

## Earnings, Productivity, and the Job Market

*Full Length Text* — Part: 5 Chapter: 25  
*Micro Only Text* — Part: 3 Chapter: 13

To Accompany "Economics: Private and Public Choice 11th ed."  
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Slides authored and animated by:  
James Gwartney, David Macpherson, & Charles Skipton

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## Why Do Earnings Differ?

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## Why Do Earnings Differ?

- Earnings would be equal if:
  - all individuals were identical
  - all jobs were equally attractive
  - workers were perfectly mobile among jobs

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### Earnings Differentials Due to Non-identical Workers

- **Worker productivity:**
  - More productive workers have greater earnings.
- **Worker preferences:**
  - Workers motivated by monetary objectives are likely to pursue jobs with higher wages.
- **Race and gender:**
  - Discrimination may lower earnings opportunities of minorities and women.

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### Earnings Differences of Skilled and Unskilled Workers

- The productivity and thus marginal product of skilled workers is greater than that of unskilled workers.
- Hence, the **demand** for skilled workers  $D_s$  exceeds the **demand** for unskilled workers  $D_u$ .
- Education and training generally enhance skill.
- Because it is costly to upgrade skills through investments in human capital, the **supply** of skilled workers  $S_s$  is smaller than the **supply** of unskilled workers  $S_u$ .

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### Earnings Differences of Skilled and Unskilled Workers

- The wages of skilled workers are high relative to unskilled workers due to the strong **demand** and small **supply** of skilled workers relative to unskilled workers.

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## The Economics of Employment Discrimination

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## Wage Discrimination

- When white workers are preferred to minority workers (*or men to women*), the **demand** for minority workers is reduced.
- Minority workers receive lower wages.

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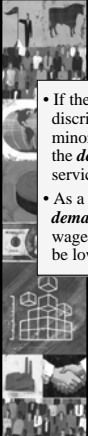
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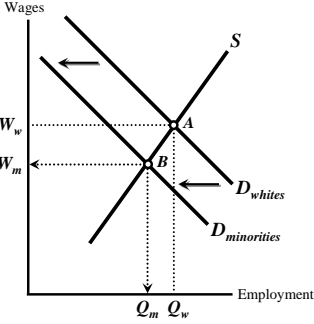
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## Impact of Wage Discrimination

- If there is employment discrimination against minorities (*or women*), the **demand** for their services will decline.
- As a result of this lower **demand**, the equilibrium wage for minorities will be lower,  $W_w > W_m$ .



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### Employment Discrimination

- When discrimination is present, the entry of minority workers into some type of jobs and occupations may be restricted.
  - If so, the **supply** in unrestricted jobs will increase, causing wages to fall in these jobs.
  - When the **supply** of minorities (*or women*) to an occupation is restricted, the wages of white males will rise.
- **Discrimination is costly** to employers.
  - When employers can hire equally productive minorities (*or women*) at a lower wage than whites (*men*), the profit motive gives them a strong incentive to do so.
    - Employers who ignore minority and gender status when employing workers will have lower wage costs than employers who discriminate.

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### Employment Discrimination and Earnings of Minorities

- Earnings may differ among groups for reasons besides employment discrimination.
- To measure the extent of employment discrimination, we must
  - adjust earnings for differences between groups in productivity-related factors such as education, and,
  - then make comparisons between similarly qualified groups of workers who differ only in race or gender.

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### The Actual and Productivity Adjusted Wages of Minorities Compared to Whites 2000-2003\*

	Men		Women	
	Actual	Adjusted	Actual	Adjusted
White	100	100	100	100
African-American	79	86	90	94
American Indian	82	92	87	95
Asian-American <sup>a</sup>	100	94	103	97
Mexican-American	67	93	75	98
Other Hispanic	79	92	85	95

<sup>a</sup> Primarily Chinese-Americans and Japanese-Americans.  
 \* Data were supplied by David MacPherson, as derived from the 2000-2003 Current Population Surveys (CPS). Data were adjusted for years of schooling, work experience, region, industry, sector of employment, union status, and marital status.

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**Questions for Thought:**

1. Which major factors that would normally explain earnings differences between
  - a. a lawyer and a minister,
  - b. an accountant and a school teacher,
  - c. a business executive and a social worker,
  - d. a country lawyer and a Wall Street lawyer,
  - e. an experienced, skilled craftsperson and a 20-year-old high school dropout, and,
  - f. an upper-story & ground-floor window washer?
2. "If it were not for employment discrimination against minorities, the average earnings of minorities and whites would be equal."  
-- Is this *true*?

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**Questions for Thought:**

3. "When employment discrimination results from the personal prejudices of employers, economic theory suggests that discrimination by an employer will reduce production costs since the employer can pay lower wages."  
-- Is this statement *true, false, or uncertain*?
4. If Congress suddenly passes legislation that required all U.S. workers to receive the same annual pay, then we would expect
  - a. less human capital investment
  - b. a shortage of workers to fill undesirable jobs
  - c. a surplus of workers to fill easy, desirable jobs

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**The Link Between Productivity and Earnings**

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### Productivity and Earnings

- Productivity is the source of high wages.
- Workers in the U.S. earn high wages because their output per hour is high as a result of:
  - Greater worker knowledge and skills (*human capital*)
  - The use of modern machinery (*physical capital*)

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### Productivity and Earnings

*Annual rate of increase of productivity and real wages*

Period	Rise in output per hour (private business sector)	Rise in real compensation (private business sector)
1948-1973	3.2 %	2.8 %
1974-1995	1.5 %	0.7 %
1996-2003	3.1 %	1.9 %

- Productivity & compensation per hour are closely related.
- Relative to the 1948-1973 period, growth in productivity and real wages slowed between 1973 and 1995. Both rebounded substantially during the 1996-2003 time frame.

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### Productivity Rebound

- Productivity rebounded significantly between 1996 and 2003 after being relatively low for the previous 20 years.
- Most economists believe that the increase in productivity growth is the result of the recent computer revolution and related technological innovations.
- If the acceleration in productivity continues, increases in wages in the years ahead will be more rapid than during the 1974-1995 period.

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### Automation

- Automated methods of production will only be adopted if they reduce costs.
- Automation may reduce employment in a specific industry.
  - But, it also releases resources that can be employed in other areas.
- Improved technology permits us to achieve larger output and income levels.

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### Questions for Thought:

1. Why are wages higher in the United States than in India or China?
2. "*Jobs are the key to economic progress. Unless we create more jobs, our standard of living will fall.*"  
-- Is this statement *true or false*?
3. Do you think the market system of wage determination is fair? Why or why not? Can you think of a more equitable system? If so, explain why it is more equitable.

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# End Chapter 25

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