Discussion of

# Capital Allocation and Productivity in South Europe

by Gopinath, Kalemli-Ozcan, Karabarbounis and Villegas-Sanchez

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# Two **big** literatures

1. Misallocation literature (Hsieh and Klenow, 2009)
   - Measurement of misallocation in capital and labor across firms
   - Large differences across rich and poor countries
   - Large potential contribution to TFP differences
   - **But**: no evidence in the time series
     (and no exploration of panel data properties of misallocation)

2. Financial frictions literature (Kiyotaki and Moore, 1997)
   - A natural model for thinking about misallocation of capital
   - Baseline framework for modeling Great Recession
   - Strong micro-data implications for patterns of misallocation
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3. This paper: happy marriage of the two!

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  (b) Stagnant (somewhat declining) TFP until 2008, then a drop
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  $\longrightarrow$ a reduction in interest rate in 1995
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- What's **missing** from the story:
  (a) Misallocation across sectors: construction vs manufacturing
  (b) Nominal and real wages inflation
  (c) Welfare evaluation

# Misallocation accounting I

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  1. Firm fixed effects dominate the dispersion of wedges (70%)
  2. Large firms too small and small firms too large ($\mathrm{corr}$ of 0.25)
  3. Little evidence of dynamic misallocation: the large constrained firms were large for a long time
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- To me this suggestions small relative role for misallocation on the input side (adjustment costs or financial frictions) and large role for either markups or technology differences
- This, however, does not mean that input misallocation is not important for dynamics over time

# Misallocation accounting II

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- But the authors can go a lot deeper inside the mechanism at the micro level. For example:
  (a) Basic decompositions:

$$\mathrm{var}(y-k) = \mathrm{var}(y) + \mathrm{var}(k) - 2\mathrm{corr}(y,k)\sqrt{\mathrm{var}(y)\mathrm{var}(k)},$$
$$\mathrm{var}\big(a+\varphi_L(\ell-k)\big) = \mathrm{var}(a) + \varphi_L^2\mathrm{var}(\ell-k) + 2\varphi_L\mathrm{cov}(a,\ell-k),$$
$$\mathrm{var}\big(a-\varphi_K(\ell-k)\big) = \mathrm{var}(a) + \varphi_K^2\mathrm{var}(\ell-k) - 2\varphi_K\mathrm{cov}(a,\ell-k),$$

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  (c) Track the firms that received capital. Who were they?
  (d) Can you say more on entry and growth of new firms?
- The model can guide this slicing of the data and these patterns should discipline the modeling choices

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