

Comment on “Wage Dispersion and Overqualification as Entailed by Reder-Competition” by Ekkehart Schlicht

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Evaluation

The paper formalizes a classical theory put forward by Melvin Reder (1955) and applies it to explain the joint increase of qualification premia and overqualification which remains puzzling in the framework of standard neoclassical analysis and is ignored in the current debate on skill-biased technical change (SBTC). Reder’s hypothesis combines neoclassical *wage competition* with the diametral extreme dubbed *job competition* to form a realistic theory of labor market adjustment. The resulting theory is more general than its components and enables us to understand and investigate wage rigidities and wage adjustment in a more clear and detailed fashion.

Schlicht’s paper is highly relevant for two reasons. First, it propagates Reder’s largely neglected thoughts by providing a simple and elegant formalization which nevertheless captures the most important aspects of the issue under consideration: heterogeneity of workers, wage compression and restricted mobility. Second, it provides an interesting alternative explanation of an important stylized empirical fact (increasing education premia and overqualification).

The paper

Suggestions

Though the exposition of the model is elegant and comprehensible, the model is quite abstract. To make the paper more accessible to impatient economists and economists interested mainly in the application, the relation between the stylized model and the empirical facts to be explained should be worked out in more detail. Let me briefly summarize the points where I see possibilities to improve the paper.

- The model deals with two types of workers (prolific and mediocre) with different productivities. By assumption, both types obtain the same wage. Though this assumption (perfect wage compression) is taken for simplicity only and the model results remain qualitatively unchanged if it is relaxed, this point will be prone to misunderstanding. At a glance, it seems to be at odds with the intention to explain increasing wage dispersion or its

connection with overqualification. Therefore the author should provide some more detailed comments on the response of wage dispersion to technical changes.

- The next point requires a short outline of Schlicht's argumentation: Schlicht first investigates the wage and price effects of an increase in job latitude (i.e. heterogeneity of workers) leaving average productivity constant. He finds that real wages rise since the selection effect¹ then becomes more important. Higher real wages in turn make education more attractive.

Education is modelled as a lottery: workers turn out as prolific or mediocre *ex post* (after completion of a training measure). Though prolific and mediocre workers obtain the same wage, it is (*ex ante*) individually efficient for all workers to train, since prolific workers are employed with greater probability. Overeducation results here because only a part of the mediocre workers becomes employed and the rest has to search for jobs in an alternative (low wage) sector where training is not required at all.

To summarize: increasing heterogeneity of workers (which may be caused by technological change) raises real wages and creates additional incentives to education and overeducation. Though the author appeals to skill biased technical change, wage dispersion and overeducation in the introduction, only the relation between overeducation and increasing worker heterogeneity is modelled and worked out in detail. Since overeducation is rather a side issue in the view of most economists whereas much attention is paid to SBTC and increasing wage inequality, the author should either state more clearly that his model focusses on overeducation or provide additional comments on the relation between the model and the latter two issues. (Why does technical change increase job latitude? Which jobs are more affected by these changes?)

- Schlicht's use of the term 'qualification' (represented through parameter q in the model) appears capable of being misunderstood too. 'Qualification' seems to capture heterogeneity of workers *within* formal qualification or education groups. This may provoke misconceptions since 'qualification' frequently is associated with formal qualification or education, especially in the SBTC literature. If my interpretation of the paper is correct, its focus is on wage dispersion *within* formal qualification (education) groups. This should be mentioned and detailed already in the introduction to put the reader on the right track.

¹firms with higher wages get a greater share of prolific workers and – by that – higher average productivity. The term 'selection effect' captures that higher wages allow the firm to select better workers.