

Discussion—Davide Furceri (IMF)

**Policy Shocks and Wage Rigidities: Empirical Evidence from
Regional Effects on National Shocks
by Maarten de Ridder and Damjan Pfajfar**

**12th ECB/CEPR Labor Market Workshop
Frankfurt, 13-14 December 2016**

What the paper does

Aim: the effect of wage rigidity on the transmission of monetary and fiscal policy shocks

Approach:

- Estimate state-specific measures of DNWR
- Interact these with monetary and fiscal policy shocks
- Estimate IRFs using LP and smooth-transition function for different regimes (low vs. high wage rigidity)

Finding

- Effect of mp larger in states with high DNWR—particularly for contractions
- Larger fiscal multipliers in state with high DNWR

About my discussion

Comments on the paper:

- Overall
- Detailed
- Suggestions for extensions

New stuff:

- Do the results of the paper can be extended to EA?
- Is there a trade-off between the response of unemployment and inequality depending on DNWR?

General Comments

- **Great paper!**
- **intuitive results, sound empirical analysis (though for a discussant)**
- **...but still some room for improvement**
- **Possible extensions**

Detailed Comments—I

- **Controls vs. alternative factors**
 - Is DNWR affecting the response of MP (FP) or other factors?
 - Mobility (which could also affect DNWR)
 - Price flexibility?
 - Financial dependence—High DNWR those where firms rely more on external finance
 - Hiring/firing turnover—High DNWR those where firms rely more on firing/hiring
- **DNWR is an outcome, which policy variables affect the transmission channel?**
 - Unionization? Minimum Wage? Union power?
 - Repeat the analysis testing for these factors?

Detailed Comments—II

- **DNWR is endogenous**
 - Use time-average for each country—but won't solve the issue
 - Admit limitations
- **Fiscal shocks**
 - Why not aggregate one: Ramey, Auerbach and Gorodnichenko, Romer and Romer?
 - 2SLS—standard errors second stage are biased. How do you address this?
 - Should we not distinguish between expansionary and contractionary shocks?
- **Others**
 - Value of smooth transition parameter is arbitrary. Robustness check
 - DNWR is an estimated variable. Robustness check (WLS, Bootstrap)
 - Larger effects during recessions? One would expect so.

Do the results applies also to other AEs?

Identification of shocks (Furceri and other 2016)

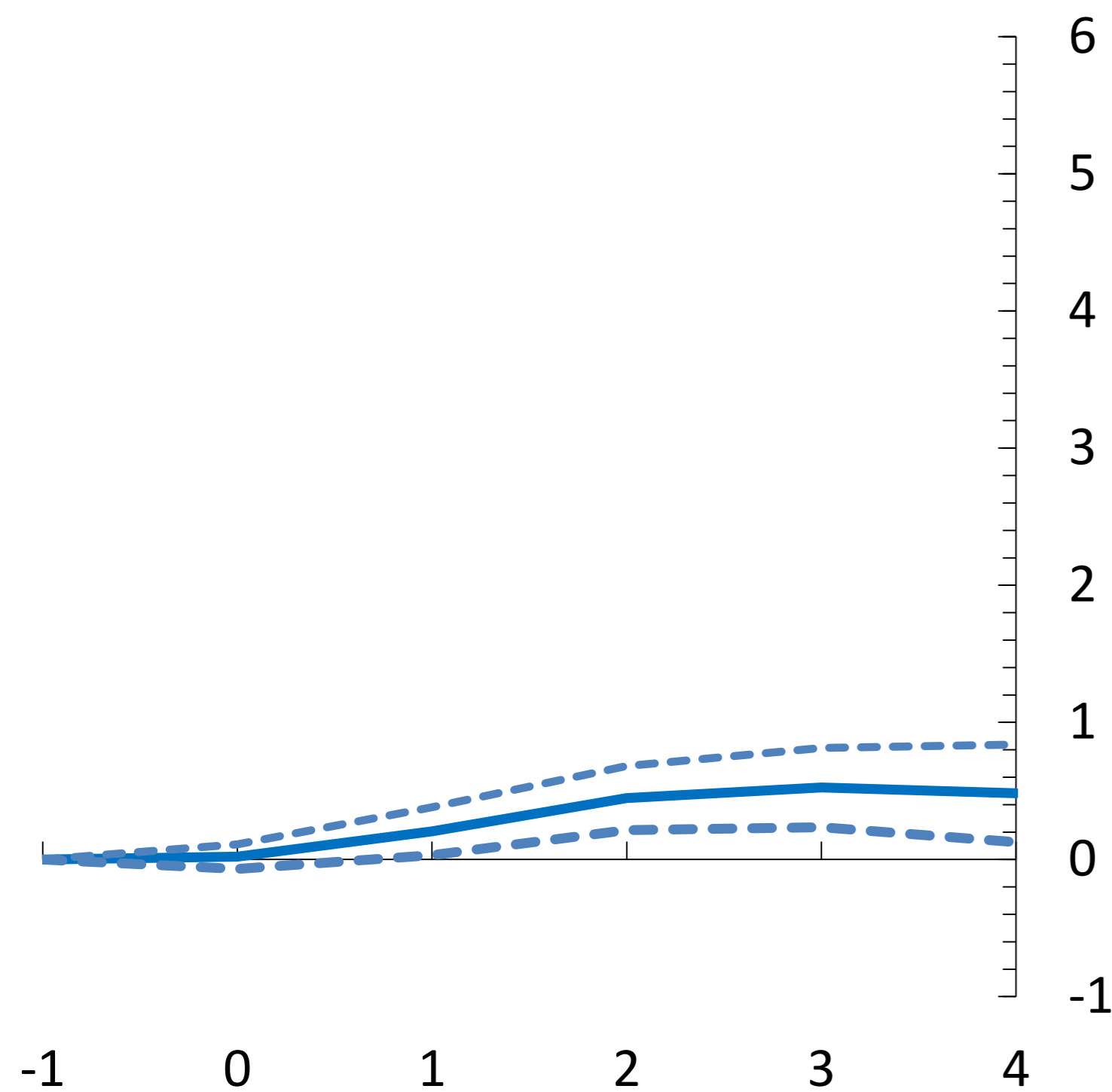
$$FE_{i,t}^i = \alpha + \beta FE_{i,t}^{inf} + \gamma FE_{i,t}^g + MP_{i,t}$$

- FE^i is the difference between the actual policy rate and the rate expected (*Consensus forecasts*);
 - FE^{inf} is the forecast error of inflation;
 - FE^g is the forecast error of growth.
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- Estimate LP to unemployment. DNWR from Holden and Wulfsberg (2007)

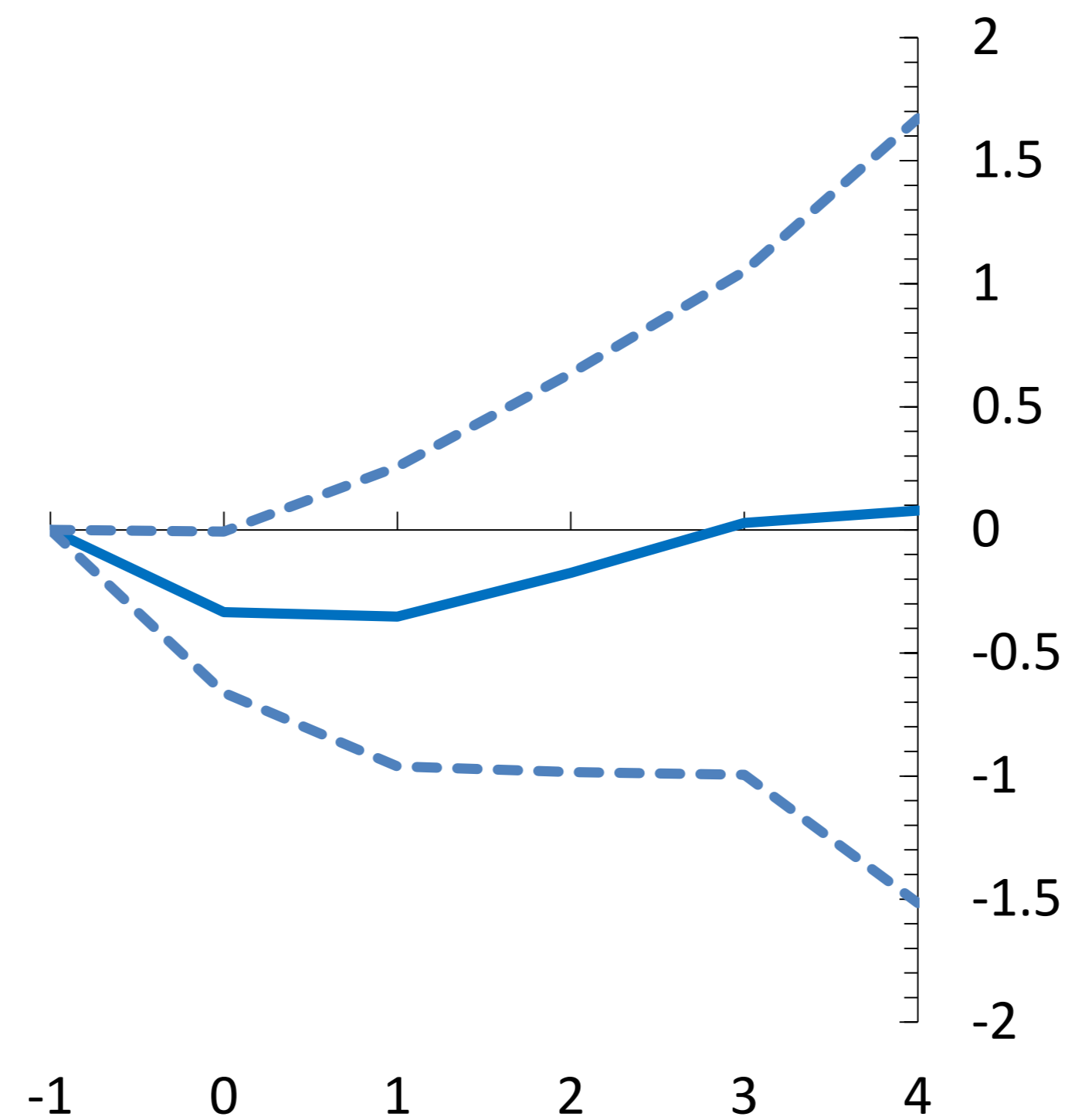
Effect of Policy Shocks on Unemployment

Effect of a 100 bps exogenous increase in policy rates

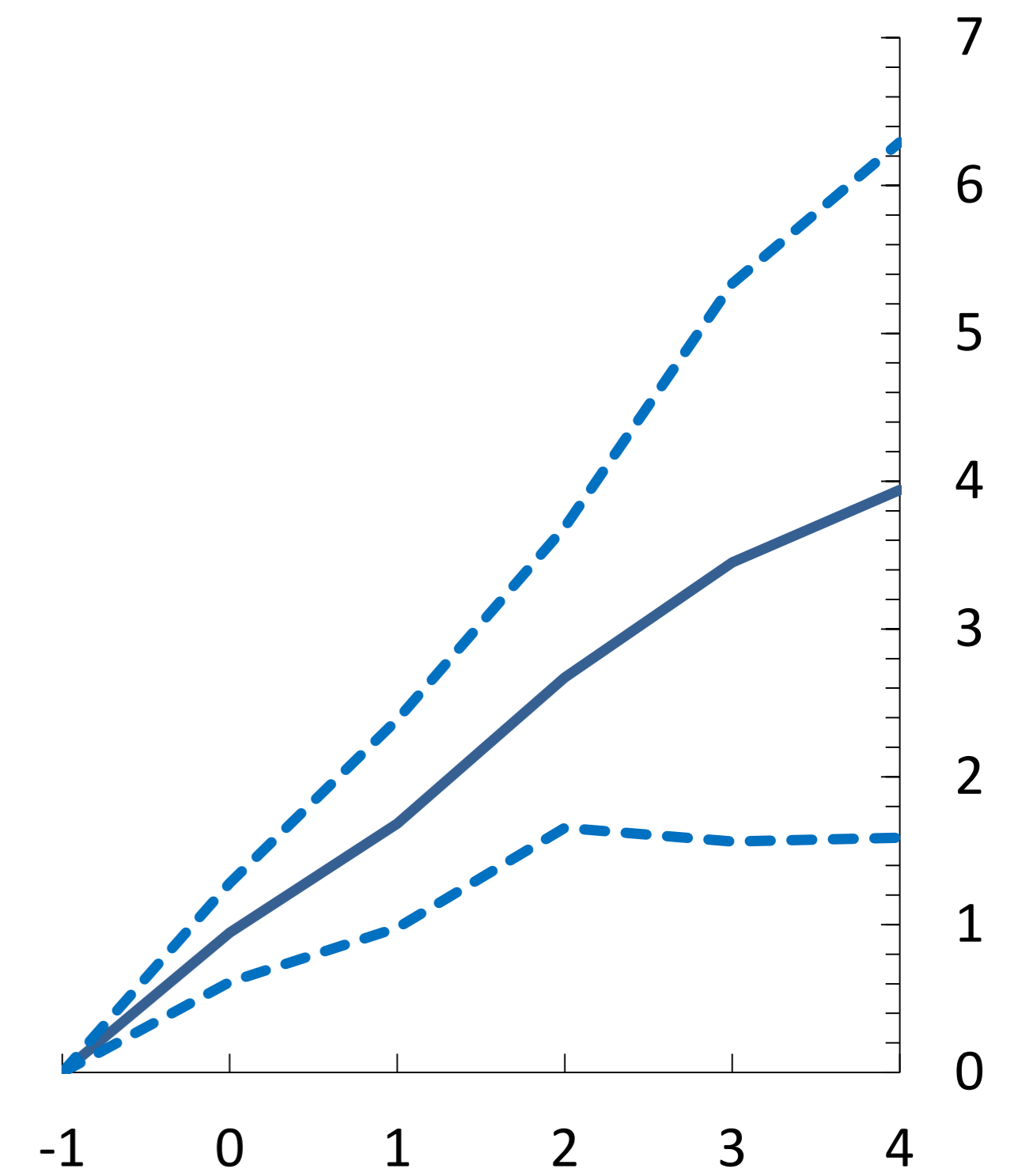
Panel A. Normal time (ppt)



Panel A. Low DNRW (ppt)



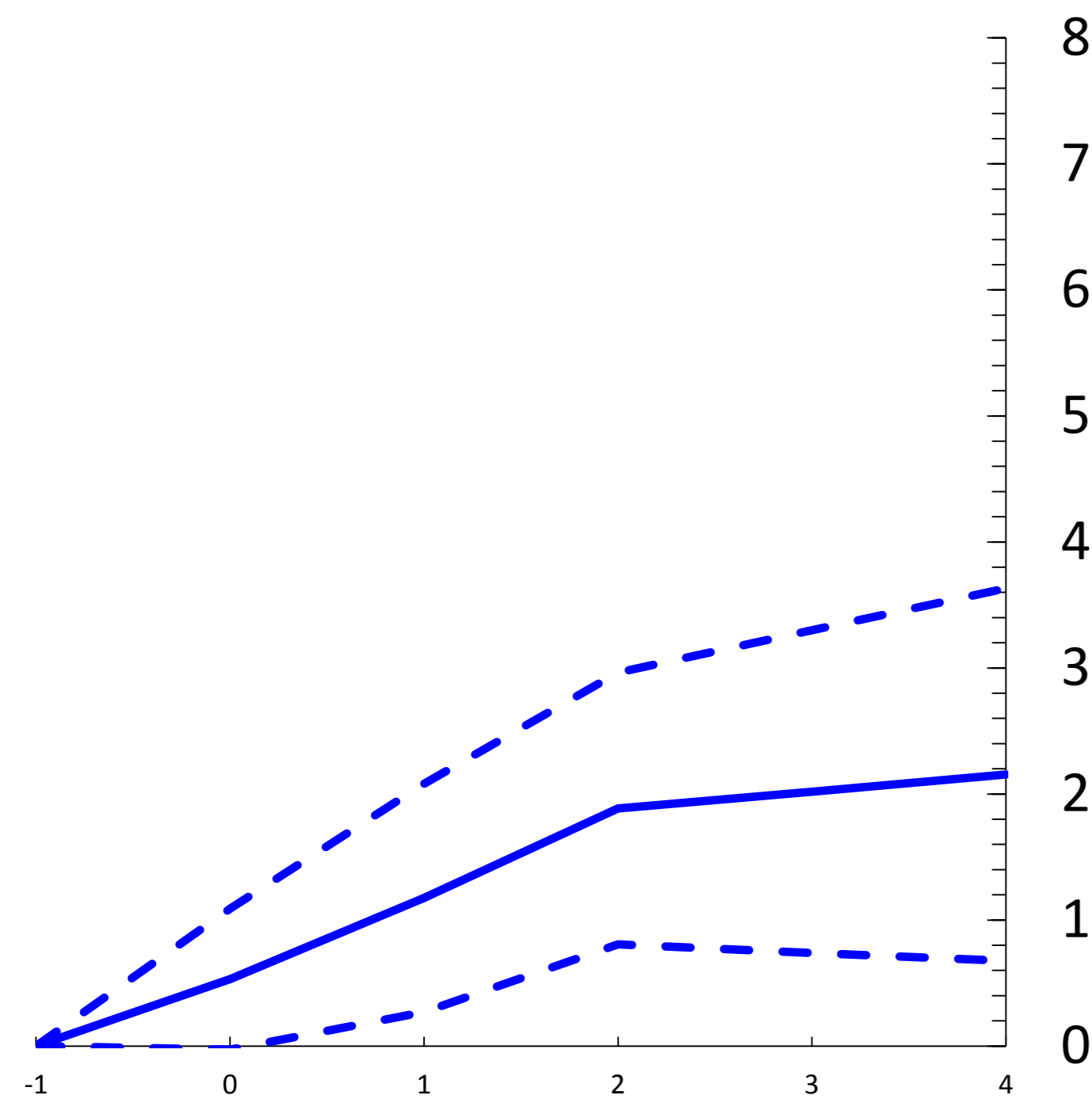
Panel A. High DNRW (ppt)



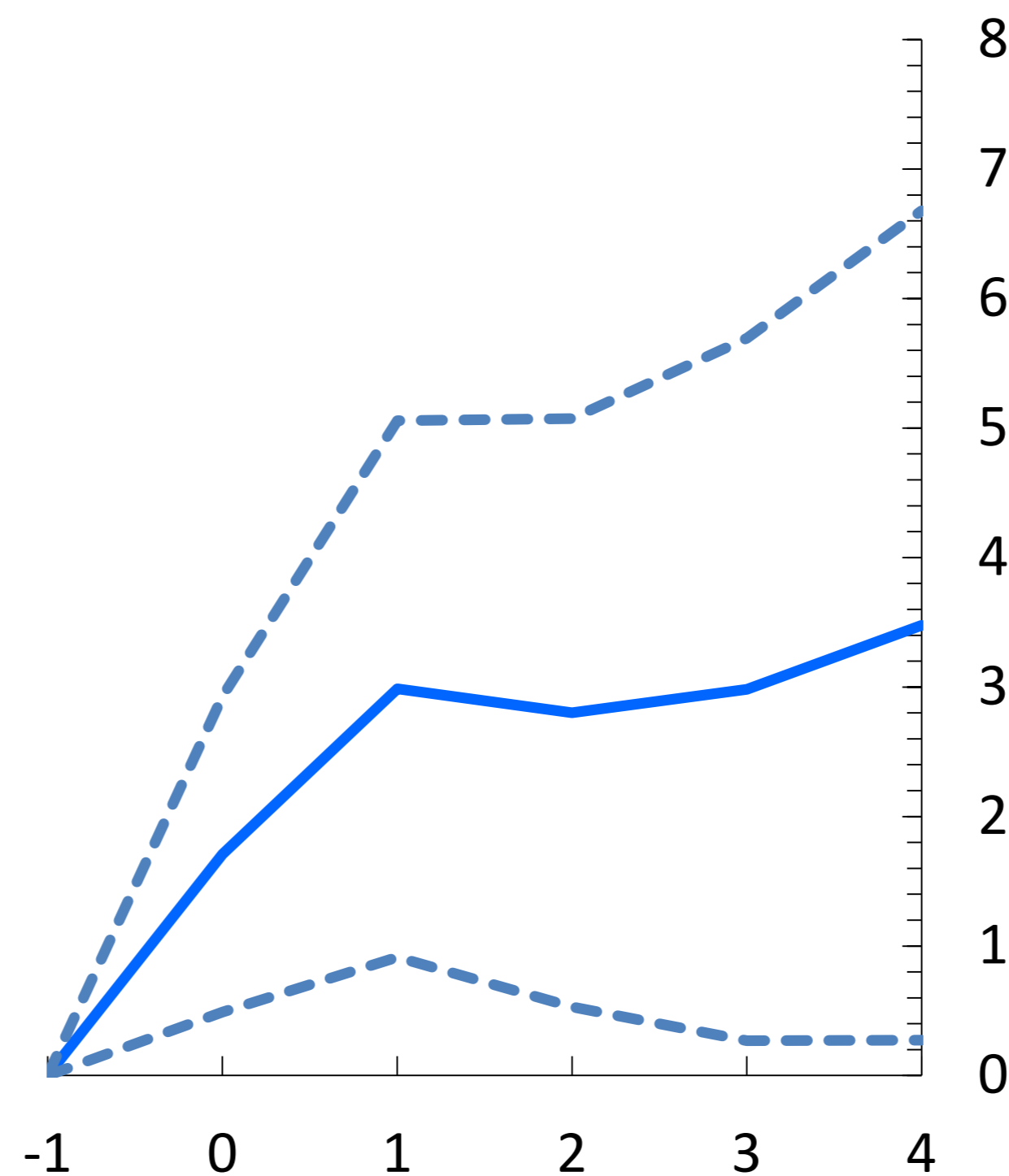
Effect of Policy Shocks on Inequality

Effect of a 100 bps exogenous increase in policy rates

Panel A. Normal time (ppt)



Panel A. Low DNRW (ppt)



Panel A. High DNRW (ppt)

