Labor Market

Just like there are product markets where goods and services are produced and demanded, there are factors of production markets where different FOPs are supplied and demanded.

Wage Determination

Is the process how wages are determined in a free market. Just like the product prices which are based on demand and supply of that particular product, the labor wages are also based on the demand and supply of labor.

<u>Labor Demand Curve</u>

Labor demand is derived demand, which means that more than quantity demanded of the final product that labor produces higher would be the demand for labor.

Labor demand curve is a graph that shows the quantity of labor / people which a company would be willing to hire at different wage rates.

Derived Demand basically means that the demand for labor is based on the demand for the final product produced by those people.

The labor demand curve is basically its Marginal Revenue Product of Labor as it shows the additional revenue that each unit of labor is generating for the company, and therefore it also represents the maximum amount that a company would be willing to pay to each unit of labor.

Hence the labor demand curve for a firm shows the wages that a company would be willing to pay to each unit of labor.

Market Demand for Labor

Market demand curve for labor is the sum of individual firms' demand for labor that are willing to hire a certain type of labor.

To find the market demand for labor curve we add the individual firms' demand for labor at different wages rates.

Individual Labor Supply

Is a graph that shows the quantities of hours a person would be willing to work at different wage rates.

Most people respond to incentives and therefore a higher wage rate would incentivize workers to work for longer hours, but beyond a certain wage rate a person might wish to work lesser hours given his / her total compensation has been higher than before.

For the upward sloping part of the individual labor supply curve, the substitution effect is dominant because workers are willing to give up their leisure for more work but when the curve starts to bend backwards then the income effect becomes more dominant as people start working fewer hours as they are making more income overall.

Market Supply of Labor

A market is made of all the individuals who are able and willing to work in a certain occupation. For instance, for teachers the market supply would be made up of individual teachers' supply of labor curves.

Market labor supply curve shows the total number of people or labor hours that are available at different wage rates.

Wage Determination

Is the process by which wages of different occupations are determined in the market based on market forces of labor demand and labor supply.

When there is any change in labor demand or labor supply the initial labor market equilibrium will change to another equilibrium.

a) Higher prices of the product that labor produces
b) Greater use of capital which enhances labor productivity
c) Increased training/education needed to join an occupation
d) Greater population in the country
e) More fringe benefits

Factors (apart from Wages) that affect Labor Demand

1. The price of the final good - with higher product price the revenue that labor generates for the company will increase and therefore the labor demand curve will shift upwards
2. The labor productivity - if labor is becoming more productive because of greater use of technology or education or training then the labor demand curve will shift upwards and vice versa.

Factors (apart from Wages) that affect Labor Supply

1. The need for training and education to join any occupation - higher the training and education requirement to join an occupation lesser will be the supply of workers in that profession.
2. The population of a country - higher the population more the supply of labor in every occupation.
3. Fringe benefits - more the fringe benefits in any occupation more people will be willing to join that occupation

Wage Differential

Wage differential looks at the reasons why people in some occupations earn more and people in other occupations.

Lets assume we want to compare receptionist workers' wages with company managers wages.

Lower the supply for any occupation and higher the demand would mean higher wages for that occupation.

Types of Labor Markets

1. Perfect Labor Market
2. Imperfect Labor Market

Perfect Labor Market

1. Many companies / firms available in the market to hire people and huge supply of workers who are willing to work
2. Workers have ***homogenous skills set***
3. Firms are ***wage takers***
4. ***Workers have complete information*** about nature of jobs and working conditions / salaries etc (there is no information asymmetry)
5. Workers ***have geographical and occupational mobility***
6. There are ***no external influences*** on wages like trade unions, government intervention like minimum wages etc.

Imperfect Labor Market

1. Where there are limited employers and / or limited workers to work
2. Workers ***do not have homogenous skill set***
3. Firms or workers can have ***disproportionate bargaining power*** against the other groups
4. There would be information asymmetry (one of the 2 groups can have more information that the other group)
5. Workers are ***not very geographically and occupationally mobile***
6. There are external factors influencing wages like government intervention, presence of trade unions and monopsony

    a. How Trade Unions Operate
    b. Monopsony: is when in a labor market there is a single firm / company that wants to hire a certain type of labor
    c. Government Intervention

a). Trade Unions
Is an organization / platform that represents workers in a certain firm or industry, the purpose of which is to advocate for workers' rights in terms of higher salaries and better working conditions.

Industrial Action refers to the techniques used by trade unions to pressurize employers/ firms to accept their demand like ***protests, going on a strike, go-slow, over-time ban.***

In case the agreement is not being met then the parties have 2 options, either take the issue to the court or to Industrial tribunal.

Industrial Tribunal is any independent entity / could be a lawyer, judge or business personnel to whom both parties have trusted to make a decision on their behalf which is then binding on both the parties.

If a bigger proportion of companies' employees are part of the labor union then it would give the trade union more bargaining power and vice versa.

Nature of Labor Unions

1. ***Closed Shop:*** when it is mandatory for every employee of a firm to be part of the trade union.
2. Open Shop: is when ***union membership is voluntary***

b). Monopsony

Refers to single employer for a certain type of labor for example ***nuclear scientists*** will only be hired by research centers conducting research on nuclear energy or nuclear weapons and so on.

If a monopsony is government owned then the chances of labor being exploited are less because government is careful with its reputation but this is less likely to be the case for a private sector firm.

c). Government Intervention

Government's objective in a mixed economy is to regulate the markets to ensure their smooth functioning and to prevent any exploitation that might be taking place.

Some possible ways through which Government intervenes in the Labor Market

1. Minimum Wage -
2. Making rules and policies like child labor, working conditions guidelines etc - increases cost of hiring labor and therefore it is likely that firms will start looking for alternates to replace labor with machines and so on.

Other Factors that affect Wages

1. Wage Elasticity of Labor Demand
2. Wage Elasticity of Labor Supply
3. Wage Discrimination

Wage Elasticity of Labor Demand is a formula that calculates the responsiveness of labor demanded due to change in wages.

For occupations which are easier to be replaced with machines / technology, will have more elastic demand and vice versa. For instance, between receptionists and scientists the demand for receptionists will be more elastic as it is easier to replace them with any software or digital screen.

Wage Elasticity of Labor Supply

A formula that calculates the responsiveness of quantity supplied of labor due to change in wages.

Wage Discrimination

When 2 employees have the same skill set (experience, qualification, education) and are working at the same designation but earn different amounts due to their gender, race, ethnicity, religion etc.