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The Insurance Role of Household Labor Supply for Older Workers

Yanan Li and Victoria Prowse *

Previous studies have documented the patterns of employment, wages, unemployment, and other labor market outcomes over the life-cycle (see, e.g., Maestas and Zissimopoulos, 2010). Older workers are generally found to have less favorable labor market outcomes than their younger counterparts. Among other age-based inequalities, the older workers are subject to greater employment risk than younger workers. In particular, while layoffs and displacements are not strongly age-related (see Farber et al., 1993), the earnings loss associated with displacement increases with age (Rodriguez and Zavodny, 2002; Farber, 2005; Couch et al., 2009). Further, older workers experience longer post-job-loss unemployment spells than their younger counterparts (Chan and Stevens, 2001). The welfare and policy implications of the relatively high level of employment risk experienced by the older population depend critically on the extent to which older households are able to use either public or intrahousehold insurance instruments to *ex post* insure against job loss and the associated subsequent unemployment spell.

Critically, a couple household may be able to adjust the secondary earner's labor supply to cushion the impact of the primary worker's job loss. While not focused specifically on older workers, an existing literature provides empirical evidence on the insurance function of the secondary earner's labor supply. In particular, several studies document an 'added worker effect,' whereby the labor supply of the secondary earner, typically the wife, increases when the primary earner is subject to an earnings shock or an employment shock (see, for example, Mincer, 1962; Heckman and MaCurdy, 1980; Lundberg, 1985; Spletzer,

* **Yanan Li** is a PhD candidate at Cornell University. **Victoria Prowse** is an assistant economics professor at Cornell University. This Research Brief is based on MRRC Working Paper 2013-309.

1997; Cullen and Gruber, 2000).** Stephens Jr (2002) takes a longer-term perspective and shows that a husband's job displacement leads to a prolonged increase in his wife's expected earnings and likelihood of employment. More recently, Blundell et al. (2012) demonstrate a consumption-smoothing role for household labor supply.

Given the relative severity of employment risk for older workers, it is important to know if spousal labor supply provides an insurance channel for older households, or whether instead the aggregate added worker effects reported previously pertain only to younger households. Taking this as motivation, in this paper we explore and compare how older and younger couple households use adjustments in the wife's labor supply to mitigate the effects of negative employment shocks. Beyond the disaggregation according to age, we extend existing work in two further respects. First, in addition to looking at the wife's employment response, we distinguish between unemployment and nonparticipation. By looking at how the likelihood of the wife being unemployed changes following her husband's employment shock, we gain insight into the extent that wives are constrained in their responses to their husbands' employment shocks. Combining with the age-based analysis, we compare the different extents that older and younger households are constrained by the labor market in their use of the wife's labor supply to smooth the impact of the husband's employment shocks. Second, in contrast to previous work using measures of annual labor supply, we use monthly information on husbands' and wives' labor market outcomes. By doing so, we are able to examine the household labor supply response in the months immediately after the husband's negative employment shock. This analysis informs on the time required before any smoothing effect of the wife's labor supply appears, and on the time that the effect persists.

Our empirical analysis uses difference-in-differences matching methods, applied to a sample of couple households drawn from the 2003-2011 waves of the Panel Study of Income Dynamics. Focusing on negative employment shocks impacting on men, we estimate the effect of an employment shock on a man's own labor market outcomes and on his wife's labor market outcomes. We find a substantial added worker effect for younger households. However, the wives of older men do not increase employment in response to their husbands' negative employment shocks. Instead, in older households, female unemployment increases and nonparticipation decreases. The latter results are consistent with older women being constrained by the labor market in the extent to which they can adjust their labor supply to mitigate the effects of spousal employment shocks. In a further round of analysis, we investigate how wives' adjustment in employment behavior impacts on household non-work, defined as the situation where neither spouse is in employment. For younger households we find that less than half of the added worker effect is located in households in which the husband is not in employment, suggesting that the smoothing or insurance role of wives' labor supply is more limited than that suggested by the added worker effect in isolation. For older households, we see neither an added worker effect overall nor an added worker effect within households in which the husband is slow in returning to employment.

*** Meanwhile, Layard et al. (1980) and Maloney (1987) find no evidence of an added worker effect.*

University of Michigan Retirement Research Center
Institute for Social Research 426 Thompson Street Room 3026
Ann Arbor, MI 48104-2321 Phone: (734) 615-0422 Fax: (734) 615-2180
mrrcumich@umich.edu www.mrrc.isr.umich.edu

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