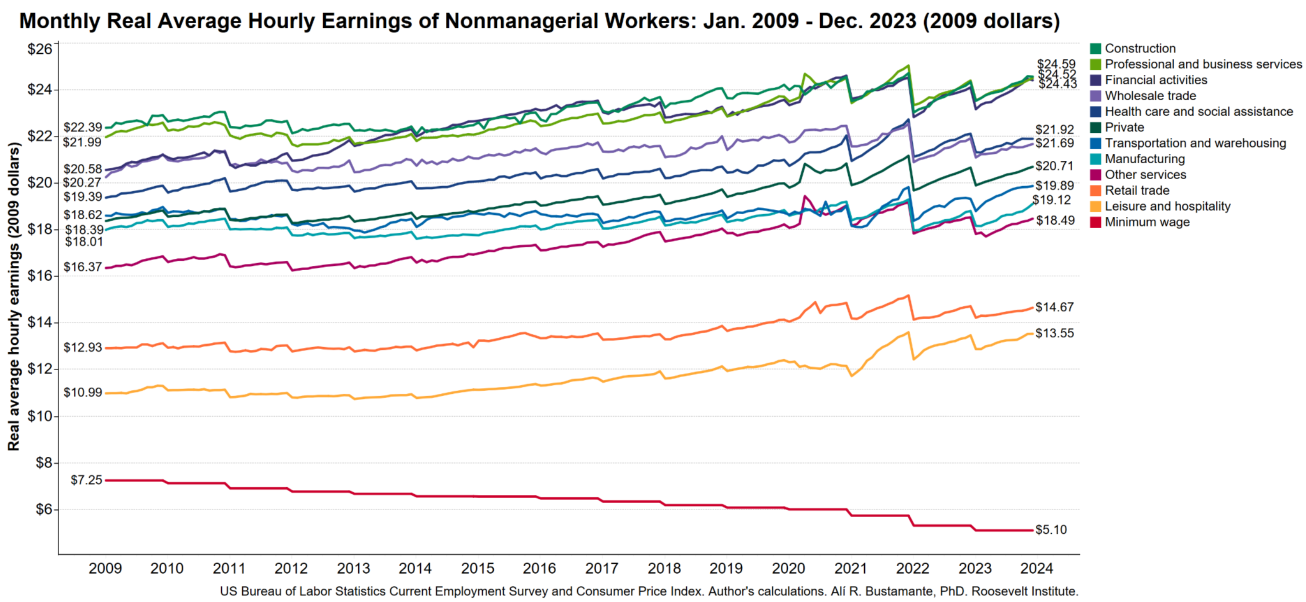
Additionally, in the US, the right to form a labor union and collectively bargain over wages and labor conditions is a foundational labor right. Unions have been instrumental in advocating for higher wages and better working conditions (Treasury 2023). However, despite enjoying high levels of public support, union membership has drastically declined from covering about 20.1 percent of workers in 1983 to standing at just 10.1 percent as of 2022 (BLS 2023a). The decline of union density in the US during the past 40 years is the outcome of concerted efforts by American corporations to undermine collective bargaining and resist union formation through the exploitation of weaknesses in labor laws (McNicholas et al. 2023).

This decrease in union representation has been broad in scope. Between 1983 and 2019, the share of workers covered by a union contract declined by more than half in the construction, retail trade, wholesale trade, and transportation and warehousing industries (BLS 2023a). During this same period, union coverage of manufacturing, communication, and mining workers declined by more than 70 percent. This decline has significantly weakened the influence of workers in wage negotiations—contributing to the stagnation of average real wages—and diminished their access to labor protections and job security.

Wages Are Depressed across Many Sectors

Currently, 57.8 million Americans are employed in five industries where the average hourly wage is below the national average of $20.71 (figure 2). The leisure and hospitality industry employs 16.8 million Americans while retail trade employment is 15.5 million, manufacturing employment is 13 million, and the transportation and warehousing and other services industries collectively employ 12.5 million.

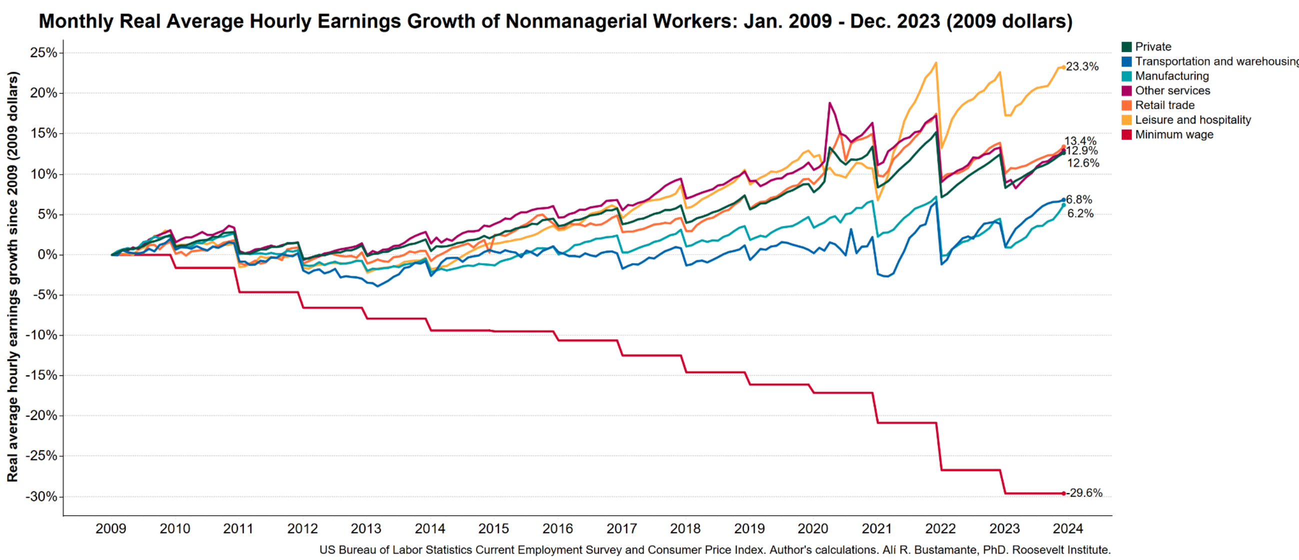
Figure 2: Monthly Real Average Hourly Earnings of Nonmanagerial Workers: Jan. 2009–Dec. 2023 (2009 Dollars)



Data show that real wage growth in these lowest-paid industries is generally at or below the private-sector average. Prior to the pandemic, between January 2009 and February 2020, private-sector real wages grew by 8.3 percent, yet wage growth in the manufacturing and transportation and warehousing industries was 3.7 percent and 0.9 percent respectively.

Most recent data for December 2023 show that private-sector wages have grown by 12.6 percent since January 2009 and that the manufacturing and transportation and warehousing industries continue to lag (figure 3). The leisure and hospitality industry has experienced the highest wage growth, at 23.3 percent, while wages for the retail trade and other services industries grew by 13.4 and 12.9 percent respectively, near the private-sector average. The data suggest that wages at the lowest-paid industries will remain low because they fail to experience above-average rates of growth, even with a historically tight labor market. This evidence calls for the introduction of policies that directly raise wages for workers in these industries through either a strong federal minimum wage or higher industry-wide wage floors.

Figure 3: Monthly Real Average Hourly Earnings Growth of Nonmanagerial Workers: Jan. 2009–Dec. 2023 (2009 Dollars)



Sectoral Bargaining Supports Wage Growth in European Countries

In the US, collective bargaining agreements typically cover only a single company. This limitation has significant implications for the breadth of wage negotiations and the ability of collective bargaining agreements to shape broader labor rights. In contrast, sectoral bargaining sets employment standards for entire industries or occupations by allowing worker organizations to represent both union and nonunion workers across multiple employers in an industry in their collective bargaining of labor conditions. This approach ensures that wage floors are not limited to individual firms or subsets of workers but are applied across sectors, providing a more uniform and equitable wage structure. This form of bargaining is prevalent in countries like France, Italy, the Netherlands, Portugal, and Spain, and has contributed to significant improvements in workers' wages at both the average and the bottom rung of wage earnings.

In countries that implement sectoral bargaining, worker organizations and employers engage in collective bargaining similar to unions and employers in the US. However, sectoral bargaining tends to occur every year as opposed to just when a collective bargaining agreement is about to expire. Additionally, while American unions and firms can negotiate drastically different terms of compensation and working conditions, regularly held sectoral contract negotiations in European countries tend to result in proportional raises in all wage floors—irrespective of industry or occupational group. These increases reflect average productivity growth, the growth in value added per worker among covered firms. Importantly, these adjustments also compensate workers for past inflation, ensuring that wages keep pace with the cost of living.

Furthermore, in the US, collective bargaining agreements tend to set pay scales for all workers in a firm, while sectoral bargaining establishes wage floors and allows employers discretion in paying wage cushions—the wage employers are willing to pay that is above the wage floor—to individual workers. These cushions vary based on negotiations between individual workers and their employers, considering factors such as experience, education, and the productivity of the firm.

Employers have considerable discretion in setting wage cushions, contributing to cross-sectional variation in wages within the same collective bargaining agreements. This flexibility ensures that while a basic standard is maintained across the sector, individual performance and firm capabilities are also recognized in wage determinations. Portugal's data exemplify the impact of sectoral bargaining in most countries, where a typical worker receives a 20 percent wage cushion over the wage floor (Card and Cardoso 2021). This wage cushion tends to be larger for older, better-educated workers, and in higher-productivity firms. Such trends highlight the flexibility within the sectoral bargaining framework, allowing for wage differentiation based on worker and firm characteristics.

The adjustments in wage floors, while beneficial to raising the lowest wages, do lead to some compression of wage cushions. However, this effect is generally seen as a move toward greater wage equity, reducing excessive wage disparities within sectors and fueling average real wage growth. The system strikes a balance between setting industry-wide standards and allowing for individual wage negotiations. As a result, European workers in countries practicing sectoral bargaining have experienced significant and consistent wage growth over the past three decades, a testament to the efficacy of this approach (Card and Cardoso 2021).

Sectoral Bargaining Raises Wages without Employment Loss

In the realm of labor economics, the discussion around wage growth often intersects with concerns about potential employment losses. Sectoral bargaining can drive wage growth without sacrificing employment. In sectoral bargaining, the average pass-through rate of wage floor increases is approximately 50 percent (Card and Cardoso 2021). This means that half of the increase in wage floors is passed through to workers, particularly benefiting those with smaller wage cushions. The remaining half is absorbed by reductions in wage cushions.

The influence of wage floor increases on wage cushions mirrors the spillover effects of a minimum wage hike. Research indicates that minimum wage increases significantly affect workers earning close to the new minimum, but the impact diminishes for those earning substantially above it (Cengiz et al. 2019). Despite the partial absorption by wage cushion compression, these increases still enhance workers' base wages and total salaries. Additionally, because wage floors are largely determined by increases in firm-specific productivity, as measured by changes in real value added per worker, increases in wage floors tend to have a pronounced positive effect on employment growth. This indicates that under sectoral bargaining, productivity growth can facilitate both wage increases and employment expansion.

Furthermore, research underscores that when wages are set by employers, the employment effect of minimum wage increases is minimal. This finding is crucial, as it suggests that employer discretion in wage setting, a feature inherent in sectoral bargaining, can contribute to a balanced approach where wage growth does not come at the expense of employment. While there might be a potential for a small negative impact, employment generally remains unaffected by higher wage floors.

Sectoral bargaining presents a viable model for achieving wage growth without incurring significant employment losses. By allowing for a 50 percent pass-through of wage floor increases and the strategic use of wage cushions, this approach manages to elevate base wages while maintaining employment stability. The key lies in balancing the standardization of wage floors with the flexibility of wage cushions, ensuring that the benefits of increased productivity are shared among workers without destabilizing employment.

Nevertheless, this does not suggest sectoral bargaining is a cure-all for labor market inequities. Indeed, while wage cushions provide employers with wage-setting flexibility, they also can and do contribute to intragroup and intergroup pay inequality. This flexibility plays a substantial role in the many wage gaps seen in the labor market, influenced by factors like gender, education, age, and employer profitability. Additionally, mean wage cushions within collective bargaining agreements are more responsive to firm profitability. This responsiveness can counteract the equalizing effect of wage floors within agreements, reintroducing some degree of wage variability based on firm performance.

Conclusion:

The Case for Sectoral Bargaining in the United States

The concept of sectoral bargaining, widely proposed but not practiced in the United States, presents a transformative opportunity for reshaping the wage landscape (Andrias and Rogers 2018). Sectoral bargaining could supplement existing minimum wage and collective bargaining frameworks and address some of their shortcomings. The federal minimum wage, intended as a baseline reflecting the average productivity of all workers, has not kept pace with worker productivity over the past 14 years. This stagnation has contributed to widening income inequality and diminishing purchasing power for low-wage workers. Sectoral bargaining could address this gap by ensuring that wage floors in various sectors align more closely with the actual productivity and economic realities of those industries. These sector-specific wage floors would be more attuned to the unique economic conditions and productivity levels of different industries, providing a more targeted approach to wage increases that have gone largely unaddressed by the national minimum wage.

States like California, Colorado, New Jersey, and New York have introduced the use of wage boards or councils in sectors where workers are particularly vulnerable to exploitation. These bodies, which bring together representatives from labor, management, and the public, set wages and working conditions in specific industries. Their success offers a model for how sectoral bargaining could be implemented on a broader scale, providing a template for the federal government to follow.

The federal government is well positioned to facilitate the creation of wage boards, using its prevailing-wage-setting power in industries where federal investments are concentrated. Additionally, the government can support the voluntary formation of wage boards in other sectors, encouraging "high-road" employers to engage in fair wage practices. This approach would enhance wage equity while also incentivizing industries to adopt sustainable and responsible labor practices.

Implementing sectoral bargaining in the United States offers a promising avenue to addressing long-standing wage inequities and the disconnect between wages and productivity. By tailoring wage floors to specific sectors and leveraging the role of the federal government in facilitating wage boards, the US can take significant steps toward creating a fairer and more competitive labor market. This shift would not only benefit workers through higher wages but also contribute to a more balanced and just economy.

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