Discussion of "A Theory of Economic Coercion and Fragmentation" by Clayton, Maggiori and Schreger

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Goal of the Paper

Develop a general framework to study

- how a hegemon can use its economic power over foreign countries
- how foreign countries can try to insulate themselves

Specific application to financial sanctions

Plan for my Discussion

The paper has a rich set of results. Cannot make justice in a short discussion.

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- Rent extractor from foreign countries through coercion
- Enforcer of contracts, helps expand production possibilities

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Outline

- Simple illustration of coercion in an Edgeworth box
- Comments

An Edgeworth Box

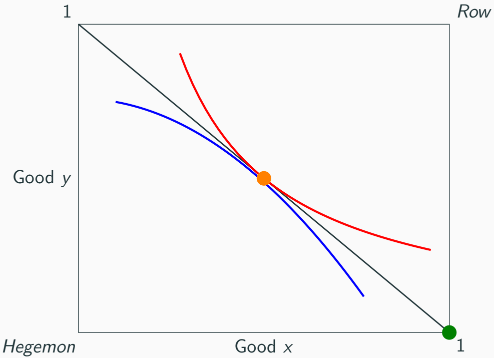
- Static, two-good, two-country with rep. agent in each country

$$U(x, y) = x^{1/2} + y^{1/2}$$

- Endowments (Hegemon and Row)
  $\omega = (1, 0)$, $\omega^* = (0, 1)$

- Resource constraint

$$x + x^\star = 1$$
$$y + y^\star = 1$$



Hegemon as a rent extractor

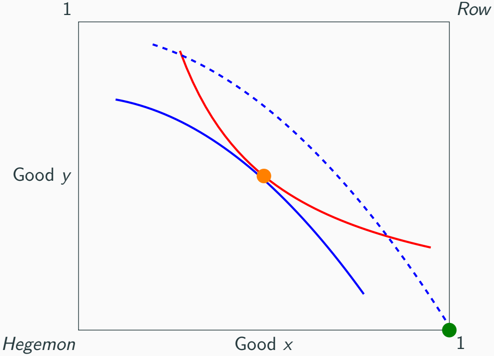
- Suppose the Hegemon can credibly threaten Row with autarky

- Hegemon can then achieve

$$\max_{x^*, y^*} U(1 - x^*, 1 - y^*)$$

subject to

$$U(x^*, y^*) \geq U(0, 1)$$



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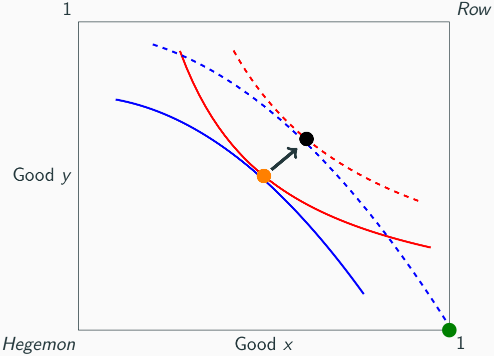

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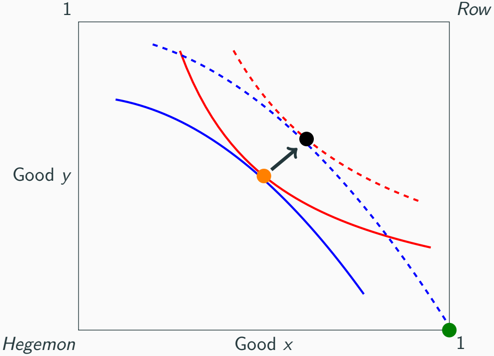
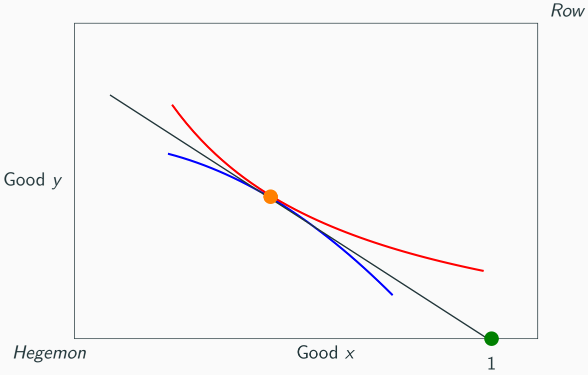


No room for tariffs or other distortionary taxes, absent externalities

Anti-coercion $\Leftarrow$ Relative increase in x resources

- Suppose Row can reallocate resources at a cost
- Assume fixed labor supply and production linear in labor (lower productivity in x)
- Best anti-coercion policy
  - Anticipating autarchy

$$\max_h U(zh, 1-h) \quad \text{with } z < 1$$



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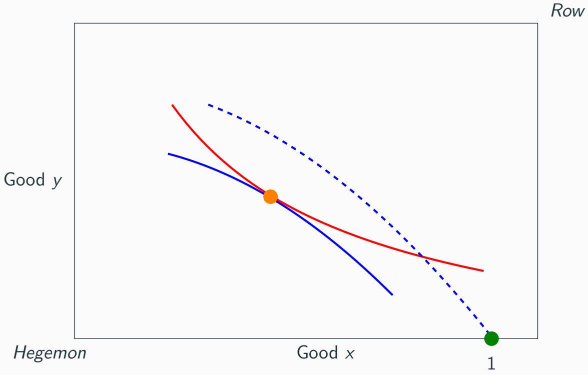

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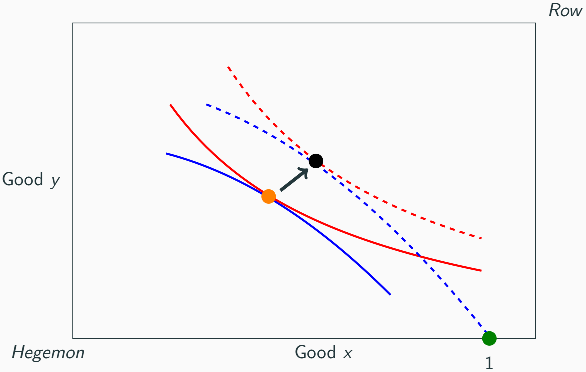

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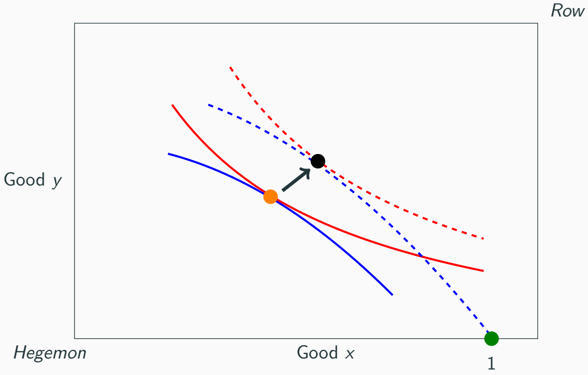

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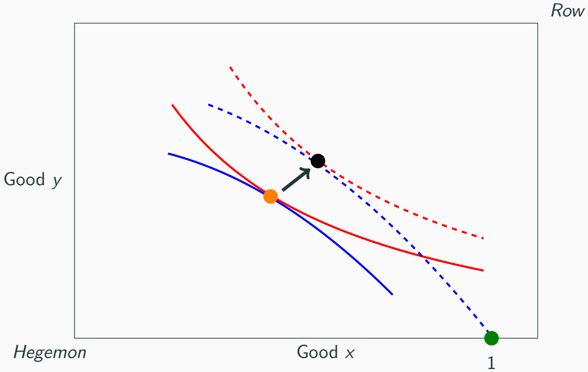

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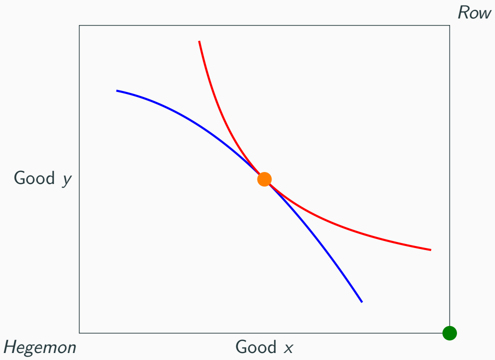
- Dynamic: reserve accumulation as anti-coercion (Bianchi-Sosa Padilla 2023)
- Connection: Schelling (1980)

Hegemon as an enforcer

- Suppose Hegemon can ↑ productivity by improving contract enforcement
  - e.g., by coordinating punishments to defaulting firms CMS (2023)



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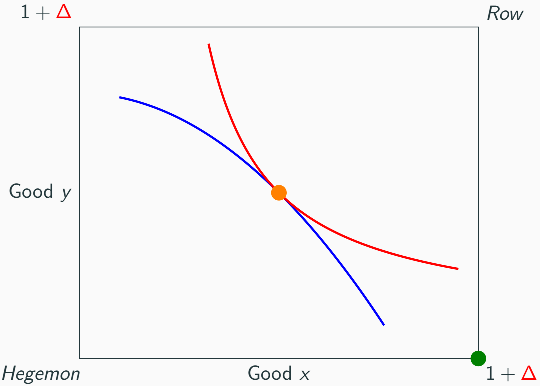

Taking Stock

- Dual role of the Hegemon
  - Rent extractor from foreign countries
  - Enforcer of contracts, helps expand production possibilities

Hegemon does not necessarily reduce world welfare $\Rightarrow$ Tradeoffs between uni-polar vs multi-polar world

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1. In the model, Hegemon coerces directly foreign firms

- In practice, the US negotiates with governments of foreign countries. and then the government enforces agreements domestically.
    - Likely the hegemon has more bargaining power with individual firms
- How does this matter for the results?

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1. In the model, Hegemon coerces directly foreign firms
   - In practice, the US negotiates with governments of foreign countries. and then the government enforces agreements domestically.
     - Likely the hegemon has more bargaining power with individual firms
   - How does this matter for the results?
2. Relatedly, hegemon can tax foreign firms and collect the revenue
   - In practice, taxation power applies to domestic government.
   - Can optimal allocations be decentralized without taxes?

Comments (ctd)

3. In the model, Hegemon is committed to carrying out the sanctions

- In practice, countries struggle to credibly promise to carry sanctions
    - And try not to promise sanctions they will not fulfill
- How would lack of commitment alter main insights?

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4. Hegemon's threat is carried out after foreign countries set anti-coercion

- Seems more realistic to assume Hegemon has first-mover advantage
- How do alternative timings affect results?

Conclusions

- Exciting paper in a growing agenda developing models w/ geo-economic tradeoffs
  - Becko; Bianchi and Sosa Padilla; Broner, Martin, Meyer and Trebesch; Clayton, Maggiori and Schreger; Kooi,...
- I look forward to reading more of the authors' work and seeing how the literature evolves

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