

Liberalization and Policies to Facilitate Labor Market Adjustment

Discussion

Guido G. Porto
Universidad Nacional de La Plata

Latin American and Caribbean Labor Markets and the Global Economy
Santiago, Chile

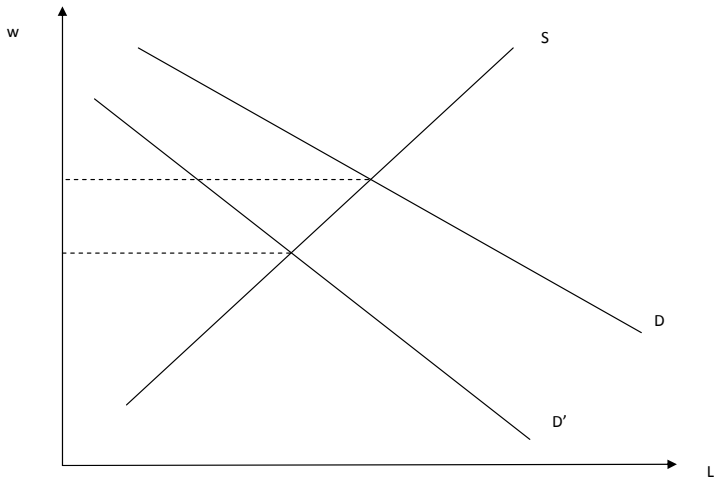
UN-ECLAC Headquarters

June 14-15, 2011

Discussion on Trade Adjustment Costs

- Marion Jansen: “Adjustment to Trade Liberalization”
- Nanno Mulder: “Trade Openness and Wage Gaps in Chile”
- José Antonio Rodríguez López: “Trade and Occupational Employment in Mexico Since NAFTA”

Motivation: No Adjustment, No Gain



A Quick Example: Argentina

- Bet, Brambilla and Porto (2011): Dynamic structural model (Artuç et al. (AER, 2010) + Cooper et al. (RES, 2006))

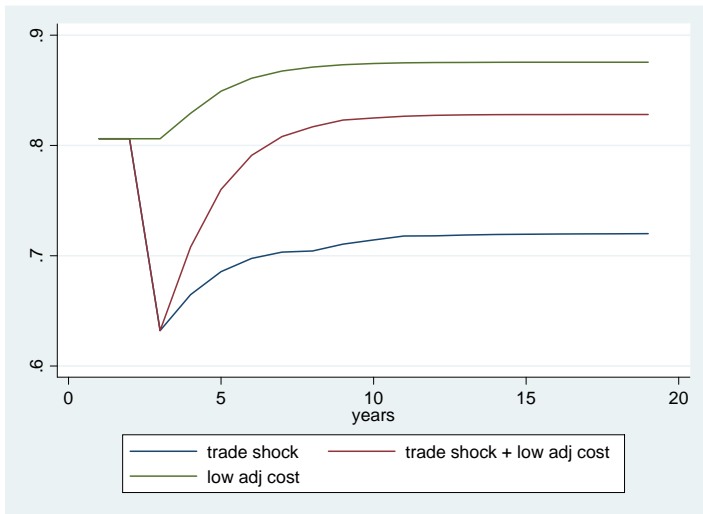
A Quick Example: Argentina

- Bet, Brambilla and Porto (2011): Dynamic structural model (Artuç et al. (AER, 2010) + Cooper et al. (RES, 2006))
- Firms:
 - 5 manufacturing sectors + 1 non-tradable
 - Profit maximization with factor adjustment costs (to be discussed)
 - Dynamic optimization delivers: supply functions + demand functions for labor in each sector

A Quick Example: Argentina

- Bet, Brambilla and Porto (2011): Dynamic structural model (Artuç et al. (AER, 2010) + Cooper et al. (RES, 2006))
- Firms:
 - 5 manufacturing sectors + 1 non-tradable
 - Profit maximization with factor adjustment costs (to be discussed)
 - Dynamic optimization delivers: supply functions + demand functions for labor in each sector
- Workers:
 - Maximize utility: demand functions (no leisure)
 - Supply labor
 - Workers can move at a mobility cost \rightarrow wage differential and individual shocks generate bilateral flows of workers across sectors and these flows define the supply of labor to different sectors

Evolution of Wages: Food & Beverages



Trade & Factor Adjustment Costs

- What do we care about?

Trade & Factor Adjustment Costs

- What do we care about?
- The welfare costs of trade reforms with costly factor adjustment
 - lost income, wages, profits
 - high in the short run, high for affected individuals (the unemployed)
 - mixed results when compared to overall intertemporal gains (sometimes high, sometimes small; higher in developing countries)

Trade & Factor Adjustment Costs

- What do we care about?
- The welfare costs of trade reforms with costly factor adjustment
 - lost income, wages, profits
 - high in the short run, high for affected individuals (the unemployed)
 - mixed results when compared to overall intertemporal gains (sometimes high, sometimes small; higher in developing countries)
- Sources of costly factor adjustment
 - what are the sources of labor adjustment costs?
 - what are the sources of capital adjustment costs?

Trade & Factor Adjustment Costs

- What do we care about?
- The welfare costs of trade reforms with costly factor adjustment
 - lost income, wages, profits
 - high in the short run, high for affected individuals (the unemployed)
 - mixed results when compared to overall intertemporal gains (sometimes high, sometimes small; higher in developing countries)
- Sources of costly factor adjustment
 - what are the sources of labor adjustment costs?
 - what are the sources of capital adjustment costs?
- The sources of the sources
 - What can we do about this?

Adjustment Costs in Labor

- Why is adjustment costly in labor markets?

Adjustment Costs in Labor

- Why is adjustment costly in labor markets?
- Worker Labor Mobility Costs: Artuç, Chaudhuri and McLaren (AER, 2010); Dix-Carneiro (WP, 2010)
- Worker Sector-specific Experience: Dix-Carneiro (WP, 2010), Davidson and Matusz (IER, 2006)

Adjustment Costs in Labor

- Why is adjustment costly in labor markets?
- Worker Labor Mobility Costs: Artuç, Chaudhuri and McLaren (AER, 2010); Dix-Carneiro (WP, 2010)
- Worker Sector-specific Experience: Dix-Carneiro (WP, 2010), Davidson and Matusz (IER, 2006)
- Firm firing and hiring costs: Kambourov (RES, 2009), Dix-Carneiro (WP, 2010)

Adjustment Costs in Labor

- Why is adjustment costly in labor markets?
- Worker Labor Mobility Costs: Artuç, Chaudhuri and McLaren (AER, 2010); Dix-Carneiro (WP, 2010)
- Worker Sector-specific Experience: Dix-Carneiro (WP, 2010), Davidson and Matusz (IER, 2006)
- Firm firing and hiring costs: Kambourov (RES, 2009), Dix-Carneiro (WP, 2010)
- Market Frictions: Cosar (WP, 2009), Cosar, Guner and Tybout (NBER, 2010)

The Sources: Distortions

- Labor market flexibility *longrightarrow* Rodríguez-López
- Regulations
- Unions *longrightarrow* Nanno results
- Taxes
- Policy uncertainty

The Sources: Distortions

- Labor market flexibility *longrightarrow* Rodríguez-López
- Regulations
- Unions *longrightarrow* Nanno results
- Taxes
- Policy uncertainty
- Think about costs and benefits...

Adjustment Costs in Capital

- Firms need to invest in product lines, machines and equipment
- Entrants must incur significant startup costs

Adjustment Costs in Capital

- Firms need to invest in product lines, machines and equipment
- Entrants must incur significant startup costs
 - fixed adjustment costs: increasing returns in installing new capital and in restructuring production activity
 - quadratic adjustment costs: increasing costs in the incorporation new capital, in the reorganization of production lines and in worker's training
 - partial investment irreversibilities: transactions costs (reselling costs, capital specificity and asymmetric information)

Adjustment Costs in Capital

- Firms need to invest in product lines, machines and equipment
- Entrants must incur significant startup costs
 - fixed adjustment costs: increasing returns in installing new capital and in restructuring production activity
 - quadratic adjustment costs: increasing costs in the incorporation new capital, in the reorganization of production lines and in worker's training
 - partial investment irreversibilities: transactions costs (reselling costs, capital specificity and asymmetric information)
- Bloom (ECA, 2009); Caballero and Engel (ECA, 1999); Cooper and Haltiwanger (RES, 2006)

The Sources: Distortions

- Imperfect capital markets
- Credit markets *longrightarrow* Rodríguez-López
- Risk
- Uncertainty

Conclusions

- It is costly to reallocate factors
- The gains from trade are reduced, but they do not vanish
- Protection is not the way to go
- How to improve/facilitate factor mobility?
- Compensation mechanisms?