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Abstracts

Political Contributions and Public Procurement: Evidence from Lithuania

Audinga Baltrunaite, Bank of Italy

This paper studies whether firms trade political contributions for public procurement contracts. Combining data on Lithuanian government tenders, corporate donors, and firm characteristics, I examine how a ban on corporate contributions affects the awarding of procurement contracts to companies that donated in the past. Consistent with political favoritism, donors' probability of winning falls by five percentage points as compared to that of nondonor firms after the ban. Evidence on bidding and victory margins suggests that corporate donors may receive auction-relevant information affecting procurement outcomes in their favor. (JEL: D72, H57)

Can Agents With Causal Misperceptions Be Systematically Fooled?

Ran Spiegler, Tel Aviv University, University College London and CFM

An agent forms estimates (or forecasts) of individual variables conditional on some observed signal. His estimates are based on fitting a subjective causal model—formalized as a directed acyclic graph, following the "Bayesian networks" literature—to objective long-run data. I show that the agent's average estimates coincide with the variables' true expected value (for any underlying objective distribution) if and only if the agent's graph is perfect—that is, it directly links every pair of variables that it perceives as causes of some third variable. This result identifies neglect of direct correlation between perceived causes as the kind of causal misperception that can generate systematic prediction errors. I demonstrate the relevance of this result for economic applications: speculative trade, manipulation of a firm's reputation, and a stylized "monetary policy" example in which the inflation-output relation obeys an expectational Phillips Curve. (JEL: D01, D84, E59)

Good Booms, Bad Booms

Gary Gorton, Yale University; Guillermo Ordoñez, University of Pennsylvania

Credit booms are not rare; some end in a crisis (bad booms) while others do not (good booms). We document that credit booms start with an increase in productivity growth, which subsequently falls faster during bad booms. We develop a model in which a crisis happens when a credit boom transits towards an information regime with careful examination of collateral. As this examination is more valuable when collateral backs projects with low productivity, crises are more likely during booms that display larger productivity declines. We test the main predictions of the model and identify the default probability as the main component of measured productivity that lies behind crises. (JEL: E32, G21, D83)

Competition for Status Creates Superstars: An Experiment on Public Good Provision and Network Formation

Boris van Leeuwen, CentER, Tilburg University; Theo Offerman, CREED, University of Amsterdam; Arthur Schram, CREED, University of Amsterdam and European University Institute

We investigate a mechanism that facilitates the provision of public goods in a network formation game. We show how competition for status encourages a core player to realize efficiency gains for the entire group. In a laboratory experiment we systematically examine the effects of group size and exogenously monetarized status rents. The experimental results provide very clear support for the concept of challenge-freeness, a refinement that predicts when a repeated game equilibrium will be played, and if so which one. Two control treatments allow us to reject the possibility that these observations are driven by social preferences, independently of the competition for status. (JEL: C91, D85, H41)

Discriminating Between Models of Ambiguity Attitude: A Qualitative Test

Robin Cubitt, University of Nottingham; Gijs van de Kuilen, Tilburg University; Sujoy Mukerji, Queen Mary University of London

During recent decades, many new models have emerged in pure and applied economic theory according to which agents' choices may be sensitive to ambiguity in the uncertainty that faces them. The exchange between Epstein (2010) and Klibanoff et al. (2012) identified a notable behavioral issue that distinguishes sharply between two classes of models of ambiguity sensitivity that are importantly different. The two classes are exemplified by the α-maxmin expected utility (MEU) model and the smooth ambiguity model, respectively; and the issue is whether or not a desire to hedge independently resolving ambiguities contributes to an ambiguity-averse agent's preference for a randomized act. Building on this insight, we implement an experiment whose design provides a qualitative test that discriminates between the two classes of models. Among subjects identified as ambiguity sensitive, we find greater support for the class exemplified by the smooth ambiguity model; the relative support is stronger among subjects identified as ambiguity averse. This finding has implications for applications that rely on specific models of ambiguity preference. (JEL: C91, D01, D03, D81, G02)

The Political Economy Of Program Enforcement: Evidence From Brazil

Fernanda Brollo, University of Warwick and CAGE; Katja Kaufmann, Mannheim University and BRIQ; Eliana La Ferrara, Bocconi University and LEAP

Do politicians manipulate the enforcement of conditional welfare programs to influence electoral outcomes? We study the Bolsa Familia Program (BFP) in Brazil, which provides a monthly stipend to poor families conditional on school attendance. Repeated failure to comply with this requirement results in increasing penalties. First, we exploit random variation in the timing when beneficiaries learn about penalties for noncompliance around the 2008 municipal elections. We find that the vote share of candidates aligned with the president is lower in zip codes where more beneficiaries received penalties shortly before (as opposed to shortly after) the elections. Second, we show that politicians strategically manipulate enforcement. Using a regression discontinuity design, we find weaker enforcement before elections in municipalities where mayors from the presidential coalition can run for reelection. We provide evidence that manipulation occurs through misreporting school attendance, particularly in

municipalities with a higher fraction of students in schools with politically connected principals. (JEL: D72, H53, I38)

Small Price Responses To Large Demand Shocks

Etienne Gagnon, Board of Governors of the Federal Reserve System; David López-Salido, Board of Governors of the Federal Reserve System

We study the pricing response of U.S. supermarkets to large demand shocks triggered by labor conflicts, mass population displacement, and shopping sprees around major snowstorms and hurricanes. We find that these large swings in demand have, at best, modest effects on the level of retail prices, consistent with flat short- to medium-term supply curves. This finding holds even when shocks are highly persistent and despite the fact that stores adjust prices frequently. We also provide evidence that retailers maintain frequent promotional sales even as their demand varies and that they seek to match movements in their local competitors' recourse to promotional sales. (JEL: E30, L11)

Human Capital Formation During The First Industrial Revolution: Evidence From The Use Of Steam Engines

Alexandra de Pleijt University of Oxford, Utrecht University, and Queen's University Belfast; Alessandro Nuvolari, Sant'Anna School of Advanced Studies; Jacob Weisdorf, University of Southern Denmark

We examine the effect of technical change on human capital formation during England's Industrial Revolution. Using the number of steam engines installed by 1800 as a synthetic indicator of technological change and occupational statistics to measure working skills (using HISCLASS), we establish a positive correlation between the use of steam engines and the share of skilled workers at the county level. We use exogenous variation in carboniferous rock strata (containing coal to fuel the engines) to show that the effect was causal. While technological change stimulated the formation of working skills, it had an overall negative effect on the formation of primary education, captured by literacy and school enrolment rates. It also led to higher gender inequality in literacy. (JEL: J82, N33, O14, O33)

Nonlinear Household Earnings Dynamics, Self-Insurance, And Welfare

Mariacristina De Nardi Federal Reserve Bank of Minneapolis, and University College London; Giulio Fella Queen Mary University of London, CFM, and IFS; Gonzalo Paz-Pardo, University College London

Earnings dynamics are much richer than typically assumed in macro models with heterogeneous agents. This holds for individual-pre-tax and household-post-tax earnings and across administrative and survey data. We estimate two alternative processes for household after-tax earnings and study their implications using a standard life-cycle model. Both processes feature a persistent and a transitory component, but although the first one is the canonical linear process with stationary shocks, the second one has substantially richer earnings dynamics, allowing for age-dependence of moments, non-normality, and nonlinearity in previous earnings and age. Allowing for richer earnings dynamics implies a substantially better fit of the evolution of cross-sectional consumption inequality over the life cycle and of the individual-level degree of consumption insurance against persistent earnings shocks. The richer earnings process implies lower welfare costs of earnings risk. (JEL: D14, D31, E21, J31)

Short-Term Migration, Rural Public Works, And Urban Labor Markets: Evidence From India

Clément Imbert, University of Warwick; John Papp, R.I.C.E.

This paper studies the effect of India's rural public works program on rural-to-urban migration and urban labor markets. We find that seasonal migration from rural districts that implemented the program decreased relative to those that were selected to, but did not implement it. We use a gravity model and find that real wages rose faster in cities with higher predicted migration from program districts. Since most seasonal migrants work outside of their district, urban wage increases were not limited to program districts, and may have attracted migrants from nonprogram districts. Difference-in-differences may hence be biased. Structural estimates indeed suggest that migration decreased by 22% in program districts, but also increased by 5% in nonprogram districts. As a result, urban wages increased by only 0.5%, against 4.1% if the program had been implemented in all selected districts. (JEL: O15, J61, R23, H53)

Pay To Quit And Team Incentives

Pak Hung Au, The Hong Kong University of Science and Technology

This paper examines the optimal compensation scheme, job design, and severance policy for a team using a model of repeated moral hazard. In the optimal contract, the agent may be paid to quit after a poor performance. We show that a generous severance policy facilitates the adoption of team incentives and team-based production by making it cost-effective to implement peer monitoring and sanction among the agents. (JEL: D86, J65)

Individual Preference For Longshots

Robin Chark, University of Macau; Soo Hong Chew, Southwestern University of Finance and Economics and National University of Singapore; Songfa Zhong, National University of Singapore

Results from studies on risk taking behavior suggest that people tend to be risk seeking when making choices over lotteries that involve longshots: small probabilities of winning sizable payoffs. To investigate preferences over longshots systematically, we conduct an incentivized experiment using state lotteries in China, each involving a single prize and fixed winning odds. This enables our construction of single-prize lotteries involving winning odds between 10-5 and 10-1 and winning prizes ranging from RMB10 (about USD1.60) to RMB10,000,000 (about USD1.60 million) across different expected payoffs. For lotteries with expected payoffs of 1 and 10, subjects exhibit heterogeneous preferences for longshots: some prefer the smallest winning probability whereas others favor intermediate winning probabilities. As the expected payoff increases to 100, subjects become predominantly risk averse, even for the lowest winning probability of 10-5. Our findings pose challenges for utility models of decision making under risk. (JEL: C91, D81)

Prices, Policing And Policy: The Dynamics Of Crime Booms And Busts

Tom Kirchmaier, Copenhagen Business School and CEP, London School of Economics; Stephen Machin, Department of Economics and CEP, London School of Economics; Matteo Sandi, CEP, London School of Economics; Robert Witt, University of Surrey and CEP, London School of Economics

In many historical episodes, criminal activity displays booms and busts. One clear example is the case of metal crime in the United Kingdom (and elsewhere) where, in the face of big increases in value driven by world commodity prices, thefts rose very sharply in the 2000s, after which they fell. This paper studies the respective roles of prices, policing and policy in shaping this crime boom and bust. Separate study of each reveals metal crime being driven up via sizeable and significant metal crime–price elasticities and driven down by changes in policing and policy. A regression-based decomposition analysis confirms that all three of the hypothesised factors considered in the paper - prices, policing and policy - were empirically important in the different stages of metal theft's boom and bust. (JEL: K42)

Sustaining Cooperation: Community Enforcement Versus Specialized Enforcement

Daron Acemoglu, MIT; Alexander Wolitzky, MIT

We introduce the possibility of coercive punishment by specialized enforcers into a model of community enforcement. We assume that, just as regular agents need to be given incentives to cooperate with each other, specialized enforcers need to be given incentives to carry out costly punishments. We fully characterize optimal equilibria in the model. When the specialized enforcement technology is sufficiently effective, cooperation is best sustained by a "one-time enforcer punishment equilibrium", where any deviation by a regular agent is punished only once, and only by enforcers. In contrast, enforcers themselves are disciplined (at least in part) by community enforcement. The reason why there is no community enforcement following deviations by regular agents is that such a response, by reducing future cooperation, would decrease the amount of punishment that enforcers are willing to impose on deviators. Conversely, when the specialized enforcement technology is less effective, optimal equilibria involve a mix of specialized enforcement and community enforcement (which might take the form of "ostracism"). Our results hold both under perfect monitoring of actions and under various types of private monitoring. (JEL: C73, D72, D74)