

# *Why did Indentured Servitude and Slavery exist in Early Colonial America?*



**Decision Making:  
Opportunity Cost & Incentives**

# Opportunity Cost

- 🍏 Highest-valued foregone alternative
  - the value (to you!) of the **next-best alternative** that you sacrificed/give up
  - What are you giving up?
- 🍏 It is always subjective
  - You know your costs
- 🍏 It is sometimes objective
  - Sometimes the costs can be measured in, say, dollars and cents or in time



# **Economic Principle #1:**

## **People choose, and individual choices are the source of social outcomes**

- Scarcity necessitates choices: not all of our desires can be satisfied.
- People make choices based on their perception of the expected costs and benefits of the alternatives.
- **Choice #1 + choice #2 + choice #3 = Social outcomes**



# OPPORTUNITY COST

## Economic Principle #2:

**Choices have costs; people receive benefits and incur (have) costs when they make decisions**

- The cost of a choice is the value of the next-best alternative foregone, measurable in time or money or some alternative activity given up.

# OPPORTUNITY COST

- **All choices have cost... some big, some small**

OPPORTUNITY COST



# Characteristics of Cost:

- Costs are “to” someone, i.e., people bear costs, not businesses or governments, etc.
- Costs are the results of choices
- Costs relevant to decision making lie in the future, i.e. those not yet incurred
  - Past, inescapable, “sunk” costs are gone
  - Example: You sacrificed \$X and 1 day to get there; these costs are sunk—inescapable
  - The costs that are **relevant for staying** are those that are avoidable



# **Economic Principle #3:**

## **People respond to incentives in predictable ways**

- Choices are influenced by incentives
  - POSITIVE INCENTIVES: the rewards that encourage (Extra Credit)
  - NEGATIVE INCENTIVES: the punishments that discourage actions. (Cleaning your room)
- When incentives change, behavior changes in predictable ways.



# Incentives

- The rewards or penalties that result from the choices people make
- They may be **negative** or **positive**
- They may be **monetary** or **non-monetary**
- But they are inescapable, and they help guide the choices we make



# Objectives, incentives, and choice

- The choices people make depend on
  1. Who they are, what they like and want to accomplish, their hopes, dreams, etc
  2. The incentives they face
- Item 1 is known to each decision-maker, but often not to us, the outside observers
- Item 2 **is** observable to us, the outside observers
- The reason that we (and other economists) focus so much on Item 2 is because it is observable, not because Item 1 is unimportant



# Choices are made at the “margin”

- **Marginal:** additional, next, a little more or a little less
- Sometimes the “margin” is large & lumpy
  - Go on big Vacation or Not
- Sometimes the “margin” is small & smooth
  - Eat one more french fry or not
- The key to good decision-making is to identify the correct “margin”



# A simple example

- When the price of gas went from \$2/gal. to \$4/gal, almost no one stopped driving
  - “To drive or not to drive” was not the question
- Does this mean the price of gas has no influence over driving decisions?
- NO! Almost everyone made any of a series of small adjustments at the margin
  - Fewer trips, more buses, bikes, & car-pooling, slower acceleration, more coasting, etc.
- “All or nothing” is almost never the margin



# *Why did Indentured Servitude and Slavery exist in Early Colonial America?*



## **Labor Markets**

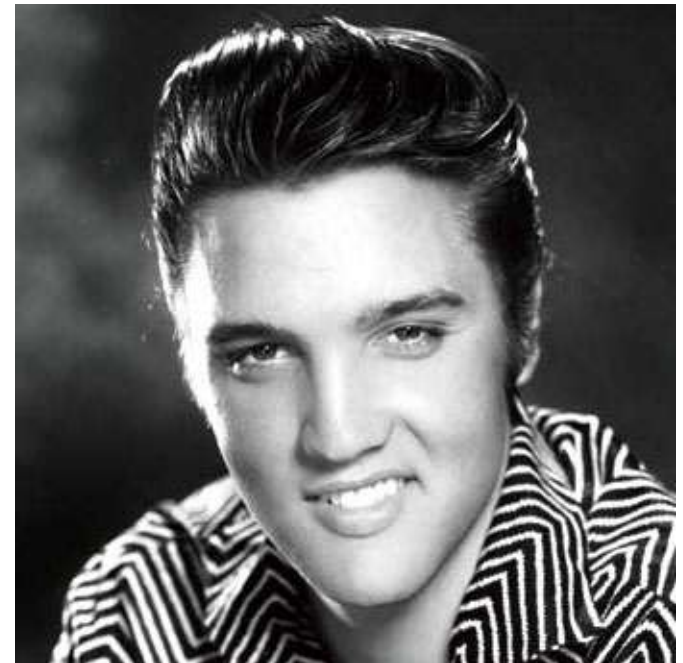
# Why are there superstars?



# Superstars!

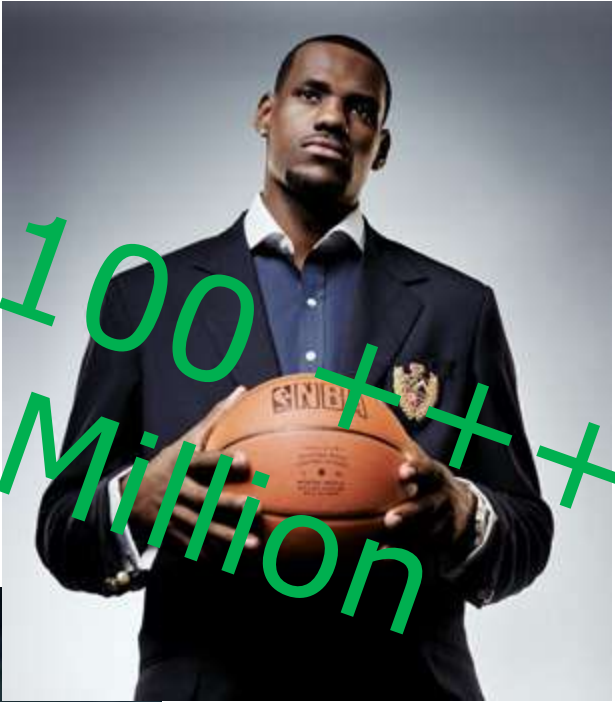


← \$275 Million  
\$52 Million ↓





← \$300 Million



\$100 Million ++++



\$110 Million



RIP

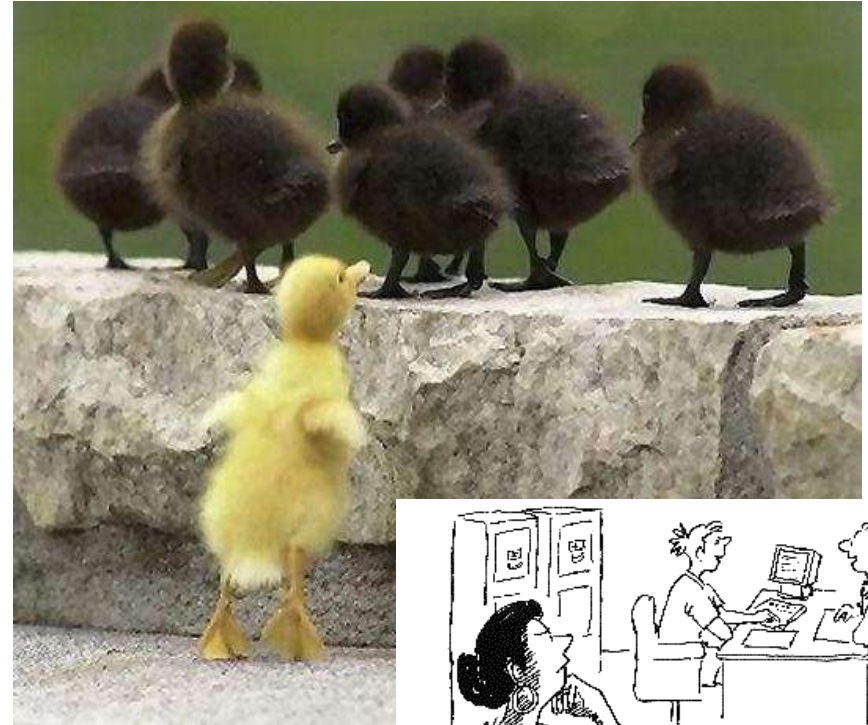
\$647  
Million



# Why Not Everyone?

Discrimination?

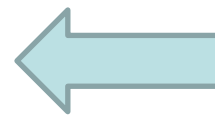
Environment?



# or is it . . . .



Poor schools?



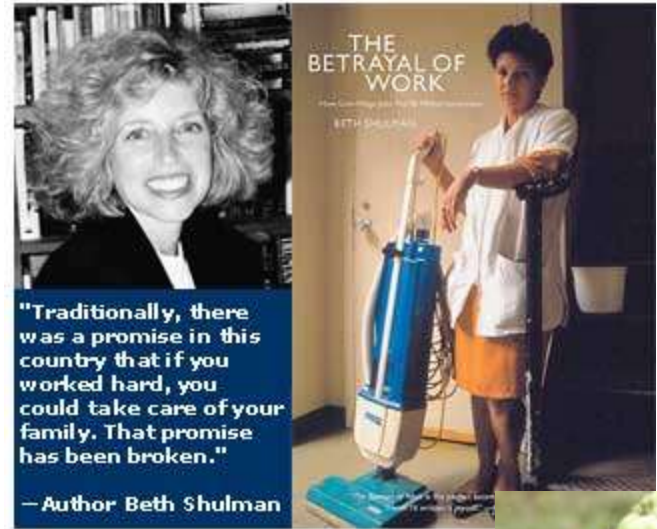
Ability?



# Why are there Working Poor?



**WORKING and POOR**



"Traditionally, there was a promise in this country that if you worked hard, you could take care of your family. That promise has been broken."

— Author Beth Shulman



\$5.15

\$5.85

\$6.55

~~\$7.25~~

\$7.67

**MINIMUM WAGE**



# Demand



Ultimately, what we are paid depends on the market for our services

# Supply



# It starts with **demand**: Somebody's willingness to pay

- 🍏 There are two elements:
  - How much do workers produce?
  - What value do consumers put on it?
- 🍏 But (for 25 cents per item +/- wage) what determines a firms' willingness to pay?
  - Skill or experience
  - Education
  - Quality & quantity of other inputs (tools, machines, etc)
  - Size of market
  - Others?



# It continues with **supply**: Willingness to accept

🍏 For 25 cents each, what affects workers' willingness to accept this wage?

1. Alternatives: WHAT R the Other Options

- Can you say “opportunity cost”?

2. Working conditions

- Safety
  - Surface vs. underground mining (WV, Chile)
- Status: Non-pecuinary
  - Prestige, co-workers, location, etc.



# Answer me this . . .

- 🍏 How do you feel about
  - Slave labor? (Boo!!!)
  - Sweatshops? (Boo! Yeah! Booh! Yeah!)
  - Child labor?  
(YEEEEEEEEEEEEAAAAAAAAAAAAAAAAAAAAAA  
AHHHHHHHHHHHHHHHHHHHHHHHHHHHHHH!!!!!!)



Ta da . . . !

The good,



the bad,



. . . and the  
ugly



# First, the **bad**: **Slave labor**

- 🍎 Involuntary and thus morally repugnant (wrong... very wrong)
- 🍎 Violation of the ultimate property right: **right to self**
  - Anti-capitalist
- 🍎 Reduces society's wealth
- 🍎 Why do we see it?
  - Because it redistributes wealth

TO BE SOLD, on board the  
Ship *Bance Island*, on tuesday the 6th  
of May next, at *Ashley-Ferry*; a choice  
cargo of about 250 fine healthy  
**NEGROES**,  
just arrived from the  
Windward & Rice Coast.  
—The utmost care has  
already been taken, and  
shall be continued, to keep them free from  
the least danger of being infected with the  
SMALL-POX, no boat having been on  
board, and all other communication with  
people from *Charles-Town* prevented.  
*Austin, Laurens, & Appleby.*  
N. B. Full one Half of the above Negroes have had the  
SMALL-POX in their own Country..



# Then the **good**: **Sweatshops**

- 🍏 Alternatives,  
alternatives,  
alternatives
- 🍏 Can you say  
“opportunity cost?”



# Sweatshops are not slave labor

Sweatshops are voluntary  
exchange

- As such they create gains to  
both worker and employer
  - Both sides benefit



# The glorious history of sweatshops

- Voluntary trade creates wealth
  - Take away trade and you leave only poverty
- 🍏 U.S. and U.K. in the Industrial Revolution
  - 🍏 Taiwan & South Korea vs. India after WWII
  - 🍏 CHINA???



# And what about the dragon?

- From 1978 to 1995, 20 fastest growing “nations” were all Chinese provinces
- Between 1986 and 2008, real wages rose by a factor of ten in South China
- It took 58 years for income to double in UK during Industrial Revolution
- Real income has been doubling every 10 years in China

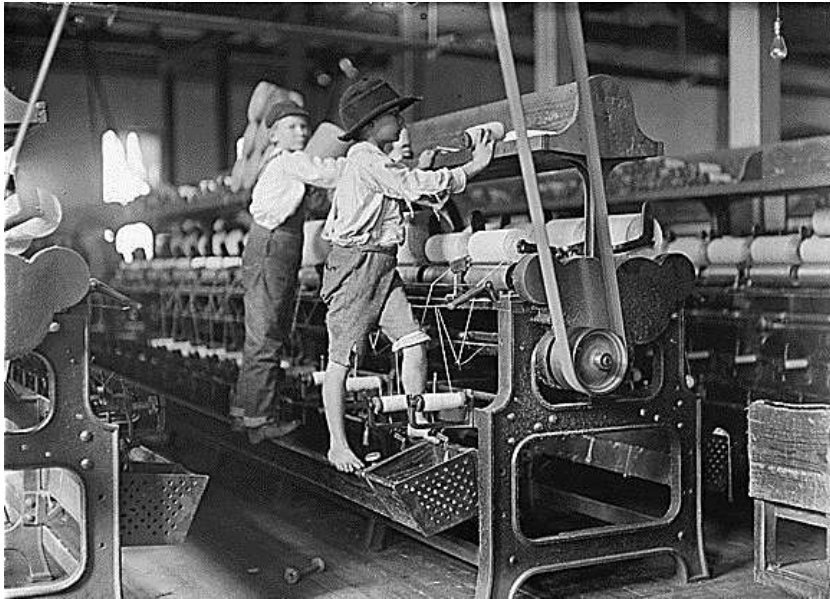


# Then why are many people appalled?

- Because sweatshops reflect a lack of alternatives
  - Surely no opportunity cost can be that low?
  - But it is, for many people around the world
    - we live in a bubble (but, not all of us)
- What can you do?
  - Recognize that today, institutions are the root of the problem for most
  - Improve workers' alternatives: buy globally, not locally
    - By patronizing sweatshops, WalMart has vastly improved the lot of workers



# And now, the **ugly**: **Child Labor**



# Question #1: Is it voluntary?

- 🍏 We know that voluntary trade creates wealth
  - True, but...
- 🍏 But can an eight-year-old choose not to work when a parent says “work”?
  - And if not, can we be confident that it raises wealth?



# Question #2:

## What are the alternatives?

- Child labor *disappears* as living standards rise
  - This suggests that the problem is alternatives
- What are the alternatives to child labor?
  - For some it is starvation
  - For others it is far worse
- Does child labor beat the relevant alternatives?
  - Starvation, prostitution, or factory work... you pick???





**Can we solve this?**

