A Traffic Jam model of Recessions*

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Abstract

I study an economy in which firms are interconnected and there is strategic complementarity in production decisions. Firms use the output of other firms as inputs to their own production. Furthermore, they make production choices before knowing the demand they face. The simultaneity of these production decisions leads to a stable dynamic system under certain regions of the parameter space. If parameters move around, however, this leads to a bifurcation in which the system becomes unstable. In this region, small pertubations can lead to stop-and-go movements in which firm output remains low for many periods. That is, the economic system undergoes a recession which resembles a traffic jam.

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