Comments on

"FDI, Skill-Specific Unemployment and Institutional Spillover Effects"

The paper builds a model explaining the effects of institutional reforms on trade, capital flows and unemployment. In particular, the model by Feenstra and Hanson (1996, 1997) is extended to include skill specific labor markets with search and matching frictions in the spirit of Mortensen and Pissarides. It is shown how all labor markets are affected by unilateral and skill specific reforms. Furthermore, capital flows across countries are explicitly addressed and their response to unilateral institutional reforms is described within the specific setting of the model.

The aspect of international institutional spillovers appears of major importance to both research and policy circles. The paper's importance lies in contributing to this literature. Furthermore, the additional consideration of capital flows adds a valuable aspect. Yet, the relevance of skill-specific institutions has to be further motivated by the author. In particular, the specific effects arising from such institutional heterogeneity in comparison to models without skill specific groups has to be established more profoundly.

Comments and suggestions

The paper could benefit from a sharpening of the focus. The introduction addresses unemployment, capital flows, and inequality across skill groups. The motivating evidence is the reversal of capital flows in and out of China. Here the evidence could be substantiated and the models contribution in explaining these trends be made more explicit. Inequality across skill groups does not feature at all in the further analysis of the paper.

The introduction states that predictions for inequality will be derived in later sections. This is not the case. In particular, the comparative static exercises and the conclusion do not directly distinguish skill specific effects. Wording is in terms of general labor and the focus seems to be on capital flows. Proposition 7 states that unemployment and wages for both skill groups are affected in the same direction. It should be made clear if there is a skill specific difference in outcomes in terms of wages and unemployment since the contribution of the paper and the motivation for introducing skill heterogeneity crucially hinge on this.

The way skill heterogeneity is introduced in the Feenstra and Hanson framework could be improved in terms of exposition. The author assumes an additional stage of intermediate input production – the skill specific inputs to be used in the production of intermediates x(z). The wording should be streamlined here to avoid confusion. For the final stage of intermediate goods production the words "final intermediate good", "final good", "final output good", and "final consumption good" are used among others.

The relevance of skill specific reforms could be established by using direct examples. Either a country specific reform could be used as an example or some general possibilities could be mentioned. Examples for "quasi" low-skill specific reforms could be minimum wage changes, since these mainly affect workers with low wages around the minimum wage level. For high skilled individuals one could

think of legal changes in management compensation allowing more or less bonuses, for instance. Shocks to skill specific labor supply could be motivated with immigration laws favoring highly skilled individuals (points based systems etc.) In the present form the relevance of skill-specific institutions seems at least questionable.

Given the explicit focus on different labor inputs in terms of skills, the assumptions regarding capital-labor substitution could be discussed. An equal elasticity of substitution for high and low skilled labor may be regarded as questionable.

The wording with regard to changes in institutions is confusing at times. What is an “improvement” in an institution? Given contradictory direct and indirect effects this is unclear. Simply giving the direction of the change in the variable in question seems more straight-forward.

If China and its capital flows are the main motivation, this could be stressed more and the relevance for other developing/emerging market economies could be highlighted.

In order to avoid confusion, the introduction could feature a clear definition of FDI as pure capital flow, given the interchangeable use of offshoring/outsourcing/FDI by parts of the literature.

Finally, some proofreading and correction of grammar and wording seems appropriate.