Latent Work Capacity and Retirement Expectations

Italo Lopez Garcia, Nicole Maestas, and Kathleen J. Mullen[*]

The United States' population is aging rapidly. The share of individuals ages 65 and older is projected to reach 16.9% in 2020 and 20.6% by 2030 (U.S. Census Bureau 2018). As a consequence, labor force growth has slowed, and the long-run fiscal health of Social Security and Medicare has eroded. One policy response is to encourage older individuals to delay retirement and work longer, for example by raising eligibility ages for claiming Social Security and Medicare benefits. However, whether or not older individuals could work longer or would want to work longer is still an open question. On one hand, age-related health deterioration has been found to be an important driver of early retirement, especially among individuals with physically demanding jobs, and to be an important limiting factor of job mobility. On the other hand, recent studies show that there is significant excess work capacity among today's older Americans relative to earlier cohorts.

In this paper, we make progress in addressing this question by developing a new measure of work capacity that stems from comparing individuals' functional abilities with functional requirements of occupations, both measured in the same way, and deducing which occupations the individual could likely perform. To create such a data set, we asked a nationally representative sample of Americans to rate their abilities along 52 dimensions, corresponding exactly to the 52 dimensions of ability used by the Occupational Information Network (O*NET) to rate the occupational ability requirements for nearly 800 occupations in the U.S. economy. Combining our new survey data with the O*NET database, we then determine for each respondent their occupation-specific work capacity—that is, whether they likely can or cannot perform a given occupation—by comparing their reported levels of functional ability to those required by each occupation. Once we determine an individual's set of potential occupations — conditional on their education — we define total work capacity as the share of the national economy's occupations an individual can do given their educational level.

We construct two alternative versions of work capacity, one more conservative and one more generous, and we use

them to test whether the set of potential jobs available to an individual for a given educational level can predict current and future labor force participation decisions by testing whether work capacity adds explanatory power to models of employment, disability benefit receipt, future retirement intentions, and future return-to-work intentions among those not in the labor force.

Our results can be summarized in three findings. First, we find that average abilities, overall and across different domains, are high relative to average occupational demands. Second, age-related declines in abilities are modest. Putting these elements together, individuals' work capacity is relatively stable with age. Third, our measures of work capacity are predictive of current labor supply outcomes. An increase in work capacity from being unable to do any job to being able to do all jobs given the individual's educational level is significantly associated with a 15 to 21 percentage point increase in labor force participation and a 10 to 17 percentage point decrease in the percentage of recipients of Social Security disability benefits. Work capacity is also predictive of subjective expectations about future labor force participation decisions. An increase in an individual's work capacity from being unable to do any job to being able to do all jobs given the educational level is associated with a 7 to 10 percentage point increase in the chance that current workers will work past age 65 or 70 (depending on the individual's age), a 9 to 12 percentage point increase in the chance that retired individuals will return to the labor force, and a 17 to 25 percentage point increase in the chance that individuals with disabilities will return to the labor force.

Finally, since these associations are significant over and above the associations between outcomes and health and are all economically relevant, we conclude that a measure of work capacity based on the (mis)match between a comprehensive set of abilities and job demands can increase understanding of labor force outcomes at older ages and inform the design of policies that would incentivize or even require individuals to extend their working lives. ❖