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Executive Summary

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HEALTH SHOCKS AND COUPLES' LABOR SUPPLY DECISIONS

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For people approaching retirement age, unexpected negative health events are unfortunately quite common. For example, men and women participating in the Health and Retirement Study (HRS), a recent, nationally representative survey of the young elderly, have a 5% chance of having a heart attack, stroke, or new cancer diagnosis, a 10% chance of being diagnosed with a new chronic illness, and a 3% chance of having an accidental injury over a twoyear period.

This paper examines the effects of negative health events on the labor supply of both the affected individual and his or her spouse using the HRS. While past work has found that negative health events are associated with a reduction in labor supply by the affected individual, much less is known about the labor supply response of the spouse. The spouse's response is of interest because it has the potential to either exacerbate or insulate the family against the drop in lifetime income suffered as a result of the health event. The spouse's labor supply response may differ across families depending on the size of the drop in lifetime income, caregiving opportunities and complementarity of leisure within the family, and the need to provide health insurance for the family, and may be "crowded out" by the existence of public insurance benefits such as Disability Insurance.

In the analysis, negative health events are found have a large effect on the labor supply of affected men and women, particularly when accompanied by large changes in functioning. The onset of a heart attack or stroke accompanied by new difficulty in performing four activities of daily living is projected to decrease men's hours by 1,030 or to raise the probability of men's exiting the labor force by 42 percentage points. The comparable effect for women is a 654 decrease in hours or a 31 percentage point increase in the probability of labor force exit.

The spouse's labor supply response to negative health events is found to be small and insignificant in aggregate, suggesting that health shocks typically represent real financial losses for the family. However, there is evidence of offsetting labor supply responses for different families, indicating that behavior is affected by factors such as the need to provide health insurance, the presence of other potential caregivers, and the importance of the lost income. Interestingly, such offsetting responses are typically significant for men but not for women, which is consistent with some previous work that has found men to be more responsive to their wives' financial incentives from Social Security and pensions. There is also some evidence that Disability benefits crowd out the spouse's labor supply, suggesting that they do not raise family income substantially.

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