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Aggregate Demand, Economic Growth, and Keynesian Unemployment

This paper argues that in a growing economy unemployment can be the cause of goods markets failures, even if these are purely transitotory. As the economy grows, new firms wish to enter product markets. It may take some time, however, until their products are accepted on the market, which we model as a purely transitory demand shock. Firms who fail early entry will renege on the job offers, causing unemployment. Workers, anticipating this, will ask for a risk premium in insecure contracts, distorting price and supply decisions of firms, reducing incentives to invest into novel products, which reduces, but does not eliminate the number precarious job offers. Thus a transitory demand shock will lead to a persistent level of unemployment in a growing economy.