Answer on Question #88812 – Economics – Macroeconomics

In the classical model of the labor market, involuntary unemployment will increase if?

Minimum wage is set above equilibrium wage by the government.

Classical model of the labor market is a labor theory which states that markets behave as described in the supply and demand model. That, wage is determined by the interplay of demand and supply in the industry and that firms in the industry are wage takers. That means, there is an equilibrium wage in the market.

When the government passes a legislation to set a minimum wage above the equilibrium wage, this will lead to involuntary unemployment. With the minimum wage being above, the equilibrium wage, employers will hire few workers at a higher wage. At the same time, people want jobs leading to a surplus. But because of the minimum wage limit legislation, the market is prevented from adjusting to equilibrium. Thus, this will lead to an increase in involuntary unemployment.

Reference

https://resources.saylor.org/wwwresources/archived/site/wp-content/uploads/2010/11/Theories-of-Unemployment.pdf