

# How hires are made: the economist's view

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# Outline

- 1 Theory: of spaghetti and workers
- 2 Empirical evidence from economics

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- How does the labor market depart from this ideal situation?

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- Workers and jobs are different across many dimensions: location, skills, etc.
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- Workers may know more about how good they are than firms do, and firms may know more about how good they are than workers do:
  - *Asymmetric information* leads to worse hires: e.g. a firm may hire workers who presented themselves as qualified but turn out to be incompetent.

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- Productivity and economic growth: bad hires mean lower productivity and lower growth.
- Mismatch: difficulty in filling some positions because of a lack of qualified workers (mismatch between skills demanded by jobs & skills workers have).
- Inequality: why are some workers more likely to be unemployed? Why do some workers make lower wages and some higher?

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- Education policy determines what kind of skills are available in the workforce, and has the potential to reduce mismatch.
- "Ban the box" increases asymmetric information because employees know more about their criminal records than prospective employers.

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- In many versions of directed search models, outcomes are efficient.
- Lesson from theory to improve matching efficiency: firms should post all relevant information in a way that is easy to access by potential candidates.

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- Wages play a supportive role: within a job title, higher wage jobs get more (7% more for 10% wage increase) and better applicants.
- Given CareerBuilder and others, are matching frictions still important?

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- Horton (2017) studies ODesk (now Upwork). Employers got up to six candidate recommendations based on their job opening.
- The job filling rate increased by 20% in technical jobs, and recommended candidates did not displace organic candidates.
- Lesson: since testing and algorithmic recommendations can improve hires, the hiring process still has matching frictions & can be improved.

## Matching frictions and policy: unemployment insurance

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- This reduction in the competition for jobs means that the market is less congested: probability of a match for a given application goes up, and this partially counteracts the overall decline in applications.
- Taking into account the impact of unemployment insurance on matching frictions, the impact of unemployment insurance on overall unemployment is 40% smaller than previously thought.

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  - Mismatch increases only slightly (to 6.9%) when also accounting for heterogeneity of jobs and job seekers by occupation (SOC2)
  - **Geographic mismatch is a minor contributor to US aggregate unemployment.**

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- Enjoyment and grades more important than labor market outcomes for major choice: surprisingly similar to 4-year college students

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- Better & more *user-friendly* information about jobs & salary could improve labor market outcomes and reduce mismatch.

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- Lesson: asymmetric information is important in the labor market and policy can have unintended consequences.

# Conclusion

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# Conclusion

- Economists have noticed that labor markets do not function perfectly due to matching frictions, heterogeneity & information asymmetries.
- Well-functioning labor markets with quick & high quality hires lead to lower unemployment and higher economic growth.
- Public policy can greatly influence the hiring process via e.g. unemployment insurance, education or anti-discrimination policies.
- Algorithmic recommendations & digital tools can improve the hiring process: exciting research ahead with economics & data science!

# Thanks and contact

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