[Description of JMP and any other relevant work]

JMP Abstract

Unemployment has long lasting negative effects on labor earnings that persists even after reemployment. In this paper, I study the macroeconomic consequences of these microeconomic effects on business cycle fluctuations and in the transmission of unemployment insurance policies. Using a heterogeneous agent New Keynesian (HANK) model with search and matching frictions augmented to include human capital dynamics, I show that precautionary saving in response to heightened unemployment risk is substantially larger when households are subject to long term earnings loss following job displacement. Over the business cycle, unemployment risk is a much stronger amplifier of fluctuations and UI multipliers rise with the policy horizon largely due to their effect on expectations as opposed to their stimulative effect on income. For longer policy horizons, extending UI is considerably more stimulative than increasing the UI replacement rate as it precisely mitigates the precautionary saving that arises against the possibility of long term unemployment.