Bonus Question: Does Flexible Incentive Pay Dampen Unemployment Dynamics?

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Meghana Gaur[4], John Grigsby[4], Jonathon Hazell[1,2] and Abdoulaye Ndiaye[3]

[1]Centre For Macroeconomics, [2]London School of Economics and Political Science, [3]NYU Stern, [4]Princeton University

We introduce dynamic incentive contracts into a model of unemployment dynamics and present three results. First, wage cyclicality from incentives does not dampen unemployment dynamics: the response of unemployment to shocks is first-order equivalent in an economy with flexible incentive pay and without bargaining, vis-a-vis an economy with rigid wages. Second, wage cyclicality from bargaining dampens unemployment dynamics through the standard mechanism. Third, our calibrated model suggests 46% of wage cyclicality in the data arises from incentives. A standard model without incentives calibrated to weakly procyclical wages, matches unemployment dynamics in our incentive pay model calibrated to strongly procyclical wages.