



Natural groups and economic characteristics as driving forces of wage discrimination



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ABSTRACT

We investigate whether the origin of an employee provides different motives for wage discrimination in gift-exchange experiments with students and migrant workers in China. In a lab and an internet experiment, subjects in the role of employers can condition their wages on the employees' home provinces. The resulting systematic differences in wages can be linked to natural groups and economic characteristics of the provinces. In-group favoritism increases wages for employees who share the same origin as the employer, while an increased probability of being matched with an employee with a different ethnicity reduces wages. Furthermore, wages in the laboratory increase with the actual wage level in the employees' home province. Nevertheless, employees' effort is not influenced by these variables; only the wage paid in the experiment influences effort.

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1. Introduction

This paper explores whether the origin of an employee provides different motives for wage discrimination. To this end, we conduct two stylized gift-exchange experiments with students and migrant workers in the PR China. Students in the role of employers can condition wages on the employees' origin, while students and migrant workers in the role of employees choose effort levels based on wages. We augment the collected datasets with complementary data on the characteristics of Chinese provinces. This combination of lab and field data demonstrates three separate, but simultaneously present, effects on wages levels: First, wages in the experiments are influenced by actual wage levels in employees' home provinces, second, in-group favoritism increases wages for employees with the same origin as the employer, and third, ethnic diversity in the employees' home provinces decreases wages.

Previous research has shown that discriminating behavior can be conditioned on such diverse characteristics as gender (e.g., Neumark et al., 1996; Kuhn and Shen, 2013), race (e.g., Bertrand and Mullainathan, 2007; Pager et al. 2009; Zussman, 2013), age (e.g., Büsch et al., 2009; Riach and Judith, 2010), and even beauty (e.g., Mobius and Rosenblat, 2006; Wilson and Eckel, 2006).

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Several potential reasons for discriminating behavior have been identified in the economic literature. While discrimination can be taste-based (Becker, 1957), differential treatment in labor markets can also be based on economic reasoning and differences in the actual or expected productivity of workers (Phelps, 1972). Employers might even offer discriminating payment schemes for identical work to provide proper incentives within teams (Winter, 2004; Goerg et al., 2010). Furthermore, varying perceptions of fair-wages among otherwise identical workers can result in wage differences. Two workers with different reference groups will consider different wage levels as fair when the perception of what constitutes a fair wage depends on the wages paid to the workers in these reference groups (Akerlof and Yellen, 1990). A similar argument can be put forward based on efficiency wages: if workers from one group have worse outside options than the others they are willing to accept lower wages for the same work or the same wage for more work hours. Kuhn and Shen (2014) propose that this as an explanation why employers in the PR China prefer migrant workers over comparable local workers as they expect higher levels of work hours for the same wage.

A different kind of motivation for discrimination has been identified in the social psychology literature. Broad evidence shows that group identity may lead to the preferential treatment of in-group members and discrimination against out-group individuals – not necessarily through hostility, but through indifference (Sherif et al. 1961; Tajfel and Turner, 1979; Halevy et al., 2008). In economics, Akerlof and Kranton (2000) introduced social identity as an important driver of economic behavior and proposed a utility function according to which individuals aim to behave appropriately given the social group to which they belong.¹ As the group affiliation defines part of one's identity it also influences the behavior towards group members and the outside. Thus, identity can provide the microfoundation for the previously discussed taste-based discrimination (see Akerlof and Kranton, 2000, p. 732).

The importance of group affiliation has been demonstrated for naturally occurring groups defined by such diverse features as race (Fershtman and Gneezy, 2001; Chen et al., 2014), gender (Charness and Rustichini, 2011), army platoons (Goette et al., 2006) and city districts (Falk and Zehnder, 2013). Furthermore, even artificial groups generated with the minimal-group paradigm (Tajfel and Turner, 1979) lead to in-group favoritism with potentially increased cooperation in social dilemmas (Yamagishi and Kiyonari, 2000; Eckel and Grossman, 2005; Chen and Li, 2009) and more efficient coordination in the minimum effort game (Chen and Chen, 2011).

This paper contributes to the literature on natural identities and discrimination by demonstrating that the previously discussed motives for discrimination are not mutual exclusive. Instead they can be present at the same time and be based on the same piece of information. In our paper, employers only know the employees' origin resulting in wage discrimination motivated by different characteristics of the home provinces. First, we observe in-group favoritism in the form of higher wages for employees with the same origin. Second, discrimination is also based on the ethnical composition in the employees' home province and employers tend to choose lower wages for workers from provinces with larger shares of ethnic minorities. Third, we show that, in addition, wages in our experiments are positively correlated with average wages paid in the home provinces. Furthermore, these different characteristics influence wages independent of each other. Thus, our paper is one of few experimental papers which successfully demonstrate the occurrence of discrimination based on multiple but simultaneously present motives. One notably exception is the work by Falk and Zehnder (2013). In their city wide trust game, first movers condition their trust on the residential districts of second movers in the city of Zürich. The exhibited trust levels differed systematically between the districts of Zürich – higher socio-economic status led to more trust and, for subjects from the same district, in-group favoritism in terms of higher trust was observed. In our experiments, we apply a similar methodology in the context of a stylized employer–employee relationship, however decisions are not conditioned on districts of a city, but on provinces of a whole country.

The remainder of the paper is organized as follows: In Section 2, we discuss the experimental design. This includes the description of the modified gift-exchange game, the implementation of the experiments with students and migrant workers as subjects, and the complementary data on the characteristics of the Chinese provinces. Section 3 presents behavioral hypotheses, Section 4 reports our results on the determinants of employers' wage discrimination and employees' effort provision. Finally, Section 5 discusses the implications of our results and concludes the paper.

2. Experimental design

We investigate how employers discriminate employees in two gift-exchange experiments in which wages are conditioned on the employees' home provinces. Using additional field data, we identify particular characteristics of the provinces on which these wages are based on.

The first experiment is a laboratory experiment conducted at the Shanghai Jiao Tong University (PR China) with students deciding in the role of employers and migrant workers in the role of employees.² The second experiment is an internet experiment at the University of Nottingham Ningbo (PR China) with students deciding in both roles – as employers and employees. The second

¹ It is worth mentioning that the implications of social identity go beyond discrimination. It applies to most situations in which people behave as they think they should. Thus, social identity provides insights into topics such as the division of labor in households, education, monitoring at the workplace (Akerlof and Kranton, 2000, 2002, 2008), as well as, discounting and risk preferences (Benjamin et al., 2010).

² In our paper we refer to workers who migrated to Shanghai from other provinces as migrant workers. In the labor literature on China the term migrant worker usually refers to workers migrating from rural areas to urban areas even if they move within a province.

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