Discussion of “US-China Tension” by John Rogers, Bo Sun and Tony Sun

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Brief Summary

- general motivation: concerning the negative impacts of the escalated US-China tension, both politically and economically
- A very interesting and well-executed empirical paper that

1. provides a text-based and time-varying measure of the degree of US-China tension (UCT)
2. identifies the real impacts of UCT on firm-level outcomes and the economic aggregates
3. explores the transmission mechanism and the robustness of results

- key mechanism: UCT brings forth negative impacts mainly through the *uncertainty channels*
  - wait-and-see effect/real-option effect (Abel and Aberly, 1996; Bloom, 2009)
  - larger impacts if a firm is more exposed to the “rising uncertainty driven by UCT”

Sketch of the Implementations

- measurement
  - share of newspaper articles of 7 U.S. major sources discussing "US-China Tension" if (1) U $\{U.S., Washington\}$; (2) C $\{China, Chinese, Beijing\}$; (3) T $\{phrasesreflectingtensionsof \text{``}contentiousissues\text{''}\}$
- for the robustness of results and good interpretability of the measured index
  - earnings-call text-based firm-level measure of UCT
  - firm exposure to UCT: stock-level beta on UCT
  - firm exposure to China: (1) trade intensity with China; (2) U.S. firms stock returns loading on China's A-share market returns
- Firm-level Q-investment regressions; VAR; decomposition of materialized vs. uncertainty

Roadmap of Comments

- Structural interpretation of measured UCT
- A Test for the Trade Decoupling
- Fitting into the literature: “China Shocks”
- Persistent vs. Transitory Shocks concerning 1st and 2nd moment shock correlations
- Investment Drops vs. Investment Pull from China
- Additional Details

Comment 1. Structural Interpretation of UCT

- Current definition of UCT
  - "the realization and uncertainty about escalation of bilateral barriers that disrupt the normal course of economic transactions between the two countries."
- some economic terms well defined
  - [example 1] (policy) uncertainty: mean-preserving second moment of fundamentals/policy
  - [example 2] precautionary motive: marginal propensity of actions in response to second moment variations
  - [example 3] Knightian Uncertainty (imperfect knowledge about the odds and the outcomes) vs. Risk (random outcome with known probability of distribution)
- it's always good to measure something that is well *motivated or defined* at least based on some very simple theory
  - meanings of "defining": definite and distinct with exact limits (Cambridge Dictionary Online)
  - so far, the measured content can improve to be more "definitive and distinctive"

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5. sentiment/perceived of one or all of these?
   - purely amplified newspaper/media anxiety and sentiments orthogonal to all aforementioned above?

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- Currently more about (4) and (5)
- identification issue
- some simple two-country model perhaps helps to clarify

Comment 2. A Test for the Trade Decoupling

- go back to the desired definition "barriers that disrupt the normal course of economic transactions between the two countries."

- to test what this UCI is really measuring

  - a simple gravity model in international trades running regressions at the aggregate level

$$\ln(\text{net exports}_t^{CN,US}) = c + \alpha \ln(Y_{CN,t}) + \beta \ln(Y_{US,t}) + \gamma UCI_t + \epsilon_t$$

- to best correspond to the definition, this is the test if this is a measure of trade frictions

Comment 3. Fitting into the Literature

- "China" Shocks Literature: earlier work like Autor et al. (2013, AER) highlights significant negative impacts of "Chinese imports competition/penetration" on U.S. job loss, unemployment, firm closure etc.

  - is there any benefit from the U.S. perspective from decoupling with China?

- need to differentiate the gain from decoupling from the first moment negative shocks vs. adverse effects of uncertainty shocks

  - short-run investment drops vs. long-run industrial recovery?

- perhaps to improve the paper scope and highlight the relative contribution to the literature involving China shocks

Comment 4. Forecastable vs. Unexpected Shocks

- escalated US-China tensions may be forecastable with a trend component, which results in the high persistence of UCI
  - if it's an uncertainty story, try obtaining the unexpected/dramatic innovations to the UCI
- this is for causal interpretations of the regression results on firms' investments
  - if it's an uncertainty story, there could be negative correlations with aggregate TFP/demand shocks (Bloom et al., 2018 ECMA)
- controlling for Chinese net imports/exports in the regressions
- two country model implications: controlling for GDP growth, CPI growth and the exchange rate

Comment 5. Investment Drops vs. Investment Pull from China

- if it's about the shock exposure to UCI uncertainty specific to China, can U.S. firms re-optimize the business operations across countries?
  - to see drops in the RHS variable: FDI to China/Firm-to-Firm links, M & A in China/trade linkages with Chinese firms etc.
  - firms can re-establish business in other countries or outsource from other countries
  - any room for hedging against the risk of running into UCI, this is espectially true if UCI is persistent and forecastable?
- if real measures are informative, e.g. firm's linkage to China (trade), stock beta, try highlighting the value added from doing textual analysis?

Additional Details

- Figure 3. what explains the divergence of two different measures over 2018Q1 to 2020Q1?
- contrast and compare, replace UCI with EPU in VAR
- alternative to isolate the materialized risks: past tense
- any statistical test on the power differences of which channels dominates, the realized vs. risk component of UCT?
- what do we read from China's reading of UCI different from others of advanced economies, perhaps, *directional* UCI also matters?
- Table 13 in the appendix. interesting to see R&D positively correlated with EPU but negatively correlated with UCI

Excellent Paper and Best of Wishes!