Why Are Prices Not Restricted to a Narrow Price Band?

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<u>Hall</u> (2005) : - w/ rigid wages, there are
significant fluctuations in unemployment in
response to productivity shocks (resolution
to Shimer (2005) puzzle)

legitimate $\rightarrow$ - rigid wags are theoretically
bilateral do not create any
inefficiencies

- but rigid wage must
remain within a fairly narrow band

$$\underline{w} \quad < \quad w \quad < \quad \overline{w}$$

$\rightarrow$ wage band exists b/c of linearity of
the model.

productivity

$$Z \quad = MRS \quad < \quad w \quad < \quad MPL \quad = \quad \overset{\curvearrowleft}{a}$$

value of home production / leisure

$$z \quad < \quad w \quad < \quad a$$

- <u>Equivalent in macro model of slack</u> :

$$O = MRS < \quad p \quad < \quad MU$$

sellers must remain w/ CES utility function,
in shop to sell $MU(c) \rightarrow +\infty$ when $c \rightarrow 0$
[Inada]

When $c \to 0$, the price band becomes infinitely wide.

$$\boxed{0 < p < +\infty}$$

$\hookrightarrow$ This is true in any concave model (satisfic Inada conditions).