

Employer: Sets no-shirking effort,  $\bar{e}$ , termination probability,  $t$  and wage,  $w$

Worker's choice:

Does not work  
 $e = 0$

Works  
 $e = \bar{e}$

Chance:

Worker is  
terminated  
 $(t)$

Worker  
keeps job  
 $(1 - t)$

Chance:

Remains  
jobless  
 $(j)$

Gets a  
new job  
 $(1 - j)$

$B$

$w - \underline{u}$

$w$

$w - \underline{u}$

