Self-Harming Trade Policy? Protectionism and Production Networks^a

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^aThe views and opinions expressed are those of the authors alone and do not necessarily reflect those of the Central Bank of Chile.

1 Intuition and Mechanisms

2 Empirical Implementation

3 Final Remarks

Intuition and Mechanisms

The propagation of import shocks on employment depends on 4 elasticities (Huneeus et al, 2020)

1. Elasticity of substitution of intermediate inputs, δ

2. Elasticity of substitution between labor and intermediate inputs, ϵ

- 3. Elasticity of substitution of demand, σ
- 4. Labor supply elasticity, γ

For example: \uparrow Input cost $\Rightarrow \downarrow$ Employment if $\sigma > \epsilon$

- Prices: Import shock increases input and output prices
 - \blacksquare Test the mechanism directly in the data: Cost shock \Rightarrow Input prices \Rightarrow Employment
 - \blacksquare Is the timing consistent? \Rightarrow Employment starts declining before increase in input price
 - Can you measure wages as well?
 - If doing that, then why not estimate the labor-materials elasticity of substitution? $\Rightarrow \log(E_{it}^M/E_{it}^L) = c + (\epsilon - 1)\log(W_{it}/Z_{it}) + (1 - \epsilon)\log\omega_{it}$

Comment 1: The Mechanisms behind the Propagation of Import Shocks

- **ES of Demand:** Employments effects are larger in industries with higher σ
 - Separate within vs between-industry ES
 - Results seem more consistent with between-industry ES
 - Within industry, the effects might go in the opposite direction
 - i.e., if shocks are idyosincratic and it is easier to substitute across firms within industry
- Would be interesting to explore heterogeneity of ES of inputs (δ)
 - Are effects stronger in industries where inputs are more specific? (Barrot & Sauvagnat, 2016)
- Is it possible to explore heterogeneity of labor supply elasticity (γ)
 - Are effects stronger in industries with a higher labor supply elasticity?

Empirical Implementation

Comment 2: Decomposition, Persistence, Heterogeneity

- Could implement Rotemberg weights to understand which countries and product drive the results
 - Exploit shift-share design (Goldsmith-Pinkham, Sorkin, Swift, 2020)
 - Same for downstream propagation
- **Take into account the persistence of the shock**, which is different to the persistence of $\hat{\epsilon}_{it}$
 - Adjust estimates in the spirit of Boehm et al. (2020) \Rightarrow Recover short vs medium-run trade elasticity
- Exploit heterogeneity (both the own and the network propagation) in:
 - 1. Industry exposure to export intensity (Handley et al., 2020)
 - 2. Industry exposure to import intensity
- Test also upstream propagation \Rightarrow Think of these shocks as demand shocks
 - Might be important to control for this when evaluating downstream propagation?

Final Remarks

- Relevant topic, good design and data, super interesting facts
- Looking forward to future versions and more research in these topics