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Wage Determination

Labor, Wages, and Earnings

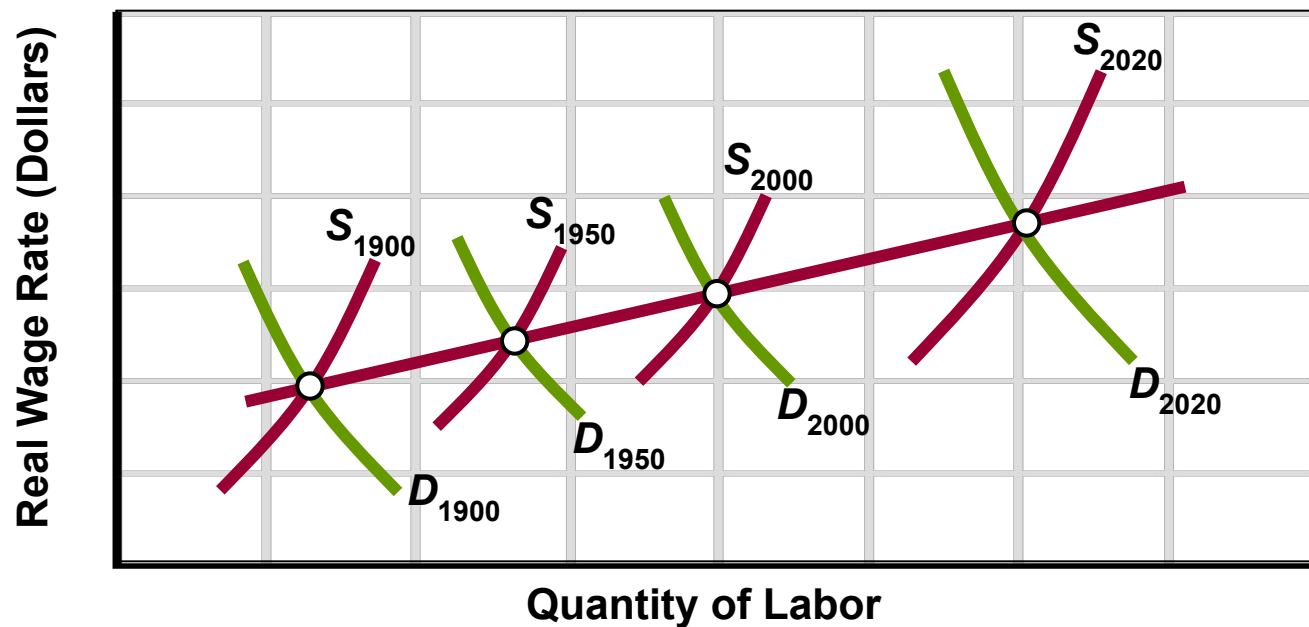
- Wages
 - Price paid for labor
 - Direct pay plus fringe benefits
- Wage rate
- Nominal wage
- Real wage
- General level of wages

Role of Productivity

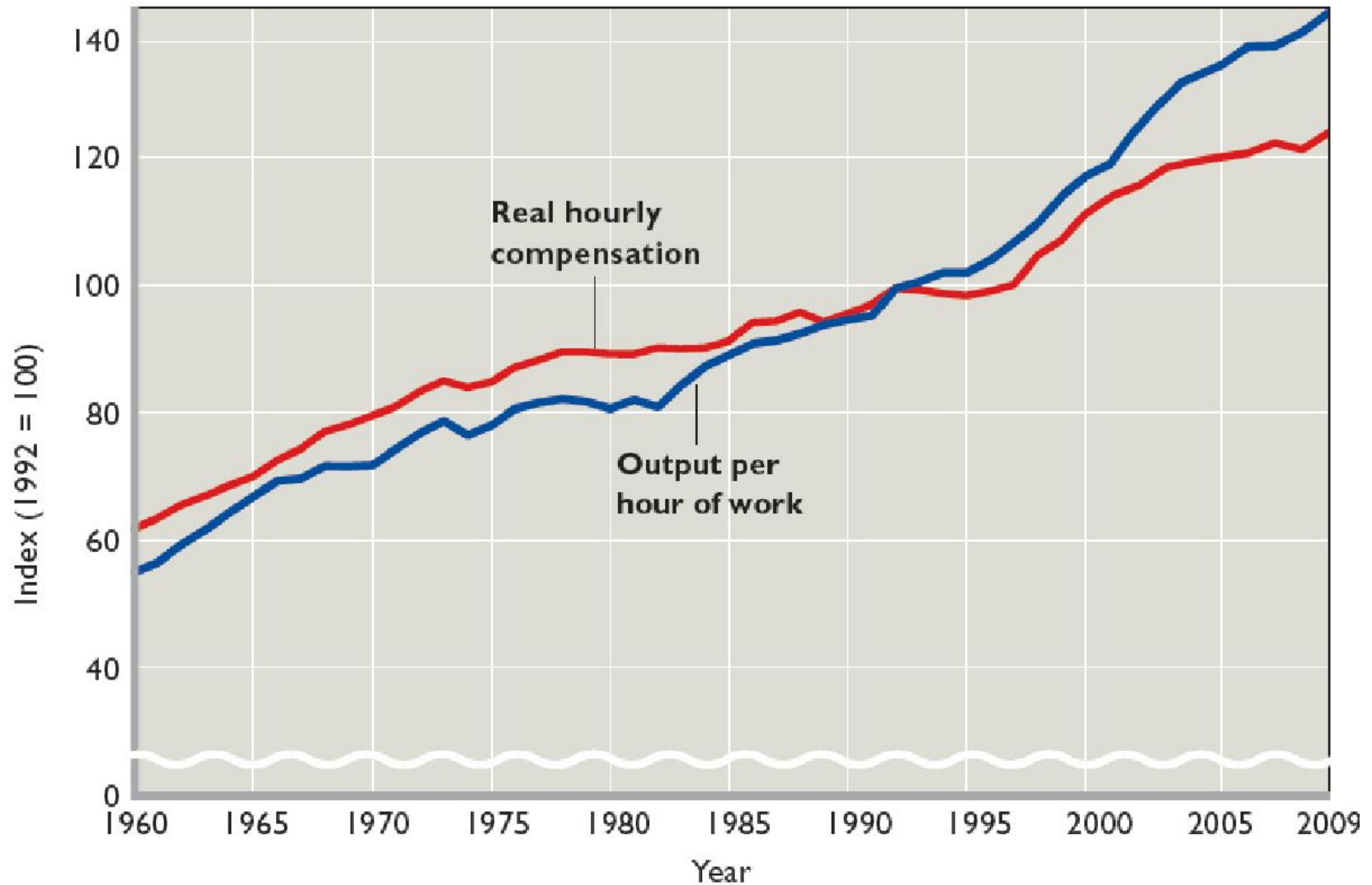
- Labor demand depends on productivity
- U.S. labor is highly productive
 - Plentiful capital
 - Access to abundant natural resources
 - Advanced technology
 - Labor quality

Real Wages and Productivity

- Long-run trend of average real wages in the U.S.



Real Wages and Productivity

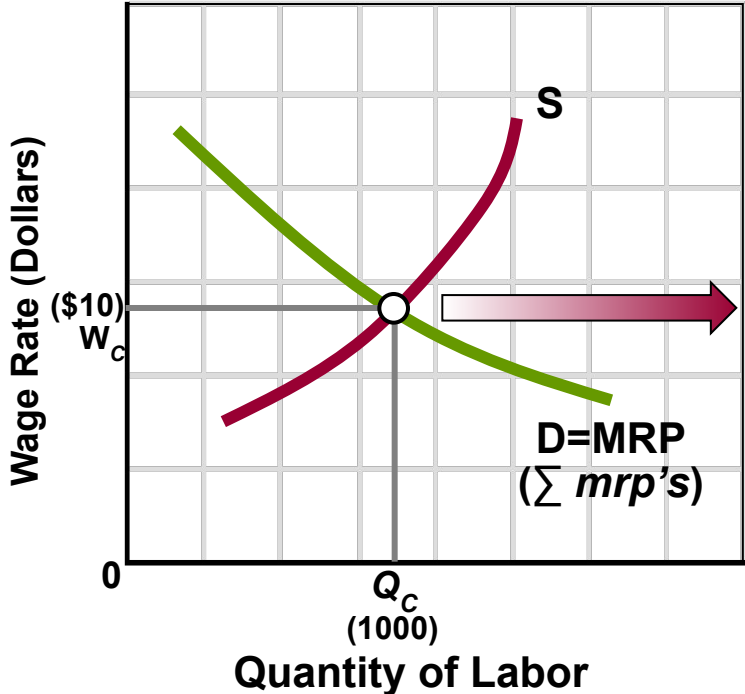


Competitive Labor Market

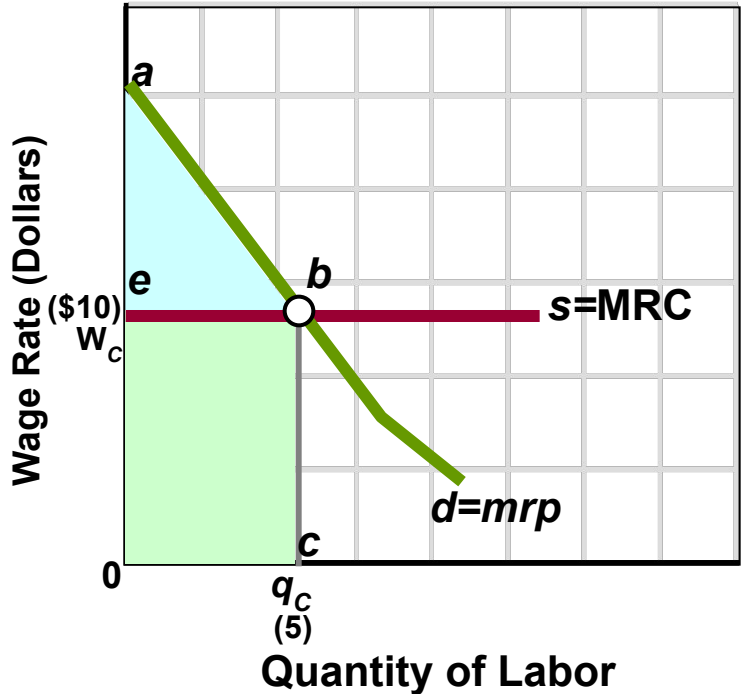
- Market demand for labor
 - Sum of firm demand
 - Example: carpenters
- Market supply for labor
 - Upward sloping
 - Competition among industries
- Labor market equilibrium
 - $MRP = MRC$ rule

Competitive Labor Market

Labor Market



Individual Firm



Monopsony Model

- Employer has buying power
- Characteristics
 - Single buyer
 - Labor immobile
 - Firm “wage maker”
- Firm labor supply is upward sloping
- MRC higher than wage rate

Monopsony Model

- Examples of monopsony power

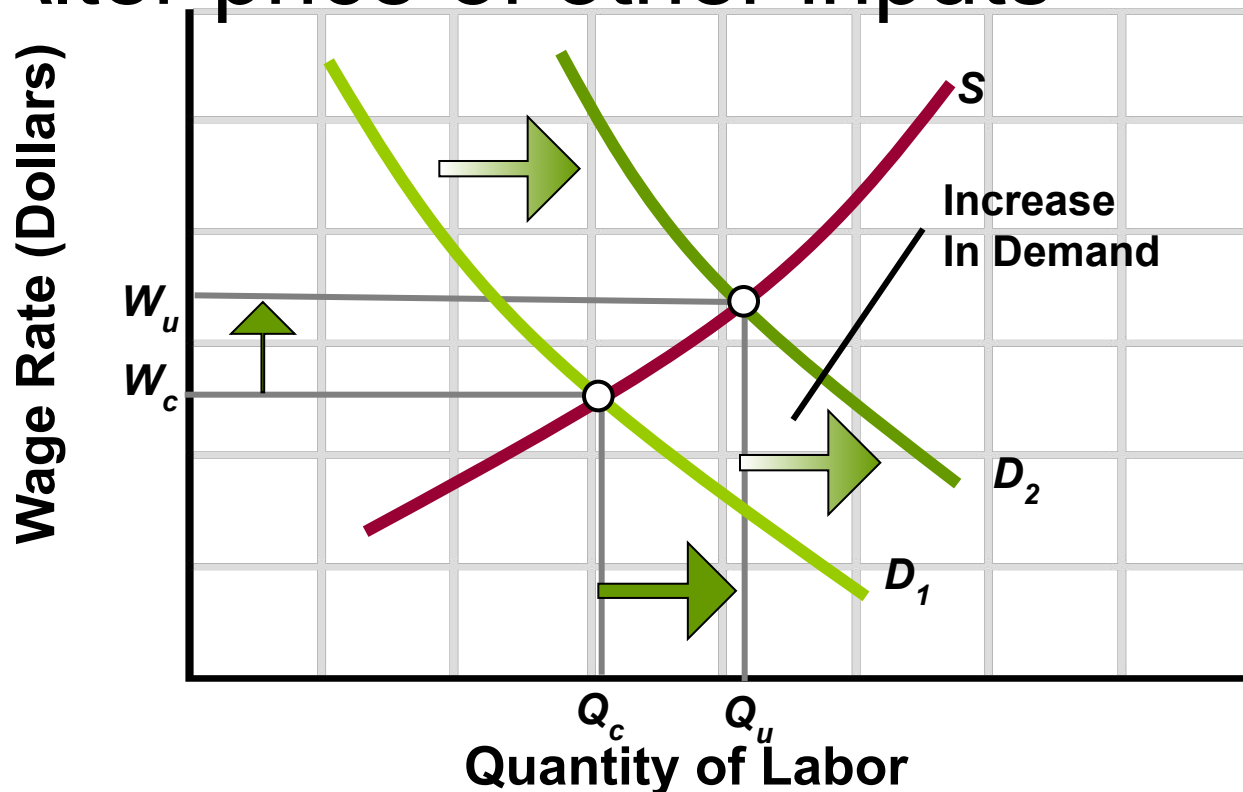


Monopsony Power

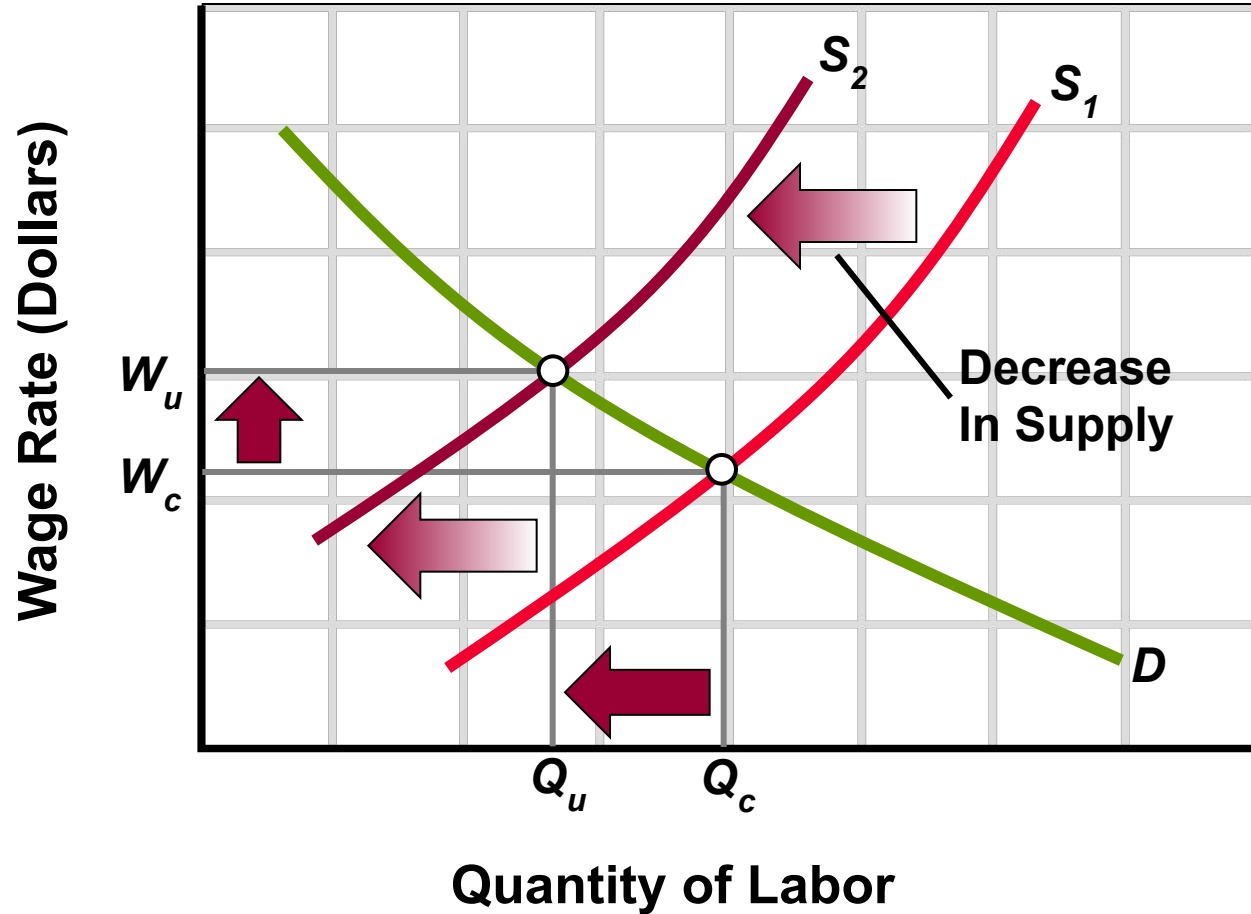
- Maximize profit by hiring smaller number of workers
- Examples of monopsony power
 - Nurses
 - Professional Athletes
 - Teachers
- Three union models

Demand Enhancement Model

- Union model
 - Increase product demand
 - Alter price of other inputs

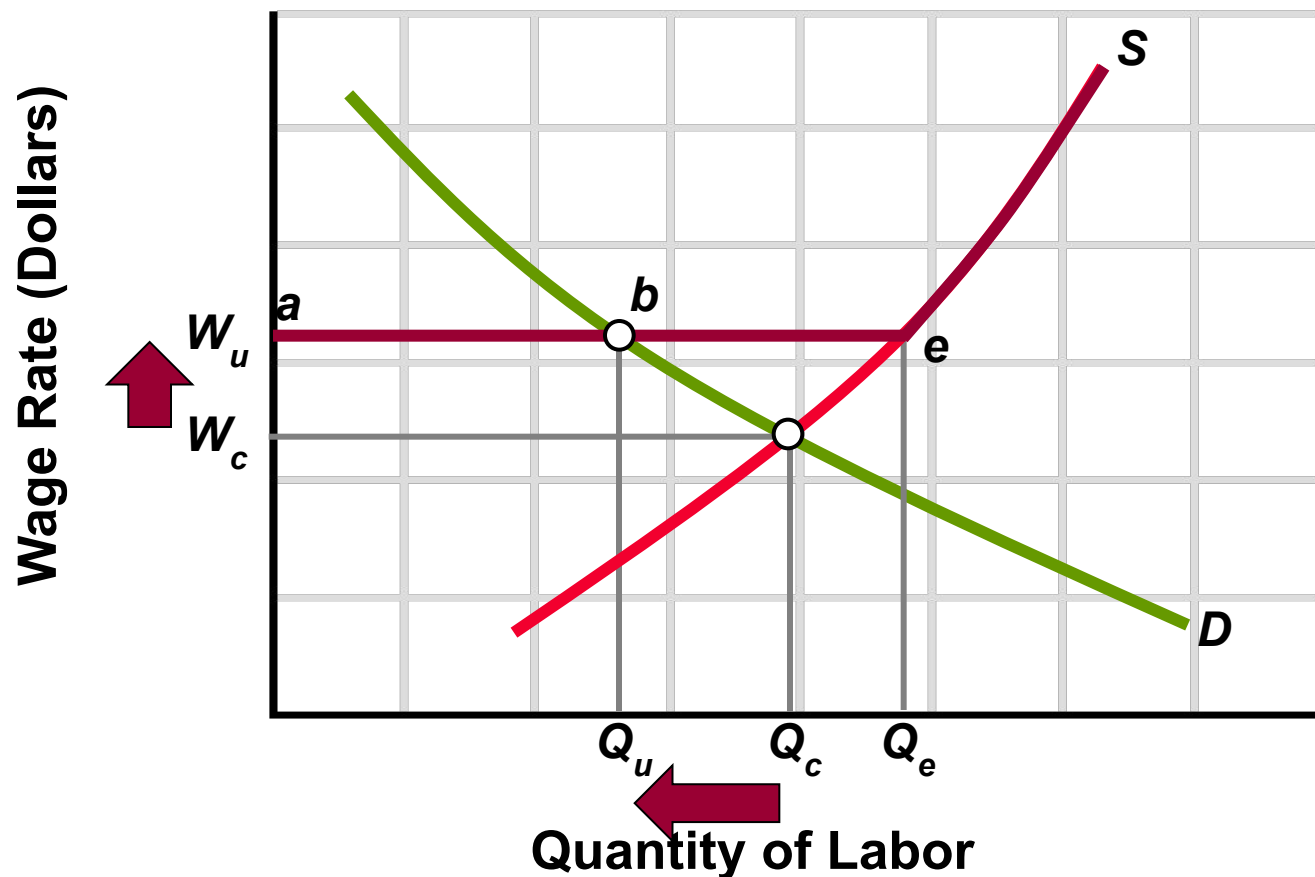


Craft Union Model



Industrial Union Model

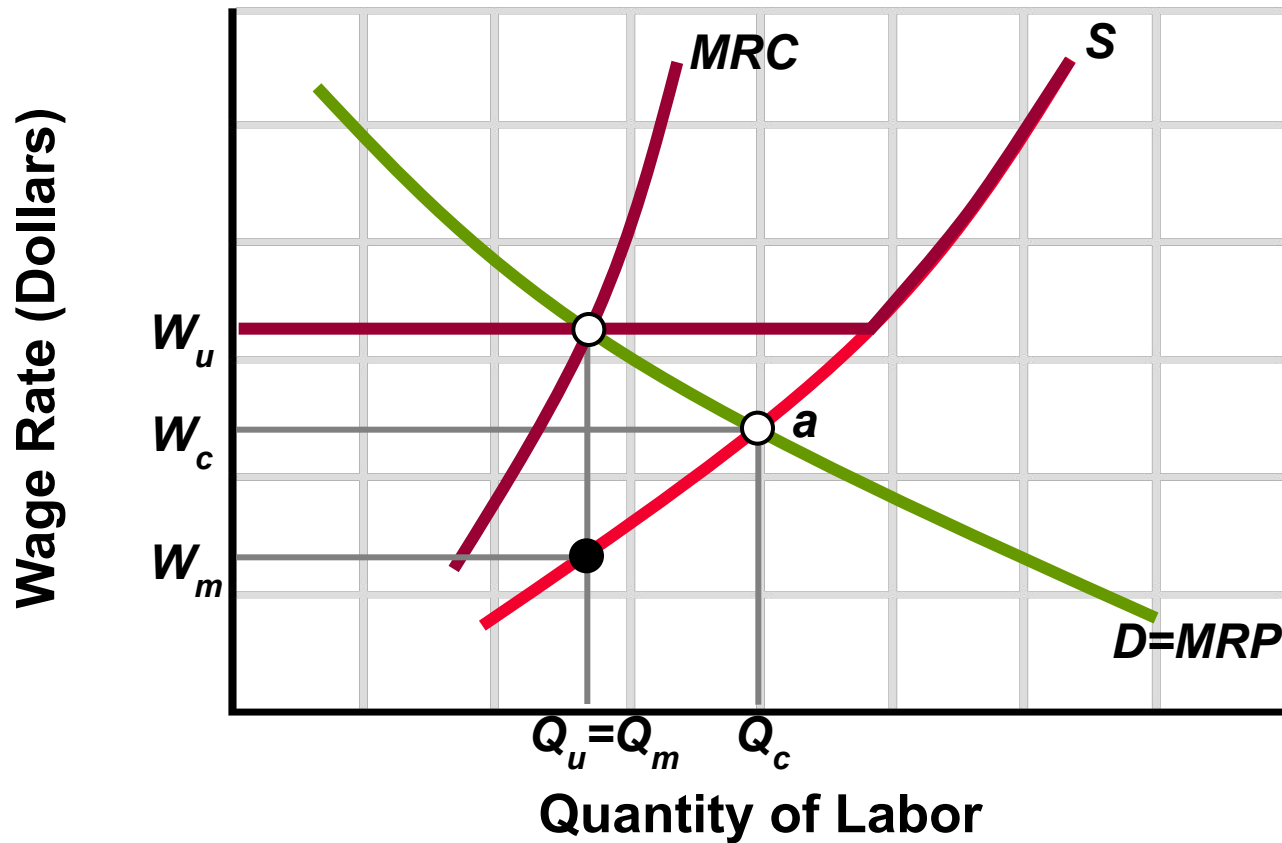
- Inclusive unionism
 - Auto and steel workers



Bilateral Monopoly Model

- Monopsony and inclusive unionism
- Single buyer and seller
- Not uncommon
- Indeterminate outcome
- Desirability

Bilateral Monopoly Model



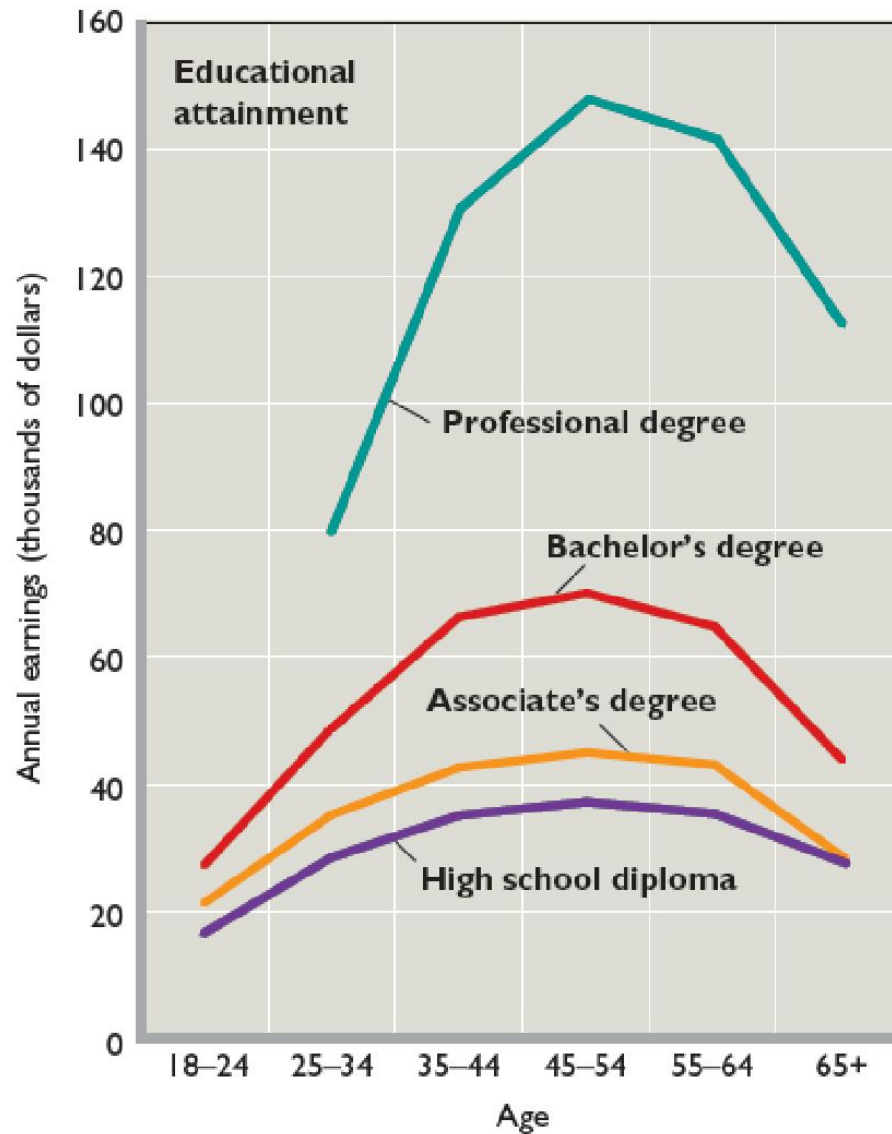
The Minimum Wage Controversy

- Case against minimum wage
- Case for minimum wage
- State and locally set rates
- Evidence and conclusions

Wage Differentials

- Differences across occupations
- What explains wage differentials?
- Marginal revenue productivity
- Noncompeting groups
 - Ability
 - Education and training
- Compensating differences

Wage Differentials



Wage Differentials

- Workers prevented from moving to higher paying jobs
- Market imperfections
 - Lack of job information
 - Geographic immobility
 - Unions and government restraints
 - Discrimination

Pay for Performance

- The principal-agent problem
- Incentive pay plan
 - Piece rates
 - Commissions or royalties
 - Bonuses, stock options, and profit sharing
 - Efficiency wages
- Negative side-effects