

The effect of transfer payments on the labor supply of single mothers

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Abstract

The Single Parent Family Law came into effect in Israel in 1992. It increased the income maintenance allowance paid to single mothers who have little or no income. In order to identify the effect of this legislative change on the labor supply of single mothers, the study uses a unique panel containing rich socioeconomic data. Applying a variety of econometric methods (difference-in-differences, panel regressions and propensity score matching), the study found that following the enactment of the law the labor supply of uneducated single mothers fell by about 10%, due to a decrease in the employment rate and working hours. However, from an economic perspective, the effect of the Law on the labor supply of single mothers is not very significant.

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1. Introduction

Since the early 1980s, income maintenance has been paid in Israel to families with little or no income, conditional on job search requirements. The Single Parent Family Law, which went into effect in April 1992, increased the level of income maintenance to divorced and never-married single mothers by an average of 20%. The proportion of single parent families in the population was about 10% at that time and about one quarter of them received income maintenance. The number of single parent families receiving income maintenance grew rapidly: from about 6000 in 1991 to about 24,000 in 2001. Benjamin Netanyahu, the finance minister in 2003–2005, claimed that the income maintenance created an enormous incentive to non-employment and that the government should eliminate the ‘inactivity trap’. Netanyahu cut the income maintenance to single mothers as part of wider ongoing program to increase the labor supply. His policy provoked a wide public protest, led by single mothers, to maintain the social security network.

Previous research had found evidence for the hypothesis that increase in income maintenance reduce the employment rate – the proportion of the working age population who are employed. Flug et al. (2005) found, using cross-sectional

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data, that the introduction of the Single Parent Family Law had indeed reduced the labor supply of single mothers between 1995 and 2003. Similar results were found in other countries. For example, in the US it was found that the increase in financial support and payments-in-kind received by single mothers in various states had reduced their employment rate (Moffitt, 2004). Meyer and Rosenbaum (2001) found that a reduction of 10% in the level of income maintenance (AFDC) led to an increase of the employment rate of single mothers of one percentage point, and that the increase was even larger among those with low levels of education and those with young children. Additional studies have pointed to the negative effect of income maintenance on the labor supply of single mothers in the UK (Gregg and Harkness, 2003) and Australia (Doiron, 2004).

This paper focuses on the effect of the Single Parent Family Law on the employment and wages of Jewish non-immigrant single mothers (hereinafter: single mothers). The research is based on an administrative panel data on the annual wages of mothers and their spouses for the period 1985–1995, combined with the population registry which includes annual data on family status and number of children in the household for the same period. To this database were added various types of socioeconomic traits taken from the population and housing census of 1995 (age, education etc.), as well as data on transfer payments paid by the National Insurance Institute. Although the cut-off of the research period at 1995 is a constraint imposed by data availability, focusing on the time period immediately following the legislative changes enables their effects to be isolated.

Based on a variety of econometric methods (difference-in-differences, panel regressions and propensity score matching), the research indicates that during the period 1992–1995, the employment rate of single mothers rose at a slower pace than that of similar married mothers, resulting in a relative decline of 3–4 percentage points. This characterized only divorced uneducated single mothers and single mothers living in the periphery – a population with a very low earning potential. The relative decline in the employment rate was a result of the decrease in both the probability of starting to work and the probability of continuing to work. The annual wage of uneducated single mothers who continued to work fell in comparison to that of similar married mothers, so that the wage differential, which was about 4% in favor of the former just prior to the introduction of the Single Parent Family Law (in 1991), disappeared following it (in 1995). This result is probably an indication that the working hours of uneducated single mothers decreased relative to similar married mothers.

The paper is divided into the followings sections: Section 2 describes the Single Parent Family Law. Section 3 describes the characteristic of the single mother population. Section 4 discusses methodological issues and describes the trends in the employment rate and wages before and after the legislation. Section 5 presents the econometric estimation results of the legislative changes impact on the labor supply of single mothers. This is followed by conclusions.

2. The Single Parent Family Law

The Single Parent Family Law went into effect in April 1992 and included an increase in the level of income maintenance for divorced and never-married single mothers (with children up to the age of 18), thus equalizing their status to that of widows with children (Table 1). For example, single mothers who entered the income maintenance program after March 1992 received an allowance equal to 40% of the average wage, compared to only 30% previously.

Table 1
Income maintenance level for single mothers (percentage of the average wage^a)

Number of children	Before the Single Parent Family Law: up until March 1992		After the Single Parent Family Law: April 1992–July 1994	After the Law to Reduce Poverty: from August 1994
	Regular rate	Special rate ^b		
1	30	37.5	40	42.5
2+	35	42.5	47.5	52.5

Source: the National Insurance Institute.

^a The monthly average wage was 3,005 New Israeli Shekel (NIS) in 1992. 1\$ = NIS 2.4590 in 1992 (on average).

^b Applies to those receiving income maintenance for more than two years.

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