### University of Texas at Austin

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# Fall 1994

RCONOMICS 385K

D. Hamermesh

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#### Introduction to Labor Sconomics-I

1. This course is designed to enable you to understand what analytical labor economics is about and how it can be applied to answer questions of interest about the labor market and public policy related to it. In particular, the course covers labor supply and the household, human capital, labor demand, migration and compensating wage differentials, and the economics of trade unions. other topics in the field are discussed in the continuation course in Spring. Since labor economics today combines econometric analysis with theory, you must ar least understand multivariate regression to benefit from the discussion of the empirical work on this list. If you do not, or if you are stale, please refresh your memory by going over Kmenta, <u>Elements of Econometrics</u>, or Johnston,

2. There is no textbook for the course. However, if you have not had an undergraduate course in analytical labor economics, you should read the sppropriate chapters (in parentheses next to the section headings below) in D. Hamermeeh and A. Rees, <u>Economics of Work and Pay</u>. (The chapter numbers are from the 5th edition, 1993.)

3. There will be a midterm exam, a final exam and one term paper. If you plan to take the second course in Spring 1995, Professor Oettinger and I would be happy to have you write one term paper that covers both courses. This should give you time to do a more extensive and original piece of work. In any case, the most desirable term paper will be a small, but original theoretical or empirical study. An empirical paper could, for example, replicate a study in the literature using a different set of data. (You should note that the new journal, Tabour Economics, has a section for replication studies; and other journals too encourage their submission.) Alternatively, but only if you wish the paper to apply to this course alone, the term paper could be an assessment of the current state of our knowledge about a particular area of labor economics, or of labormarket policy, that is covered in this course. The assessment should stress the relation between theory and empirical work; it should be current; the topic should be fairly narrowly defined; and it should be a constructive criticism, not merely a summary. Whichever type of paper you choose to do, if you are doing it for this course alone, it should be turned in by Monday, December 19.

4. Everything on the reading list is required. Bibliographical material can be found in the articles, especially those from the <u>Handbook of Labor Economics</u>. Thave tried to construct a list that is short enough to be read by everyone, but that still covers most of the important material. Some of the readings are at this point at least as much of historical as of current interest. These are marked with an "H." Each student will be assigned one (empirical) reading for presentation to the class.

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#### READING LIST

- 1. LABOR SUPPLY AND THE HOUSEHOLD (1, 2) -- 4 weeks
- A. Background and Static Theory

John Pencavel, <u>Handbook</u>, pp. 3-26.

Mark Killingsworth and James Heckman, <u>Handbook</u>, pp. 103-124.

Jacob Mincer, "Labor Force Participation of Married Women," in NBER, <u>Aspects</u> of Labor Economics, 1962. (H)

Gary Becker, "A Theory of the Allocation of Time," Economic Journal, 1965.

Angus Deaton and John Muellbauer, <u>Economics and Consumer Behavior</u>, pp. 86-97, 273-294.

Pencavel, <u>Handbook</u>, pp. 27-44.

Killingsworth-Heckman, Handbook, pp. 125-144.

B. Static Empirical Studies

James Heckman, "Shadow Prices, Market Wages, and Labor Supply," <u>Econometrica</u>, 1974.

Rebecca Blank, "Simultaneously Modeling the Supply of Weeks and Hours of Work among Pemale Household Heads," <u>Journal of Labor Economics</u>, 1988.

C. Dynamic Models

Pencavel, <u>Handbook</u>, pp. 45-50.

Thomas MaCurdy, "An Empirical Model of Labor Supply in a Life-Cycle Setting," Journal of Political Economy, 1981.

Martin Browning, Angus Deaton and Margaret Irish, "A Profitable Approach to Labor Supply and Commodity Demands over the Life Cycle," <u>Econometrica</u>, 1985.

D The Household

Reuben Gronau, Handbook.

Gary Becker, "A Theory of Social Interactions," <u>Journal of Political Economy</u>, 1974.

Marjorie McElroy and Mary Jean Horney, "Nash-Bargained Household Decisions: Toward a Generalization of the Theory of Demand," <u>International Economic</u> <u>Review</u>, 1981.

Shelly Lundberg and Robert Pollak, "Separate Spheres Bargaining and the Marriage Market," Journal of Political Economy, 1993.

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H. Elizabeth Peters, "Marriage and Divorce: Informational Constraints and private Contracting," <u>American Economic Raview</u>, 1986.

William Johnson and Jonathan Skinner, "Labor Supply and Marital Separation," American Economic Review, 1986.

Peter Kooreman and Arie Kapteyn, "A Disaggregated Analysis of the Allocation of Time within the Household," <u>Journal of Political Economy</u>, 1987.

Shelly Lundberg, "Labor Supply of Husbands and Wives," <u>Review of Economics</u> and <u>Statistics</u>, 1988.

g, Policy Analyses

Michael Keeley <u>et al</u>, "The Estimation of Labor Supply Models Using Experimental Data," <u>American Economic Review</u>, 1978.

Jerry Hausman, "Taxes and Labor Supply," in Handbook of Public Economics.

John Graham and Andrea Beller, "The Effect of Child Support Payments on the Labor Supply of Female Family Heads," <u>Journal of Human Resources</u>, 1989.

Alan Krueger and Jörn-Steffen Pischke, "The Effect of Social Security on Labor Supply: A Cohort Analysis of the Notch Generation," <u>Journal of Labor</u> Economics, 1992.

# II. Human Capital -- Education OJT and Occupational Choice (3) (2 weeks)

A. Background and Theory

Gary Becker, Human Capital, Chapters 3 and 4 (1993 edition). (H)

Yoram Weiss, <u>Handbook</u>, pp. 603-629.

Michael Spence, "Job Market Signalling," Quarterly Journal of Economics, 1973.

Gary Zarkin, "Occupational Choice: An Application to the Market for Public School Teachers," Quarterly Journal of Economics, 1985.

### B. Estimation and Policy Issues

Zvi Griliches, "Estimating the Returns to Schooling: Some Econometric Problems," <u>Econometrica</u>, 1977.

Orley Ashenfelter and Alan Krueger, "Estimates of the Economic Return to Schooling from a New Sample of Twins," Princeton University, Working Paper, 1992.

Stephen Cameron and James Heckman, "The Nonequivalence of High School Equivalents," <u>Journal of Labor Economics</u>, 1993.

John Bound and George Johnson, "Changes in the Structure of Wages in the 1980s," American Economic Review, 1992.

David Card and Alan Krueger, "Does School Quality Matter?" Journal of Political Economy, 1992.

Joshua Angrist and Alan Krueger, "Does Compulsory School Attendance Affect Schooling and Earnings?" <u>Ouarterly Journal of Economics</u>, 1991.

- III. Labor Demand (4, 5) -- 3 weeks
- A. Background and Static Theory

Paul Douglas, "The Cobb-Douglas Production Function Once Again: Its History, Testing and Some Empirical Values," <u>Journal of Political Economy</u>, 1976. (H)

Daniel Hamermesh, Labor Demand, Chapter 2.

B. Static Empirical Studies

Hamermesh, Handbook, pp. 447-471.

Stephen Nickell and Jim Symons, "The Real Wage-Employment Relationship in the United States," Journal of Labor Economics, 1990.

George Borjas, "The Demographic Determinants of the Demand for Black Labor," in Freeman and Holzer, <u>The Black Youth Employment Crisis</u>, 1986.

C. Dynamic Models

Walter Oi, "Labor as a Quasi-fixed Factor," <u>Journal of Political Economy</u>, 1962. (H)

Hamermesh, Labor Demand, Chapter 6.

Sherwin Rosen, "Short-Run Employment Variation on Class-I Railroads in the U.S., 1947-1963, <u>Econometrica</u>, 1968.

Daniel Hamermesh, "Labor Demand and the Structure of Adjustment Costs," American Economic Review, 1989.

Daniel Hamermesh <u>et al</u>, "New Facts about Factor-Demand Dynamics," NBER Working Paper, 1994.

D. Policy Analyses

Charles Brown <u>et al</u>, "The Effect of the Minimum Wage on Employment and Unemployment," Journal of Economic Literature, 1982.

Ronald Ehrenberg and Paul Schumann, Longer Hours or More Jobs, Chapter 2.

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Gary Burtless, "Are Targeted Wage Subsidies Harmful? Evidence from a Wage Youcher Experiment," <u>Industrial and Labor Relations Review</u>, 1985.

Patricia Anderson, "Linear Adjustment Costs and Seasonal Labor Demand: Rvidence from Retail Trade Firms," <u>Quarterly Journal of Economics</u>, 1993.

IV. Migration and Compensating Differentials (7, 13) -- 2 weeks

A. Migration

George Borjas, "Self-Selection and the Sarnings of Immigrants," <u>American</u> Economic Review, 1987.

Barry Chiswick, "The Effect of Americanization on the Earnings of Foreignborn Men," <u>Journal of Political Economy</u>, 1978.

Jacob Mincer, "Family Migration Decisions," <u>Journal of Political Economy</u>, 1978.

George Borjas, "What Happened to Immigrants' Skills in the 1980s?" Unpublished paper, University of California--San Diego, 1993.

David Card, "The Impact of the Mariel Boatlift on the Miami Labor Market," Industrial and Labor Relations Review, 1990.

8. Compensating Differentials

Sherwin Rosen, <u>Handbook</u>.

Shulamit Kahn, "Occupational Safety and Worker Preferences: Is There a Marginal Worker?" <u>Review of Economics and Statistics</u>, 1987.

Hae-shin Hwang <u>et al</u>, "Compensating Wage Differentials and Unobserved Productivity," <u>Journal of Political Economy</u>, 1992.

Stephen Trejo, "The Effects of Overtime Pay Regulation on Worker Compensation," <u>American Economic Review</u>, 1991.

Glenn Blomquist, Mark Berger and John Hoehn, "New Estimates of Quality of Life in Urban Areas," <u>American Economic Review</u>, 1988.

V. Unions (10, 11, 12) -- 3 weeks

A. Background

Richard Freeman and James Medoff, What Do Unions Do? 1984, Chapters 1, 2.

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B. Growth and Goals

Henry Farber, <u>Handbook</u>.

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Henry Farber, "The Determination of the Union Status of Workers," <u>Econometrica</u>, 1983.

James Brown and Orley Ashenfelter, "Testing the Efficiency of Employment Contracts," Journal of Political Economy, 1986.

Stephen Bronars and Donald Deere, "The Threat of Unionization, the Use of Debt and the Preservation of Shareholder Wealth," <u>Ouarterly Journal of</u> <u>Economics</u>, 1991.

Robert Planagan, "Compliance and Enforcement Decisions under the NLRA" Journal of Labor Economics, 1989.

#### C. Methods

John Kennan, Handbook, pp. 1091-1112.

Joseph Tracy, "An Empirical Test of an Asymmetric Information Model of Strikes," Journal of Labor Economics, 1987.

Harry Paarsch, "Work Stoppages and the Theory of the Offset Factor," <u>Journal</u> of Labor Economics, 1990.

Orley Ashenfelter and David Bloom, "Models of Arbitrator Behavior," American Economic Review, 1984.

Morley Gunderson and Angelo Melino, "The Effect of Public Policy on Strike Duration," <u>Journal of Labor Economics</u>, 1990.

#### D. Effects

H. Gregg Lewis, <u>Handbook</u>.

Kim Clark, "Unionization and Firm Performance," <u>American Economic Review</u>, 1984.

William Boal and John Pencavel, "The Effects of Labor Unions on Employment Wages and Days of Operation," <u>Ouarterly Journal of Economics</u>, 1994.

Richard Freeman, "The Exit-Voice Tradeoff in the Labor Market," <u>Ouarterly</u> Journal of Economics, 1980.

John Pencavel, Labor Markets under Trade Unionism, Chapter 2.

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### ECONOMICS 385K FINAL EXAM, Fall 1994

### D. Hamermesh

You have 2-1/2 hours for this exam. Please answer all the questions using your blue book.

L (30 minutes)

A recent country song, "He Thinks He'll Keep Her," describes a woman who was married at age 21, had her third child at age 29, made sure that everything in her house was "polished 'til it shined," divorced her husband at age 36, then spent 15 years "in the typing pool without a raise in pay." Discuss this scenario in terms of life-cycle models, household production and investment in human capital.

IL (30 minutes)

The new Republican majority in Congress has proposed a flat tax at 17 percent applying to all income, as opposed to the current tax structure that taxes income progressively at rates of 15, 28, 31, 36 and 39 percent.

A Discuss how you would use currently available data to estimate the likely effects of this change on labor supply. Base your discussion on the appropriate theory and measurement technique.

B. What does current evidence suggest that the effects of this change would be on the labor supply of workers at different hourly wage rates?

III. (20 minutes)

A common finding in equations like:

 $\mathbf{E}_{1} = \lambda \mathbf{E}_{11} + \alpha \mathbf{X}_{1},$ 

where E is employment, X is a vector of variables that shock equilibrium employment,  $\alpha$  and  $\lambda$  are parameters,  $\lambda < 1$ , is that  $\lambda$  is larger when shocks are positive than when they are negative.

What does the estimated value of  $\lambda$  imply about the underlying structure of costs facing the typical firm? What does the difference between values of  $\lambda$  in response to positive and negative shocks imply about those costs? What policies might affect the values of  $\lambda$ that we observe, and in what directions and why?

## IV. (20 minutes)

Endogenous selectivity has been mentioned as a severe problem confounding attempts  $t_1$  estimate a variety of effects in the labor market. Pick one such example and explain how selectivity affects the outcomes. Stress the economics of the selectivity problem, not the econometric issues involved.

### V. (40 minutes)

As part of its research into the relationship between a worker's appearance and his/her wage rate a study published in the December 1994 <u>American Economic Review</u> estimated the following relationships between each of a number of variables and the logarithm of the hourly wage for a sample of male American workers in 1977:

### Variable

## Coefficient

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School:	12 years	.06
	13-15 years	.07
1 a	16+ years	.25
(<12 years is the excluded category)		
Experience (	years)	.0288
Experience <sup>2</sup>	,	00052
Years of ten	ure: 1-3 years	.135
	3-10 years	.149
	11+ years	.199
(<1 year is the excluded category)		
Married		.083
Firm size:	10-499 workers	.083
10	500-999 workers	.115
	1000 + workers	.204
(<10 workers is the excluded category)		
Union member		.162
Work in:	Large metropolitan area	.231
	Small metropolitan area	.124
(Nonmetropolitan location is the excluded category)		

For each coefficient or group of coefficients: 1) Justify the pattern or sign in terms of some underlying theory; 2) Discuss whether the size of the coefficient (or group of coefficients) is in accord with what the theory would lead you to expect.