Discussion of

Large Shareholders and Sticky Prices: Evidence from a Corporate Governance Reform

by Jin Xie, Kang Shi and Jenny Xu

Oleg Itskhoki

Princeton and UCLA

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Question

- Does corporate governance affect firm price setting?

- In particular, the extent of nominal rigidities?
  - few correlates of price stickiness in the data

- Connecting corporate finance with monetary economics

- Great data and a corporate governance reform in China

- Interesting results from an exchange rate pass-through framework

Empirical specification

$$ln(p_{i,p,d,s}) = \alpha + \beta_1 \cdot ln(RER_{s,d}) + \beta_2 \cdot ln(RER_{s,d}) \times Post_{i,t} \times Nontrade\%_i +$$

$$\beta_3 \cdot ln(RER_{s,d}) \times Post_{i,t} + \beta_4 \cdot ln(RER_{s,d}) \times Nontrade\%_i$$

$$+\beta_5 \cdot Nontrade\%_i \times Post_{i,t} + \beta_6 \cdot Post_{i,t} + \beta_7 \cdot Nontrade\%_i \quad (3)$$

$$+\gamma \times Z + \epsilon_{i,p,d,s}.$$

- The coefficient of interest: $\beta_2 < 0$

- Interpretation:
  firms with a corporate government issues (high *Nontrade*)
  exhibit lower pass-through (=more "pricing-to-market")
  post reform, which alleviates the incentive problem

- Additionally: allocative effects of prices on quantities

Background: Framework
(see Amiti, Itskhoki and Konings, 2019, working paper)

- Desired price:

$$\tilde{p}_i = \max_p \Pi(p|\Omega)$$

- Markup identity (all in logs):

$$\tilde{p}_i = \mu_i + mc_i$$
$$= (1 - \alpha_i)mc_i + \alpha_i p_{-i}$$

- Reset price:

$$\bar{p}_i = \mathbb{E}\tilde{p}_i$$

- Observed price:

$$p_i = (1 - \theta_i)\tilde{p}_i + \theta_i \bar{p}_i$$
$$= (1 - \theta_i)(\mu_i + mc_i) + \theta_i \bar{p}_i$$

- In what currency is $\bar{p}_i$ sticky?

Exchange Rate Pass-through (ERPT)

1. Marginal cost mc_i depends on exchange rate due to intermediate inputs:

$$\Delta mc_i = -\varphi_i \Delta e$$

— Amiti, Itskhoki and Konings (2014, AER)

2. Markup μ_i depends on exchange rate due to strategic complementarities in price setting:

$$\mu_i = -\gamma S_i \Delta e$$

— Amiti, Itskhoki and Konings (2019, REStud)

3. Currency choice in pricing (sticky prices) is endogenously shaped by these firm characteristics:

$$\bar{p}_i = -\iota_i \Delta e$$

— Gopinath, Itskhoki and Rigobon (2010, AER)

Empirical Specification

$$\Delta p_i = \big[\overbrace{\underbrace{\alpha - \beta\varphi_i - \gamma S_i}_{\text{flex. price}} \underbrace{-\theta\, \iota_i}_{\text{sticky price}}}^{\text{ERPT}} \big] \cdot \Delta e + \text{F.E./controls} + \varepsilon_i$$

- This paper: introduces an additional determinant of ERPT
  — a corporate governance proxy *Nontrade*

- It further shows the differential effect before/after the reform, and a stronger diff-in-diff effect in certain destinations

- Two small questions:
  1. Regression in levels vs changes?
  2. Firm-time fixed effects?

Three main concerns

1. The specification in the paper does not control for standard determinants of ERPT:

   — size, intermediate inputs, currency choice

   — and they are likely correlated with *Nontrade*

2. The reform coincides with many other changes

   — sharp increase in world trade participation trade

   — end of a strong peg and RMB appreciation

3. There is no way to separate flexible price response (PTM) from the effects of sticky prices (LCP), namely intensive vs extensive margin of price adjustment

   — pricing to market (PTM) is not the same as sticky prices

   — data not suitable for this question as it features unit values, not transaction prices (*cf.* Gopinath and Itskhoki, 2010, QJE)

   — perhaps look at dynamics of prices

Correlation with size

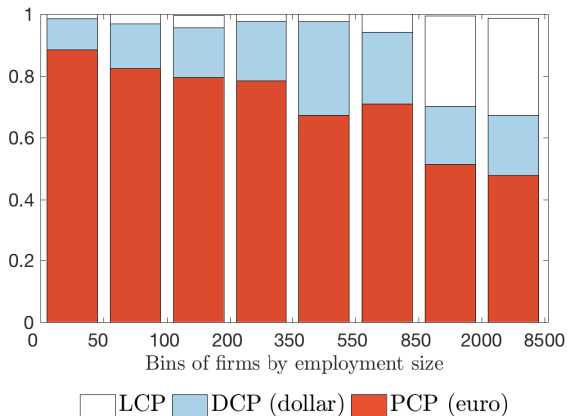(Amiti, Itskhoki and Konings, working paper)

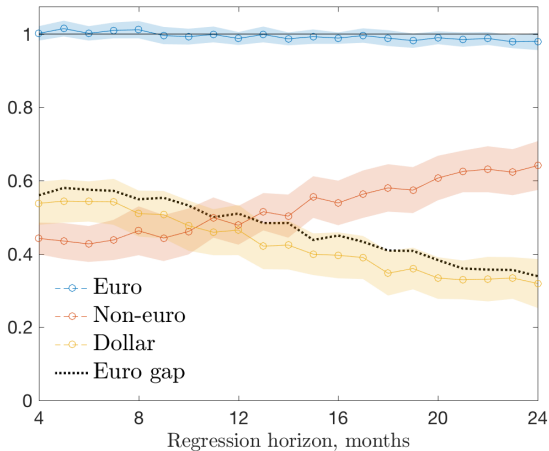Figure: Firm size and currency choice in exports

Dynamics of ERPT

(Amiti, Itskhoki and Konings, working paper)

Figure: Pass-through dynamics