

Open economy secular stagnation, unemployment and underemployment^{*}

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Abstract

We develop an open economy secular stagnation model with labor market frictions. This analytical framework gives quite different economic and policy implications from those under no stagnation. An improvement in the terms of trade decreases world demand for the home commodity and lowers working hours, which worsens deflation and reduces consumption and aggregate demand. As such, an improvement in the terms of trade decreases firm profits and increases unemployment. Those results are opposite to those under no stagnation. Under no stagnation an improvement in terms of trade increases consumption and has no effect on employment rate.

Key Words: aggregate demand shortages, unemployment, labor market frictions, underemployment, secular stagnation

JEL Classification: E24, F31, F41

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