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THE FRENCH CENTRE FOR RESEARCH
AND STUDIES ON THE WORLD ECONOMY

CONTENTS:

FOCUS

Ten Years of Euro: As Anticipated, Gains and Costs

Ten years ago, eleven European countries, later joined by five others, gave up their national currencies to create the euro. Their motivation was that the gains in terms of reduced transaction costs, increased competition, increased credibility, better coordination, and possibly currency internationalization, would overcome the costs arising from the loss of national monetary-policy independence. After ten years of operation, it seems that all the promises of the single currency - good or bad - have, at least partially, come true.

Recent research carried out at CEPII investigates the effects of the euro adoption on individual export flows, one flow being a single firm exporting a single product to a single destination. Estimations on French exports to Eurozone countries show that the monetary union has increased by around 6.5% the number of export flows to Eurozone destinations, from 1998 to 2003. No effect can be observed on the average value of individual flow. In other words, the euro contributed positively to the aggregate value of French exports through its extensive margin, while the intensive margin of French exports did not behave differently for eurozone and non-eurozone destinations. After breaking down the extensive margin, results point out that the euro stimulated a rise in the number of different products categories exported by firm, with no effect on the number of exporting firms or destination markets. These results suggest that the reduction in transaction costs and a greater price transparency increased competition on the export market. This did not give French domestic non-exporters more incentive to access Eurozone markets.

The reinforcement of competition can be observed in export prices. Considering a single product category, the average export price level to the Eurozone destinations is slightly lower than to other

OECD markets. Furthermore, euro adoption reduced price discrimination across markets within the Eurozone: before 1999, the average dispersion of prices was 5% lower in Eurozone destinations, as compared to other OECD destinations; after the introduction of the euro, this difference in the extent of price discrimination almost reached 7%.

On the macroeconomic front, the objective of low inflation has clearly been achieved for the Eurozone as a whole. However, some countries – Greece, Spain and Ireland – experienced higher inflation than Eurozone average. This can be seen as one expected consequence of the single currency: a single nominal short term interest rate means that the most inflationary countries have the lowest real interest rates. These low rates encourage households and companies to get into debt in order to consume and invest, which reinforces the increasing pressure on demand, and therefore on prices. Thus, the single monetary policy proved to be destabilizing for the most inflationary countries, and possibly contributed to real estate bubbles. These countries would have needed more restrictive fiscal policies than those required by the Stability and Growth Pact. In Spain for instance, even though the public budget balance regularly improved, the continuous increase in the current account deficit revealed insufficient private savings, which would have justified a more restrictive policy. Conversely, Germany infringed the stability pact several times, but this did not prevent it from recording increasing external surpluses.

The cost of the single currency or, more precisely, of national policies unsuited to the single currency, must be weighed against the improvement in coordination produced by the euro. Since 1999, the Eurozone has experienced several major world shocks: the burst of the Internet bubble, the September 11th attacks, increases in oil prices and - since 2007 - the global financial and economic crisis. So far the Eurozone resisted as a monetary group and the reactivity of the ECB to the liquidity crisis in autumn 2008 was particularly noticed. The fall of the pound sterling and other European currencies since summer 2008 suggests that things might have been very different in the absence of a single currency. However, the recent surge in sovereign spreads points at some uncertainty regarding the application of the Treaty, with the “no-bail out” and/or the “no monetization” rules having to be circumvented if some sovereign defaults are to be avoided.

Finally, the euro did emerge as an international store of value, although not yet as an international unit of account or means of payment. The emergence of the euro as a store of value may have accentuated the ups and downs of the euro/dollar exchange rate. European exporters suffered from the pro-cyclical nature of the fluctuations of the euro, which depreciated when the demand was vigorous (1999-2000) and appreciated during the activity deceleration (2002-2003, 2008). This pro-cyclicality can be related to the ECB mandate, centered on prices while that of the Fed is more balanced between price and activity objectives. It can also be related to a difference in philosophy concerning the handling of interest rates, the ECB having proved to be more cautious than the Fed, perhaps by fear of a too rapid expansion of credit...

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ON THE RESEARCH AGENDA

The Art of Exception: Sensitive Products in the Doha Negotiations

WTO negotiations are supposed to set general rules for reducing trade barriers. But there are numerous exceptions to that principle since political stakes in each country compel to keep a high level of protection for some sensitive sectors. For example, terms of agricultural trade negotiations allow each country to label as sensitive some products for which opening to trade will be limited. This restricted liberalization results in lower tariff cuts, and also in the implementation or expansion of Tariff Rates Quotas (TRQs), usually set through complex mechanisms.

Trade protection being highly concentrated on a few products, and particularly agricultural products for developed countries, trade liberalization cannot be efficiently approached at an aggregated level of sectors.

We tackle this problem by extending CEPII's multi-country computable general equilibrium model MIRAGE, to work at a product level. We explicitly model agricultural trade flows at the 6-digit level for European and US imports, which allows us to study the specific impact of agricultural market access improvement in these countries. In doing so, we combine assets from general equilibrium and partial equilibrium modeling, taking into account all interdependencies and representing policies in an explicit way.

A first conclusion is the concentration of the gains from trade liberalization in a limited number of products. Eight HS6 positions concentrate half of the trade increase. The 4–6% of sensitive products of the Falconer proposal in the WTO negotiation covers 75–83% of potential trade increase of developing countries exports to European and US markets. It means that the bulk of liberalization will occur in this list of sensitive products, whose specific treatment and consideration appear crucial. The share of trade in products under TRQs also significantly increases after liberalization, which shows how restrictive this instrument can be.

Christophe Gouel & Maria Priscila Ramos

Neither Migration nor Development: the Contradictions of French Co-development Policy

Co-development is based on the idea that migrants contribute to the development of both their host and origin countries, and that public authorities should aim to maximize the positive effects of migration by spurring the financial and human capital gains associated with international population movements. Against this background, French co-development policy, mainly oriented towards African countries, rests on three main thrusts: productive investment, brain circulation, and immigrant return. Yet, a detailed analysis shows that there is a discrepancy between announced objectives and actual means. As a result, the impact of co-development on African countries is very limited since it is more designed according to France’s interests rather than actual recipient countries’ benefits. Above all, it appears that co-development, in its current conception, is not compatible with French immigration policy, since it is difficult to maximize the impact of migration while trying to restrict entries.

David Khoudour-Castéras

Macroeconomic Consequences of Global Endogenous Migration: A General Equilibrium Analysis

History teaches how the pursuit of better living conditions and higher wages is a strong incentive for emigration. In the arrival country, the increase in the labor force, as long as most of the new comers do work, entails an increase in the capital return, which attracts capital flows. Of course, the reverse effect characterizes the leaving country. As a consequence, migration flows change the geographic structure of wages across the world.

From this perspective, using a world general equilibrium model as INGENUE 2 in evaluating the migration flows for the next century has two main advantages. First, it allows studying simultaneously the impact of the migration flows on the arrival country as well as on the leaving country. Second, it makes possible the evaluation of the feedback effect of capital flows and wage changes on migration flows. With this interaction between the demographic part and the economic part of the model, we are able to project dynamic endogenous migrations flows, which brings some light on several important demographic and economic questions.

First, migration could have substantial impact on GDP growth in the region receiving the migrants (positive impact) but also on the region sending the migrants (negative impact). According to our simulations, Western Europe and North America should benefit substantially from the arrival of cohorts of migrants in the next decades. Second, our methodology induces major changes in the volume and distribution of migration flows between regions. For example, net migration flows from Africa are almost four times bigger than the United-Nations 2006 projections for 2050. Third, despite their size, these flows will not be sufficient to counteract the impact of an ageing population in these regions: even when immigration flows are taken into account, pension reforms will remain necessary.

Vladimir Borgy, Xavier Chojnicki, Gilles Le Garrec & Cyrille Schwellnus

Local Export Spillovers in France

The recent theoretical and empirical literature in international trade has recently focused on the micro-determinants of exporting behavior at firm level. However, policy makers of many countries are increasingly interested in the role of local externalities on firms' performance, either in terms of productivity or in terms of exports.

This work is at the intersection of these two concerns. It investigates the presence of local export spillovers on both the extensive (the decision to start exporting) and the intensive (the export volume) margins of trade. We use data on French individual export flows, at the product-level and by destination country, between 1998 and 2003. We investigate whether the individual decision to start exporting and exported volume are influenced by the presence of nearby firms exporting the same product and/or to the same destination, using a gravity-type equation estimated at the firm-product-destination country level.

Spillovers are considered at a detailed geographical level corresponding to employment areas (348 in France). We control for the new economic geography-type selection of firms into agglomerated areas, and for the local price effects of firms agglomeration. Results show evidence of export spillovers on the export decision but not on the exported volume. We interpret this as a first evidence of export spillovers acting through the fixed rather than the variable cost.

Spillovers on the decision to start exporting are stronger when specific, by product and destination, and are not significant when considered on all products or on all products-all destinations. Moreover, export spillovers exhibit a spatial decay within France: the effect of other exporting firms on the export decision is stronger within employment areas and declines with distance.

Sandra Poncet, Pamina Koenig & Florian Mayneris

DATABASES

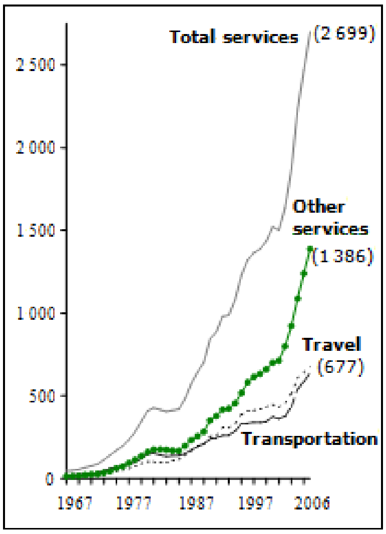
Bilateral Trade Flows in Services: Towards a Harmonized Database

Since its integration into multilateral negotiations through the GATS in 1995, trade in services has experienced a tremendous growth, driven by globalization of financial flows and technological progress. Thus, besides transportation and tourism, new services sectors have emerged like software, insurance, finance and business services (see figure 1) showing unexpected growth rates during the last decade, 1995-2006: +23% of average annual growth rate for computer and information services, +14% for financial services.

Figure 1

World Trade in Services

(exports and imports average, billion US$)

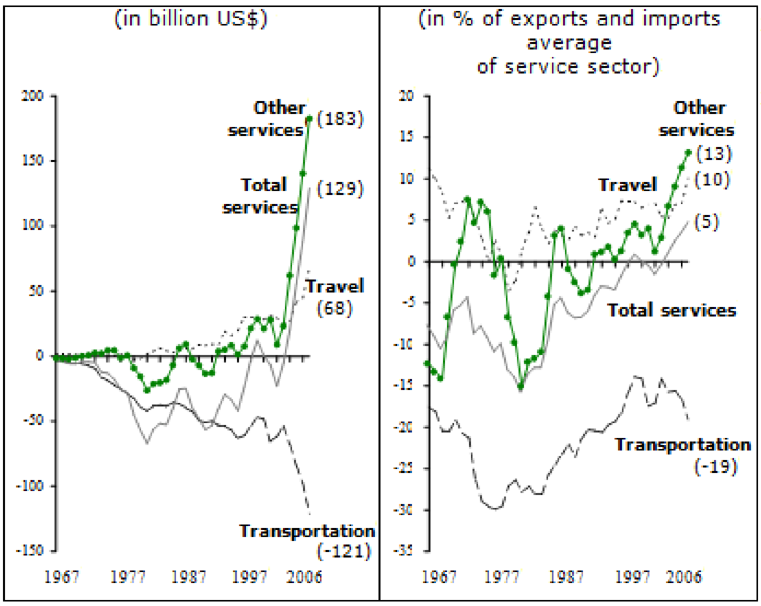


Source: CEPII, CHELEM-BOP database.

The immaterial nature of this specific trade makes flows uneasy to measure and leads to a real statistical challenge for countries and international organizations in finding new ways of collecting statistics (bank declarations, firm's surveys…). Thereby, available statistics show large discrepancies. Indeed, world trade is rather imbalanced: exports and imports data differ much from one another. The magnitude of the gap has considerably increased since the late nineties (see figure 2), because of the difficulty in properly recording e-transactions. The disequilibrium between credits (exports) and debits (imports) is 13% of the total trade in services. At a more detailed level, the discrepancies are even larger, particularly for the new incoming sectors: financial services (81%), computer and information services (77%) and insurance services (61%).

Figure 2

World Trade Imbalances in Services



Source: CEPII, CHELEM BOP Database.

CEPII is currently building a worldwide bilateral reconciled database on trade in services. Raw data come from diverse sources but mainly rely on balance of payments, collected by the IMF, Eurostat and OECD. Each database uses the same sectoral classification but proposes its own geographical breakdown. Eurostat and OECD offer bilateral data for a limited number of countries, whereas the IMF distributes almost all countries in a unilateral framework.

The dissection of raw data is the first step in constructing CEPII's database. The detailed analysis of differences is a crucial input to exhaustively describe world trade in services. Thus, the construction of CEPII's database relies on the allocation of the differences inside a database (between the aggregate and the fine level) but also between the databases. Several methods for balancing matrices already exist. The CEPII tests some of them and chooses the most appropriate one.

The second step in constructing the dataset is the reconciliation process itself. A large part of bilateral trade flow is reported twice, once by the exporter and once by the importer. Most of the time, these mirror flows have different value. The gap between the two values is often quite large and reaches billions of dollars. For example, in the Eurostat database, trade balance in total services between France and the USA in 2005 equals a surplus of € 2.199 million for France according to its statistics whereas USA also reports a surplus of € 1.600 million in their own favor. France, which is a net exporter of services to the USA in the first case, becomes a net importer in the second. These differences have, of course, numerous explanations (lag in declaring the data, definitions, quality of surveys, thresholds for bank's reporting…) but it appears that the gap between mirror flows is even larger at a fine level. Several methods already exist to solve this problem. Given its experience in reconciling mirror flows in trade in goods, the CEPII has started to build such a database.

Houssein Boumellassa & Deniz Ünal

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WORKING PAPERS

The Trade-Growth Nexus in the Developing Countries: a Quantile Regression Approach

N° 2009-04, March 2009

This paper investigates whether terms of trade have an impact on real exchange rates for commodity exporters and oil exporters. To this end, we estimate a long term relationship between the real effective exchange rate and economic fundamentals, including the commodity terms of trade. The estimation relies on panel cointegration techniques and covers annual data from 1980 to 2007. Our results show that real exchange rates co-move with commodity prices in the long run and respond to oil price somewhat less than to commodity prices. We also find that some pegged currencies have been driven away from their equilibria by wild fluctuations in the key currencies, on which they are anchored.

Gilles Dufrénot, Valérie Mignon & Charalambos Tsangarides

Price Convergence in the European Union: Within Firms or Composition of Firms?

N° 2009-03, March 2009

In this paper we use data on French export prices at the disaggregated firm and product level to evaluate the effect of economic integration on price convergence. We use the European integration 'experiment' and firm-level data on export prices to distinguish between two possible margins of adjustment: at the intensive margin economic integration induces different pricing strategies within the firm, whereas at the extensive margin it affects the composition of firms with different pricing strategies. In our sample, price convergence is 40 percent faster in the European Union than in an appropriately defined control group. 30 percent of this effect can be attributed to the fact that a higher share of firms with a low propensity to price discriminate serve European markets.

Isabelle Méjean & Cyrille Schwellnus

Labour Productivity: Are Diverging Trends Between Developed Countries Durable?

N° 2009-02, March 2009 (in french)

Between 1950 and 1973, a process of absolute convergence was at work between the technological leader, the USA, West European countries and Japan. The catching up process between developed countries gradually vanished between 1973 and 1995. On the one hand, we had a revival of US labour productivity growth while, on the other hand most, European countries and Japan have registered a steep decline in their productivity. This paper investigates the source of these diverging trends. First we use an econometric test developed by Bai and Perron in order to find and measure breaks in productivity trends over the long term. It appears that although technological change played an important role in the US revival between 1995 and 2001 it is the low increase in employment between 2001 and 2007 than explains the continuing rise in productivity. The technological factor does not contribute either to explain the growth rate decline in other developed countries. Even if they were lagging behind the US in investing in these new technologies they had considerably increased their efforts. One crucial element in explaining these diverging trends is the change in the labour content of growth both in the US where it is declining and in most European countries where it increases. This article uses various data bases in order to find out the time and frequency in productivity trend breaks both at the macro-economic level and at the sectoral level. The most up to date data for 2008 tend to confirm our diagnosis of divergence.

Clément Bosquet & Michel Fouquin

From Various Degrees of Trade to Various Degrees of Financial Integration: What do Interest Rates Have to Say?

N° 2009-01, January 2009

This paper proposes a systematic study of the degree of financial integration following the degree of trade integration according to Balassa's (1961) classification, from preferential trading area to complete economic integration. To this end, we exploit all the information contained in interest rates and rely on the expectations hypothesis of the term structure of interest rates and real interest rate parity. These two conditions are empirically investigated on various regional trade agreements, using cointegration techniques by paying a special attention to potential breaks. Our results show that customs unions, corresponding to step 3 of the Balassa's classification, seem to be a decisive threshold after which financial integration robustly takes place.

Adeline Bachellerie, Jérôme Héricourt & Valérie Mignon

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RECENT PUBLICATIONS

ECONOMIE INTERNATIONALE, QUARTERLY

Issue 115, 3rd Quarter 2008

Migration, International Trade, and Finance

Introduction
Xavier Chojnicki, Cécily Defoort & Vincent Dupont

Brain Drain, Remittances, and Fertility
Luca Marchiori, Patrice Pieretti & Benteng Zou

Diaspora Externalities and Technology Diffusion
Elisabetta Lodigiani

The Brain Drain Between Knowledge-Based Economies: the European Human Capital Outflow to the US
Ahmed Tritah

Learning-by-Exporting or Managerial Quality? Evidence from the Czech Republic
Branislav Saxa

Disaggregated Trade Flows and the "Missing Globalization Puzzle"
Siliverstovs Boriss & Dieter Schumacher

A Two-Sector Small Open Economy Model with Monopolistically Competitive non Traded Markets
Romain Restout

Currency Transaction Tax Elasticity: an Econometric Estimation
Francis Bismans & Olivier Damette

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LA LETTRE DU CEPII, QUARTERLY

Pensions in Italy: Work in Progress
N° 283, November 2008

Work on pensions has been in progress in Italy since 1992. The Italian pension system, essentially a public Pay-As-You-Go pension system, face up to a particularly marked ageing of the population. The Dini reform introduced a notional defined contribution system; the Berlusconi, then Prodi reforms pushed back the minimum retirement age. We present a general equilibrium analysis of the macroeconomic impact of the last two reforms and their effect on the viability of the pension system. Our simulations show that their effectiveness will only be temporary and important political decisions are still to be made.

Riccardo Magnani

FORTHCOMING

Quelle gouvernance mondiale après la crise ?

13th meeting of the Groupe d'analyses de la mondialisation

April 9, 2009

IXth Doctoral Meeting in International Trade and International Finance

Organized by the RIEF

April 23-24, 2009

Le Japon : conjoncture, prévisions et crise

Organized by the CEPII Business Club

April 28, 2009

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Organized by the CEPII Business Club around Georges Sokoloff 's new book: *La démesure russe: mille ans d'histoire* (Fayard)

April 30, 2009

Regional Economic Outlook: Europe &

Organized by the CEPII and the IFM around the release of the IMF report

May 12, 2009

The Crisis and Beyond for a Stronger, Cleaner, Fairer Economy

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Organized by CEPII for the release of its yearly publication

September 16, 2009

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Organized by GROUPAMA, CEPII and CIREM

October 22, 2009

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