Discussion on Boostani and Gervais (Jaimovich, Siu?) *"Optimal Unemployment Insurance in a Directed Search Model"*

Marco Cozzi (et al.?)

Queen's University

Montreal - CIREQ - Apr 2011

UI - Why Do We Care?

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- Great Recession $\longrightarrow$ soaring costs of the program, i.e. aggregate shocks are important.

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- [...]*In the absence of moral hazard,* **replacement ratios** *as high as* **.65 are optimal** *and the welfare benefits of unemployment insurance are quite large. However, if there is* **moral hazard** *and the replacement ratio is not set optimally, but is instead set to an empirically plausible value, the economy* **can be much worse off** *than it would be without unemployment insurance.*[...]

Optimal UI - Hansen and Imrohoroglu, JPE 92

TABLE 2

OPTIMAL REPLACEMENT RATIOS

	A. Selected Results for $\rho = 2.5$					
Moral Hazard ($\pi(0)$)	.00	.05	.10	.30	.50	1.00
Optimal θ	.65	.65	.35	.15	.10	.05
	B. Selected Results for $\rho = 10$					
Moral Hazard ($\pi(0)$)	.00	.55	.60	.65	.75	1.00
Optimal θ	.40	.40	.35	.30	.25	.20

NOTE.—The values for $\pi(0)$ used in this table correspond to the values used in figs. 2 and 3.

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- [...]*We provide estimates of the* **cost reduction** *obtained by shifting from the current unemployment insurance scheme* **to the optimal one**, *holding the ex ante utility of the unemployed agent constant. The* **gains** *are particularly large (about* **30 percent***).*[...]

Optimal UI - Hopenhayn and Nicolini, JPE 97

TABLE 1

OPTIMAL UNEMPLOYMENT INSURANCE

WEEKS OF UNEMPLOYMENT	OPTIMAL WITH TAX			OPTIMAL WITH NO TAX: REPLACEMENT RATIO
	Replacement Ratio (1)	*C* Emp (2)	Tax (%) (3)	(4)
1	99.0	100.5	−.5	85.8
2	98.9	100.4	−.4	80.8
3	98.8	100.3	−.3	76.3
4	98.7	100.2	−.2	72.1
5	98.6	100.1	−.1	68.2
6	98.5	100.0	.0	64.7
7	98.4	99.9	.1	61.4
8	98.3	99.8	.2	58.4
12	97.9	99.4	.6	48.2
16	97.5	99.0	1.0	40.5
26	96.5	98.0	2.0	27.7
52	94.0	95.5	4.5	13.4

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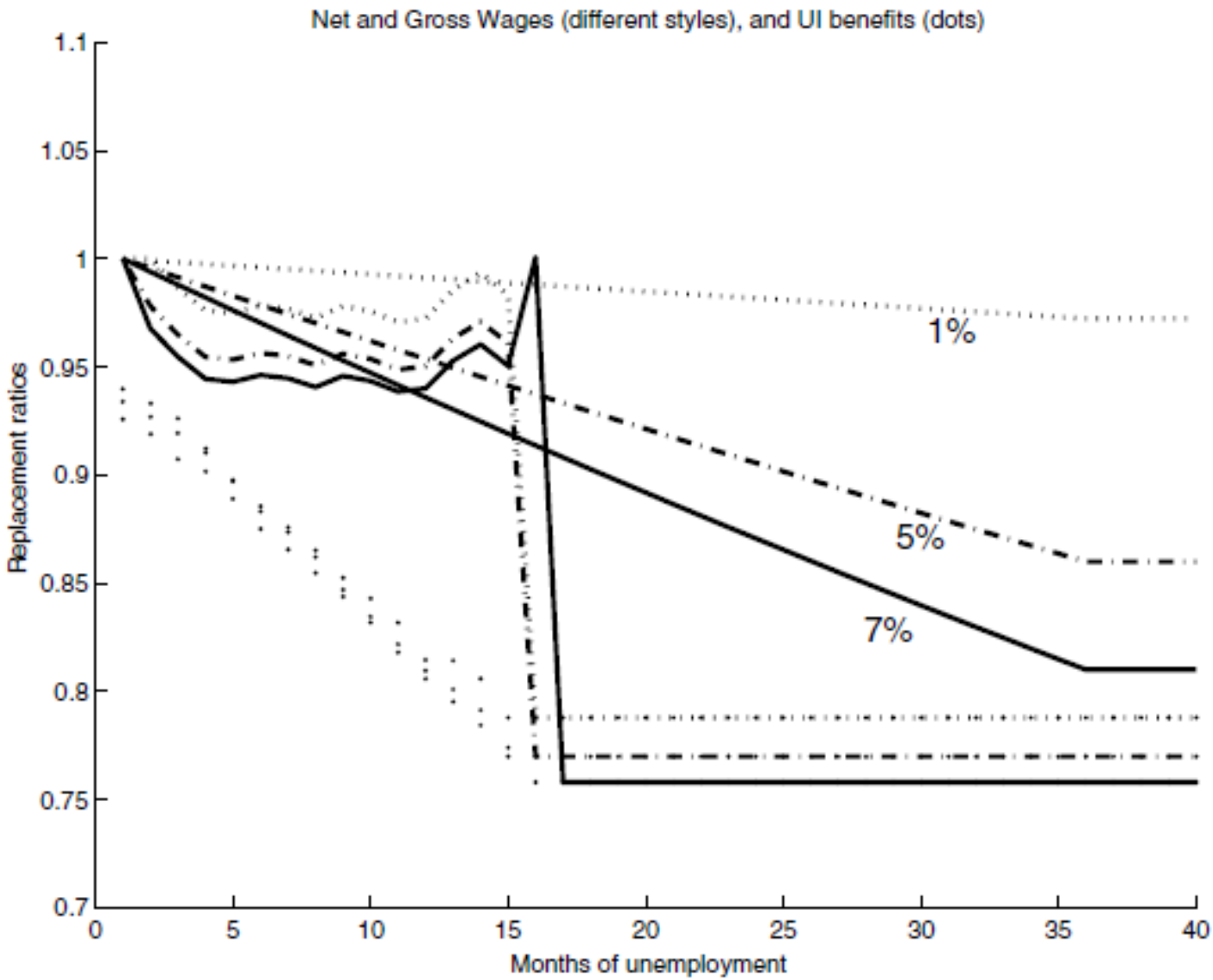
- [...] *The optimal UI scheme requires the* **UI benefits to decrease** *with the duration of unemployment.* [...] *UI transfers are* **bounded below** *by a minimal assistance level that arises* **endogenously** *in the efficient contract. The optimal scheme implies a* **wage subsidy for long-term unemployed** *workers.*[...]

Optimal UI - Pavoni IER 09 (Spain)



NOTES: The optimal UI scheme for different human capital depreciation rates. All other exogenous parameters at their benchmark levels.

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- [...] *Evaluate a tax financed unemployment insurance scheme. Higher* **insurance** *is beneficial for consumption smoothing, but because it* **raises workers' outside option** *value, it* **discourages firm entry**. *The* **latter effect** *is* **more potent for welfare** *outcomes.* **Productivity changes** *in the model generate rather* **limited unemployment effects** *thus, recent findings are corroborated in our more general setting.*[...]

Optimal UI - Krusell, Mukoyama and Sahin, RES 10

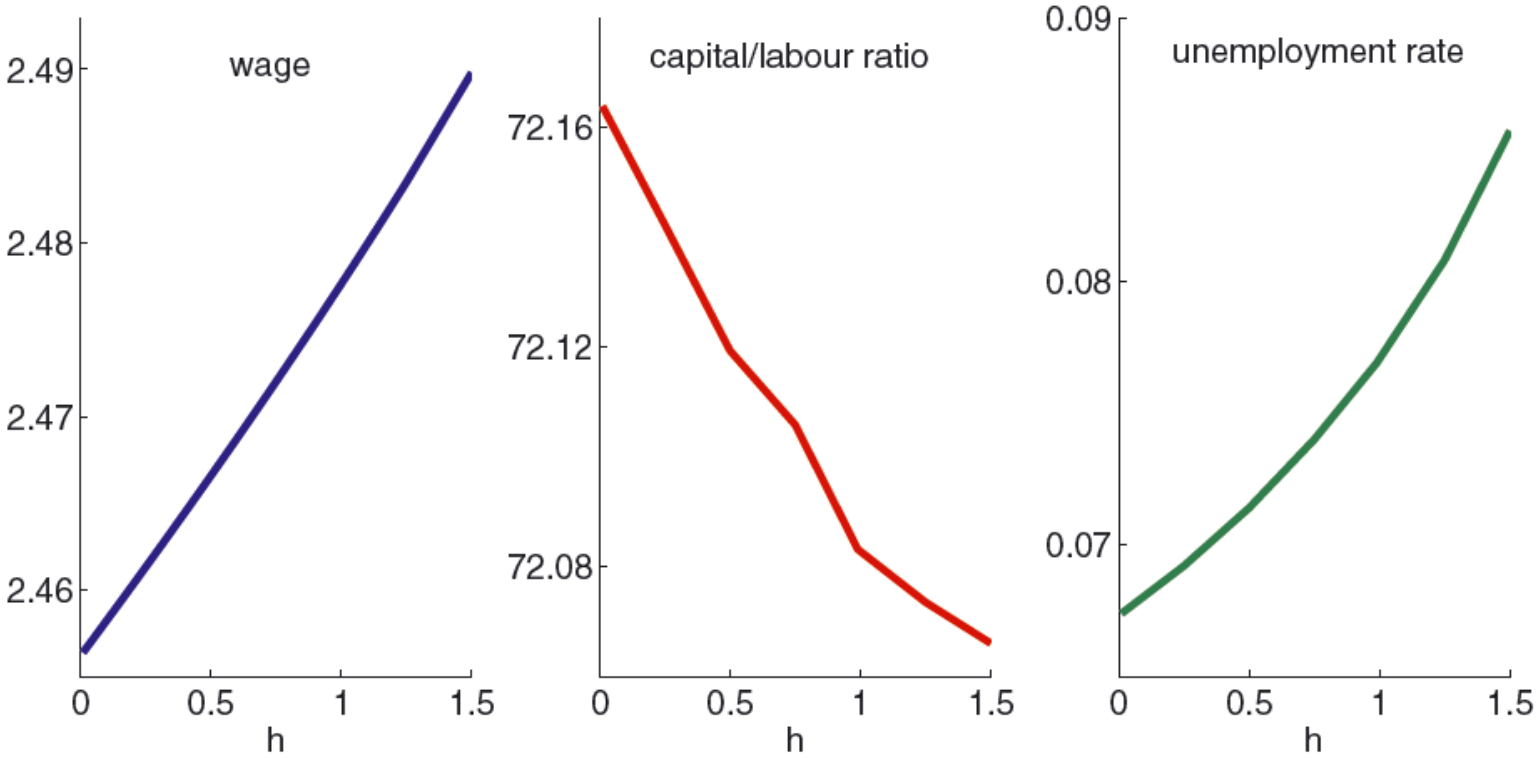

FIGURE 2

Wages and capital/labour ratio and the unemployment rate as a function of h

Optimal UI - Krusell, Mukoyama and Sahin, RES 10

- h stands for U benefit; $h = .99$ corresponds to a 40% replacement rate, λ stands for $\%c$ change in the baseline that equates welfare to the counterfactual.

TABLE 2

Average values of λ, compared with the benchmark of h = 0.99

h from 0.99 to	Total (%)	Unemployed (%)	Employed (%)	% gaining	Poorest unemployed (%)	Poorest employed (%)
0.01	0.11	−0.09	0.13	92.10	−4.0	−1.0
0.25	0.12	−0.02	0.14	92.29	−1.2	−0.3
0.50	0.11	0.01	0.12	99.22	−0.54	−0.09
0.75	0.07	0.02	0.07	99.96	−0.2	0.00
1	0	0	0	0	0	0
1.25	−0.14	−0.09	−0.15	0.00	0.06	−0.1
1.50	−0.38	−0.27	−0.39	0.00	−0.04	−0.32

Other Contributions

- Bils, Chang and Kim, AEJ - Macroeconomics 11
- Burdett, Carrillo-Tuleda and Coles, WP 09
- Mukoyama, WP 10
- Nakajima, IER Forthcoming - WP 11
- Shimer and Werning, AER 08 - QJE 07

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- However, should we expect a very different behavior? Basic trade-off between unemployment insurance and search incentives/'reservation wage'.
- And... a firing probability specified in a labor contract?!?

UI - Some Institutional Features and Empirical Findings

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- Alvarez and Veracierto, JME 01 propose a tractable specification.

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- Savings? Feasible.

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  4. Size of labor market risk?

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- In the data it's hard to distinguish between U and NLF, Jones and Ridell, ECTA 99. With large and persistent aggregate shocks $\longrightarrow$ discouraged workers (KMRS).
- Counterfactuals and decompositions to disentangle the quantitative effects: assess the role of Directed Search (shut down a market).