

## Bubbles and unemployment in an endogenous growth model <sup>\*</sup>

Ken-ichi Hashimoto<sup>†</sup> and Ryonfun Im<sup>‡</sup>

### Abstract

We construct a continuous-time overlapping-generations model with labor market friction in order to examine the relationship between bubbles, economic growth, and unemployment. We show that the existence of bubbles is contingent upon the equilibrium unemployment rate. Asset bubbles can (not) exist when unemployment is low (high), which leads to higher (lower) interest rates and economic growth through labor market efficiency. Hence, economic growth under the bubble regime where bubbles can exist is higher than that under the non-bubble regime where bubbles cannot exist. Furthermore, policy or parameter changes that have a positive effect on the labor market shift the economy from a non-bubble regime to a bubble regime.

**Keywords:** overlapping generations, endogenous growth, labor market friction, unemployment

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<sup>†</sup>Graduate School of Economics, Kobe University, 2-1 Rokko-dai, Nada, Kobe 657-8501, JAPAN; E-mail: hashimoto@econ.kobe-u.ac.jp.

<sup>‡</sup>Graduate School of Economics, Kobe University, 2-1 Rokko-dai, Nada, Kobe 657-8501, JAPAN; E-mail: tdrsk@gmail.com.