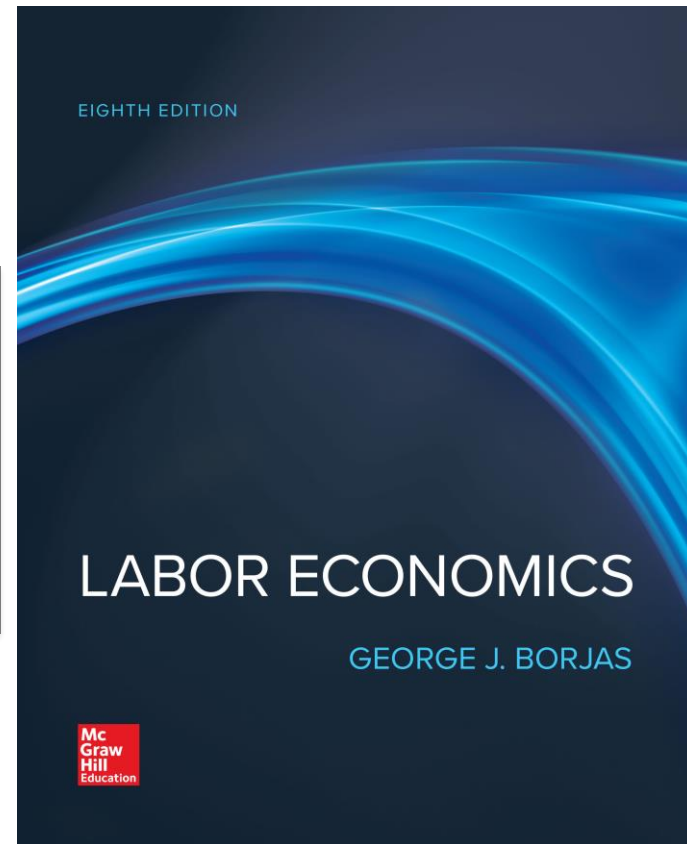


Chapter 1

Introduction to Labor Economics



“Observations always involve
theory.”
-Edwin
Hubble

Why Study Labor Economics

Human resources allocate substantial time and energy to labor markets.

Labor economics studies how labor markets work.

Labor economics helps us understand and address many social and economic problems facing modern societies.

Basics of the Labor Market

Participants are assigned motives:

- Workers look for the “best” job.
- Firms look for profits.
- Government uses regulation to achieve goals of public policy.
 - Minimum wages
 - Occupational safety

Three “Actors”

Workers

- The most important actor; without workers, there is no “labor”.
- Desire to maximize utility (i.e., to optimize by selecting the best option from available choices).
- Supplies more time and effort for higher payoffs, causing an upward sloping labor supply curve.

Three “Actors”

Firms

- Decide who to hire and fire.
- Motivated to maximize profits.
- Relationship between price of labor and the number of workers a firm is willing to hire generates the labor demand curve.

Three “Actors”

Government

- Imposes taxes, regulations.
- Provides ground rules that guide exchanges made in labor markets.

Why Do We Need a Theory

Explain and understand how labor markets work.

Focus on the essential variables while leaving out other, less crucial, factors.

Create a model that helps explain the theory.

Positive vs. Normative Economics

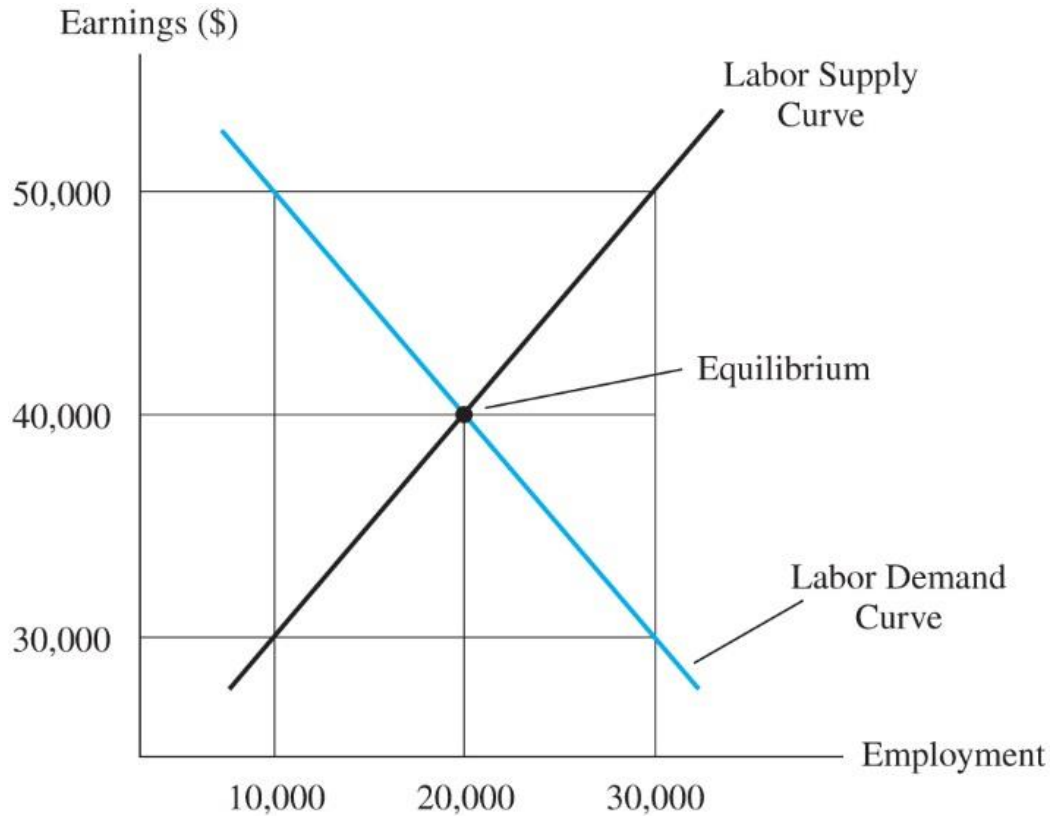
Positive economics

- Addresses the facts
- Focus on “what is”
- Questions answered with the tools of economists

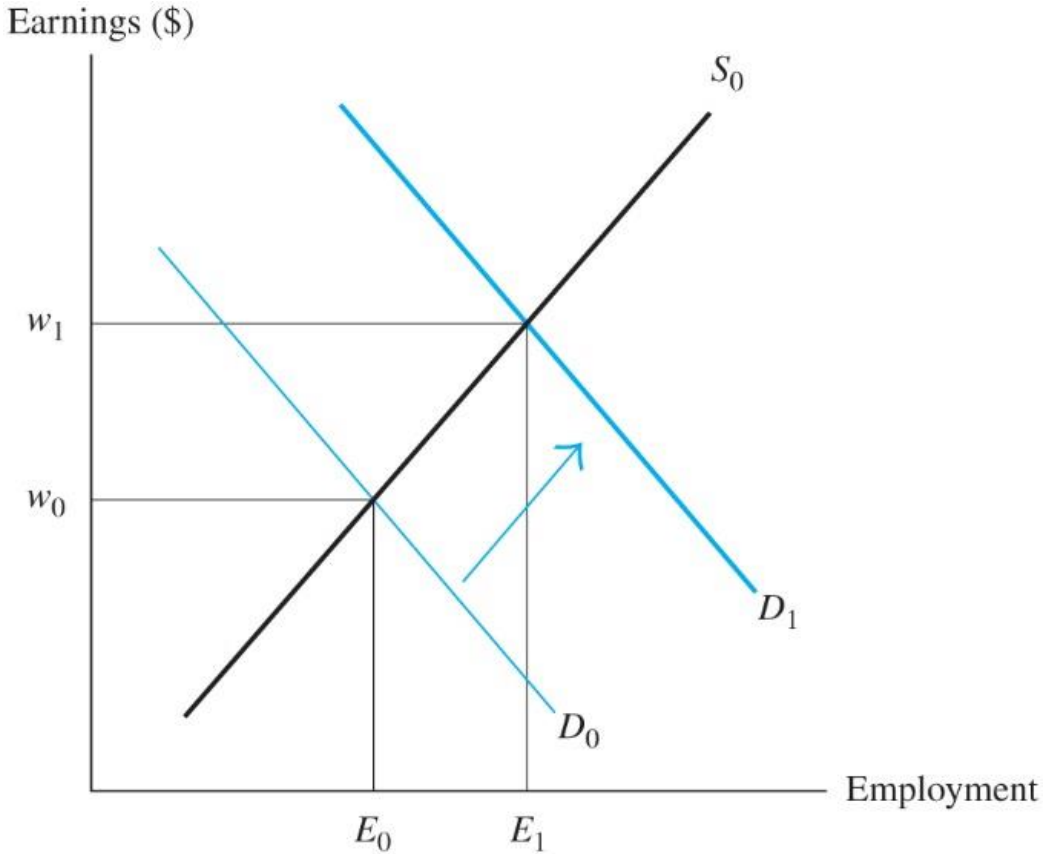
Normative economics

- Addresses values
- Focus on “what should be”
- Requires judgments

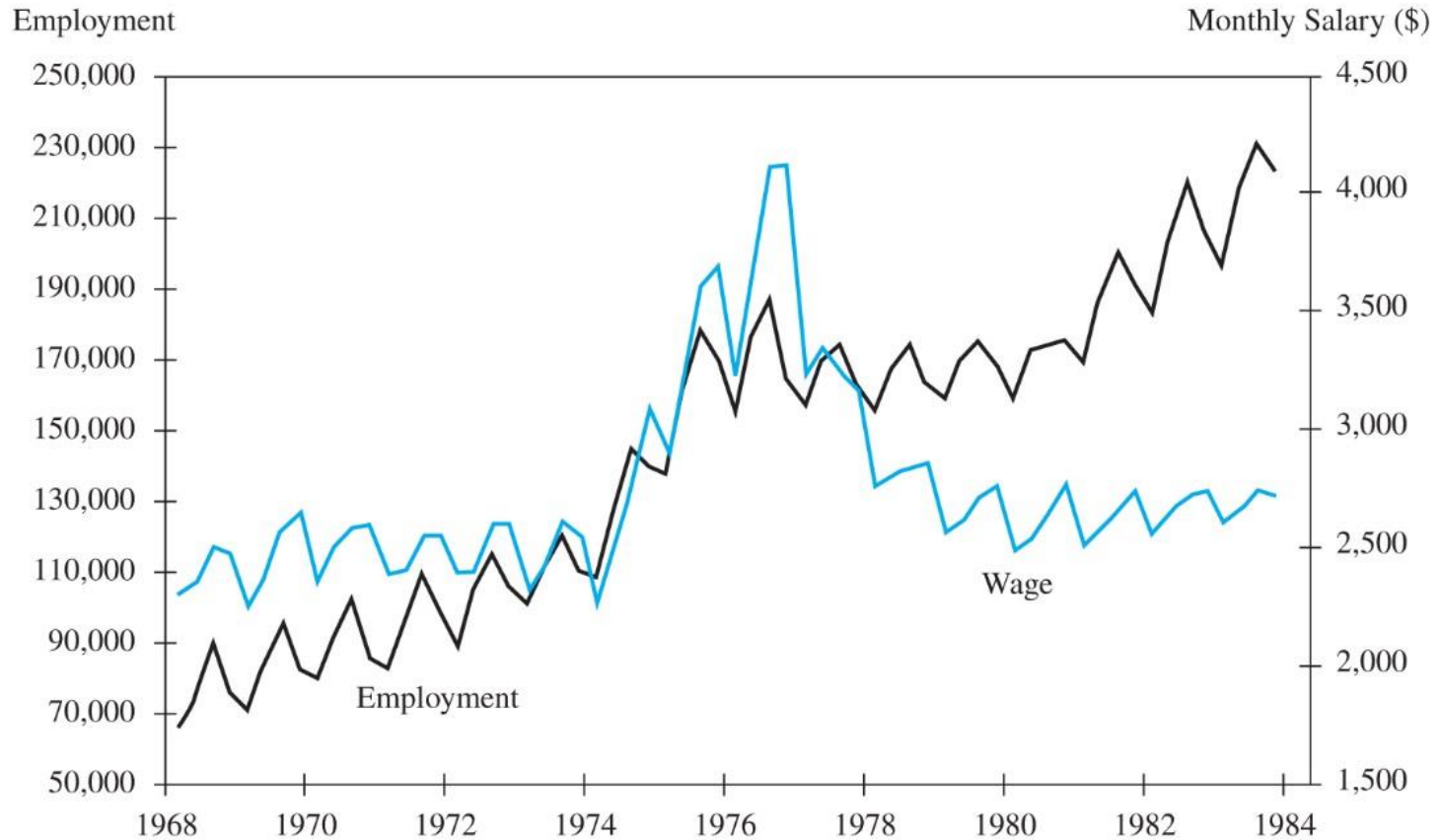
Supply and Demand in the Engineering Labor Market



The Alaskan Labor Market and Construction of the Oil Pipeline



Wages and Employment in the Alaskan Labor Market, 1968-1984



Summary

Labor economics studies how labor markets work.

Models in labor economics typically contain three actors: workers, firms, and governments.

A good theory should have realistic assumptions and can be tested with real-world data.

The tools of economics are helpful in answering positive questions.

Where Are We Going?

Worker supply decisions

Firm demand decisions

Labor market equilibrium

Differences in job characteristics

Differences in worker characteristics

Labor mobility

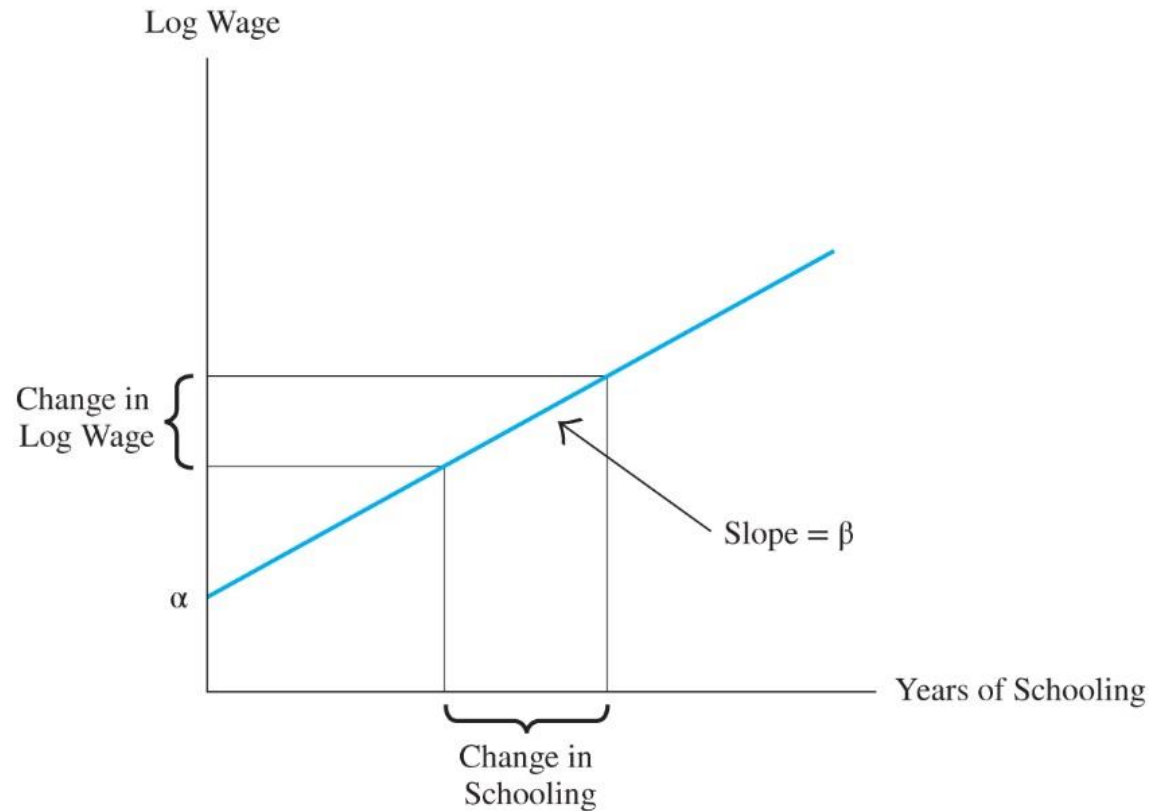
Labor market discrimination

Unionization

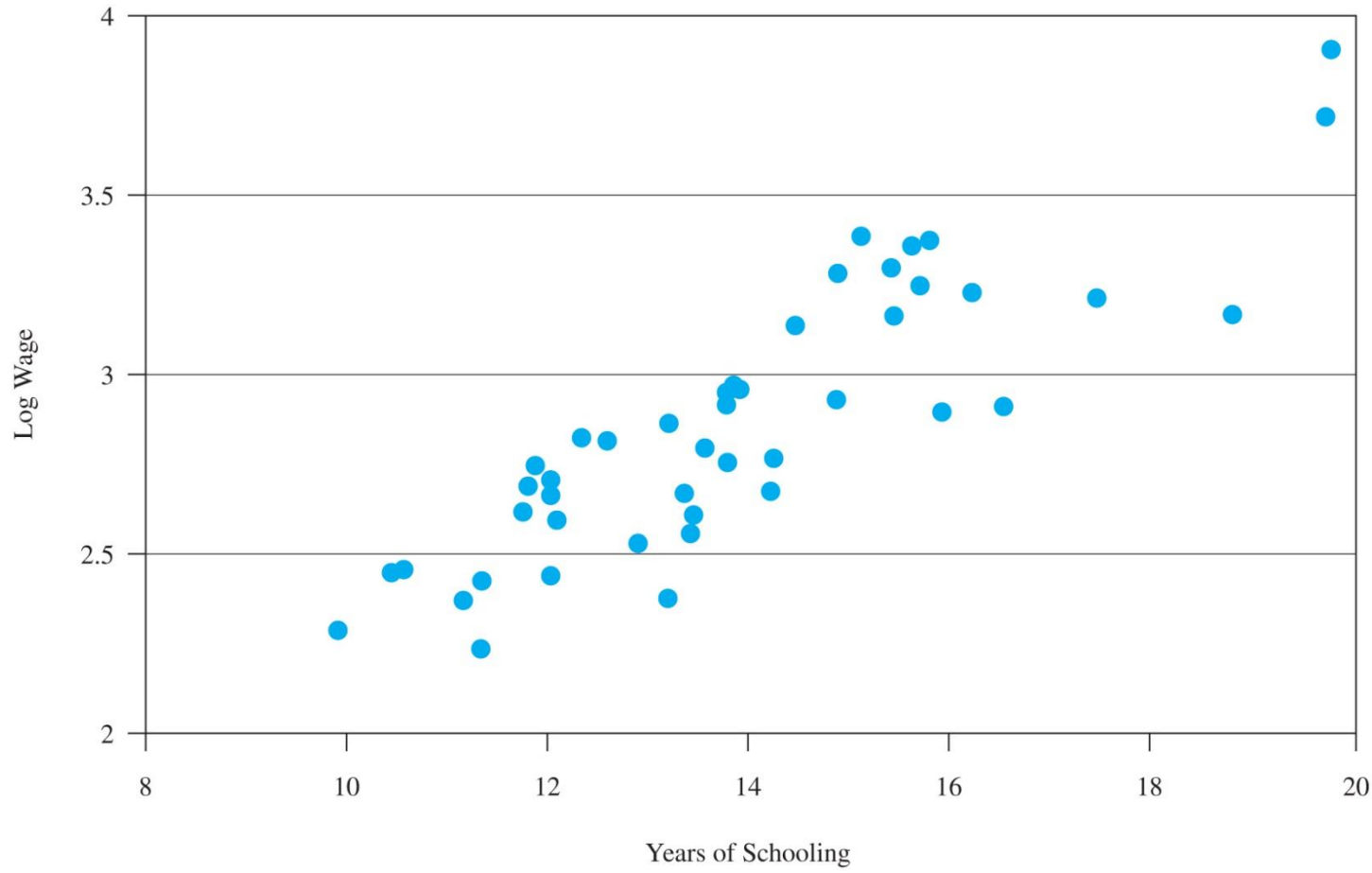
Incentive pay schemes

Unemployment

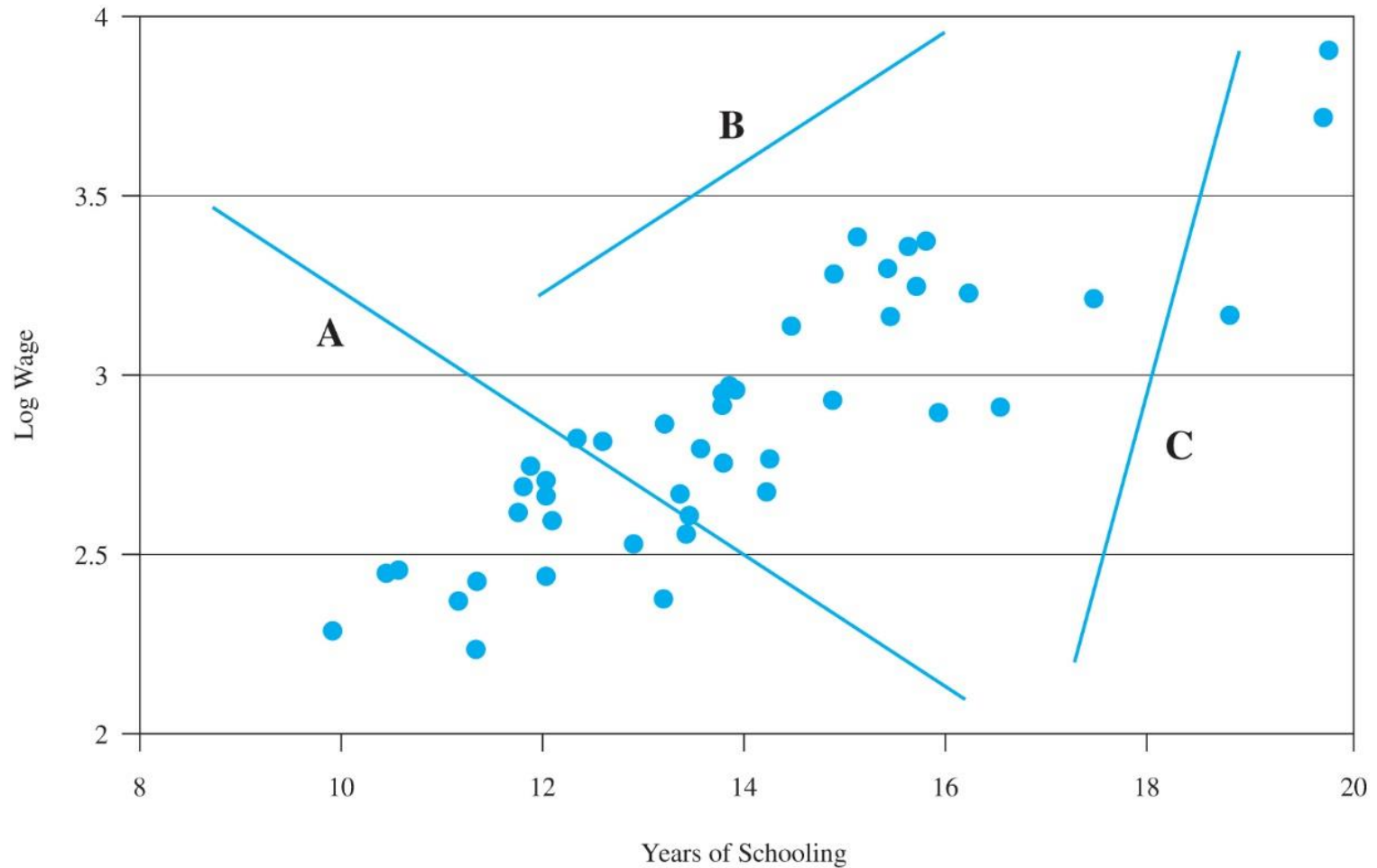
Appendix: Regression Analysis



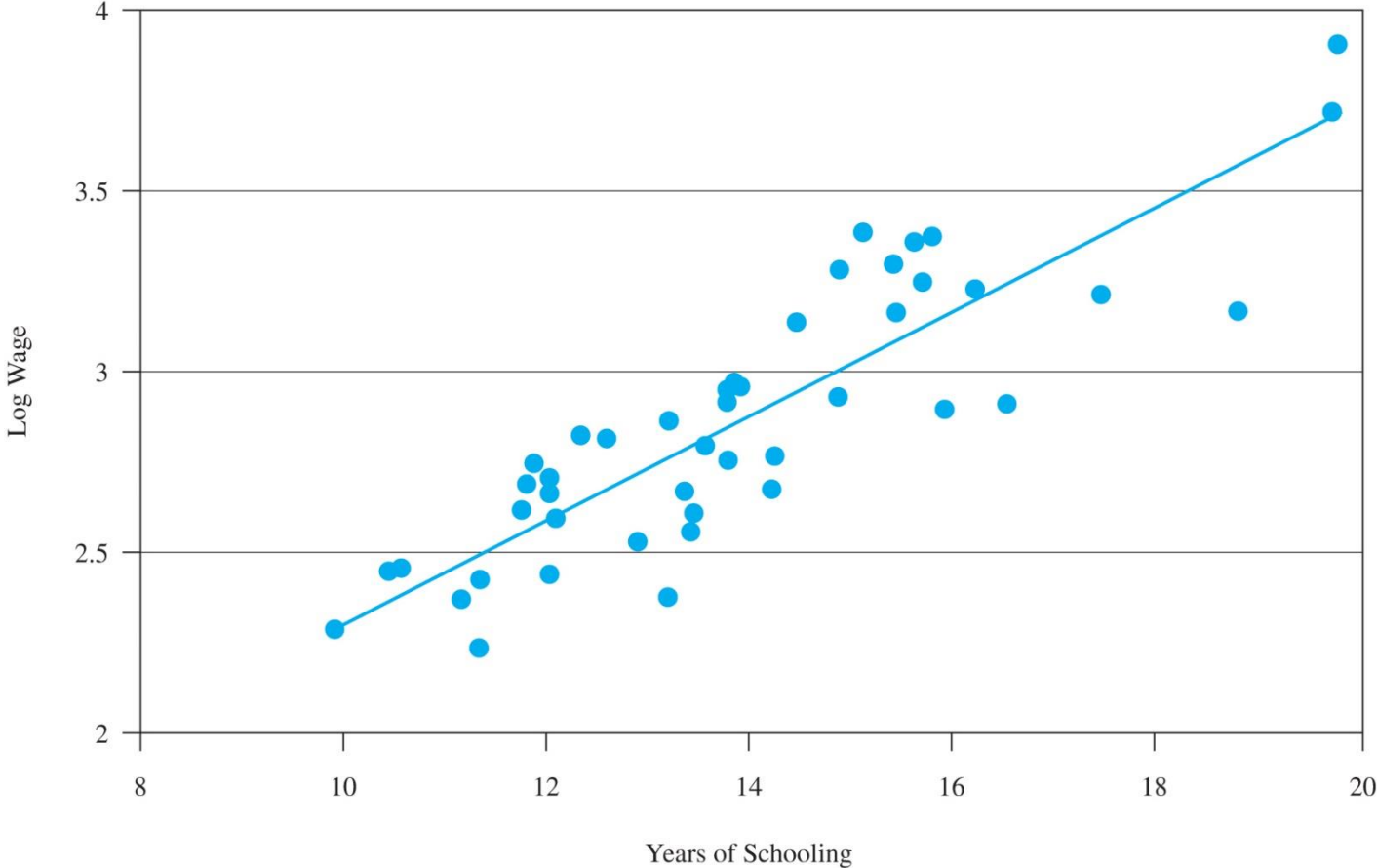
Scatter Diagram: Wages and Schooling by Occupation, 2001



Choosing Among Lines Summarizing Trends in Data



The Best-Fit Regression Line



Multiple Regression

Extending regression analysis to include multiple independent variables

Each estimated coefficient shows the impact of a particular variable on the dependent variable, other things constant

Standard errors of the regression coefficients are used to evaluate significance of the relations between each particular variable and the dependent variable