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HOW MUCH DO STATE ECONOMICS AND OTHER CHARACTERISTICS AFFECT RETIREMENT BEHAVIOR?

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Economic conditions vary significantly across the states of the Union: the unemployment rate was 3 percent in Virginia, while neighboring Kentucky had unemployment of 5.7 percent (Bureau of Labor Statistics 2007); average wages were $29,500 in Maine versus $45,000 in Massachusetts (Bureau of Labor Statistics 2007); income taxes are 6 percent in Tennessee but Texas does not tax income (Tax Foundation 2007), etc. Despite these marked differences in factors that are associated with earnings and retirement income, little is known about the regional variations in retirement patterns and labor force participation decisions and the causes for such variations.

This study documents the existence and magnitude of the differences in labor force participation by state. In that sense it builds on the work of Black and Liang (2005) and von Wachter (2007) that analyzes the effect of local labor market conditions on the labor force participation and retirement decisions of older workers. It goes beyond these studies, however, by trying to determine whether the state variation is due to differences in the population or to unique aspects of the states.

Using the *Current Population Survey* for the period 1977-2007, we first document the differences in the labor force participation of men age 55-64 and estimate an equation that includes the labor market conditions, the nature of employment, and the employee characteristics in each state, as well as a pseudo replacement rate. These variables explain more than one-third of the total variation; even moving to a fixed-effects model only cuts the explanatory power by half.

To determine whether the explanatory power of the state-level variables reflect simply the aggregation of individuals within the state or unique state characteristics, we turn to the *Health and Retirement Study* (HRS). We estimate equations for the probability of working and for the expected retirement for men in their late fifties and early sixties. In each case, the first equation includes just the state-level variables and the second the state-level variables and the HRS demographic and economic for each individual. The results show that the state-level variables explain very little of the variation in the probability of working or the expected retirement age, but most of the state-level variables are statistically significant both before and after the inclusion of the HRS information. And some – most noticeably the unemployment rate – have an economically meaningful impact.

The findings of this paper suggest that states will face varying degrees of pressure as the baby boomers start to retire in the face of a contracting retirement income system, plummeting house prices, and a bear stock market. The findings also suggest that the best way for policymakers to help struggling states is to develop policies targeted at individuals with certain characteristics rather than states themselves.

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