Chapter 16

Put into practice questions

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Calculate the elasticity of supply of labour for the wage changes shown in Figure 16.3.

(a) +25%/+300% =
(b) +200/+20= +10

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The wage rate increases by 10 per cent. The quantity of labour demanded falls by 20 per cent.

- **What is the elasticity of demand for labour? -20/+10= -2**

What would happen to the quantity of labour demanded if the elasticity of demand were to stay the same and the wage rate to increase by 2 per cent?

Quantity demand of labour would fall by 20%

The price elasticity of demand for a product is −0.1.

- **Is this price inelastic or elastic? Inelastic as the value is less than one.**
- **Does this mean that demand for labour in this industry is likely to be elastic or inelastic?**

Likely to be inelastic as an increase in wage leading to an increase in costs and an increase in price will lead to a smaller proportionate change in quantity demanded.

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An inward shift in supply could be caused by:

An increase in emigration

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What is the equilibrium wage in the labour market? The wage at which the quantity demanded in labour equals the quantity supplied and there is no incentive to change, If the government introduced a minimum wage of £10 what would the effect be on:

- The quantity demanded of labour? Reduce if labour became more expensive
- The quantity supplied of labour? Increase as more incentive to work

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• The total earnings of those employed? This depends in how much there is a fall in the quantity demanded of labour. Those in work earn more but there are less employed.

End of chapter put into practice questions

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The average wage in an industry increases from £12 an hour to £13. The quantity of labour demanded falls by 5 per cent. What is the wage elasticity of demand for labour?

Change in wages = (+ 1/12)*100 = +8.33%

Wage elasticity = -5/+8.3= -0.6

Show the effect on transfer earnings and economic rent of an increase in the demand for labour.

Demand will shift outwards increasing the equilibrium wage and quantity of labour. This will increase the transfer earnings and economic rent areas

Show the effect on transfer earnings and economic rent if the supply of labour becomes more wage elastic over time.

Supply becomes flatter; this will increase transfer earnings and reduce economic rent.

Using a diagram show the effects on the equilibrium wage and number of people employed if the demand for labour falls. Assume the supply of labour is wage inelastic.

Demand shift inwards. This reduces equilibrium wage and quantity of labour. If supply is wage inelastic the effect is on wages more than quantity.

Using a diagram show the effects on the equilibrium wage and number of people employed if the demand for labour falls. Assume the supply of labour is wage elastic.

Demand shift inwards. This reduces equilibrium wage and quantity of labour. If supply is wage elastic the effect is on quantity more than wages.

'Higher wages reduce the quantity of labour demanded.' 'Higher wages are caused by higher demand for labour'. Show how both these statements can be true.

Higher wages caused by an inward shift in supply of labour lead to a movement along the demand curve.

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An increase in demand for labour leads to an outward shift; this pulls up wages and increases the quantity employed.

Using a diagram show the effect on the equilibrium wages and quantity of people employed of an increase in supply of labour

An increase in the supply of labour leads to an outward shift. This will reduce the equilibrium wage and increase the quantity employed,

Assume demand and supply of labour are wage inelastic. Assume a minimum wage above the equilibrium wage is introduced. Show using a diagram the impact on the quantity of people employed and the total earnings of those employed.

A minimum wage above equilibrium leads to a fall in quantity demanded and an increase in quantity supplied. This leads to excess supply of labour. Given that demand and supply are wage inelastic the effect of the quantity demanded and supplied will be relatively small. Earning will increase as the fall in quantity demanded is relatively low and those still employed earn a higher wage.

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