Answer on Question#39500 – Economics – Macroeconomics

Assignment

Explain why without a big drop in wages, weak demand for labour yields a jobless recovery.

Solution

Uncovering why reduced wages should be necessary to put people to work is a trickier matter. In a paper of 2012 Guillermo Calvo and Pablo Ottonello, of Columbia University, and Fabrizio Coricelli, of the Paris School of Economics, blame financial havoc. After crises chastened banks are willing to lend only to firms with tangible capital—like buildings and equipment—that can be seized after a default. Firms that rely more on machines than labour therefore perform better in the recovery, pushing down demand for workers. Without a big drop in wages, weak demand for labour yields a jobless recovery. The economists examine data on financial crises since the Second world war and find that post-crisis recoveries are jobless when inflation is low, but merely “wageless” when inflation is relatively high. Low inflation may help consumers in good times, but higher inflation is a useful shock absorber when recession strikes.