How Extended Unemployment Benefits for Older Workers Affect Labor Market Exit, Disability Enrollment, and Social Security Claims

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Key Findings and Policy Implications
This paper examines how extended unemployment insurance (UI) benefits targeted to older workers affect early retirement and social welfare. The analysis focuses on Austria’s regional extended benefit program, which extended regular UI benefits to up to 4 years. The study relies on two data sources. The Austrian Social Security Database (ASSD) provides longitudinal information on labor market and earnings histories of all private-sector workers in Austria. The Austrian unemployment register contains information on the socioeconomic characteristics and place of residence of unemployed workers. The paper finds that:

- Extended UI benefits have a strong effect on the incidence of early retirement. The probability that a job loser aged 50-54 permanently withdraws from the labor market increases by 16.2 percentage points when the worker is eligible for the regional extended benefit program. Among job losers aged 55-57, the incidence of early retirement increases by 14.8 percentage points for those eligible for the program.

- Extended UI benefits also affect the pathways into early retirement. For workers aged 50-54, program complementarity – increased take-up of UI followed by higher DI benefit claims and/or retirement benefits – is quantitatively important. The 16.2 percentage point increase in early retirement is associated with a 12.2 percentage point increase in a subsequent DI take-up. For workers aged 55-57, both program complementarity and program substitution – higher take-up of UI but lower take-up of DI – are at work. The 14.8 percentage point increase in early retirement is associated with a 24 percentage point increase in subsequently claiming of retirement benefits and a 9.7 percentage reduction in claiming of DI benefits.

- Given Austrian early retirement rules of the late 1980s and early 1990s, the extension of UI benefits was welfare-improving only if the degree of risk aversion exceeds 2.22. Since past studies typically find values of risk aversion below 1, we conclude that extended UI through the program was most likely too generous relative to the socially optimal policy.

The findings are important to disability insurance policy because of the large numbers of individuals who may use disability insurance as a pathway into early retirement. The findings advance our understanding of how the financial incentives of benefit programs like DI affect labor market behavior in the years leading up to normal retirement ages.

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