

ECA Research Notes

OFFICE OF THE CHIEF ECONOMIST

EUROPE AND CENTRAL ASIA

ECA Academy Winning Research

January 2020



Hi Everyone,

Happy New Year! I hope you had a restful holiday season with family and friends. We are back and excited about all that we have in store in the new year.

Last week, we decided to start the year with an event that featured some of the most interesting Bank research relevant for our region. These were the winning papers of a competition - ECA Academy - where we sought submissions from across the World Bank Group.

The idea is to find out about the exciting new research that is going on, as well as recognize and incentivize more of it. And I was not disappointed! We got many interesting papers which made our job of selecting the top three a lot of fun but also quite difficult. It took us two rounds, but we ended up with papers that generate important insights for big policy questions that we face in the region. Whether analyzing the impact of a minimum wage hike in Turkey or evaluating the impact of the Belt and Road initiative for the countries involved, or documenting and exploring implications of city decline in the region, - these are all papers that address significant policy issues and make us think.

You can read more about the winning papers below. But there were many more interesting submissions than we could award, some of which I am also including to this newsletter. Thanks again for submitting your papers. And we intend to make this an annual event, so keep up the good work.

Happy Reading!
Asli

[Event recording](#)



From left to right: Michele Ruta, Alen Mulabdic, Francois de Soyres, Laurent Bossavie, Michael Lokshin, Paula Restrepo, Mattia Macovec, and Luis Quintero

WINNING RESEARCH



[Do Firms Exit the Formal Economy after a Minimum Wage Hike?](#)

*Laurent Bossavie, Social Protection & Labor, Global Practice, World Bank
Ayşenur Acar Erdoğan, Social Protection & Labor, Global Practice, World Bank*

Mattia Makovec, Social Protection & Labor, Global Practice, World Bank

Firms can respond to minimum wage increases in many ways, beyond employment cuts. One question on which evidence is particularly scarce is whether firms exit the formal economy as a result of an increase in the statutory minimum wage. By increasing the labor costs of firms that operate formally, minimum wage hikes can put pressure on profit margins and raise the relative attractiveness of informal economic activities. This question is particularly relevant for developing economies where small and low-productivity firms predominate and informality remains common.

The recent paper by Bossavie, Acar and Makovec (2019) investigates this question in the Turkish context. The authors take advantage of a 33 percent increase in the nominal minimum wage in December 2015. As the hike was nationwide, they use wage levels in firms prior to the increase to classify them as high-exposure (or “treated”) and low-exposure (or “control”) firms and estimate the effect of the increase. They find that the destruction of formal firms significantly rose as a result of the minimum wage hike. Impacts are concentrated on small and low-productivity firms, suggesting that the minimum wage hike primarily drives low-performing firms out of the formal economy. They also report that most workers from exiting formal firms transition into informal employment. These results are consistent with the idea that informality can help alleviate labor market shocks that hit the formal sector. These findings also suggest possible trade-offs between improving workers’ conditions in the formal sector and simultaneous efforts to reduce informality, a common policy priority in developing countries. [Read more»](#)



[Common Transport Infrastructure: A Quantitative Model and Estimates from the Belt and Road Initiative](#)

Alen Mulabdic, Equitable Growth, Finance & Institutions Practice Group, World Bank

Michele Ruta, Equitable Growth, Finance & Institutions Practice Group, World Bank

François de Soyres, the Federal Reserve Board of Governors

This paper presents a structural general equilibrium model to analyze the effects on trade, welfare, and gross domestic product of common transport infrastructure. Specifically, the model builds on the framework by Caliendo and Parro (2015)—a Ricardian model with sectoral linkages, trade in intermediate goods and sectoral heterogeneity—to allow for changes in trade costs due to improvements in transportation infrastructure, financed through domestic taxation, connecting multiple countries. The model highlights the trade impact of infrastructure investments through cross-border input-output linkages.

This framework is then used to quantify the impact of the Belt and Road Initiative. Using new estimates on the effects on trade costs of transport infrastructure related to the initiative based on Geographic Information System analysis, the model shows that gross domestic product will increase by up to 3.4 percent for participating countries and by up to 2.9 percent for the world. Because trade gains are not commensurate with projected investments, some countries may experience a negative welfare effect due to the high cost of the infrastructure. The analysis also finds strong complementarity between infrastructure investment and trade policy reforms. [Read more»](#)



[City Decline in an Urbanizing World](#)

Paula Restrepo, Social, Urban, Rural and Resilience Global Practice, World Bank

Luis E. Quintero, Johns Hopkins Carey Business School

Urban studies and policy often focus on how to manage urban growth in the developing world. However, over the past decades demographic transition has advanced in developed countries and many countries in Eastern Europe and Central Asia have started to see their population decline. This paper is one of the first to provide evidence of the striking phenomenon of city population decline in ECA. It uses a novel dataset of more than 5,000 cities spanning three decades in countries across the region. The paper presents a simple theoretical model that aims at predicting how a system of cities behaves when facing a negative population shock. The theoretical model suggests that in a

context of population decline, large cities – having large local markets – loose relatively less population while cities that are close to large markets - loose relatively more population. The model also predicts that productivity will increase after population declines, especially in large cities. The model is tested empirically using the city-dataset. The empirical analysis confirms the positive effect on population growth of having a large local market and the negative effect of having large access to markets. The short run impact of population decline on productivity is mixed. [Read more»](#)

OTHER INTERESTING SUBMISSIONS

[The Effect of Immigration on Natives' School Achievement](#)

Laurent Bossavie, Policy Research Working Paper 8492 - June 2018

Using a rich data set of primary school students, this paper estimates the effects of immigrant concentration in the classroom on the academic achievement of natives. The author exploits rare information on age-at migration to estimate separate spillover effects by duration of stay of immigrant classmates.

[Can Government Intervention Make Firms More Investment-Ready? A Randomized Experiment in the Western Balkans](#)

Ana Paula Cusolito, Ernest Dautovic, and David McKenzie, Policy Research Working Paper 8541 - August 2018

The study described in the paper conducted a five-country randomized experiment in the Western Balkans that worked with 346 firms and delivered an investment readiness program to half of the firms. The results show that treated firms attained significantly more media attention and were 5 percentage points more likely to have made a deal with an outside investor.

[Welfare benefits of EU integration in the Western Balkans when domestic workers' mobility is limited](#)

Mathilde Lebrand, August 2019

This paper is focusing at the welfare benefits from better integration with the European Union (EU) driven by regional transport and trade facilitation investments when regions are differently impacted and workers imperfectly relocate. The author finds that transport investments favor development in regions with a comparative advantage in manufacturing while people in more distant regions tend to lose out.

[Where They Live: District-Level Measures of Poverty, Average Consumption, and the Middle Class in Central Asia](#)

William Seitz, Policy Research Working Paper 8940 - July 2019

This study looks at nationally (and regionally) representative data from four Central Asian countries (Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan) and focuses on sharpening the reliability of the survey estimates to allow reporting at a level below what is traditionally reported. The results provide detailed measures of welfare that in turn can be disaggregated to the district level.

BLOGS

Common transport infrastructure: Welfare effects of the Belt and Road Initiative

Francois de Soyres, Alen Mulabdic and Michele Ruta, July 2019

This column uses new data on China's Belt and Road Initiative (BRI) transport projects to quantify the economic impact of the initiative. The results show that the gains from the BRI could be positive on aggregate. But they are unevenly distributed across countries, with some economies potentially losing from the infrastructure investment. [Read the blog »](#)

Taking Stock of Bank Regulatory Reforms Ten Years After the Failure of Lehman Brothers

Deniz Anginer, Ata Can Bertay, Robert J. Cull, Asli Demirgüç-Kunt, and Davide Salvatore Mare, January 2020

In this blog the authors summarize developments since the Global Financial Crisis in capital regulation, market discipline and supervisory monitoring using information from the World Bank's Bank Regulation and Supervision Survey (BRSS). [Read the blog »](#)

CALENDAR OF EVENTS

- **February 20, 2020:** ECA Talks "Jobs Creation and Automation" with Mary C. Hallward-Driemeier
- **April 7, 2020:** ECA Talks "Successes and challenges of the ECA countries transition to the market economy after the fall of the Berlin wall" with Joseph Stiglitz and William Easterly

Check [ECA Lectures](#) and [ECA Talks](#) to learn more about our events.

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