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The Labor Market Consequences of Financial Crises with or Without Inflation: Jobless and Wageless Recoveries

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Abstract

This paper offers empirical evidence showing that, relative to "normal" recessions, financial crises hit the labor market by either enhancing the degree of joblessness and/or by further depressing the real wage ➡ a situation that the paper labels "wageless recovery." This holds for a sample of both advanced and emerging-market economies recession episodes, using credit market data prior to the recession episode as instrumental variable for financial crises. Results also indicate that inflation determines the type of recovery: low inflation is associated with jobless recovery, while high inflation is associated with wageless recovery. The paper shows that these outcomes are consistent with a simple model in which collateral requirements are higher (lower), the larger is the share of labor costs (physical capital expenditure) involved in a loan contract. This is motivated by the conjecture that if a loan becomes delinquent, physical capital is easier to confiscate than human capital. Evidence from advanced economies supports the model. An implication of these findings is that a spike of inflation during financial crisis may help to reduce jobless recoveries, but at the expense of sharply lower real wages. Only relaxing credit constraint might help both unemployment and wages.

Keywords: Financial crises, Jobless recovery, Wageless recovery**JEL Classification:** E24, E44, G01[Suggested Citation](#) >[Show Contact Information](#) >CEPR Subscribers Download (<http://cepr.org/active/accounts/login.php>)

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