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Detrimental Effects of Uniform Wages and Collective Action in Reciprocal Labor Relations

We study the effect of uniform wages and collective action on the performance of laboratory firms with an employer and twelve employees. In our gift exchange setting, the employer first offers a fixed uniform wage and then the employees choose effort levels. We replicate the finding that uniform wages lead to a downward spiral of decreasing average effort levels, wages, and firm output, all falling significantly below the corresponding values in firms with individually differentiated wages. We investigate whether the introduction of collective action structures that are commonly found in unionized labor can stop or reverse the downward spiral of wage and effort choices, thus, improving the efficiency of the firm. Neither the possibility to coordinate effort choices via non-binding communication, nor the option to strike leads to an enhanced firm performance with higher effort and wage choices. Enabling the employer to terminate a selected labor relationship after each period of financial distress leads to wage and effort choices that are on average indistinguishable from the corresponding values in firms with differentiated wages. But, the performance of the firms with uniform wages and a termination possibility remains significantly below the performance of the firms with differentiated wages.