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RISING PROFIT SHARES, FALLING WAGE SHARES

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Rising Profit Shares, Falling Wage Shares

DESPITE A PROLONGED PERIOD of economic expansion, income inequality is growing in Canada (Statistics Canada 2007, Green and Milligan 2007, Yalnizyan 2007). At an intuitive level, Canadians know economic growth is not translating into widespread benefits. In fact, 65% of Canadians told Environics Research they feel they are not benefiting from economic growth — that a greater share of economic growth is going to the richest among us (Canadian Centre for Policy Alternatives 2006).

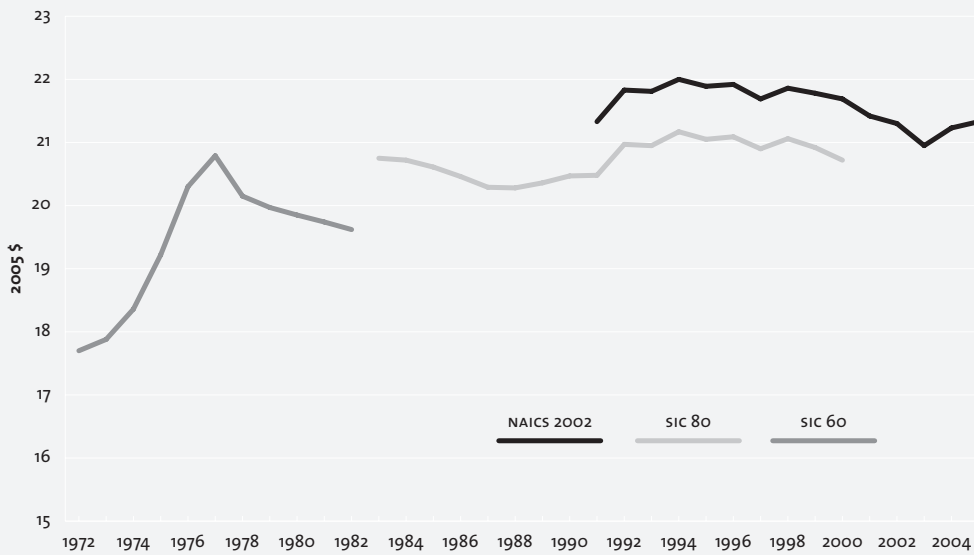
This paper addresses Canada's growing income inequality trends within the context of a growing economy and improved productivity. It does so by focusing on wages and salaries. Since Canadians derive their livelihood principally from wages and salaries, what happens to wages and salaries plays an important role in the overall problem of income inequality.¹

In this report we find that the benefits of economic growth have not been widely reflected in Canadians' paycheques over the course of a generation. Canadians' average real wages — which are wages adjusted for inflation — have not increased in more than 30 years. Real wages have decreased for the lowest paid workers — those earning minimum wage. In the context of a growing economy, stagnant average real wages have led to a decreased share of the gross domestic product (GDP) going to workers, with an increased share going to corporate profits. This represents a significant break from trends established in the post-war era and the trend is showing no signs of letting up.

REAL WAGE STAGNATION IN A GROWING ECONOMY

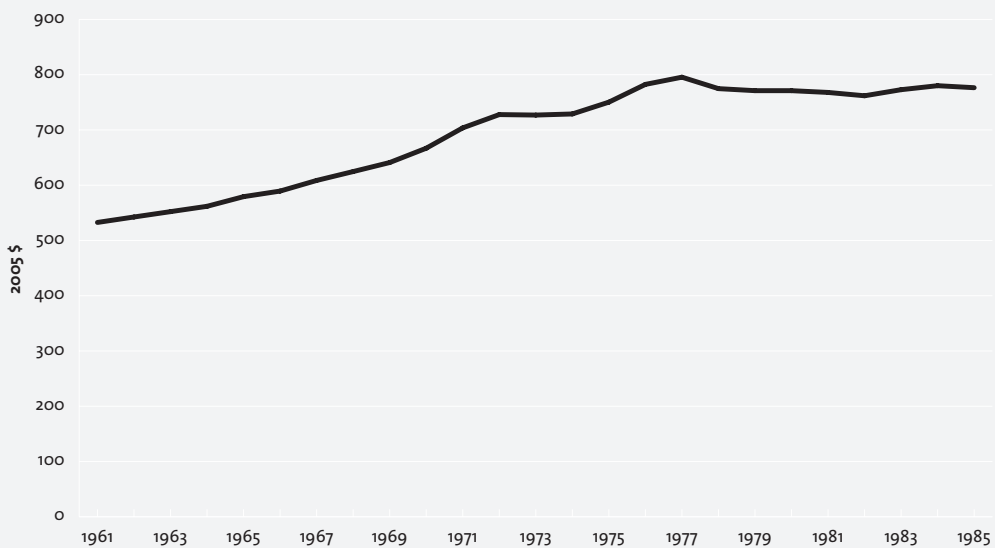
The Canadian economy has enjoyed a prolonged period of economic prosperity. Canada's economy grew by 72% between 1975 and 2005, in real per capita terms.² Over the same time period, labour productivity (measured as GDP/hour) grew by

CHART 1 Average Hourly Wage Rate Adjusted for Inflation
Various Industry Composites



Source Statistics Canada, CANSIM database, tables 326-0002 and 281-0022; and data obtained upon request.

CHART 2 Average Weekly Wages Adjusted for Inflation

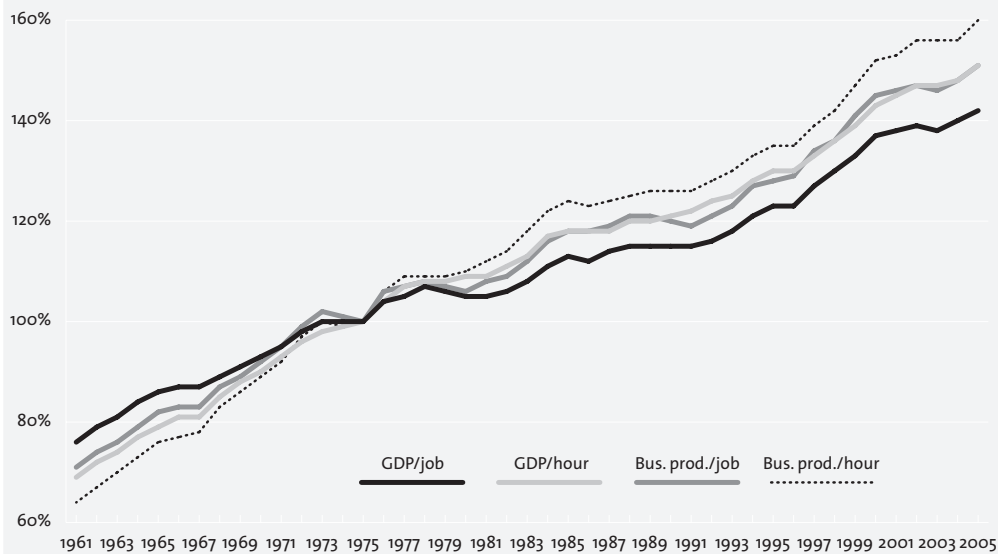


Source Statistics Canada, CANSIM database, tables 281-0019 and 326-0002.

51% (see below). A growing economy with rising labour productivity seems like it would translate into rising real wages. But this has not been the case.

The discussion of long-term real wages and salaries is complicated by the fact that Statistics Canada changed the way it categorizes jobs and industries over time. While there is no continuous data that spans the entire historical period we examine, unmistakable trends are still apparent. Chart 1 depicts Canadian workers' real

CHART 3 Average Labour Productivity in the Total Economy and the Business Sector (1975=100)



Source Own calculations with data from the Centre for the Study of Living Standards.

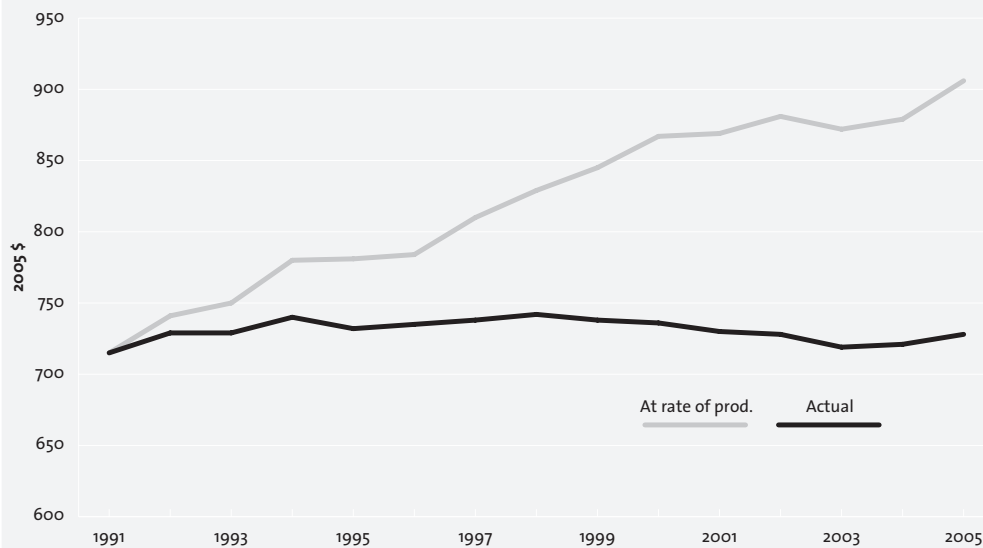
hourly wages and salaries between 1972 and 2005. The breaks on Chart 1 represent the points where Statistics Canada changed its method of categorizing the data.³ Despite the breaks in the data series, it is clear that Canadian workers' real hourly wages grew steadily in the early 1970s but those wages have since flattened.⁴ Astoundingly, after steady increases in Canadian workers' real hourly wages between 1972 and the late-1970s, their real wages have been stagnant for 30 years running.

This 30-year stagnation of Canadian workers' real wages is dramatically at odds with previous historical experience. To get a sense of what happened to workers' real wages before the 1970s, we looked at the continuous data series for real average weekly wages collected by Statistics Canada between 1961 and 1985 (Chart 2). From 1961 until the late-1970s, it was the norm for workers' real wages to rise continuously. By the late-1970s until 1985, the stagnation of real average weekly wages kicked in.

The stagnation of workers' real average wages is remarkable, given that Canadian workers are increasingly productive. Chart 3 displays four different measures of productivity — all four have been steadily rising for over 40 years. As we discuss in our forthcoming paper, most economic models would predict that real wages rise as productivity rises. But it is evident that rising productivity is not generating a commensurate rise in real wages. A stagnation of workers' real average wages despite their rising productivity is a powerful indictment of the promise that a growing economy — and increased productivity — will produce benefits widely shared by the majority of Canadian workers. It simply isn't happening.

This disconnection between improved worker productivity and real wages has immense ramifications. Consider Chart 4, where we show the actual average weekly wage level with overtime, adjusted for inflation, of all Canadian workers from 1991 to 2005. In addition, we have constructed what the average weekly wage *would have*

CHART 4 Comparison of Weekly Wage Levels with Overtime for All Workers Adjusted for Inflation



Source Centre for the Study of Living Standards; Statistics Canada, CANSIM database, table 281-0027.

been if workers' wages had fully reflected their improved average productivity. If Canadian workers had earned real wages that rose in proportion to their productivity increases between 1991 and 2005, their incomes would have been \$200 higher each week in 2005 (in 2005 dollars). Canadians who work full-time for a full year⁵ could have been receiving at least \$10,000 more in average real pay in 2005.

While average real wages are stagnant, it doesn't mean all workers had their real wage frozen. Real wages increased in some industries and decreased in others. For example, between 1983 and 2005 the hourly wage of employees in finance, insurance, and real estate sectors increased by 15–20%, while workers in the transportation sector experienced a loss of 16–17%.⁶

Since average real wages are constant, if there are "winners" (those with real wage increases) there must also be "losers" (those with real wage decreases). While there are limitations with the availability of data, we can illustrate this point with average hourly wage data available between 1997 and 2005. We divided the average hourly wages into two groups: the more highly paid hourly workers (those with average hourly wages that are above average) and the lower paid hourly workers (those with average hourly wages that are below average). The higher paid hourly workers experienced a real increase of 5.74% on their paycheques. In 1997 they earned \$23.32 an hour; by 2005 they were earning \$24.46 (all dollar amounts expressed in 2005 dollars).⁷ Earnings for the lower paid hourly workers went from \$14.87 an hour in 1997 and dropped slightly to \$14.75 in 2005 — a decline of 0.53%. It's even worse for those at the very bottom end of the income spectrum. After adjusting for inflation, the average provincial minimum wage has decreased from \$9.14 to \$7.32 between 1976 and 2006 in terms of 2006 dollars (CUPE 2006). Workers earning minimum wage are experiencing real wage decline.

WHAT DO STAGNANT WAGES MEAN FOR THE DISTRIBUTION OF INCOME?

Canada's economy has been growing but average real wages have not. So where are the benefits of economic growth going? To understand how income is being distributed in the economy, we look at the ways Canada's GDP is divided according to how various groups in the economy earn their income (e.g. corporations earn profits, workers earn wages and salaries, etc.).⁸

Statistics Canada provides a classification system that is used to explore distribution issues. However, we have elected to make a few changes to the categories of that classification system in order to focus on trends related to wages and profits. These changes are discussed in detail in our forthcoming paper.⁹

After making these modifications — for example after subtracting taxes from GDP — we are left with what we call the “remaining economic pie”, the great majority of which is divided between workers as wages and salaries and corporations as profits.¹⁰ We focus on two particular shares of income: the proportion of this remaining economic pie earned by Canadian workers through wages and salaries¹¹ (referred to as “the wage share”) and the proportion going to corporations in the form of profits (referred to as “the profit share”).

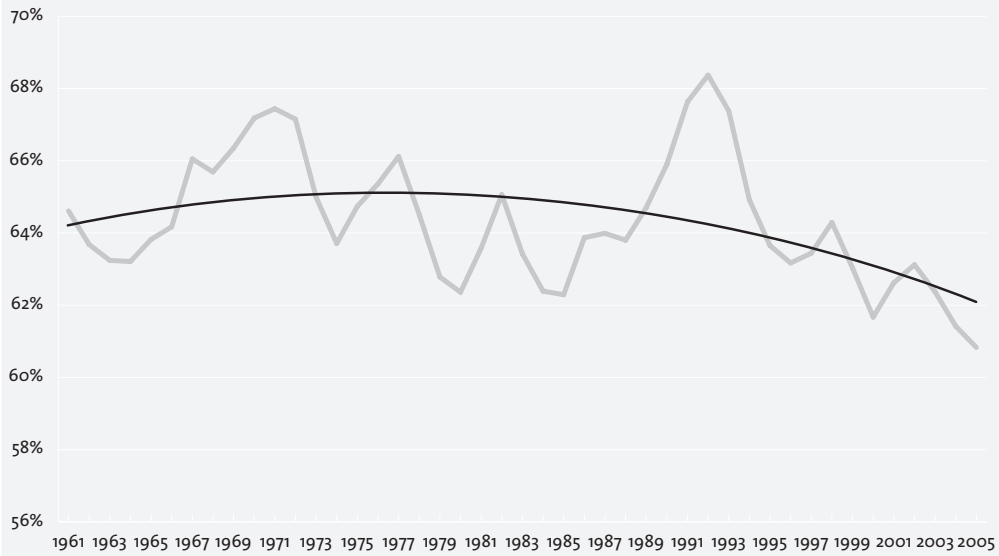
Based on our reorganization of Statistics Canada data, we show the wage share in Chart 5 and the profit share in Chart 6. We also insert a trend line¹² in both graphs to better illustrate the longer-term trends in profit and wage shares. While interpreting Charts 5 and 6, it is important to note that the wage share and profit share fluctuate with economic cycles. Wages tend to be less volatile than profits during economic shocks, so the share of the remaining economic pie going to wages is likely to increase during recessions and decrease during economic expansions.¹³ Because the wage and profit share can fluctuate in the short term for a variety of reasons, we focus on the long-term trends, looking at what happened to the wage and profit share over several decades.

As the trend line in Chart 5 indicates, Canadian workers' wage share increased between 1961 and the late-1970s, then it started a steady decline that continues today. (In terms of yearly data, the short-lived peak in the recession of the early-1990s is due to the fact that firm profitability was especially bad during that period; it is not due to improved workers' pay.) In 1961 workers' wage share was 64.61% of the remaining economic pie, while by 2005 their wage share had fallen to just over 60% — the lowest level we've seen in workers' wage share since 1961.

Corporate profit shares follow the opposite path, as the trend line in Chart 6 indicates. Corporate profit shares dropped in the 1960s, through the late-1970s and early-1980s. After that the profit share rose steadily — dramatically so in the last several years. (In terms of yearly data, the small dips in the early-1980s and early-1990s were associated with recessions.) Corporate profit shares went from 28.91% of the remaining economic pie in 1961 to 33.68% by 2005 — the highest level we've seen in profit share since 1961.

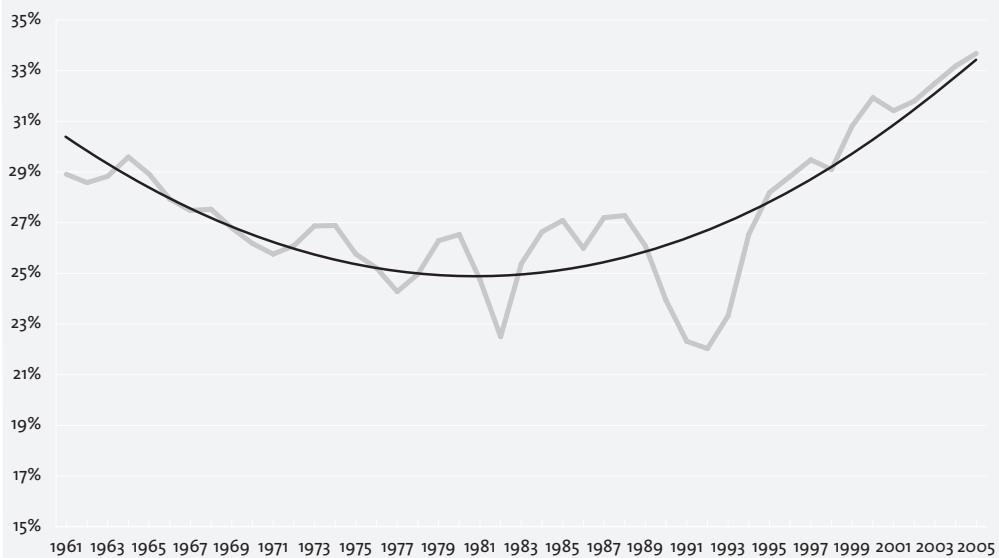
Charts 5 and 6 illustrate an unmistakable trend: corporations' profit share has been persistently increasing while workers' wage share has been persistently decreasing since the late-1970s. This result follows logically from our earlier findings:

CHART 5 Labour Share



Source Statistics Canada, CANSIM database, table 380-0016.

CHART 6 Profit Share



Source Statistics Canada, CANSIM database, table 380-0016.

If real wages are held constant while the economy is growing, this suggests that the share of total income going to workers has been decreasing. (Note this proposition is considered more rigorously in our forthcoming article.)

Chart 4 shows that corporations have been capturing the benefits of economic growth, so that the distribution of total income is increasingly slanted in favour of corporations rather than Canadian workers.

The consequences of changes in the distribution are not trivial. Looking at just the period between 1991–2005, the changing distribution of income is striking. In 1991 the corporate profit share was at a low point of just over 22%; by 2005 it was close to 34%. This represents a large increase in gross corporate profits. The increase in the profit share between 1991 and 2005 implies that gross corporate profits are \$130 billion more in 2005 than they would have been if the profit share had remained at the 1991 level.

Workers' share shrank within Canada's growing economic pie. This significant change in income distribution trends sets the stage for the intensification of income inequality in Canada. Some Canadian workers have fared well despite a shrinking share of the economy. Others were left behind by economic growth. In our forthcoming paper, we advance an argument to account for the disparity among workers as well as the changing distribution of income between profits and wages.

CONCLUSION

The promised benefits of economic growth are not reflected in many Canadian workers' paycheques, despite the fact they are increasing their productivity to help grow Canada's economy. The benefits of economic growth are increasingly flowing to corporate profits rather than to workers' wages and salaries.

How long must Canadian workers wait to enjoy the fruits of their labour? Is economic growth really all it's cracked up to be, if workers stay stuck at 1970s real wage levels while corporations pocket the lion's share of the economic growth? If these trends continue — more economic growth, improved worker productivity, stagnant wages and salaries — these findings suggest that income inequality will undoubtedly become more pronounced in Canada.

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Notes

1 Other types of income may include income from investments as well as income from government programs (such as old age security, employment insurance and so on).

2 Source: Statistics Canada, CANSIM database, Tables 380-0017 and 051-0001.

3 Readers should focus on the trend, not the level, of any given data series. At the break points, the later series shifts up vertically. This does not reflect any sudden increase in real wages; rather it reflects the different categorization methodology employed by Statistics Canada. The different wage series from Statistics Canada overlap in certain years; these overlaps are also shown in Chart 1.

4 Because of the breaks in the data series, it is not possible to comment upon the smaller fluctuations in hourly real wages since the 1970s.

5 Assuming two weeks' unpaid holidays.

6 Sources: CANSIM tables 281-0009, 281-0022, and 281-0030; as well as CANSIM table 326-0002. Our thanks to Henri Sader regarding this point.

7 Source: Statistics Canada, CANSIM database, Tables 326-0002 and 282-0070. The wage data in these tables is obtained from the Labour force survey and differs slightly from the one used in Charts 1, 2, and 4.

8 Alternatively, GDP can be calculated by adding up all the expenses incurred in the purchase of goods and services produced in an economy. Since all goods and services have a seller and a buyer, abstracting from unsold stocks, the income of sellers and the expenses of buyers should be equivalent.

9 We abstract from taxes by subtracting them from total income and regroup the categories of corporate profits, profits of government business enterprises, inventory adjustments, and depreciation under a single "profit share" category, since income in these categories all goes to corporations. We elect to keep the investment and farm shares separate, given that they don't neatly correspond to profits or labour earnings. Finally, following a method suggested

in Morel (2006), we dispense with the income of unincorporated businesses rather than try to divide it between profits and labour income.

10 The “remaining economic pie” is the amount of GDP earned as gross corporate profits, wages and benefits, farm income and income from investments.

11 “Wages and salaries” refer to all forms of employment income: anyone who gets a paycheque — whether they are high or low income earners — will be counted in this category.

12 It appeared to us that the movement in both shares could be very aptly represented by a second degree polynomial, since they go through the same three different phases — increase, plateau, decrease — giving rise to a cupola-shaped relation for the wage share and a bowl-shaped one for the profit share, so this is the trend line we adopted in both cases.

13 In a recession, GDP decreases (by definition). Wages are difficult to reduce (at least in the short term) since outstanding contracts often fix wage rates. If the total amount of wages paid stays constant while the total value of GDP falls, wages/GDP rises. By contrast, in an economic expansion, the relative stability of wages implies that profits tend to grow faster than wages. Thus the profits/GDP ratio will tend to increase relative to wages/GDP. For these reasons, readers are cautioned that a sudden expansion or drop in one share may simply mean that other income components are moving, not that the entities in this category are earning more income or less *per se*. Hence we use these figures to discern long-term trends, rather than sudden shifts.