DOES EMPLOYMENT PROTECTION CREATE ITS OWN POLITICAL SUPPORT?

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Abstract
This paper investigates the ability of employment protection to generate its own political support. A version of the Mortensen–Pissarides model is used for this purpose. If wages are set through Nash bargaining, workers value employment protection because it strengthens their hand in wage negotiations. Workers in high productivity matches benefit most from higher wages as they expect to stay employed for longer. By reducing turnover employment protection shifts the distribution of match-specific productivity toward lower values. Thus stringent protection in the past actually reduces support for employment protection today. Introducing involuntary separations reverses this conclusion. Now workers value employment protection because it delays involuntary dismissals. Workers in low productivity matches gain most since they face the highest risk of dismissal. The downward shift in the productivity distribution is now a shift towards supporters. (JEL: E24, J41, J65)