Hallock: “Job Loss and the Fraying of the Implicit Employment Contract”

1. What are employment contracts, and how are they changing?
   A. Spot market: wages and employment can change daily, considerations about the future are largely absent e.g., day laborers, temp agencies
   B. Contract market: have an “invisible handshake” or tacit understanding about the future (e.g., layoffs, job tenure, etc.)
   C. Explicit/formal contracts: written, specify hours, pay, job duties, term of employment, fringe benefits, etc.
   D. Implicit/informal contracts: unwritten; includes expectations (sometimes vague) about length of employment, loyalty to the firm, etc.
   E. Contracts can be a form of insurance provided by firm to workers (risk of job loss is especially serious for most workers) – related to firm’s policy on layoffs vs. job cuts
   F. Hallock concludes:
      * implicit contracts have changed in ways that negatively affect workers, while producing only modest benefits for firms
      * so it’s unclear who benefits from these changes in the implicit contract
      * “if employers have become less involved with cushioning the blow of unemployment and avoiding layoffs where possible, then public policy might have a role to play”
2. Changes in employment tenure and layoffs
   A. Reliable layoff data hard to get (e.g., true layoff vs. firing for cause); Wall St. Journal layoff announcement data (with reasons for layoff) may be particularly problematic (e.g., self-serving PR)
   B. Despite the caveats, data seem to indicate:
      * layoffs occur more quickly, are larger than in the past
      * “no-layoff” companies have begun to have layoffs (e.g., Enterprise)
      * reasons given for layoffs have changed over time
        -- “slump in demand” reason given less frequently recently
        -- “reorganization” given more in 80’s-90’s but now given less often
        -- “cost control” reason has increased substantially
      * layoff announcements now occur at all points of the year, not just early or late in the year (Dec.-Jan.)

3. Studies of displaced workers
   A. “Displacement” = lost/left a job because of plant/company moved or closed; or no work to do; or position or shift abolished
   B. 1/3 of fulltime workers who are displaced not employed two years later, another 13% are holding part-time jobs
   C. earnings losses for displaced workers (esp. relative to workers who stayed) can be substantial – 13-17% plus
4. Job tenure and long-term employment
   A. between 1973-2006,
      * mean job tenure (time on the job) fell, esp. for older men
      * fraction of workers working at least 10, or 20, years has fallen
   B. these effects are for the private sector –
      tenure in public sector may actually have gone up
   C. more “churning” (short-term jobs)
   D. why has the employment contract changed? possible reasons…
      -- decline in unionization
      -- employers more powerful now than before
      -- layoffs (and unemployment) more socially acceptable,
         entail less stigma for both firms and workers

5. Effects of job loss on workers
   A. job loss a “blessing in disguise”? economically-efficient job loss?
      reallocate labor whenever marginal productivity < wage,
      whenever workers and firms are mismatched
   B. but there can be negative effects of job loss, including…
      -- long periods of unemployment
      -- big (and long-lasting) reductions in earnings: 15, 25, 33, 40%?
      -- poor physical and emotional health (but could it be the other way around?)
6. Effects of job loss on firms
   A. Do layoffs benefit the firms? (if not, why do firms have them?) or do they just benefit executives?
   B. Use changes in stock prices to see if layoffs benefited firms:
      “share price reaction to job loss announcements was typically negative in the 1970’s, but seems to have flattened out and more often become positive by the middle to end of this decade. In essence, layoff announcements were bad for firm stock prices decades ago, and are clearly less bad (and, in some years, even weakly positive) now.” (p. 83)
   C. setup: event-history analysis
      regress the company’s daily stock return, $R_{it}$,
      on the value-weighted return for the market, $R_{mt}$: $R_{it} = \alpha_i + \beta_i R_{mt}$
      (use data in the past, e.g., 30-60 days before the layoff)
      “excess returns” for days around the layoff are $R_{it} - [\alpha_i + \beta_i R_{mt}]$
      where the calculations use the estimates of $\alpha_i$ and $\beta_i$
   D. see Figure 5: slight evidence of increase (less negative/more positive) in excess returns
   E. possibly: in old days, layoffs indicated the company was in bad shape; more recently, layoffs indicate that company’s future will be better?
   F. Table 2: excess returns do not seem to be “explained” by reasons given for the layoffs, and most recently are minimal
   H. Hallock (1998): firms that announce layoffs pay their CEO’s more, give them larger raises – but controlling for firm X’s, this effect vanishes
7. Are there alternatives to layoffs?

A. “shared sacrifice” (or just different sacrifice):
   -- widespread pay cuts, work sharing, voluntary furloughs/unpaid vacations, shorter hours, etc.
   -- allow “choice” in layoffs, e.g., buyouts, early retirement, etc.
   -- pay workers (e.g., newly-hired lawyers) to work at base pay or less for a charity for a year (NB: avoids losing the firm’s investment in hiring costs)

B. problems: adverse effects on morale

C. possible government program: Work-Sharing Unemployment Insurance if all of a firm’s workers take a 20% cut in hours, they can all get WSUI – a pro-rated share of full-time Unemployment Insurance (allows firms to save on hiring/rehiring costs)

D. other countries have some combination of…
   -- advance notification requirements
   -- two-tier labor markets (some with job protection, others without) (in US, this takes the form of outsourcing, temp workers)

E. provide retraining, job search assistance, relocation assistance