

## **Empirical Topics in International Trade, Macroeconomics, and Applied Micro, 2017/2018**

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### **Executive Summary**

This seminar focuses on tackling bits and pieces of the big questions in the multifarious fields of International Trade, (Open-Economy) Macroeconomics, Economic Growth and Development, and Applied Micro. The uniting theme is a common (Applied Micro) empirical methodological approach with an overarching focus on valid identification, such as that arising from natural or quasi-natural historical experiments, and high-frequency identification in Macro policy announcements, or from actual large-scale randomized controlled trials, and supported by intuition and theory. I believe that the focus in Applied Micro on randomized experiments and quasi-experiments is a methodology with wide-ranging applications in business, finance, policy, and politics (full disclosure: I used to design experiments for a political party in the US). Among the various research questions we are interested in answering include: What is the impact of the rise of China on manufacturing in Russia? What is the impact of the rise of China on other developing and developed countries, including other FSU economies? What is the impact of monetary policy in a liquidity trap, both recently and during the Great Depression? What is the impact of fiscal policy in a liquidity trap vs. in normal times?

### **The Impact of the Rise of China on Global Manufacturing**

Arguably the most major event in the past 25 years of economic history has been the rise of the People's Republic of China. Recent research including Autor, Dorn, and Hanson (2013), Autor, Dorn, Hanson and Song (2014), and Acemoglu, Autor, Dorn, Hanson, and Price (2014), and Campbell (2014, 2016b, 2016c), have found that one impact of the rise of China was the shifting of the world's manufacturing core from America to China, while Smirnov (MAE thesis 2016) found evidence that Russian manufacturing was also hurt. Another impact was a reversal in the long-term downwards trend in oil prices and other commodities which happened to coincide with the tenure of Vladimir Putin. In the US, the large trade deficits and the collapse in American manufacturing led the Fed to keep interest rates low, feeding a housing bubble, and helping lead to a "balance sheet recession" once the bubble burst, leading to talk that the US and other developed countries have staggered into a "secular stagnation" – a sustained period of diminished economic expectations (Campbell, 2014).

But, what was the impact of the rise of China on Russian manufacturing, and on manufacturing of other FSU and developing countries? Smirnov (2016) found some evidence of an impact of Chinese import competition on Russian manufacturing, but what was the impact on local Russian labor markets? What was the impact on Europe (Van Reenen *et al.*, 2012, found an impact for Italy, but what about other countries)? What was the impact on other developing countries? Was the impact of the rise of Chinese manufacturing on many developing countries manufacturing bases hidden by the concomitant rise in commodities prices in the 2000s? Was Germany and Europe as affected by the rise of China as the US and Canada were? How much has Germany benefitted from a real exchange rate depreciation caused by the formation of the Euro? How much has Russian manufacturing been helped by the recent weakness of the Ruble (compared with Ukraine)? Based on geography (such as the gravity equation, see Campbell 2010, 2013), and sector specialization, which countries were set up to be the most exposed to China? These are some examples of open questions that students working in this area might work on answering.

### **Dutch Disease**

Given that Russia is an oil-rich country, the potential for high oil prices to result in Dutch Disease retarding the development and diversification of Russian industry is a real worry. However, recently Brock Smith (2016) has found that oil rich countries actually saw their manufacturing sectors increase in size following the oil price shocks in the 1970s, and that this increase was persistent, contra the classic Dutch Disease hypothesis. However, he only considered countries which were initially not industrialized, and he only considered data up to the mid-1990s, before oil prices rose again in the 2000s.

### **Macro Policy in a Liquidity Trap**

As of now, Japan has experienced more than 20 years of stagnation. The youth unemployment rate in Spain is still 50.1% -- and this is nearly 7 years after the financial crisis of 2008. Even in the US, where economic fortunes have recently shown signs of rebounding, the population-to-employment ratio is still well below where it was in 2007, while the Federal Funds rate is still close to zero. Regardless of whether or not it was the initial shock of China that led most of the developed world to become stuck in a liquidity trap, the most pressing question in economic policy today is undoubtedly the question of the efficacy of monetary policy in a liquidity trap (the situation in which central banks lower short-term interest rates all the way to the zero lower bound). Many people have believed that once a central bank hits the zero lower bound, monetary policy has run its course as President Obama once remarked to Christina Romer, the Chairwoman of his Council of Economic Advisors.[1] However, recent research, including Krishnamurthy and Vissing-Jorgenson (2011) suggests that QE (quantitative easing) can be effective, while Denmark has recently lowered its prime rate to -.75, suggesting that monetary policy isn't as impotent at the zero lower bound as had been previously thought. However, this is very much still an active and evolving area of research, and ripe for new contributions. (*I.e.*, what is the impact of QE announcements on exchange rates? Do the Krishnamurthy results hold up for more recent

announcements? How did other non-standard monetary policies impact countries caught in liquidity traps during the Great Depression?)

Yet, if monetary policy can be effective at the zero lower bound, then why have the US, Europe, and Japan been stuck in liquidity traps for so long? Ben Bernanke wrote that the problem in Japan lied not in its stars but in its central bankers – he famously called for some “Rooseveltian Resolve” at the Bank of Japan to provide more vigorous measures to stimulate the economy. During most of the period from 1995-2014, the Bank of Japan did nothing. From 1955 to 2008, there had never been a six month period in which the US Federal Reserve had left the Federal Funds Rate constant for more than 6 months, but from the end of 2008 to the end of 2010, the Fed left interest rates constant and also made no substantive changes to its balance sheet. During their periods in liquidity traps, the central banks in Europe, the US, and Japan all have also repeatedly tightened monetary policy, and then subsequently had to reverse course soon after when the great stagnation continued. The problem, in short, then appears not to be that the tools of central bankers are not effective, but rather that when central bankers find themselves in a liquidity trap – an unfamiliar policy environment, they become very passive. Research testing the reaction function of central bankers as a function of economic news and whether an economy is at the zero lower bound would be helpful. An example would be to use data on surprises in Economic Announcements to trace out how the market views central banks as responding over time, and compare this with how the market has reacted to central bank meetings.

### **Trade**

In a working paper (Campbell 2010) proposed that due to persistence in habits and market-specific learning-by-doing, that the widely-used gravity equation should be replaced with a dynamic gravity equation. It would also be interesting to measure the impact of various changes in trade policy on trade in a dynamic context. For example, while there is work suggesting that NAFTA had a large impact on trade, there are some severe shortcomings of this research, which does not provide evidence of how this played out over time, nor does it provide clear estimates of the impact of NAFTA on manufacturing employment. And, what impact have changes in Russian trade policy had on Russian trade and employment in recent years?

### **Discrimination**

In a recent working paper, Lusher, Campbell, and Carrell (2015) find that, for a large public university in California, when students have a TA of the same race, they get substantially higher grades. The result was only there for courses with exams graded by TAs and was not statistically significant for courses with scantron (computer) grading. Thus the results likely suggest some kind of bias in grading. In a randomized experiment, Bertrand and Mullainathan (2003) sent out resumes with typically white and black names, and found that companies responded more quickly and more often to resumes which had conventionally white names. What would happen if such a study were conducted in Russia with minority names vs. common Russian names?

### **Example Thesis Titles**

*The Local Labor Market Impact of the Rise of China on Russian Manufacturing*

*The Impact of Free Trade Agreements on Russian Manufacturing*

*The Impact of the Rise of China on the XXXX Manufacturing Sector (Insert your favorite country here: XXXX)*

*The Euro, Relative Price Movements, and Euro Area Imbalances*

*Collapse: The Local Economic Consequences of Real Exchange Rate Movements (on the US)*

*Monetary Policy at the Zero-Lower Bound: A Case of Self-Induced Paralysis?*

*Fiscal Policy Multipliers In-and-out of a Liquidity Trap: Evidence from Policy Announcements Using High-Frequency Identification*

*Monetary Policy in a Liquidity Trap: Evidence from Policy Announcements Using High-Frequency Identification*

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[1] In fact, the President's remark was far more crude – he remarked that monetary policy had "shot its wad".