“Trade Policy Uncertainty and Stock Returns”

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Disclaimer: It does not necessarily represent IMF’s view.
Summary of the paper

- It examines whether the exposure to trade uncertainty affects stock returns, with the exposure proxied by the NTR gap (as in Pierce and Schott (2016)).

- Main finding: From 1990 to 2001, stock returns are higher for sectors more exposed to trade uncertainty, reflecting a risk premium.
Overall

- Interesting paper, with implications for the current global trade tension.
- A nice linkage of trade literature with the finance literature.
- The paper also performs many robustness checks both to document the positive stock returns and to establish the channel of risk premium.
Comment 1. Factors beyond risk premium?

- The risk premium channel was proposed as the explanation. (For example, Table 8 looks into the effects on stock return volatility).

- Could the annual NTR votes protect the US sectors with higher Non-NTR rates, and thus generate higher returns for them? So rather than a risk premium channel but a competition channel?
Competition channel

- The competition channel is consistent with Table 9: when PNTR was granted to China on Oct-10 2000, stock returns of industries with high NTR gap were negative.

- Table 13 adds a triple interaction term: NTR gap*China exposure dummy*PrePNTR.
  
a. China exposure dummy (imports from China) is measured from 2000 to 2007. Why not using the imports from China over the sample period from 1990 to 2000?

b. What about using the actual trade, instrumented by China’s exports to other countries?
Comment 2: linking stock responses more directly to types of trade exposure?

- In Table 14 (IO Linkages and Stock Returns), trade exposure (for year 1995 only) is included as a control variable. Why not interact with the NTR gap?

- Can the model separate imports/exports exposure? What about the exports from the US to China? Do sectors with high NTR gaps also face higher tariffs in China?
Comment 3: Linking tariff more directly to stock performance?

- The model assumes that the effects of NTR gaps are proportional to stock returns across sectors.
- But do sectors have the same price elasticities and responses to tariff movements? (e.g., the literature on price elasticities, such as Broda and Weinstein 2006).
- Also, is trade equally important across industries? How about normalizing the trade by sector-level production/sales?
Comment 4: Does the impact of uncertainty vary across years?

- Could the paper examine the risk premium by year? A time-series plot?
- Table 10 reports the event-studies for the eleven votes from 1990 to 2000. Could the paper explore more why the signs are mixed across the years?
Comment 5. Economic magnitude?

- Could the paper explore more whether the economic impact is large or small?
- “increases stock returns by 4.3% per year during the uncertainty period.” Based on Table 2, the effect is around: $1\% \times (0.42 - 0.18) = 0.24\%$?