Unemployment, Financial Frictions, the Crisis, and the Slow Recovery†

Goro Komatsu‡

Kyushu University

April 2019
(First draft: June 2018)

Abstract

The origins of unemployment fluctuations are still controversial among macroeconomists. This paper contributes to this debate by disentangling labor market and financial shocks in an estimated unemployment DSGE model by Galí, Smets, and Wouters (2012) augmented with the financial accelerator mechanism á la Bernanke, Gertler, and Gilchrist (1999).

We argue that the answer is financial shocks, but it is the interaction of contractionary shifts of both aggregate demand and supply that account for the slow recovery. Our findings imply the irrelevance of labor market disturbances as the key factor underlying unemployment and the output gap fluctuations during and after the crisis.

JEL Classification: E24, E32, E52,
Keywords: DSGE models, Business cycles, Financial frictions, Unemployment fluctuations, Output gap, Bayesian estimation

†The author is grateful for comments and suggestions to Taro Takimoto from Kyushu University, and 56th Annual Conference at Kyushu Association of Economic Science, Shimonoseki. The author gratefully acknowledges that a part of this research was supported by Graduate School of Economics, Kyushu University.

‡Graduate School of Economics, Kyushu University. East Zone Building 2 EE301, 744 Motooka, Nishi-ku, Fukuoka, Japan. E-mail: goro.komatsu@gmail.com.