

Module 11 — Key Concepts (Ch. 11 & 12)

Chapter 11 — Labor Markets

1. Labor Markets

- Labor markets work **just like regular markets**, BUT roles are flipped:
 - **Firms demand labor.**
 - **Households supply labor.**

2. Labor Demand

What determines how much labor a firm hires?

Firms hire labor up to the point where:

$$\text{Marginal Revenue Product (MRP)} = \text{Wage}$$

- **MRP = Marginal Product of Labor × Price of Output**, we want to convert to money units.

What shifts labor demand (firm side)?

- **Demand for the product increases** → labor demand ↑
- **Productivity improvements** (technology, better capital) → labor demand ↑
- **Price of the output rises** → labor demand ↑
- **Price of substitute inputs changes** (e.g., robots become cheaper) → labor demand ↓

3. Labor Supply

Decision: Work vs. Leisure

Individuals decide based on:

- **Benefit:** wage
- **Cost:** value of leisure/other activities
- Everyone has 24 hours → time allocation matters.

What shifts labor supply?

- **Changes in population**
- **Changes in preferences for work vs. leisure**
- **Changes in alternative opportunities**
- **Changes in household structure** (e.g., more dual-income families)

4. Equilibrium

Equilibrium wage & employment determined by:

- Intersection of **labor supply** and **labor demand**.

Shifts in either curve change:

- **Wages**
 - **Employment levels**
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Chapter 12 — Wage Differences

1. Human Capital

Workers earn different wages partly because of differences in education, training, experience, skills, etc.

More human capital → higher productivity → higher wages.

2. Signaling

Education may not directly increase productivity but may signal intelligence, work ethic, reliability, endurance, etc.

Employers pay more because these signals predict job performance.

- **A** in a hard college course might not directly help you be a better worker but it signals that you are smart and work hard.

3. Compensating Differentials

Some jobs pay more because they are, for instance, dangerous, unpleasant, stressful or require odd hours.

Higher pay compensates workers for undesirable job attributes.

4. Institutions

Wages can also be affected by:

- **Minimum wage laws**
 - **Unions**
 - **Government regulations**
 - Large employers with bargaining power
- These can raise wages above competitive-market levels.

5. Discrimination

Even after controlling for skills and experience:

- Women and minorities often receive **lower wages**