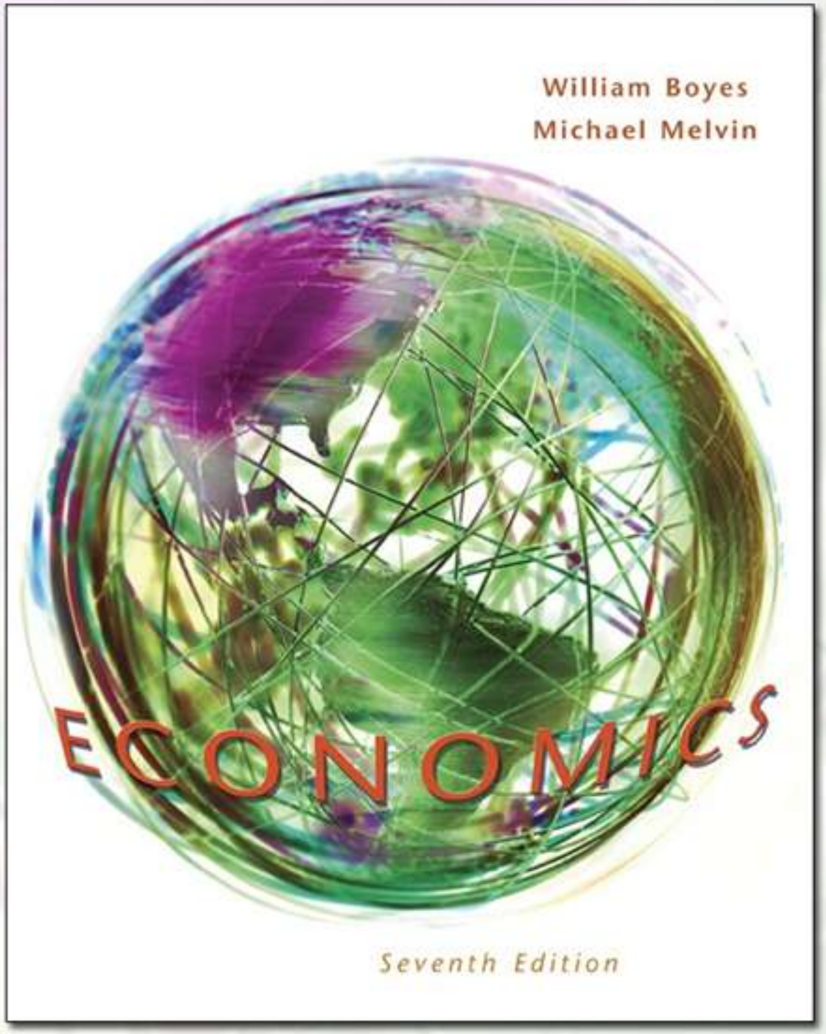


Chapter 29 and 30

Resource

Economics, 7th Edition

Boyes/Melvin

Resource or Factor Markets

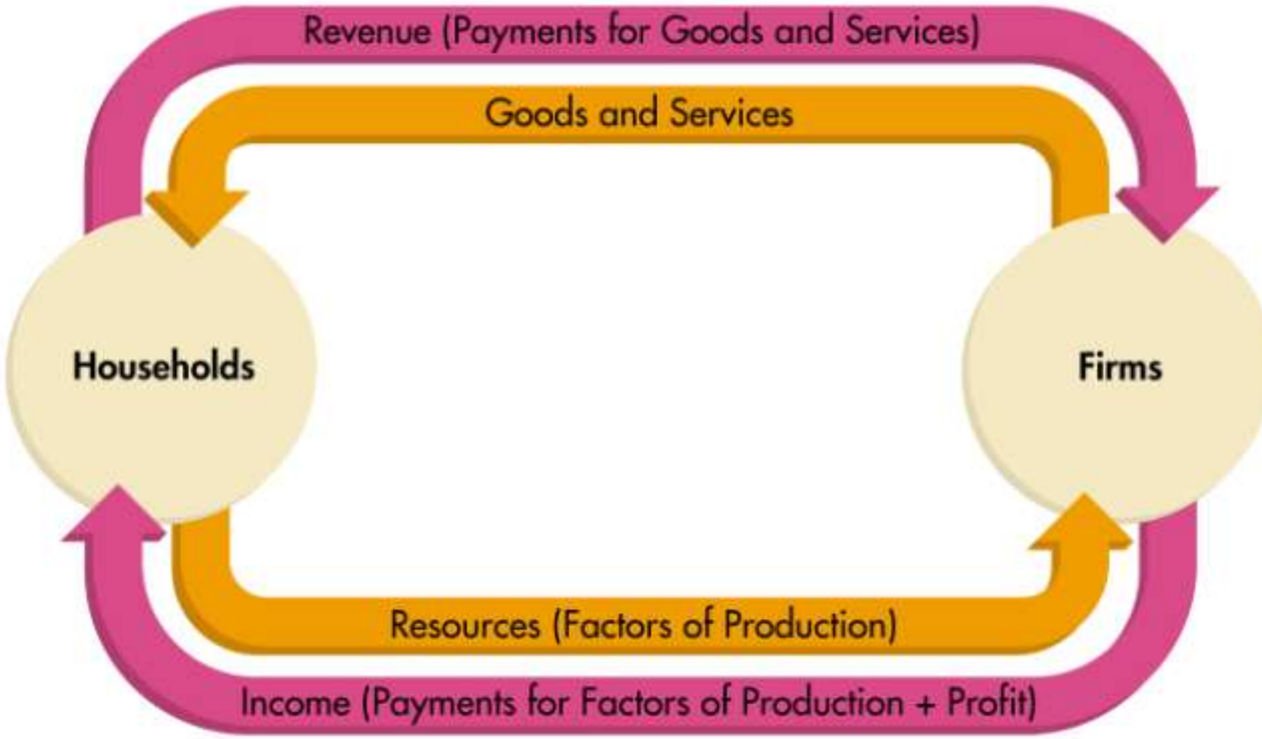
- Resource market: a market that provides one of the resources for producing goods and services: labor, capital, land.
  - Rent and quantity of land used are determined in the **land market**
  - The wage rate and employment are determined in the **labor market**
  - The interest rate and the quantity of capital used are determined in the **capital market**

Firms and Households

- Households sell resources
- Firms buy resources

The Market for Resources

FIGURE 1 The Market for Resources



The buyers of resources are firms that purchase resources in order to produce goods and services. The sellers of resources are households that supply resources in order to obtain income with which to purchase goods and services.

Derived Demand

- **derived demand**— resource demand is based on the demand for the product that the resource is producing

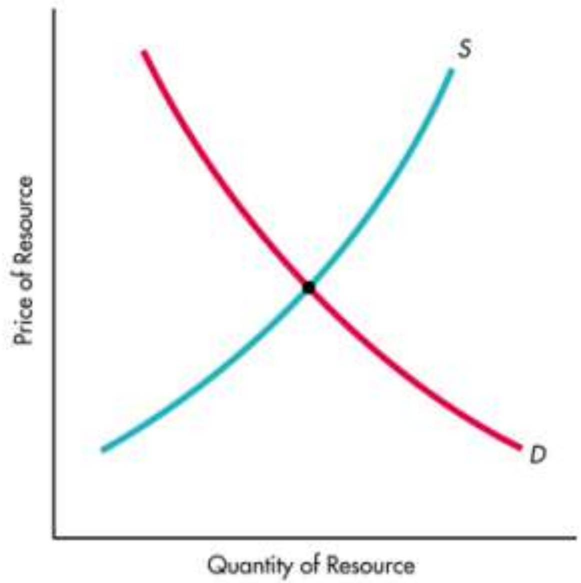
The Firm’s Demand

- **Marginal factor cost (*MFC*)**: the additional cost of another unit of a resource
- **Marginal revenue product (MRP)**: the additional revenue an additional resource can create for a firm.

- Firms hire resources until MFC=MRP

Resource Market Demand and Market Supply

FIGURE 2 Resource Market Demand and Market Supply



The demand curve for a resource slopes down, reflecting the inverse relation between the price of the resource and the quantity demanded. The supply curve for a resource slopes up, reflecting the direct relation between the price of the resource and the quantity supplied. Equilibrium occurs where the two curves intersect; the quantities demanded and supplied are the same at the equilibrium price. If the resource price is greater than the equilibrium price, a surplus of the resource arises and drives the price back down to equilibrium. If the resource price is less than the equilibrium price, a shortage occurs and forces the price back up to equilibrium.

Hiring Resources in a Perfectly Competitive Market

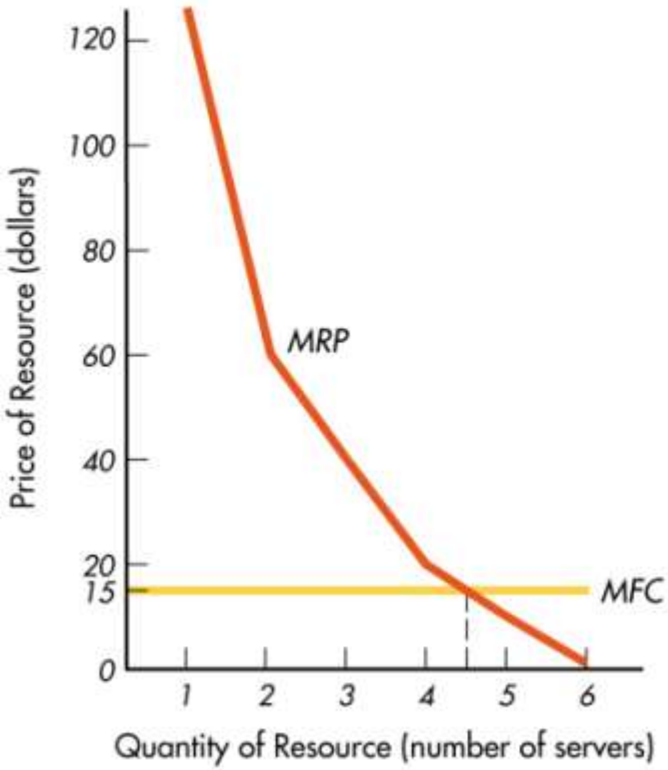
- Resource cost is constant.
- Example: low skilled labor.

The Employment of Resources

FIGURE 3 **The Employment of Resources**

The marginal revenue product and the marginal factor cost together indicate the number of servers the restaurant would hire. The *MRP* and the *MFC* for a restaurant are listed in the table. The *MRP* curve and the *MFC* curve are shown in the graph. The marginal revenue product exceeds the marginal factor cost (wage rate) until after the fourth server is hired. The firm will not hire more than four, for then the costs would exceed the additional revenue produced by the last server hired.

(1)	(2)	(3)
Number of Servers	*MRP*	*MFC*
1	$130	$15
2	$60	$15
3	$40	$15
4	$20	$15
5	$10	$15
6	$0	$15



Monopsony

- A **monopsonist** is a firm that is the only buyer of a resource.

The only business in a small town.

Mining towns, for example.

When Hiring More than One Resource

- At equilibrium, the last dollar spent on resource must yield the same marginal revenue product no matter what resource the dollar is spent on.

$$\frac{MRP_{land}}{MFC_{land}} = \frac{MRP_{labor}}{MFC_{labor}} = \cdots = \frac{MRP_{n}}{MFC_{n}}$$

If a resource is very expensive relative to other resources, it must generate a significantly larger MRP than the other resource.

Economic Rent

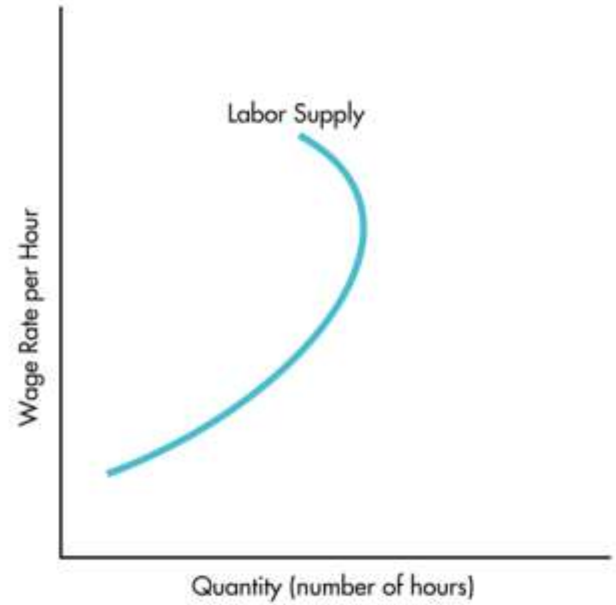
- Transfer earnings: the minimum amount of payment it would take to get a resource to move from one firm to another. (My salary, for example)
- **economic rent** is anything that I may earn over my transfer earnings.

- My new job pays me $20,000 more than I'm currently earning, my Economic Rent is 20,000.

- Who earns more in economic rent, Mrs. Unger or Tiger Woods?

The Individual’s Labor Supply Curve

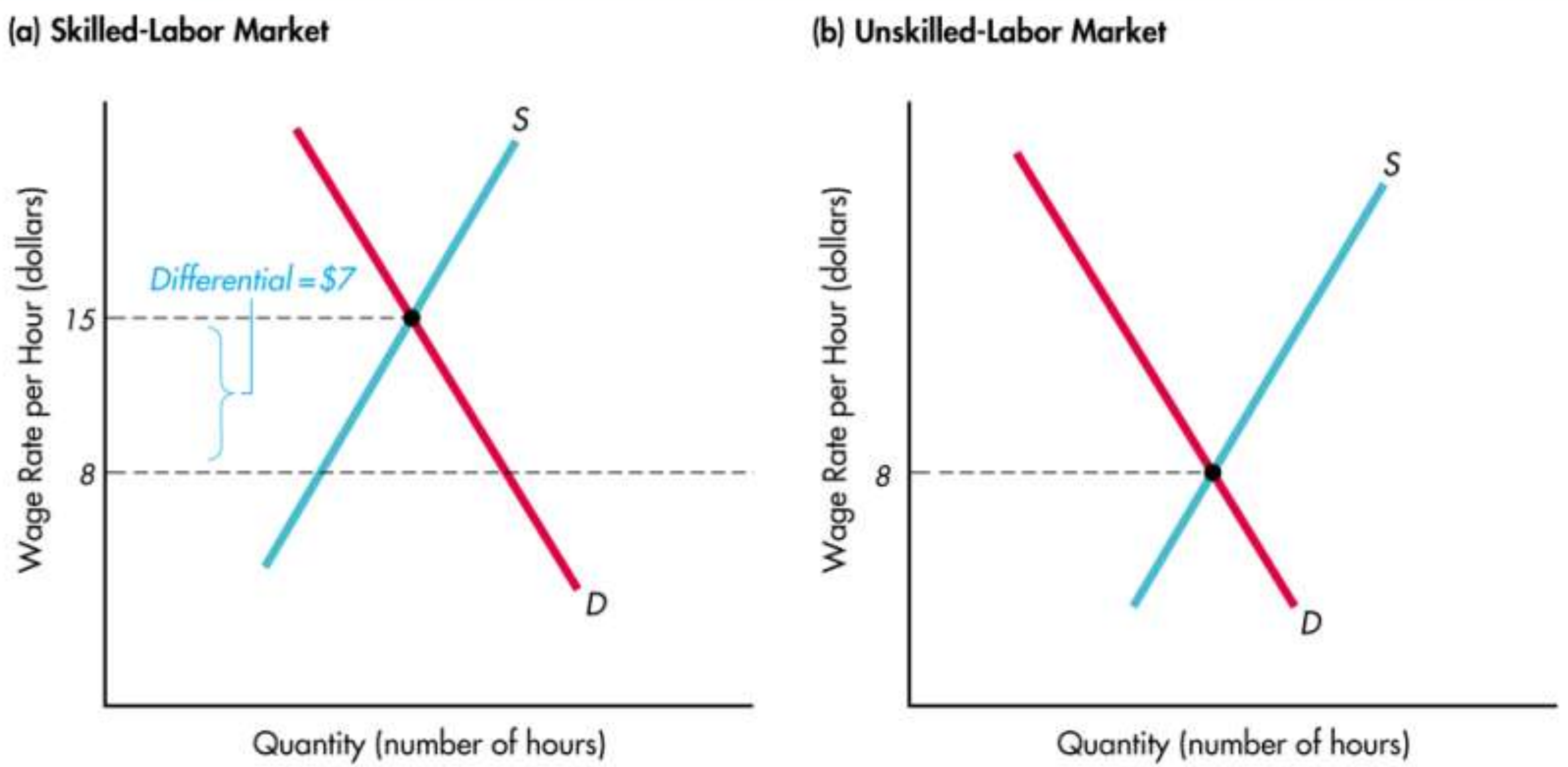
FIGURE 1 The Backward-Bending Labor Supply Curve



As the wage rate rises, people are willing and able to supply more labor, at least up to some high wage rate. A higher wage rate means that the opportunity cost of leisure time increases, so that people will purchase less leisure (will work more). Conversely, as the wage rate rises and people’s incomes rise, more of all goods are purchased, including leisure time. As a result, fewer hours of work are supplied. Which of these opposing effects is larger determines whether the labor supply curve slopes upward or downward. The most commonly shaped labor supply curve is one that slopes upward until the wage rate reaches some high level and then, as people choose more leisure time, begins to bend backward.

Human Capital

FIGURE 4 **Human Capital**



Two labor markets are pictured. Figure 4(a) shows the market for skilled labor. Figure 4(b) shows the market for unskilled labor. The smaller supply in the skilled-labor market results in a higher wage there. The equilibrium differential between the wages in the two markets is the return to human capital.

Discrimination

- **Discrimination** is an economically unsound practice, no matter what type (sex, age, gender, etc)

- **Discrimination is costly** and it is contrary to profit maximization.