Discussion of

Globalization, Trade Imbalances, and Labor Market Adjustment

by Dix-Carneiro, Pessoa, Reyes-Heroles, Traiberman

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Question

• What are the current account implications of trade shocks?
  1. Can tariffs be a useful tool to close current account deficits?
  2. Does productivity growth abroad lead to trade deficit at home? and, if yes, what does this imply for labor market adjustment?
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• This papers attempts to offer a serious quantitative treatment of this issue, with the implication for labor market dynamics
  ○ two separate issues: (a) trade imbalance & (b) labor adjustment
Tariffs and Current Account
(The Macroeconomic Effects of Tariffs, 2019)

- **Lerner symmetry**  Lerner (1936) fundamental result:
  
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  \[ \text{Import tariff} \Rightarrow \text{Imports} \downarrow \Rightarrow \text{CA imbalance} \Rightarrow \text{RER appreciation} \Rightarrow \text{Exports} \downarrow \]

However: Lerner symmetry does not hold under sticky prices

1. Fiscal devaluations (Farhi, Gopinath & Itskhoki 2014)
2. BAT and VAT (Barbiero, Farhi, Gopinath & Itskhoki 2019)
3. Output gap shifting in liquidity traps (Jeanne 2018)
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  1. Intertemporal budget constraint → on-impact jump in RER
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• This allows for a one-time on-impact adjustment to the shock that ensures long-run balanced budget
  ◦ Is it really the case in practice?
Simple three-equation model
From Itskhoki and Mukhin (2019)

- Risk sharing and intertemporal budget constraint:

\[ \mathbb{E}_t \{ \sigma (\Delta c_{t+1} - \Delta c^*_{t+1}) - \Delta q_{t+1} \} = 0, \]

\[ nx_t = 2 \theta q_t - (c_t - c^*_t), \quad b_0 + \sum_{t=0}^{\infty} \beta^t nx_t = 0 \]
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  - Brunnermeier, Gourinchas & Itskhoki (2020) drop risk sharing to study growth trajectories under arbitrary path of CA
What about Labor Market Dynamics?

- Costs of switching \((C_k, k')\) are highly relevant for big trade shocks
  - but firms, or industries, or occupations, or geography?
  - perhaps, a stand-in for specific human capital
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  ○ if duration of unemployment is only 4–6 months
  ○ one-time adjustment to a permanent shock
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- Perhaps, downward wage rigidity or wait unemployment are more relevant than search unemployment in response to large trade shocks
Labor Dynamics with Search Frictions
Itskhoki and Helpman (2016)

Necessary ingredients (conclusion slide):
1. Downward wage rigidity and inefficient separations
2. Slow mobility across sectors
3. Slow firm entry and job creation (perhaps, causing CA deficits)

Worker Income Loss
Fired eventually
Fired on impact
No Firing by Stayers
No Firing
No Exit

Unemployment duration (years), $1/x$
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