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# Wage Determination

# Labor, Wages, and Earnings

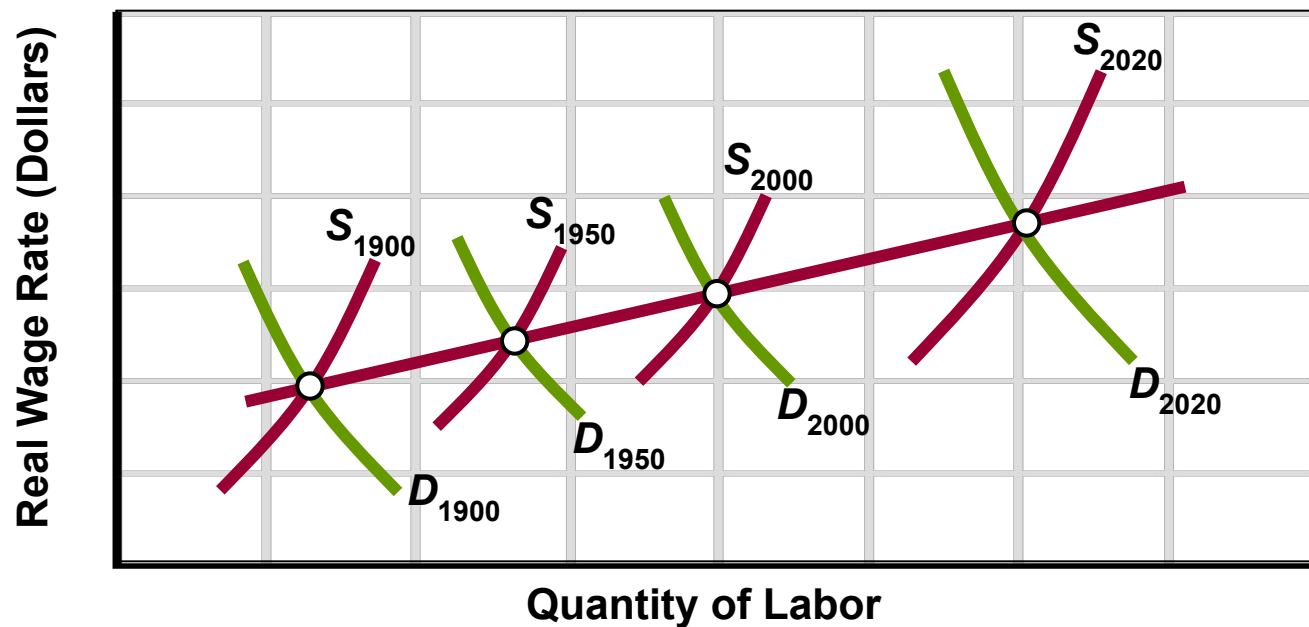
- Wages
  - Price paid for labor
  - Direct pay plus fringe benefits
- Wage rate
- Nominal wage
- Real wage
- General level of wages

# Role of Productivity

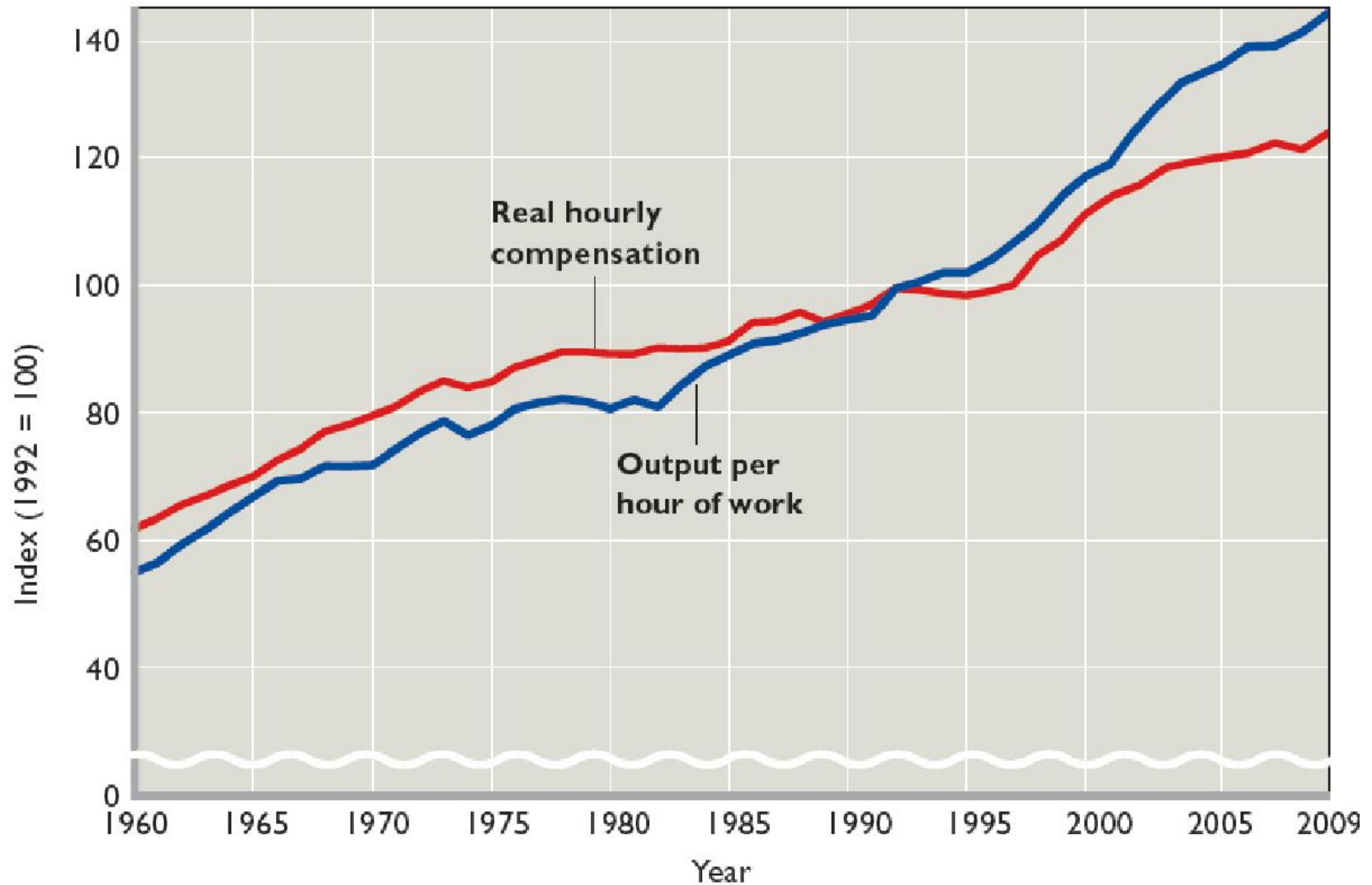
- Labor demand depends on productivity
- U.S. labor is highly productive
  - Plentiful capital
  - Access to abundant natural resources
  - Advanced technology
  - Labor quality

# Real Wages and Productivity

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



# Real Wages and Productivity

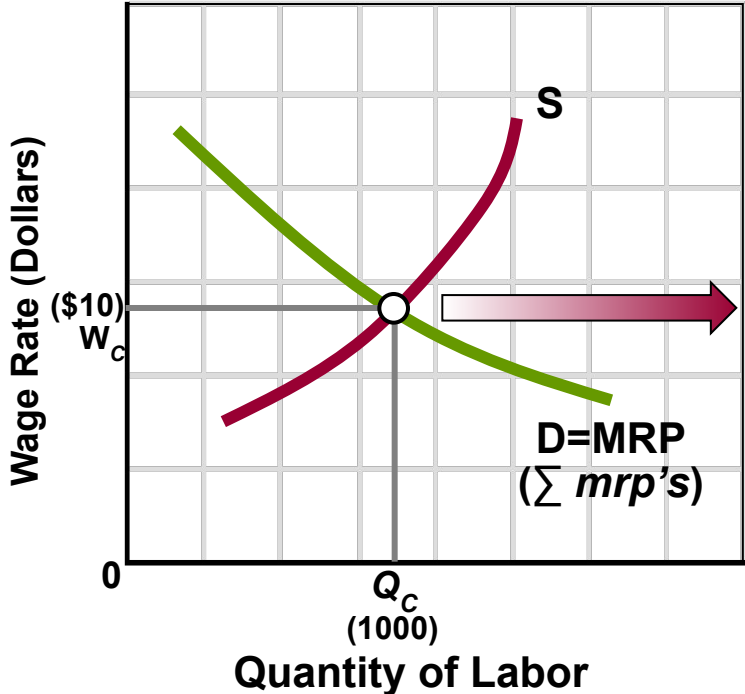


# Competitive Labor Market

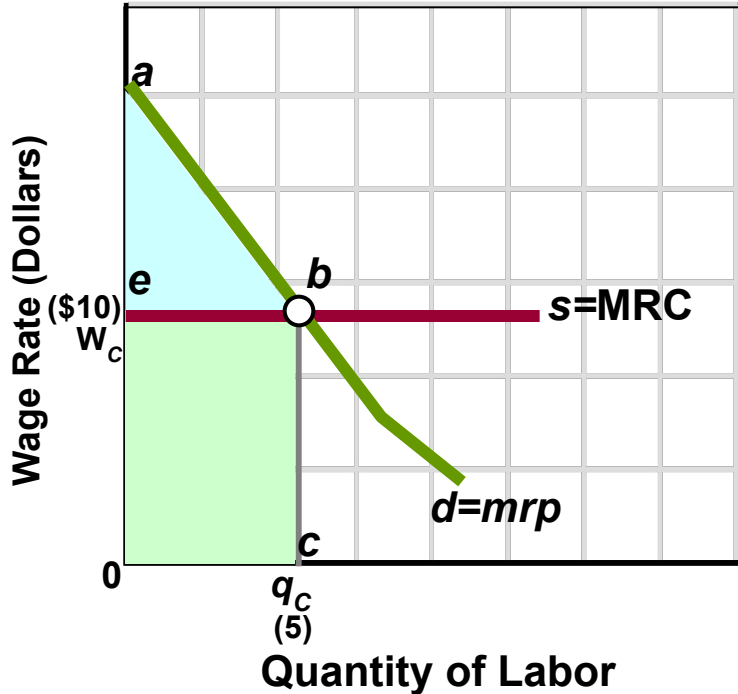
- Market demand for labor
  - Sum of firm demand
  - Example: carpenters
- Market supply for labor
  - Upward sloping
  - Competition among industries
- Labor market equilibrium
  - $MRP = MRC$  rule

# 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

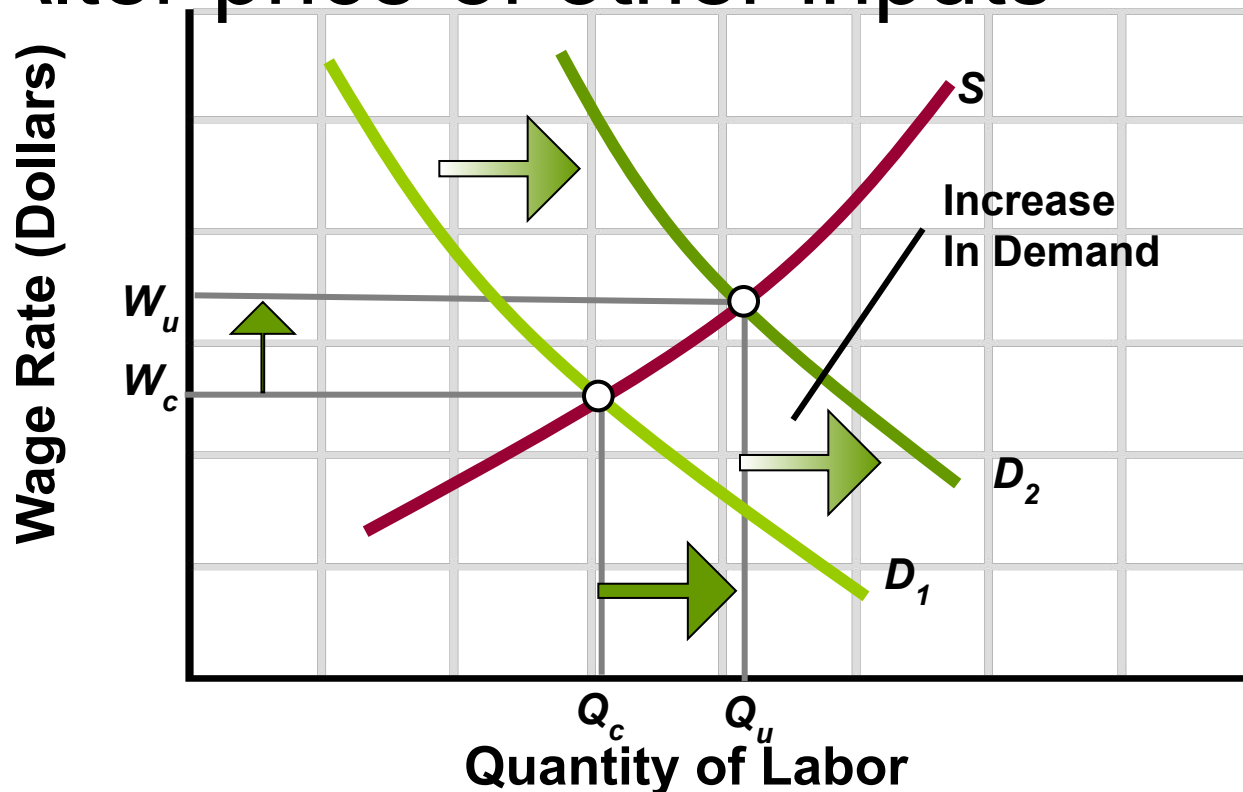


# Monopsony Power

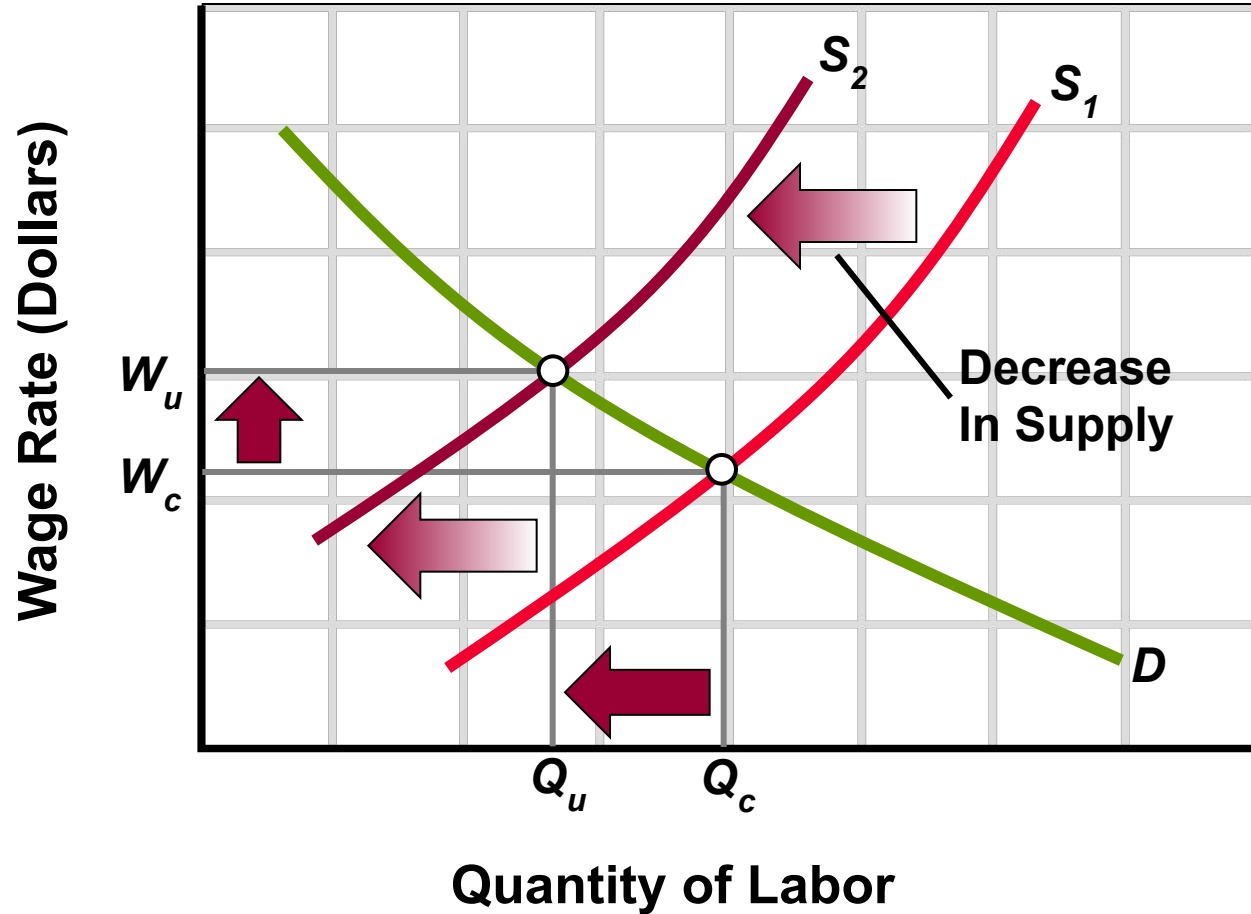
- Maximize profit by hiring smaller number of workers
- Examples of monopsony power
  - Nurses
  - Professional Athletes
  - Teachers
- Three union models

# Demand Enhancement Model

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

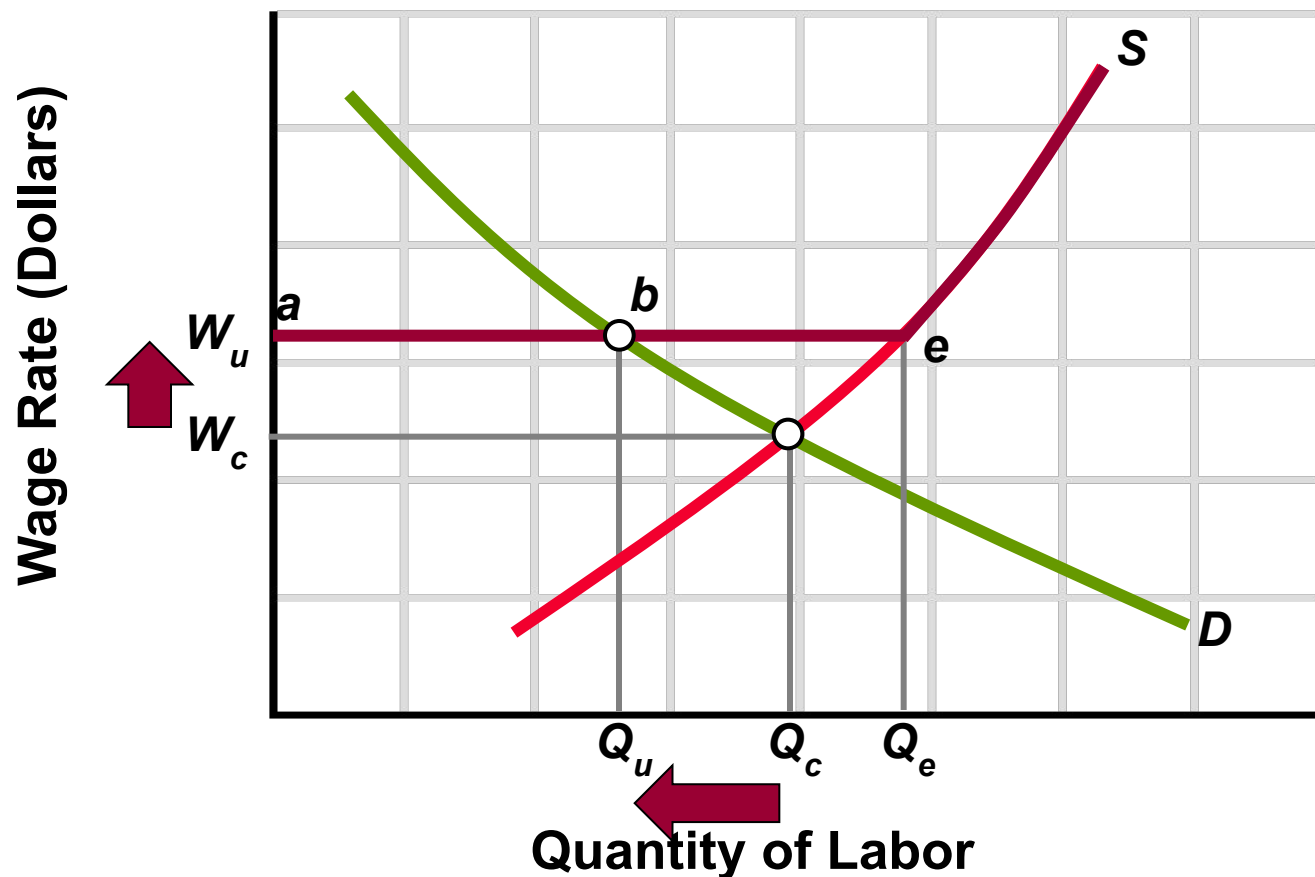


# Craft Union Model



# Industrial Union Model

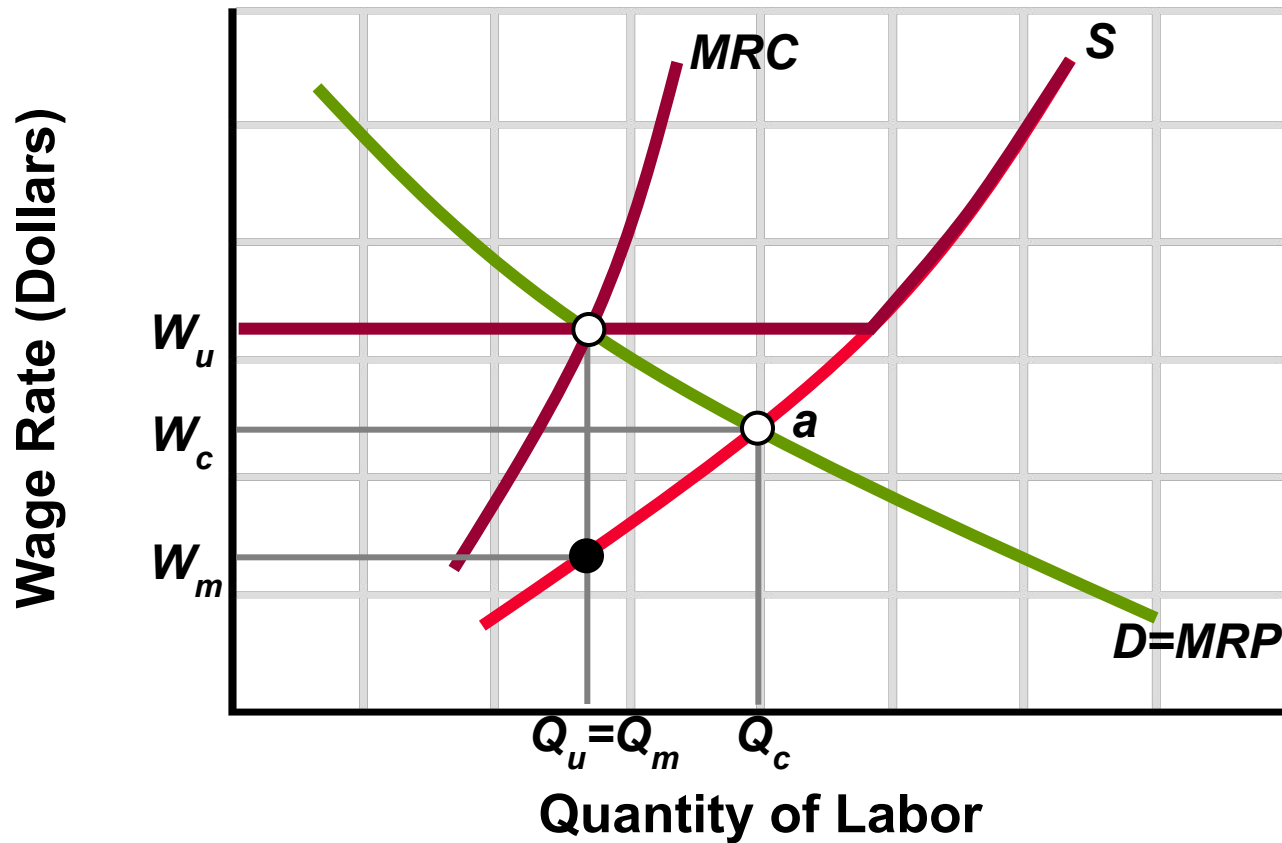
- Inclusive unionism
  - Auto and steel workers



# Bilateral Monopoly Model

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

# Bilateral Monopoly Model



# The Minimum Wage Controversy

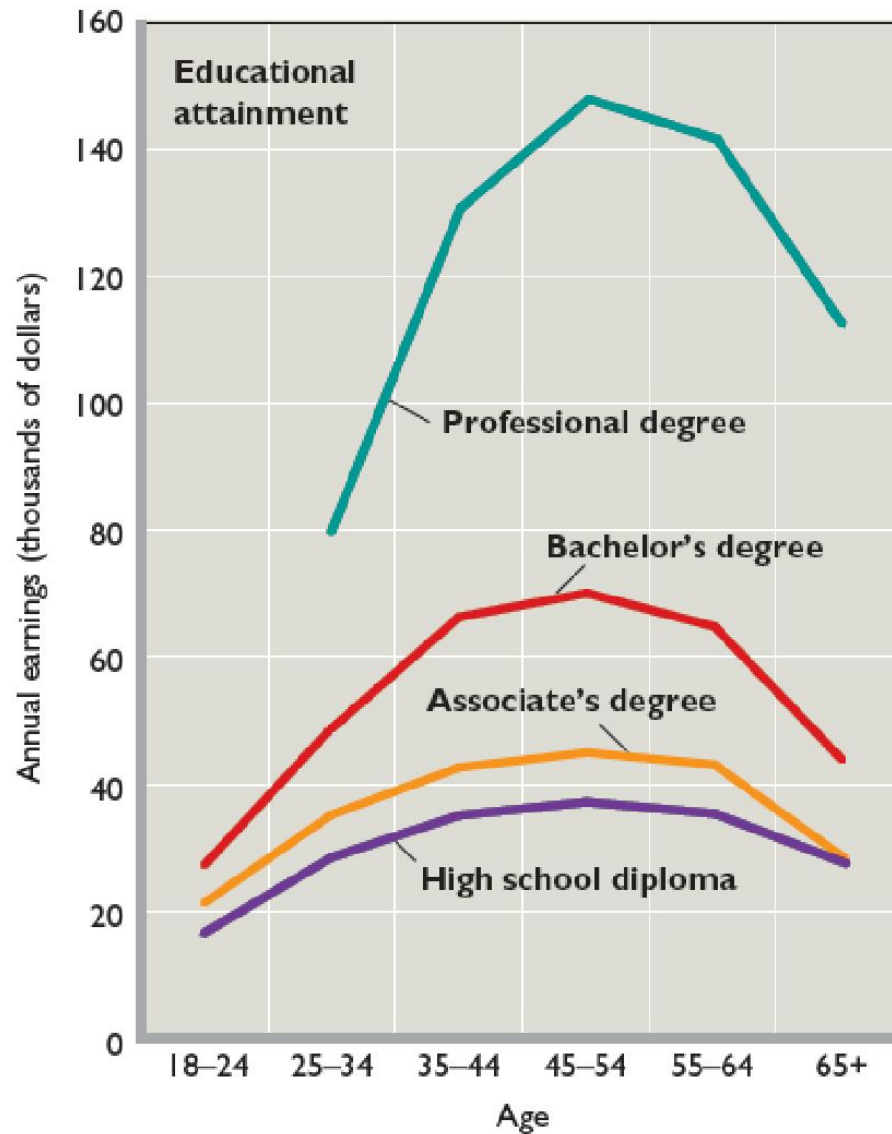
- Case against minimum wage
- Case for minimum wage
- State and locally set rates
- Evidence and conclusions



# 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