In this lesson we will:
- Explain how earnings are determined and why earnings vary across different groups
- Discuss why employment and wages increase and how jobs will be created in the future

Earnings in the US greatly vary, a low skill workers working in McDonald may earn the minimum wage, currently $5.15, (there are 2.2m people with wage or below minimum) while a lawyer or a physician may earn several hundred dollars per hour.

- If all individuals were identical in preference, skills and background, all jobs were equally attractive and all workers were perfectly mobile real wages (wage plus fringe benefits adjusted for prices) would be the same. Why? Do these assumptions hold?
- Differences in earnings results from both fortune and decisions. Why don’t all college students select the major with the highest income?

How Do Workers Differ?

- Workers differ in their productivity: Individuals with better innate ability, parental training, work ethics, and human capital (how are these related?) will be more productive and will have a higher Marginal Revenue Product. There is a strong, positive correlation between education and earning (with college grad having a 27k premium)
- Innate ability, preferences and the cost of education limits the supply of skilled workers while their high productivity increases their demand (see figure 10-1)
- Some jobs like the entertainment industry and others resemble a tournament play, where slight difference in performances can lead to huge differences in compensation.

- Work Preference: Some individuals are more concerned about making money and are willing to work hard for it. Some individual are more risk loving and are willing to risk more for a higher potential compensation (what type of occupation are risky and why?)

- Gender and Race: Employment discrimination and discrimination in acquiring education or training may hinder the earning potential of minorities.

Figure 11-1: Skilled & Unskilled Labor

Figure 10-1 shows the demands and supplies for skilled and unskilled labor. Skilled labor has a higher demand (why?) and a lower supply (why?), resulting in a higher wage rate of $w^S$ is opposed to $w^U$ for unskilled labor.
Other reasons for differences in wages:

- Jobs are different in the nonpecuniary job characteristics such as location (how will location affect wages?), safety (name some hazardous jobs), stress-level (what types of jobs can be very stressful?) and other amenities (what amenities do professors have).
- Jobs that are less desirable must pay a compensating wage differentials
- Lack of labor mobility (what will cause labor immobility) can cause wage differences to remain for a long time (how will wages adjust over time?)

Employment Discrimination:

- If certain minorities are discriminated against, they would be pushed to less desirable jobs where their high supply will cause their wage to be lower.
- African-Americans earned 79c for every dollar that a Caucasian earns, but 85c when adjusted to productivity. Mexican (the second largest minority) earned 66c per dollar, but 92c when adjusted for productivity. Other evidences show reverse discrimination.
- American workers are about 15 times more productive than Chinese or Indian workers and, therefore, receive far higher wages. What makes them more productive?
- Increases in education, organization and capital have increased wages over time. Automation, for the most part, has made labor more productive and increased demand for labor. (Automation of cars tripled demand for cars & raised demand for workers by 50%)

Productivity increased rapidly before 1973 but slowed down between 1974 and 1995. What are some of the events that led to this slowdown?

- In the late 1990s, productivity increased by 2.6% annually causing an annual rise in wages of 2.2%. What caused this boost in productivity?
- Recessions tend to decrease productivity because firms underutilize their workers since they are reluctant to lay them off (why?) and demand for manufactured goods and high-end services (where productivity is high) tend to drastically fall.