

Search and Knightian Uncertainty

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Suppose that "uncertainty" about labor market conditions has increased. Does this change induce an unemployed worker to search longer, or shorter? This paper shows that the answer is drastically different depending on whether an increase in "uncertainty" is an increase in risk or that in true uncertainty in the sense of Frank Knight. We show in a general framework that, while an increase in risk (the mean-preserving spread of the wage distribution that the worker thinks she faces) increases the reservation wage, an increase in Knightian uncertainty (a decrease in her confidence about the wage distribution) reduces it.