Earnings Inequality: The Role of Industry Effects

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A number of studies point to industry effects, such as a growing wage gap between industries and changing composition of workers across industries, as being the key drivers behind rising earnings inequality. We provide further insights into rising between-industry inequality in Korea, using earnings-related microdata (Survey on Employment Conditions by Employment Type).

The key empirical findings are as follows. First, rising earnings variance is dominated by rising between-industry variance. While the variance of earnings has been increasing since the Global Financial Crisis, a decomposition of the variance shows a reduction in intra-industry factors, but a hike in inter-industry factors.

Second, a small share of industries (10 out of 72 categories) accounts for most of the increase in the inter-industry earnings variance. More specifically, job growth in the high-wage industries takes place with a relatively larger increase in earnings, while that in the low-wage industries occurs with smaller hikes.

Third, a combination of an increased industry premium gap and changing composition of workers through sorting and segregation leads to the widening of inter-industry earnings variance. This reflects how firms organize themselves in terms of their workforce. However, caution is needed in this process, given that excessive sorting and segregation could result in further escalation of earnings inequality and a possible restriction to labor mobility between industries in the long term.

Lastly, an increase in the employment share of large firms (500 employees or above) coupled with a significant reduction of the size premium in low-income industries also partly contributes to the rise in inter-industry differences in earnings.

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