EMPLOYMENT FLUCTUATIONS WITH EQUILIBRIUM WAGE STICKINESS

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RESEARCH QUESTION

How sticky wage can explain the large magnitude of unemployment after a recession shock

POSITIONING

- Peter Diamond(1982) Dale Mortensen(1982) Christopher Pissarides(1985)
  - Labor matching model with Nash Bargaining (DMP)
  - not very sensitive to driving forces (stable job finding rate)
- Guillermo Calvo (1983)
  - arbitrary restriction
- What this paper had
  - sticky wages but not employer-worker pair forgoes bilateral opportunities for mutual improvement

MODEL

- Wage is determined by the demand game auction
  - Pin down the wage in the bargaining set
- Wage is constant
  - The way that the wage got pinned down is not related to the tightness
- The constant wage is an equilibrium of the model
- Make wages rigid in a dynamic setup by making wages move with the slow-moving trend of labor productivity
  - $z_t = z_t^P z_{s_t}^M$
  - $w_t = w z_t^P$

COMPARISON WITH THE CLASS CONTENTS

- Model in class is static
- In the static set-up this model is the same as fixed wage
- But the wage is not totally exogenous