REM Newsletter 9/2019

November 26, 2019

Editors: António Afonso, Isabel Proença, Joana Pais
https://rem.rc.iseg.ulisboa.pt/
Contacts: Phone: +351 213 925 912. e-mail: rem@iseg.ulisboa.pt

The Latest REM Working Papers

The center of **Research in Economics and Mathematics** (REM) circulates research, notably by its affiliated members, as working papers intended for professional and public discussion and comment. The papers have not been peer reviewed.

Table of contents

Events

REM Young Researcher Award

REM - Research in Economics and Mathematics, launches in 2019 the REM Young Researcher Award, with a monetary value of 1000 EUR. The prize awards the best Master thesis defended at ISEG, in the period October 2018 - December 2019, and whose supervisor is a member of REM in one ISEG Master courses. To apply, the candidates should send their thesis, together with the proof of the public defense and approval, by 31 December 2019, to rem@iseg.ulisboa.pt.

REM Working Papers

Polluting Emissions and GDP: Decoupling Evidence from Brazilian States , João Tovar Jalles, *Working Paper 0104-2019*

We provide a comprehensive analysis of the relationship between greenhouse gas (GHG) emissions and GDP in Brazil using both aggregate and state-level data. The trend or Kuznets elasticity is about 0.8 for Brazil, higher than that in advanced countries but below that of major emerging markets. The elasticity is somewhat higher for consumption-based emissions than for production-based emissions, providing evidence against the "pollution haven" hypothesis. Additional evidence comes from state-level data analysis where one can observe a great deal of heterogeneity but also some hope as far as decoupling is concerned. In addition to the trend relationship between emissions and output, we find that there does not seem to exist a cyclical relationship holding in Brazil at the aggregate level (despite having become more procyclical over time), but it does exist in a few states.

Fiscal Discipline and Exchange Rates: Does Politics Matter? , João Tovar Jalles, Carlos Mulas-Granados, José Tavares, *Working Paper 0103-2019*

We look at the effect of exchange rate regimes on fiscal discipline, taking into account the effect of underlying political conditions. We present a model where strong politics (defined as policymakers facing longer political horizon and higher cohesion) are associated with better fiscal performance, but fixed exchange rates may revert this result and lead to less fiscal discipline. We confirm these hypotheses through regression analysis performed on a panel sample covering 79 countries from 1975 to 2012. Our empirical results also show that the positive effect of strong politics on fiscal discipline is not enough to counter the negative impact of being at/moving to fixed exchange rates. Our results are robust to a number of important sensitivity checks, including different estimators, alternative proxies for fiscal discipline, and sub-sample analysis.

Monetary Aggregates and Macroeconomic Performance: the Portuguese Escudo, 1911-1999, João Tovar Jalles, *Working Paper 0102-2019*

This paper takes a long time span approach to provide a full characterization of several monetary aggregates over Portuguese's historical economic business cycles. By focusing on the 1911-1999 period (the life span of the currency Escudo), the paper also revisits the issue of the role of money on real macroeconomic outcomes. We get inspiration from the monetarists versus Keynesians debate about direction of causality in the output-money relation and the quest for validity of money (non-)neutrality. By means of descriptive statistics we first uncover that money changes were associated with changes in real economic activity. Most monetary aggregates are more volatile than GDP, display high serial autocorrelation, are generally countercyclical and lead the economic cycle (except checking accounts). Then, through formal time series techniques, our results show that our monetary series were characterized by unit roots and were cointegrated with real GDP (after accounting for endogenously estimated breaks). Evidence suggested that money supply Granger-caused real GDP supporting the money non-neutrality hypothesis in the case of Portugal.

Wagner and the Fading Voracity Effect: Short vs. Long-Run Effects in Developing Countries, João Tovar Jalles, *Working Paper 0101-2019*

This paper empirically revisits the validity of Wagner's proposition in a panel of 149 developing countries between 1980-2015 by focusing on different components of government expenditure. We rely on an ARDL approach which allow us to uncover short and long-run cyclicality coefficients. Our results do not overwhelmingly support the existence of higher than unity long-run elasticities of government spending components vis-a-vis economic growth, suggesting that the Wagner's regularity is more the exception than the norm. Moreover, the case for voracity is fading away as developing countries catch-up the development ladder and graduate from procyclicality. In fact, most short-run elasticities are countercyclical. Finally, some macroeconomic and institutional and political characteristics affect the degree of government spending cyclicality.

Explaining Africa's Public Consumption Procyclicality: Revisiting Old Evidence,João Tovar Jalles, *Working Paper 0100-2019*

This paper compiles a novel dataset of time-varying measures of government consumption cyclicality for a panel of 46 African economies between 1960 and 2014. Government consumption has, generally, been highly procyclical over time in this group of countries. However, sample averages hide serious heterogeneity across countries with the majority of them showing procyclical behavior despite some positive signs of graduation from the "procyclicality trap" in a few cases. By means of weighted least squares regressions, we find that more developed African economies tend to have a smaller degree of government consumption procyclicality. Countries with higher social fragmentation and those are more reliant on foreign aid inflows tend to have a more procyclical government consumption policy. Better governance promotes counter-cyclical fiscal policy whileincreased democracy dampens it. Finally, some fiscal rules are important in curbing the procyclical behavior of government consumption.

Long-run relationship between exports and imports: current account sustainability tests for the EU, António Afonso, Florence Huart, João Tovar Jalles and Piotr Stanek, *Working Paper 099-2019*

We assess the sustainability of external imbalances for EU countries using panel stationarity tests of Current Account(CA) balance-to-GDP ratios and panel cointegration of exports and imports of goods and services, for the period 1970Q1-2015Q4.We find that: i) the country panel is non-stationary; ii) cross-sectional dependence plays an important role; iii) there is non-stationarity of the CA, imports, and exports with cross-sectional panel dependence and multiple structural breaks; iv) however, there is a stable long-run relationship between exports and imports in the panel. Hence, trade imbalances can be less unsustainable but this is not sufficient to make current account imbalances sustainable.

Improving Schools through School Choice: An Experimental Study of Deferred Acceptance , Flip Klijn, Joana Pais, Marc Vorsatz, *Working Paper 098-2019*

In the context of school choice, we experimentally study the student-optimal stable mechanism where subjects take the role of students and schools are passive. Specifically, we study if a school can be better off when it unambiguously improves in the students' true preferences and its (theoretic) student-optimal stable match remains the same or gets worse. Using first-order stochastic dominance to evaluate the schools' distributions over their actual matches, we find that schools' welfare almost always changes in the same direction as the change of the student-optimal stable matching, i.e., incentives to improve school quality are nearly idle.