

## Labor Economics I Fall 2002

### Instructor:

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### Office Hours:

Tuesday, 4:30-6, or by appointment.

### Course Web Page:

<http://www.nyu.edu/econ/user/flinn/courses/labor02/labor02.htm>

### Course Objectives:

The objective of the course is to acquaint students with modern topics, modeling strategies, econometric methods, and empirical work in the field of labor economics. In this first semester of the two-semester sequence in labor economics, we will cover topics in the analysis of labor market dynamics [(unemployed) search and informational models of turnover], models of the employment relationship in the presence of moral hazard, labor supply in both static and dynamic contexts, alternative models of wage determination, and bargaining models of household behavior. For each of the topics covered we will begin by presenting some of the relevant theoretical models that have been developed. We will then turn our attention to issues of model specification and estimation given the type of data typically available to labor economists. We intend to spend roughly equal amounts of time on theoretical and empirical issues.

### Prerequisites:

One year of microeconomic theory and Econometrics II or its equivalent.

### Requirements and Grading:

There will be two examinations in the course, a midterm and a final. The midterm exam will be a take-home which students will have approximately one week to complete and the final will be given during the final examination period. Both examinations will ask the student to apply what they have learned in class to the modeling of labor market phenomena, as well as to synthesize and/or critique the theoretical and econometric models which are presented in the lectures and/or the required readings. The examinations will have equal weight in the determination of the student's final grade.

In addition students will be asked to give a report on one or more of the assigned readings in class [the readings will be selected by the student after consulting with me]. The reports will consist of a summarization of the basic argument of the paper(s), the model and the econometric

methodology and empirical results [where appropriate]. The purpose of this exercise is to increase class participation and to familiarize students with the presentation of economic research.

Over the course of the semester three or four homework assignments will be distributed that must be completed. They will involve simulation and/or estimation of models discussed in the lectures and/or contained in the papers (I will provide the data sets when estimation is called for). I will also distribute sample programs from time to time (written in GAUSS) to illustrate estimation and simulation techniques.

**Readings:**

The items on the reading list marked with an asterisk (\*) are required readings. Copies of these will be on reserve in the C.V. Starr Center library on the third floor of 269 Mercer, and whenever possible will be available on line. Students who have difficulty finding other readings in which they are interested should contact me.

<i>Week</i>	<i>R.L. #</i>	<i>Topic</i>
<b>Labor Market Dynamics</b>		
1	1.A	<i>Course Introduction; Describing Labor Market Dynamics</i>
2	1.B	<i>Unemployed Search Theory</i>
3	1.C	<i>Econometrics of Unemployed Search</i>
4	1.D	<i>Matching, Bargaining, and Search</i>
5	1.E	<i>Job Mobility</i>
<b>Labor Supply and Household Economics</b>		
6	2.A	<i>Static Labor Supply</i>
7	2.B	<i>Life-Cycle Labor Supply</i>
8	2.C	<i>Household Bargaining and Labor Supply</i>
9	2.D	<i>Bargaining Models of Household Formation and Dissolution</i>
<b>Asymmetric Information in the Labor Market</b>		
10	3.A	<i>Signalling Models</i>
11	3.B	<i>Principal-Agent Problems in the Labor Market</i>
12	3.C	<i>Econometric Models of Moral Hazard</i>
<b>Human Capital Investment Decisions</b>		
13	4.A	<i>Human Capital Investment Decisions</i>
14	4.B	<i>Equilibrium Models of Human Capital Investment</i>

## Reading List

**Note: Selections with (\*) are required**

### 1.A. Describing Labor Market Dynamics

1. \*Burdett, K. and D. Mortensen. "Labor Supply under Uncertainty." In *Research in Labor Economics, Vol. 2* (Ehrenberg, ed.). Greenwich:CN: JAI Press, 1979.
2. \*Flinn, C. Chapter 2 of *Minimum Wages and Labor Market Outcomes: Theory and Evidence*. Downloadable from course home page.
3. \*Flinn, C. and J. Heckman. "Are Unemployment and Out of the Labor Force Behaviorally Distinct Labor Force States?" *Jour. of Labor Economics* 1 (1983): 28-42
4. Flinn, C. and J. Heckman. "Models for the Analysis of Labor Force Dynamics" in *Advances in Econometrics, vol. 1* (Basmann and Rhodes, eds.). Greenwich, CN: JAI Press, 1982.
5. Flinn, C. "Econometric Analysis of CPS-Type Unemployment Data." *J. of Human Resources* (1986)21: 456-484.
6. Toikka, R. "A Markovian Model of Labor Market Decisions by Workers." *A.E.R.* 66 (1976): 821-834.

### 1.B. Unemployed Search Theory

1. \*Burdett and Mortensen (from 1.A), continued.
2. \*Flinn (from 1.A), continued.
3. Mortensen, D. "Job Search and Labor Market Analysis." Chapter 15 in *Handbook of Labor Economics, Volume 2* (Ashenfelter and Layard, eds), Amsterdam: North-Holland, 1986..
4. Lippman, S. and J. McCall (1976b) "Job Search in a Dynamic Economy." *J. Econ. Theory* 12 (1976): 365-390.
5. Danforth, J. "On the Role of Consumption and Decreasing Absolute Risk Aversion in the Theory of Job Search." In *Studies in the Economics of Search* (Lippman and McCall, eds). Amsterdam: North-Holland, 1979.
6. \*Rothschild, M. "Searching for the Lowest Price when the Distribution of Prices is Unknown." *J. Pol. Econ.* 82 (1974): 689-711.
7. \*Salop, S. "Systematic Job Search and Unemployment." *Rev. Econ. Studies* 40 (1973): 191-201.

### 1.C. Econometrics of Unemployed Search

1. \*Flinn, C. and J. Heckman. "New Methods for Analyzing Structural Models of Labor Force Dynamics." *J. Econometrics* 18 (1982): 115-168.
2. Wolpin, K. "Estimating a Structural Search Model: The Transition from School to Work." *Econometrica* 55 (1987): 801-818
3. \*Wolpin, K. *Empirical Methods for the Study of Labor Force Dynamics*. Harwood Academic Publishers, 1995. Chs. 2,3.
4. \*Van den Berg, G. "Nonstationarity in Job Search Theory." *Rev. Econ. Studies* 57 (1990), pp. 255-277.
5. Lancaster, T. and A. Chesher. "An Econometric Analysis of Reservation Wages." *Econometrica* 51 (1983), pp. 1661-1676.

### 1.D. Matching, Bargaining, and Search

1. Pissarides, C. *Equilibrium Unemployment Theory, Second Edition*. Cambridge, MA: MIT Press, 2000. Ch. 1.
2. \*Dey, M. and C. Flinn. "An Equilibrium Model of Health Insurance Provision and Wage Determination." Mimeo, 2000. Downloadable from Research section of my web page.
3. \*Flinn, C. "Minimum Wage Effects on Labor Market Outcomes in the Presence of Search and Matching." Mimeo, 2000. Downloadable from Research section of my web page.
4. \*Postel-Vinay, F. and J-M Robin. "Wage Dispersion with Heterogeneous Firm Technologies and Worker Abilities: An Equilibrium Job Search Model for Matched Employer-Employee Data." Mimeo, 2000. Downloadable at

[http : //www.inra.fr/Internet/Departements/ESR/UR/lea/wp/wp0008.pdf](http://www.inra.fr/Internet/Departements/ESR/UR/lea/wp/wp0008.pdf)

### 1.E. Job Mobility

1. \*Jovanovic, B. "Job Matching and the Theory of Turnover." *J. Pol. Econ.* 87 (1979): 972-990.
2. Jovanovic, B. "Matching, Turnover, and Unemployment." *J. Pol. Econ.* 92 (1984): 108-122.
3. \*Flinn, C. "On-the-Job Search with Information Obsolescence." C.V. Starr Center Report 96-07, February 1996.

4. Burdett, K. "A Theory of Employee Job Search and Quit Rates." *Amer. Econ. Rev.* 68 (1978): 212-220.
5. Lippman, S. and J. McCall. "The Economics of Belated Information." *Int. Econ. Rev.* 22 (1981): 135-146.
6. Mortensen, D. "Specific Capital and Labor Turnover." *Bell J. Econ.* 9 (1978): 572-586.
7. Salop, S. "Wage Differentials in a Dynamic Theory of the Firm." *J. Econ. Theory* 6 (1973): 321-344.
8. \*Flinn, C. "Wage and Job Mobility of Young Workers." *J. Pol. Econ.* 94 (1986): S88-S110.
9. \*Miller, R. "Job Matching and Occupational Choice." *J. Pol. Econ.* 92 (1984): 1086-1120.
10. McCall, B. "A Dynamic Model of Occupational Choice." *Journal of Econ. Dyn. and Control* 15 (1994): 387-408.

## 2.A Static Labor Supply

1. \*Deaton, A. and J. Muellbauer. *Economics and Consumer Behavior*. Cambridge: Cambridge University Press, 1980. Chapters 4.1, 11.1-11.2.
2. \*Heckman, J. "Shadow Prices, Market Wages, and Labor Supply." *Econometrica* 42 (July 1974): 679-694.
3. Hausman, J. "The Effect of Wages, Taxes, and Fixed Costs on Women's Labor Force Participation." *J. of Public Economics* 14 (October 1980): 161-194.
4. \*Aaberge, R., U. Colombino, and S. Strom. "Labour Supply in Italy: An Empirical Analysis of Joint Household Decisions, with Taxes and Quantity Constraints." *J. of Applied Econometrics* 14 (July-August 1999): 403-422.
5. \*Moffitt, R. "The Estimation of a Joint Wage Hours Labor Supply Model." *J. of Labor Economics* 2 (October 1984): 550-566.

## 2.B Life-Cycle Labor Supply

1. \*MaCurdy, T. "An Empirical Model of Labour Supply in a Life-Cycle Setting." *JPE* 89 (December 1981): 1059-1085.
2. Heckman, J. and T. MaCurdy. "A Life Cycle Model of Female Labour Supply." *Rev. Econ. Studies* 47 (Jan 1980): 47-74.
3. Browning, M., A. Deaton, and M. Irish. "A Profitable Approach to Labor Supply and Commodity Demands over the Life-Cycle." *Econometrica* 53 (May 1985): 503-543.

4. \*Hotz, V.J., F. Kydland, and G. Sedlacek. "Intertemporal Preferences and Labor Supply." *Econometrica* 56 (March 1988): 335-360.
5. Abowd, J. and D. Card. "On the Covariance Structure of Earnings and Hours Changes." *Econometrica* 57 (March 1989): 411-445.
6. \*Eckstein, Z. and K. Wolpin. "Dynamic Labour Force Participation of Married Women and Endogenous Work Experience." *Review of Economic Studies* (July 1989): 375-90.
7. \*Altug, S. and R. Miller. "The Effect of Work Experience on Female Wages and Labour Supply." *Review of Economic Studies* (January 1998): 45-85.
8. \*Shaw, K. "Life-Cycle Labor Supply with Human Capital Accumulation." *International Economic Review* 30 (May 1989): 431-56.

## **2.C Household Bargaining and Labor Supply**

1. McElroy, M. and M. Horney. "Nash-bargained Decisions: Towards a Generalization of the Theory of Demand." *International Economic Review* 22 (1981): 333-349.
2. \*Manser, M. and M. Brown. "Marriage and Household Decision-Making: A Bargaining Analysis." *International Economic Review* 21 (1980): 31-44.
3. \*Chiappori, P-A. "Rational Household Labor Supply." *Econometrica* 56 (1988): 63-89.
4. \*McElroy, M. "The Empirical Content of Nash-bargained Household Behavior." *Journal of Human Resources* 25 (1990): 559-583.
5. \*Browning, M, F. Bourguignon, P-A Chiappori, and V. Lechene. "Incomes and Outcomes: A Structural Model of Intra-Household Allocation." *Journal of Political Economy* 102 (1994): 1067-1096.
6. Fortin, B. and G. Lacroix. "A Test of the Unitary and Collective Models of Household Labor Supply." *Economic Journal* (1997): 933-955.
7. Kooreman, P. and A. Kapteyn. "On the Empirical Implementation of some Game Theoretic Models of Household Labor Supply." *Journal of Human Resources* 25 (1990): 584-598.
8. \*Del Boca, D. and C. Flinn. "Modes of Spousal Interaction and the Labor Market Environment." On my web site.

## **2.D Models of Household Formation and Dissolution**

1. \*Weiss, Y. and R. Willis. "Children as Collective Goods and Divorce Settlements." *Journal of Labor Economics* 3 (July 1985): 268-292.

2. \*Flinn, C. "Modes of Interaction between Divorced Parents." *International Economic Review* (August 2000): 545-578.
3. \*Del Boca, D. and C. Flinn. "Rationalizing Child Support Decisions." *American Economic Review* 85 (December 1995): 1241-1262.
4. Del Boca, D. and C. Flinn. "The Determination of Welfare in Nonintact Families." Chapter 5 in *The Measurement of Household Welfare* (Blundell, Preston, and Walker, eds.). Cambridge: Cambridge University Press, 1994
5. Brien, M., L. Lillard, and S. Stern. "Cohabitation, Marriage, and Divorce in a Model of Match Quality." Mimeo, University of Virginia. Downloadable from  
  
*http : //www.people.virginia.edu/~sns5r/resint/structstf/bls.html*
6. Weiss, Y. "The Formation and Dissolution of Families: Why Marry? Who Marries Whom? and What Happens upon Divorce." In Rosenzweig,-Mark-R.; Stark,-Oded, eds. *Handbook of Population and Family Economics, Volume 1A* (Rosenzweig and Stark, eds.). Handbooks in Economics, vol. 14. Amsterdam; New York and Oxford: Elsevier Science, North-Holland, 1997, pages 81-123.
7. \*Brown, M. and C. Flinn. "Investment in Child Quality over Marital States." Downloadable from web site.

### **3.A Job-Market Signalling**

1. \*Spence, M. "Job Market Signalling." *Q.J.E.* 87 (1973): 355-374.
2. \*Kreps, D. *A Course in Microeconomic Theory*. Princeton: Princeton Univ. Press, 1990. Ch. 17.
3. \*Greenwald, B. "Adverse Selection in the Labor Market." *Rev. Econ. Studies* 53 (1986): 325-347.
4. Berkovitch, E. "A Stigma Theory of Unemployment Duration." In *Advances in the Theory and Measurement of Unemployment* (Y. Weiss and G. Fishelson, eds.), New York: MacMillan, 1990.
5. Waldman, M. "Job Assignments, Signalling, and Efficiency." *Rand J. Econ.* 15 (1984): 255-270.

### **3.B Principal-Agent Problems in the Labor Market**

1. \*Kreps, D. *A Course in Microeconomic Theory*, Ch. 16.

2. \*Shapiro, C. and J. Stiglitz. "Equilibrium Unemployment as a Worker Discipline Device." *A.E.R.* 74 (1984): 433-444.
3. \*Foster, J. and H. Wan. "Involuntary Underemployment as a Principal-Agent Equilibrium." *A.E.R.* 74 (1984): 476-484.
4. Malcomson, J. "Work Incentives, Hierarchy, and Internal Labor Markets." *JPE*. 92 (June 1984): 486-507.
5. \*MacLeod, B. and J. Malcomson. "Implicit Contracts, Incentive Compatability, and Involuntary Unemployment." *Econometrica* 57 (March 1989): 447-480.
6. Albrecht, J. and S. Vroman. "Nash Equilibrium Efficiency Wage Distributions." *International Economic Review* 39 (February 1998): 183-203.

### **3.C. Estimation of Models with Moral Hazard**

1. \*Flinn, C. "Equilibrium Dismissal without Stigma." Chapter 5 in *Labor Demand and Equilibrium Wage Formation* (van Ours, Pfaan, and Ridder, eds.). Amsterdam: North-Holland, 1993, pages 249-275.
2. \*Flinn, C. "Equilibrium Wage and Dismissal Processes." *Journal of Business and Economic Statistics* 15 (April 1997): 221-236.
3. \*Abbring, J., P-A Chiappori, J. Heckman, and J. Pinquet. "Testing for Moral Hazard on Dynamic Insurance Data." Mimeo, 2002, to be distributed.

### **4.A Human Capital Investment Decisions**

1. Ryder, H., F. Stafford, and P. Stephan. "Labor, Leisure and Training over the Life Cycle." *International Economic Review* 17 (October 1976): 651-674.
2. Snow, A. and R. Warren, Jr. "Human Capital Investment and Labor Supply under Uncertainty." *International Economic Review* 31 (February 1990): 195-206.
3. \*Keane, M. and K. Wolpin. "The Career Decisions of Young Men." *JPE* 105 (June 1997): 473-522.
4. \*Willis, R. and S. Rosen. "Education and Self-Selection" *JPE* 87 (October 1979): S7-S36.

### **4.B. Human Capital Investment and Cohort Size**

1. \*Flinn, C. "Cohort Size and Schooling Choice." *J. of Population Economics* 6 (1993): 31-55.

2. \*Welch, F “Effects of Cohort Size on Earnings: The Baby Boom Babies Financial Bust.” *J.P.E* 87 (1979): S65-S97.
3. Stapleton, D. and D. Young. “Educational Attainment and Cohort Size.” *J. of Labor Economics* 6 (1988): 330-361.
4. \*Siow, A. “Occupational Choice under Uncertainty.” *Econometrica* 52 (1984): 631-645.