Discussion of "Unemployment Crisis"

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What Does the Paper Do?

- Search and matching model calibrated to match the US postwar data can generate periods that resemble the Great Depression.
- Key elements: Nonlinearities and endogenous wage rigidity.
  - Vacancy creation persistently low during Great Depression.
  - Large rises in unemployment from small changes in the vacancy creation rate (Beveridge curve almost flat).
- Welfare costs of fluctuations large.

Its Place in the Literature

- Contributes to literature examining the amplification of $S\&M$ model.
- Relative to majority of studies, it emphasizes non-linearities and alternative wage setting mechanism.

Its Place in the Literature

- I find the overall message of the paper surprising: From the perspective of the labor market, the Great Depression was no different than any recession in the postwar period. It was business as usual.

- Same economy, same structural parameters, same wage setting parameters, etc.

Several Ways to Read this Paper

- A paper about unemployment and labor markets during the Great Depression (and comparison to postwar recessions.)
- A paper about asymmetric dynamics around recessions in the unemployment rate.
- A paper about nonlinearities in the search and matching model.
- A paper about achieving large welfare costs in a model of fluctuations.

A Paper About the Great Depression?

- Looking at labor markets during the Great Depression through the lens of the DMP model is a valuable contribution.
- As a study of the Great Depression the mapping between model and data is still rough.
- Wage dynamics? Investment? Discount rates? Dividends?

Emphasize Asymmetry?

From Mortensen and Pissarides (1992):

" This imparts a cyclical asymmetry in the job destruction rate and the dynamic behavior of unemployment. The short-run cyclicality of the job destruction rate increases and speed of change of the economy at the start of the recession is faster than the speed of change at the start of the boom. "

Emphasize Asymmetry?

- My conjecture: the degree of asymmetry in this model is lower than what you obtain in models with endogenous job destruction.

- How does asymmetry compare in the data and the model?

- Fit a VAR for each of the two regimes (Great Depression (enough data?) and Postwar). Is asymmetry apparent in impulse responses?

- Alternatively, fit a regime-switching VAR to post-war period. Is asymmetry apparent in impulse responses.

- Horse race against state-of-the-art *S&M* models with endogenous job destruction (e.g. Ferraro (2013)).

Why Are Business Cycles So Costly

- Changes in steady-state unemployment vs. fluctuations in unemployment.
- Welfare costs large even with risk-neutrality, because steady-state unemployment changes.
- Why does steady state unemployment change?

Why Are Business Cycles So Costly

- Law of motion for unemployment:

$$u_{t+1} = s + u_t(1 - s - f_t)$$

- Non-stochastic u is :

$$u = \frac{s}{s + f}$$

- Expected (with fluctuations) u is:

$$E(u) = s + E(u)(1 - s) - E(u)E(f) - Cov(f, u)$$

- If $Cov(f, u) << 0$ (true in US data), and if $E(f)$ is not very different from f, then $E(u) > u$

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- Results in P. Jung and K. Kuester (2011).

Conclusions

- Well-crafted contribution to the macroeconomics of labor markets.
- Useful exercise to better understand some non-linearities present in the standard $S\&M$ model.
- Not convinced yet that the model in its current form is appropriate to study the Great Depression (or similar episodes).