The Application of Oaxaca Decomposition Analysis to the Change of Females' Probability of Work

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Female-headed families constitute the prime eligibility group for welfare programs. With the rising illegitimate birth rate and the high rate of divorce, the size of the female-headed population is expected to grow, increasing the incidence of welfare dependence. Since U.S. Congress passed a new welfare bill which eliminates the federal guarantee of cash assistance for poor children (AFDC) in 1996, new AFDC program, TANF (Temporary Assistance for Needy Families Programs), emphasizes on self-sufficiency for women on welfare through workfare.

There is a route to self-sufficiency for a female on welfare: work. The probability of work (workability) has changed over time period. The change of workability over time period can be attributed to the change of the average sample characteristic and the change of the coefficients. This paper analyzes the change of workability, decomposing it into the change of the average sample characteristic and the change of the coefficients. During the sample period (1975~1987), women's workability improved mainly due to the improvement of their personal characteristics. If this is the case, welfare policies should emphasize on improvement of job market opportunities for women to strengthen the effectiveness of welfare policies.

Key Word: The Probability of Work, Decomposition Analysis, Welfare Policy

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I. Introduction

In 1996, U.S. Congress passed a new welfare bill which eliminates the federal guarantee of cash assistance for poor children (AFDC). Instead it provides states with a fixed amount of federal money to run their new AFDC programs, TANF (Temporary Assistance for Needy Families Programs). According to TANF, the head of every family on welfare would have to work within two years, or the family would lose benefits. Lifetime welfare benefits would be limited to five years. The latest welfare reform by U.S. Congress moves in the right direction to improve the effectiveness of the welfare program focusing on the self-sufficiency for a female on welfare: work. Therefore thorough analysis on a woman's workablility (probability of work) is needed to strengthen the effectiveness of welfare policies.

The probability of work has changed over time period. The change of workability over time period can be attributed to the change of the average sample characteristic and the change of the coefficients (job market situations). Finding out which change is the dominant effect and measuring the magnitude of effect would be a crucial pre-step before setting up welfare policies. It is the purpose of this paper to decompose the change of probability of work and to estimate the amount attributable to the change of the average sample characteristic and the change of the coefficients. The analysis in this paper is based on women who are aged between 16 and 60 by using

data from the Michigan Panel Study of Income Dynamics (PSID) between 1975 and 1987.

Ⅱ. A Model of Decomposition Analysis

A Model of decomposition analysis used in this paper is called Oaxaca decomposition analysis (Oaxaca, 1973). Oaxaca uses his decomposition analysis to explain the male-female wage differential in terms of productive characteristics (endowments) and treatment effects (discrimination). According to Oaxaca (1973), culture, tradition, and overt discrimination tend to make restrictive the terms by which women may participate in the labor force. These influences combine to generate an unfavorable occupational distribution of female workers vis-a-vis male workers and to create pay difference between males and females within the same occupation. The result is a chronic earnings gap between male and female full-time, year-round workers. In his paper (1973), Oaxaca estimates the average extent of discrimination against female works in the Unites States and provides a quantitative assessment of the sources of male-female wage differentials.

According to Oaxaca, discrimination against females can be said to exist whenever the relative wage of males exceeds the relative wage that would have prevailed if males and females were paid according to the same criteria. Oaxaca formalizes his notion by proposing the concept of a discrimination coefficient (D) as a measure of discrimination:

$$D = \frac{W_m/W_f - (W_m/W_f)^0}{(W_m/W_f)^0} \quad \cdots\cdots (1)$$

where

(W_m/W_f) = the observed male-female wage ratio

and

$(W_m/W_f)^0$ = the male-female wage ratio in the absence of discrimination

An equivalent expression in natural logarithms is

$$\ln(D+1) = \ln(W_m/W_f) - \ln(W_m/W_f)^0 \quad \cdots\cdots (2)$$

Since $(W_m/W_f)^0$ is unknown, the estimation of D is equivalent to estimating $(W_m/W_f)^0$. On the basis of either of his two assumptions, the male-female wage ratio that would exist in the absence of discrimination can be estimated: If there were no discrimination, 1) the wage structure currently faced by females would also apply to males; or 2) the wage structure currently faced by males would apply to females. These assumptions implicate that females (males) would on average receive in the absence of discrimination the same wages as they presently receive, but that discrimination takes the form of males (females) receiving more (less) than a nondiscriminating labor market would award them.

Oaxaca used ordinary least squares estimation of a wage equation in his paper to estimate the wage structure. The wage equation he used in paper is:

$$\ln(W_i) = Z_i'\beta + u_i \qquad i = 1, \ldots\ldots n \quad \cdots\cdots (3)$$

where

W_i = the hourly wage rate of the i-th worker,

Z_i' = a vector of individual characteristics,
β = a vector of coefficients,
u_i = a disturbance term

When the male-female wage differential is expressed in natural logarithms, the wage differential can be decomposed into the effects of discrimination and the effects of differences in individual characteristics. The decomposition method used by Oaxaca is as follows:

Let

$$G = \frac{\overline{W_m} - \overline{W_f}}{\overline{W_f}}$$

$$\ln(G+1) = \ln(\overline{W_m}) - \ln(\overline{W_f}) \quad \cdots\cdots (4)$$

where $\overline{W_m}$ and $\overline{W_f}$ are the average hourly wages for males and females, respectively. From the properties of ordinary least squares estimation, we have

$$\ln(\overline{W_m}) = Z_m'\widehat{\beta_m} \quad \cdots\cdots (5)$$

$$\ln(\overline{W_f}) = Z_i'\widehat{\beta_f} \quad \cdots\cdots (6)$$

where

Z_m' and Z_f' = the vectors of mean values of the regressors for males and females, respectively
$\widehat{\beta_m}$ and $\widehat{\beta_f}$ = the corresponding vectors of estimated coefficients

Upon substitution of (5) and (6) into (4), we obtain

$$\ln(G+1) = Z_m'\widehat{\beta_m} - Z_f'\widehat{\beta_f} \quad \cdots\cdots (7)$$

If we let

$$\triangle Z' = Z_m' - Z_f' \quad \cdots\cdots (8)$$

$$\triangle \hat{\beta} = \hat{\beta}_f - \hat{\beta}_m \quad \cdots\cdots (9)$$

and substitute $\hat{\beta}_m = \hat{\beta}_f - \triangle \hat{\beta}$ in (7), the male-female wage differential can be written as

$$\ln(G+1) = \triangle Z' \hat{\beta}_f - Z_m' \triangle \hat{\beta} \quad \cdots\cdots (10)$$

Since the current female wage structure would apply to both males and females in a nondiscriminating labor market, it can be shown that

$$\ln\left(\frac{\widehat{W_m}}{W_f}\right)^0 = \triangle Z' \hat{\beta}_f \cdots\cdots (11)$$

$$\ln(\widehat{D+1}) = -Z_m' \triangle \hat{\beta} \quad \cdots\cdots (12)$$

Therefore expressions (11) and (12) represent the decomposition of the wage differential into the estimated effects of differences in individual characteristics and the estimated effects of discrimination, respectively.

An alternative decomposition of the wage differential is obtained by substituting $\hat{\beta}_f = \triangle \hat{\beta} + \hat{\beta}_m$ in (7):

$$\ln(G+1) = \triangle Z' \hat{\beta}_m - Z_f' \triangle \hat{\beta} \quad \cdots\cdots (13)$$

Also it can be shown that

$$\ln\left(\frac{\widehat{W_m}}{W_f}\right)^0 = \triangle Z' \hat{\beta}_m \quad \cdots\cdots (14)$$

$$\ln(\widehat{D+1}) = -Z_f' \triangle \hat{\beta} \quad \cdots\cdots (15)$$

Ⅲ. Decomposition Analysis of the Change of Probability of work

1. Specification and Empirical Results of Work Equation

We define

W (work status) = 1 if labor income is larger than state AFDC maximum guarantee amount 0 otherwise

The probability of work, P(W=1), is as follows:

$$P(W=1) = P_r\{(\beta_w' X_w + u_w) > 0\} \quad \text{..... (16)}$$

where β_w is the parameter vector of the work equation, X_w is a vector of variables determining the work decision, and u_w is a random error term of the work equation. Table 1~3 present parameter estimates from the probit model of work. Age (AGE) and age squared (AGESQ) have significant impacts on the probability of work. The coefficients for age and age squared suggest that age has at first a positive and then a negative effect on the probability of work. Living in a large city leads to an increase in the probability of work.

Education (ED) has a strong positive effect on the probability of work. Women with 12 years or more education are more likely to work than women with less education. The work equation also shows that the probability of work increases with fewer children (KID).

From 1975 to 1980, the coefficient on the race dummy variable (BLACK) has an unexpected positive though insignificant effect on the probability of work. However, from 1981 to 1987, the coefficient

on the race dummy variable has the expected negative effect on the probability of work. The negative coefficient on the BLACK variable after 1980 could be a result of work disincentive effects generated by the AFDC program. The work equation shows that the probability of work increases with lower unemployment rates (UR) and less family income (OTINCOME). These demographic correlates of work are the same as those found in many previous female labor supply studies.

Table 1. Probit Estimate of the Probability of Work (1975～1977)

Variable	1975	1976	1977
CONSTANT	-1.123 (-3.531)**	-1.055 (-3.426)**	-1.379 (-4.326)**
AGE	0.93E-01 (5.380)**	0.86E-01 (5.102)**	0.104 (5.984)**
AGESQ	-0.12E-02 (-5.379)**	-0.11E-02 (-5.145)**	-0.13E-02 (-6.234)**
CITYSIZE	0.10E-06 (1.690)	0.12E-06 (2.219)**	0.13E-06 (2.102)*
ED	0.416 (6.457)**	0.352 (5.759)**	0.494 (7.741)**
BLACK	0.135 (2.139)*	0.155 (1.922)	0.39E-01 (0.628)
KID	-0.102 (-9.769)**	-0.104 (-9.873)**	-0.71E-01 (-6.664)**
UR	-0.25E-01 (-2.776)**	-0.30E-01 (-3.369)**	-0.31E-01 (-2.695)**
OTINCOME	-0.72E-05 (-4.379)**	-0.66E-05 (-4.493)**	-0.84E-05 (-5.064)**
GUARANTEE	-0.13E-03 (-6.110)**	-0.10E-03 (-4.826)**	-0.11E-03 (-5.592)**

Notes: t-ratios are in parentheses

* Significant at the 5% level, ** Significant at the 1% level

Table 2. Probit Estimate of the Probability of Work (1978～1983)

Variable	1978	1979	1980
CONSTANT	-1.064 (-3.454)**	-1.540 (-6.110)**	-1.744 (-7.227)**
AGE	0.85E-01 (5.213)**	0.121 (8.847)**	0.126 (9.666)**
AGESQ	-0.11E-02 (-5.663)**	-0.16E-02 (-9.238)**	-0.16E-02 (-9.902)**
CITYSIZE	0.71E-07 (1.146)**	0.13E-06 (2.358)*	0.73E-07 (1.311)*
ED	0.428 (6.890)**	0.516 (9.179)**	0.552 (10.248)**
BLACK	0.63E-01 (1.058)	0.79E-03 (0.014)	0.84E-01 (1.601)
KID	-0.74E-01 (-6.989)**	-0.71E-01 (-7.015)**	-0.70E-01 (-6.753)**
UR	-0.15E-01 (-1.388)	-0.40E-01 (-3.603)**	-0.47E-01 (-5.115)**
OTINCOME	-0.40E-05 (-3.583)**	-0.71E-05 (-8.154)**	-0.12E-05 (-2.707)**
GUARANTEE	-0.11E-03 (-5.802)**	-0.12E-03 (-7.016)**	-0.10E-03 (-5.752)**

Variable	1981	1982	1983
CONSTANT	-2.008 (-7.923)**	-1.862 (-7.391)**	-2.377 (-9.173)**
AGE	0.146 (10.807)**	0.145 (10.940)**	0.167 (12.512)**
AGESQ	-0.18E-02 (-10.871)**	-0.18E-02 (-11.041)**	-0.21E-02 (-12.479)**
CITYSIZE	0.92E-07 (1.499)	0.18E-06 (3.145)**	0.17E-06 (2.827)*
ED	0.538 (9.438)**	0.566 (10.081)**	0.537 (9.524)**
BLACK	-0.126 (2.249)*	-0.133 (-2.493)	-0.165 (-2.968)**
KID	-0.68E-01 (-6.230)**	-0.64E-01 (-5.876)**	-0.88E-05 (-7.233)**
UR	-0.48E-01 (-4.958)**	-0.45E-01 (-5.097)**	-0.31E-01 (-3.470)**
OTINCOME	-0.69E-05 (-7.247)**	-0.66E-05 (-8.216)**	-0.85E-05 (-7.124)**
GUARANTEE	-0.97E-04 (-4.870)**	-0.14E-03 (-7.106)**	-0.11E-03 (-5.925)**

Notes: t-ratios are in parentheses

* Significant at the 5% level, ** Significant at the 1% level

Table 3. Probit Estimate of the Probability of Work (1984～1987)

Variable	1984	1985	1986	1987
CONSTANT	-2.301	-2.366	-1.960	-1.790
	(-8.953)**	(-9.167)**	(-8.093)**	(-7.586)**
AGE	0.166	0.172	0.150	0.140
	(12.378)**	(13.123)**	(12.394)**	(11.653)**
AGESQ	-0.21E-02	-0.21E-02	-0.19E-02	-0.17E-02
	(-12.453)**	(-13.180)**	(-12.329)**	(-11.506)**
CITYSIZE	0.12E-06	0.11E-07	0.78E-07	0.11E-06
	(1.197)**	(-0.181)**	(1.276)	(1.914)
ED	0.630	0.638	0.608	0.702
	(11.050)**	(11.256)**	(11.260)**	(13.265)**
BLACK	-0.150	-0.175	-0.138	-0.190
	(-2.656)**	(-3.173)**	(-2.662)**	(-3.751)**
KID	-0.80E-01	-0.81E-01	-0.84E-01	-0.70E-01
	(-6.244)**	(-6.720)**	(-7.537)**	(-6.370)**
UR	-0.50E-01	-0.48E-01	-0.54E-01	-0.71E-01
	(-5.481)**	(-4.960)**	(-5.813)**	(-6.744)**
OTINCOME	-0.50E-05	-0.52E-05	-0.33E-05	-0.62E-05
	(-4.822)**	(-8.742)**	(-5.132)**	(-12.251)**
GUARANTEE	-0.13E-03	-0.14E-03	-0.14E-03	-0.12E-03
	(-6.356)**	(-5.868)**	(-6.693)**	(-6.128)**

Notes: t-ratios are in parentheses
* Significant at the 5% level, ** Significant at the 1% level

The AFDC guarantee (GUARANTEE) has a strong negative effect on the probability of work. The probit estimates of work show that a woman is more likely to choose not to work with the higher welfare guarantee. The coefficient on the AFDC guarantee (GUARANTEE) indicates that a $1000 increase in the AFDC guarantee, for example, in 1980, will lead to a 0.042 decrease in the probability of work. This result shows that the AFDC benefits designed to help alleviate poverty discourages work, worsening poverty.

2. Decomposition Analysis

The estimated probability of work (workability) changed between 1975 and 1987. During this period, the estimated probability of work, P^(W=1), increased from 0.423 to 0.619. The change in the estimated probability of work during the sample period is attributed to the change of the average sample characteristics and the change of the coefficients. We need to decompose differentials of the estimated probability of work between 1975 and 1987 to find out which change is the dominant effect. In this paper, we use Oaxaca's decomposition analysis to explain the change of the probability of work between 1975 and 1987 in terms of the sample characteristics and the estimated coefficients. It starts with an equation explaining the probability of marriage, P(W=1), for the years 1987 and 1975.

$$W_t = \text{Probit}(\beta_t X_t), \quad t=\text{year 1987, year 1975} \quad \text{..... (17)}$$

where W is the probability of work, β is a vector of the work equation coefficients to be estimated, and X is a vector of variables determining workability.

The difference in the probit estimates of probability of work between 1987 and 1975 is written as:

$$\overline{W_{87}} - \overline{W_{75}} = \text{Probit}(\widehat{\beta_{87}}\,\overline{X_{87}}) - \text{Probit}(\widehat{\beta_{75}}\,\overline{X_{75}}) \quad \text{..... (18)}$$

where $\overline{W_{87}}$, $\overline{W_{75}}$, $\widehat{\beta_{87}}$, $\widehat{\beta_{75}}$ are the means of probability of work in 1987 and 1975, and the coefficient estimates for work equations in 1987 and 1975, while $\overline{X_{87}}$, $\overline{X_{75}}$ are the average sample characteristics of 1987 and 1975 respectively.

Equation (18), which is $\triangle \overline{W}$, can be expressed as:

$$\triangle \overline{W} = \{\Pr obit(\widehat{\beta_{87}}\overline{X_{87}}) - \Pr obit(\widehat{\beta_{87}}\overline{X_{75}})\} + \{\Pr obit(\widehat{\beta_{87}}\overline{X_{75}}) - \Pr obit(\widehat{\beta_{75}}\overline{X_{75}})\} \quad \cdots\cdots\cdots\cdots\cdots (19)$$

The first expression of the right-hand side of equation (19) is the part of the differential that is attributed to differences in sample characteristics between 1987 and 1975. The second expression on the right-hand side of equation (19) is the part of the differential attributable to differences in coefficients that represent the difference in the market between 1987 and 1975.

The results of the decomposition analysis are presented in Table 5, which reports the decomposition of differential of the estimated probability of work between the years 1987 and 1975. The estimates of the probability of work, $\widehat{P}(W=1)$, in 1987 and 1975 are 0.619 and 0.424 respectively. The estimated probability of work changed by 0.194 during the sample period. The amounts attributable to the change in coefficients and sample characteristics are 0.002 and 0.192 respectively. During the sample period, women's workability improved mainly due to the improvement of their personal characteristics. Table 6 presents the estimates of probability of work between 1975 and 1987 evaluated at the average sample characteristics and the coefficients of 1975 and 1987. It also shows that the probability of work increased due to the improvement of the sample characteristics between 1975 and 1987.

The stagnating job market during the sample period could be due to shifts in the structure of labor demand. Demand for low-skilled workers fell because of collapsing demand for the goods or services

produced by industries such as manufacturing, in which low-skilled labor is concentrated.

Table 5. Decomposition of Differentials of the Estimated Probability of Work, P(W=1) between the Years 1987 and 1975

	A[1)4)]	B[2)]	C[3)]
P(W=1)	0.194	0.192	0.002

Notes : 1) Differential between the years 1987 and 1975
2) Amount attributable to differences in sample characteristics
3) Amount attributable to differences in coefficients
4) A = B + C

$$= \{\Pr obit(\widehat{\beta_{87}}\overline{X_{87)}} - \Pr obit(\widehat{\beta_{87}}\overline{X_{75}})\} + \{\Pr obit(\widehat{\beta_{87}}X_{75)} - \Pr obit(\widehat{\beta_{75}}X_{75})\}$$

Table 6. Estimates of the probability of work, $P(W=1)=\Phi(\beta'_{w,t}\ \overline{X}_{w,t})$, between 1975 and 1987 evaluated at the average sample characteristics ($\overline{X}$) and the coefficients (β) of 1975 and 1987

Year	$\Phi(\beta'_{w,t}\ \overline{X}_{w,1975})$	$\Phi(\beta'_{w,t}\ \overline{X}_{w,1987})$	$\Phi(\beta'_{w,1975}\ \overline{X}_{w,t})$	$\Phi(\beta'_{w,1987}\ \overline{X}_{w,t})$
1975	0.424	0.578	0.424	0.426
1976	0.404	0.549	0.450	0.471
1977	0.418	0.551	0.479	0.529
1978	0.443	0.563	0.491	0.553
1979	0.403	0.556	0.510	0.554
1980	0.433	0.590	0.514	0.524
1981	0.434	0.577	0.519	0.525
1982	0.448	0.610	0.528	0.503
1983	0.460	0.595	0.543	0.531
1984	0.433	0.604	0.554	0.570
1985	0.422	0.602	0.568	0.591
1986	0.430	0.616	0.562	0.589
1987	0.426	0.619	0.578	0.619

Note: t = from 1975 to 1987

Ⅳ. Concluding Remarks

Female-headed families constitute the prime eligibility group for welfare programs. With the rising illegitimate birth rate and the high rate of divorce, the size of the female-headed population is expected to grow, increasing the incidence of welfare dependence. Since U.S. Congress passed a new welfare bill which eliminates the federal guarantee of cash assistance for poor children (AFDC) in 1996, new AFDC program, TANF (Temporary Assistance for Needy Families Programs), emphasizes on self-sufficiency for women on welfare through work.

There is a route to self-sufficiency for a female on welfare: work. The probability of work (workability) has changed over time period. The change of workability over time period can be attributed to the change of the average sample characteristic and the change of the coefficients. This paper analyzes the change of workability, decomposing it into the change of the average sample characteristic and the change of the coefficients. The empirical results show that the estimated probability of work changed by 0.194 between 1987 and 1975. The amounts attributable to the change in coefficients and sample characteristics are 0.002 and 0.192 respectively. During the sample period, women's workability improved mainly due to the improvement of their personal characteristics. If this is the case, welfare policies should emphasize on improvement of job market opportunities for women to strengthen the effectiveness of welfare policies.

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Summary

女性의 就業能力 分析에 관한 硏究

洪 碩 杓

빈곤층 편모가정은 미국 공공부조 프로그램의 주된 대상이 되어 왔다. 이혼율의 증가와 배우자 없이 자녀를 가지는 현상이 늘어나면서 편모가정은 증가하고 있으며, 따라서 공공부조 프로그램에 대한 의존도 이에 상응하여 늘어날 것으로 예상된다. 1936년에 시작된 생계비 지원 위주의 아동부양가족 프로그램인 AFDC는 1997년부터 저소득 가정을 위한 한시적 지원프로그램인 TANF로 바뀌면서 근로를 통해 자활을 이룰 수 있는 취업지원 정책 중심으로 변화하였다. 따라서 공공부조 프로그램이 효과적으로 운영되기 위해서는 여성의 취업할 능력에 대한 분석이 우선적으로 수행되어야 한다.

여성은 근로활동을 통한 자활을 통해 공공부조 프로그램의 의존에서 자립할 수 있다. 자활을 위한 여성의 취업 능력은 변화하게 되는데 이러한 변화는 교육수준 등과 같은 여성 개인 특성의 변화와 외부요인, 즉, 노동시장의 변화로 구분할 수 있다. 본 연구에서는 여성의 취업능력의 변화를 여성 개인의 특성 변화와 노동시장의 변화로 분해하여 분석하였다. 분석결과 1975년부터 1987년까지 여성의 취업능력은 향상되었는데 노동시장의 변화보다는 여성 개인의 특성 향상이 주된 요인으로 밝혀졌다. 따라서 근로를 통해 자활을 이룰 수 있는 취업지원 정책 중심의 공공부조 프로그램이 더욱 효과적으로 수행되기 위해서는 여성이 노동시장에 참여할 수 있는 기회를 늘려주는 정책이 우선되어야 할 것이다.