BANQUE DE FRANCE
EUROSYSTÈME

Research Newsletter

EDITED BY THE DIRECTORATE GENERALE ECONOMICS AND INTERNATIONAL RELATIONS OF THE BANQUE DE FRANCE

2nd half 2012

Coming up

"Banking Models and Banking Structures" • Banque de France and Toulouse School of Economics conference • December 11, 2012.

"The economics of sovereign debt and default" • Banque de France, Sciences Po and CEPR • Paris, December 17-18, 2012.

"Globalization and Labor Markets" • Banque de France conference • May 16-17, 2013.

"Fourth Macroeconomics and Finance Conference" • Banque de France and Deutsche Bundesbank conference • May 23-24, 2013.

"Global spillovers and international cycles" • Banque de France/EABCN conference • May 30-31, 2012.

Past events

Conferences and symposiums

"Firm financing & default risk during and after the crisis" • organised by Banque de France and Oséo • Paris, February 9-10, 2012.

"Conference on data gaps for economies in the European Region" • organised by Banque de France • April 25-26, 2012.

"Macro-Finance" • organised by Science Po, Bern University, Wisconsin School of Business and Banque de France • June 29-30, 2012.

Editorial

Marc-Olivier Strauss-Kahn, Director General for Economics and International Relations

The Banque de France has for a long time been involved in research, but significant developments in recent years offer us a good opportunity to draw some first conclusions.

The organisation of research activities at the Directorate General, Economics and International Relations (DGEI) and, more generally, the Banque de France is particular in more than one respect and this organisation should be maintained and even strengthened.

Its first characteristic is that it does not concentrate research in a few units of the Bank, but enables most departments of the DGEI to conduct research work, alongside their other tasks (studies, forecasting, coordination, international affairs, etc.), in conjunction with the other Directorates General and the Prudential Supervision Authority (*Autorité de contrôle prudentiel*). This approach has the advantage of facilitating the creation of bridges between research and operational activities, as regards both topics studied and staff mobility.

A second characteristic is the diversity of research subjects. Of the publications of the DGEI in 2011, half cover "traditional" central bank issues (monetary policy, financial economics and inflation), while the other half deals with other topics: forecasting tools, international trade, fiscal policy, real estate and econometrics. Despite their differences, all of these topics contribute to the preparation and implementation of monetary policy and to the discussions on economic and financial stability.

Its third characteristic is to mix researchers with different profiles and to offer in-house career opportunities: in 2012, after several years of intensive recruitment at the DGEI, the number of managerial staff is equivalent whether they have passed the competitive entrance exam or have been offered a contract. This also holds true in the case of heads of division and their deputies.

These developments have generated a positive momentum evidenced by the spectacular progression of the Banque de France in international rankings. In the Saint Louis Fed RePEc ranking, which is based on publication stocks, the Bank climbed up from 186th position in Europe in 2008 to 65th at end-2011 and is now ranked among the top five percent of economic institutions worldwide and among the top 10 institutions in France. Roughly fifty articles are now published every year by Banque de France researchers, compared with 18 in 2006. The quality of publications has also improved: between 2009 and 2011, 9 publications were in Group 1 of the "Journal Quality and Impact Factor List" drawn up by the DGEI and based on three sources: the ECB, the CNRS and Mingers & Harzing (2007), compared with zero between 2006 and 2008; 2012 looks very promising.

Efforts must be pursued to consolidate these internal achievements and radiate outward. The partnerships established with academic institutions, the Toulouse School of Economics (TSE), the Paris School of Economics (PSE), Sciences Po, the University of Auvergne and shortly Aix-Marseille Sciences Economiques (AMSE) should contribute to this through mutual exchanges. Interactions are in place (seminars, exchanges with high-level academics such as Jean Tirole, interviewed in this letter) and should be intensified.

It is by pursuing these objectives of versatility and excellence and by further expanding its international reach that the Bank will continue to improve its research scoreboard.

Publications in the 1st half of 2012

"Financial variables as leading indicators of GDP growth: Evidence from a MIDAS approach during the Great Recession", L. Ferrara and C. Marsilli, *Applied Economics Letters*, May.

Labour Productivity and Compensation of Employees in Europe, D. Fuentes-Castro, *Applied Economics Letters*, May-June, 19 (7-9), pp. 689-93.

"Generalised Taylor and Generalised Calvo Price and Wage Setting: Micro-evidence with Macro Implications", H. Dixon and H. Le Bihan, *Economic Journal*, May, 122 (560), pp. 532-54.

"ICT Demand Behaviour: An International Comparison", G. Cette and J. Lopez, *Economics of Innovation and New Technology*, April-June, 21 (3-4), pp. 397-410.

« Fragmentation urbaine et chocs économiques : deux déterminants de l'offre de logements sociaux en France », G. Verdugo, *Économie et Statistique*, March, 446.

"Trade, Conflict, and Political Integration: Explaining the Heterogeneity of Regional Trade Agreements", V. Vicard, *European Economic Review*, January, 56 (1), pp. 54-71.

"The Rise of Emerging Economies in the EU15 Trade", G. Gaulier, F. Lemoine and D. Unal, *European Journal of Comparative Economics*, April, 9 (1), pp. 133-75.

"Reserve Requirements for Price and Financial Stability: When Are They Effective?", C. Glocker and P. Towbin, *International Journal of Central Banking*, March, 8 (1), pp. 65-113.

Discretionary Fiscal Policies over the Cycle: New Evidence Based on the ESCB Disaggregated Approach, L. Agnello and J. Cimadomo, *International Journal of Central Banking*, June, 8 (2), pp. 43-85.

"Comments on: Examining the quality of early GDP component estimates", L. Ferrara, *International Journal of Forecasting*, June.

"Employment and Productivity: Disentangling Employment Structure and Qualification Effects", R. Bourles, G. Cette and A. Cozarenco, *International Productivity Monitor*, April-May, 23, pp. 44-54.

"Tax Revenue Instability in Sub-Saharan Africa: Consequences and Remedies", C. Ebeke and H. Ehrhart, *Journal of African Economies*, January, 21 (1), pp. 1-27.

"Asset Pricing with Second-Order Esscher Transforms", A. Monfort and F. Pegoraro, *Journal of Banking and Finance*, June, 36 (6), pp. 1678-87.

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Three questions to... Jean Tirole

Economist, Professor. Toulouse School of Economics, MIT, EHESS.

Against the backdrop of the current European sovereign crisis, many policy proposals have revolved around transfer strategies based on explicit public bailout schemes by solvent states (e.g., eurobonds). Your recent research [1] has challenged that view. Could you explain why?

There are two different questions, one normative (are such joint-and-several liability schemes desirable?) and the other positive (are they likely to arise?).

As for the first question, one can think of joint liability as an insurance contract, in which guarantors commit to a rescue level in excess of what they would choose spontaneously ex post (once the mishap has materialised). As with any insurance contract, such solidarity can work only if moral hazard is reasonably under control; this is why both the Stability and Growth Pact and the more recent Fiscal Compact specify limits on deficits and debts (at least in principle, since enforcement institutions have so far failed to perform their duty, but that's another story; all eurobond proposals indeed call for a reinforcement of monitoring and compliance). Such an insurance contract facilitates the beneficiary's access to financial markets (Spain will borrow at lower rates if Germany's signature covers its debt) and raises global surplus.

The problem is that it is not in the interest of healthy states to commit to a joint liability. To be certain, the benefits of joint liability for Spain exceed the cost to Germany; the question is how Spain can compensate Germany for its solidarity. The very nature of the problem is that Spain has no money; it would have to borrow to compensate Germany, but this would only reinforce markets' doubts about the former's solvency. This insight does not mean that Germany will not help Spain ex post (since a Spanish default would impose both political and economic costs on Germany), but simply that it is not in its interest to go beyond what it will do spontaneously if faced with an impending Spanish default.

Joint-and-several liability by contrast can improve the welfare of all (a "Pareto improvement" in the jargon of economists) if designed before the veil of ignorance (countries are equally likely to face hardship). And even so conditions are required; in particular the likelihood that they face hardship simultaneously must be limited – otherwise the risk of domino effects is too large.

You mentioned the monitoring issue. Independent fiscal councils, veterans or newcomers, are somewhat heterogeneous across Europe. Given the inherent feature of the deficit bias, what in your opinion are the key features that might render their influence more effective in the future?

The first requirement is obvious, although it has faced much resistance in Southern Europe. The government cannot be judge and party; for instance, governments systematically overestimate the growth rate when preparing the budget; and they allocate some of the country's best minds to conceal the budget deficit through complex off-balance sheet arrangements. Fiscal councils therefore should be independent, as in Sweden or Germany for instance; they should validate growth forecasts, indicate before and during the implementation of the budget whether the trajectory of public finances is sustainable, and finally serve as experts for another independent actor, the courts in charge of constraining deviant budgetary behaviors.

In this respect the forthcoming *Haut Conseil des finances publiques* in France is a welcome innovation, even though the presence of equally independent members standing for European

1 Country solidarity, private sector involvement and the contagion of sovereign crises, mimeo IDEI, September 2012.

"The Impact of Unconventional Monetary Policy on the Market for Collateral: The Case of the French Bond Market", S. Avouyi-Dovi and J. Idier, *Journal of Banking and Finance*, February, 36, (2), pp. 428-38.

"Firm-Network Characteristics and Economic Robustness to Natural Disasters", F. Henriet, S. Hallegatte and L. Tabourier, *Journal of Economic Dynamics and Control*, January, 36, (1), p. 150-67.

"The Dynamics of US Inflation: Can Monetary Policy Explain the Changes?", F. Canova and F. Ferroni, *Journal of Econometrics*, March, 167 (1), pp. 47-60.

"Nowcasting German GDP: A comparison of bridge and factor models", P. Antipa, K. Barhoumi, V. Brunhes-Lesage and O. Darné, *Journal of Policy Modeling*, January.

"Firms and the Global Crisis: French Exports in the Turmoil", J. C. Bricongne, L. Fontagné, G. Gaulier, D. Taglioni and V. Vicard, *Journal of International Economics*, May, 87 (1), pp. 134-46.

"Has the CDS Market Influenced the Borrowing Cost of European Countries during the Sovereign Crisis?", A. L. Delatte, M. Gex and A. Lopez-Villavicencio, *Journal of International Money and Finance*, April, 31 (3), pp. 481-97.

"Optimal Extraction of a Polluting Nonrenewable Resource with R&D toward a Clean Backstop Technology", F. Henriet, *Journal of Public Economic Theory*, April, 14 (2), pp. 311-47.

"EU Enlargement and the Evolution of European Production Networks", L. Curra and S. Zignago, *Research in International Business and Finance*, May, 26 (2), pp. 240-57.

"The Predictive Information Content of External Imbalances for Exchange Rate Returns: How Much Is It Worth?", P. Della Corte, L. Sarno and G. Sestieri, *Review of Economics and Statistics*, February, 94 (1), pp. 100-115.

"Bank Output in the National Accounts: Methodological Aspects and Evaluation in the French Case (1980-2011)", M. Beaujour, *Revue d'Économie Financière*, June, 106, pp. 125-38.

"A Macro-prudential Regulation to Make Value Creation Really Sustainable?", O. Bandt and G. Levy-Rueff, *Revue d'Économie Financière*, June, 106, pp. 243-61.

interests would have increased its credibility and there is some debate as to whether its recommendations will be heard. Clearly some connection of these national councils with European institutions (the European Court of Justice and the European Commission for example) seems needed to reflect the fact that the implicit solidarity among countries makes Europe a large stakeholder in national policies.

Given the costs of the debt overhang problem in terms of investment and growth, shouldn't unsustainable sovereign debts in the euro area lead to the recognition that the no-bailout clause could be reinstated and that a framework for the orderly default of public debtors would be warranted?

As things stand, troubled countries may be unable to reduce their debt to sustainable levels solely through improved budget management. Europe will then face the unpalatable choice between debt repudiation and debt monetization. I would predict the former, although such bets are obviously risky. But orderly debt repudiation anyway won't suffice either, as troubled countries' efforts to keep budget under control and to improve competitiveness might stop once sovereign debts have been alleviated and market pressure has disappeared. Institutions are paramount. Policies keeping institutions roughly unchanged can buy time, but will not solve problems. European countries must accept substantial losses of sovereignty if they are to stay together.

Focus

Fluctuations in international trade and crises: the role of demand composition

The collapse of world trade following the 2008 financial crisis is for many observers an enigma. The decomposition of demand using input-output tables provides a key.

During the year that followed the financial crisis at the end of 2008, international trade collapsed to an unprecedented degree, a phenomenon that is difficult to reconcile with developments in demand, which fell during this period but to a lesser extent.

In an article to be published in the *American Economic Journal: Macroeconomic*s, Matthieu Bussière, Giovanni Callegari, Fabio Ghironi, Giulia Sestieri and Norihiko Yamano use the OECD input-output tables to estimate a new model that helps to better explain developments in international trade flows. These tables reveal that some components of GDP are more import-intensive than others, and it was precisely these that were most affected during the crisis: this is the case notably for investment and exports, which prove to be very procyclical.

M. Bussière, G. Callegari, F. Ghironi, G. Sestieri and N. Yamano, "Estimating Trade Elasticities: Demand Composition and the Trade Collapse of 2008-09",* American Economic Journal: Macroeconomics*, to be published.

Matthieu Bussière has headed the International Research Division since 2009, having worked at the ECB and IMF. He holds a Ph.D. in Economics from the European University Institute in Florence, an MA from Cambridge University and is a graduate of Sciences Po Paris. He has had articles published in *AEJ: Macro*, *Journal of International Money and Finance*, *Oxford Bulletin of Economics and Statistics*, *Review of International Economics*, and *The World Economy*.

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Banque de France Working Papers

384 “Forecasting GDP over the business cycle in a multi-frequency and data-rich environment”, M. Bessec and O. Bouabdallah.

383 “Macroeconomic forecasting during the great recession: the return of non-linearity”, L. Ferrara, M. Marcellino and M. Mogliani.

382 “How does fiscal consolidation impact on income inequality”, L. Agnello and R. M. Sousa.

381 “Price as a choice under nonstochastic randomness in finance”, Y. Ivanenko and B. Munier.

380 “Disintermediation or financial diversification? The case of developed countries”, M. Boutillier and J. C. Bricongne.

379 “A pitfall with DSGE-based, estimated, government spending multipliers”, P. Fève, J. Matheron and J.-G. Sahuc.

378 “A mathematical treatment of bank monitoring incentives”, H. Pagès and D. Possamai.

377 “Bank Monitoring incentives and optimal ABS”, H. Pagès.

376 “The changing role of expectations in US monetary policy: a new look using the Livingston survey”, A. Banerjee and S. Malik.

375 “The Dynamics of gasoline prices: evidence from daily French micro data”, E. Gautier and R. Le Saout.

374 “The Macroeconomic effects of reserve requirements”, C. Glocker and P. Towbin.

373 “Commonality in hedge fund returns: driving factors and implications”, M. Bussière, M. Hoerova and B. Klaus.

372 “Financial Regulation in General Equilibrium”, C. A. E. Goodhart, A. K. Kashyap, D. P. Tsomocos and A. P. Vardoulakis.

371 “Optimal price setting during a currency changeover: theory and evidence from French restaurants”, N. Berardi, T. A. Eife and E. Gautier.

370 “Changes in Wage Inequality in France: the Impact of Composition Effects”, G. Verdugo, H. Fraisse and G. Horny (in french).

369 “Rent building, rent sharing: a panel country-industry empirical analysis”, P. Askenazy, G. Cette and P. Maarek.

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Price and wage rigidity: micro evidence with macro implications

Macroeconomic price and wage rigidity models are extremely stylized. Hervé Le Bihan proposes an approach that is more consistent with both the observed distributions of price and wage durations and the stylized facts of monetary policy.

In DSGE models, which have become standard tools for analysing and defining monetary policy, an important role is given to the assumption of price and wage rigidity. Its representation is most often based either on the Calvo model, in which the price reset probability is constant over time, or on the Taylor model, in which durations are staggered but fixed and deterministic (for example one year). However, several recent studies on microeconomic data show that neither of these assumptions is a suitable proxy for the distribution of price and wage durations.

Hervé Le Bihan and Huw Dixon consider generalised Calvo and generalised Taylor wage and price-setting models and show that they accurately reflect the distributions of wage and price durations observed at the microeconomic level. They then use microeconomic French data to develop calibrated versions of these models. By incorporating these elements into a standard DSGE model of the euro area, they are able to assess the consequences for monetary policy transmission.

Their main finding is that the generalised Taylor model predicts a gradual and hump-shaped response of inflation to a monetary policy shock. This specification makes it possible to rationalize an empirical stylized fact of monetary macroeconomics, without resorting to the counterfactual assumption – often used on an ad-hoc basis in DSGE models – of systematic wage and price indexation in each period.

H. Dixon and H. Le Bihan, "Generalised Taylor and generalised Calvo prices and wage setting: Micro-evidence with macro implications",* Economic Journal *(1), May 2012, 122(560), pp. 532-54.

Hervé Le Bihan is Head of the Macroeconomic Analysis and Forecasting Division. His work focuses on price and wage rigidity, macroeconometric modelling, the use of microeconomic data for monetary macroeconomics. He has published a number of articles on macroeconomics and applied econometrics in various journals such as the *American Economic Journal: Macroeconomics*, the *Journal of Econometrics*, the *Journal of Economic Perspectives*, and the *Journal of the European Economic Association*.

Unemployment durations and unobserved characteristics

Econometric analyses show regularities in employer-employee relationships that are not accounted for by their usual determinants. Guillaume Horny highlights the importance of unobserved characteristics.

Employment durations are heterogeneous. There is abundant evidence that, in OECD countries, long-term employment relationships are common, most new jobs end early, and the probability of a job ending declines with tenure. Since job exit involves both the worker and the firm, it is plausible that exit rates are affected by worker and firm characteristics. While the relevance of worker heterogeneity in job durations is well established, the empirical evidence on the importance of firm heterogeneity is much more limited.

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368 “Shock on variable or shock on distribution with application to Stress-Test”, S. Dubecq and C. Gourieroux.

367 “Breakeven inflation rates and their puzzling correlation relationships”, G. Cette and M. De Jong.

366 *“Les effets des hausses du SMIC sur le salaire moyen”*, G. Cette, V. Chouard and G. Verdugo (in French).

365 “Global versus local shocks in micro price dynamics”, P. Andrade and M. Zachariadis.

364 “Global value chains during the great trade collapse: a bullwhip effect?”, C. Altomonte, F. Di Mauro, G. Ottaviano, A. Rungi and V. Vicard.

363 “Reserve requirements for price and financial stability: when are they effective?”, C. Glocker and P. Towbin.

362 “The determinants of intrafirm trade: evidence from French firms”, G. Corcos, D. Irac, G. Mion and T. Verdier.

361 “How do anticipated changes to short-term market rates influence banks’ retail interest rates? Evidence from the four major euro area economies”, A. Banerjee, V. Bystrov and P. Mizen.

360 “The European way out of recessions”, F. Bec, O. Bouabdallah and L. Ferrara.

359 “A Term Structure Model with Level Factor cannot be Realistic and Arbitrage Free”, S. Dubecq and C. Gourieroux.

In a publication co-authored with Rute Mendes and Gerard van den Berg, Guillaume Horny shows that employers and employees’ specific characteristics unobserved by the econometrician have a non-negligible impact on labour market outcomes. These variables can be related to individual preferences for mobility, features making some individuals highly productive, or workforce management strategies. Their influence can be identified in an empirical analysis of job durations, thanks to the follow-up of employers and employees. The results imply that unobserved firm characteristics explain around 30% of the variation in job durations (expressed in logarithms). In addition, they find a positive correlation between unobserved worker and firm characteristics. This is informative about the extent to which specific types of firms match with specific types of workers. It indicates that if job durations are typically short in a firm, this is not only because of high job exit rates at the firm, but also because the firm attracts workers who have high job exit rates.

G. Horny, R. Medes and G. Van den Berg (2012), “Job Durations With Worker- and Firm-Specific Effects: MCMC Estimation With Longitudinal Employer”,* Journal of Business and Economic Statistics*, 30(3), pp. 468-80.

Guillaume Horny is senior economist at the Microeconomic Analysis Division (SAMIC). He holds a Ph.D. in Economics from the University of Strasbourg. His research interests cover mostly microeconometrics, but include also Bayesian econometrics. His research has appeared in the *Journal of Business and Economic Statistics*, *Applied Economics and Statistical Papers*.

Sticky wages: Evidence from quarterly microeconomic data

Nominal wage stickiness is a crucial element of monetary analysis. Microeconomic data suggest that wage changes are much more frequent and complex than one might think.

Nominal wages generally appear to adjust infrequently and with some delay to shocks. This wage rigidity is a central issue in New Keynesian literature, because of its influence on the degree of inflation persistence and the optimal monetary policy rule. While there are numerous microeconomic studies on this issue, these have focused on assessing downward nominal rigidity using annual data.

In a study co-authored with Hervé Le Bihan and Thomas Heckel, Jérémi Montornès completes the scarce empirical work on the subject with French infra-annual data. The findings suggest that wage changes are relatively frequent, at around 38% per quarter. They are mainly synchronized within firms but staggered across them. However, a certain degree of synchronization is induced by minimum wage revisions and seasonal wage changes (more frequent in the first quarter). In addition, estimating a selection model shows that wage adjustments are time-dependent, i.e. revised at regular intervals, rather than state-dependent.

The analysis also shows that wages are indexed to inflation and unemployment, both past and future. There is some evidence of predetermination in wage changes. While wage changes occur on average every two quarters, the decisions underlying these changes are actually much less frequent.

H. Le Bihan, J. Montornès and T. Heckel, “Sticky wages: Evidence from quarterly microeconomic data”, AEJ: Macroeconomics (2A), 2012, 19(7-9).

Jérémi Montornès (Monetary Analysis and Statistics Division) was working at the Microeconomic Analysis Division at the time this study was conducted.

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Securitisation and risk retention: Are the US regulators right?

The tight risk retention requirements proposed by US regulators following the Dodd-Frank Act have drawn fierce opposition from the securitization industry. For Henri Pagès, they have got it (almost) right.

In April 2011, six federal agencies issued new credit risk retention rules to address the conceptual weaknesses of current securitization agreements. The most contentious issue was the funding of a "premium capture" account that would stand first in line over and above the five per cent risk retention prescribed by the Dodd-Frank Act. Given the fierce opposition voiced by the financial industry, it is likely that the agencies will move forward with a modified proposal for rulemaking.

From the vantage point of a world with optimal contracts, Henri Pagès shows in two companion papers that the agencies' view is basically right. The idea is that sponsors should be prevented from realizing value at closing by monetizing the gains on sale and high-risk tranches, as this creates incentives for poor underwriting. The main difference between the model and the regulation is that the "premium capture" account is not a low-return liquidity buffer subordinated to all other interests in the pool, but is instead high-return collateral liable to capture fees during the life of the transaction. One advantage is that it can track ongoing performance: defaults trigger withdrawals in the amount of the risk retained, but servicing and other fees are then applied to the reserve account until the balance is restored to an appropriate level. By this token, performance-based compensation allows investors to effectively correct sponsors' incentives and save on costly resources when sponsors' rates of return are high.

H. Pagès, "Bank monitoring incentives and optimal ABS",* Journal of Financial Intermediation, *forthcoming.
H. Pagès and D. Possamaï, "A mathematical treatment of bank monitoring incentives",* Finance and Stochastics*, forthcoming.

Henri Pagès is Scientific Advisor at the DGEI. He holds a Ph.D. in Economics from MIT. His research interests cover banking theory, continuous finance, and credit risk. He has published in various journals such as *Economic Theory*, *Mathematical Finance* and the *Journal of Financial Intermediation*.

Welfare implications of heterogeneous labor markets in a monetary union

Given heterogeneous labor markets, some reforms are more likely to result in large welfare gains. Jean-Guillaume Sahuc indicates which ones should be carried out in a monetary union.

More than ten years into the creation of the euro area, economic disparities are still pronounced, especially in terms of labor market performances. The issue is not only how the overall performance of the monetary union is affected by a modification of the frictions in the labor market, but also (i) how the country-specific environment is modified and (ii) which structural changes offer the highest payoff in terms of fostering adjustment.

In a recent paper, Céline Poilly and Jean-Guillaume Sahuc propose a normative analysis to investigate which institutional modifications are required in the presence of heterogeneous labor markets to achieve a particular unemployment rate.

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Acknowledgement of discussants

The following discussants contributed insightful remarks and suggestions to DGEI's weekly seminar over the first Semester of 2012. They are thanked wholeheartedly for their support.

David Spector (PSE), Roberto Pancrazi (TSE), Olivei Giovanni (Fed Boston), Chira Criscuolo (OCDE), Jean-Paul Laurent (PSE), Guillaume Plantin (TSE), Stefan Hirth (Aarhus University), Claude Diebolt (University of Strasbourg), Marek Jarocinski (ECB), Dalibor Stevanovic (UQAM), Enrique Sentana (CEMFI), Kumar Mallick (Queen Mary University London), Andrew Meldrum (BoE), Pierre-Olivier Gourinchas (Berkeley), Sandra Poncet (University of Paris 1), Christian Francq (University of Lille 3), Eduardo Morales (Princeton), Klaus Adam (University of Mannheim), Katheline Schubert (PSE)

To do so, they introduce labor market search and matching frictions into a dynamic stochastic general equilibrium model of a two-country monetary union that accounts for the rich structure of propagation mechanisms and international spillover in a monetary union. They find that improvements in the services offered by employment agencies and structural reforms ensuring that jobs are less often destroyed are conducive to significant welfare gains. Moreover, structural changes in the labor market of a country have spillover effects onto the rest of the area. Indeed, the foreign economy may benefit from successful matches without being constrained by its own restrictive labor institutions in the bargaining process, implying faster convergence to the new employment rate. Finally, the authors argue that the higher the degree of price rigidity in a given country, the higher the benefits it gets from a permanent structural change in the labor market, suggesting that matching frictions can offset the negative effect of price rigidities in the economy.

C. Poilly and J.-G. Sahuc, "Welfare implications of heterogeneous labor markets in a currency area",* Macroeconomic Dynamics*, forthcoming.

Jean-Guillaume Sahuc is deputy head of the Monetary Policy Research Division and a lecturer at the Edhec Business School. His research on quantitative macroeconomics and macroeconometrics has been published in journals such as *The Economic Journal*, the *Journal of Money, Credit and Banking*, the *Journal of Macroeconomics*, and the *International Journal of Central Banking*.

The conference "Macroeconomic modeling in times of crisis"

25 and 26 October 2012 in Paris

The conference entitled "Macroeconomic modeling in times of crisis" was held at the Banque de France on 25-26 October 2012. This conference was organized in collaboration with the Federal Reserve Bank of Atlanta, the *Centre d'Analyses Stratégiques* and the *Centre pour la recherche économique et ses applications* (CEPREMAP). The conference was also an opportunity to pay tribute to the contribution of Lawrence Christiano of Northwestern University to DSGE modeling.

During the first day, six papers presented by Marco Del Negro, Antoine Devulder, Günter Coenen, Jesper Lindé, Ulf Söderström and Rafael Wouters used DSGE models to shed light on different aspects of the crisis that began in 2008 and the way in which some of these models have been used to prepare monetary policy decisions. The day ended with a roundtable in which David Altig, Lawrence Christiano, Douglas Laxton and Tao Zha participated.

The second day was devoted to more prospective papers, with contributions from Fabio Canova, Varadarajan Chari, Lawrence Christiano, Frank Portier and Thomas Sargent. A roundtable on the expectations of political leaders with regard to modeling chaired by Marc-Olivier Strauss-Kahn brought together Olivier Blanchard, Claudio Borio, Benoît Coeuré, Daniel Cohen and Athanasios Orphanides.

The conference programme is available at http://www.banque-france.fr/en/economics-statistics/research/seminars-and-symposiums/macroeconomic-modeling-in-times-of-crisis-paris-25-26-october-2012.html

Michel Julliard is coordinator of the DSGE network at the Banque de France and researcher at the CEPREMAP

Research Newsletter

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The Directorate General Economics and International Relations (DGEI) is a DIrectorate General of the Banque de France. Its task is to contribute to the preparation of monetary policy decisions by conducting macroeconomic analyses and research work.

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