

Family Decisionmaking and Labour Force Participation

Shelly Lundberg
University of Washington

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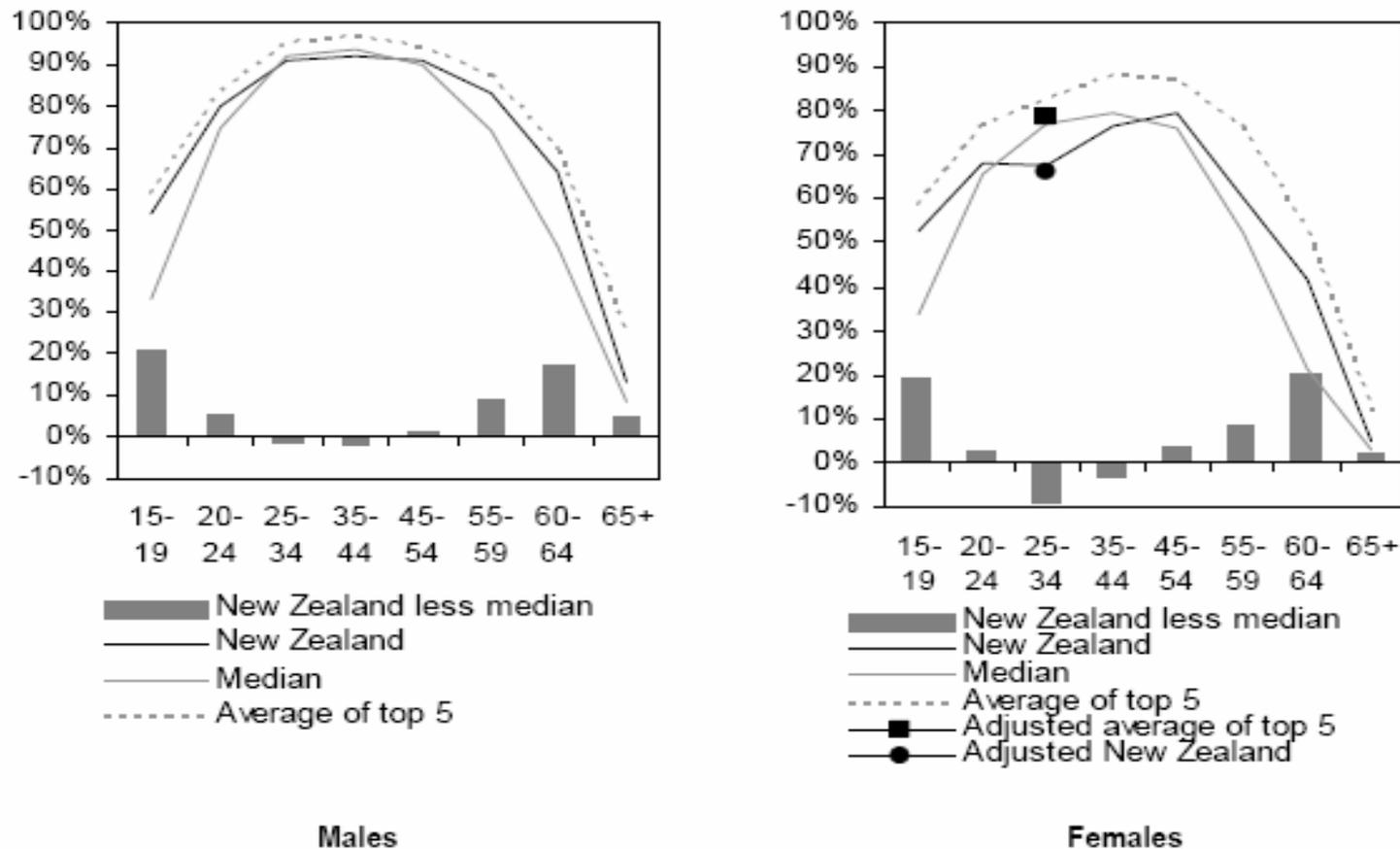


A nation's principal source of wealth is the skill and energy of its people.

Labor force participation in New Zealand vs. OECD median and OECD top 5 (Bryant, Jacobsen, Bell, and Garrett, 2004)

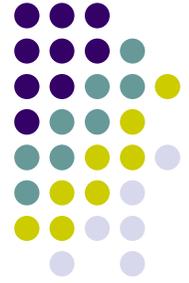


Figure 2 – Labour force participation rates, 2001



Source – Calculated from data in the OECD *Labour Market Data* online database.

Labour force participation decisions for 3 key groups have a distinct family dimension:



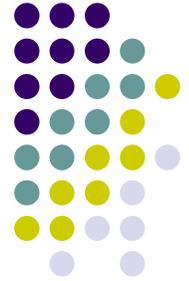
- Youth (age 15-19)
- Young women (25-34)
- “Mature” men and women (55-64)

Employment rates as a policy issue:



- European Union: Lisbon Strategy for economic reform includes ambitious employment goals for 2010
 - 70% overall, 60% women, 50% older adults

EU Reform Goal--To create a dynamic and efficient economy.

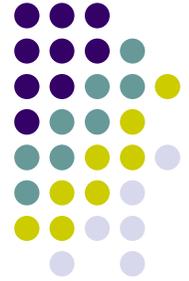


- Concerns:
 - high rates of unemployment, especially for the young
 - aging population—low fertility rates, pressure on social welfare systems
- Recommendations to member states:
 - “...develop policies to increase labour market participation and entrepreneurship of women, young people, ethnic minorities, immigrants, and of those people at a disadvantage...and ...measures to reconcile work and family life.”

New Zealand—somewhat different concerns:



- Unemployment relatively low.
- Fertility rate close to 2.
- Desire to restore GDP to or above OECD average—promote income growth
- Keep employment rates for most groups high; encourage more market work for young women?



Related policy issues:

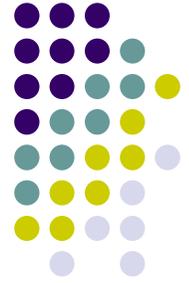
- Youth—school-to-work transition
 - job quality, human capital development
- Young women—moms (and dads) and jobs?
 - child wellbeing, gender equity
- Older adults—retirement timing
 - “active aging”
- Inequality
 - barriers to employment for the disadvantaged
 - poverty, intergenerational persistence

The Economics of Labour Force Participation



- A simple static model
- A dynamic, life-cycle model
- Joint decision-making in families
- Equilibrium considerations: economic, political, and social

A Simple Static Model of Labour Force Participation



- Join the paid labour force when the marginal return to the first hour in a market job $>$ marginal return to the best alternative use of that hour
- Complications that don't cause problems:
 - restrictions on work hours
 - non-pecuniary returns to work
 - job search

Important note: Participation decisions are made by people with something else to do with their time.



When young mothers enter paid employment, much of the work they were doing at home is replaced by market substitutes—the “marketization” of home production.

Hours worked per adult are lower in Europe than in the U.S.

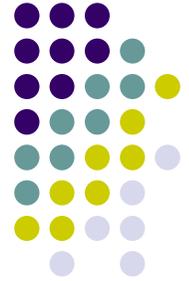


- Time-use studies show that total work hours (home and market) are about the same (Freeman & Schettkat, 2005; Schettkat, 2003)
- Europeans (esp. women) spend more time in food prep., care of children and elderly, and cleaning
- U.S. has “marketized” the production of household goods and services more than Europe.

National income accounting:



- Standard national accounts are a flawed and incomplete measure of welfare
 - do not include value of home production
- Part of the increase in GDP that results from increased employment of young mothers is illusory.
 - Welfare effects < measured effect on GDP



What do we lose?

- Home childcare and eldercare
 - quality issues, economies of scale
- Other household production
 - the Big Mac effect
- Community externalities
 - volunteering, neighborhood effects

Policy levers in the static model— increase LFP by increasing the net return to market work:



- Increase value of market work
- Reduce prices of market substitutes for home production
- Remove bureaucratic, legal barriers to work-family juggling

Labour Force Participation Over the Life-Cycle



- Working now has implications for future opportunities—employment, stable employment, attachment to a particular employer yield higher wages later.
- Retirement to some extent irrevocable—termination of career job
- Women who stay home with children can expect wage losses when they return to work



The “Family Gap”

- Women with children have lower wages than women without children
- Difference cannot be explained with observable human capital variables—including detailed measures of work experience (Waldfogel, Joshi)



- Some evidence that severing ties to pre-birth employer (Waldfogel), substantial period out of the labour force (Lundberg & Rose) are important sources of the family gap
- Wage gaps are highest for women in middle skill levels—inflexible working conditions? (Anderson, Binder, Krause)
- Parental leave reduces family gap by allowing women to maintain ties to employer

Incentive effects of parental leave:



- Reduce market work by mothers of very young children
- Long-term: Increase value of employment
 - analogous to Mortensen result about UI
- Employer-provided: Increase returns to acquiring a “good” job

Policy levers in life-cycle model:



- Facilitate receipt of future returns to labour force participation
- An historical example:
 - Access to fertility control (the pill) increased women's labour force participation in the U.S. after 1970 (Bailey), as well as higher education and career entry (Goldin & Katz)

Family



- For many, labour force participation is part of joint decisions about specialization and exchange in a long-term relationship with a spouse/partner
- Policy effects will depend on, and potentially change, within-family economic arrangements

Traditional gender specialization depends on the existence of a long-term contract



- Specialization in home production limits outside options
- Couples have limited ability to enter into binding intertemporal contracts

Without lifetime marriage, home partner is at a strategic disadvantage



- If relationship ends, and even if it does not
- Incentive to engage in strategic investments prior to union
 - education (Konrad & Lommerud)
 - household production skills (Vaage)

Does individual control over income/resources affect intrahousehold allocation?



- Substantial evidence from developing countries that resources controlled by women increase wellbeing of women and children
- Weaker evidence from wealthy countries
 - difficult to find measures of individual bargaining power that are exogenous

Does empowering women increase their market participation?



- Contradictory evidence for U.S.
 - Chiappori, Fortin, & LaCroix
 - Gray
- But marital uncertainty does

Retirement in a family context



- Strong evidence that married couples tend to retire together
- Motives?
 - complementary leisure
 - Gustman & Steinmeier suggest a strategic element
- Aging couples may have divergent interests regarding labour supply, consumption

Does retirement reduce individual bargaining power?



- Discrete drop in potential earnings
- Source of the retirement consumption puzzle? (Lundberg, Startz, & Stillman, 2003)
- Contrary evidence for New Zealand (Gibson, Le, & Scobie, 2004)
 - importance of policy



Is family behavior efficient?

- Requires ability to make binding contracts and complete information
- U.S. Retirement Equity Act of 1984
- Response suggests non-unitary households and inefficiency

Equilibrium considerations for policies that affect labour force participation



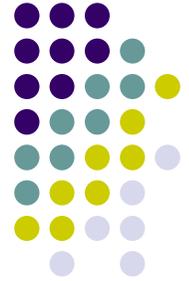
- Micro-estimates of labour supply responses to net wages, childcare prices, may not be reliable guides to policy responses
- Heckman and others: education subsidies will change wage structure
- Labour supply changes will lead to new labour market equilibrium



Other market responses:

- Price and availability of market substitutes for household goods and services
- Residential, leisure options for the retired

Political responses—labour market changes create new constituencies for:



- Immigration
- Taxation
- Parental leave
- Pensions

Social externalities: What other people are doing matters



- Rapid decline in U.S. modal retirement age from 65 to 62
 - Axtell and Epstein (2001)
 - Jenkins and Osberg (2004)
- TV and labour supply (Corneo, 2001)
- Decline in marriage/fertility rates in Spain, Italy, Japan (Sevilla-Sanz, 2004)

Family structure is endogenous



- Most studies estimate labour supply responses of individuals within a particular household arrangement
- Partnering, as well as fertility, will respond to changes in labour force participation
- Marriage tends to be increasing in men's economic opportunities, decreasing in women's



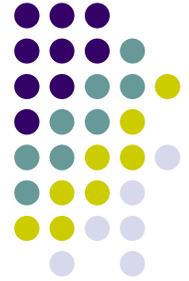
Akerlof, Yellen, and Katz

- Increases in contraception, abortion availability in 1970s in U.S. reduced “shotgun” marriages
- Changing beliefs about preferences, resources of pregnant partners who chose to bear children
- Change in equilibrium family structure

Classic economic policy dilemma:



- If women become more able to support themselves and their children, more of them will end up doing it, *ceteris paribus*
- Predicting changes in distribution of outcomes requires more than a partial equilibrium approach



Bottom line:

- Any policy designed to affect labour force participation will have:
 - secondary effects on household composition
 - life-cycle impacts on fertility and the human capital acquisition of the affected and subsequent generations
- Any direct impacts on growth will be dominated by the indirect effects

“Because there is an upper bound on the level of labour utilisation, in the long-term it will be growth in labour productivity that will ultimately determine New Zealand’s future real income and its ability to climb back up the international ladder.”



John Whitehead
Secretary to the Treasury

***New Zealand’s Economic Growth:
A Near and A Far View***

Paper presented to the New Zealand Association of
Economists’ Annual Conference
30 June 2004

