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THE FRENCH CENTRE FOR RESEARCH  
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## *FOCUS*

### **Trading Sustainably: Opportunities and Challenges for Biofuel Policies**

Since the early 2000s, biofuel production and trade have grown up at a very fast pace. As a result of ambitious programs in OECD countries, biofuel output has increased fourfold, and trade in ethanol expanded from US\$ 1.7 billion in 2004 to US\$ 5.5 billion in 2008. This trend is expected to continue: in the United States, the Energy Independence and Security Act passed in 2007 set the objective of 36 billion gallons of biofuel for road transportation by 2022. In the European Union, the Directive on Promotion of the Use of Energy from Renewable Sources, finally adopted in April 2009, confirmed the 10% bioenergy share in the EU road transportation by 2020.

These policies have been decided based on several biofuels theoretical virtues: first, they alleviate the dependency on oil imports. Second, their production brings complementary revenues to farmers; and last but not least, biofuels have a lower environmental footprint than fossil fuels, since their use implies less greenhouse gas emissions.

But the rent sharing of this consumption mandate is a sensitive issue. The United States and the European Union will unlikely produce all their needs domestically, especially since first generation fuels (ethanol from corn, wheat, sugar crops and biodiesel from rapeseed, soy and palm oil) appear to be by far the main source of supply for the next decade. Domestic production is politically attractive, but alternative production pathways can be more affordable and more environmentally friendly in other parts of the world. For example, the production cost for sugar cane ethanol is one third cheaper in Brazil than in the United States, and palm oil yield is five times the rapeseed one.

Brazil has a great potential to meet a large share of developed economies' needs for ethanol. In spite of some market access restrictions, 8% of the ethanol consumed in the US, and 25% of that

consumed in the EU come from Latin America. Biodiesel trade is more liberalised, even though there may be occasional setbacks as in March 2008 when the European Commission imposed an anti-dumping tariff and countervailing duties on biodiesel originating from the US.

Recently, net CO<sub>2</sub> emission reductions have been questioned regarding some biofuel production processes (corn ethanol produced with coal-fired energy, for example) and differentiated reduction targets have been set in the US and the EU.

The debates have become even more complex with collateral effects related to the change in the use of land. The need for an expansion in arable land is expected to highly increase greenhouse gas emissions related to deforestation and conversion of idle land to cropland. Consequently, both the US Environmental Protection Agency and the European Commission have decided that these effects should be considered, measured, and addressed in the legislation in order to assess the eligibility of ethanol to be produced.

The CEPII, in a joint study with IFPRI, has made its own assessment of the indirect effects of biofuel production with a Computable General Equilibrium analysis using an extended version of the MIRAGE model. The study confirms that the impact of biofuel mandates on ethanol and biodiesel – besides the high cost of this policy – is harmful in the short run and that several decades of sustained biofuel production would be needed to repair the initial environmental damage of expanded cropping area. Additional studies, however, would be helpful to discern the exact effects of different crops grown in different regions.

Research on these topics is still at an infant stage, especially when it comes to indirect effects through land use change, which are still poorly understood. However, taking into account more precisely environmental impacts related to a production pathway (with direct and indirect effects) and enacting a legislation defining eligible goods on the domestic market is certainly an interesting shift. It will require strong input from science but, as long as it can resist protectionist temptations, it could help reshape, in a more sustainable way, the trade structure of numerous agricultural goods.

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## *ON THE RESEARCH AGENDA*

### **Immigration and Host Countries Income and Productivity: a Channel Accounting Approach**

The real impact of immigration on the host economy is still hotly debated. While there is a strong literature tradition to focus on the immigrants' impact on employment and wages of natives, this study aims at understanding the economy-wide impact of immigration.

We construct a new and unique dataset on migrant characteristics by age and education level in twenty OECD countries, decomposing total shares of migrants over natives by three age and two skill groups, by five-year intervals, in the period from 1960 to 2005, using individual country-year censuses and labor force surveys. Using these data, we study the impact of heterogeneous migration on income and labour productivity, as well as its main components: total factor

productivity, physical capital, human capital, and employment. We do this by combining level accounting approach with panel income regressions, and thus analyzing through which channels the migration impact is diffused.

The main findings are that, on average, immigrants have a positive impact on income and labour productivity in host countries, which works primarily through the TFP, and mostly in the long run. We show that this aggregate result can be explained by complementarities in age and education dimensions of immigrant relative to native population. There are also a few other channels, notably capital adjustment, through which the effect of immigration works.

Mariya Aleksynska & Ahmed Tritah

### **Currency Misalignments and Growth: a New Look using Nonlinear Panel Data Methods**

There has recently been a revival of interest in equilibrium exchange rates' assessment due to the current context of global imbalances. Indeed, since the end of the 1990s, the accelerating financial integration process accompanied with the preeminence of capital movements over trade in goods between countries, has engendered a growing disconnection between exchange rate fluctuations and the real economic activity. In order to assess long-run values of real exchange rates that would be consistent with the realization of a long-run stable macroeconomic equilibrium, various equilibrium exchange rate concepts have been developed, among which the Behavioral Equilibrium Exchange Rate (BEER).

Although numerous contributions have explored the links between exchange rate volatility or the choice of exchange rate regime and growth, the influence of long-run exchange rate misalignments on real economic activity remains an open question. Lasting misalignments may induce distortions in relative prices of traded-over-non traded goods that may be misinterpreted by economical agents and, as a consequence, may generate an insufficient resource allocation. In addition, the effects may be differentiated in case of an over- or undervaluation of currencies.

Our aim is to investigate the relationship between real exchange rate misalignments and economic growth, while paying special attention to potential asymmetric effects of over-and underevaluation. Our contribution is threefold. First, while most of the previous studies consider developing countries, we rely on a wider sample of countries, including both developed and developing economies. This is of particular importance in the current context of global imbalances, that calls for a consistent set of equilibrium exchange rates. Second, we conduct a detailed analysis to derive robust measures of currency misalignments by relying on the BEER methodology. In this sense, we go further than most of the existing literature investigating the link between currencies and economic growth based on PPP measures of exchange rate misalignments. Third, we specifically account for the sign (and the size) of the misalignment by estimating a panel nonlinear model. More specifically we rely on the estimation of a Panel Smooth Transition Regression (PSTR) model, allowing for a differentiated impact of currencies' overvaluations and under-valuations on economic growth.

Sophie Béreau, Antonia Lopez-Villavicencio & Valérie Mignon

### **On Selective Tariff Cuts for Environmentally Preferable Products**

The opportunity to concede selective tariff reductions for certain Environmentally Preferable Products is under discussion within current WTO negotiations on Environmental Goods and Services. The underlying arguments in favour of such a "green liberalization" are to combine traditional gains from trade with environmental benefits from cleaner production/consumption, and also to improve developing countries' exporting capacities in green products. Using a simple North-South trade, partial equilibrium model with two goods (a conventional variety produced with a polluting technology, and a green substitute produced with an environmentally preferable technology), we analyze the validity of these three arguments, and provide a comparison with a full liberalization scenario (unselective tariff reduction for both varieties).

We show that, if consumers in the importing country value the "green" product, selective tariff cuts result in lower pollution levels in both countries, due to substitution in consumption patterns. Although the comparison of welfare implications under a green- and a full-liberalization scenario is ambiguous, it is possible to show that selective tariff reductions result in an interesting distribution

of benefits among agents. However, simulations suggest that at the aggregated (country) level, neither a full nor a green liberalization is optimal, while it is possible to find Pareto-improving tariff reforms.

Estelle Gozlan & [Maria Priscilla Ramos](#)

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## *DATABASES*

### **Market Potentials Database**

The distribution of economic activities across countries is a subject of increasing interest in international economics. Empirically, economic geography is often described by indicators labelled “Market Potentials” or “Market Access”. The concept of Market Potentials goes back to Harris (1954). It states that a reliable proxy for the demand addressed to producers in a given location is the sum of expenditures in all locations, weighted by transport costs. Hence, Market Potentials combine in a single index the size of possible destination markets and trade frictions. New economic geography models (Fujita, Krugman and Venables, 1999) provide a solid theoretical background showing the impact of Market Potentials on countries and economic fortune.

Redding and Venable (2004) propose an original methodology to estimate such indicators of countries’ proximity to worldwide demand. They also show that market potentials have a strong influence on countries’ GDP per capita. Mayer (2008) provides evidence on the long-term impact of Market Potential on economic development. Besides, a large body of empirical work provides strong evidence that Market Potentials heavily determines multinational firms’ location choices (see for instance Head and Mayer, 2004).

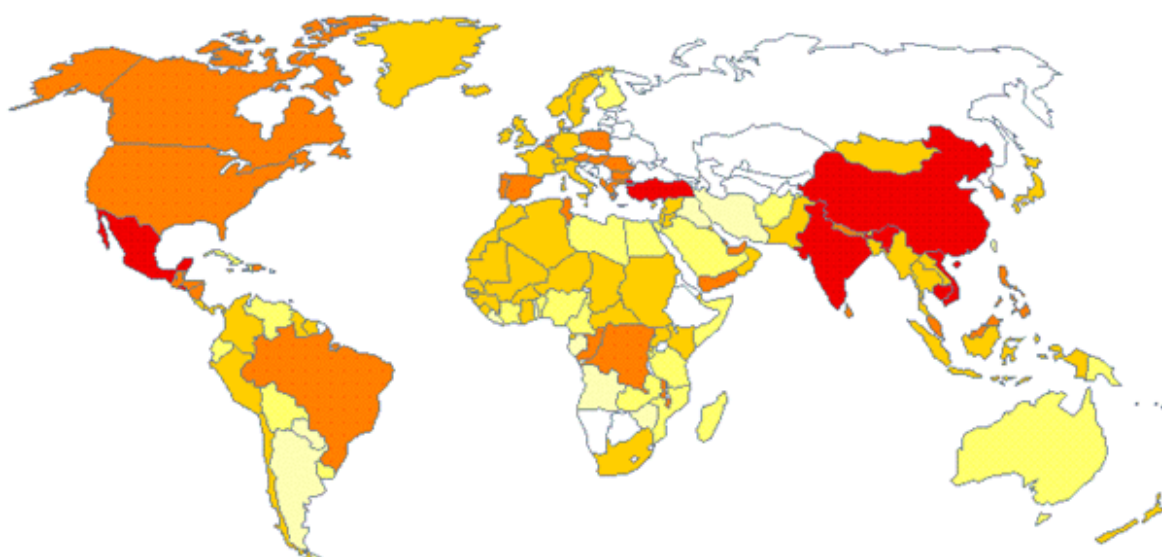
CEPII’s Market Potentials database provides indices synthesizing the evolution of countries’ economic geography. The database contains six distinct measures of Market Potential for a very large set of countries (between 152 and 205, depending of the year) and 44 years.

This database is a practical tool to describe and study the evolution of economic geography of the world. Maps 1 and 2 show two examples. They display the evolution of market potential hierarchy for textiles and Professional and Scientific equipment respectively. Values are normalized as deviations from the mean of each industry, and they are grouped in five classes ranging from big progress (intense red) to big decline (soft yellow). Due to data limitations, it is not possible to compute a market potential for a number of countries in 1980 (blank on the maps).

Map 1

#### **Market Potential Rank Evolution 1980-2003**

(Textiles, ISIC 321)

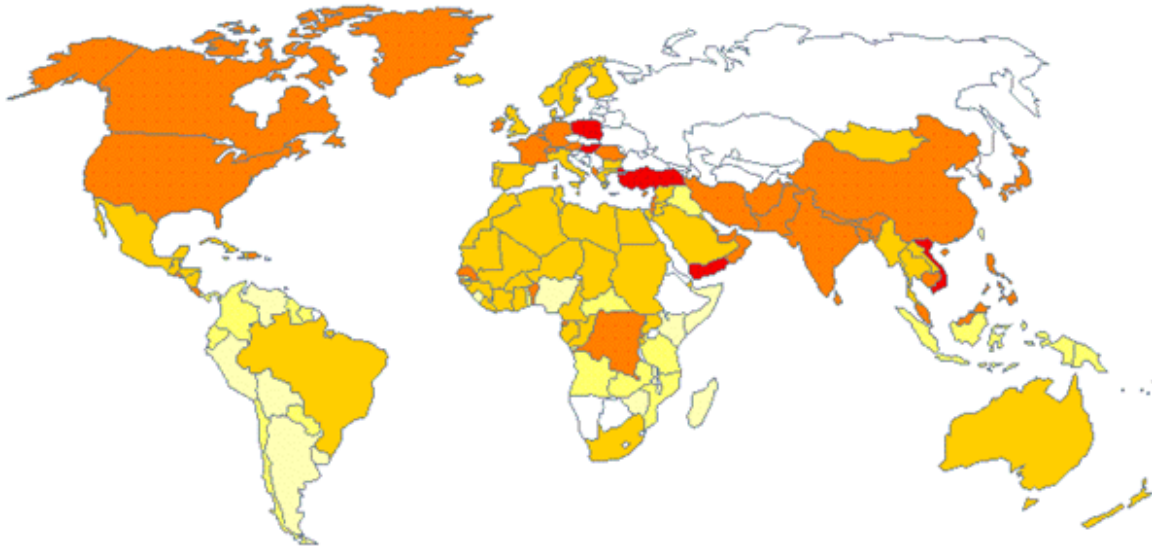


*Note:* Rank evolution is the change in gained or lost places in the market potential hierarchy, relative to the United States. Values are normalized as deviations from the mean across regions, and they are grouped in 5 classes. The middle group is comprised

between the mean +/- 0.5 standard deviation, and the next groups are delimited by 1 standard deviation. Blanks correspond to countries with no data.

For textile (Map 1), we notice a strong progression for China, Vietnam, Mexico, India and Turkey, and strong downfalls for Argentina, Iran, and Angola. A moderate progress is observed in some peripheral European countries (Spain, Portugal, Poland, Romania, etc), reflecting the proximity advantage, rather than low-wage competitiveness. Other countries avoid decline by virtue of their internal demand, like Brazil or the United States.

Map 2  
**Market Potential Rank Evolution 1980-2003**  
(Prof. & Scientific Equipment, ISIC 321)



Note: See Map 1.

Map 2 shows the rank evolution for the industry Professional & Science Equipment. Changes are much less pronounced than in Textiles, with Turkey, Vietnam and Poland gaining relatively important places in the world ranking. Ireland, China, India and other Asian countries exhibit moderate advances, and Latin American decline is noteworthy.

Thierry Mayer & Rodrigo Paillacar

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## WORKING PAPERS

### Quality Sorting and Trade: Firm-Level Evidence for French Wine

N° 2009-14, July 2009

Firm-level regressions show that Champagne producers that receive better ratings from wine guides also export to more markets, charge higher prices, and sell more on each market. Our

method corrects for a severe selection bias predicted by the model. By using direct measures of quality, we can recover estimates of parameters from a Méltz-based model of heterogeneous firms. We then regress averages of the quality, price, and quantity shipped to a country on measures of its attractiveness and entry costs. Champagne exhibits quality-sorting: more attractive markets tend to have lower average qualities and prices, but higher quantities.

Matthieu Crozet, Keith Head & Thierry Mayer

### **New Evidence on the Effectiveness of Europe's Fiscal Restrictions**

N° 2009-13, July 2009

This paper investigates the past effectiveness of the Maastricht Treaty (MT) and Stability and Growth Pact (SGP) in disciplining fiscal policy in the Euro zone. We estimate fiscal reaction functions for a panel of 11 members of the Euro zone including the more recent period of the reformed SGP, and compare them with fiscal responses from other "industrialized" OECD countries. Our main finding is that in contrast with the MT, the SGP has been ineffective in tackling excessive deficits in the Euro zone. Moreover, it has also not induced a countercyclical behavior of the fiscal authorities in the region. These results evince the need for reforms in Europe's fiscal restrictions in order to restore their credibility.

Marcos Poplawski Ribeiro

### **Remittances, Capital Flows and Financial Development during the Mass Migration Period, 1870-1913**

N° 2009-12, June 2009

This paper addresses the question whether the substantial financial flows received by emigration countries in the four decades running up to World War I contributed to domestic financial development in peripheral Europe. We quantify a sizable and significant relation between remittances and measures of development of the financial sector that is both larger than the contribution of other international capital flows and than the best estimates of the same relation in our days. Given that financial development is regularly included among the conditions for economic growth and catch up of developing nations, this paper adds to our understanding of the multiple impacts of the mass migration phenomenon on the economies of emigration countries.

Rui Esteves & David Khoudour-Castéras

### **Evolution of EU and its Member States' Competitiveness in International Trade**

N° 2009-11, June 2009

After a long period of domination by the industrialised countries of the North, international trade is today driven by the dynamism of developing countries. This work seeks to analyse how the EU is performing in the light of this emerging competitive threat, by comparing the EU's export performance on the world market with that of its key competitors between 1995 and 2004. The figures show that the EU has performed particularly well in the more upmarket, expensive and high tech levels of the market. Most notably, Europe is the market leader in up-market products, with almost 31% of the world market in 2004 (versus 20% of the market for all goods). In addition, there is evidence that the EU's recent enlargement has helped it to maintain a strong performance, thanks to an increasing division of labour within the region. The new member states have become important suppliers of intermediate goods to key EU producers, and in particular German firms, thus becoming increasingly vital to EU competitiveness.

Louise Curran & Soledad Zignago

### **Exchange-Rate Misalignments in Duopoly: the Case of Airbus and Boeing**

N° 2009-10, June 2009

We examine the effect of exchange-rate misalignments on competition in the market for large commercial aircraft. This market is a duopoly where players compete in dollar-denominated prices while one of them, Airbus, incurs costs mostly in euros. We construct and calibrate a simulation model to investigate how companies adjust their prices to deal with the effects of a temporary

misalignment, and how this affects profit margins and volumes. We also explore the effects on the long-run dynamics of competition. We conclude that, due to the duopolistic nature of the aircraft market, Airbus will pass only a small part of the exchange-rate fluctuations on to customers through higher prices. Moreover, due to features specific to the aircraft industry, such as customer switching costs and learning-by-doing, even a temporary departure of the exchange rate from its long-run equilibrium level may have permanent effects on the industry.

Agnès Bénassy-Quéré, Lionel Fontagné & Horst Raff

### **Market Positioning of Varieties in World Trade: is Latin America Losing Out on Asia?**

N° 2009-09, April 2009

There is increasing empirical evidence that trade specialisation and competition takes place in varieties rather than in products or industries. This paper examines recent changes in the export specialisation of Latin America and the Caribbean (LAC) and their Asian competitors by looking at their vertical specialisation through prices. Three price (or quality) segments are distinguished to compare export performance between the two regions using BACI database, which provides harmonised bilateral unit values for most countries in the world at the most disaggregated product-level (5,000 products) for the period 1995 to 2004. The technology-content of products is also taken into account. The evidence suggests that LAC is losing out on China which is gaining large market shares, notably in the low-quality segment and low-tech segment. However, LAC has retained its initial overall market share, by slightly upgrading the quality and technology content of its exports. Our estimates of similarities in export structures confirm that varieties exported by the two continents are very different. Moreover, LAC export prices are much higher than those of China, but relatively similar to the ones of other Asian nations. Finally, we analyse the determinants of unit values of Latin American and Asian exports. Econometric tests confirm that the type of global competition differs between the two regions: prices play a bigger role in the case of Asian exports, whereas Latin America competes more on quality in world markets.

Nanno Mulder, Rodrigo Paillacar & Soledad Zignago

### **The Dollar in the Turmoil**

N° 2009-08, April 2009

We study the impact of the global financial crisis on the equilibrium exchange rate of the US dollar. We first simulate the impact of the crisis on the US net foreign asset position. Then, we calculate the equilibrium value of the dollar according both to a BEER and to a FEER approach. We find the case for a strong, although temporary, depreciation of the dollar even more acute than before the crisis. This suggests that the strength of the dollar in late 2008 and early 2009 may be short-lived.

Agnès Bénassy-Quéré, Sophie Béreau & Valérie Mignon

### **Term of Trade Shocks in a Monetary Union: an Application to West-Africa**

N° 2009-07, April 2009

We propose a two-country DSGE model of the Dutch disease in a monetary union, calibrated on Nigeria and WAEMU. Three monetary regimes are successively studied at the union level: a flexible exchange rate with constant money supply, a flexible exchange rate with an accommodating monetary policy, and a fixed exchange rate regime. We find that, in the face of oil shocks, the most stabilizing regime for Nigeria is a fixed money supply whereas it is a fixed exchange rate for WAEMU. However, the introduction of an oil stabilization fund can reduce the disagreement on the common policy rule. Furthermore, the two zones may agree on a fixed money-supply rule in the face of both oil and agricultural price shocks.

Loïc Batté, Agnès Bénassy-Quéré, Benjamin Carton & Gilles Dufrénot

### **Macroeconomic Consequences of Global Endogenous Migration: a General Equilibrium Analysis**

N° 2009-06, April 2009

In this paper, we analyze the demographic and economic consequences of endogenous migrations flows over the coming decades in a multi-regions overlapping generations general equilibrium model (INGENUE 2) in which the world is divided in ten regions. Our analysis offers a global perspective on the consequences of international migration flows. The value-added of the INGENUE 2 model is that it enables us to analyze the effects of international migration on both the destination and the origin regions. A further innovation of our analysis is that international migration is treated as endogenous. In a first step, we estimate the determinants of migration in an econometric model. We show, in particular, that the income differential is one of the key variables explaining migration flows. In a second step, we endogenize migration flows in the INGENUE 2 model. In order to do so, we use the econometrically estimated relationships between demographic and income developments in the INGENUE model, which enables us to project long-run migration flows and to improve on projections of purely demographic models.

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

### **Equivalence Between Taxation and Tradable Emission Permits (in French)**

N° 2009-05, March 2009

The paper deals with the equivalence between taxation and emission permits according to different viewpoints: the first one sets prices, the second one quantities. But equivalence is more formal than substantial: taxation is the generating fact, the market of permits does not exist spontaneously. Its price is unstable because supply is not independent from demand. It is manipulatable either ex ante when free allowances are allocated or ex post during the period of compliance through Walrasian tatonnement.

Pierre Villa

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## ***RECENT PUBLICATIONS***

### **ECONOMIE INTERNATIONALE**, QUARTERLY

Issue 116, 4rd Quarter 2008

#### **Openness and Economic Growth: a Comparative Study of Alternative Trading Regimes**

Rosa Capolupo & Giuseppe Celi

#### **Foreign Aid Inflows and the Real Exchange Rate in the CFA Franc Zone**

Bazoumana Ouattara & Eric Strobl

#### **China's Exchange Rate Policy and Asian Trade**

Alicia Garcia-Herrero & Tuuli Koivu

#### **The EU Emissions Trading Scheme: the Effects of Industrial Production and CO2 Emissions on Carbon Prices**

Emilie Alberola, Julien Chevallier & Benoît Chèze

#### **The Turkish Experience in Inflation Targeting: Uncertainties and the Efficiency of Monetary Policy**

Yesim Gürbüz, Thomas Jobert & Ruhi Tuncer

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*Economie internationale/International Economics* publishes papers dealing with a wide range of issues in applied international economics. Papers cover topics like macroeconomics, money



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Articles should be not more than 25 pages (50,000 characters), including tables, figures, bibliography, and appendix. The first page of the manuscript should contain the following information: (i) title, (ii) name(s) and institutional affiliation(s) of the author(s), (iii) an abstract of not more than 100 words, (iv) the name, address, e-mail address, telephone and fax numbers of the corresponding author. Moreover, at least one classification code according to the Classification System for Journal Articles as used by the Journal of Economic Literature and up to three keywords should be supplied.

Papers should be submitted electronically to Véronique Le Rolland: [veronique.lerolland@international-economics.eu](mailto:veronique.lerolland@international-economics.eu)  
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## *LA LETTRE DU CEPII*, QUARTERLY

### **Bad Weather for the Stability and Growth Pact**

N° 286, 2 April 2009

Everywhere in the world, the need for fiscal stimulus has caused a severe deterioration of fiscal balances and raised the unavoidable question of debt sustainability. In the Euro area, the recent initiation of Excessive Deficit procedures by the European Commission against the countries with high deficits has heated this debate. Still, the Euro area needs a credible scheme of budgetary discipline that would allow fiscal authorities to reassure sovereign debt markets and to dissipate the reticence of the ECB in adopting a policy of quantitative easing. That would also facilitate the implementation of fiscal stimulus packages, which could open an exit away from the crisis. Such a scheme should be designed to enforce more discipline, but also more counter-cyclical fiscal policies.

Agnès Bénassy-Quéré & Marcos Poplawski Ribeiro

### **Terms of Trade and Exchange Rates: a Relationship Complicated by Anchor Policies**

N° 285, 11 March 2009

The terms of trade of commodity-exporting countries are directly affected by the large-scale swings of worldwide prices. These terms of trade represent one of the key determinants of the real exchange rates of these economies. By estimating long-term equilibrium exchange rates we can gauge their impact for oil exporters and for exporters of other commodities. We then evaluate currency 'misalignments' as the discrepancies between the observed real exchange rates and their equilibrium values. Can these misalignments themselves be explained? In countries whose currencies are anchored to the dollar or to the euro, the misalignments are shown to depend on the behaviour of the anchor currency. When the anchor currency appreciates, the anchored currencies tend to be overvalued; when it depreciates, their undervaluation is likely.

Virginie Coudert, Cécile Couharde & Valérie Mignon

### **Euro: as Expected, Gains and Costs**

N° 284, December 2008

Ten years ago, eleven European countries, since joined by five others, gave up their national currencies to create the euro. This anniversary is the occasion to evaluate whether the promises regarding the euro were kept. Various studies undertaken on French exports indicate that the

single currency indeed produced the expected microeconomic benefits of a reduction in the transaction costs and greater price transparency. However, the single currency policy has led to strong divergences of real interest rates between countries, whose effects have not been corrected for lack of suitable macroeconomic co-operation. Ten years after the creation of the euro, the bursting of the real estate bubble in certain countries of the zone and the consequences of the financial crisis point to the necessity of strongly counter cyclical macroeconomic policies in the monetary union.

Agnès Bénassy-Quéré, Antoine Berthou & Lionel Fontagné

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## FORTHCOMING

### **International Cooperation in Times of Global Crisis: Views from G20 Countries**

Organized by ICRIER, Bruegel and CEPII

New Delhi, September 14-15, 2009

### **L'économie mondiale 2010**

Organized by CEPII for the release of its yearly publication

Paris, September 16, 2009

### **Nationalisme économique : le retour ?**

Organized by IFRI and The CEPII's Business Club

Paris, September 30, 2009

### **L'avenir des politiques budgétaires et des marchés obligataires européens**

Organized by GROUPAMA, CEPII and CIREM

Paris, October 22, 2009

### **Seventh ELSNIT Annual Conference on Trade and Regional Disparities**

Kiel, October 23-24, 2009

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