

Wage inequality between permanent and fixed-term contracts: a firm-level analysis[†]

Marta Silva (Banco de Portugal, BRU-IUL, DINÂMIA'CET-IUL)

and

Luis F. Martins (ISCTE-IUL, BRU-IUL)

This paper empirically studies the effects of extending the maximum legal duration of fixed-term contracts on the distribution of the within-firm wage gap between permanent and fixed-term contracts. We use Portuguese linked employer-employee data to estimate a quantile regression with fixed effects. Our results show that in the period in which the maximum legal duration of fixed-term contracts was extended, wage inequality decreased at the bottom and increased at the median and top of the conditional relative wage distribution. We interpret this result as potential evidence that the relative wage may reflect the primary use that firms assign to fixed-term contracts. Finally, we find that although firms in the tradable sector pay higher relative wages to permanent workers, especially at the top of the conditional relative wage distribution, they seem to be less significantly affected by the change in legislation than firms in the non-tradable sector. The results in this study draw attention to the importance of promoting the conversion of fixed-term into open-ended contracts to tackle labour market segmentation and reduce intra-firm wage inequality.

Keywords: Employment Protection Legislation, Fixed-term Contracts, Relative Wages, Tradable Sector, Quantile Regression, Fixed Effects

[†] The opinions expressed in this paper are the sole responsibility of the authors and do not necessarily reflect those of the *Banco de Portugal* or the Eurosystem. The authors gratefully acknowledge the comments and suggestions of Helena Lopes. The authors thank Office for Strategy and Studies (GEE), Ministry of Economy and Employment for allowing access to the data and Matthew Baker, David Powell and Travis Smith for making available the *qregpd* Stata package to estimate quantile regression with nonadditive fixed effects. Marta Silva gratefully acknowledges the financial support of Fundação para a Ciência e a Tecnologia under the Doctoral Grant SFRH/BD/8592/2012.