

CHAPTER 7 - LABOR SUPPLY: HOUSEHOLD PRODUCTION, THE FAMILY, AND THE LIFE CYCLE

Chapter 7 analyzes the labor supply decision (the decision to work for pay) in the context of household production theory. In this chapter, the primary alternative to working for pay is not assumed to be leisure, but household production. This framework quite naturally leads the discussion of labor supply into the context of families, thereby raising the issue of family labor supply decisions. Further, since one's household productivity varies considerably across the life cycle (as, of course, do wages), the concepts of household production also lead to a discussion of labor supply over the life cycle.

Instructors facing severe time constraints may wish to skip this chapter. The insights provided by the analysis in Chapter 7 are refinements of the basic concepts introduced in Chapter 6, and they do not contradict the insights or predictions of Chapter 6. However, Chapter 7 summarizes some recent directions in which labor supply theory has been going, and to sacrifice Chapter 7 would mean forgoing concepts and empirical work close to the frontiers of economic analysis.

The chapter begins with an introduction to the concept that households combine time and goods to produce commodities that are consumed at home. The graphic analysis of household production and the choice of household production technology is shown to be completely analogous to the graphic analysis and fundamental implications of the labor/leisure choice discussed in Chapter 6. The household production context of the labor supply decision, however, yields insights about that decision that go beyond those of Chapter 6. These insights are discussed after our brief introduction to household production theory in the first section.

In particular, we point out the tripartite choice between market work, household work, and leisure in analyzing why the substitution effects for women might be expected to be larger than those for men. We discuss such family labor supply decisions as who stays home to care for children (if anyone does), whether both spouses will work for pay, and the interdependency of the spouses' labor supply decisions. The "additional worker" and "discouraged worker" hypotheses are also discussed in this context.

Our discussion of the life-cycle aspects of labor supply begins with the observation that household productivity does indeed vary over the life cycle. The traditional interrupted careers of married women cannot be explained without reference to the shifts in household productivity that take place when children are born and as they grow older. Labor supply over the life cycle is also affected by the way wages typically vary with age, causing intertemporal substitution effects; in this context, we discuss the important issue of choice of retirement age (including data on the way lifetime Social Security benefits vary with age of retirement).

The chapter concludes with a policy analysis of "child support assurance" programs.

List of Major Concepts

1. The basic concepts of household production theory include the combining of goods and time to produce commodities that yield the family utility.
2. Household commodities may be produced by time-intensive methods or by goods-intensive methods; the method chosen is in part a function of the price placed on time.
3. The principal predictions associated with the income and substitution effects in the labor/leisure model are unchanged in the context of the household production model. The latter model, however, adds a third dimension of choice about time usage (market work, household work, leisure).
4. As wages change, there will be changes in the time intensity of commodities consumed as well as in the time intensity of household production technologies.
5. Joint household production decisions (which spouse, if either, should remain home instead of working for pay) have yet to be completely modeled, but they must clearly take account of the partners' marginal productivities at home and the wages they can command in the "market."
6. The "discouraged worker hypothesis" and the "additional worker hypothesis" are discussed in the context of household production theory.
7. Labor supply decisions over the life cycle are affected by household productivity changes and predictable changes in wages over the life cycle that create intertemporal substitution effects without corresponding income effects.
8. Graphic analysis of the choice of optimum retirement age is presented, emphasizing how delaying retirement by a year can affect the present value of one's total income over the remaining years of expected life.
9. Child support assurance programs ensure transfer payments to custodial parents based on the age and number of children, not on income. In contrast with welfare programs, which tend to create budget constraints with zero net wage rates, child support assurance programs preserve incentives to engage in market work. However, for those who worked for pay in the absence of such programs, the pure income effect created by support assurance programs should tend to induce fewer hours of paid work.