



[The Dark Corners of the Labor Market](#)

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Standard models predict that episodes of high unemployment are followed by recoveries. This paper shows, by contrast, that a large shock may set the economy on a path towards very high unemployment, with no recovery in sight. First, I estimate a reduced-form model of flows in the U.S. labor market, allowing for the possibility of multiple steady states. Next, I estimate a non-linear search and matching model, in which multiplicity of steady states may arise due to skill losses upon unemployment, following Pissarides (1992). In both cases, estimates imply a stable steady state with around 5 percent unemployment and an unstable one with around 10 percent unemployment. The search and matching model can explain observed job finding rates remarkably well, due to its strong endogenous persistence mechanism.

The findings imply that, during the Great Recession, the U.S. economy came very close to making a transition towards very high unemployment, as happened in for example Spain or Greece during this period. The model further predicts that uncertainty about aggregate unemployment declines during booms and increases during recessions, consistent with evidence from the Survey of Professional forecasters.