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## Fairness Considerations in Labor Union Wage Setting: A Theoretical Analysis

by Matthias Striffler, Thomas Beissinger  
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### Abstract:

We consider a theoretical model in which unions not only take the outside option into account, but also base their wage-setting decisions on an internal reference, called the fairness reference. Wage and employment outcomes and the shape of the aggregate wage-setting curve depend on the weight and the size of the fairness reference relative to the outside option. If the fairness reference is relatively high compared to the outside option, higher wages and lower employment than in the standard model will prevail. If hit by an adverse technology shock, the economy will then react with a stronger downward adjustment in employment, whereas real wages are more rigid than in the standard model. With a low fairness reference the opposite results are obtained. An increase in the fairness weight amplifies the deviations of wages and employment from those of the standard model. It also leads to an increase in the degree of real wage rigidity if the fairness reference is high and an increase in the degree of real wage flexibility if the fairness reference is low. Thus, higher wages go hand in hand with more pronounced wage stickiness.

**Text:** See [Discussion Paper No. 6799](#)



[Back](#)