

# THE REAL GENDER PAY GAP

Neither discrimination nor market failure explain the true gap so the case for government intervention is flawed, argues **Ross Guest**

The gender pay gap is never far from the spotlight in Australia and internationally, with the media and sport industries featuring prominently in the debate. In January this year the British BBC Director General was invited by the British Parliament to give evidence on the gender pay gap.<sup>1</sup> When asked, Australia's ABC managing director Michelle Guthrie claimed late last year that there is no pay gap unfavourable to women at any level in the ABC.<sup>2</sup> Morning television presenter Lisa Wilkinson quit Channel 9 partly because she was being paid less than her male co-host Karl Stephanovic. In sport, a 2016 report by the Australian organisation, Women on Boards, found that there remained a huge gap in the pay of women relative to men in virtually all sports.<sup>3</sup>

This article argues that attempts to correct any such pay gaps through 'equal pay for equal work' are flawed and would only end in tears, as do most attempts to fix prices that would otherwise be determined by markets. Men and women earn different pay for 'equal work' for reasons that render invalid the case for regulatory intervention through the Workplace Gender Equality Agency (WGEA) for example.

Evidence suggests that women and men have different preferences for the intensity of paid work and other behavioural differences, and they respond differently to changes in wages, which implies differences in their market wage rates. From the employers' perspective, women and men are seen as complementary rather than perfect

substitutes in terms of the skills and attributes that they bring to their work. This implies that if, for example, women's labour force participation increases relative to men then their market wage should fall relative to men—it would have nothing to do with discrimination and there would be no market failure.

## Explanations for the gap

First we need to define the gender pay gap. It is certainly true that women in the labour force are paid less on average than men. In Australia the average female weekly earnings in November 2017 was \$960 and for men was \$1428—33% less for women<sup>4</sup>. However, this partly reflects the fewer hours worked by women than by men in a working week. If we adjust for this by taking full-time workers, excluding overtime—which is the preferred measure adopted by the WGEA—the gender gap is 15.3%.<sup>5</sup>

The gap has fluctuated between 14% and 19% over the past two decades, and has fallen several per cent over the past three years. It is 8.5% larger in the private sector than the public sector; several per cent higher for workers over age 50 than under 30; at least 5% higher for managers than non-managers; and the gap varies



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considerably by industry—9% in retail, 21.9% in health care and social assistance, and 29.6% in financial and insurance services.

The pay gap may be due to many factors, as listed by the WGEA:<sup>6</sup>

- discrimination and bias in hiring and pay decisions
- women and men working in different industries and different jobs, with female-dominated industries and jobs attracting lower wages
- women's disproportionate share of unpaid caring and domestic work
- lack of workplace flexibility to accommodate caring and other responsibilities, especially in senior roles
- women's greater time out of the workforce impacting career progression and opportunities

Taking this evidence together it does seem that the available data is unable to explain a wage gap of between 4% and 8%.

The next question is which of the above factors would warrant a government regulatory response. The first one—discrimination in hiring and pay decisions—is already regulated under Australia's anti-discrimination law.<sup>7</sup> Pure sex discrimination is objectionable as a breach of human rights and as a market failure, both of which may justify government intervention. This article is concerned more with the market failure issue. Sex discrimination is a type of market failure in the sense that a failure to pay women what they are worth in certain roles means we get less than the optimal supply of women in those roles—hence the case for regulation.

Market failure in the other cases is much less clear cut as they are matters that to some extent involve choices made by families and by businesses (in the case of workplace flexibility). A potential source of market failure in labour markets is lack of information held by either the employee in terms of the nature of the job, or the employer in terms of the characteristics of the employee. Either

of these information deficiencies can result in a sub-optimal allocation of workers to jobs. However, it is hard to see significant information problems in any of the other pay gap explanations listed earlier. Hence the case for regulation in these areas is also much less clear, which is not to say that cultural change in these matters may not be desirable.

On the first of the listed pay gap explanations, what evidence is there for systemic discrimination and bias (against women) in hiring and pay decisions? There is relatively little data available to establish clearly the extent to which this is the case.<sup>8</sup> According to the 2016-17 Australian Human Rights Complaints statistics, there were 385 sex discrimination complaints in 2016-17, but it is not clear how many related to pay. Many discrimination complaints are resolved without proceeding to a hearing.

Econometric studies for Australia find that there is indeed an unexplained gender pay gap after controlling for a range of factors: work interruptions (due to childbirth for example), the types of industries and occupations in which women work in higher proportions than men and which tend to be lower paid, work experience, and part-time employment. In a 2016 study KPMG found that of the total gender pay gap of 16.2%, a little over one third or 6.2% remained unexplained.<sup>9</sup> They attribute this to sex discrimination, which they define as lower pay of women than men where they have equal skill, experience, and are in a job with the same characteristics. Graduate Careers Australia found an unexplained gap of 4.4% in the labour market for graduates in 2013.<sup>10</sup> An earlier study by the National Centre for Social and Economic Modelling (NATSEM) found an unexplained gap of 8%.<sup>11</sup>

Taking this evidence together it does seem that the available data is unable to explain a wage gap of between 4% and 8%. So, for example, if a man is being paid \$100 for a day's work a woman on average would be paid between \$92 and \$96 after accounting for all of the above factors for which we have data.

### Preferences matter

This is puzzling in one sense: why should women accept lower pay for the same work? Melbourne

University professor Michelle Brown argues that it is partly due to bias (unconscious or conscious) in performance reviews, citing data that women tend to receive lower performance ratings than men, often based on personality traits rather than productivity, and that this affects their pay.<sup>12</sup> Again, if bias on the grounds of sex exists in performance reviews, it leads to economic inefficiency which is obviously against the interests of employers. It would be in their interests to identify it and remedy it.

Brown also argues that women are less successful negotiators, citing research that says they are not socialised to negotiate and that their style is more accommodating and less competitive than men.<sup>13</sup> If so, the next questions are: why are they less successful negotiators and does this warrant public policy intervention? There is considerable psychology literature on this question,<sup>14</sup> suggesting a number of possible reasons including sociological conditioning, women's concept of self, moral values and innate competitiveness. None of these necessarily amount to a market failure in terms of information problems or discrimination. Rather they would be, if true, behavioural characteristics of women. They are more akin to 'preferences'.

It seems quite possible that women have different innate preferences for the use of their time outside of work and for the trade-off between work effort and pay, and such innate preferences do not imply any market failure. A January 2018 study of male and female Uber drivers is instructive here.<sup>15</sup> The authors examined the work choices and earnings of more than one million Uber drivers in the United States. They found a gender pay gap of 7%, which could be entirely explained by three factors: their experience defined as number of trips completed as an Uber driver (which affects their knowledge of where and when to work in order to find the more lucrative trips) and their driving speeds. Because men drive more intensively than women—more trips per week—they accumulate experience faster and therefore find more lucrative trips than women for any given number of weeks worked. They also found that men drive slightly faster than women which increases men's returns relative to women. None of this has anything to do with discrimination—it is about preferences for driving speed and for work hours per week.

The point about the intensity of work is echoed by another US study<sup>16</sup> in which Harvard economist Claudia Goldin argues that although the gender pay gap is shrinking (although it isn't much in Australia) due mainly to better education of women and family-friendly workplaces including child care which allow work participation—as well as technology that allows work flexibility—a gap remains nonetheless. The reason is that more senior roles in the corporate, financial and legal occupations pay a premium for an inflexible work schedule, for the willingness to work extremely long hours at unpredictable times. The preference of women to avoid such inflexible work schedules is costly.

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Economists capture these preferences relating to work through labour supply data. Reliable data exists on the responsiveness (or 'elasticity') of the labour supply of women and men to changes in their (after-tax) wages. An Australian Treasury study<sup>17</sup> reviewed the literature and found that the elasticity of labour supply of both married and single women was significantly (in the statistical sense) higher than for men, meaning that women adjust their labour supply more than men in response to wage changes. This implies that even if the labour demand for women and men is identical, implying they have the same productivity and are regarded as perfectly substitutable by employers, they can be expected to have different wages and the wages of women will fluctuate less than for men in response to fluctuations in labour demand. It would have nothing to do with discrimination.

The difficult question, however—not addressed in the U.S. studies cited—is how much of these 'preferences' could be eliminated by changes in technology and domestic arrangements that remove the necessity for inflexible work schedules in some jobs, and how much is due to deeper innate

preferences for time allocation to professional work versus family/household time. If there are innate preference differences among women and men, then we should expect the gender pay gap to continue and it would be entirely consistent with an efficient labour allocation of male and female workers in the economy, assuming no direct discrimination against women since that would be a type of market failure. If women are prepared to work for less pay due to preferences, their labour supply at any given wage would be lower than for men, resulting in a lower market wage for women even where the productivity of both women and men is the same.

History is littered with examples of failed government attempts to regulate prices in markets. It usually brings unintended consequences that hurt the people who are meant to be helped.

On the other hand, the opposite could be true—women could generally require a higher wage than men in order to take a given job. In that case their efficient market wage would be higher than for men. It is, however, very difficult to get reliable data on ‘preferences’ and therefore to test empirically either of the above propositions. The point is nevertheless that different preferences would imply different market wages that are consistent with efficient labour allocation.

On the labour demand side, the assumption that women and men are perfectly substitutable and therefore face identical labour demand is highly questionable and can further explain different market wages of women and men doing equivalent work. Women and men are more likely to have complementary rather than identical skills. If so, a mixed gender workforce is likely to be more productive overall than a single gender workforce—this applies even if men and women are equally good at their job, but just good in different ways, and even if they have the same elasticity of labour supply. In that case if women’s labour force participation increases then their market wage will fall relative to men, which makes sense for businesses and is good for national productivity.

## Unintended consequences

To sum up, we should expect the market wages for men and women to differ even for the same work and even without any discrimination for the following reasons: (i) women and men have either different preferences for work, and these preferences respond differently to (after-tax) wages; (ii) women and men have complementary job capabilities. The equal pay for equal work mantra is therefore flawed as a general principle. It would be a mistake to coerce employers to increase pay of women relative to men—the outcome would be fewer women employed relative to men and a loss of productivity for individual businesses and the economy.

Yet this is exactly what the WGEA sets out to do—put pressure on employers with over 100 employees to ensure equal pay of women relative to men for work ‘in the same or similar roles’, as well as ensuring compliance with several other ‘gender equality indicators’. Relevant businesses must comply with the Workplace Gender Equality Act 2012 by reporting to the WGEA each year explaining what strategies and measures they have to meet the ‘minimum standards’ for achieving the gender equality indicators. Pressure is brought to bear through the consequences of non-compliance. The WGEA may name a non-compliant employer in a report to the Minister. Non-compliant employers may not be eligible to tender for government contracts and may not be eligible for government grants. A total of 51 businesses were listed on the website as non-compliant at 31 Dec 2017.

Coercion or pressure of this type amounts to a soft form of price fixing in the labour market. History is littered with examples of failed government attempts to regulate prices in markets. It usually brings unintended consequences that hurt the people who are meant to be helped. Examples include bank home loan interest rate caps in the 1980s that drove poorer households out of the housing market or into the hands of higher cost lenders; the floor price for wool which collapsed in 1991 leaving a debt and wool stockpile that the wool industry had to carry; the housing rent controls that exist in some large cities such as New York and London that generally reduce

overall supply of rental housing and force out those with poorer work and credit histories.

It should be no different when it comes to interfering with women's wages. Fewer jobs would be available to women at the new higher pay levels, which may discourage women from seeking such jobs in the first place. In one sense we should be pleased that the WGEA Director told a Senate estimates hearing last year that Australia is 50 years away from closing the gender pay gap. On the other hand, 50 years of the red-tape costs of complying with WGEA legislation would be a burden, along with the expenditure by the agency of \$6 million in 2016-17,<sup>18</sup> not justified by any benefits.

A better approach would be to ensure employers are aware of the benefits of complementary capabilities of women and men for their own business success, and let them make judgements about the optimal mix of men and women employees—and at the most make gender balance disclosure voluntary. This is put well by Adam Schwab, the founder and CEO of the AussieCommerce Group which employs a majority of women through its retail brands: 'Any business which needs to be told by the government not to discriminate is running a business that will almost certainly not be around in the decades to come.'<sup>19</sup>

## Endnotes

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- 2 'Pay Hikes Put Wind in Guthrie's ABC Gender Parity Pitch', *The Australian* (25 October 2017).
- 3 Women on Boards, *Gender Balance in Global Sport Report* (September 2016), <https://www.womenonboards.net/womenonboards-AU/media/AU-Reports/2016-Gender-Balance-In-Global-Sport-Report.pdf>
- 4 Australian Bureau of Statistics (ABS), 'Average Weekly Earnings, Australia', Cat 6302.0 (May 2017).
- 5 <https://www.wgea.gov.au/>
- 6 ABS Cat 6302.001; Workplace Gender Equality Agency (WGEA), 'Australia's Gender Pay Gap Statistics' (August 2017), p.2.
- 7 The Fair Work Act 2009 and the Sex Discrimination Act 1984 require that male and female employees receive equal remuneration for work of equal value. Also, the Workplace Gender Equality (Minimum Standards) Instrument 2014 requires employers with more than 500 employees to have a formal policy or strategy that supports equal remuneration between women and men.
- 8 Alice Orchiston, *The Conversation* (11 January 2018), <https://theconversation.com/for-women-fighting-the-gender-pay-gap-discrimination-law-is-limited-89918>
- 9 KPMG Australia, *She's Price(d)less: The Economics of the Gender Pay Gap*, Update Report Prepared for Diversity Council of Australia and the Workplace Gender Equality Agency (October 2016).
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- 11 Cornelis Reiman, *The Gender Wage Gap in Australia*, Discussion Paper No. 54 (Canberra: University of Canberra, National Centre for Social and Economic Modelling, March 2001), <http://www.natsem.canberra.edu.au/storage/dp54.pdf>
- 12 Michelle Brown, 'To Close the Gender Pay Gap We Need to End Pay Secrecy', *The Conversation* (16 September 2014), <https://theconversation.com/to-close-the-gender-pay-gap-we-need-to-end-pay-secrecy-31626>
- 13 There is a considerable literature on this topic, which is beyond the scope of this short piece and somewhat outside the expertise of this author. However, it is a finding at odds with this author's personal experience, in higher education, that women are very successful negotiators, probably more skilled than men.
- 14 Laura J. Kray and Leigh Thompson, 'Gender Stereotypes and Negotiation Performance: An Examination of Theory and Research', *Research in Organisational Behaviour*, vol. 26 (2004), 103-182
- 15 Cody Cook, Rebecca Diamond, Jonathan Hall, John A. List and Paul Oyer, 'The Gender Earnings Gap in the Gig Economy: Evidence From Over a Million Rideshare Drivers', Working Paper 3637 (Stanford University Graduate School of Business and NBER, January 2018).
- 16 Claudia Goldin, 'A Grand Gender Convergence: Its Last Chapter', *The American Economic Review*, 104: 4 (2014), 1091-1119.
- 17 Sandra Dandie and Joseph Mercante, 'Australian Labour Supply Elasticities: Comparison and Critical Review', Treasury Working Paper 2007-04 (Australian Treasury, October 2007).
- 18 Workplace Gender Equality Agency Annual Report, 2016-17, <https://www.wgea.gov.au/sites/default/files/wgea-annual-report-16-17.pdf>
- 19 Adam Schwab, 'Why the Workplace Gender Equality Agency Should Be Disbanded', *Australian Financial Review* (14 May 2015), <http://www.afr.com/leadership/why-the-workplace-gender-equality-agency-should-be-disbanded-20150514-ka16b>