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Earnings Losses of Displaced Older Workers: Accounting for the Retirement Option

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Abstract

In this paper I estimate the magnitude of earnings losses faced by workers who are displaced when over the age of 50. This is potentially complicated by the self-selection of older individuals out of the labour force and into activities such as retirement, preventing observation of their potential earnings losses. Using data from the Survey of Labour and Income Dynamics (1993-2004), I use a Heckman selection model that accounts for individuals' departure from the labour force following displacement. Results indicate that self-selection is an important factor to consider when studying the earnings of older workers but does not bias estimates of earnings losses due to displacement. Further, the results suggest that workers over 50 do not face larger earnings losses upon displacement than 35-49 year olds. Losses are only slightly larger than that experienced by 25-34 year olds. Consistent with the existing literature, those workers displaced over 50 with high tenure on the lost job experience the largest earnings losses.

JEL Code: *J63, J31, J26*
Keywords: *Layoffs, Wage level, Wage Structure, Retirement, Retirement Policies*

The statistical analysis in this study relies on Statistics Canada microdata, made available through the South Western Ontario Research Data Centre.

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Executive Summary

As the Canadian population continues to age, the experiences and needs of older workers are taking on greater importance and relevance in the development of labour market policies and initiatives. Although experienced workers' earnings losses resulting from job displacement has long been an important policy concern, very little is known about the losses faced by our oldest workers. Are the earnings losses of older displaced workers in Canada actually larger than that experienced by their younger counterparts? Is it worth directing public resources to these older displaced workers? To date, there has not been enough information available about displaced older Canadian workers to answer these questions.

This paper provides estimates of the magnitude of short term and medium term earnings losses faced by Canadian workers who are displaced when over the age of 50 and under age 69. Displaced workers are those who have lost their job due to the company closing, the company moving, or being laid off due to business slowdown. This does not include workers laid off due to seasonal conditions or voluntary job separation.

To obtain my estimates, I use data from the Survey of Labour and Income Dynamics which is a panel data set covering the years 1993-2004. When forming these estimates, I have accounted for the self-selection of older individuals out of the labour force and into activities such as retirement. This self-selected departure prevents us from observing their potential earnings losses following displacement. It could be the case, for example, that older high tenured displaced workers face the smallest wage losses and have the best pensions available for retirement. By excluding these workers from our samples, we would overestimate the earnings losses of displaced older workers near retirement ages. To account for self-selection, I use a Heckman selection model in the estimation of earnings losses. The use of this model relies on the fact that a spouse's non-participation in the labour force is a strong predictor of an individual's likelihood to enter retirement after job loss. At the same time, a spouse's non-participation in the labour force is not a good predictor of earnings losses following job loss.

The results of this study indicate that, as with younger workers, older workers face large and persistent earnings losses upon displacement. When displaced over the age of 50, older men can expect earnings losses around $14,000 in the year following displacement - representing roughly 37% of their predisplacement earnings. Furthermore, some earnings losses begin before displacement actually occurs, particularly among those workers who are laid off due to the company closing (relative to the workers laid off due to business slowdown). The earnings losses of younger men age 25-34 in the first year after displacement are slightly smaller than those experienced by older men, but not significantly smaller (even in terms relative to pre-displacement earnings). There are not substantial or significant differences between the earnings losses of displaced individuals aged 35-49 and those aged 50-69.

High-seniority older men face the largest earnings losses upon displacement, of over $22,000 in the first year following displacement and longer-term losses of $16,314. Low tenured men face earnings losses of only $10,592 in the first year and longer-term losses of only $6,394.

There are also important differences by education level. Both high and lower education experience similar levels of earnings losses following displacement – around $13,000 in the first year following displacement. Relative to expected earnings, however, a highly educated worker may expect losses amounting to 23% of their predisplacement earnings while lower educated workers may expect losses close to 40% of predisplacement earnings. Interestingly, there are no significant differences between the earnings losses of displaced workers in rural or urban areas. Relative to predisplacement earnings, however, the losses of rural workers are slightly larger (at roughly 40%) than urban workers (at roughly 29%). Several previous studies have shown that displaced workers suffer large and persistent earnings losses, with losses continuing long after displacement. The estimates provided in this paper are consistent with those provided by Jacobson, Lalonde and Sullivan (1993) for U.S. workers under age 55 in Pennsylvania. They found that even six years after displacement, earnings remained 25% lower than predisplacement earnings.

Morissette, Zhang, and Frenette (2007) provide comparable Canadian estimates of earnings losses for workers between age 25 and 49. They find that high seniority displaced men in their sample experienced long-term losses between 18% and 35% of their predisplacement earnings. Again, these findings are consistent with estimates provided in this study.

From these results, it is not clear that directing resources to older displaced workers is merited. Recent initiatives such as the Targeted Initiative for Older Workers, which provides funds to help reintegrate older displaced workers over age 55 back into the labour force, may not be justified. Given the longer remaining working life of younger workers these resources might be more efficiently used in programs targeting these groups. In the interest of providing a social safety net for older workers, it appears some resources could be targeted toward the less educated and rural displaced workers who are facing the largest relative losses.