Unemployment Insurance and Learning: Evidence from Reservation Wages*

Patrick Arni Yanos Zylberberg

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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.

*Arni: University of Bristol, IZA, CESifo; patrick.arni@bristol.ac.uk.; Zylberberg: University of Bristol, CESifo; yanos.zylberberg@bristol.ac.uk. We are grateful to Steffen Altmann, Pierre Cahuc, Bart Cockx, Bernd Fitzenberger, Dylan Glover, Simon Jaeger, Camille Landais, Andreas Mueller, Barbara Petrongolo, Imran Rasul, Roland Rathelot and Gerard Van den Berg for useful discussions and comments. We also thank participants in the 6th AMSE-BdF Labor Market Conference (2017), the Bristol Workshop on Economic Policy Interventions and Behaviour (2018), the CEPR/IZA Annual Labour Economics Symposium (2018), SOLE Toronto (2018) and the Workshop on Wages and the Labor Market (Helsinki, 2017) for helpful comments. The usual disclaimer applies.