Employment Adjustment and COVID: Some Thoughts on Theory and Reality

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CEPR-IZA-OECD Workshop:
Employment Support Strategies during COVID-19

A Separation: Micro

Firm's and worker's present values from the job:

$$V_{\text{now}}^{\text{Firm}} = \boxed{p_{\text{now}}} - w_{\text{now}} + \boxed{\beta^{\text{Firm}}} V_{\text{later}}^{\text{Firm}}$$
$$V_{\text{now}}^{\text{Worker}} = a_{\text{now}} + w_{\text{now}} + \beta V_{\text{later}}^{\text{Worker}}$$

Separate if either value is smaller than respective outside options, $O_{\text{now}}^{\text{Firm}}$, $O_{\text{now}}^{\text{Workers}}$.

Privately inefficient separation: firm & worker could have found a wage w to bribe each other into continuing. Hall Lazear JLE 1984, Jaeger Schoefer Zweimueller WP 2020

Can think of COVID shock as

Static: Marginal revenue product of labor $\downarrow$
- Friction: wage rigidity Jaeger Schoefer Zweimueller WP 2020
- Policy remedy: payroll tax cuts; short-term work

Dynamic: Firm's $\beta \downarrow$
- Friction: financial constraints – "wrong discount factor" e.g., Schoefer WP 2015
- Policy remedy: liquidity provision (loans, transfers, equity)

A Separation: Micro with Layoff Taxes τ and STW σ

Firm's and worker's present values from the job:

$$V^{\text{Firm}}_{\text{now}} = p_{\text{now}} - (w_{\text{now}} - \sigma) + \beta^{\text{Firm}} V^{\text{Firm}}_{\text{later}}$$
$$V^{\text{Worker}}_{\text{now}} = a_{\text{now}} + w_{\text{now}} + \beta V^{\text{Worker}}_{\text{later}}$$

Separate if either value is smaller than respective outside options, $O^{\text{Firm}}_{\text{now}} - \tau$, $O^{\text{Workers}}_{\text{now}}$.

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STW: Challenges & Alternatives

- France — Cahuc Kramarz Nevoux WP 2018
- Germany — Baleer Gehrke Lechthaler Merkl EER 2016
- Italy — Giupponi Landais WP 2020
- Switzerland — Kopp Siegenthaler WP 2019
- Austria — Jaeger Osterwalder Schoefer Zweimueller $\geq$2021

Policy alternatives: Birinci Karahan Mercan See WP 2020

- Wage rigidity: payroll tax cuts for incumbents — Saez Schoefer Seim AER 2019, WP 2020
- Preserving matches: temp layoffs & recalls — Nekoei Weber WP 2020
- Insurance: UI
- Liquidity provision: loans, transfers — Granja Makredis Yannelis Zwick WP 2020

Challenges:

- Hard to measure surplus $\Rightarrow$ diagnose ineff sep's — Jaeger Schoefer Zweimueller WP 2020
- High replacement rates of STW vs. UI
- How transitory is the COVID shock really?

Separations: Macro Aspects

An EU separation moves one more worker from employment into unemployment...

Externalities:

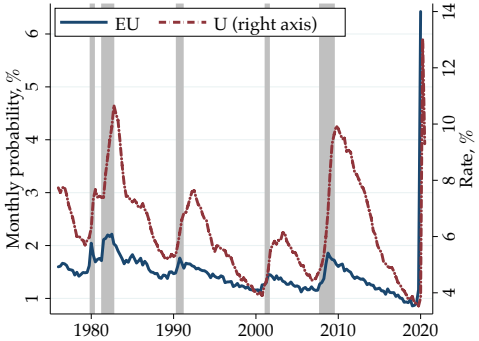
- Search externalities, augmented Hosios conditions,... Lalive Landais Zweimueller AER 2015
- Aggregate consumer demand channel Lorenzoni Guerreri Straub Werning WP 2020

Key Q: effect of EU sep'ns on unemployment (!) Mercan Schoefer Sedlacek WP 2020

- Standard search and matching (DMP) models: **extremely short half life** of sep-induced disturbance to unemployment
- Data: large & persistent effects on unemployment of EU separations
- Consistent with non-standard "congestion" models Mercan Schoefer Sedlacek WP 2020

Separations: US Time Series

Mercan Schoefer Sedlacek WP 2020



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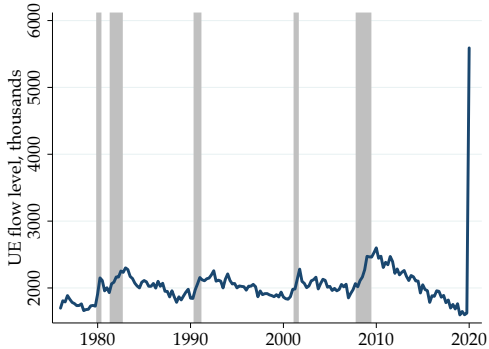
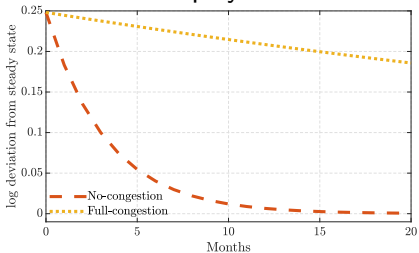


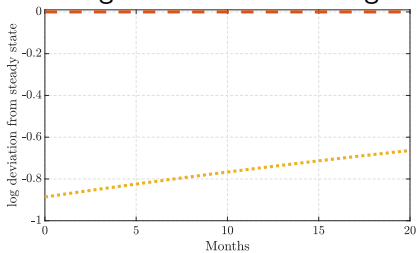
Slow Reall'n: "Congestion" in IRF to Sep's ↑

Mercan Sedlacek Schoefer WP 2020

Unemployment



Market Tightness ⇒ Job Finding Rate



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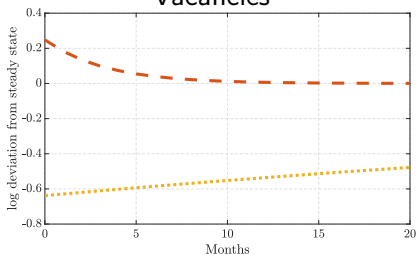
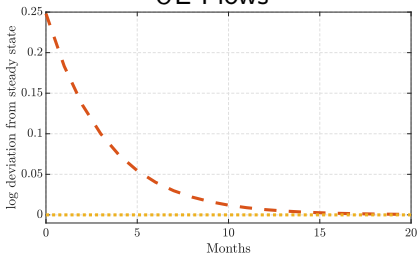
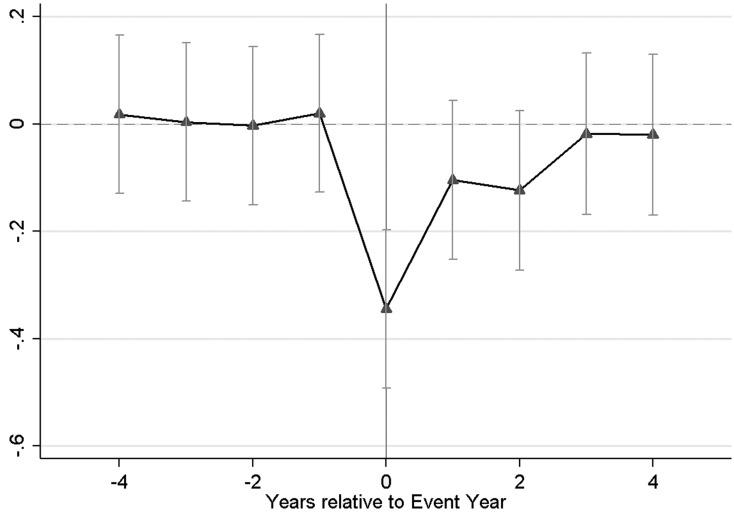


UE Flows



Reallocation is Slow: Mass Layoffs

Gathmann, Helm, Schoenberg JEEA 2020



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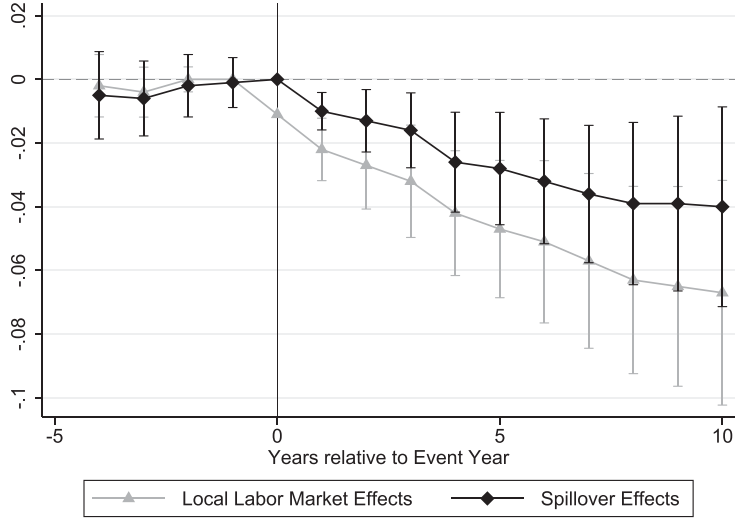

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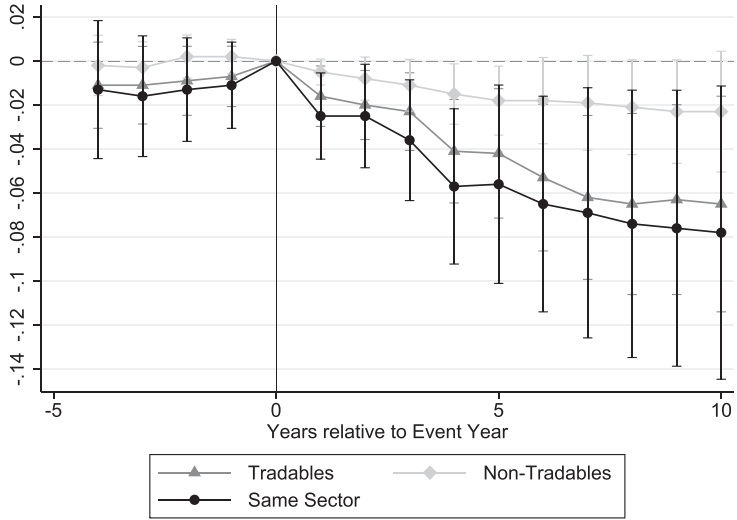
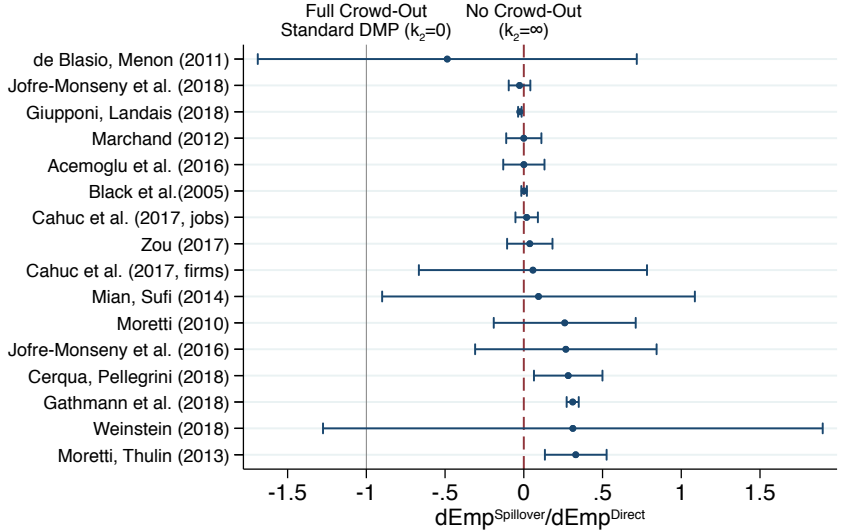
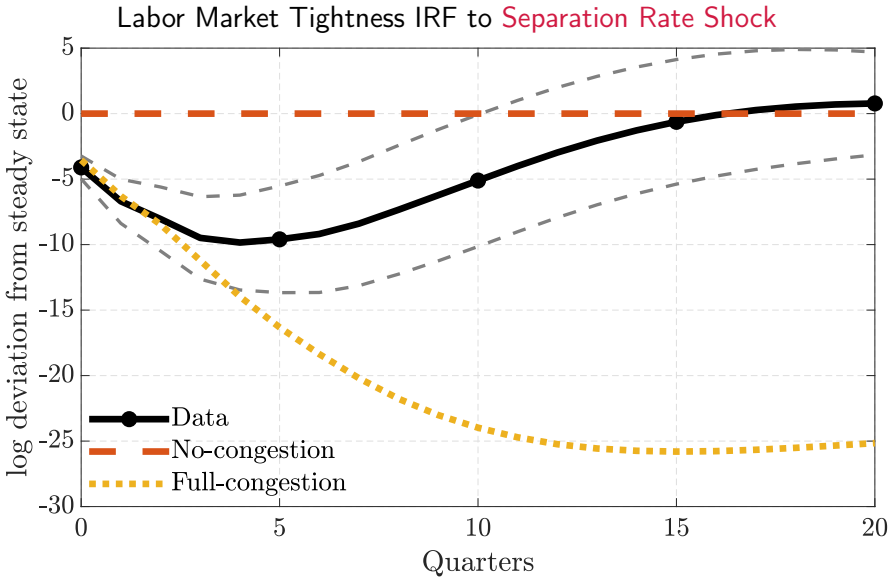


Reallocation is Slow Everywhere: Meta-Analysis Mercan and Schoefer AERI 2020



Reallocation is Slow in the Data

Mercan Sedlacek Schoefer WP 2020



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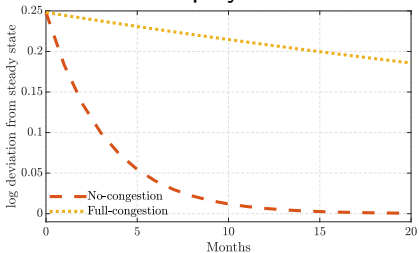

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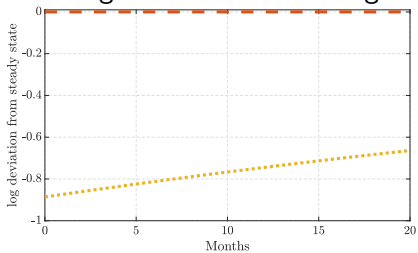

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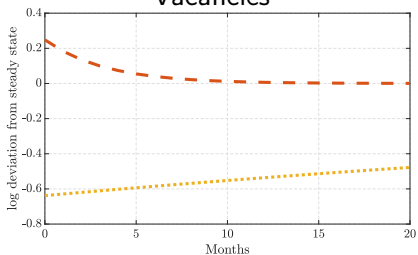

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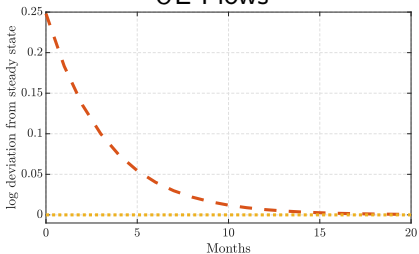

Beyond the Labor Market

Perhaps most importantly, displacement, particularly in recessions, is associated with negative effects on

see Davis von Wachter 2011 for lit review

- Well being
- Health & mortality
- Family outcomes

"If not now, when else?"

vs.

"If now yes, should we ever not?"

"We should blanket-subsidize (STW etc.) match preservation in response to COVID, which is perhaps among the largest (transitory?) shocks imaginable."

$\Rightarrow$ "We should blanket-subsidize (STW etc.) match preservation in response to all transitory shocks."

Uncomfortable implication (at least in simple models) – perhaps not in the presence of informational frictions etc... I do not see a clear answer.