CASE PROGRAM 2014-160.2

Pay slip at the ABC (B): Supplementary teaching resource

The CONVERSATION

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What is Tony Jones really worth?

Tony Jones. ABC

There is currently much ballyhoo – in the Murdoch Press at least – about the release of secret files on the salaries paid to the top talent at our ABC. **Tony Jones**, for instance, pulls down A$355,789, making him a **one-percenter**, as we used to say. (Occupy Ultimo, anyone?)

But what are Tony Jones and the rest of the ABC mob really worth? Economics can help with this question.

Karl Marx once said "From each according to their ability, to each according to their need." It's a fine and noble sentiment that works well in small-scale societies, such as a hunter-gatherer tribe, or within the family. Yet in the real world the problem with this mechanism is it is not what economists call **incentive compatible**. People have an incentive to understate their abilities, and to overstate their needs.

When I taught economics of social issues I had a strict rule in my classroom about the four-letter F-word.

This supplementary teaching resource has been accessed from: http://theconversation.com/what-is-tony-jones-really-worth-20629. for use with 2014-160.1

If you thought that something was as it was because it was “fair”, or that something was wrong because it was “not fair” you were sent out of the class. That’s how children speak, not economists. Yet many of what I presume are adults (in the various letters to editors, blogs, twittering) have argued that these wages paid to the ABC talent are not fair. Or that criticism of the ABC is not fair. That’s not going to get us anywhere.

In modern economic theory, people are paid what they are worth. In a competitive market, you are worth your **marginal revenue product**. That’s the additional value to the company’s revenue that your additional labour adds. Theoretically, a well-run company will keep hiring up to the point where the wages of the last person hired (the marginal cost) equals the added value to revenue that they produce (their marginal revenue product).

Now this is a theory and in practice all sorts of other considerations come into it. But it provides a framework for thinking about what a particular unit of labour is worth. So what about this ABC talent? What is its marginal revenue product (MRP)?

Here’s the thing: we don’t know that because there is no revenue from which to figure this out. Public broadcasters don’t sell into a market. When the commercial broadcasters pay their talent the big dollars they do so because they do know their MRP. They know that adding Johnny Bigsmiles to the breakfast line-up will bring in 100,000 extra viewers, which they can sell to advertisers for A$10 each, making Johnny’s MRP A$1,000,000. In a competitive market for media talent, that is also Johnny’s wage.

But in public broadcasting, there is no way to figure out the MRP, and so no basis for figuring out the proper wage, other than by comparison with the market generated price. So Jimmy Seriousface at the ABC gets a wage that is based on some comparison with Johnny’s wage.

Note this is not just a problem for the ABC, but affects the whole of the public sector’s pay scales, none of which have access to true prices from which to figure out MRP and thus wages based on economic worth. Back when people thought **market socialism** might work, the same problem arose. The theory was that every country could be socialist except one (Switzerland, say), which would need to remain capitalist so that it could figure out the correct prices to be copied by all the other countries.

The real question is about the legitimacy of the comparison with the market-determined wages. Here the economics gets trickier. The theory of **efficiency wages** suggests that motivating efforts requires some degree of comparability. The theory of **compensating differentials** means that because of the perks of public sector work (greater job security, for instance), public sector work will be less well remunerated compared to the private sector. In the economics of information, high salaries can serve as a **screening mechanism** to encourage people to invest in revealing their true talents and capabilities, which may mean investing many years working for very low wages in order to have a shot at the top jobs.

Another theory is that public sector wages need to be “competitive” in order to attract top talent. But that’s a sly argument, because it’s zero-sum: the talent attracted is now no longer available in the private sector, where it may have added greater value. A Tony Jones at the ABC is no longer available to produce the great work in the market media environment, which is presumably the poorer for that. Competitive wage claims based on attracting talent may make us all worse off (except for Tony, of course).

The point is that while we may know in theory how to figure out what someone is worth, in practice this is extremely difficult, and doubly so where we cannot rely on the marginal contribution to firm revenue.

So how should we figure out what Tony Jones is really worth? The reality is that in a market economy we can figure that out, but in a non-market economy (such as the ABC operates in) we can’t. Selling the ABC and seeing what extra value we get for Tony is probably the only sure fire way we can resolve this dilemma.