Labour Markets: Wage Differentials

A2 Economics Presentation
2005
Key Areas to Cover

- Differentials in different occupations;
  - Between men and women
  - Between skilled/unskilled workers
  - Across ethnic groups – labour market discrimination

- Explain wage differentials in terms of a variety of contexts
  - Productivity
  - Educational qualifications and environment
The Distribution of Wages in the UK (April 2003)
Data from the New Earnings Survey

<table>
<thead>
<tr>
<th>Highest paid</th>
<th>Average gross weekly pay (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Directors and chief executives of major organisations</td>
<td>2,301</td>
</tr>
<tr>
<td>Medical practitioners</td>
<td>1,186</td>
</tr>
<tr>
<td>Financial managers and chartered secretaries</td>
<td>1,124</td>
</tr>
<tr>
<td>Solicitors and lawyers, judges and coroners</td>
<td>926</td>
</tr>
<tr>
<td>Marketing and sales managers</td>
<td>889</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lowest paid</th>
<th>Average gross weekly pay (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kitchen and catering assistants</td>
<td>228</td>
</tr>
<tr>
<td>Waiters and waitresses</td>
<td>218</td>
</tr>
<tr>
<td>Bar staff</td>
<td>218</td>
</tr>
<tr>
<td>Launderers, dry cleaners and pressers</td>
<td>218</td>
</tr>
<tr>
<td>Retail cashiers and check-out operators</td>
<td>208</td>
</tr>
</tbody>
</table>

1 Full-time employees on adult rates, whose pay was unaffected by absence. Certain occupations have been excluded due to the small size of the sample.

Source: New Earnings Survey 2003, Office for National Statistics
Explanations for Wage and Earnings Differentials

• Compensating differentials
  – Higher pay as a reward for risk-taking, working in poor conditions and having to work unsocial hours

• Differences in accumulated human capital
  – Wages and salaries should help to compensate people for making an investment in education
  – There is an opportunity cost in acquiring qualifications - measured by the current earnings foregone by staying in full or part-time education. The private rate of return on achieving A-levels or a university degree should be sufficient to justify the investment made
Wage Differentials (continued)

- Differences in productivity and revenue creation
  - MRPL theory suggests that workers whose efficiency is highest and ability to generate revenue for a firm should be rewarded with higher pay
    - City economists and analysts are often highly paid not least because they can claim annual bonuses based on performance
    - Top sports stars can command top wages because of their potential to generate extra revenue from ticket sales and merchandising
- Employer discrimination
- Trade Union protection and collective bargaining
  - Many workers in low paid jobs do not have trade unions acting on their behalf to protect them from the power of employers
Labour shortages and pay

- In industries where there are shortages of skilled labour, excess demand drives average wages and earnings higher.
- Specific and scarce skills makes the available labour supply less elastic.
- Good examples include booming pay levels in ICT and the construction industry.
The Return to Acquiring Human Capital

- No formal qualifications
- A-level or equivalent
- University degree or equivalent

Income vs. Age
Wage Premiums

- Literacy - achievement at NVQ level 1 - 16%
- Numeracy - achievement at NVQ level 1 - 26%
- GCSEs - 21% over non-qualified
- A levels - 17% over GCSEs
- With a degree - 28% over A levels
- Graduates - 66% over non-qualified
- Level 3 is threshold above which earnings exceed national average
- Unskilled earn 30% less than national average
- Women aged 30-44 - premium of degree holders over level 3 is 110% - highest in the OECD
Monopsony and Wage Determination

- A monopsony producer has significant buying power in the market for their inputs, be they raw materials and components or labour inputs.
- A monopsony employer is that they might use their buying-power to drive down wage rates.
- The monopsonist faces an upward sloping labour supply curve - to attract more workers in their industry, they must pay a higher wage rate – so the average cost of employing labour rises with the number of people taken on.
Monopsony and Wage Determination

• Because the average cost of labour is increasing, the marginal cost of extra workers will be even high.

• The profit maximising level of employment is where the marginal cost of labour equates with the marginal revenue product of employing extra workers.
  – Eq workers are taken on.
  – The monopsonist can employ these workers at an average wage rate of Wq – a pay level below the marginal revenue product of the last worker.
Wages and Employment Under a Monopsony

- A monopsony producer has significant buying power in the labour market when seeking to employ extra workers.
- A monopsony employer may use their buying-power to drive down wage rates.
Monopsony in labour markets

Wage Rate \( (W) \)

Demand = MRPL

Marginal Cost of Labour \( (MCL) \)

Labour Supply \( (ACL) \)

Employment of Labour \( (E) \)

\( Wq \)

\( Eq \)
Wages and Employment Under a Monopsony

- Wage Rate (W)
- Labour Supply (ACL)
- Demand = MRPL
- National Minimum Wage
- Marginal Cost with NMW
- Employment of Labour (E)

Equilibrium Wage (Wq) and Employment (Eq) with Minimum Wage (NMW)
The Gender Pay Gap

2003
Gross hourly earnings:
by sex and whether working full-time or part-time
(£ per hour)

<table>
<thead>
<tr>
<th></th>
<th>Males</th>
<th></th>
<th>Females</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>part-time</td>
<td>full-time</td>
<td>part-time</td>
<td>full-time</td>
</tr>
<tr>
<td>2003</td>
<td>8.82</td>
<td>12.88</td>
<td>7.78</td>
<td>10.56</td>
</tr>
</tbody>
</table>
The Gender Pay Gap in 2004

- According to the Office of National Statistics
- In 2004, women's median hourly pay was 85.7 per cent of men's, compared with the 85.4 per cent recorded in April 2000
- Median weekly earnings of full-time employees in 2004 for women (£358) were 77.5 per cent of those for men (£462)
- Women's weekly earnings (including overtime) were lower than men's, partly because they worked around two hours fewer per week
- The gender pay gap is measured by the median hourly pay of full-time employees, excluding overtime
- Pay medians are affected by the different work patterns of men and women, such as the proportions in different occupations and their length of time in jobs
Explaining the gender pay gap

- **Human capital**: i.e. there are differences in educational levels and work experience between males and females. Breaks from paid work, including time to raise a family, can impact on women's level of work experience.

- **Part-time working**: a significant proportion of women work part-time and part-time work typically pays less well than full-time jobs.

- **Travel patterns**: on average, women spend less time commuting than men with the result that they will have a smaller pool of jobs to choose from.
Explaining the gender pay gap

- **Occupational segregation**: women's employment tends to be concentrated in certain occupations. There is continued under-representation in higher paid jobs within occupations – the so-called "glass ceiling" effect.

- **Employer discrimination**: Work by the LSE calculates that up to 42% of the gender pay gap is attributable to direct discrimination against women.

- The **effects of monopsony power**: Females may be relatively geographically immobile (because they are tied to their husbands' place of employment) and may be paid less than a competitive wage by a monopsonist employer.
Explanations for the Gender Pay Gap (1)

- Human capital: differences in educational levels and work experience
- Breaks from paid work which impact on women's work experience
- Part-time working: a large proportion of women work part-time (often to balance family commitments) this is a major contributor to the gender pay gap.
- Travel patterns: on average, women spend less time commuting than men
  - They will have a smaller pool of jobs to choose from
  - It may also result in lots of women wanting work in the same location (i.e. near to where they live) which will result in lower wages for those jobs
Explanations for the Gender Pay Gap (2)

- Occupational segregation: women's employment is concentrated in certain occupations (60 per cent of working women work in just 10 occupations)
  - Occupations which are female-dominated are often the lowest paid jobs
  - Under-representation in higher paid jobs within occupations - "glass ceiling" effect.
- Other factors which affect the gender pay gap including:
  - (i) appraisal systems, reward systems and retention measures
  - (ii) wage-setting practices
  - (iii) employer discrimination affecting the perceived productivity / marginal revenue product from female employees