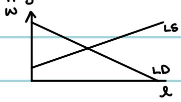
Chapter 11 : The Labor Market

- the labor market := an input market where workers supply ℓ^* to firms who demand ℓ^* for a wage of w^* determined by downward sloping demand and upward sloping supply



↓ there is an associated output market for the service produced by the labor & the input market is derived from it

- labor demand : employers exist in a competitive labor market & therefore cannot change w^* on their own ... can only see w^* & determine LD(w)
  - marginal product of labor := MP_L := extra production from hiring 1 more worker
  - marginal revenue product of labor := MRP_L := marginal revenue from hiring 1 more worker := $MP_L \cdot P$

  Rational Rule := hire as long as $MRP_L \geq w$ => hire where profits are maximized

  demand curve = MRP_L curve = downward sloping & moved along as wage changes

  ↳ shifted by shifts in output market

  shifted by changes in price of capital <
  - scale effect : price of capital ↓ => buy more capital => need more workers TO PRODUCE MORE
  - substitution effect : price of capital ↓ => buy more capital => workers replaced

  better management & productivity gains => demand shifts out

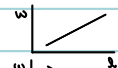
  nonwage benefits & taxes shift demand back

- individual labor supply : workers choose between labor & leisure through the income & substitution effects of wages
  - income effect := higher income makes leisure more attractive
  - substitution effect := higher wages make work more attractive

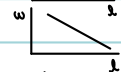
  } COMPETING EFFECTS

  Rational Rule : work as long as wage $\geq MB_{Leisure}$

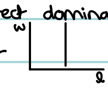
  supply curve : upward sloping if substitution effect dominates



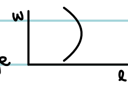
  downward sloping if income effect dominates



  vertical if effects cancel eachother



  bending if dominating effect depends on wage



  - at low wages, substitution effect dominates ; at high wages income effects dominate

  ↳ shifted by other uses of time, other sources of income, changes in need for labor / income, experience

- market labor supply : upward sloping
  ↳ 1 job type = 1 market
  - more people enter workforce, existing workers put in more hours, ppl switch jobs

  ↳ shifted by other occupation wages changing, population changes, unemployment benefits changing, taxes & employment benefits change