LABOR MARKETS AND EMPLOYMENT RELATIONSHIPS

A Comprehensive Approach

JOYCE P. JACOBSEN *and* GILBERT L. SKILLMAN

Blackwell Publishing

Labor Markets and Employment Relationships

Joyce Jacobsen: To Bill, Catherine, and Kenneth
Gilbert Skillman: To Sue and my parents

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PREFACE

The study of labor markets and employment relationships is among the most exciting and dynamic fields of inquiry in the discipline of economics. As such, it has given rise to a number of ongoing debates concerning matters of fundamental importance to the human condition, including the organization of work, the distribution of income, the nature, incidence and causes of unemployment, and the appropriate functions of the state and the market in the determination of economic outcomes. These debates have prompted in turn the development of new methods of theoretical analysis, new means of assessing competing hypotheses, and new sources of relevant data.

However, it is difficult for students to appreciate the significance and vitality of these debates without the perspective offered by an analytical framework broad enough to encompass all sides of prevailing controversies in the field. Start with the presumption that labor markets are perfectly competitive or virtually so, for example, and it becomes arbitrarily easy to dismiss the possibility of persistent unemployment in the absence of government intervention in the labor market. Conversely, categorical rejection of competitive market analysis or other formal theoretical treatments of labor market phenomena raises the risk of losing insights yielded by these approaches which remain relevant even if their premises are not strictly satisfied.

Our primary motive in writing this text has been to develop an analytical approach to the subject matter of labor economics that is versatile enough to accommodate competing positions in most of the major controversies and lines of inquiry animating the contemporary discipline, yet tractable enough to be understood by new students of the field who have some background in the larger discipline of economics. In keeping with this goal, the text begins on the familiar turf of competitive market theory, but presents this material so as to promote critical awareness of the core assumptions undergirding this approach and of labor market conditions that may clash with these assumptions. We then use this critical perspective to motivate the introduction of a broader theoretical framework

that is nonetheless recognizably grounded in the methods of economic analysis most students learn in their introductory and intermediate economic theory courses.

The key to this more general framework lies in the observation that institutions of exchange, particularly those manifested in labor market transactions, are generally premised on individual efforts devoted to searching for and pairing with prospective trading partners, negotiating terms of trade with selected partners, and ensuring that negotiated terms of trade are carried out; and that these economic activities, like all others, incur costs. The presence of significant mobility or transaction costs undercuts the economic logic of the perfectly competitive model, and gives rise to conditions of market power or imperfect contracting that may yield outcomes that are fundamentally at odds with the model's standard predictions and normative claims. Therefore, allowing for various configurations of these costs (including their virtual absence) makes it possible to investigate a much broader array of labor market phenomena, while maintaining the familiar tenets of optimization and equilibrium that give structure to the simpler theory.

While this approach owes an obvious debt to "transaction cost economics," associated with the influential work of Oliver Williamson, it differs from that construct in at least two significant ways. One difference is a matter of scope: while the main focus of transaction cost analysis concerns the organizational implications of factors giving rise to contractual incompleteness, the approach outlined in this text also embraces forms of exchange costs that give rise to wage-setting power and that create incentives for monitoring of effort or the provision of signals about unseen characteristics. A second difference is methodological, in that the strategic analysis of costly labor exchange presented in this text is grounded more explicitly in the basic framework of noncooperative game theory.

The analytical material in the text, including its game-theoretic foundation, is presented in verbal and graphical form with occasional mathematical supplements placed in chapter appendices. While the theoretical analysis is entirely self-contained, students familiar with the notions of indifference and isoquant maps will find the going easier, especially in the early chapters. Accordingly, the text is intended primarily for use in upper-level undergraduate courses in economics or in masters' programs in economics, industrial relations, and public policy.

Every topic addressed in the text is motivated and illustrated by reference to contemporary and historical empirical trends. However, given the rapidity with which labor market conditions change, it is impossible for any text to provide completely up-to-the minute data, and we have not attempted to do so. We encourage instructors to supplement the empirical information in the text as desired with additional readings or web-based sources.

Some additional suggestions for using this text: first, most instructors will find it difficult at best to cover the entire book in a single semester course, and therefore it will generally be necessary to decide beforehand which chapters to omit, which to cover partially or in broad outline, and which to give special attention. We consider the introductory chapter plus chapters 1 through 8, comprising parts I and II, to provide the foundation for the analytical approach developed in the

text. Instructors might therefore consider spending the first half of the semester on these "core" chapters, depending on the preparation levels of their students.

The topics to be covered in the second half of the semester will depend on the particular focus of the course being taught. Courses emphasizing the nature and operation of labor market institutions might therefore concentrate on the chapters in part III, which address various features of the employment relationship, plus chapters 15 and 16, dealing respectively with discrimination and the hypothesis of labor market segmentation. A more traditional survey course might wish to skip part III entirely except for the chapter 11 discussion of on-the-job training, and focus instead on the chapters of part IV concerning labor market divisions, in particular those concerning variations in working conditions (chapter 13) and formal educational attainment (chapter 14).

The end-of-chapter questions are designed to promote students' hands-on understanding of the material, either by suggesting concrete applications of abstract analytical material or pursuing extensions of ideas and results suggested in the text. Instructors can obtain suggested answers to these questions by contacting the authors.

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