Unemployment, Hysteresis and Transition

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Abstract: In this paper, we quantify the degree of persistence in the unemployment rates of transition countries using a variety of methods benchmarked against the EU. In part of the paper, we work with the concept of linear ‘Hysteresis’ as described by the presence of unit roots in unemployment as in most empirical research on this area. Given that this is potentially a narrow definition, we also take into account the existence of structural breaks and nonlinear dynamics in unemployment. Finally, we examine whether CEECs’ unemployment presents features of multiple equilibria, that is, if it remains locked into a new level whenever some structural change or sufficiently large shock occur. Our findings show that, in general, we can reject the unit root hypothesis after controlling for structural changes and business cycle effects, but we can observe the presence of a high and low unemployment equilibria. The speed of adjustment is faster for CEECs than the EU, although CEECs tend to move more frequently between equilibria.

Keywords: Unemployment, Hysteresis, Unit Root, Transition, Markov Switching.

JEL: E24, C22, C23.

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