

Discussion: Quantifying the Benefits of Labor Mobility in a Currency Union

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Research Question: Factor Mobility under a Currency Union

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- Mundell hypothesis: factor mobility and flexible exchange rate are substitutes in achieving efficient allocation outcome
- Some naive economics
 - Flexible exchange rate effectively “corrects” relative price and wage across countries, a main source of inefficiency in the typical NK models
 - Factor mobility: if prices cannot move, let’s move quantities to accommodate the fixed prices

This Paper

- Empirics: Description of labor immobility in the Euro area and US
 - Negative migration response to unemployment rate
 - Stronger response across states in the US than in Euro area countries

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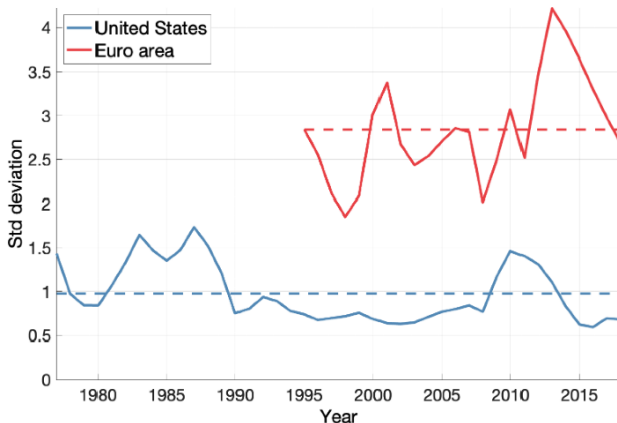
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- Quantitative model: a formal evaluation of Mundell's hypothesis
 - A multicountry DSGE model featuring price/wage rigidity, international goods trade, labor mobility and different exchange rate regimes
 - An estimated version of the model quantifies the effect of labor mobility in a currency union

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- Quantitative model: a formal evaluation of Mundell's hypothesis
 - A multicountry DSGE model featuring price/wage rigidity, international goods trade, labor mobility and different exchange rate regimes
 - An estimated version of the model quantifies the effect of labor mobility in a currency union
- Key insights
 - Demand shock dominates: factor mobility substitutes flexible exchange rates in achieving flexible price outcome
 - Supply shock dominates: factor mobility deviates even further to the flexible price outcome

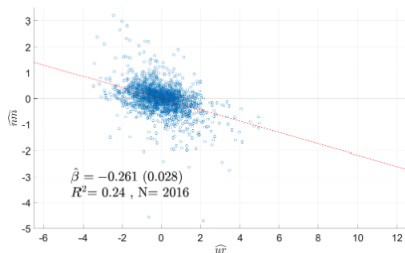
Stylized Fact #1

Unemployment differentials are much larger across countries in the Euro area than across states in the US

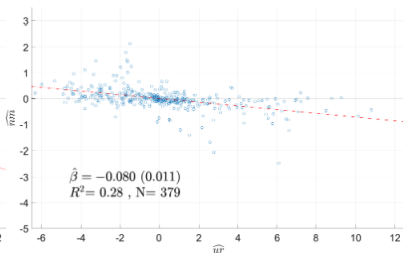


Stylized Fact #2

A response of migrant outflow in response to a higher unemployment rate. The response is stronger across US states than across Euro area countries

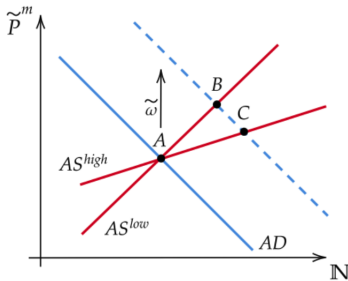


(a) UNITED STATES: 1977 - 2018

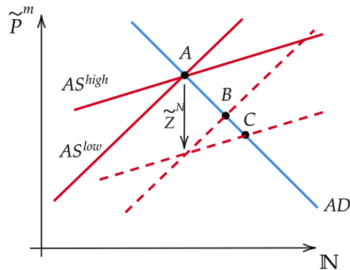


(b) EURO AREA: 1995 - 2018

The Economics from a Simplified Model



(a) Response to positive demand shock



(b) Response to positive supply shock

Figure 7: EFFECT OF LABOR MOBILITY IN SIMPLIFIED MODEL

Desirable policy: stabilizing \tilde{P}^m

Quantitative Model: Main Ingredients

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 - Tradable productivity differs across countries: **comparative advantage**
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- Monetary policy (Mankiw rule) and alternative exchange rate regimes

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- Welfare assessment
 - If demand (supply) shocks are dominant, labor mobility alleviates (exacerbates) the cost of business cycles under the currency union
 - In the estimated model, supply shocks are dominant, so labor mobility does not substitute independent monetary policy

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 - Empirics: consider commuters as non-migrants since the measure is population-based
 - Model: not allowing for commuters: if a worker moves from i to j , she works and consumes in country j

Why Does It Matter? Empirics

- Cross-border commuters are common
- The current empirical analysis does not count commuters as workers that change working location, which may underestimate the migration response to unemployment rate differential
- May also complicate measurement: a worker living in France works in Germany leads to a decrease in French unemployment rate, but the actual production takes place in Germany

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- May also complicate measurement: a worker living in France works in Germany leads to a decrease in French unemployment rate, but the actual production takes place in Germany
- **Suggestion:** If data allows, check robustness of the results separately for commuters, migrants and address the measurement concern
- **Suggestion:** Data near the border can be very informative in distinguishing commuting vs. migration

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- **Suggestion:** Consider two extreme cases, all migrants (the current model) and all commuters

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- **Suggestion:** Elaborate how will the model change if we adopt the standard IRBC specification (Stockman and Tesar' 95)

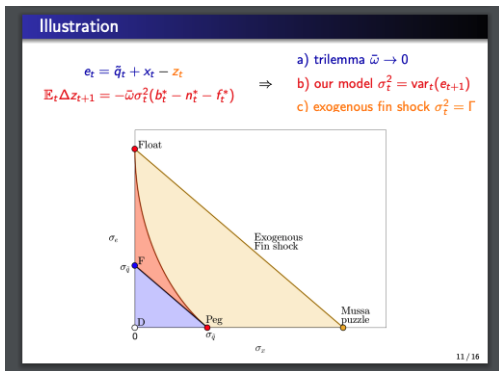
Comment #3: The Source of Exchange Rate Fluctuations

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 - Absorbs shock and overcomes inefficiencies due to stickiness
- Recent literature highlighting the financial determination of exchange rate, in which a significant portion of exchange rate fluctuations come from financial market frictions (Itskhoki and Mukhin'21)
- Does not affect the currency union result, but affects the welfare implication of flexible exchange rates, and thus affects the comparison

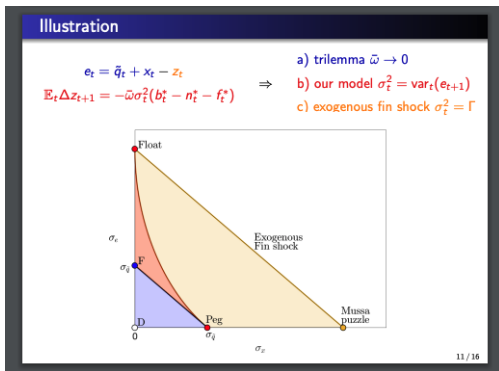
Floating Exchange Rates



Source: Oleg Itskhoki's presentation slides of "Optimal Exchange Rate Policy"

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- **Suggestion:** Check the robustness of welfare comparison allowing for financial frictions (if possible)

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- The labor market in the current paper is very simple: a labor union sets the wage and firms make hiring decisions

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- In reality, richer labor market dynamics across countries/states, e.g., job search, job posting, changing tightness, different responses of heterogeneous worker, etc (Todd and Zhang'22)
- May be too complicated to incorporate into the model, but worth empirically examining job posting rate, vacancy filling rate and market tightness for high- and low-skilled labor across countries
 - Deserve a separate paper

Conclusion

- An excellent paper, answering a first-order important question with rich economics and clear policy implications, I learn a lot
- Nice facts, clear economics and solid quantitative analysis
- Main suggestions
 - More discussion on migrants vs. commuters
 - Clarify what Eaton-Kortum trade structure brings
 - Check the robustness of welfare comparison considering exchange rate fluctuations due to financial frictions