



DID HENRY FORD PAY EFFICIENCY WAGES?

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Week 3



How Does the Paper Relate to Lecture?

- The study of the Efficiency Wage Theory
 - Increases productivity
 - Increases satisfaction
 - Decreases turnover
- Studying the Labor market and how wages affect workers and productivity
- How Efficiency Wage theory is used

Positioning: What We Already Know

- In a perfect competition labor market wages would be flexible, there would be no involuntary unemployment, and wages would not be affected by outside factors (age, race, sex)
- Employers would hire low wage workers and high wage workers would be in excess supply.
- In the real world outside factors affect employment: wages are sticky, there is a minimum wage, unions, and other frictions in the labor market
- Ford was not unionized at this time
- Efficiency Wages: wages that are above market price used by an employer to increase workers productivity, raise moral, and reduce turnover

Question: What Does the Paper Want to Find?

- Did Henry Ford Pay Efficiency Wages?
- Did Ford's five dollar a day wage support the efficiency wage theory?
- Did the higher wages increase workers effort, efficiency, moral, or retention?

Supporting Papers and Background Research

- "Efficiency Wage Theories: A Partial Evaluation" (Katz 1986)
- Shapiro-Stiglitz theory (1984)
- Efficiency wage theory and analysis
- Profit maximizing firms don't lower wages in times of high unemployment is because of the increasing function of labor to profit: Lowering wages lowers profits
- Henry Ford himself: "There was. .. no charity in any way involved. . . . We wanted to pay these wages so that the business would be on a lasting foundation. We were building for the future. A low wage business is always insecure. ..The payment of five dollars a day for an eight hour day was one of the finest cost cutting moves we ever made"
(Ford 1922, pp. 126, 1

Process

- The paper found issues with retention by around 370% turnover rate, high levels of absent workers, and high employee dissatisfaction before the policy was implemented
- Evaluating the Employment Department keeping foreman from firing people without reason: provides context and precursor for \$5 day motivation
- Initial Test by a British company yielded promising results (Increased Worker Productivity)

The \$5 Program

- Added eligibility requirements of time requirements of 6 months, age 22+ (except young heads of households), and a “will not make poor use of the extra money” clause entailing investigations and good behavior requirements
- The tenure requirement, pamphlets outlining good habits and moral responsibilities to the company, if rules broken the worker had 30 days to clean up or be removed from the program, calling the wage a “gift” not a wage, gained an excess supply of laborers, had to apply more restrictions to the hiring process, not switching to more highly skilled workers, are all signs of efficiency wage
- Concluding with dramatic decrease in turnover and increase in productivity: reduced cost from turnover likely made up for the wages

Graphical Illustration

Table 2
Ford Motor Company Net
Income, 1910–15

| | Nominal (\$) | Real (1910 \$) |
|------|-----------------|-------------------|
| 1910 | 4,163,451 | 4,163,451 |
| 1911 | 7,338,588 | 7,413,464 |
| 1912 | 13,542,678 | 13,139,301 |
| 1913 | 27,087,204 | 26,452,347 |
| 1914 | 31,757,769 | 30,419,318 |
| 1915 | 40,307,167 | 36,901,187 |

SOURCE.—Nevins(1954, p. 647). The 1914 and 1915 figures have been (crudely) adjusted to put them, like the others, on a calendar year basis. The real values use the gross national product deflator from U.S. Department of Commerce (1975, p. 224).

- This table shows the real net income (adjusted to 1910 prices) for the Ford Motor Company before and after the Efficiency wage \$5 day policy was implemented
- After the implementation, the real net income continued to rise at the same rate or faster than before the policy

Conclusion

- The Henry Ford \$5 day is an example of efficiency wages
- Increased wages increased productivity in this case
- Higher wages increased Ford Motors income

