



Labor markets and wage determination

LABOR, WAGES, AND EARNINGS

Wages Defined...

Wages - - Salary - - Earnings

Wage Rate

Nominal Wages

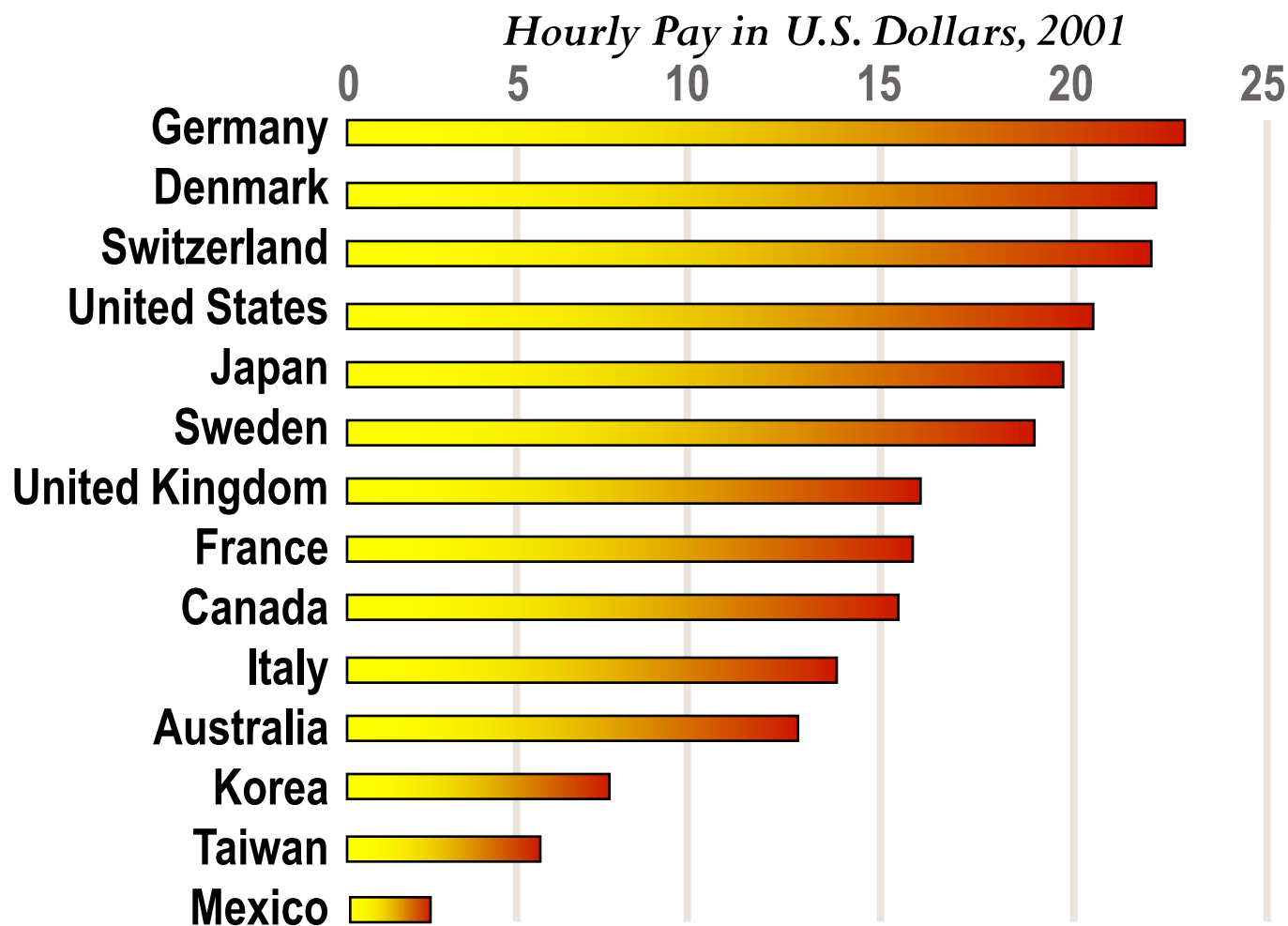
Real Wages

International differences...



GLOBAL PERSPECTIVE

Hourly Wages of Production Workers, Selected Nations



Source: U.S. Bureau of Labor Statistics, 2003

GENERAL LEVEL OF WAGES

Role of Productivity

- **Plentiful Capital**
- **Access to Abundant Natural Resources**
- **Advanced Technology**
- **Labor Quality**

REAL WAGES AND PRODUCTIVITY

Growth in real income (earnings)
Growth in output per worker-hour

*Can only grow at
about the same rate!*

PURELY COMPETITIVE LABOR MARKET

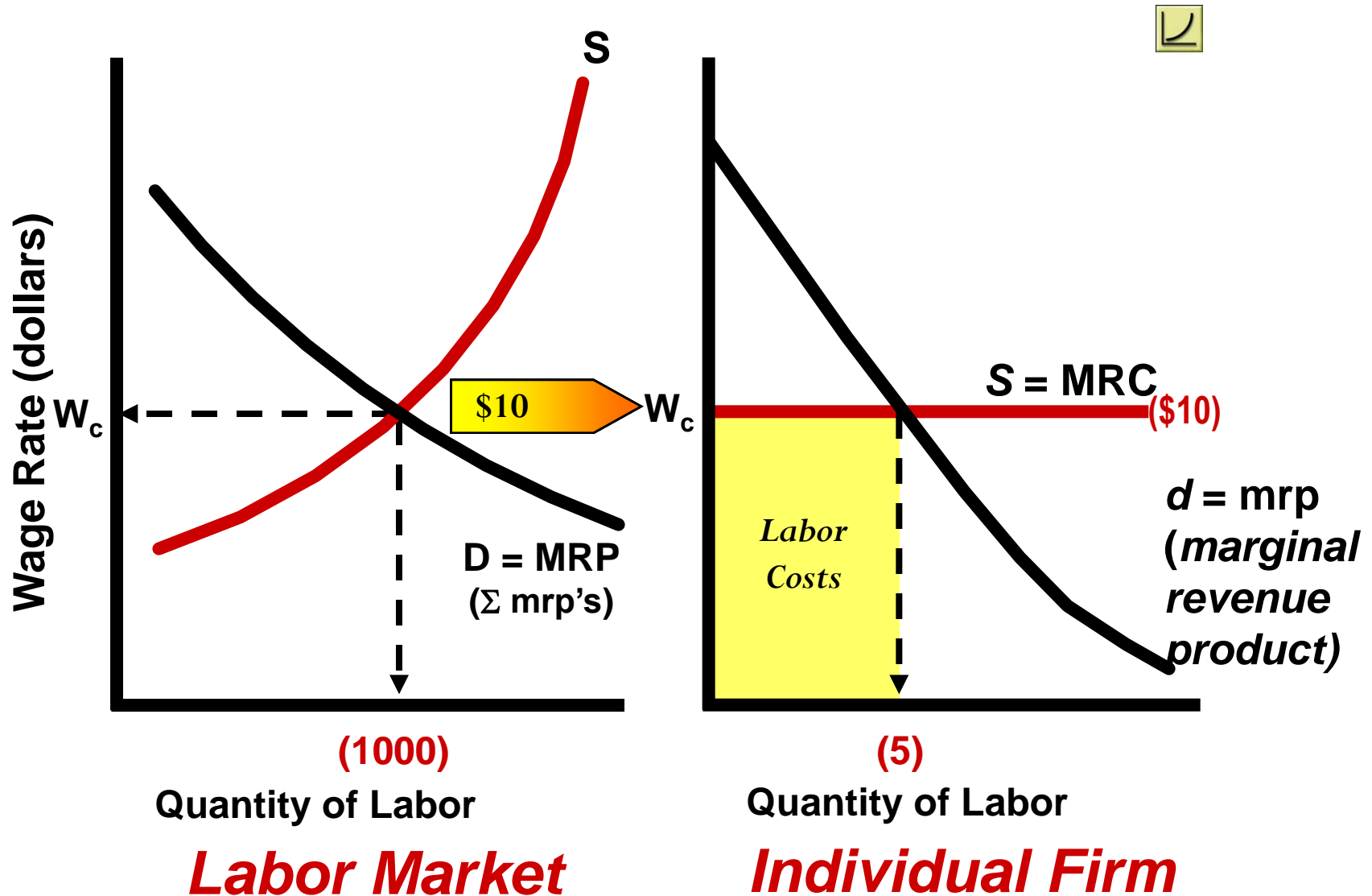
Purely competitive labor market:

Many Firms

Numerous Qualified Workers

***“Wage Taker”* Behavior**

PURELY COMPETITIVE LABOR MARKET EQUILIBRIUM



PURELY COMPETITIVE LABOR MARKET EQUILIBRIUM



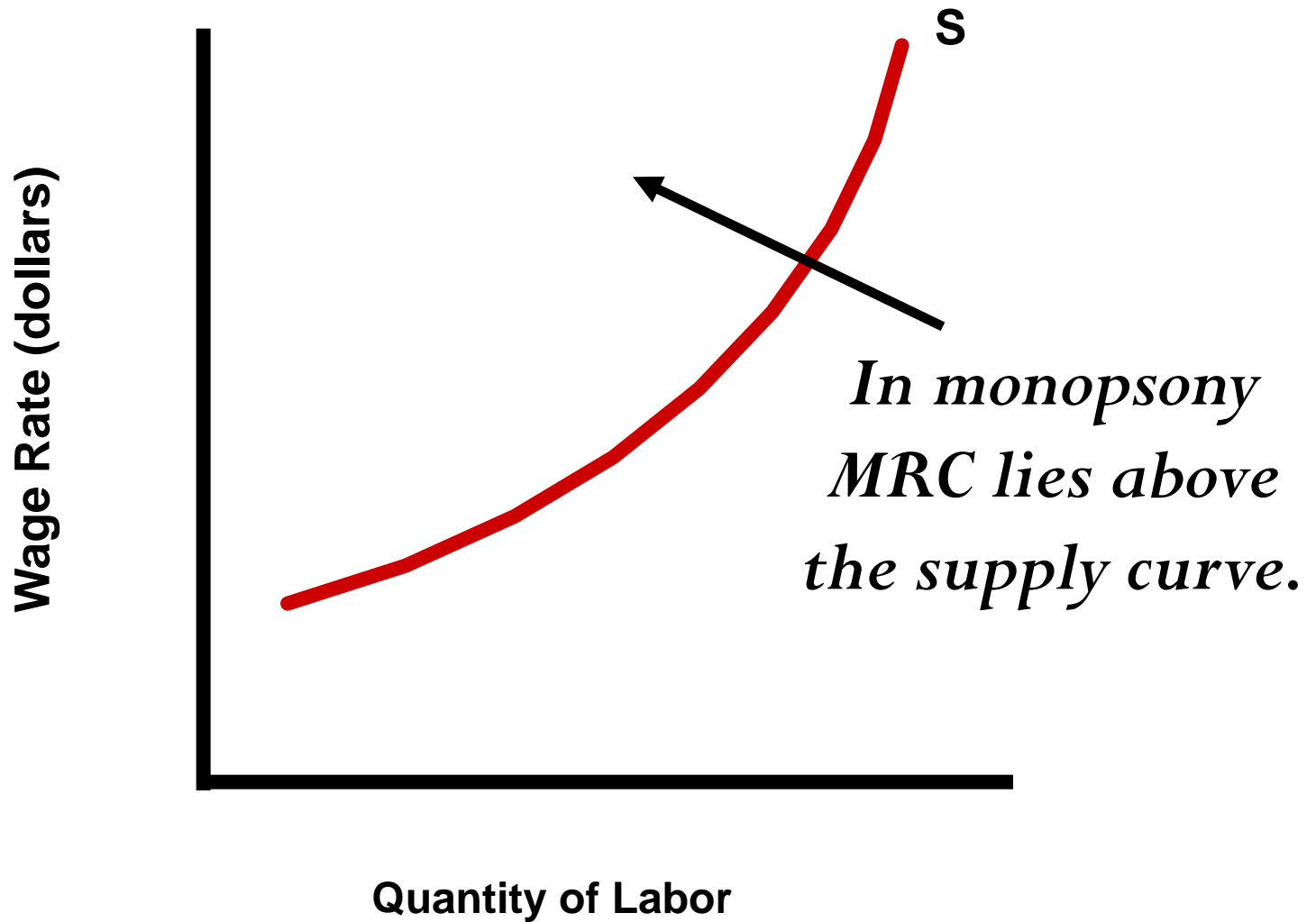
MONOPSONY MODEL



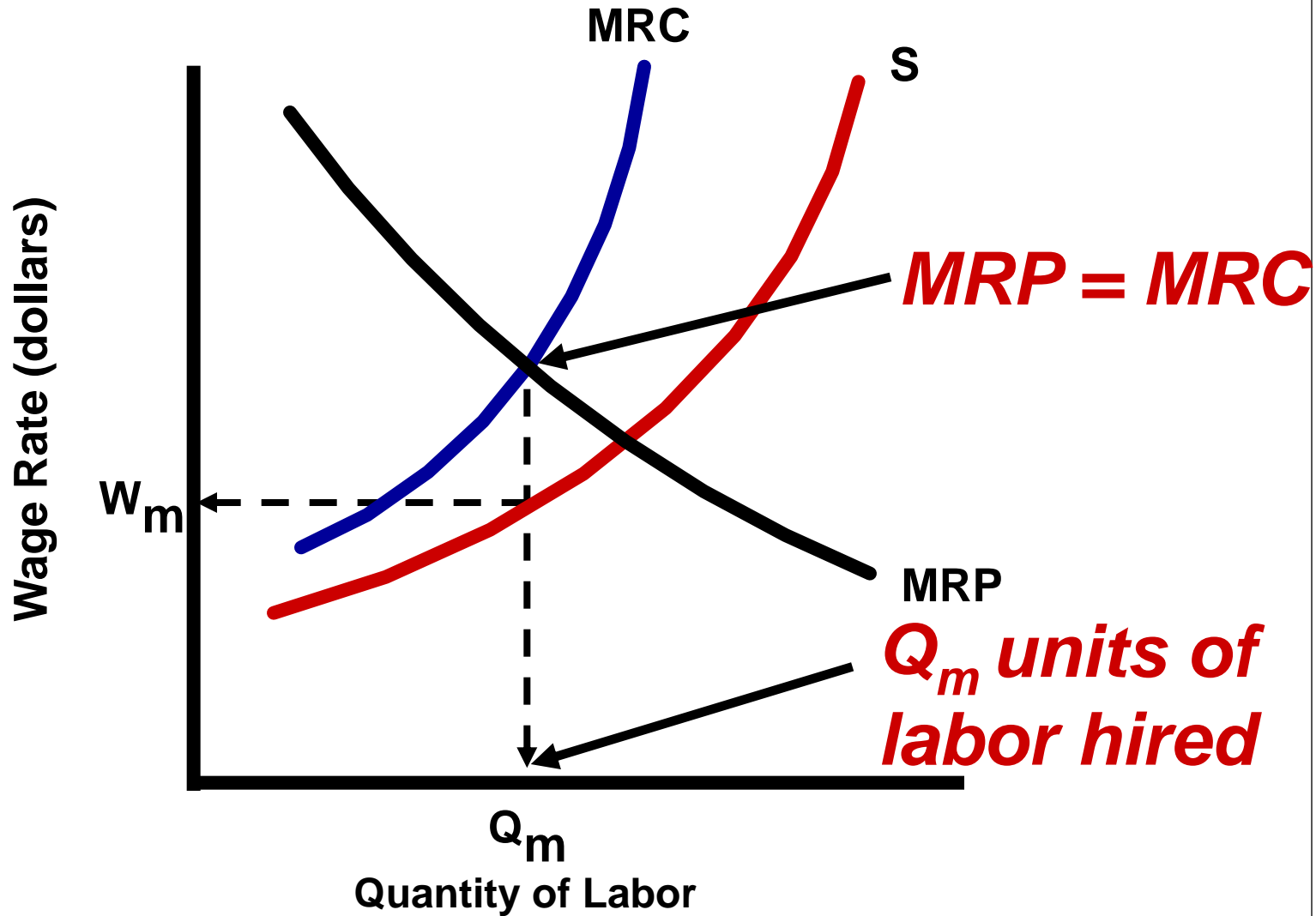
- **Single Buyer of a type of labor**
- **The type of labor is relatively immobile**
- **“Wage Maker” Behavior**

*Upward-Sloping Supply
Curve to Firm*

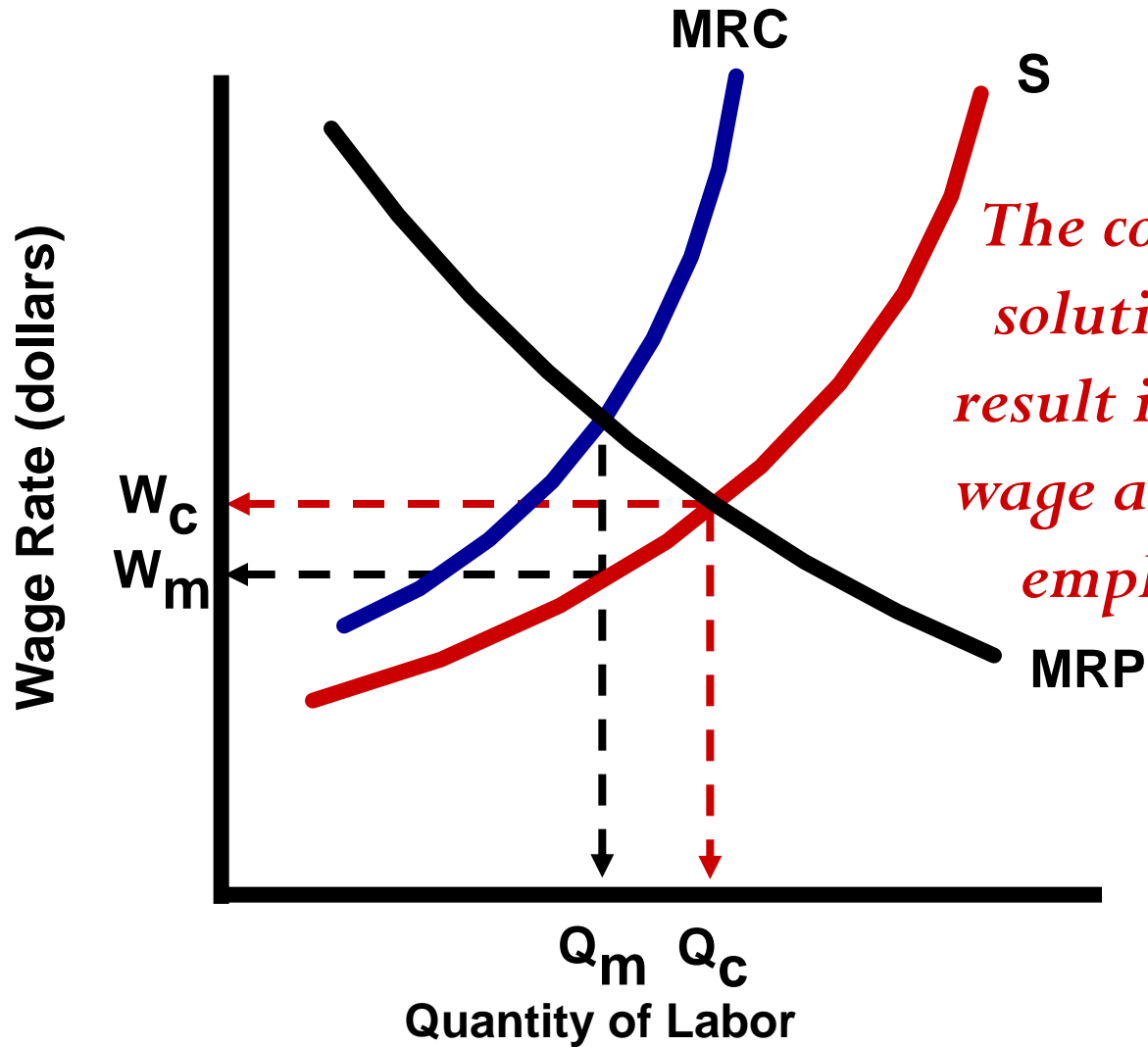
MONOPSONISTIC LABOR MARKET



MONOPSONISTIC LABOR MARKET



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MONOPSONISTIC LABOR MARKET

Monopsonists maximize profits by hiring a smaller number of workers and thereby paying a less-than-competitive wage rate.

Wage rate

Q_m Q_c

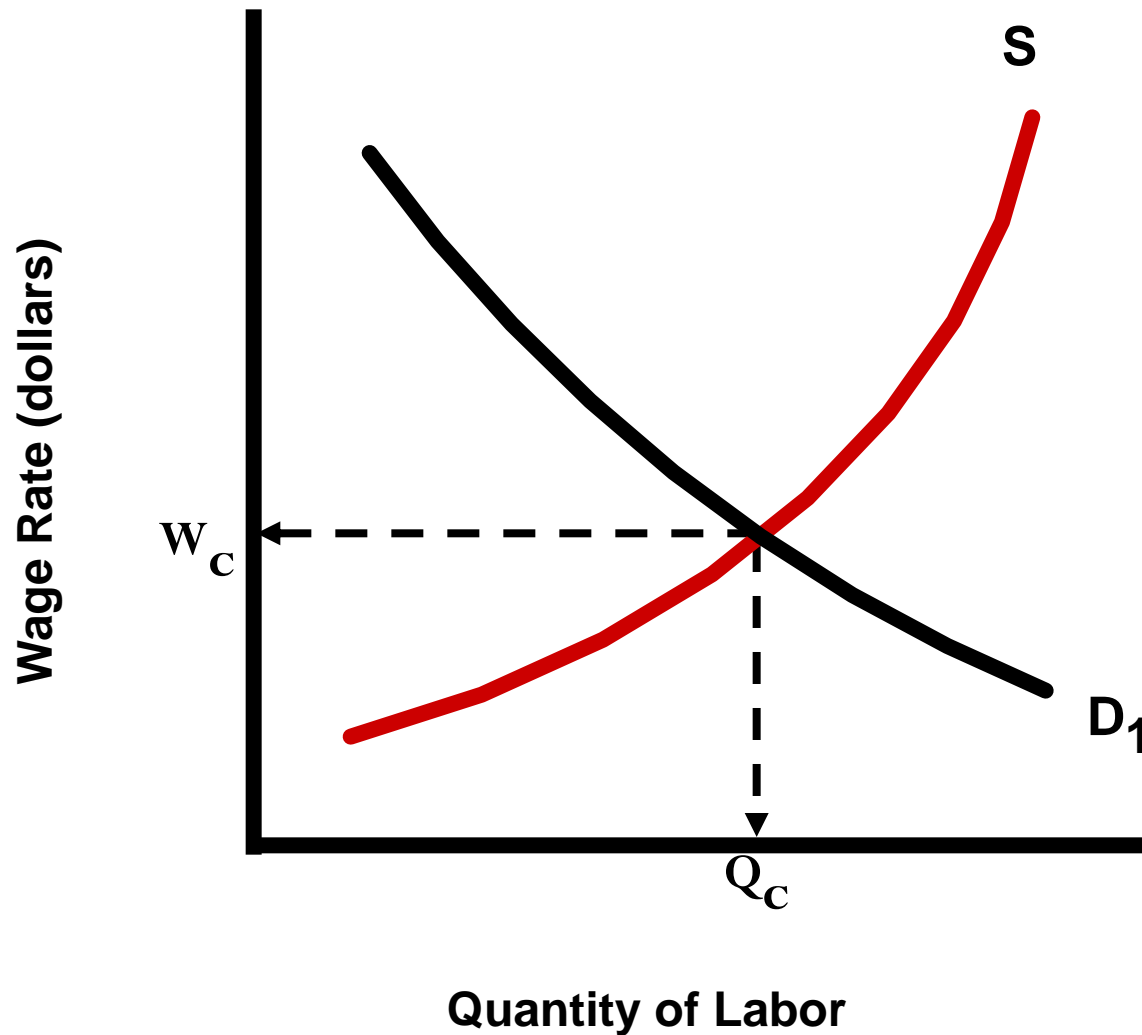
Quantity of Labor

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THREE UNION MODELS

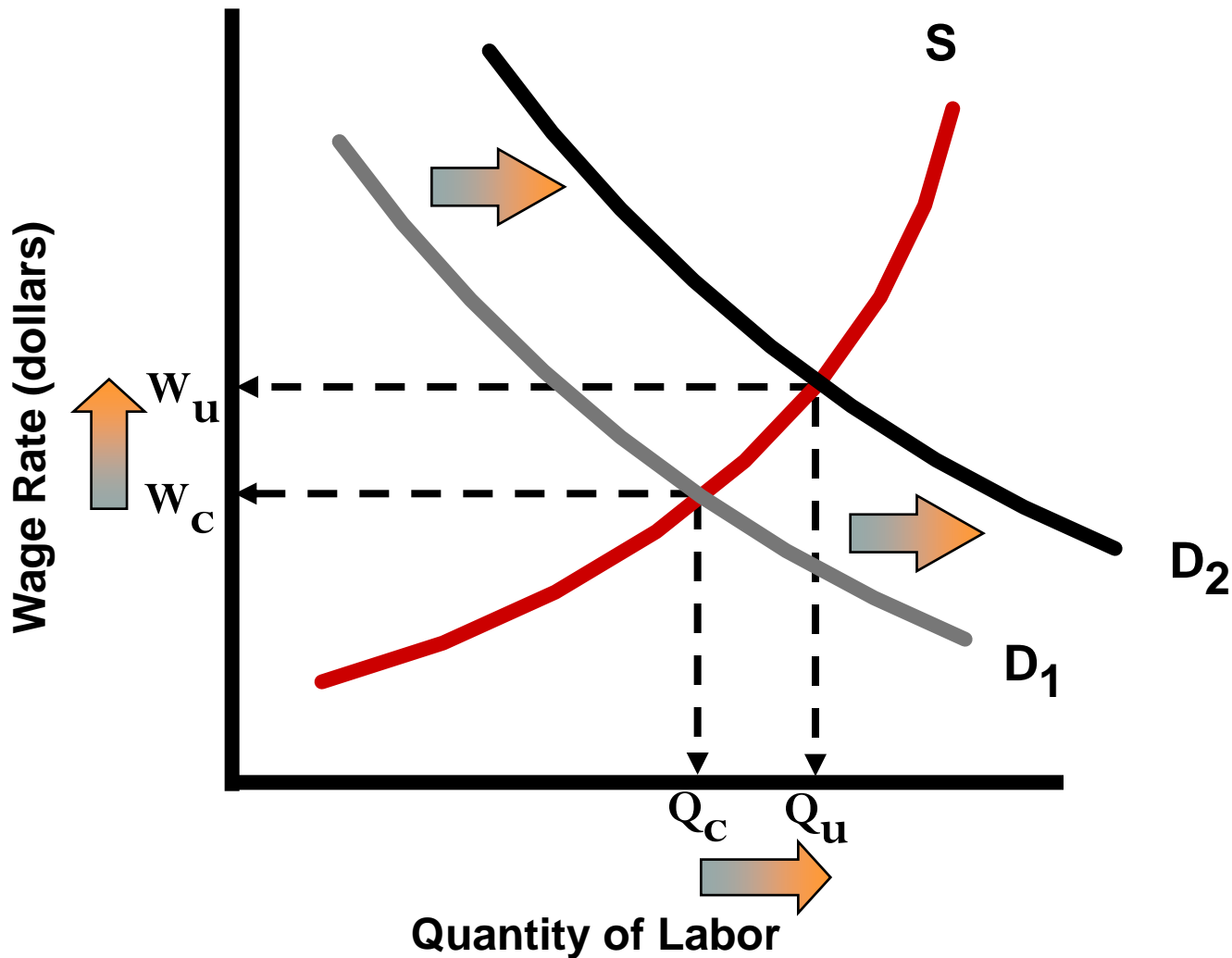
Demand-Enhancement Model



THREE UNION MODELS

Demand-Enhancement Model

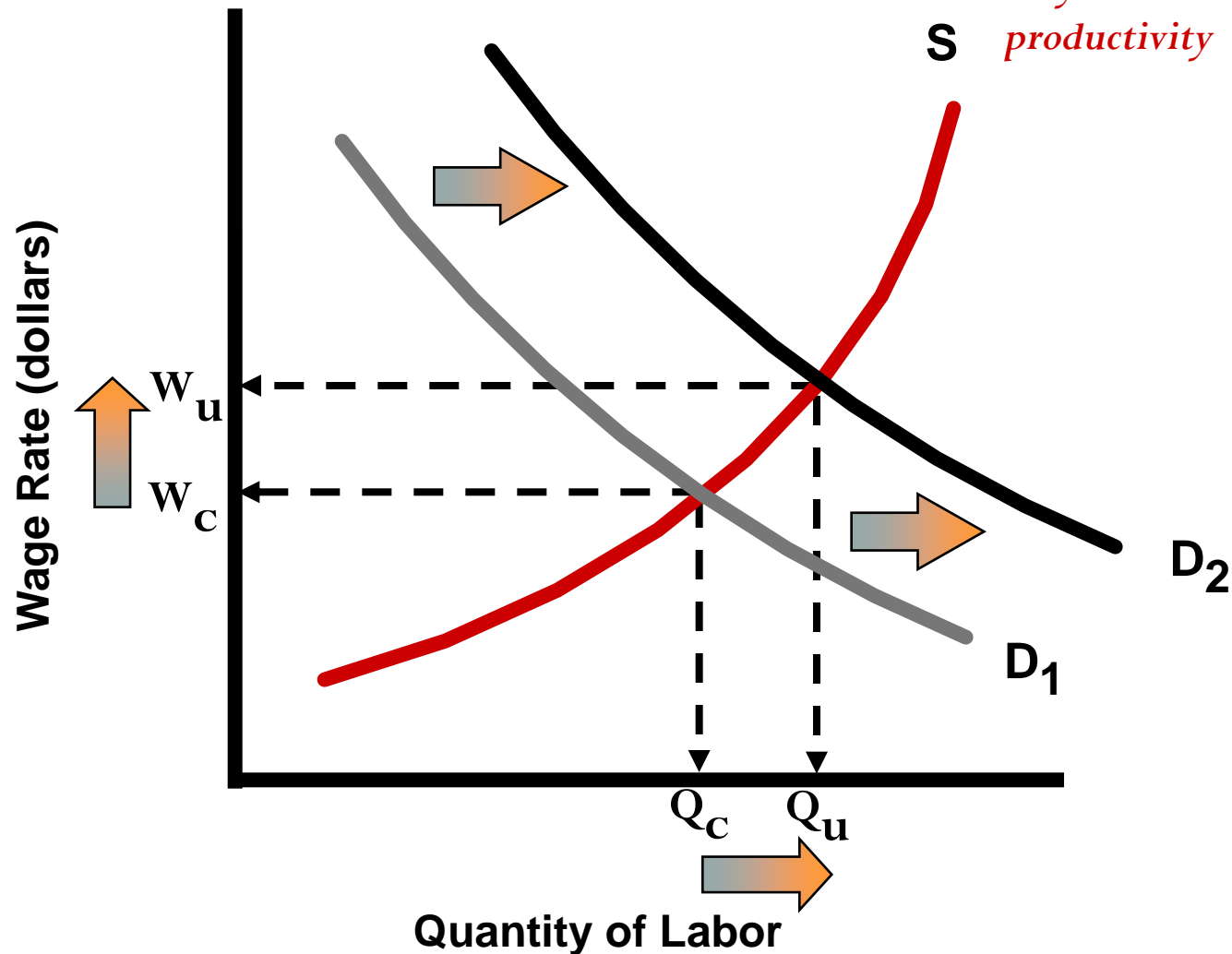
*...by increasing
product demand*



THREE UNION MODELS

Demand-Enhancement Model

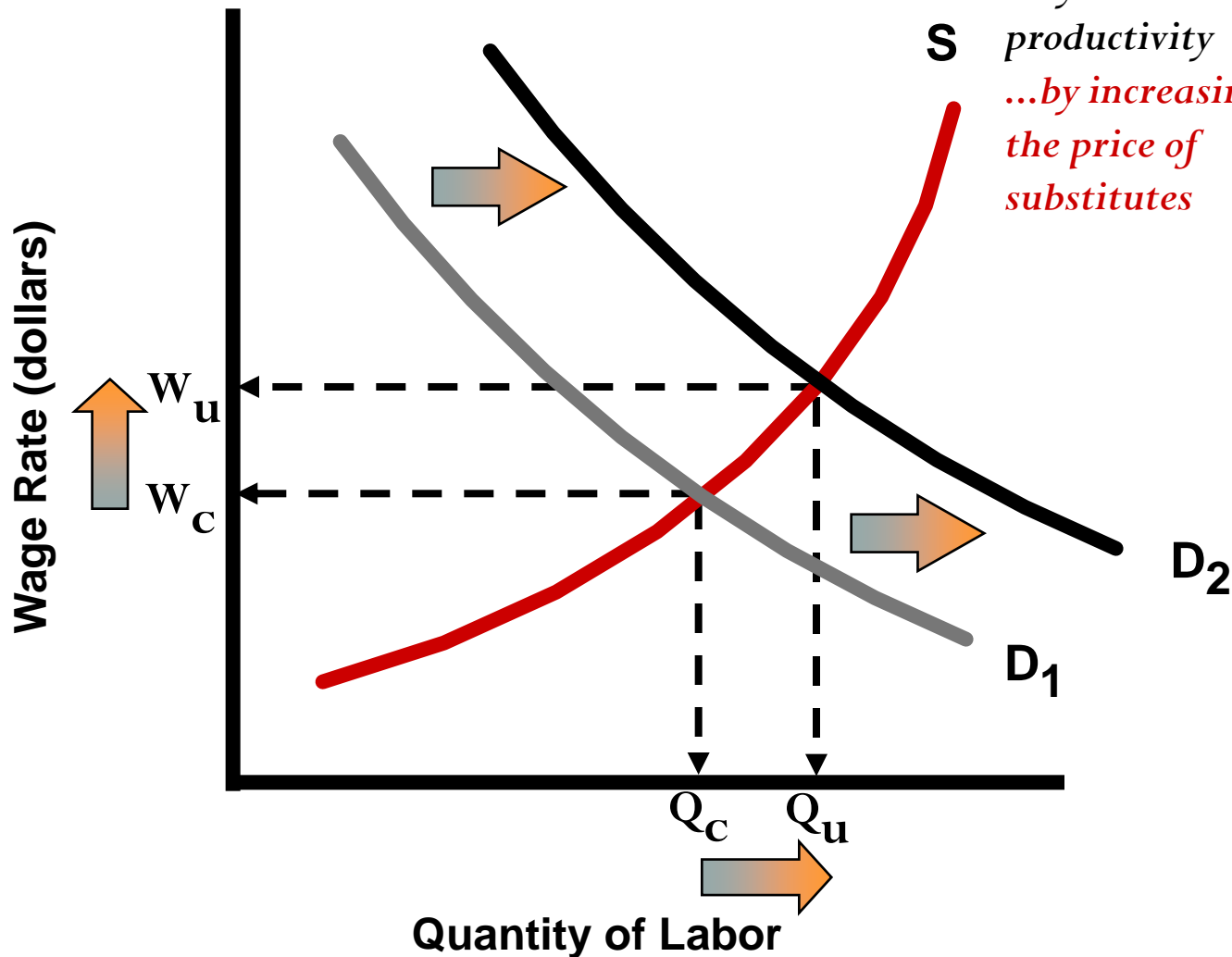
*...by increasing
product demand*
*...by increasing
productivity*



THREE UNION MODELS

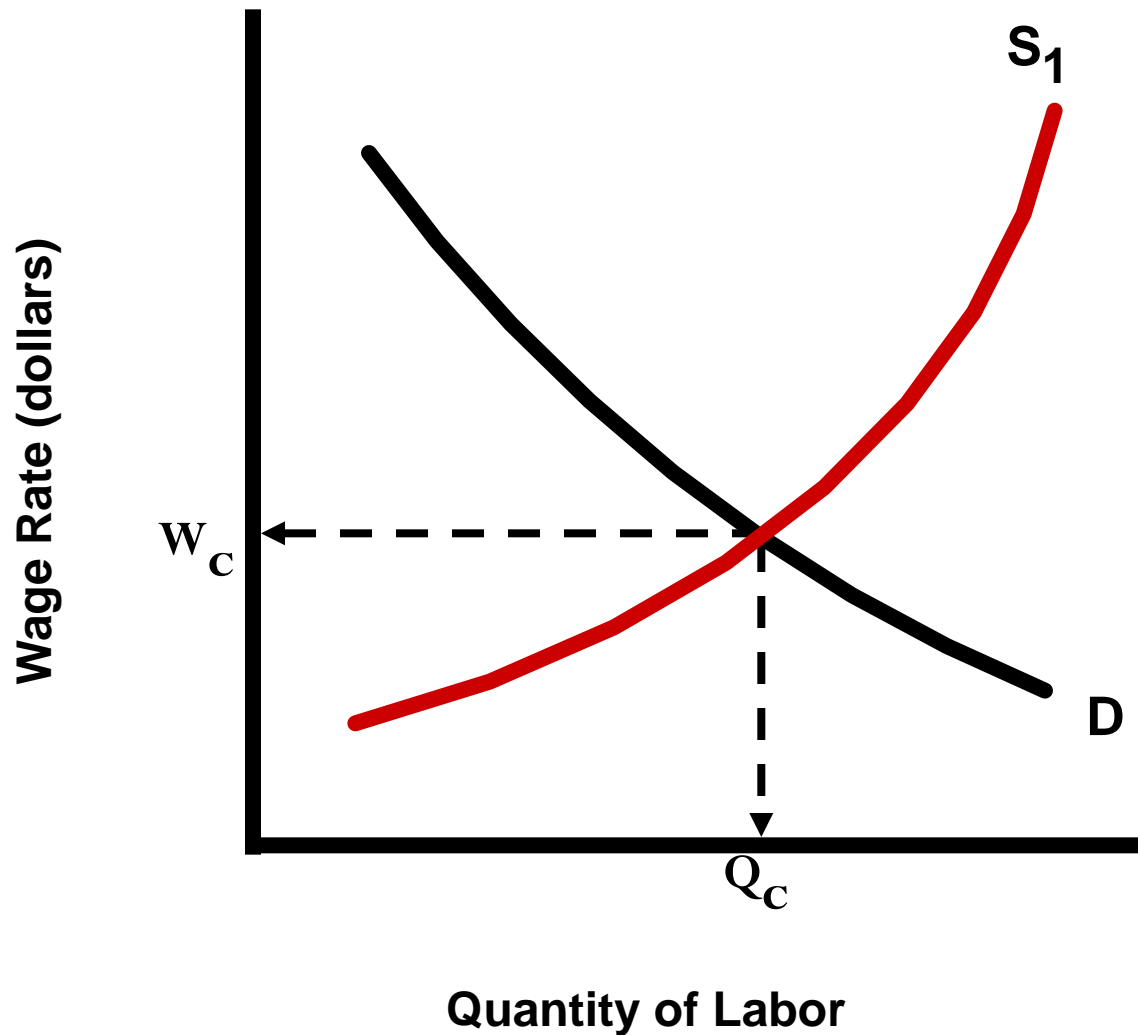
Demand-Enhancement Model

*...by increasing
product demand
...by increasing
productivity
...by increasing
the price of
substitutes*



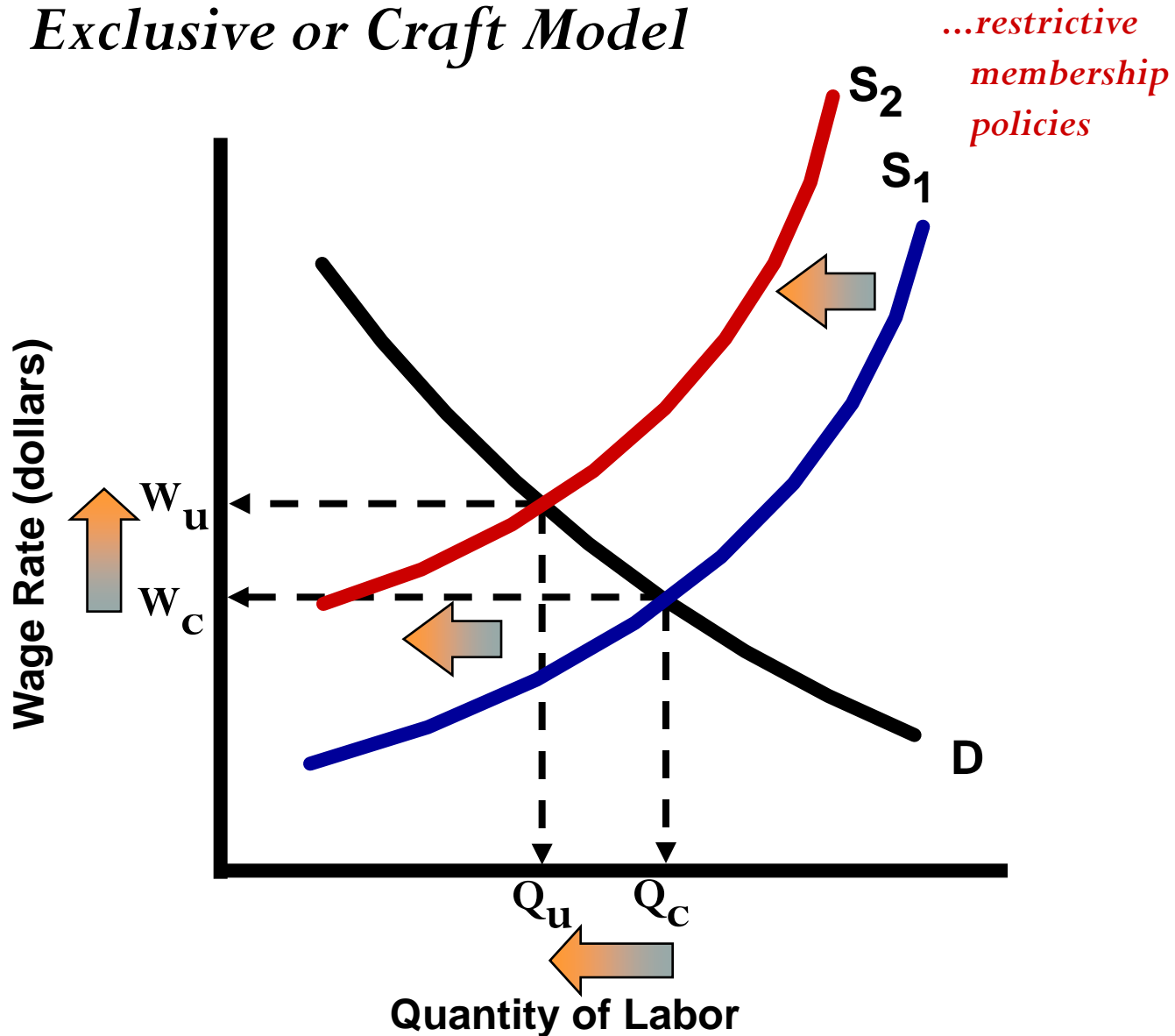
THREE UNION MODELS

Exclusive or Craft Model



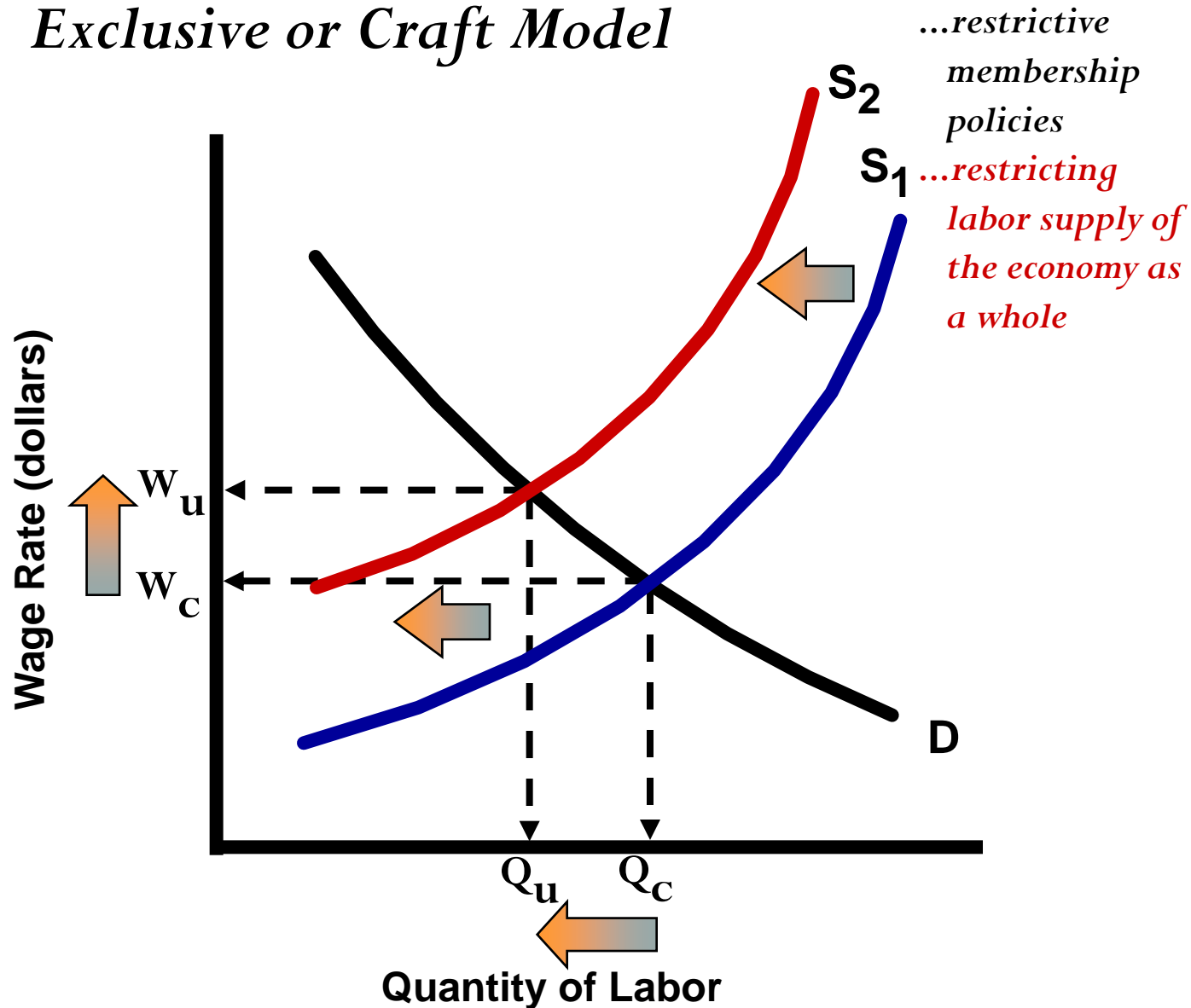
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Exclusive or Craft Model



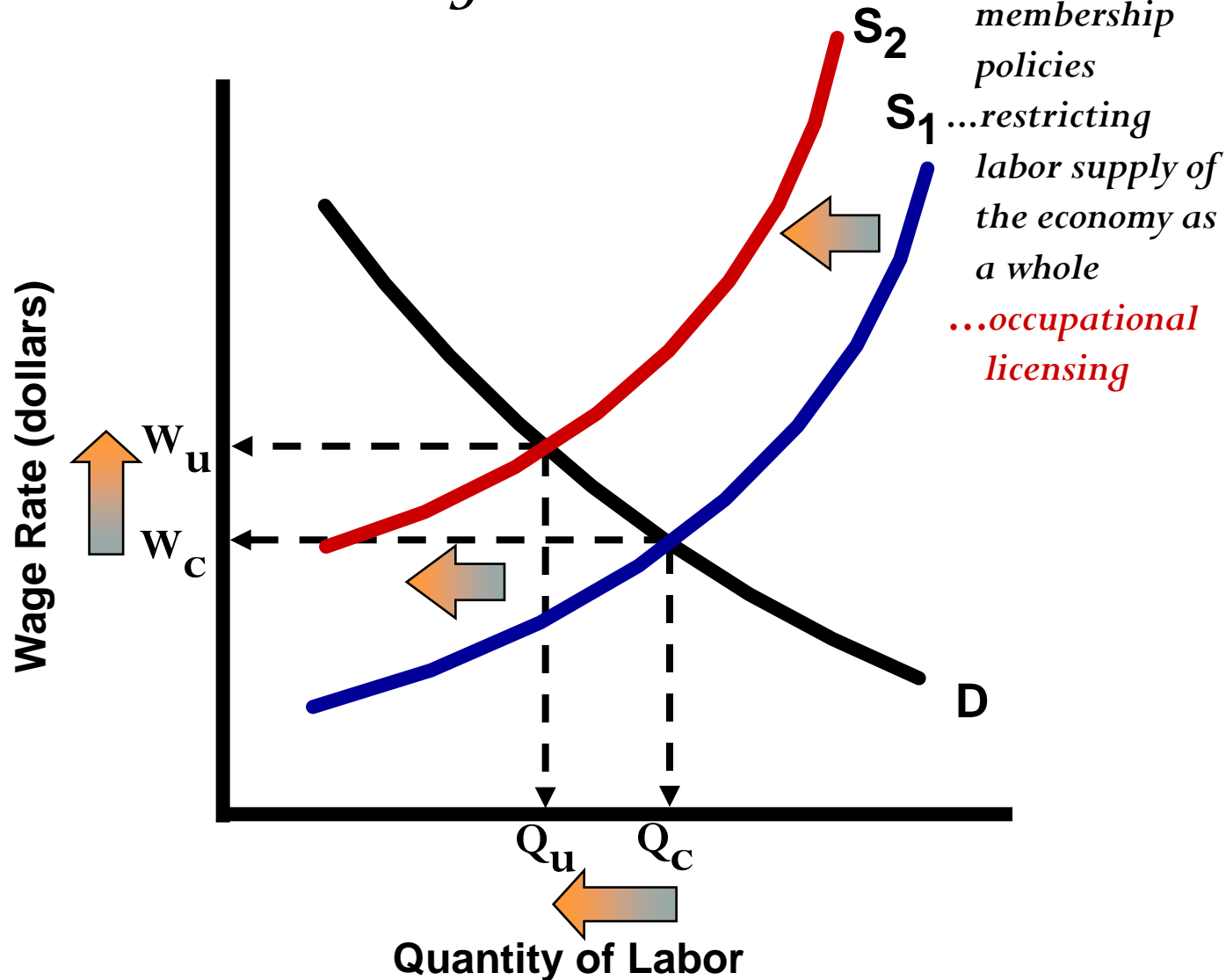
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Exclusive or Craft Model



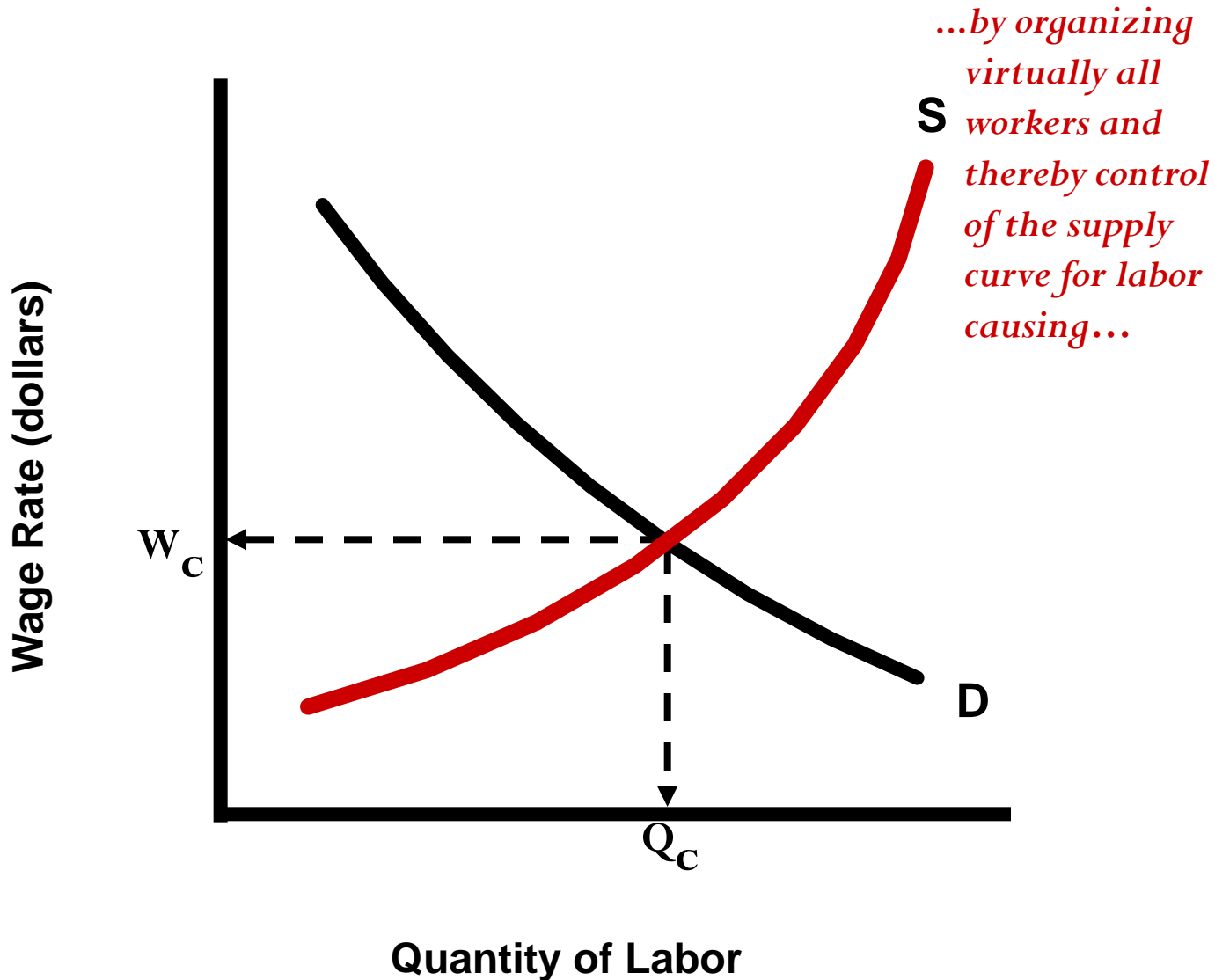
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Exclusive or Craft Model



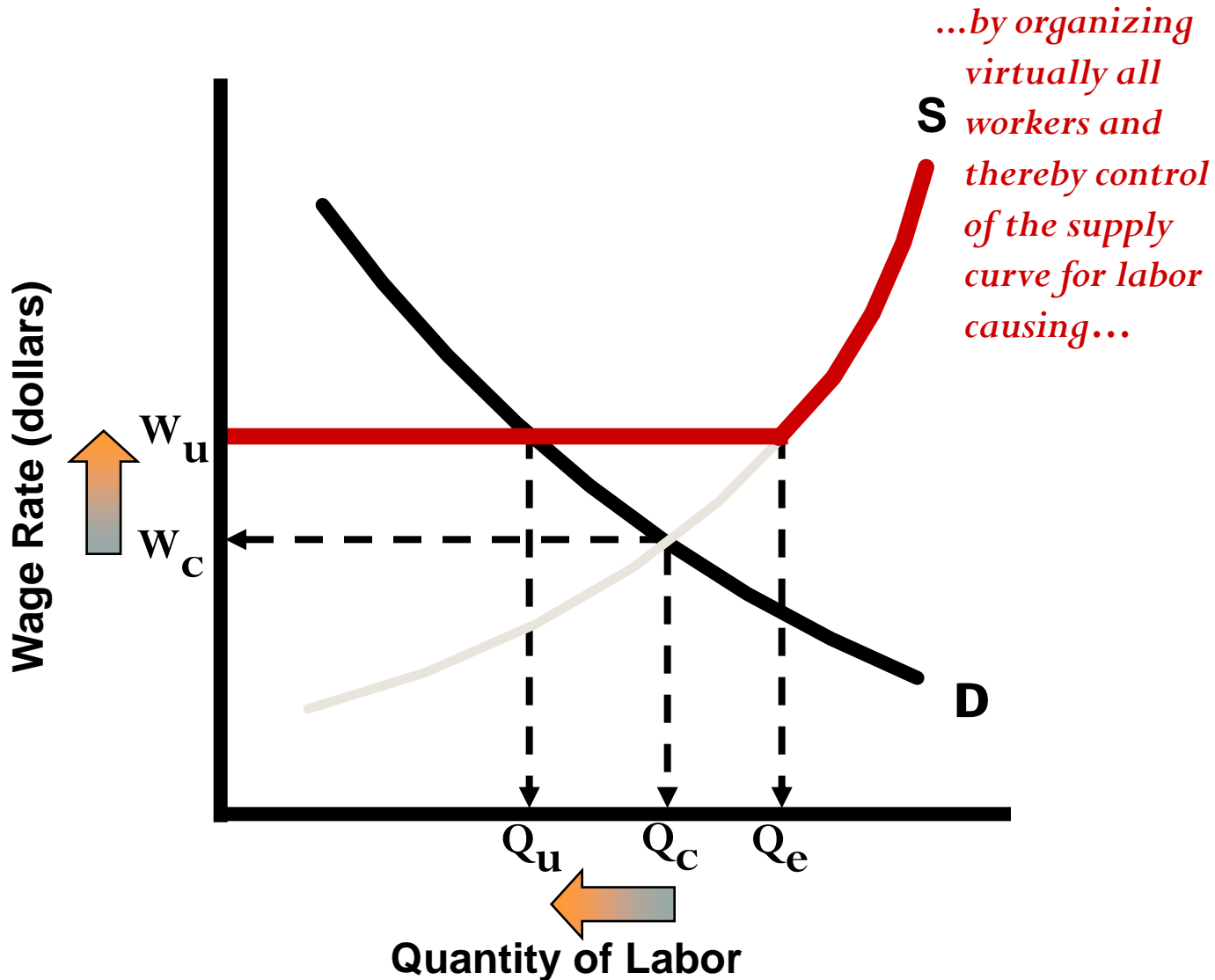
THREE UNION MODELS

Inclusive or Industrial Model



THREE UNION MODELS

Inclusive or Industrial Model



WAGE INCREASES AND UNEMPLOYMENT

- Union members receive about 15% higher wages
- Negative impact on level of employment

Negative unemployment effect

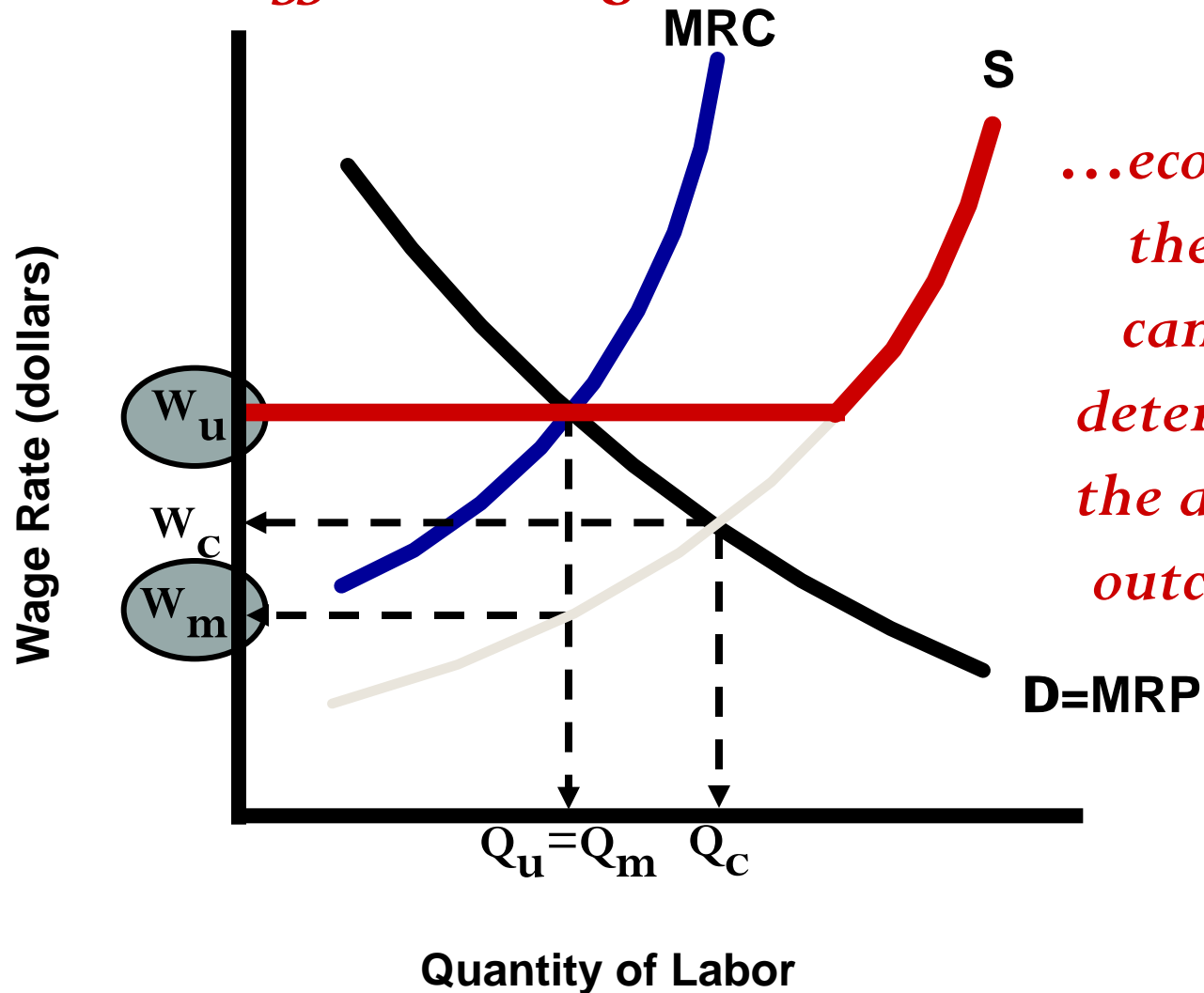
reduced by:

Growth

Elasticity

BILATERAL MONOPOLY MODEL

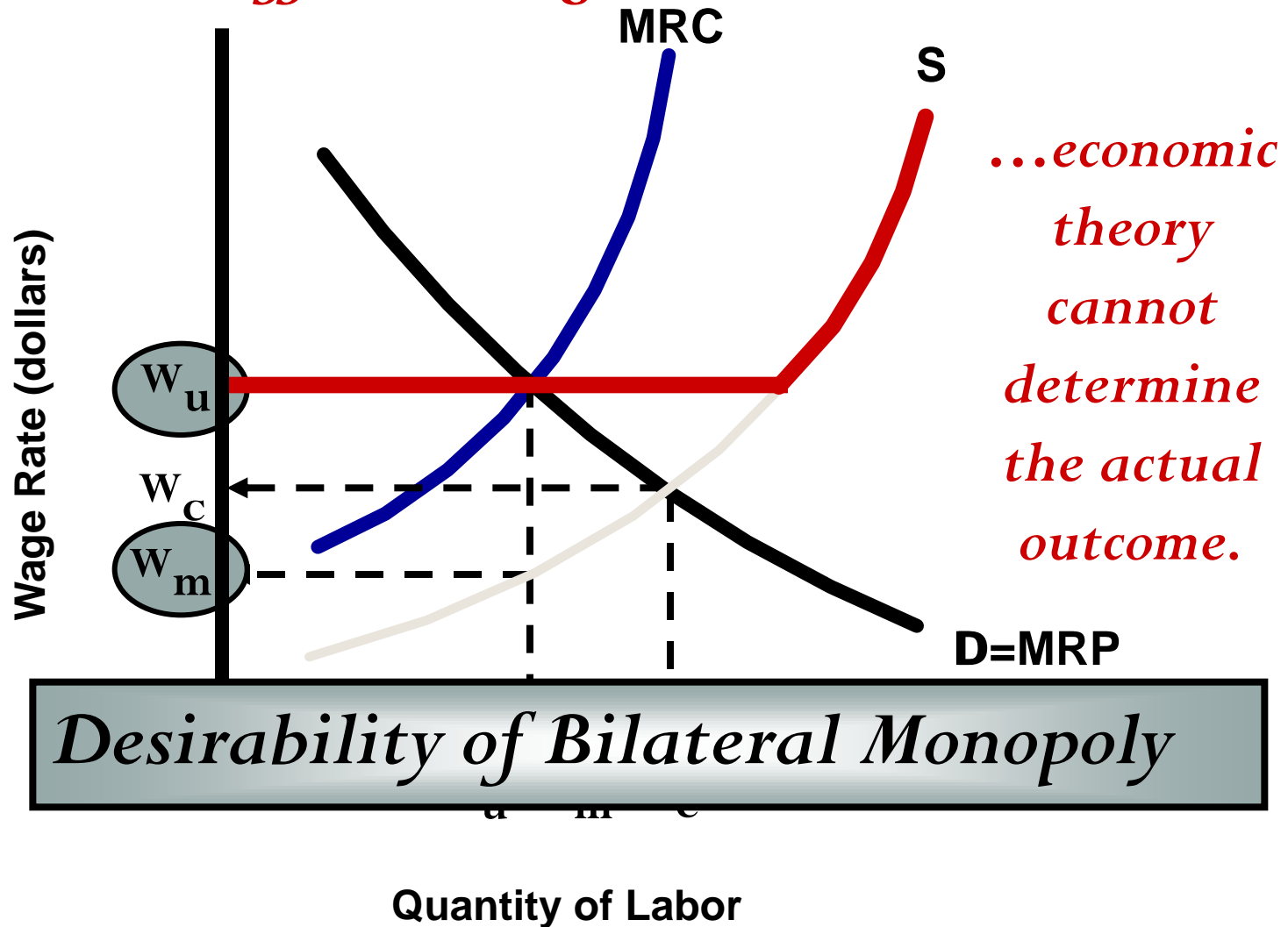
*Monopsonist & Union Seek
Different Wage Rates...*



*...economic
theory
cannot
determine
the actual
outcome.*

BILATERAL MONOPOLY MODEL

*Monopsonist & Union Seek
Different Wage Rates...*



MINIMUM WAGE CONTROVERSY

- **Case Against
Minimum Wage**
- **Case For Minimum
Wage**
- **Evidence and
Conclusions**

WAGE DIFFERENTIALS

Marginal Revenue

Productivity

Noncompeting Groups

- **Ability**
- **Education and Training**
- **Investment in Human Capital**



WAGE DIFFERENTIALS

Compensating Differences

- Nonmonetary Differences

Market Imperfections

- Lack of Job Information
- Geographical Immobility
- Unions & Government Restraints
- Discrimination

PAY FOR PERFORMANCE



The Principal-Agent Problem

Incentive Pay Plan

- Piece Rates
- Commissions or Royalties
- Bonuses, Stock Options,
& Profit Sharing
- Efficiency Wages



PAY FOR PERFORMANCE

Negative Side-Effects of Pay for Performance

- Poor Product Quality**
- Questionable or Fraudulent
Sales Practices**
- Disruption of Teamwork**
- Free Ride by Low Producers**
- Low Turnover Decreases
Hiring Opportunities**