Labor Market Expectations

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Overview

Motivation

- Labor risk
- Rational expectations of agents
- (Biased) Subjective labor market expectations affect macroeconomic results and individual decision making

Literature review

- US agents tend to be over-optimistic about their own labor market prospects. (Balleer et al., 2021)
  - Unemployed workers overestimate the probability to be employed in four months the most.
- German workers overestimate their individual probabilities to separate from their job when employed as well to find a job when unemployed. (Balleer et al., 2023)
  - East Germans are significantly more pessimistic than West Germans.
- Men are more optimistic than women in assessing their labor market prospects. (Dawson, 2017)
- Longer unemployed individuals (3-5 years) underestimate their probability of re-employment. (Kassenboehmer and Schatz, 2017)

Research Questions

1. What is the (average) subjective expectation of an unemployed individual to be employed in 4 months?
2. Does this (average) subjective employment probability differ from the actual employment probability?
3. If yes, what is the extend of the bias and who is prone to overestimate the subjective employment probability the most?

Data

- Survey of Consumer Expectations (SCE)
  - released by Federal Reserve Bank of New York
  - sample period Jun 2013 - March 2023
  - internet-based survey
  - rotating panel of approximately 1,300 household heads
  - up to twelve months participation
  - focus on expectations about economic outcomes related to inflation, the labor market, and household finance

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- SCE Labor Market Survey
  - additional module every 4 months (March, July, November) since 2014
  - answered by all SCE participants except first-time participants

Sample

Focus on the expectations and actual transitions of unemployed individuals only.

Sample Period:

- March 2014 – March 2022 (every 4 months)
  → All available waves of the SCE Labor Market Survey

Selection Criterion:

- 25 – 60 years old
- Not in school or training

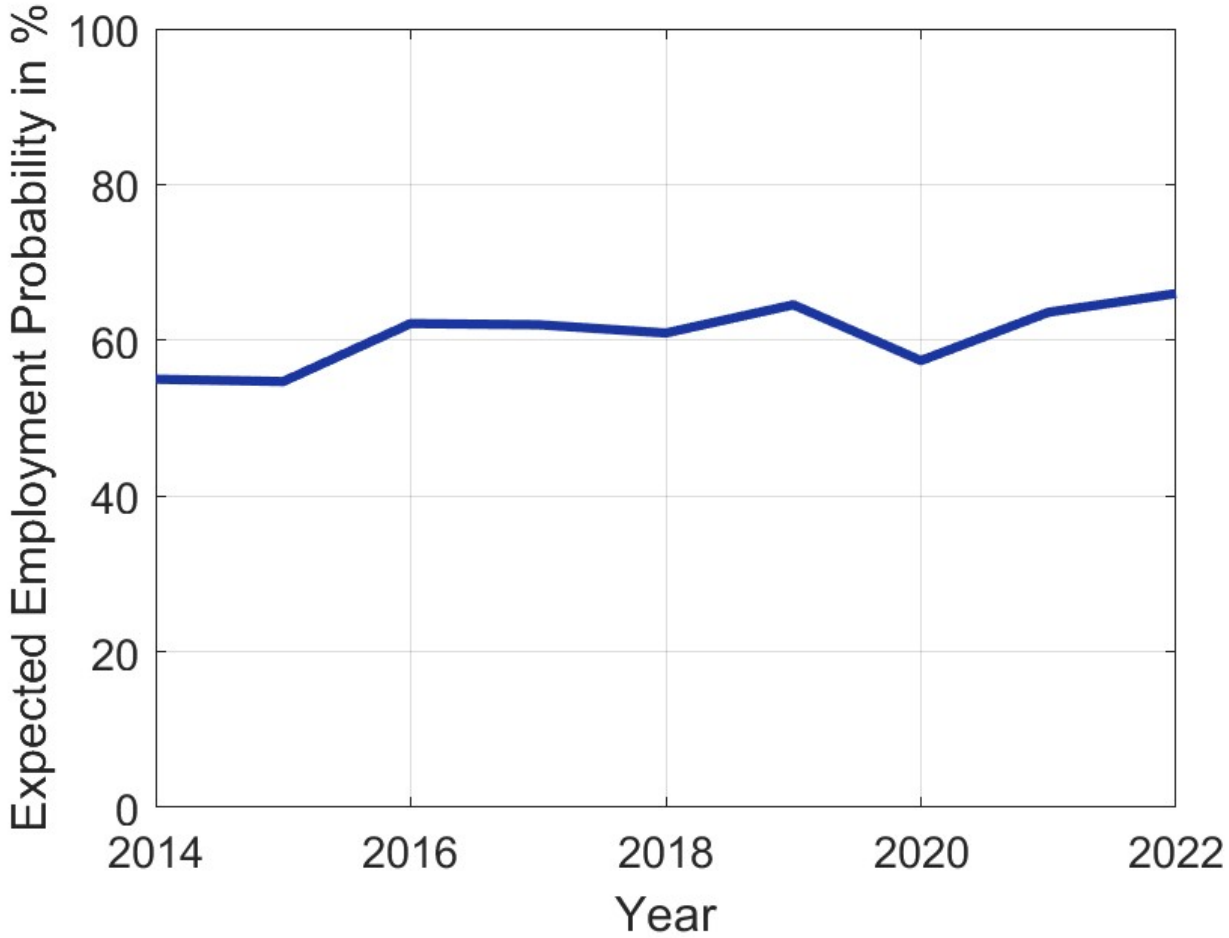
→ Applying survey weights in most results

sample composition

1. Research Question

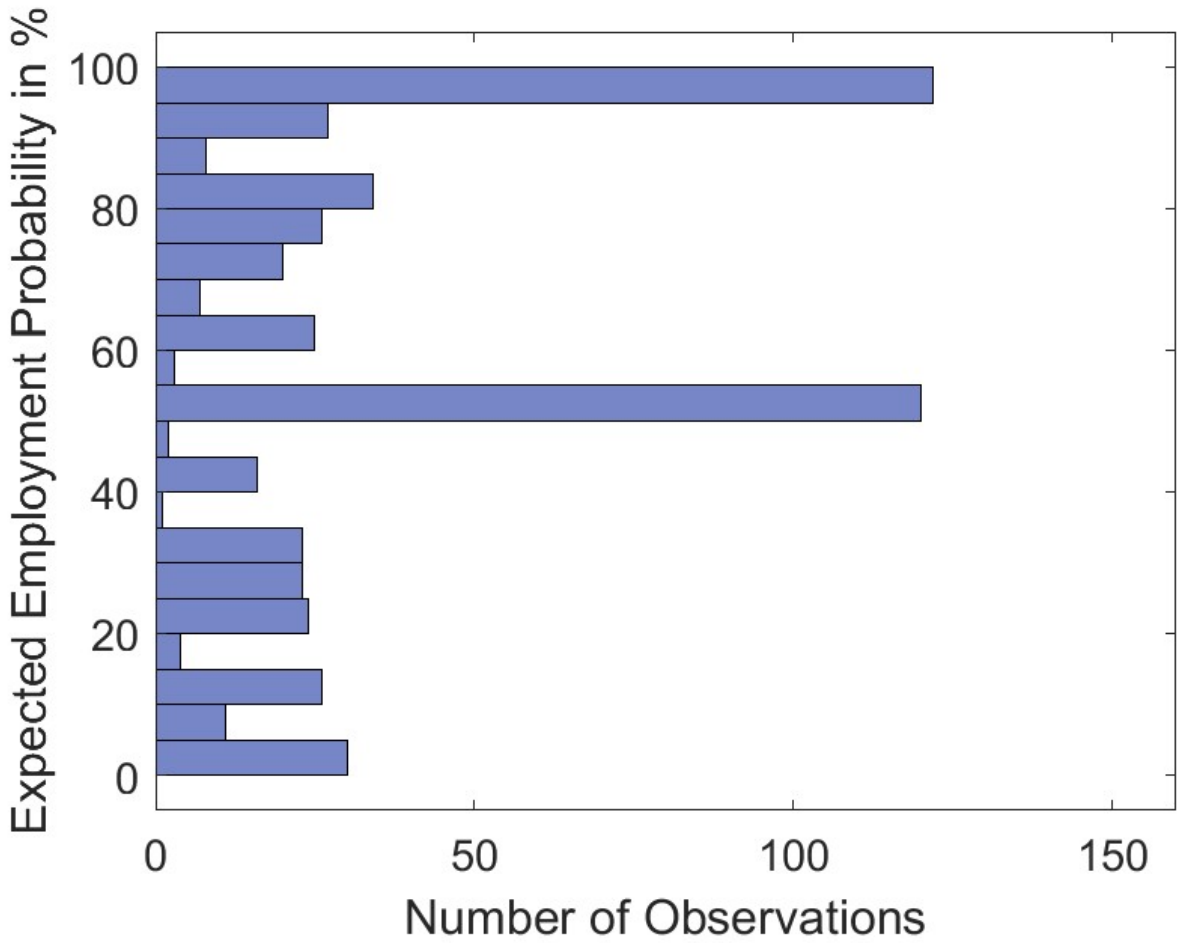
What is the (average) subjective expectation of an unemployed individual to be employed in 4 months?

Expected Employment Probability of Unemployed



→ The annual average of employment expectations ranges between 55% – 65% and is rather stable over time.

Expected Employment Probability of Unemployed



→ **On average**, unemployed individuals expect to be employed in 4 months with a probability of **59.9%**.

2. Research Question

Does the (average) subjective employment probability differ from the actual employment probability?
If yes, what is the extent of the bias?

Survey Questions

Expected transition probability:

- *What do you think is the percent chance that four months from now you will be...*
  - employed
  - unemployed and looking for work
  - unemployed and not looking for work (not in the labor force)

Actual transition probability:

- *What is your current employment situation?*
  - employed
  - unemployed
  - not in the labor force

classification

- Average transition probabilities calculated as the share of actual transitions over 4 months

Average Employment Expectation Bias

How does the **average employment expectation** compare to the **actual probability** to get employed in 4 months?

	Expected Probability	Actual Probability	Bias (Expected - Actual)
Unemployed$_t$ $\rightarrow$ Employed$_{t+4}$			
Observations			

Average Employment Expectation Bias

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	Expected Probability	Actual Probability	Bias (Expected - Actual)
Unemployed$_t$ $\rightarrow$ Employed$_{t+4}$	59.9		
	(1.4)		
Observations	552		

Average Employment Expectation Bias

How does the **average employment expectation** compare to the **actual probability** to get employed in 4 months?

	Expected Probability	Actual Probability	Bias (Expected - Actual)
Unemployed$_t$ $\rightarrow$ Employed$_{t+4}$	59.9	43.1	
	(1.4)	(2.9)	
Observations	552	285	

Average Employment Expectation Bias

How does the **average employment expectation** compare to the **actual probability** to get employed in 4 months?

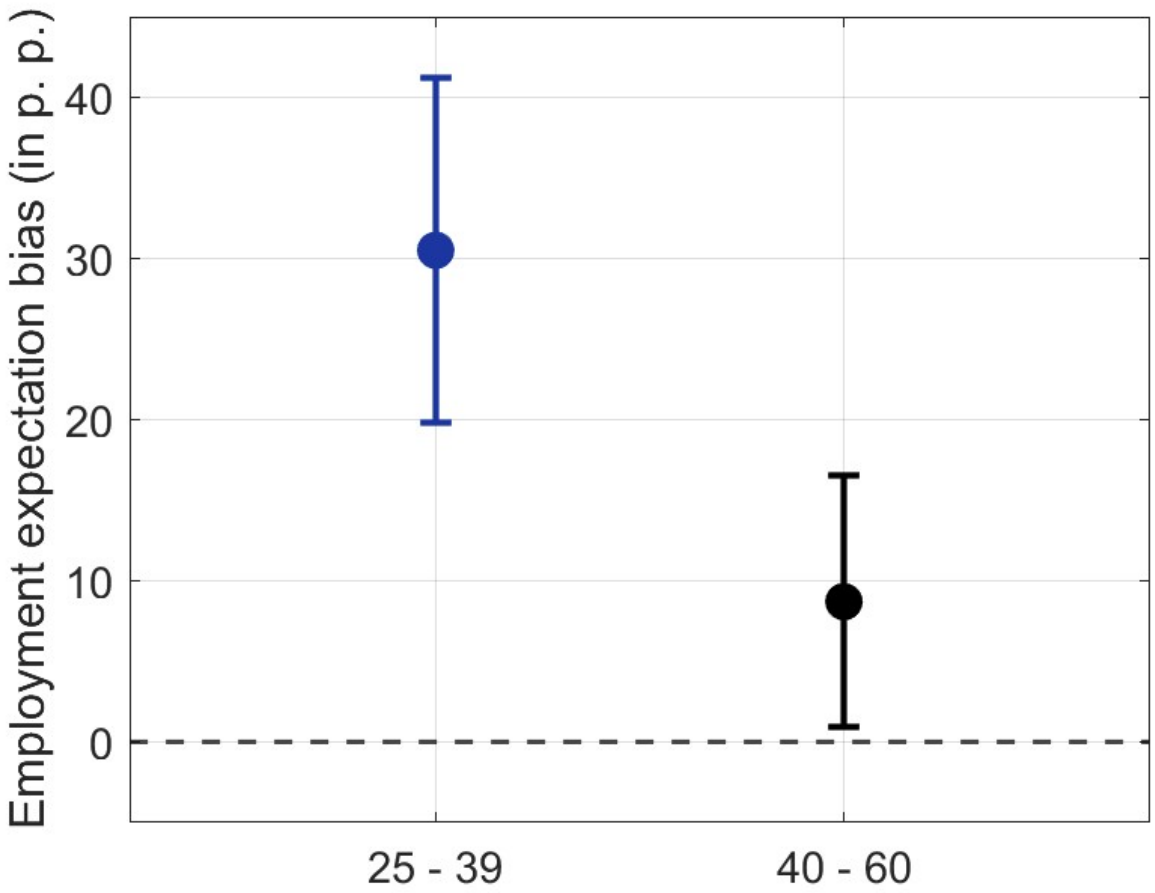
	Expected Probability	Actual Probability	Bias (Expected - Actual)
Unemployed$_t$ $\rightarrow$ Employed$_{t+4}$	59.9	43.1	16.8
	(1.4)	(2.9)	(3.2)
Observations	552	285	

$\rightarrow$ Unemployed individuals on average **overestimate** the probability to get employed in 4 months **by 16.8 p.p**.

3. Research Question

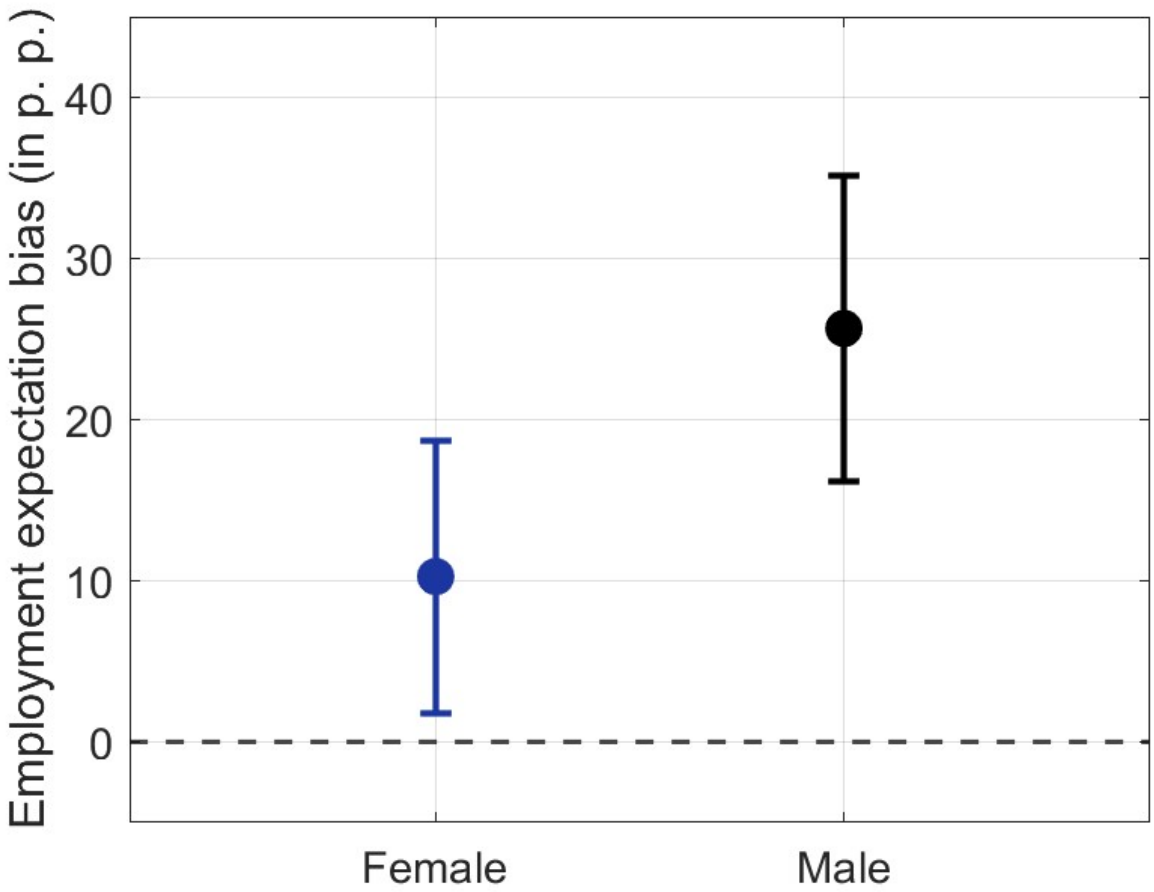
Who is prone to overestimate the subjective employment probability the most?

Heterogeneity by Age



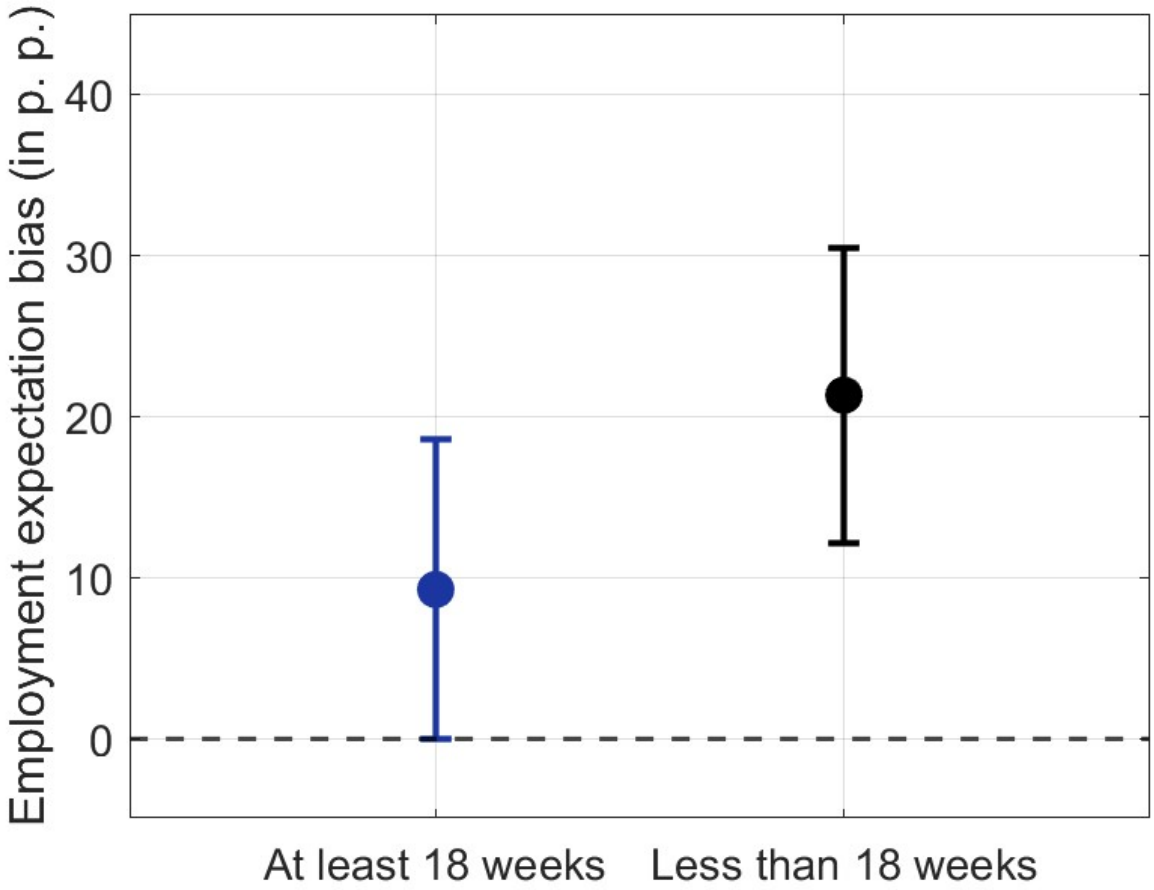
→ Younger unemployed individuals are more prone to overestimate the employment probability with an average bias of 30.5 p.p.

Heterogeneity by Gender



→ Male unemployed overestimate the employment probability stronger.

Heterogeneity by Job Search Duration



→ Unemployed individuals that are in job search for a shorter period of time overestimate the employment probability stronger.

Summary

Heterogeneity:

- Younger, male, and shorter unemployed have significantly higher expectation bias
- No significant difference by education, marital status, or race
- All groups have a significant positive bias

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Robustness:

- Employment expectations do predict transitions to employment at the individual level, but not perfectly result
- The results do not significantly differ for...
  - ... pre- vs. post-Covid months
  - ... high- vs. low-numeracy individuals

Conclusion

- The bias in employment expectations exists and its extend is in line with Balleer et al. (2021)
  - 16.8% (using data from 2014-2022)
  - 18.8% (using data from 2014-2018)
- Confirmed findings of Dawson (2017) that males are more optimistic about their labor market outcomes
- Following Kassenboehmer and Schatz (2017), job search duration influences the employment expectations

References

Balleer, A., Duernecker, G., Forstner, S., and Goensch, J. (2021). The effects of biased labor market expectations on consumption, wealth inequality, and welfare. *SSRN Electronic Journal*.

Balleer, A., Duernecker, G., Forstner, S., and Goensch, J. (2023). Biased expectations and labor market outcomes: Evidence from german survey data and implications for the east-west wage gap. *SSRN Electronic Journal*.

Dawson, C. (2017). The upside of pessimism biased beliefs and the paradox of the contented female worker. *Journal of Economic Behavior and Organization*, 135.

Kassenboehmer, S. C. and Schatz, S. G. (2017). Re-employment expectations and realisations: Prediction errors and behavioural responses. *Labour Economics*, 44.

Thank you for your attention!

Labor Market Status Classification (Balleer et al., 2021)

- Employed
  - Working full-time
  - Working part-time
  - On sick or other leave
- Unemployed
  - Temporarily laid-off
  - Not working, but would like to work and has done anything in the last four weeks to look for work
- Not in the labor force
  - Disabled or unable to work, retired, homemaker
  - Not working, but would like to work and has **not** done anything in the last four weeks to look for work

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Sample Composition

	Expected		Actual	
	N	Share	N	Share
Male	235	43%	162	44%
Female	317	57%	123	56%
White	422	76%	224	79%
Non-White	129	23%	64	22%
25 – 39 years old	188	34%	90	32%
40 – 60 years old	364	66%	195	68%
No college degree	282	51%	139	49%
College degree	269	49%	146	51%
$<$ 18 weeks job search	295	53%	133	47%
$\geq$ 18 weeks job search	216	39%	131	46%
Total	552	100%	285	100%

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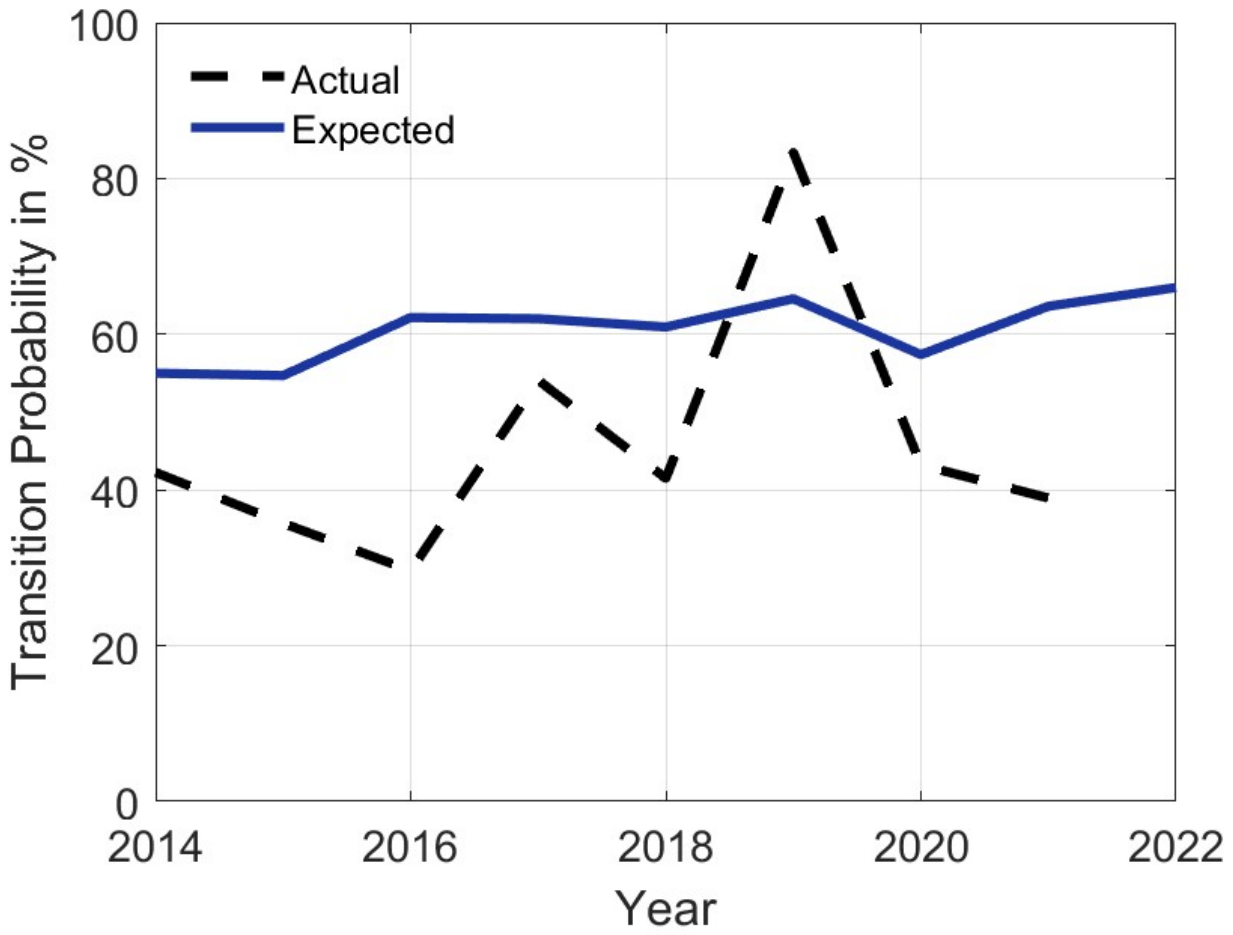
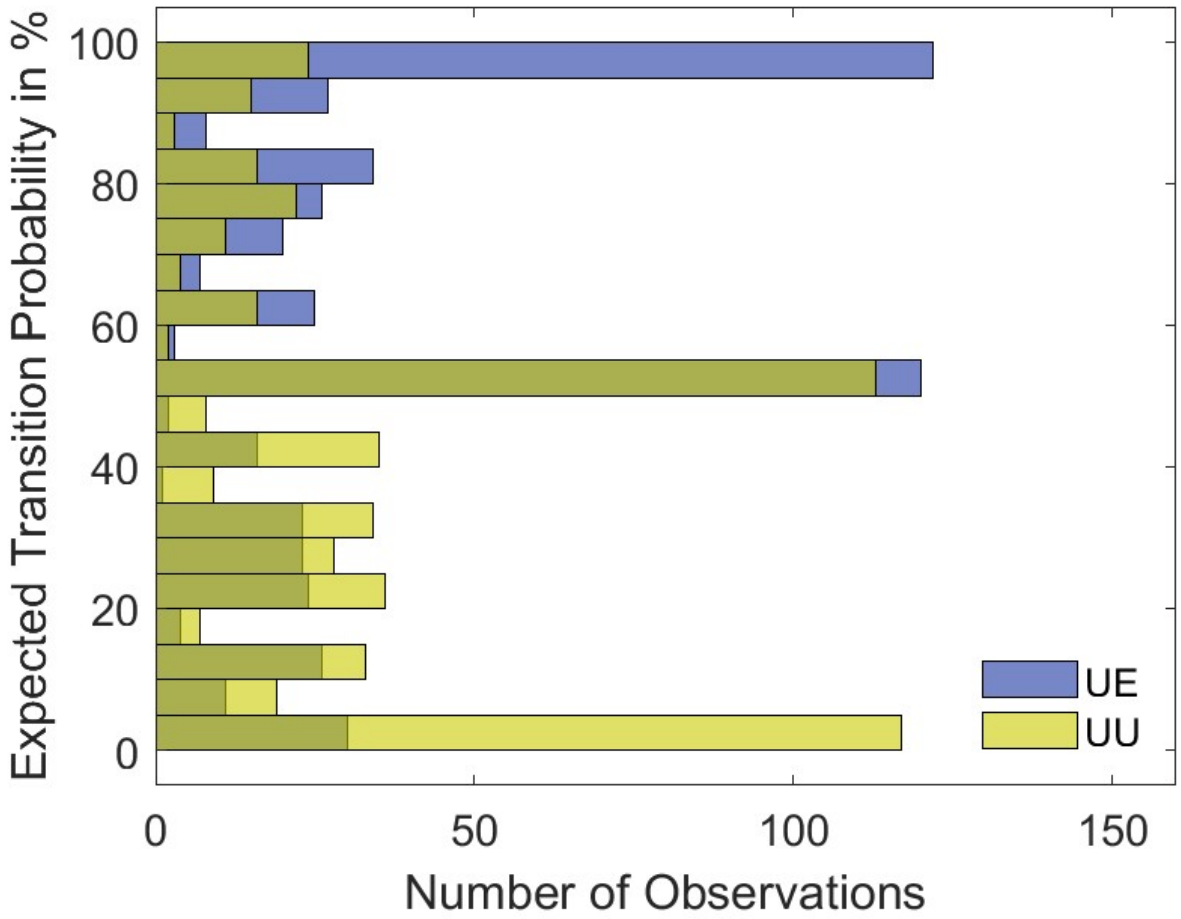
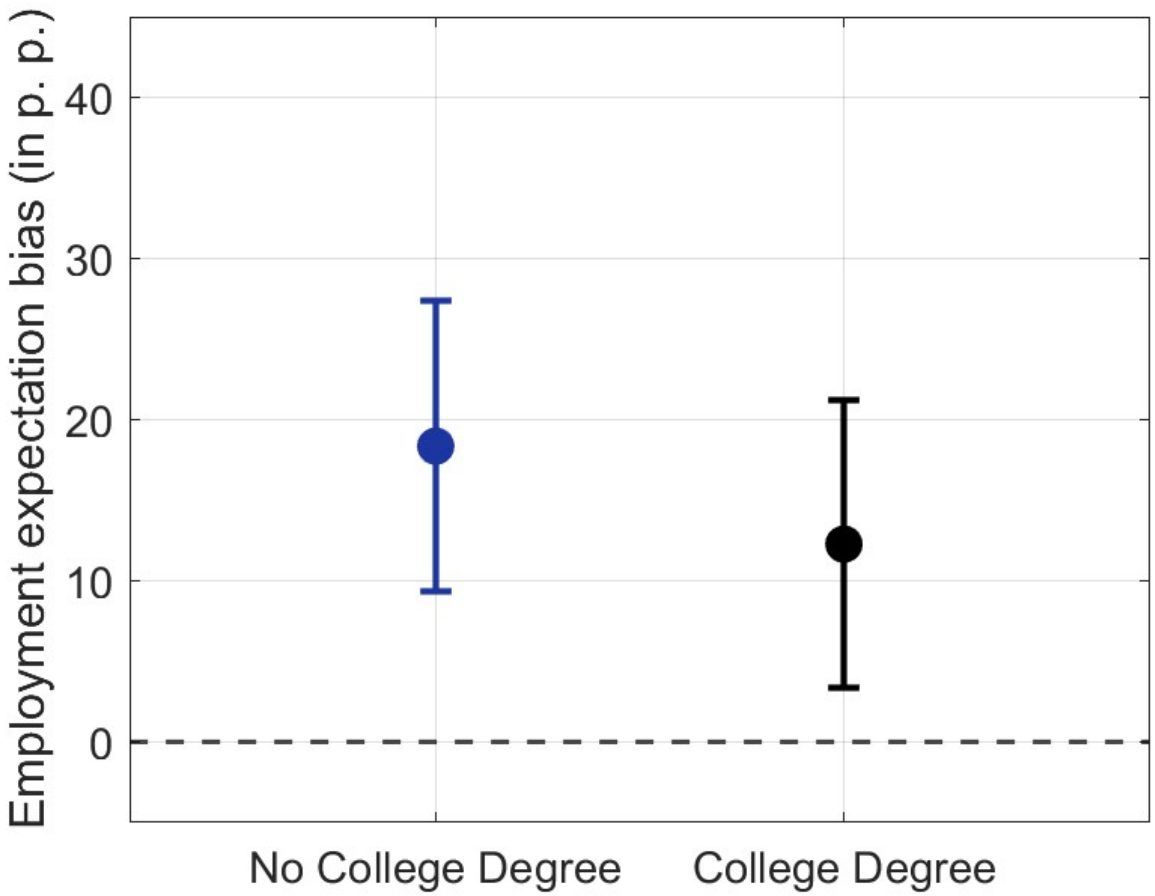
Expected and Actual Employment Probability by Year



Expected Transition Probabilities of Unemployed

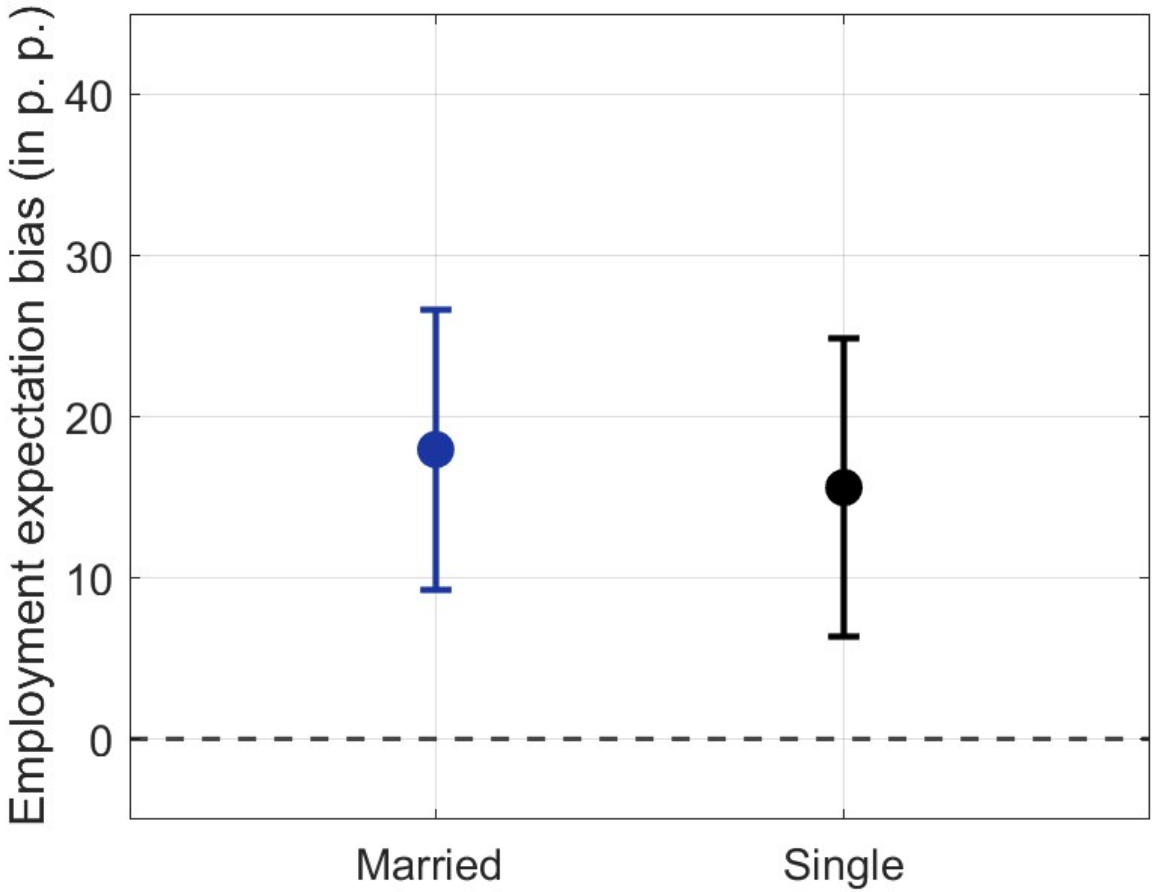


Heterogeneity by Education

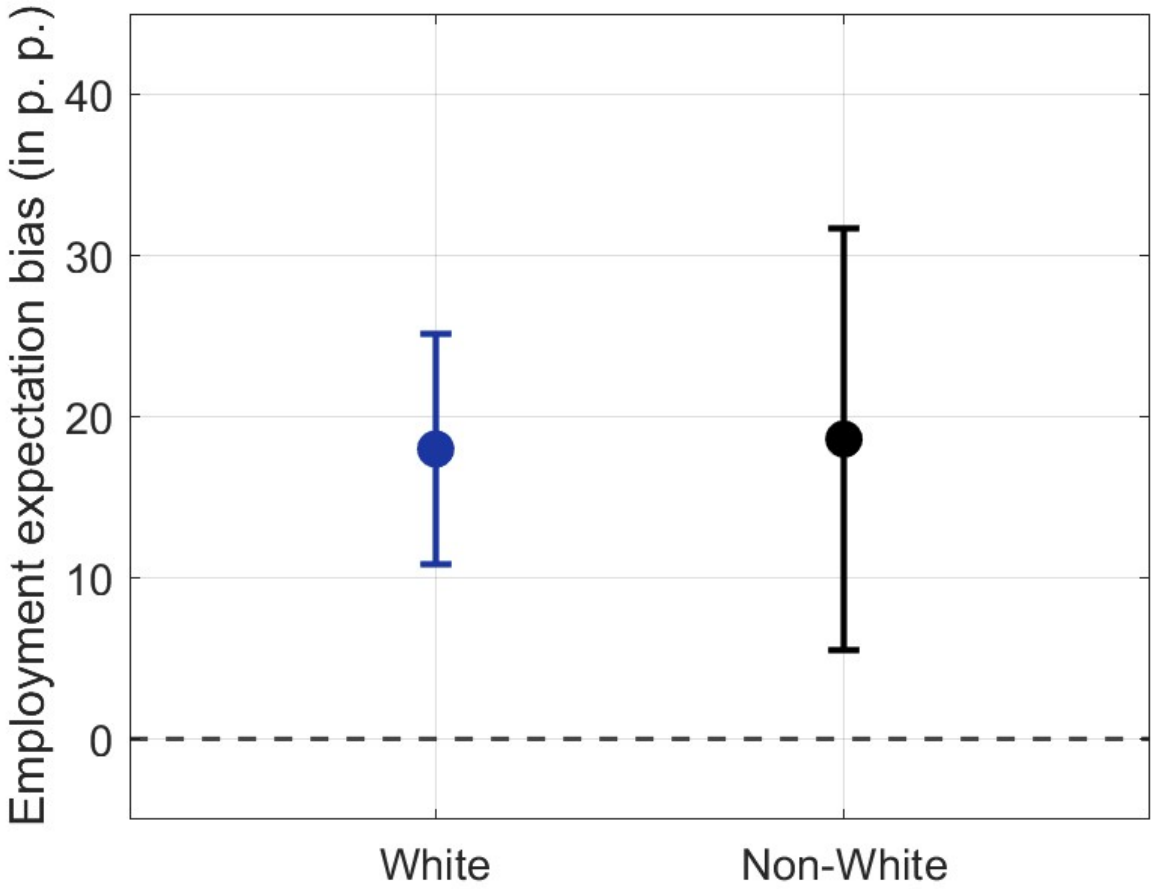


→ Less educated unemployed individuals seem to overestimate the employment probability more but the difference is not significant.

No Heterogeneity by Marital Status



No Heterogeneity by Race



Expected vs. Actual Transitions at the Individual Level

Does the expected employment probability predict actual transitions at the individual level?

	$\mathbb{1}[\text{Unemployed}_{i,t}, \text{Employed}_{i,t+4}] \times 100$	
	(1)	(2)
Expected Employment Probability$_{i,t}$	0.61***	0.61***
	(0.09)	(0.09)
Constant	6.22	4.17
	(5.86)	(9.42)
Observations	269	269
Year FE	–	✓

→ 1 p.p. higher expected employment probability is associated with 0.61 p.p. higher actual employment probability on average

→ The coefficient is < 1 indicating upward biased expectations

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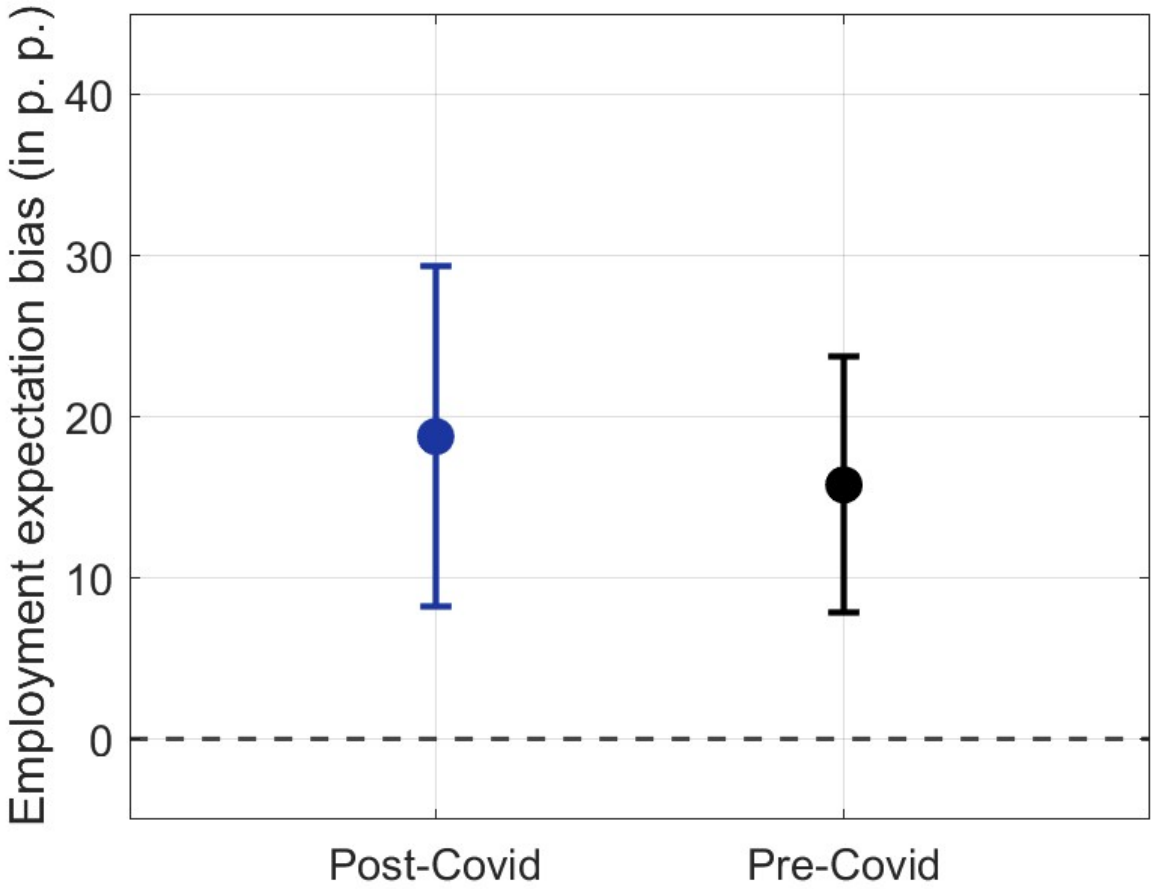
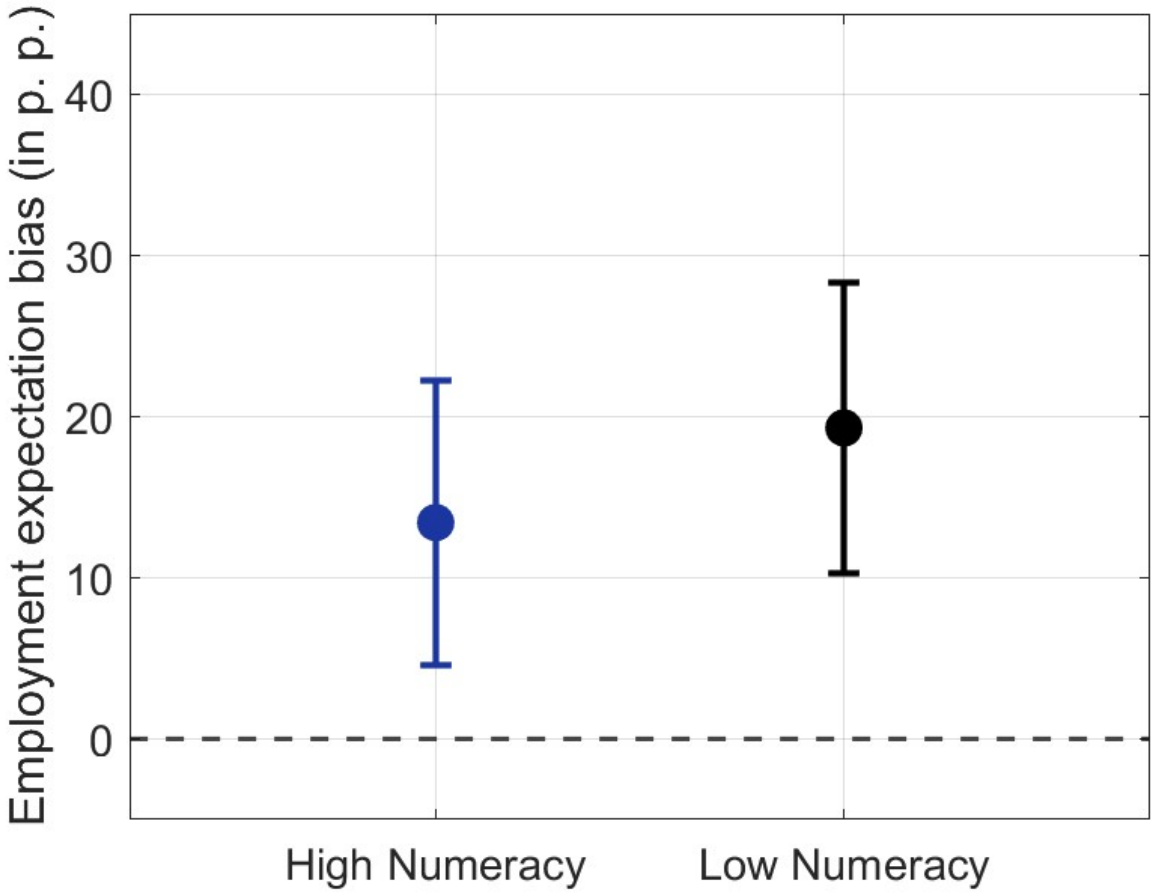
Robustness: No Difference Pre- vs. Post-Covid



Robustness: No Heterogeneity by Numeracy



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