Unemployment Insurance and Learning: Evidence from Reservation Wages

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Preliminary

Abstract

The impact of unemployment insurance on job match quality is ambiguous. Insurance allows job seekers to select job offers carefully (a selectivity effect). However, choosier individuals remain unemployed for longer and job offers might become less frequent or generous with unemployment duration. Using unique data combining reservation wages of job seekers with extensive register data and exogenous variation in the generosity of unemployment insurance, we quantify the selectivity effect (or reservation wage effect) and show that it sharply differs across job seekers with different initial priors. Unexperienced job seekers — with noisy priors — strongly adjust their initial expectations but revise them downwards along the unemployment spell. We show in a quantitative model that uninformed job seekers use insurance to learn about employment prospects. The model rationalizes the differential response of job seekers to the generosity of benefits and the ambiguous findings of the empirical literature on match quality and the size of the duration effect.

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Keywords: unemployment insurance, benefits, reservation wage, job search behavior, priors, uncertainty, learning, natural experiments, heterogeneity.

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