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Labor economics redux

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Program Report

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Labor Economics Redux

Richard B. Freeman*

Labor economics has increased the number of tools it uses to analyze people's behavior in market settings by augmenting econometrics and models of rational behavior with increased analyses of field or laboratory experiments. This widening, and a greater focus on the ways economic institutions affect outcomes, as opposed to how hypothetical rational actors behave in ideal competitive settings, has helped the field to become an increasingly important and growing contributor to economic research. This growth is evidenced in the massive increase in the number of NBER Working Papers produced in the Labor Studies Program. In 1979, the Program published ten working papers over the entire year. In a single month in 2007 (February), the Program produced 18 working papers, making it the single largest producer of Working Papers among all NBER programs, as it was in 2006 when the program published 176 Working Papers. Once upon a time, I read all of the papers, but this has become a near impossibility. Moreover, labor specialists have spawned additional programs at the NBER — Education, Children, Aging — and smaller groups of labor researchers are working on particular topics, including personnel economics, shared capitalism, the science and engineering work force, immigration, and the economics of the welfare state in Sweden.

One reason for the growth in the NBER's Labor Studies Program has been the increased attention given to labor issues in economic debate. One of the great economic issues of our time relates to the differing economic performance of capitalist economies. In the 1980s many researchers sought to understand the great success of Japan. From the 1990s to the present, many analysts have sought to explain the difference between European

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Union and U.S. economic performance in terms of the more market-oriented labor institutions and weaker welfare state in the United States. Seeking to explain why some firms or establishments do better than others, other analysts have looked at differences in incentives and work practices. In international trade, the most contentious issue relates to how trade affects workers, including the likelihood and costs of displacement, the role of off-shoring in reducing demand for skilled as well as unskilled labor, and the impact of trade on earnings inequality.

The concern over rising inequality has generated a huge labor literature in which NBER researchers have played a significant role as they seek to document the effect of institutions, technology, and/or trade in the growth of inequality in wages and hours worked in the United States. In addition, there is always interest in such perennial labor topics as the minimum wage, unions, female labor force participation, immigration, discrimination, and crime. Indicative of the standing of labor in economics is that, at this writing, the head of the President's Council of Economics Advisers, Ed Lazear, is a longstanding Research Associate in the Program (author of 10 percent of the 1979 crop of Working Papers). The field must be doing something right!

One of the things that the labor field is definitely doing right is widening the range of topics covered. When the leading Australian economist, Bob Gregory, visited NBER in the 1980s, he remarked that American labor economists were narrower in their research topics than Australian labor economists. Why? It was the economics of specialization in a large market. The United States had so many labor economists that we invariably ended up specializing to a greater extent than labor economists in Australia, where a small band had to cover the whole field and, in some cases, work on trade, monetary policy, and natural resource economics as well. Breadth over depth, as it were.

But over time the topics that have attracted NBER labor research have widened and widened. Consider, for example, some of the subjects of labor Working Papers in January and February 2007: happiness and well-being¹; peer effects in juvenile corrections and attack assignments in terror organizations²; interpersonal styles and labor outcomes; the production of female artists³. This isn't your thesis advisor's or thesis advisor's advisor's set of labor topics. The idea that practitioners of the dismal science would have anything to contribute on happiness

seems almost an oxymoron, but in fact we do. And artists? Why, the next thing you know labor economists will be studying the economics of wine!⁴

Research on more traditional labor topics, such as unemployment benefits, job training, human capital investments, geographic mobility, and the like, also shows an expanding arc beyond what would have been treated a decade or so earlier. The youth training paper in February 2007 is about a program in the Dominican Republic; the human capital paper is about the effect of Indian Tariff reform on investment in skills; the mobility paper focuses on optimal migration in the world.⁵ Five of the 13 working papers published in March 2007 were focused on evidence from other countries.⁶ What had once been a field that devoted itself almost exclusively to U.S. evidence has become global, looking for natural experiments, variation in institutions and regulations across the world to draw inferences about economic behavior.⁷

Gregory may still be right that individual researchers in Labor Studies are more hedgehogs than foxes, per Isaiah Berlin's famous essay "The Hedgehog and the Fox" ("The fox knows many things, but the hedgehog knows one big thing.") but as a collective, NBER labor studies cover many things and many datasets and labor behavior and outcomes in many countries.

Another important development in labor and economics more broadly is that research has become increasingly collaborative, involving researchers across different countries. The trend for increased numbers of authors per working paper, noted in my 2002 review of the program, has continued. In January-February 2007, there were five single-authored papers, 18 double-authored papers, 10 triple-authored papers, and one paper with five authors. The authors cover people working in many different countries, as well. Some of this occurs because NBER research affiliates and fellows working on data from foreign countries collaborate with nationals of those countries; in other cases, it is U.S. data and topics that attract the interest of graduate students and researchers from other countries. The

open source policy that covers many U.S. datasets, some of which the NBER makes available on its web site, naturally inspires some research around the world.

Finally, as labor studies has grown in its coverage of issues, it has become less clear who is "labor" and who is not. There is a substantial overlap of Labor Studies Working Papers with those in public economics, and a growing pattern in which labor researchers collaborate with specialists in other fields to examine topics of interest.

Tools and Findings

One of the important additions to the tool kit of economists has been experimental economics—the use of laboratory experiments that have traditionally been the meat and potatoes of psychology for testing diverse forms of economic behavior. Labor studies has become a home for experimental economics, both field experiments and laboratory experiments.⁸ At virtually every Labor Studies program meeting or summer workshop, there are papers using experimental laboratory techniques to analyze behavior. This adds to the attention that labor has long given to field experiments, in which policymakers and/or researchers use random assignment and differential incentives or program designs to help assess behavior and to determine the most effective program interventions. While labor is empirical to its core, it has close ties to econometrics and has played a major role in using such techniques as difference-in-differences (comparing changes in one group subject to some new incentive to changes in a control group), instrumental variables analyses that seek to isolate the effect of the hopefully truly exogenous part of the variation in an explanatory variable on some behavior.

The pudding is the research findings. What do we now know that we didn't know five or so years ago when I last reviewed the status of labor studies? We know more about the complexities of supply responses to incentives in diverse areas. Yes, incentives matter, but studies have found that their impact can vary between groups, depend on peer effects

and on diverse behavioral issues that the simplest models of rational optimization miss. We know more about the determinants of inequality, though we also know more about how difficult it is to pin down the causes and effects of the rise in inequality in the United States. We know more about how institutions behave, though there clearly remains much more to be learned through the combination of cross-country analyses, case investigations, econometrics, and the whole panoply of tools that we have come to rely on to attack problems.

If the trends in research continue, I expect to see further use of laboratory experiments to help answer labor questions, the development of sufficient numbers of studies across countries to allow us to pin down the universals in economic behavior, and the specifics associated with particular incentives and structures. As globalization proceeds, the economic impact of female workers keeps growing, and innovation and productivity continue to play major roles in economic progress, I expect to see much greater understanding of the labor markets in developing countries, more about how gender affects economic behavior, and more about the impact of incentives and institutions on creativity and innovation, as well as on the more traditional employment and hours measures of labor.

¹ D.G. Blanchflower and A. J. Oswald, "Is Well-being U-Shaped over the Life Cycle?" NBER Working Paper No. 12935, February 2007, and "Hypertension and Happiness across Nations," NBER Working Paper No. 12934, February 2007.

² P. Bayer, R. Hjalmarsson, and D. Pozen, "Building Criminal Capital behind Bars: Peer Effects in Juvenile Corrections," NBER Working Paper No. 12932, February 2007, and E. Benmelech and C. Berrebi, "Attack Assignments in Terror Organizations and the Productivity of Suicide Bombers," NBER Working Paper No. 12910, February 2007.

³ D. W. Galenson, "Who Were the Greatest Women Artists of the Twentieth Century? A Quantitative Investigation," NBER Working Paper No. 12928,

February 2007.

⁴ Indeed, one of the earliest members of the Labor Studies Program, Orley Ashenfelter, has specialized in the economics of the wine industry. See for example, O. Ashenfelter and K. Storchmann, "Using a Hedonic Model of Solar Radiation to Assess the Economic Effect of Climate Change: The Case of Mosel Valley Vineyards," NBER Working Paper No. 12380, July 2006.

⁵ E. V. Edmonds, N. Pavcnik, and P. Topalova, "Trade Adjustment and Human Capital Investments: Evidence from Indian Tariff Reform," NBER Working Paper No. 12884, February 2007; D.A. Card, P. Ibarrraran, F. Regalia, D. Rosas, and Y. Soares, "The Labor Market Impacts of Youth Training in the Dominican Republic: Evidence from a Randomized Evaluation," NBER Working Paper No. 12883, February 2007; and J. Benhabib and B. Jovanovic, "Optimal Migration: A World Perspective," NBER Working Paper No. 12871, January 2007.

⁶ A. Bjorklund, M. Jantti, and G. Solon, "Nature and Nurture in the Intergenerational Transmission of Socioeconomic Status: Evidence from Swedish Children and Their Biological and Rearing Parents," NBER Working Paper No. 12985, March 2007; M. Muendler, "Trade and Workforce Changeover in Brazil," NBER Working Paper No. 12980, March 2007; M. Diaye, N. Greenan, and M. Urdanivia,

"Subjective Evaluation of Performance Through Individual Evaluation Interview: Empirical Evidence from France," NBER Working Paper No. 12979, March 2007; T. Lallemand, R. Plasman, and F. Rycx, "Wage Structure and Firm Productivity in Belgium," NBER Working Paper No. 12978, March 2007; and A. Hunnes, J. Møoen, and K.G. Salvanes, "Wage Structure and Labor Mobility in Norway 1980–97," NBER Working Paper No. 12974, March 2007.

⁷ R. B. Freeman "Learning from Other Economies: The Unique Institutional and Policy Experiments Down Under," NBER Working Paper No. 12116, March 2006.

⁸ These include studies by specialists in experimental economics, who have joined the program: M. Niederle, "Competitive Wages in a Match with Ordered Contracts," NBER Working Paper No. 12334, June 2006; M. Niederle and L. Vesterlund, "Do Women Shy Away From Competition? Do Men Compete Too Much?" NBER Working Paper No. 11474, July 2005; C. N. McKinney, M. Niederle, and A. E. Roth, "The Collapse of a Medical Clearinghouse (and Why Such Failures Are Rare)," NBER Working Paper No. 9467, February 2003; and M. Niederle and A. E. Roth, "Unraveling Reduces the Scope of an Entry Level Labor Market: Gastroenterology With and Without a Centralized Match," NBER Working Paper No. 8616, December 2001.

But the experimental analysis has

come to be used by diverse labor specialists: J. R. Kling, "Methodological Frontiers of Public Finance Field Experiments," NBER Working Paper No. 12931, February 2007; J. Angrist, D. Lang, and P. Oreopoulos, "Lead Them to Water and Pay Them to Drink: An Experiment with Services and Incentives for College Achievement," NBER Working Paper No. 12790, December 2006; D.A. Card and D. R. Hyslop, "The Dynamic Effects of an Earnings Subsidy for Long-Term Welfare Recipients: Evidence from the SSP Applicant Experiment," NBER Working Paper No. 12774, December 2006; R. B. Freeman and A. M. Gelber, "Optimal Inequality/Optimal Incentives: Evidence from a Tournament," NBER Working Paper No. 12588, October 2006; E. Field, "Educational Debt Burden and Career Choice: Evidence from a Financial Aid Experiment at NYU Law School," NBER Working Paper No. 12282, June 2006; U. Gneezy and J. A. List, "Putting Behavioral Economics to Work: Testing for Gift Exchange in Labor Markets Using Field Experiments," NBER Working Paper No. 12063, March 2006; M. Bertrand, D. Karlin, S. Mullainathan, E. Shafir, and J. Zinman, "What's Psychology Worth? A Field Experiment in the Consumer Credit Market," NBER Working Paper No. 11892, December 2005; J. R. Kling, J. B. Liebman, and L. F. Katz, "Experimental Analysis of Neighborhood Effects," NBER Working Paper No. 11577, August 2005.