



Does the first job really matter? State dependency in employment status in Japan

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This paper examines whether the failure to obtain regular full-time employment at the time of graduation has a long-term impact on subsequent employment status. Using micro data from the Japanese General Social Surveys and the job opening ratio (*yuko kyujin bairitu*) as an instrument for entry-level employment status, I show that the observed correlation between current and entry-level employment status produces a true causal link, which is not attributable to sorting on unobserved aptitude. I also discuss various underlying mechanisms including social institutions and stigmatization. *J. Japanese Int. Economies* **21** (3) (2007) 379–402. Department of Economics, Columbia University, 420 w118th Street, New York, NY 10027, USA.
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1. Introduction

The recent growth of young people who are neither in full-time education nor in regular employment, the so-called “*freeters*,” has been drawing considerable attention as a major social phenomenon in Japan. More importantly, various economists (Mitani, 2001; Sakai and Highchi, 2005) have documented a strong correlation between the employment status at the time of graduation and employment prospects down the road. This observed correlation could in fact be causal, namely, that the employment status of the first job could have a real effect on employment prospects in the future. Nevertheless, the commonly accepted explanation for this correlation is

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that *freeters* are unable to commit to working. In economic parlance, the observed correlation is attributed to sorting by unobserved aptitude to regular employment. Despite this debate about *freeters*, the literature has not explored this important question in a rigorous way. This paper attempts to examine whether the adverse effects of failure to land a regular job at the time of graduation is spurious (due to unobserved heterogeneity) or real (causal).

This paper addresses the endogeneity of employment status by using the instrumental variable method. Specifically, I use micro data of the Japanese General Social Surveys (JGSS), which contains recall data of the employment status of one's first job as well as current employment status. As an instrument for the employment status of a first job, I use the job opening ratio (*yuko kyujin bairitsu*) in the year of completing education. This strategy is similar to Neumark (2002): since the job opening ratio is a macro index of labor demand, it is independent of heterogeneity within a cohort. I also provide evidence against direct effects of the instrument of a cohort level.

Even controlling for potential endogeneity, failure at labor market entry has a negative effect on the current probability of regular full-time employment. More precisely, people who failed to obtain a regular full-time job, due to lack of labor demand at the time of their entry, have a 40–50% less chance of having a regular full-time job at present. Given the aggregate level evidence for employers' preference for new graduates, this result is not surprising. However, most of the previous studies on the negative consequences of being a *freeteer*, including Mitani (2001) and Sakai and Higuchi (2005), have treated initial employment status as exogenous. Therefore, they have been subject to the criticism that observed persistency in employment status might be due to sorting on individuals' preferences or abilities. To the best of my knowledge, this is the first paper addressing this point among the studies on *freeters* or youth employment stability in Japan.

People who failed to obtain a regular job at entry continue to miss out on investments in employment-based human capital. Thus, increasing youth joblessness may harm the productivity of the Japanese work force in the long run. At the same time, rapid population aging means that, unless Japanese society accepts a huge number of immigrants, today's young workers must be relied upon to work to their full potential to support the economy. Consequently, deteriorating youth employment emerged as a major public concern in the early 2000s.¹ Under these circumstances, it is beneficial to shed light on the prolonged unstable employment suffered by young people who stumbled at entry to the labor market.

While Japan has been known for stable employment, it is true only for regular full-time employees. There is a clear distinction between regular full-time employees, called *seishain* in Japanese, and provisional employees. Provisional employees receive less protection by law, experience with almost double turnover rates and earn lower wages and lower returns to tenure.² In this sense, provisional employment in Japan forms the secondary market defined by Doeringer and Piore (1971), with internal labor markets for regular employees corresponding to the primary market. When there is a barrier between the two labor market, a person's current employment

¹ For further discussion about aging workforce and youth joblessness, see Hashimoto and Higuchi (2005) and Genda (2001).

² There is little penalty for terminating the employment contract of fixed-term workers, while it is hard to fire regular workers because of *kaikoken ranyou houri* ("just cause" required in judicial practice); Passet (2003) provides detail. For turnover, the Survey of Employment Trend in 2002 reports that the quitting rates of full-time and part-time workers are 14.2 and 26.9%, respectively. For wages, according to the Wage Census, average wages per hour in 2002 for 20–24-year-old full-time and part-time workers were 1193 yen and 904 yen, respectively. As a rough proxy for returns to tenure, the ratio of average annual payment (including bonus) of tenure 3–4 years to that of tenure 0 year for workers aged 25–29 is 1.36 for full-time the ratio, while for part-time it is only 1.07.

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