

How Sweden's unemployment became more like Europe's

Comment on Ljungqvist-Sargent paper

Structure of discussion

- General comments
- What policy issues should the model be used to highlight?
- Labour market programmes as a device to terrorize the unemployed

Two model vintages

1. Ljungqvist-Sargent 1997
 - multiple equilibria
 - low-unemployment equilibrium before the 1990s
 - generous benefits offset by close monitoring and high tax progressivity
 - high-unemployment equilibrium once unemployment increases because close monitoring no longer possible

2. Ljungqvist-Sargent 2006
 - multiple equilibria
 - low-unemployment equilibria if low "turbulence" because employment protection "offsets" generous benefits
 - high-unemployment equilibrium with high "turbulence" because of high *effective* replacement rates

General comments

- Elegant and thought-provoking models
- Both tackle the problem of explaining both earlier low unemployment and current high unemployment
- Example of interaction between shocks and institutions
- Neglect of collective bargaining but OK
- First model is more convincing than second one
- Is there really convincing evidence that economic turbulence has increased a lot?

Table 2: Unemployment effects of layoff costs with different degrees of economic turbulence. (Tranquil times have an index of turbulence equal to T00.)

		WS economy			LF economy		
		0	5	10	0	5	10
<i>Turbulence</i>	<i>Layoff cost</i> ^a						
T00		5.85	4.77	3.83	5.70	4.43	3.51
T03		5.65	4.74	4.18	5.24	4.14	3.23
T05		5.76	5.03	5.06	5.18	4.06	3.16
T10		6.01	5.92	6.75	5.11	4.03	3.19
T20		6.31	7.00	8.76	5.07	4.00	3.19
T99		6.60	8.08	10.95	5.02	3.98	3.24

^a A layoff tax of 5 (10) corresponds to roughly 7 (14) weeks of the average productivity of all employed workers.

The focus of the paper

- Comparison US – Europe (Sweden)
 - Why 0 replacement rate in the US?
 - OECD calculations of 5-year net replacement rates: around 35 %
 - How interesting is the comparison?
- More interesting to analyse relevant policy options for Europe (Sweden)

Swedish (European) policy issues

- Danish "flexicurity": high benefits and low employment protection
 - empirical research in general suggests it is a myth
 - changes in benefits and labour market policy in Denmark but not in employment protection
 - the degree of turbulence crucial according to the model
 - employment effects of employment protection at moderate replacement rates
- Time profile of benefits
 - short-term versus long-term benefits
- Benefit reductions and tax cuts
 - implications for after-tax wages
 - effects of focus on low-wage earners

Reducing the "return" to unemployment through requirements on "social work"

- "Threat effects" important in Denmark
 - Danmarks økonomiske råd 2002
 - Rosholm and Svarer (2004)
 - the only effects in these studies of labour market programmes
- But difficult to make programme participation both pleasant and unpleasant at the same time
- Time-inconsistent preferences?

Conclusions

- Potentially important mechanism explored
- Empirical relevance?
- Don't use the model only for US-Europe comparisons but also for analysing relevant Swedish (European) policy options!
- More discussion of happiness-unhappiness trade-off in labour market policy