

## **Flexibility, Dualism and the Great Recession**

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Most of the recent literature on the effects of labor market institutions on wages and employment draws on reforms used as natural experiments. This is a significant improvement with respect to the earlier literature which was based solely on cross-country variation in (highly imperfect) measures of these institutions. But this new literature lacks guidance from a body of theory acknowledging the fact that regulatory changes often create long-lasting asymmetries, two-tier regimes, between a reformed and an unreformed segment of the labor market. This presentation provides new evidence on reforms in Europe, a continent with well established institutions and a very intense reform activity in the last 25 years. In light of this evidence, it extends a general equilibrium model of the labor market allowing for two-tier reforms of employment protection, unemployment benefits and employment conditional incentives. Next, it provides evidence on the scale and macroeconomic effects of the dualism induced by these reforms.

The presentation is based on a chapter that will appear in Handbook of Labor Economics:

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