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INTER-SECTORAL LABOUR MOBILITY AND THE WAGE GAP: THE DIFFERENCE IN MATCHING EFFICIENCY

Abstract:

The wage gap between sectors have been substantial and even increasing over the last two decades in advanced economies. Nevertheless, labour mobility from the low wage sector such as retail service to the high wage sector such as ICT industry has been sluggish, with workers tending to puzzlingly cluster in the low wage sector. This situation accordingly worsens the wage inequality between sectors. This observation hints towards the existence of barriers or frictions to the upward movement of labour, and multiple evidence of frictions to labour mobility and their recent increase has been explored. To discover the relationship between inter-sectoral labour mobility and wage differential, it is necessary to identify the source of labour market frictions and assess its role in labour market dynamics.

One convincing and probable source of frictions is the difference in job matching efficiency between sectors. From the US labour market, we can see that it takes much longer to fill a job vacancy in the high wage sector than in the low wage sector. This duration gap is largely attributed to the difference in matching efficiency between sectors rather than the difference in market tightness. More interestingly, asymmetric matching efficiency originates from unbalanced sector-specific productivity progress.

A two-sector search and matching model, which is equipped with the different matching efficiency mechanism, can account for current labour market distortions well by showing that the productivity-driven matching efficiency gap triggers the wage differential, labour misallocation and further the welfare loss. And its deterministic model economy fits the actual data of the upward trend in wage gap and the downward trend in labour share of the high wage sector since the 2000s. What is more, the model demonstrates that a high wage sector biased shock amplifies the wage gap and even drags its labour share down, which a normative frictionless framework cannot encapsulate.

The analyses and arguments put forward in this paper summarise that the matching efficiency gap which acts as friction impedes a seamless inter-sectoral labour mobility and thus impacts upon the labour market negatively in a way that widens the wage gap and distorts labour allocation. Such results suggest that a reduction of the difference in matching efficiency via a balanced productivity progress across sectors might improve labour market distortions and even increase the welfare of the economy. (382 words)

Keywords:

Matching efficiency, Two-sector search and matching model, Wage gap, Inter-sectoral labour mobility, Labour market friction