

## **Research Statement**

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The globalized economy is not, and will not be for a long time, simply a larger world-wide closed economy. In my view, there are three important distinctions: first, in the globalized economy there is an unprecedented level of heterogeneity in terms of financial development. This dimension of heterogeneity, which is typically considered irrelevant in the closed economy literature, plays an important role in shaping financially induced risk. Second, in the absence of a centralized government and in the presence of incomplete cross country risk sharing arrangements, the distributional implications of financial globalization gain a newfound importance. We can no longer focus on equity and assume that the government, or other market arrangements, will simply handle the redistribution of surplus. Third, there is greater importance for understanding institutions that facilitate international coordination, both in terms of production and in terms of finance and policy.

An important part of my work focuses on the implications of financial heterogeneity. In my job market paper, “Financial Distortions and the Distribution of Global Volatility”, I argue that many key features of the distribution of macroeconomic volatility in recent years can be explained in terms of financial globalization. It has long been understood that global shocks to liquidity supply are important driving forces of fluctuations in emerging markets. This paper argues that in the globalized economy, the same global forces that shape volatility patterns in emerging economies can also account for volatility patterns in the developed world. In particular, I show that both the “Great Moderation” trend and the amplification of the subprime crisis are potential consequences of financial globalization. The type of financial heterogeneity driving the results is heterogeneity in the efficiency of the allocation of funds. Financial integration shifts the margin of adjustment to fluctuations in liquidity supply from developed to emerging economies. The moderation in output volatility in the developed world is simply the equilibrium counterpart of the increased vulnerability of emerging markets to shocks to external funding. However, endogenous structural changes in the financial system in the developed world induced by globalization will amplify large contractions in liquidity supply.

In joint work in progress with Nir Avni from the Harvard Math department, we develop a model in which the endogenous structural change in the financial system takes the form of an increase in the complexity of securitized assets. Our starting point is that financial heterogeneity creates a large demand for safe savings originating from emerging market economies. In our model, this demand forces the financial system to gravitate towards an unstable equilibrium in which the level of complexity is close to a critical threshold. The equilibrium can be sustained only in the presence of dispersed private information regarding the aggregate state of complexity. Relatively small sectoral shocks force the financial system to reevaluate securitized products, thereby revealing the aggregate state of complexity and potentially leading to a large crisis.

Another part of my work touches upon the distributional implications of financial integration and its efficiency properties. In my paper “The Inefficiency of Financial Intermediation in General Equilibrium”, I demonstrate that financial intermediation may decrease equilibrium welfare, both because it absorbs productive resources and because it increases the economy’s vulnerability to financial crises. I consider a closed economy in which the supply of inputs is inelastic and financial intermediation is costly. In this model, financial intermediation bids up the price of inputs but does not improve the efficiency of allocation. As the price of inputs increases, the economy becomes increasingly reliant on financial intermediation, and thus increasingly vulnerable to financial crises. Though the paper is written as a closed economy model, the results are insightful for thinking about the distributional implications of *global* financial intermediation. Emerging markets are liquidity constrained entities, in which, as a first approximation, the supply of labor and capital is inelastic. In this model, intermediated funds from developed economies will not improve efficiency, but only extract some of the surplus. Moreover, emerging economies will become increasingly reliant on external funding and susceptible to international liquidity supply shocks.

Finally, some of my work explores ways in which economic institutions should facilitate global coordination in production. As a first step towards this broader research agenda, I focus on two economic institutions that have traditionally facilitated *local* coordination: the city and the week. My view is that both these institutions will (and should) see changes induced by economic globalization. In addition, I believe that understanding the nature of the benefits of coordination through the study of these institutions will help shed light on the broader question of the benefits from globalization. In joint work with Matt Notowidigdo at Chicago Booth, we are trying to construct a statistical benchmark for the economic interpretation of the correlation between city size and wages. The high correlation between

city size and wages suggests that coordinated economic activity – traditionally, a coordinated location – facilitates production efficiency. However, we argue that the literature so far has used an incorrect benchmark, ignoring the following statistical principle: if the distribution of income is skewed, there is a mechanical correlation between city size and income. In estimating the correct benchmark, we hope to make progress towards understanding the magnitude of city wide agglomeration economies.

In a long term research project, I am working towards developing an economic understanding of the week and its changing role in light of need for wider coordination on the one hand, and better communication and travel technologies on the other hand. The long-standing institution of the week reflects the same economic forces as those that shape the city: in order to produce and, in some degree, in order to consume leisure, it is good for people to be at the same place at the same time. While the spatial aspect of this issue has received a lot of attention from the Urban Economics literature, surprisingly, the aspect of time coordination has remained largely unexplored. The standard models of intertemporal labor supply deliver nothing that resembles a labor-leisure cycle; the supply of labor is typically smoothed over time, and changes only following macroeconomic shocks. I augment the standard model by adding switching costs between labor and leisure. This idea resonates with one of the most famous microfoundations of the week: the story of Creation in Genesis is told in terms of separation (separated light from darkness, water from water, etc.), suggesting that there is some surplus generated from social separation of labor time and leisure time. I study the development of the week over time, and try to better understand the nature of this separation and how it depends on work coordination, leisure coordination, and the switching costs between labor and leisure.

To summarize, my work focuses both on the financial aspects and on the production aspects of globalization. I hope to continue working on these fascinating issues and believe that my training and previous research has prepared me for doing so.