



## Are Wage Inequalities Fair?

**Pay-for-performance or collective bargaining: The pay system we prefer says as much about the way we view the world as the economic conditions in which we find ourselves.**

The global financial crisis has added weight to questions of high executive pay, rising wage inequality and the diverse ways in which countries are responding to the rich-poor divide.

In France, for example, many company leaders have acknowledged the need to pay higher tax and the government has moved to cap the pay of top executives at state controlled companies. It would be hard to imagine this attitude prevailing in the U.S. where executives' compensation (**in some cases more than 300 times the salary of average production and supervisory workers**) is considered by many to be well-earned.

These two extremes reflect the striking discrepancies in views around the world as to whether the world is perceived as a just and fair place - where individuals are responsible for their own fate and everyone gets what they deserve - or whether success and failure is largely dependent on luck.

### Pay preferences and a 'Just-World' view

We recently published a **series of studies** to establish the extent to which these 'just-world' beliefs influenced people's preferences for compensation policies.[1] The data showed that the more individuals believe they are living in a just and

fair world, the greater the preference they have for being paid for performance – and awarded the money they feel they have earned. Conversely, individuals, who believe the world is not fair and that people's standing is due more to luck than to their individual effort, are more likely to favour a wage system which evens out payments, redistributing the money earned among workers.

Where an individual is from also appears to play a role. In one study, participants from Anglo-Saxon countries – the U.K., U.S., Canada, Australia and English-speaking South Africa – rated themselves significantly higher on the just-world-belief scale and had a much stronger preference for performance-based, winner take all payments, than participants from Europe and South America, who were less positive about whether the world was fair and preferred a redistributive payment system.

### Not everyone "thinks like us"

A second study looking at aggregated differences on a national level, in this case comparing participants from France and the U.S. - two countries that strongly differ in their overall belief in a just world - found a similar phenomenon. The American participants had a significantly stronger preference for more pay-for-performance compensation and scored noticeably higher on the just-world belief

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scale.

To get a better understanding as to the extent to which these cultural differences were a result of individuals' perception of the world, or whether uncontrolled differences between the groups contributed to the findings, we conducted a third study with U.S. undergraduate students. Half the students were subconsciously primed with 'just-world' ideas, while others in the 'control' group were assigned an unrelated priming exercise. They were then given identical tasks to perform and, as in the first two studies, asked how they would like to be compensated for future sessions. Students in the 'just-world' condition showed a much greater preference for performance-based compensation than those who were not.

That Europeans in general, and the French in particular, would have a stronger preference for equal pay and a far less positive view of the fairness of the world than Americans, may be somewhat intuitive. What was surprising was that the American college students sampled in the third study were also less likely to believe the world was a fair place (although not to the extent of the French) and showed a strong preference for redistributed pay.

### Tips for expanding abroad

There is no universal answer as to what degree of wage inequality is fair. What this research shows is that different values or economic conditions are not the only factors that influence compensation preferences; deeper cognitive differences in beliefs about the justness of the world also come into play.

This will come as no surprise to many corporations who discovered the hard way that not all pay systems are equally acceptable in different countries. **Walmart's** refusal to take on board the relatively egalitarian wage-setting practices considered fair in Germany, for example, contributed to its failure in that country. Similarly, Lincoln Electric Company found its **expansion plans stymied** when its pay-for-performance wage system (which had great success in the U.S.) was less well received in more egalitarian cultures.

Organisations looking to expand abroad need to stop and think about whether employees in the communities they are entering share the same notion of fairness as their home state. A U.S. business entering a country where people generally believe that outcomes are due more to luck than effort may find that workers consider an individual performance-based wage system fundamentally unfair. Conversely, a company from a country where it's considered fair to even out pay differences looking to expand into the U.S. may find that American employees are unhappy being denied

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pay they believe is rightfully theirs from hard work.

This is not to say different compensation systems can't be applied. Lincoln Electric's success in **Mexico** is one example where a company, by introducing the system gradually and on a voluntary basis was able, over time, to implement a U.S.-style pay scheme in a country with very different ideas of social fairness.

### An evolving sense of fairness

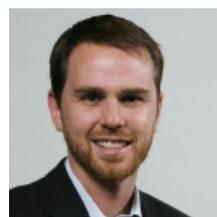
Companies would also do well to look at the changing cultures in their home country. Just as the Great Depression shook up fundamental assumptions about what is fair in the 1930s, the Global Financial Crisis and the European Debt Crisis has prompted another shift in society's view as to how just the world really is - especially the world of financial rewards as a function of individuals' merit. While business practices in Europe continue to evolve towards the U.S. model, there is a groundswell of opinion globally, supported by a number of academics and economists, who believe this can't go on, that, politically and economically, the model is unsound and there will be a backlash from society.

Our findings suggest that the intensity of the backlash will differ from country to country as a function of the difference in their cultures' just-world beliefs. And, as more people believe the world is unfair, the more they will expect changes to pay structures.

For access to the full research paper contact Douglas Frank [here](#).



**Klaus Wertenbroch** is Professor of Marketing at INSEAD, and the launching editor-in-chief of the European Marketing Academy's (EMAC) Journal of Marketing Behavior



**William Maddux** is an Associate Professor of Organizational Behavior at INSEAD



***Douglas Frank*** is an Adjunct Professor of Strategy at INSEAD and Associate Professor of Management at The Catholic University of America

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[1] Frank, Douglas H., Klaus Wertenbroch, and William W. Maddux (2015), "Performance Pay or Redistribution? Cultural Differences in Just-World Beliefs and Preferences for Wage Inequality," *Organizational Behavior and Human Decision Processes*, 130 (September), 160-170.

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