Referee Report

for economics-ejournal
on

"Technology Shocks and Employment in Open Economies"

The present paper studies the response of aggregate employment to domestic technology shocks in a sticky-price open-economy model. The open economy dimension is used to generate impulse responses that are consistent with Gali's (1999) provoking evidence stating that employment falls after a technology shock. At the heart of the mechanism lies the expenditure-switching effect of nominal exchange rate changes. A technology shock induced a nominal appreciation, which in turn increases the relative price of domestic goods and shifts global demand to foreign goods leading to contraction of domestic employment. The author finds that under Producer Currency Pricing (PCP), the model indeed generates a fall in employment following a technology shock. Under Local Currency Pricing, however, the model is unable to reproduce this negative response.

The analysis appears to be based on solid theoretical foundations and is carefully conducted. The topis is certainty relevant and adds interesting perspectives to the debate on the effects of technology shocks. Some aspects of the present paper, however, should be extended or need further clarification:

- The model is an open economy model. Hence, the impulse response functions are conditional on this open economy dimension. The author nevertheless contrasts these responses to Gali's (1999) evidence, which is derived from a closed economy reduced form VAR. The author should convincingly explain that his model not only matches the response of employment to technology shocks, but is also able to match other empirical regularities. Matching the model to the data along just one dimension, i.e. the negative response of employment, seems to provide rather weak support.

- There is surely ample evidence on the responses to technology shocks in open economy VARs and in estimated open economy DSGE models. Are these findings consistent with the results of this paper. In particular, do we see a nominal appreciation following a technology shock in the data?

- Several authors, e.g. Larry Christiano and others, have challenged the results of Galí on various methodological grounds. There is also quite some evidence

showing an *in*crease in employment, i.e. the conventional RBC result. In other words, the author should be more cautious in interpreting the evidence.

- The paper does not mention monetary policy. Which role could the policy rule play in this model? The author should touch upon this.

- Minor comments:

  - Referring to Gali's (1999) paper as a "significant paper" (p. 2), is probably unfortunate. It rather is a seminal contribution that stimulated the literature over the last decade.
  - Avoid equations in the introduction.
  - Footnote no. 5 seems to be doubled.
  - Check the reference section and avoid "?.".