The Ins and Outs of Retirement: Labor Market Dynamics of Older Workers

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The U.S. labor market increasingly relies on older workers---workers of 55 and above account for an increasing share of the population, and the labor force participation rate (LFPR) of older workers exhibits a secular increase in sharp contrast to the decline in the LFPR of younger workers. There is not only a large stock of older workers but also large flows in and out of retirement. According to the Current Population Survey, every month, nearly 2% of retired workers go back to the labor force. Given the large size of the retired population, this implies an enormous flow of retirees returning to work. A unique feature of the COVID-19 pandemic labor market is a sudden and persistent collapse of this flow from retirement to employment. The decline in the outflow from retirement to employment coupled with a steady rate of inflows from employment to retirement completely offset the increase of the LFPR of older workers achieved over the past few decades. Such changes in older workers' labor market dynamics did not happen in previous recessions. In the proposed research we aim to understand the causes and economic consequences of the changing flows of retirees into the labor force induced by the pandemic and inform the appropriate policy response. The proposed research is closely related to SSA Focal Area #7: Informing Trust Fund Projections as it aims to uncover the combined effect of population aging and the effect of the pandemic on demand and supply of labor by retired workers and their labor force participation. The induced large changes in composition of employment by age may lead to significant effects on productivity that we would like to uncover. Moreover, the proposed research will inform Focal Area #4: Economic Security of SSA Beneficiaries as the sharp decline in labor force participation of older workers following the pandemic increases their dependency on SSA-administered benefits, as well as Focal Area #6: Return-to-Work by identifying barriers to re-entry of the retired workers into the labor force and formulating the appropriate policy response.

More specifically, to assess effective policy responses, one needs a theoretical framework that can rationalize the observed labor market dynamics of older workers. This project aims at providing such a framework to understand the nature of the labor market dynamics of older workers. To this end, we first document two sets of empirical facts on the labor market dynamics of retirement-age workers during normal times to guide and discipline the development of the theory. First, we use HRS-SSA linked data in addition to publicly available US data to document the driving forces of the return to work decisions of retired workers. Is it driven by workers seeking additional sources of income or searching for the more fulfilling life? What types of jobs do unretired workers take? Do they return to their previous jobs or similar jobs? Do they take high-end jobs requiring lots of experience accumulated during their working career or marginal jobs with some easy tasks and light burden? Second, at this stage we use administrative data from Germany to understand the demand for retired workers on the employer side, specifically the extent to which it is driven by unexpected demand fluctuations or temporary worker shortages. In the longer run, we hope to extend this analysis to the administrative data from the US. In the second part of this project, we will design a quantitative theoretical model consistent with the facts about older workers' labor market dynamics. The model can serve as a laboratory to assess policy implications for the social security system and quantitatively measure the effects of alternative policies on labor force participation of the retired workers.