

# The male/female earnings gap and female self-employment<sup>☆</sup>

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## Abstract

This paper examines the gender differences in the choice to become self-employed. Of particular interest is the relationship between the male/female earnings gap in wage and self-employment, and the male/female differences in the average predicted probability of self-employment. It has been argued that earnings inequality in wage-employment lead women to choose self-employment. However, it may be the case that inequality in the form of consumer discrimination causes an earnings gap between males and females in self-employment. If inequality is higher in self-employment than in wage-employment, then there would be females in wage-employment who would be in self-employment in the absence of inequality in both sectors.

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## 1. Introduction

It is observed in the US that the male/female earnings gap is larger in self-employment than in wage-employment. Devine (1994) showed that in 1990, the ratio of median female to male hourly earnings in wage and self-employment was 0.75 and 0.48, respectively.<sup>1</sup> It is also observed that the incidence of self-employment is much lower for females than males. Although males and

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<sup>1</sup> Devine (1994) uses the March 1991 Current Population Survey (CPS) and Income Supplement. The numbers presented here are for full-time, full-year workers.

females share many common determinants in their wage versus self-employment decision, it has been found that there are notable gender differences as well. Boden (1996, 1999a), Carr (1996), Connelly (1992), and Hundley (2000) find that the probability of self-employment for females is positively associated with marriage and having young children, whereas for males they find no significant relationship. Some of the above authors have also suggested that self-employment is seen by males as a way to capture the benefits of extra work effort. Boden (1999a) revealed that 11.9% of males claimed that the main reason they became self-employed was for the money or because the money was better, compared to 6.6% for females.<sup>2</sup> Hundley uses some of these gender differences in the probability of self-employment to explain differences in the earnings between males and females in the self-employment sector. In his paper, he argues that females enter self-employment because it offers them the opportunity to choose their own hours, enabling them to perform their role as the primary worker at home and to perform market work. If there is a certain amount of time an individual must work before they produce any output, then hourly earnings of females in self-employment would tend to be lower than their male counterparts who spend more time in the market. Hundley hypothesizes that marriage and the number of young children increases the work load of females at home and thus indirectly lowers their productivity in market work.

In his empirical work, he finds that the ratio of female to male hourly earnings in both employment sectors are almost identical and close to one when comparing similar males and females who are single with no children.<sup>3</sup> If one is married with no children, then the ratio remains close to one in self-employment but falls to 0.88 in wage-employment. This is contrary to his hypothesis that females choose self-employment to accommodate increased home work because of marriage. However, in line with his hypothesis, an increasingly positive difference between the ratio in wage-employment and self-employment opens as one has more children. A drawback of Hundley's work is that he does not control for actual labor market experience. Since experience is probably negatively correlated with marriage and the number of children, the lower returns to marriage and children for females compared to males could be exaggerated in the wage and self-employment sectors.

This paper synthesizes the research on the male/female differences in the probability of self-employment and the male/female differences in the earnings in wage and self-employment. Using the Canadian Survey of Labour and Income Dynamics (SLID) in 1994, the log hourly earnings gap in wage and self-employment are decomposed into the portion explained by differences in the endowment of productivity related variables and the residual—the portion explained by differences in the returns to these endowments. The residual portion of the earnings gap can be attributed to many things. As hypothesized by Hundley, differences in non-market productivity that cause one gender to specialize more in non-market work may be the cause. Alternatively, the residual gap could be explained by other unmeasured differences in productivity or differences in the reporting of earnings or hours worked between the sexes. This paper considers the effect of misreporting of hours worked and specialization in non-market activities in explaining the earnings gap in both employment sectors.

Using the coefficients from the earnings equations, the expected earnings differential between self and wage-employment is then calculated and used in the estimation of structural probit equations for male and female self-employment choice. In this way, the direct effect of individual

<sup>2</sup> Boden (1999a) uses data from the Contingent Worker supplement of the February 1995 CPS.

<sup>3</sup> He uses the final wave in 1986 of the National Longitudinal Study of the High School Class of 1972 and the Panel Study of Income Dynamics in 1989.

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