

The retirement-consumption puzzle: a marital bargaining approach

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Abstract

Evidence from several countries reveals a substantial drop in household consumption around the age of retirement that is difficult to explain with life-cycle models. Using food consumption data from more than 550 households from the Panel Study of Income Dynamics for the years 1979–1986 and 1989–1992, we find that married couple households decrease their expenditures on both food consumed at home and away from home by about 9% following the retirement of the male household head. No significant decrease in consumption is found for single households, either in a sample of males or a pooled sample of single males and females. These results are consistent with a model of marital bargaining in which wives prefer to save more than their husbands do to support an expected longer retirement period, and relative control over household decisions is affected by control over market income. The pattern of the consumption decline, which is increasing in the age gap between husband and wife, lends further support to this interpretation.

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1. Introduction

Households appear to reduce their consumption expenditures substantially around the age of retirement. This pattern has been documented for the US by Hamermesh (1984), Mariger (1987), and Bernheim et al. (2001), for Canada by Robb and Burbridge (1989), and for the UK by Banks et al. (1998). The consumption decline appears to be fairly widespread across consumption categories, rather than concentrated on work-related expenses, and to take the form of a discrete drop at the year of retirement.

This behavior is puzzling, since life-cycle consumption models predict that households will want to smooth consumption (or rather, the marginal utility of consumption) when they experience a predictable drop in income, as at retirement. After examining alternative explanations that are consistent with forward-looking life-cycle behavior, other researchers have attributed this consumption drop to myopic behavior or to the systematic arrival of discouraging information at retirement. Understanding the cause of the consumption drop at retirement is important both to researchers who are trying to understand how individuals make complex decisions when the future is uncertain and to policy makers who are concerned about the adequacy of retirement savings by the baby boom generation.

In this paper, we explore an empirical hypothesis suggested by a non-unitary model of household behavior. If married couple households make decisions collectively (for example, by cooperative bargaining), and their ability to make binding agreements into the future is limited, then current consumption and savings decisions may be affected by each spouse's current control over resources. Most wives expect to live several years longer than their husbands, and therefore prefer, in the absence of perfect altruism, to consume less as the couple ages than husbands do. If the husband's bargaining power depends upon his current income or employment status, retirement from a career job will cause a relative deterioration in his influence on household decisions and a decline in the couple's consumption spending.

This story generates a testable hypothesis: we should see a consumption drop at retirement for married couple households, but not for single households who, though they also experience a drop in income, can be expected to act in a way that is consistent with life-cycle utility maximization by the unitary consumer. We also expect the consumption drop to be more pronounced for couples with more divergent interests — i.e. for couples in which the husband is substantially older than his wife. We use food consumption data from the Panel Study of Income Dynamics for the years 1979–1986 and 1989–1992 to test these hypotheses and find that expenditures drop at retirement by 8 to 10% for married couples, but do not decrease significantly for single households. The magnitude of the consumption drop is increasing in the relative age of the husband. These results are robust with respect to alternative specifications of the consumption equation and

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