

A Dynamic Framework for Identification and Estimation of Nonseparable Production Functions

Justin Doty

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Introduction

- This paper identifies and estimates a nonseparable production function with unobserved heterogeneity
- Allows for interactions in the unobservable (productivity) with inputs, in a sense, allowing for non-Hicks neutral productivity shocks
- The conditional output distribution is allowed to vary with productivity
- Inputs can contain unobservable demand shocks which would violate identification arguments of OP, LP, ACF
- The identification argument does not rely on the control function approach so there are no identification issues between using value-added and gross-output production functions
- A more flexible model for productivity and non-linear persistence
- Productivity can be allowed to depend on the magnitude and sign of current and future innovation shocks

The Production Function

- Consider a nonseparable model for a firm's gross-output production function (in logs)

$$y_{it} = f_t(k_{it}, l_{it}, m_{it}, \omega_{it}, \eta_{it}) \quad (1)$$

- Allows for non-linear interactions between inputs and unobserved productivity
- Assume the following

Assumption 1 (Production Function)

- The unanticipated production shocks η_{it} are i.i.d. over firms and time.*
- The unanticipated production shock η_{it} follows a standard uniform distribution independent of $(k_{it}, l_{it}, m_{it}, \omega_{it})$.*
- $\tau \rightarrow Q_t^y(k_{it}, l_{it}, m_{it}, \omega_{it}, \tau)$ is strictly increasing on $(0, 1)$.*

Productivity

- Productivity evolves according to an exogenous first-order Markov process given by

$$\omega_{it} = Q_t^\omega(\omega_{it-1}, \xi_{it}), \quad \xi_{it} \sim \text{Uniform}(0, 1), \quad (2)$$

where $\xi_{i1}, \dots, \xi_{iT}$ are independent uniform random variables which represent innovation shocks to productivity

- The function Q^ω is a nonlinear function that allows the persistence in productivity in firms to be nonlinear across different quantiles

Assumption 2 (Productivity)

- 1 The productivity innovation shocks ξ_{it} are i.i.d. across firms and time.
- 2 ξ_{it} follows a standard uniform distribution independent of previous period productivity ω_{it-1} .
- 3 $\tau \rightarrow Q_t^\omega(\omega_{it-1}, \tau)$ is strictly increasing on $(0, 1)$.

Flexible Inputs

- Labor and Material inputs are chosen to maximize current period profits
- Therefore they are a function of current period state variables

$$l_{it} = Q_t^\ell(k_{it}, \omega_{it}, \epsilon_{\ell,it}), \quad \epsilon_{\ell,it} \sim \text{Uniform}(0, 1), \quad (3)$$

$$m_{it} = Q_t^m(k_{it}, l_{it}, \omega_{it}, \epsilon_{m,it}), \quad \epsilon_{m,it} \sim \text{Uniform}(0, 1), \quad (4)$$

- $\epsilon_{\ell,it}$ and $\epsilon_{m,it}$ are i.i.d. unobservable input demand shocks that are assumed to be independent of current period state variables
- In the control function approach, with material inputs as a proxy, this function could not be inverted as an expression of productivity only
- This framework is similar to that of Hu, Huang, and Sasaki, 2020
- This can also be extended to the case where labor has adjustment frictions

Assumption 3 (Flexible Inputs)

- 1 *The unobserved input demand shocks $\epsilon_{\ell,it}$ and $\epsilon_{m,it}$ are i.i.d. across firms and time.*
- 2 *$\epsilon_{\ell,it}$ and $\epsilon_{m,it}$ follow a standard uniform distribution independent of (k_{it}, ω_{it}) and $(k_{it}, l_{it}, \omega_{it})$, respectively.*
- 3 *$\tau \rightarrow Q_t^\ell(k_{it}, \omega_{it}, \tau)$ and $\tau \rightarrow Q_t^m(k_{it}, l_{it}, \omega_{it}, \tau)$ are strictly increasing on $(0, 1)$.*

Capital and Investment

- Capital accumulates to the following generalized law of motion

$$K_{it} = \kappa_t(K_{it-1}, I_{it-1}, v_{it-1}) \quad (5)$$

where I_{it-1} denotes firm investment in the prior period

- Eliminates the deterministic relationship of capital with respect to previous period state and choice variables
- Assume this error term is independent of the arguments in the capital accumulation law
- In each period, a firm chooses investment to maximize its discounted future profits:

$$I_{it} = \iota_t(K_{it}, \omega_{it}) = \underset{I_{it} \geq 0}{\operatorname{argmax}} \left[\Pi_t(K_{it}, \omega_{it}) - c(I_{it}, \omega_{it}) + \beta \mathbb{E}[V_{t+1}(K_{it+1}, \omega_{it+1}) | \mathcal{I}_t] \right], \quad (6)$$

Capital and Investment

- $\pi_t(\cdot)$ is current period profits as a function of the state variables $c(\cdot)$ is the cost function, \mathcal{I}_t is information set
- Empirical investment rule is

$$i_{it} = Q_t^i(k_{it}, \omega_{it}, \zeta_{it}), \quad \zeta_{it} \sim \text{Uniform}(0, 1). \quad (7)$$

Assumption 4 (Capital Accumulation and Investment)

- 1 The unobserved investment demand shocks ζ_{it} is i.i.d. across firms and time.
- 2 ζ_{it} follows a standard uniform distribution independent of (k_{it}, ω_{it}) .
- 3 The production shock η_{it} and ζ_{it} are independent conditional on $(k_{it}, l_{it}, m_{it}, \omega_{it})$. In addition, v_{it} is independent of η_{it} conditional on $(k_{it}, l_{it}, m_{it}, \omega_{it})$
- 4 $\tau \rightarrow Q_t^i(k_{it}, \omega_{it}, \tau)$ is strictly increasing on $(0, 1)$

Nonparametric Identification

- I show that the conditional densities corresponding to production, inputs, and productivity are nonparametrically identified
- Let $Z_t = (l_t, k_t, m_t, k_{t+1})$ denote conditioning variables

Assumption 5 (Conditional Independence)

- 1 $f(y_t|y_{t+1}, l_t, \omega_t, Z_t) = f(y_t|\omega_t, Z_t)$
- 2 $f(y_{t+1}|l_t, \omega_t, Z_t) = f(y_{t+1}|\omega_t, Z_t)$

- First equality states that conditional on ω_t and Z_t , y_{t+1} and l_t do not provide any additional information about y_t
- Second equality states that conditional on ω_t and Z_t , l_t does not provide any additional information about y_{t+1}
- Satisfied by mutual independence assumptions on η_t and ζ_t conditional on $(\omega_t, k_t, l_t, m_t)$

Nonparametric Identification

- Begin by relating a conditional density as a function of observable to densities containing unobserved productivity
- Using the conditional independence assumption, I can write

$$f_{y_t, l_t | y_{t+1}, Z_t} = \int f_{y_t | Z_t, \omega_t} f_{l_t | Z_t, \omega_t} f_{\omega_t | y_{t+1}, Z_t} d\omega_t \quad (8)$$

- The identification strategy follows HS by using a eigenvalue-eigenfunction decomposition of integral operators of (8)

Definition 1

(Integral Operator) Let a and b denote random variables with supports \mathcal{A} and \mathcal{B} . Given two corresponding spaces $\mathcal{G}(\mathcal{A})$ and $\mathcal{G}(\mathcal{B})$ of functions with domains \mathcal{A} and \mathcal{B} , let $L_{b|a}$ denote the operator mapping $g \in \mathcal{G}(\mathcal{A})$ to $L_{b|a}g \in \mathcal{G}(\mathcal{B})$ defined by

$$[L_{b|a}g](b) \equiv \int_{\mathcal{A}} f_{b|a}(b|a)g(a)da,$$

where $f_{b|a}$ denotes the conditional density of b given a .

Nonparametric Identification

- The observed density in (8) can be written in operator notation

$$L_{y_t, I_t | y_{t+1}, Z_t} = L_{y_t | Z_t, \omega_t} \Delta_{I_t | Z_t, \omega_t} L_{\omega_t | y_{t+1}, Z_t} \quad (9)$$

- Will show that under a set of assumptions, the conditional density is identified from an eigenvalue-eigenfunction decomposition of (9)

Assumption 6 (Injectivity)

The operators $L_{y_t | Z_t, \omega_t}$ and $L_{y_{t+1} | Z_t, \omega_t}$ are injective

- The above assumption allows us to take inverses of the operators.
- Consider the operator $L_{y_t | Z_t, \omega_t}$, injectivity of this operator can be interpreted as its corresponding density $f_{y_t | Z_t, \omega_t}(I_t | K_t, \omega_t)$ having sufficient variation in ω_t given Z_t .
- This assumption is often phrased as completeness condition in the nonparametric IV literature on the density $f_{y_t | Z_t, \omega_t}(y_t | Z_t, \omega_t)$.

Assumption 7 (Uniqueness)

For any $\bar{\omega}_t, \tilde{\omega}_t \in \Omega$, the set $\{f_{I_t|\omega_t, Z_t}(I_t|\bar{\omega}_t, Z_t) \neq f_{I_t|\omega_t, Z_t}(I_t|\tilde{\omega}_t, Z_t)\}$ has positive probability whenever $\bar{\omega}_t \neq \tilde{\omega}_t$.

- This assumption is relatively weak
- Satisfied if there is conditional heteroskedasticity in $f_{I|\omega, Z}$
- Satisfied if any functional of its distribution is strictly increasing in ω_t
- I assume $E[I_t|\omega_t, Z_t]$ is strictly increasing in ω_t
- Similar to the invertibility condition in Olley and Pakes, 1996

Nonparametric Identification

Assumption 8 (Normalization)

There exists a functional Γ such that $\Gamma[f_{y_t|\omega_t, Z_t}(y_t|\omega_t, Z_t)] = \omega_t$.

- This functional does not need to be known
- Sufficient to consider a known function of the data distribution as shown by Arellano and Bonhomme, 2016
- In my empirical application, I consider a nonseparable translog production function
- The assumption can be satisfied by the normalization $E[y_t|\omega_t, 0] = \omega_t$
- For more generalized production functions, if $E[y_t|\omega_t, Z_t]$ is strictly increasing in ω_t , then one could normalize $\omega_t = E[y_t|\omega_t, Z_t]$
- These restrictions are easily adaptable in estimation as it amounts to centering the coefficients in the model

Theorem 1 (Identification)

Under Assumptions 5, 6, 7, and 8, given the observed density $f_{y_t, l_t | y_{t+1}, Z_t}$, the equation

$$f_{y_t, l_t | y_{t+1}, Z_t} = \int f_{y_t | \omega_t, Z_t} f_{l_t | \omega_t, Z_t} f_{\omega_t | y_{t+1}, Z_t} d\omega_t \quad (10)$$

admits a unique solution for $f_{y_t | \omega_t, Z_t}$, $f_{l_t | \omega_t, Z_t}$, and $f_{\omega_t | y_{t+1}, Z_t}$

- The proof follows using Hu and Schennach, 2008
- However it does not directly identify the Markov transition function for productivity $f_{\omega_{it+1} | \omega_{it}}(\omega_{it+1} | \omega_{it})$

Nonparametric Identification

Corollary 1 (Identification of Markov Process: Stationarity Case)

Suppose that the production function is stationary, $f_{y_t|\omega_t, Z_t} = f_{y_1|\omega_1, Z_1}, \forall t \in \{1, \dots, T\}$. Then, under Assumptions 5, 6, 7, and 8, the observed density $f_{y_t, l_t|y_{t+1}, Z_t}$, uniquely determines the density $f_{\omega_{t+1}|\omega_t}, \forall t \in \{1, \dots, T-1\}$

Corollary 2 (Identification of Markov Process: Non-Stationarity Case)

Under Assumptions 5, 6, 7, and 8, the observed density $f_{y_{t+1}, l_{t+1}|y_{t+2}, Z_{t+1}}$, uniquely determines the density $f_{\omega_{t+1}|\omega_t}, \forall t \in \{1, \dots, T-2\}$

Econometric Procedure: Production

- The production function is specified as Translog with non-Hicks neutral effects

$$Q_t^y(k_{it}, l_{it}, m_{it}, \omega_{it}, \tau) =$$

$$\begin{aligned} & \gamma_0(\tau) + (\gamma_k(\tau) + \sigma_k(\tau)\omega_{it})k_{it} + (\gamma_l(\tau) + \sigma_l(\tau)\omega_{it})l_{it} + (\gamma_m(\tau) + \sigma_m(\tau)\omega_{it})m_{it} \\ & + (\gamma_{kl}(\tau) + \sigma_{kl}(\tau)\omega_{it})k_{it}l_{it} + (\gamma_{lm}(\tau) + \sigma_{lm}(\tau)\omega_{it})l_{it}m_{it} + (\gamma_{km}(\tau) + \sigma_{km}(\tau)\omega_{it})k_{it}m_{it} \\ & + (\gamma_{kk}(\tau) + \sigma_{kk}(\tau)\omega_{it})k_{it}^2 + (\gamma_{ll}(\tau) + \sigma_{ll}(\tau)\omega_{it})l_{it}^2 + (\gamma_{mm}(\tau) + \sigma_{mm}(\tau)\omega_{it})m_{it}^2 + \sigma_\omega(\tau)\omega_{it} \end{aligned} \quad (11)$$

- Similar model was estimated by Akerberg and Chen (2015)
- In my approach I can simulate productivity from estimated initial conditions and Markov process to compute average derivative effects
- Provides a better picture of heterogeneity instead of reporting individual coefficients

Econometric Procedure: Productivity

- I specify productivity using 3rd order polynomial

$$Q^{\omega}(\omega_{it-1}, \tau) = \rho_0(\tau) + \rho_1(\tau)\omega_{it-1} + \rho_2(\tau)\omega_{it-1}^2 + \rho_3(\tau)\omega_{it-1}^3. \quad (12)$$

- Initial productivity

$$Q^{\omega_1}(k_{i1}, \tau) = \sum_{j=1}^J \rho_{\omega_1,j}(\tau) \phi_{\omega_1,j}(k_{i1}), \quad (13)$$

- I can also consider the case where productivity may evolve endogenously as Doraszelski and Jaumandreu, 2013

$$Q^{\omega}(\omega_{it-1}, r_{it-1}, \tau) = \mathbb{1}\{R_{it-1} = 0\} Q^{\omega}(\omega_{it-1}, \tau) + \mathbb{1}\{R_{it-1} > 0\} Q^{\omega,r}(\omega_{it-1}, r_{it-1}, \tau). \quad (14)$$

Econometric Procedure: Flexible Inputs

- I specify the labor input demand equation as follows:

$$Q_t^\ell(k_{it}, \omega_{it}, \tau) = \sum_{j=1}^J \alpha_{\ell,j}(\tau) \phi_{\ell,j}(k_{it}, \omega_{it}), \quad (15)$$

where $\phi_{\ell,j}$ can be another non-linear function

- Material inputs are specified as

$$Q_t^m(k_{it}, l_{it}, \omega_{it}, \tau) = \sum_{j=1}^J \alpha_{m,j}(\tau) \phi_{m,j}(k_{it}, l_{it}, \omega_{it}), \quad (16)$$

- Again, $\phi_{m,j}$ can be a non-linear function

Econometric Procedure: Investment

- The investment demand function is specified as

$$i_{it} = Q_t^i(k_{it}, \omega_{it}, \tau) = \sum_{j=1}^J \delta_j(\tau) \phi_{i,j}(k_{it}, \omega_{it}), \quad (17)$$

where $\phi_{i,j}$ is specified similarly as the labor and material input decision rule.

- In the case where investment is censored, I can write

$$Q_t^{i*}(k_{it}, \omega_{it}, \tau) = \max\{0, \sum_{j=1}^J \delta_j(\tau) \phi_{i,j}(k_{it}, \omega_{it})\}, \quad (18)$$

due to the equivariance properties of quantiles

- The censored quantile regression model avoids distributional assumptions at the cost of computational complexity
- Censored investment levels are not an issue in Compustat

Econometric Restrictions

Note that the following conditional moment restrictions hold as an implication of Assumptions 1-4

$$\mathbb{E} \left[\Psi_{\tau} \left(y_{it} - Q_t(y_{it} | k_{it}, l_{it}, m_{it}, \omega_{it}; \beta(\tau)) \right) \middle| k_{it}, l_{it}, m_{it} \right] = 0 \quad (19)$$

$$\mathbb{E} \left[\Psi_{\tau} \left(l_{it} - \sum_{j=1}^J \alpha_{l,j}(\tau) \phi_{l,j}(k_{it}, \omega_{it}) \right) \middle| k_{it}, \omega_{it} \right] = 0 \quad (20)$$

$$\mathbb{E} \left[\Psi_{\tau} \left(m_{it} - \sum_{j=1}^J \alpha_{m,j}(\tau) \phi_{m,j}(k_{it}, \omega_{it}) \right) \middle| k_{it}, \omega_{it} \right] = 0 \quad (21)$$

$$\mathbb{E} \left[\Psi_{\tau} \left(i_{it} - \sum_{j=1}^J \delta_j(\tau) \phi_{i,j}(k_{it}, \omega_{it}) \right) \middle| k_{it}, \omega_{it} \right] = 0 \quad (22)$$

For $t \geq 2$,

$$\mathbb{E} \left[\Psi_{\tau} \left(\omega_{it} - \rho_0(\tau) - \rho_1(\tau) \omega_{it-1} - \rho_2(\tau) \omega_{it-1}^2 - \rho_3(\tau) \omega_{it-1}^3 \right) \middle| \omega_{it-1} \right] = 0, \quad (23)$$

$$\mathbb{E} \left[\Psi_{\tau} \left(\omega_{i1} - \sum_{j=1}^J \rho_{\omega_1,j}(\tau) \phi_{\omega_1,j}(k_{i1}) \right) \middle| k_{i1} \right] = 0, \quad (24)$$

Econometric Restrictions

- The function $\Psi_\tau(u) = \tau - \mathbb{1}\{u < 0\}$
- Estimating the above conditional moment restrictions is infeasible due to the unobserved productivity component
- Use the unconditional moment restriction and integrate out productivity
- Let the finite and functional parameters be indexed by a finite dimensional parameter vector $\theta(\cdot)$.
- To fix ideas, consider the unconditional moment restriction corresponding to the production function

$$\mathbb{E} \left[\int \Psi_\tau \left(y_{it} - Q_t^y(k_{it}, l_{it}, m_{it}, \omega_{it}; \beta(\tau)) \right) \otimes \begin{pmatrix} k_{it} \\ l_{it} \\ m_{it} \\ \omega_{it} \end{pmatrix} g_i(\omega_i^T; \theta(\cdot)) d\omega_i^T \right] = 0, \quad (25)$$

- The posterior density $g_i(\omega_i^T; \theta(\cdot)) = f(\omega_i^T | y_i^T, k_i^T, l_i^T, m_i^T, i_i^T, \theta(\cdot))$ involves the entire set of model parameters

Implementation

- Therefore, it is impossible to estimate the model parameters in a τ -by- τ procedure
- To eliminate the intractability of this problem, the continuous model parameters are approximated by piece-wise linear splines
- θ is a piecewise-polynomial interpolating splines on a grid $[\tau_1, \tau_2], [\tau_3, \tau_4], \dots, [\tau_{Q-1}, \tau_Q]$, contained in the unit interval and is constant on $[0, \tau_1]$ and $[\tau_Q, 1)$
- The intercept coefficient β_0 is specified as the quantile of an exponential distribution on $(0, \tau_1]$ (indexed by λ^-) and $[\tau_{Q-1}, 1)$ (indexed by λ^+).
- The remaining functional parameters are modeled similarly.
- With piece-wise linear splines, the posterior density has a closed form expression without relying on strong distributional assumptions for estimation

Implementation

- In order to estimate the model, the integral inside the expectation of Equation (25) needs to be approximated
- This can be done using quadrature methods or Monte Carlo integration by converting the problem into a weighted quantile regression
- Due to the high-dimensionality of my application I choose to use a random-walk Metropolis Hastings algorithm to compute the integral
- This is known as a Monte Carlo Expectation Maximization (MCEM) procedure where the maximization step is performed using quantile regression
- This type of estimator is used by Arellano and Bonhomme, 2016 and Arellano, Blundell, and Bonhomme, 2017

Implementation

Given an initial parameter value $\hat{\theta}^0$. Iterate on $s = 0, 1, 2, \dots$ in the following two-step procedure until converge to a stationary distribution:

- ① *Stochastic E-Step*: Draw M values $\omega_i^{(m)} = (\omega_{i1}^{(m)}, \omega_{i2}^{(m)}, \dots, \omega_{iT}^{(m)})$ from

$$g_i(\omega_i^T; \hat{\theta}^{(s)}) = f(\omega_i^T | y_i^T, k_i^T, l_i^T, m_i^T, i_i^T; \hat{\theta}^{(s)}) \propto \\ \prod_{t=1}^T f(y_{it} | k_{it}, l_{it}, m_{it}, \omega_{it}; \hat{\beta}^{(s)}) f(l_{it} | k_{it}, \omega_{it}; \hat{\alpha}_l^{(s)}) f(m_{it} | k_{it}, l_{it}, \omega_{it}; \hat{\alpha}_m^{(s)}) \\ \times f(i_{it} | k_{it}, \omega_{it}; \hat{\delta}^{(s)}) \prod_{t=2}^T f(\omega_{it} | \omega_{it-1}; \hat{\rho}^{(s)}) f(\omega_{i1} | k_{i1}; \hat{\rho}_{\omega_1}^{(s)})$$

- ② *Maximization Step*: For $q = 1, \dots, Q$, solve (e.g for production function)

$$\hat{\beta}(\tau_q)^{(s+1)} = \underset{\beta(\tau_q)}{\operatorname{argmin}} \sum_{i=1}^N \sum_{t=1}^T \sum_{m=1}^M \psi_{\tau_q} \left(y_{it} - Q_t^y(k_{it}, l_{it}, m_{it}, \omega_{it}^{(m)}; \beta(\tau_q)) \right)$$

Empirical Implementation

- $\psi_\tau(u) = (\tau - \mathbb{1}\{u < 0\})u$ is the “check” function from quantile regression
- Repeat Step 2 for estimating the productivity process, input decision rules and investment
- Take $M = 1$ in the MCEM algorithm and the report estimates as the average of the last $\tilde{S} = S/2$ draws
- This is known as the stochastic EM algorithm (stEM) of Celeux and Diebolt, 1985
- The sequence of maximizers $\hat{\theta}^{(s)}$ is a time-homogeneous Markov chain which, if ergodic, will converge to its stationary distribution
- Nielsen, 2000 provides sufficient conditions for ergodicity and asymptotic properties of the estimator when the “M-step” is solved using maximum likelihood
- Arellano and Bonhomme, 2016 discuss the asymptotic properties of the estimator when the M-step is solved using quantile regression

Empirical Implementation

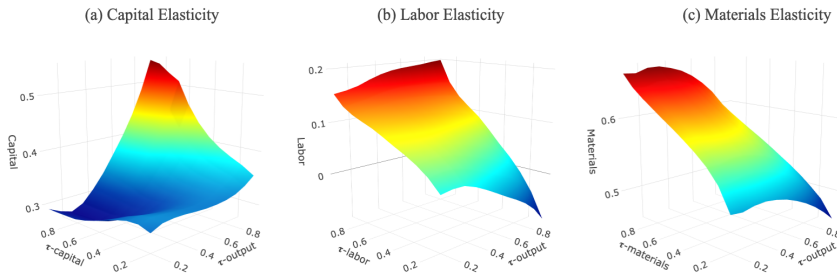
- Estimation procedure is ran with 500 random walk Metropolis-Hastings steps keeping the last draw for estimation
- 200 EM steps where the average is taken over half the draws
- $Q = 11$ for grid size for the interpolating spline
- Experimented with many different proposal distributions and initial values
- Normal distribution centered at the current draw of productivity with variance equal 0.01
- Acceptance rate $\approx 10\%$
- Initial values for productivity are simulated from TFP estimated from the LP model
- Replication code is available on author's Github

Application

- Standard and Poors Compustat database 1997 – 2016
- Productivity is simulated from its estimated parameters and used to construct investment, inputs, and output using their estimated parameters
- Capital is simulated from a linear accumulation process with constant depreciation rate 0.02
- Results are not too different from reasonable specifications for the capital accumulation process
- Interested in a variety of average and individual marginal quantile effects
- Using these estimates, can analyze how firms react to latest shocks to production, inputs, and productivity
- How long does it take for firms to recover from bad shocks to productivity?

Production Elasticities

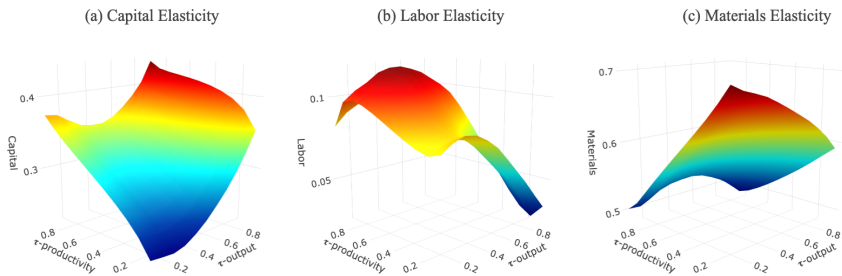
Figure 1: Output Elasticities



* Panel (a): Capital elasticity evaluated at τ_{η} and percentiles of capital τ_k averaged over values of (l_{it}, m_{it}) that correspond to τ_k . Panel (b): Labor elasticity evaluated at τ_{η} and percentiles of labor τ_l averaged over values of (k_{it}, m_{it}) . Panel (c): Materials elasticity evaluated at τ_{η} and percentiles of materials τ_m averaged over values of (k_{it}, l_{it}) .

Production Elasticities

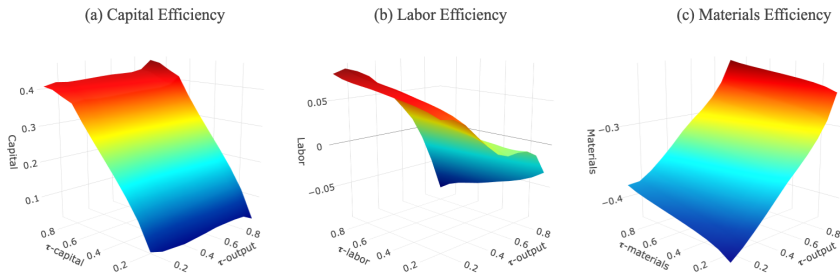
Figure 2: Output Elasticities



*Panel (a): Capital elasticity evaluated at τ_η and τ -productivity averaged over values of (k_{it}, l_{it}, m_{it}) that correspond to τ -productivity. Panel (b): Labor elasticity evaluated at τ_η and τ -productivity averaged over values of (k_{it}, l_{it}, m_{it}) that correspond to τ -productivity. Panel (c): Materials elasticity evaluated at τ_η and τ -productivity averaged over values of (k_{it}, l_{it}, m_{it}) that correspond to τ -productivity.

Production Elasticities

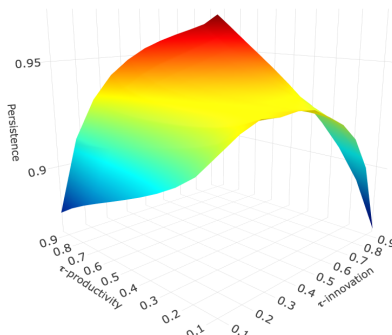
Figure 3: Non-Hicks Neutral Elasticities



* Panel (a): Capital efficiency evaluated at τ_{η} and percentiles of capital τ_k averaged over values of (l_{it}, m_{it}) that correspond to τ_k . Panel (b): Labor efficiency evaluated at τ_{η} and percentiles of labor τ_l averaged over values of (k_{it}, m_{it}) . Panel (c): Materials efficiency evaluated at τ_{η} and percentiles of materials τ_m averaged over values of (k_{it}, l_{it}) .

Productivity Persistence

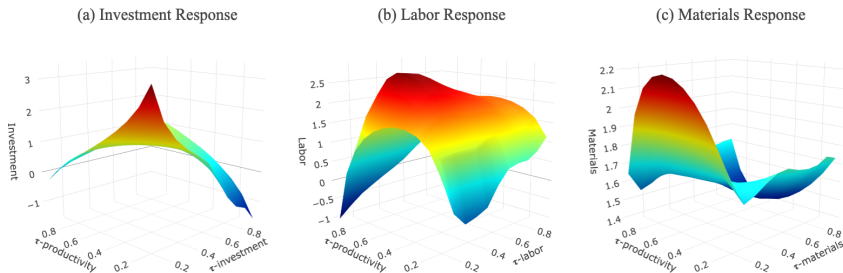
Figure 4: Productivity Persistence



* Estimates of average productivity persistence evaluated at τ_{ξ} and percentiles of previous productivity.

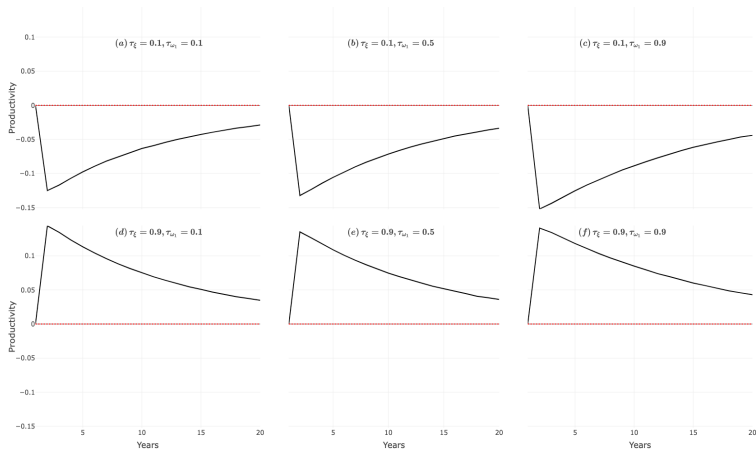
Marginal Productivities

Figure 5: Input Demand Responses to Productivity



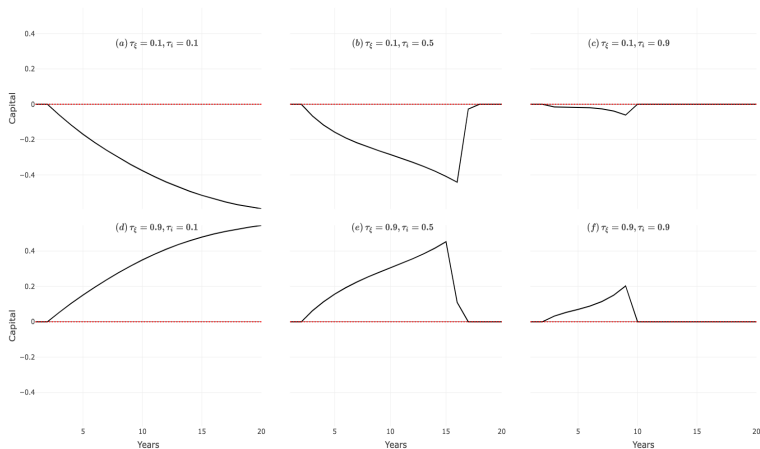
* Panel (a): Investment demand evaluated at τ_{ζ} and percentiles of productivity τ_{ω} averaged over values of k_{it} . Panel (b): Labor demand evaluated at $\tau_{\epsilon\ell}$ and percentiles of productivity τ_{ω} averaged over values of k_{it} . Panel (c): Material demand evaluated at $\tau_{\epsilon m}$ and percentiles of productivity τ_{ω} averaged over values of k_{it} and l_{it}

Productivity Innovation Shocks



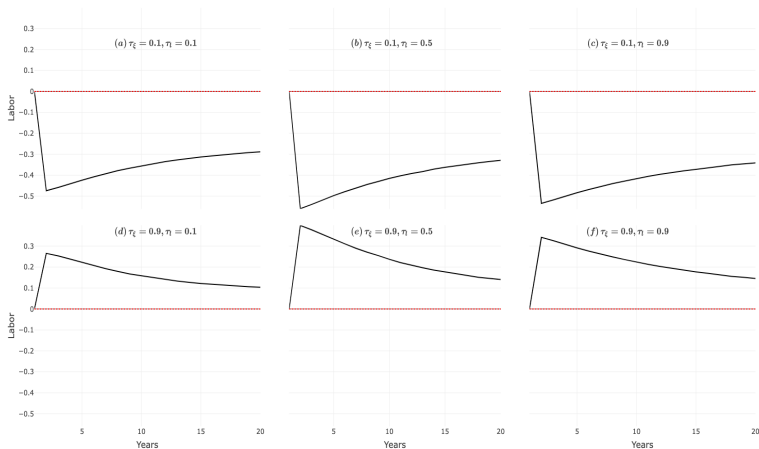
*Top row: Differences between firms hit with low productivity shock $\tau_{\xi} = 0.1$ and medium shock $\tau_{\xi} = 0.5$ at different levels of initial productivity. Bottom row: Differences between firms hit with high productivity shock $\tau_{\xi} = 0.9$ and medium shock $\tau_{\xi} = 0.5$ at different levels of initial productivity.

Productivity Innovation Shocks to Capital



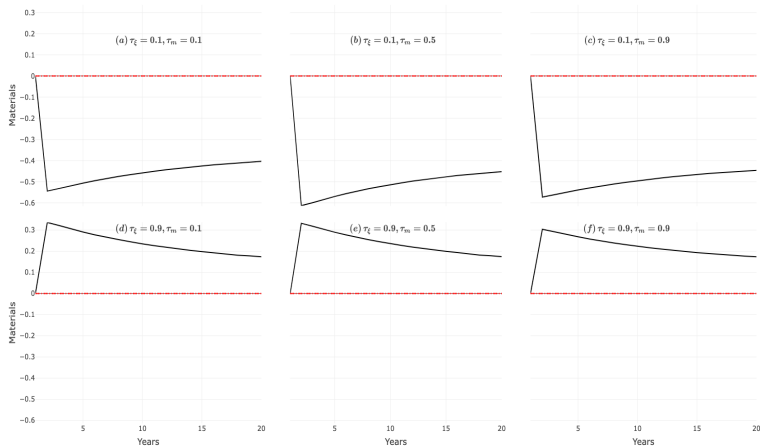
*Top row: Differences between firms hit with low productivity shock $\tau_\xi = 0.1$ and medium shock $\tau_\xi = 0.5$ at different levels of investment demand. Bottom row: Differences between firms hit with high productivity shock $\tau_\xi = 0.9$ and medium shock $\tau_\xi = 0.5$ at different levels of investment demand

Productivity Innovation Shocks to Labor



*Top row: Differences between firms hit with low productivity shock $\tau_\xi = 0.1$ and medium shock $\tau_\xi = 0.5$ at different levels of labor demand. Bottom row: Differences between firms hit with high productivity shock $\tau_\xi = 0.9$ and medium shock $\tau_\xi = 0.5$ at different levels of labor demand.

Productivity Innovation Shocks to Materials



*Top row: Differences between firms hit with low productivity shock $\tau_\xi = 0.1$ and medium shock $\tau_\xi = 0.5$ at different levels of materials demand. Bottom row: Differences between firms hit with high productivity shock $\tau_\xi = 0.9$ and medium shock $\tau_\xi = 0.5$ at different levels of materials demand.

Conclusion

- Nonparametric identification of production function, input demand, and productivity
- Proposed an estimation framework to document firm heterogeneity in production, input decisions, and productivity
- Asymmetric productivity persistence depends on size of innovation shock and levels of previous productivity
- Some firms respond to productivity shocks by using more inputs, but this affect is asymmetric for different productivity levels input demand size
- Asymmetric impact of innovation shocks to inputs after bad/good shocks
- Extension to multi-dimensional unobservables: fixed effects, labor-augmenting productivity
- Implications for TFP estimates? Market power?