Global Economy

Why is the share of labour in total income falling?

Expansión (Spain)

Luis Díez

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It seems that in the age-old battle between labour and capital the latter has been gaining ground recently. In the majority of advanced economies the share of national income going to wage and salary earners is falling. For example, in the United States in the decades leading up to 1980 the share of wages represented about 60% of national income. Yet in the early 80s this figure began to gradually come down and presently stands at about 54%. This decline has involved the annual transfer of several billion dollars of income from labour to capital, and this may give cause for concern, since historically the less income has been in the hands of workers, the greater the risk of growing economic inequality and social instability.

The growing portion of income taken by owners of capital, ranging from owners of major corporations through to the self-employed, savers large and small, and home owners, is something of a mystery, since for many years workers’ slice of the cake had remained practically unchanged. However, this “bit of a miracle” as Keynes himself described it came to an end in the 1980s, and since then the share of wages in total income has fallen in the majority of developed economies.

Nonetheless, although the general trend is downward, a more detailed analysis of developments by branch of activity shows that the phenomenon is not common to all sectors. For example, the share of wages in services has seen appreciable growth in the US, Germany and Spain, in contrast with its decline in other sectors.

What is the reason for the fall in labour’s share of income? There are several possible explanations. Among those most frequently advanced are the decline in workers’ bargaining power as a consequence, for example, of lower trade union membership; offshoring in the most labour-intensive sectors to countries such as China, India and other emerging economies; and the rise of giant, heavily capital-intensive global technology companies able to create value without having to make so much use of labour in relative terms.

A recent BBVA Research publication looks at another explanation: the development of technological improvements such as the automation of production processes, which have led to a substantial fall in the relative price of investment and capital goods relative to labour in the past few decades. The relative cheapening of machinery and capital goods has led businesses to acquire capital instead of hiring workers, reducing the share of wages in national incomes.

As is logical, the results of this study show that this process of substitution differs widely from one business sector to another. By way of illustration, one can imagine that in the automotive industry, with its numerous routine tasks, a robot might be used to assemble the various parts of a vehicle more efficiently than a person. On the other hand, in a restaurant or an office a machine cannot replace a person so easily, given that for example interpersonal skills in dealing with customers or cognitive skills in interpreting results come into play. Service companies therefore find it harder than companies in other sectors of the economy to incorporate the technological advances associated with capital goods and replace manpower.

The fall in the relative price of investment and capital goods is very unlikely to be the only reason behind these trends. However, this decline, and technological developments, look set to continue in the near future and point to the need for more and better investment in human capital focused on promoting skills that are complementary to the new advances.

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ENQUIRIES TO:
BBVA Research: Calle Azul, 4 Edificio La Vela, Floors 4 & 5 28050 Madrid, Spain. Tel. +34 91 374 60 00 y +34 91 537 70 00 / Fax (+34) 91 374 25 - bbvaresearch@bbva.com www.bbvaresearch.com