The Rate of Return to Schooling: The Mincer Equation and Beyond Extract

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Mincer Equation Extract

What is "The" Rate of Return to Schooling?



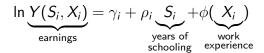
- Previous estimates traditional: based on a single cross-section
- Challenges faced in estimating rates of return
 - a Lifetime earnings profiles required
 - **b** Observed earnings profiles subject to selection bias
 - Identifying and quantifying nonmarket benefits and nonpecuniary costs is a difficult task
 - Identifying agent expectations about future returns (what are their information sets?)
 - Cohort effects (school quality; labor market entry effects)

• Challenges in understanding schooling decisions made

- What is model of schooling choices: Family? Individual?
- **b** What is in agent information set?
- O What constraints does agent confront?
- 8 Role of parental transfers and altruism/paternalism



What is Proper Measure of Causal Rate of Return? Use a Slightly Less Cumbersome Notation:



- Becker and Chiswick (1966); Mincer (1974)
- γ_i : "ability to earn" source of "ability bias"
- ρ_i: "rate of return"



(1)

- Causal relationships generated by hypothetical variations of each of γ_i, ρ_i and φ(X_i).
- Correlation between γ_i and S_i is the source of "ability bias" (e.g., Griliches, 1977).
- Strictly speaking, γ_i may or may not be related to ability.
- ρ_i : "return to a unit of schooling" for person *i*.

