

Hiring Policies, Worker Employability, and Labor Market Performance

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Abstract

This paper extends Shapiro-Stiglitz's efficiency wage model to explore the possible interaction between firms' hiring policy and outsiders' employability. Specifically, firms determine their hiring policies, based on the accepted view about the employability of outsiders, whereas outsiders decide whether or not to maintain their employability, given firms' hiring policies. Such an interaction is responsible for the unconditional existence of the "no-second-chance" equilibrium, in which firms believe that outsiders are no longer employable, and thus choose to fill their vacancies exclusively with new entrants into the labor market, which discourages outsiders from making efforts to preserve their employability. On the other hand, the "second-chance" equilibrium, in which firms believe that outsiders are still employable, and thus choose to fill some vacancies with them, exists only when the labor demand is sufficiently active. Outsiders are motivated to preserve their employability if and only if there is a good chance of being re-hired and making a good living again, which entails a sufficiently high demand for labor.

Keywords:

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