

# New Ideas to Handle Employment Issues Under Epidemic Normalization - Based on Profit-Sharing Theory

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## ABSTRACT

The profit-sharing theory used to be an effective way to solve economic stagflation problems in western countries. This article is committed to finding new ideas to deal with employment issues under the current epidemic normalization by analyzing its specific theoretical content to explore a sustainable path to steadily reduce unemployment and expand employment in the whole society.

**Keywords:** *Profit-sharing, labor supply, job market, wage system*

## 1. INTRODUCTION

In the 1970s, there was a long-term coexistence of price increases and economic stagnation in western countries. Under such a macro background, Martin Weitzman, professor of economics at the Massachusetts Institute of Technology in the United States, proposed the theory of profit-sharing. It brought important enlightenment to western economics, which was troubled by labor-management contradictions and stagflation at the time, and achieved noticeable results after its application, reducing workers' unemployment and improving labor-management relations. Therefore, this theory was widely spread in the western world in the middle and later periods of the last century.

## 2. BACKGROUND

In the second half of 2020, a sudden new crown pneumonia epidemic disrupted the pace of people's lives and changed the operation course of enterprises. In order to prevent the spread of the virus, the government ordered the implementation of strict epidemic prevention and control policies, all walks of life were forced to suspend work, all residents were isolated at home. Therefore, the entire society was in a state of stagnation. With the effective control of the epidemic gradually, the resumption of work and production has begun to proceed in an orderly manner. However, in the face of repeated epidemics, the development prospects of enterprises are not that clear, instead, there are too many changes and uncertainties. Coupled with the heavy blow of the epidemic, many companies are unable to operate and even go bankrupt. Some big companies have to face the dilemma of layoffs to reduce costs and maintain operations, resulting in a large number of unemployed labor wandering in the society, which seriously affects the stability of the social

environment, and will have a huge adverse impact on the smooth and steady recovery of the economy. At this stage, when epidemic prevention and control have become a normal situation, it is obviously not a long-term solution to stop work and wait for production. In addition, enterprises also cannot blindly lay off employees to overcome difficulties. Therefore, finding a sustainable path to solve employment and resume production has become a top priority.

Facing the current severe employment situation, the profit-sharing theory that was once popular in the western world has regained attention. Although there are differences in political system and social environment, its theoretical results provide a new perspective into the solution to the current employment problems, which has a certain enlightening significance.

## 3. THEORY

### 3.1. Theoretical Content

Simply put, the profit-sharing theory refers to the overall incentive plan of the organization in which employees obtain a part of the company's profits based on their work performance. In Professor Weitzman's view, the root cause of stagflation in economic operations lies in traditional wage system, because it must be prerequisite for equilibrium under the conditions of full employment to be effective. Once the economy is in recession, under the condition of fixed wage, employers will inevitably reduce costs by cutting workers based on the principle of profit maximization. And it is not hard to imagine that widespread unemployment will lead to a new round of insufficiency of effective demand and deterioration of living standards [1]. Therefore, Professor Weitzman reformed the traditional wage system and changed fixed wage into shared wage. Shared wages consist of two parts:

basic wage and floating wage. The basic wage level is determined by the enterprise itself, while floating wage combine the wages of workers with an index that can properly reflect business operation, so as to achieve the purpose of allowing workers to share the fruits of enterprise development. In this way, what workers and enterprises reach in the labor market is no longer an agreement that specifies a fixed wage contract for each work unit, but an agreement that determines how much employees and the employers share in the income of the enterprise.

### **3.2. Theoretical Analysis**

The profit-sharing system can work mainly because it is connected with the operating revenue or operating profit of the enterprise, so it has the effect of automatically resisting unemployment and inflation [2]. On the one hand, the sharing system means the income of each new unit of labor is shared by employees and employers in proportion, so the marginal cost of labor is always lower than the average cost of labor, which enables companies to continuously expand production and employment. On the other hand, under the sharing system, workers' wages are directly proportional to product prices, and any price changes will automatically be fed back to labor costs, that is, the higher the product price, the higher the wage level that needs to be paid. Since the labor cost (wage) of an enterprise is directly linked to the price of the product, it has an inherent tendency to counter inflation.

That is to say, under the fixed wage system, based on the western economic principle that marginal revenue and marginal cost are equal, the value created by the last worker hired by the enterprise will be exactly equal to the wage cost. Therefore, companies lack inherent power to hire more workers. The profit sharing system is just the opposite. By determining the standard of the sharing coefficient, the value created by the last worker under the fixed wage system is higher than the basic wage cost under the shared wage system. Consequently, companies are willing to expand production and hire more workers, and workers will work harder and pay more efforts to get higher wages.

### **3.3. Case Analysis**

Here is a simple example to analyze how Professor Weitzman's profit-sharing idea make a stimulus to enterprises to increase the supply of labor by reforming the traditional salary system, thereby solving the employment problem of the entire society.

Assuming that the company hires 10 workers in total, the fixed wage level of the workers is \$200 per week, and the value created by the first worker hired by the company is \$300 per week, then the company must make the value created by the last worker exactly match \$200 to keep cost below profit and avoid corporate losses. After the

enterprise reforms the profit sharing system, assuming that the basic wage level of each worker becomes \$160 per week, and the weekly floating wage is \$40 ( $200 - 160$ ), and then the sharing coefficient can be calculated as  $2/7 [40 / (300 - 160)]$ . Under the new institutional arrangement, the value created by the tenth worker originally hired by the company at this time is about \$171 [ $2/7 \times (200 - 160)$ ], which is lower than the fixed wage cost that the company needs to pay. Under the circumstances, enterprises can easily generate internal motivation to expand labor scale. The reason can be attributed as follows. According to the microeconomics principle that marginal revenue equals marginal cost, an enterprise must equalize the amount of value created by the last worker and the cost to be paid before reaching the maximum employment scale. However, after the profit sharing system is implemented, as long as the amount of value that new workers can create is higher than the basic wage level of shared wages, the company will not stop hiring workers, because every additional worker hired by the company will earn a net profit of about \$30 ( $200 - 171$ ). As profits increase, companies have more funds to expand the scale of production; as output increases, the sales price of their products in the market will drop; as prices decrease, companies can sell more products, thus forming a virtuous circle. For other enterprises, the expansion of an enterprise's production scale has produced a positive external influence on the operation of the market, prompting more and more enterprises to implement profit-sharing system. In this way, the more companies that implement profit-sharing system, the greater the possibility of eliminating unemployment. This is the so-called "Weitzman effect"[3].

## **4. PROSPECTS**

From the perspective of the enterprise, the profit-sharing theory enhances the enterprise's ability to expand production, which provides the enterprise with the motivation to solve the employment of workers. More importantly, it also creates a hopeful vision for the workers. Workers are willing to put more effort to make the enterprise develop better, because they believe that hard work can share more corporate operation fruits, which will help companies retain talents, reduce unnecessary personnel turnovers, reduce human resource costs, and cultivate employees' corporate loyalty and sense of responsibility.

Under the traditional fixed wage system, there is no direct economic relationship between the wages of workers and the quantity and quality of labor input. However, under the profit-sharing system, the beneficiaries cover all employees, and the basis for verification is the company's production and operation performance, so it is a special group incentive plan. It is precisely the group characteristic of this incentive plan that establishes a direct connection between the labor remuneration of a single person and the diligence of each member in the group, so each member will not only works hard by themselves, but

also consciously supervise other members. Because the profit-sharing system gives enterprises the inherent motivation to refuse to dismiss workers, the working period of each worker is greatly extended, which not only helps a lot to improve workers' production skills. Besides, refusal to lay off workers also effectively enhances employees' sense of responsibility towards the company and shared recognition among group members. Hence, it will greatly reduce the incidence of disputes and the rate of employee turnovers, which will promote the formation of the company's unique human resource advantages and the accumulation of necessary professional knowledge and skills. At the same time, the profit-sharing system has improved the cooperative relationship between labor and management, strengthened the collaborative intention, broadened communication channels, reduced conflicts, and improved the operating efficiency of the entire enterprise. Professor Weitzman suggested that a "focused and strong national plan that emphasizes awareness, education, and information should be developed to inject social responsibility into the collective agreement process." [4] Also, he suggested tax deductions for employees' shared income. Since the implementation of the profit-sharing system will lead to a decline in the overall profit of the enterprise, companies may lack the motivation to implement profit-sharing plan. In order to solve this problem, Professor Weitzman proposed that the government should adopt an "inducible tax policy", which is used to promote the implementation of profit-sharing system by enterprises through some shared income tax relief policies [5]. The typical practical results of the profit-sharing plan include the British profit-sharing system, the American employee stock ownership plan, the Japanese employee stock ownership association, the Spanish Monteragon Workers' Cooperative and the Chinese joint-stock cooperative system, which have improved the micro-efficiency of enterprises to a certain degree.

## 5. LIMITATIONS

There is no doubt that the "Weitzman effect" has positive impacts, but in the specific implementation process, the following two aspects must be paid attention to. Firstly, basic salary cannot have a lower limit, and the standard of the level of basic salary cannot be determined without a minimum limit [5]. In some industries, the basic wage level is set too low or even not, which can easily lead to negative consequences. For example, some intermediary and sales promotion industry employees rely entirely on their personal performance for their income, which determines how much they get paid. In other words, there will be no reward without excellent performance. The creed of performance first has led to more and more "black-hearted intermediaries" and some vicious frauds in the market, which has severely weakened consumers' trust and affected the stability of social order and the smooth operation of the economy.

Secondly, there cannot be no limit on sharing, and the sharing coefficient for employees to share the results of enterprise development cannot be determined without a maximum limit [6]. If the sharing coefficient is set to exceed a certain limit, on the one hand, corporate profits will be greatly reduced, and corporate capital reserves and cash flow will be correspondingly reduced, which is not conducive to the expansion of production scale and business scope of the company, and it is greatly detrimental to the long-term sustainable development of the company; on the other hand, due to differences in personal abilities and skills, employees have different contributions to the company, large or small, and more or less. On account of this, some employees may get higher sharing income, while the other part is relatively small. If things go on like that, the income gap between employees will continue to expand, which is likely to cause internal conflicts, which is not conducive to the internal unity of employees. Workers cannot form a unified external centripetal force, which is harmful to the harmony and unity of the internal environment of the company and successful achievement of the development goals of an enterprise. Once it encounters an unforeseen crisis, the enterprise is likely to fall apart due to the intensification of internal conflicts.

## 6. CONCLUSION

A good model depends on how it creates value and saves costs on the one hand, and how it solves problems on the other. The profit-sharing system inspires new perspectives and directions to manage employment issues, which is committed to providing better service for sustainable economic and social development and bringing greater convenience to people's daily life. Nevertheless, at the same time, although profit-sharing plan has bright prospects for development and has made great achievements in coping with unemployment and inflation, the standard for establishing basic wages for employees and the sharing coefficient of floating wages must be determined through precise calculation based on large amounts of data in a long period, which are influenced by many specific factors, so how to effectively implement the plan to achieve desirable outcome needs to be further explored.

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