

ECON 5103 Unit 4, Video 3
Individual behavior, part III

Work vs. Leisure

Benefit of work:

Earn income to spend today (or save to spend another day)

Cost of work:

"Leisure": You give up time that you could spend doing other things not for pay.

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How does an increase or reduction in wages affect the amount that someone wants to work?

Example: Buffy gets an increase in her hourly wage. Will she want to work MORE hours or FEWER hours?

"Substitution effect": The reward for working each extra hour has increased, giving Buffy an incentive to work more hours.

"Income effect": Buffy could work fewer hours (spending more time with her family) yet still earn the same total weekly pay as before.

Without knowing more about Buffy, we can't be sure whether she'll work more or less, because she's being pulled in two directions.

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Know your employees before designing a compensation package (especially salespeople who may some base pay + commission)

Example: An apartment manager increased the commissions he paid to his leasing agents per apartment leased.

INTENTION: Motivate the leasing agents to lease more apartments.

ACTUAL EFFECT: Leasing agents leased fewer apartments, understanding that their total pay would still be higher even though they leased fewer apartments.

For the leasing agents, the income effect was the dominant effect. (the apartment manager had hoped that the substitution effect would be the dominant effect.

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Income-Leisure Table: A table that shows some income/leisure options facing a worker

Zippy earns \$20 per hour and can choose his amount of daily hours worked from 0 to 18.

Hours of <u>leisure</u>	Daily Labor Income
0 hours	$18 \times \$20 = \360.00
3 hours	$15 \times \$20 = \300.00
8 hours	$10 \times \$20 = \200.00
14 hours	$4 \times \$20 = \80.00
18 hours	$0 \times \$20 = (\$0.00)$

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