MBS 93-04
Implicit Contracts and the Determination of Hours Worked
Paul Beaudry and John Di Nardo

This paper examines whether the behavior of wages and hours worked exhibit features predicted by the presence of implicit contract models. In contrast to previous work on contracts, we concentrate on the implications of the model that arise directly from considering the labor market as a market for contract. In particular, we argue that in the presence of contract, wages and hours worked should display "Year of Entry" effects. Moreover these effects should have opposite impact on wages relative to hours, since a year where the labor market is tight allows a worker to lock in to a high wage contract and therefore buy back leisure. Using data from the PSID we find evidence of both the year of entry effects and of their predicted interrelation. We exploit the simple structure of the risk sharing model to examine how labor supply can be analyzed in the presence of contracts and use the framework to shed light on the debate surrounding the value of the intertemporal elasticity of substitution.