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CONTENTS:

FOCUS

The Economic Impact of Immigration for Aging Countries

Western Europe has long been a point of departure towards the new world, but it has now become a region of net immigration, notably due to its level of development and wealth. Nonetheless, although immigration was considered as a resource until the first oil shock, questions about the benefits of this phenomenon surfaced at the end of the post-war economic boom, marked by the appearance of mass unemployment.

Regarding the labor market, the local adjustments by workers and firms lead to an almost imperceptible impact on the scale of the country receiving the immigration flow, even though redistributive effects are clearly manifest. Thus, the consequences are microeconomic. Some natives find themselves in competition with an external work force and thus lose employment opportunities, while others benefit from reduced labor costs as a consequence of the arrival of new potential workers and firm creation produced by a local rise in the consumer population. Once aggregated, these effects compensate for each other almost exactly, leaving no visible effect of immigration on the macroeconomic landscape.

The consequences of immigration likewise deserve to be considered at the level of national budgets equilibrium. The existence of generous welfare systems in Western Europe, intended to mitigate certain imbalances in the labor market (e.g., unemployment, exclusion, insufficient income for access to housing or health care) or to direct family policy, may exert an attractive force on populations living in the poorest regions. The impact of immigration on public finances is a controversial issue that has given rise to a vast literature, particularly in the United States.

One of the conclusions of these studies is that the impact of immigration on welfare systems is limited. For example, in France, immigrants tend to be younger than natives and the difference in the age distribution of both populations leads to a higher net average contribution to the public budget. In this context, immigration appears as an important variable both through its direct effects on public finances and as an instrument of policy seeking to reduce the aging process.

In the French case, the old age dependency ratio (population aged 65 and over related to the population aged 16-64) is projected to increase from around 25% in 2000 to nearly 45% in 2050. With a welfare system essentially based on upward redistribution (from young to old), this aging population will mechanically result in financing needs of social security that could reach 3 points of GDP by 2050 (and remain constant until 2100). Immigration, as projected in official forecasts, reduces the tax burden of an aging population. Without migration, the financing needs of social protection at the end of the century would increase from 3% to about 5% of GDP. These benefits are mainly explained by the age structure of net flows, younger than the French population as a whole, and mostly affect unsurprisingly the two pillars of social protection the most sensitive to demographic changes: pensions and health.

For similar reasons, a more ambitious migration policy (corresponding to a doubling of net inflows) would contribute to reducing the tax burden of an aging population. But the financial gains are relatively moderate in comparison to the demographic changes they imply: a burden reduction between 20% and 30% depending on the selectivity degree is combined with an increase in the working age population between 16% and 20% and an immigrant share that will double by the end of the century. A more selective policy (in favor of skilled workers) can amplify these gains in the short-medium term but in relatively low proportions. However, this improvement is only temporary. In the long term, demographic changes of a more selective immigration policy (skilled migrants have lower fertility rates and a longer life expectancy) outweigh its positive effects compared to a non-selective policy.

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More Bankers, More Growth? Evidence from OECD Countries

Does finance spur economic growth? At the end of the 1990s, this debate seemed definitively closed: an abundant empirical literature supported a causal and positive effect of finance on GDP. However, the recent crisis has altered the mindset on this issue. In particular, there have been intense debates on the size of the financial industry, regarded by some as excessive. One of the problems in the literature on the finance-growth nexus is that financial development is typically measured by the size of the financial market which might be misleading: an increase of credit volume for instance does not mean that the financial sector completes its functions better. Sometimes, this is even just the opposite: an excessive growth of credit may undermine the financial system and hurt economic growth. The subprime mortgage crisis is a good example of such an unproductive financial deepening.

We argue that financial deepening should not only be assessed with familiar measures of financial activities outputs (e.g. credit volume), but also through its inputs (e.g. number of employees) or the efficiency of the financial intermediation process (measured by the ratio number of employees/credit volume). Overall, our study supports the absence of a positive relationship between financial deepening and economic growth for OECD countries over the last forty years.

Gunther Capelle-Blancard & Claire Labonne

Who Carries the Burden of Bank Taxation?

In the wake of the crisis, a number of proposals were put forward to impose a levy on financial institutions. Some proponents argue that the sole purpose of such a tax is to recover the costs of direct fiscal support. Others argue that the bank levy could be designed as a “Pigouvian” tax both helping to raise revenues and serving as a macro-prudential tool to motivate banks to undertake less risky activities. In light of these proposals, we propose to study the impact of bank taxation on the cost of financial intermediation and, hence, cost of capital for firms. Despite the importance of this issue, there is little available evidence. The notable exception is the paper by Demirguc-Kunt and Huizinga (2001) that analyzes bank level data for 80 countries from 1988 to 1995.

We propose to investigate whether the burden of taxation is passed through by banks to their customers, relying on a sample of 27 EU countries from 1996 to 2009. The data for estimations is drawn from the BankScope database that provides balance sheets and income statements of individual banks. Our initial results confirm previous findings that bank taxation partly falls on bank customers by increasing the wedge between interest rates on loans and deposits. However, taxation is responsible for only 6% of this wedge, much less than the structure of liabilities, market power and cost-efficiency. We next proceed to investigate a potential heterogeneity between banks in the pass-through depending on the market structure (Herfindahl index, market share and bank size) and competition (Panzar and Rosse h-statistic, Lerner index).

Gunther Capelle-Blancard, Olena Havrylchyk & Claire Labonne

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Immigration, Unemployment and Growth in the Host Country: Panel Granger Causality Analysis for OECD Countries

During the last decades, most OECD countries experienced an increase in international migration.

Economists have studied the impact of immigration on a variety of host country outcomes and also how economic conditions in the receiving countries affect migration flows.

This paper contributes to the existing literature on immigration by investigating the causality relationship between immigration and host country economic conditions (unemployment and growth) using the panel Granger causality testing approach, that is based on SUR systems and Wald tests with country specific bootstrap critical values. This approach allows testing for Granger causality on each individual panel member separately by taking into account the possible contemporaneous correlation across countries.

Using annual data over the period 1980-2005 for 22 OECD countries which are the major migrants-recipients countries, our study provides evidence that the interaction between immigration and host economic activity depends on the host country. Our findings suggest that, only in Portugal does unemployment negatively Granger cause immigration inflow. In four countries (France, Iceland, Norway and United Kingdom) economic growth positively Granger causes the immigration inflow.

Ekrame Boubtane, Dramane Coulibaly & Christophe Rault

DATABASES

Export Sophistication Measures

One of the many aspects of China's trade integration that have puzzled the economists is the rapid upgrading of China's exports: since the mid-Nineties the range of China's export products, impressively expanded. In particular, Chinese producers have been able to export capital- and skill-intensive products, high-technology products, and products that are usually considered as belonging to the area of specialization of more developed countries. How does this export upgrading contribute to the Chinese growth?

In order to quantify the export sophistication of Chinese regions and to identify their capacity to grasp growth benefits through the reshaping of the structure of production beyond the boundaries established by factor endowments, CEPII's researchers have computed yearly indicators of Chinese localities' export sophistication and linked them to economic growth.[1]

They use the Hausmann, Hwang and Rodrik (2007)[2]'s measure of the sophistication of a country's export basket, resulting from the comparison to the income level of countries with similar export structures. In this indicator, each good k that a country can potentially produce and export has an intrinsic level of sophistication, (PRODYk). This level is the weighted average of the income levels of good k 's exporters. The weights correspond to the revealed comparative advantage of each country j in good k. The sophistication level of country j's exports, denoted by EXPYj, is then computed as the average level of sophistication of its export basket.

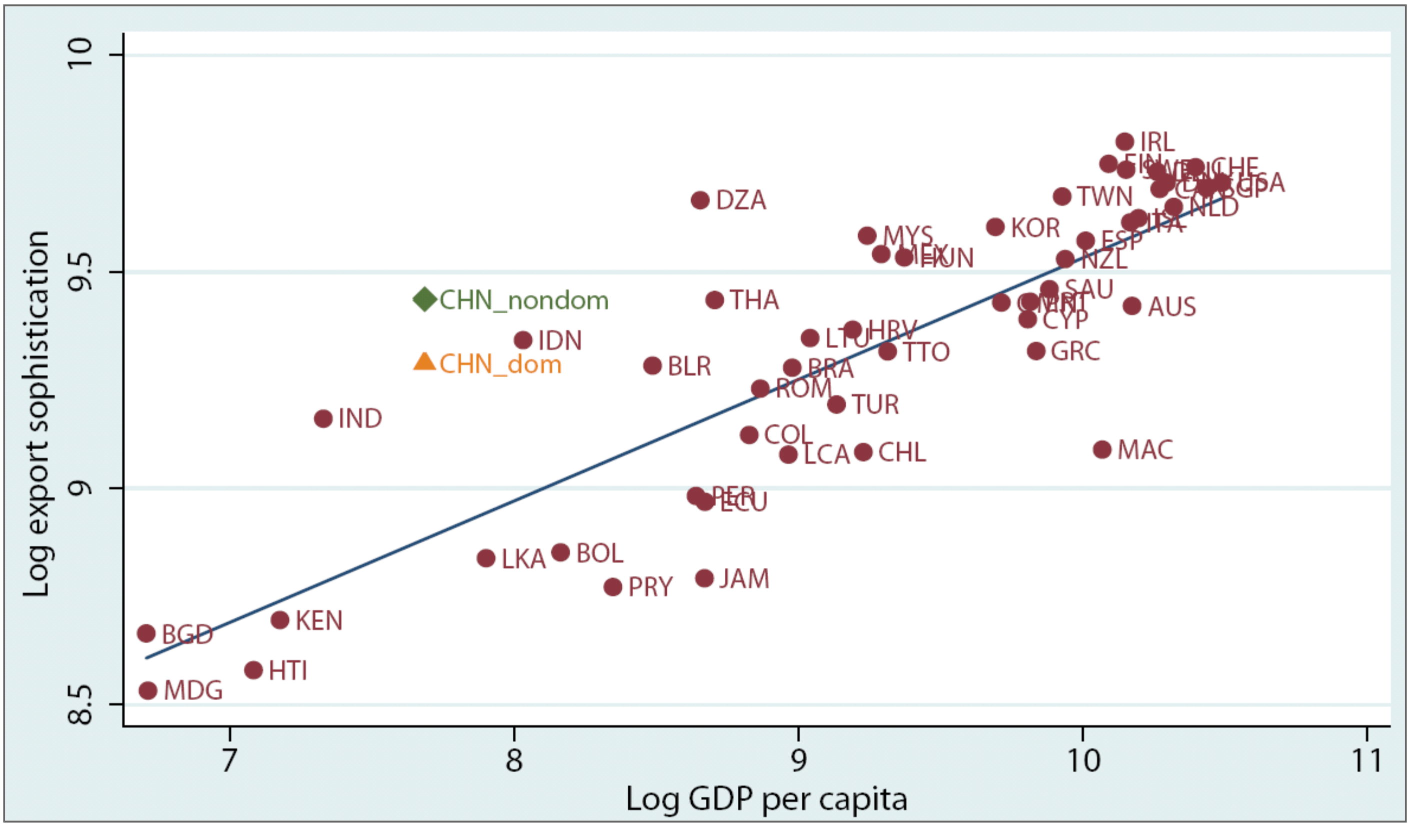
Measures of product-level sophistication PRODY for 1997 were developed using the BACI world trade dataset,[3] and EXPY indexes were constructed for the export baskets of Chinese localities (provinces and prefectures) based on Chinese customs data, which report region-level exports and imports by 6-digit product over the 1997-2007 period. One feature of interest in this dataset is that it allows us to differentiate between domestic and foreign trading firms, and between processing trade and ordinary trade.

The following scatterplot of EXPY against per-capita GDP indicates, in line with previous findings by Rodrik (2006)[4] that rich (poor) countries export products that tend to be exported by other rich (poor) countries. China is an 'outlier' in this relationship, in terms of both the product bundles exported by domestic and foreign firms. In 1997, the export bundle of domestic firms was as sophisticated (10800$) as that of Belarus, a country 2.5 times richer than China in PPP per capita terms; that of foreign firms was higher, at 12500$, similar to that of Portugal, a country eight times richer than China in PPP per capita terms in 1997. The per capita income level associated with exports by domestic entities increased by 15.5% between 1997 and 2007 to reach a figure of 12,500$, similar to that in Lithuania, a country which is three times richer than China in PPP per capita terms. This figure remains however lower than that of foreign entities, which rose by 25.7% over the period to reach 15,776$, a figure similar to that in the UK, a country seven times richer than China in PPP per capita terms.

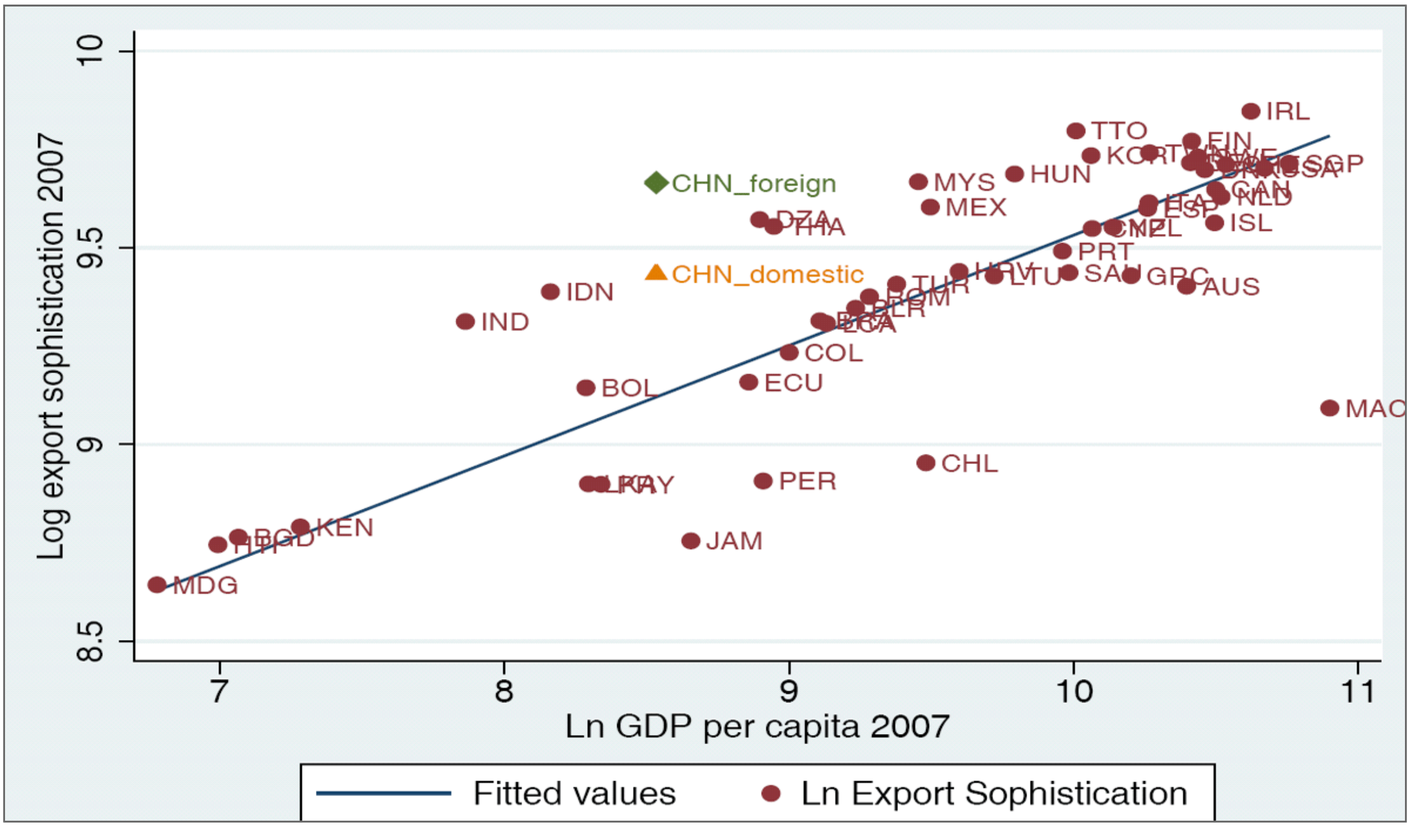
Figure 1: The relationship between per-capita PPP GDP and EXPY

(in logs)

1997



2007

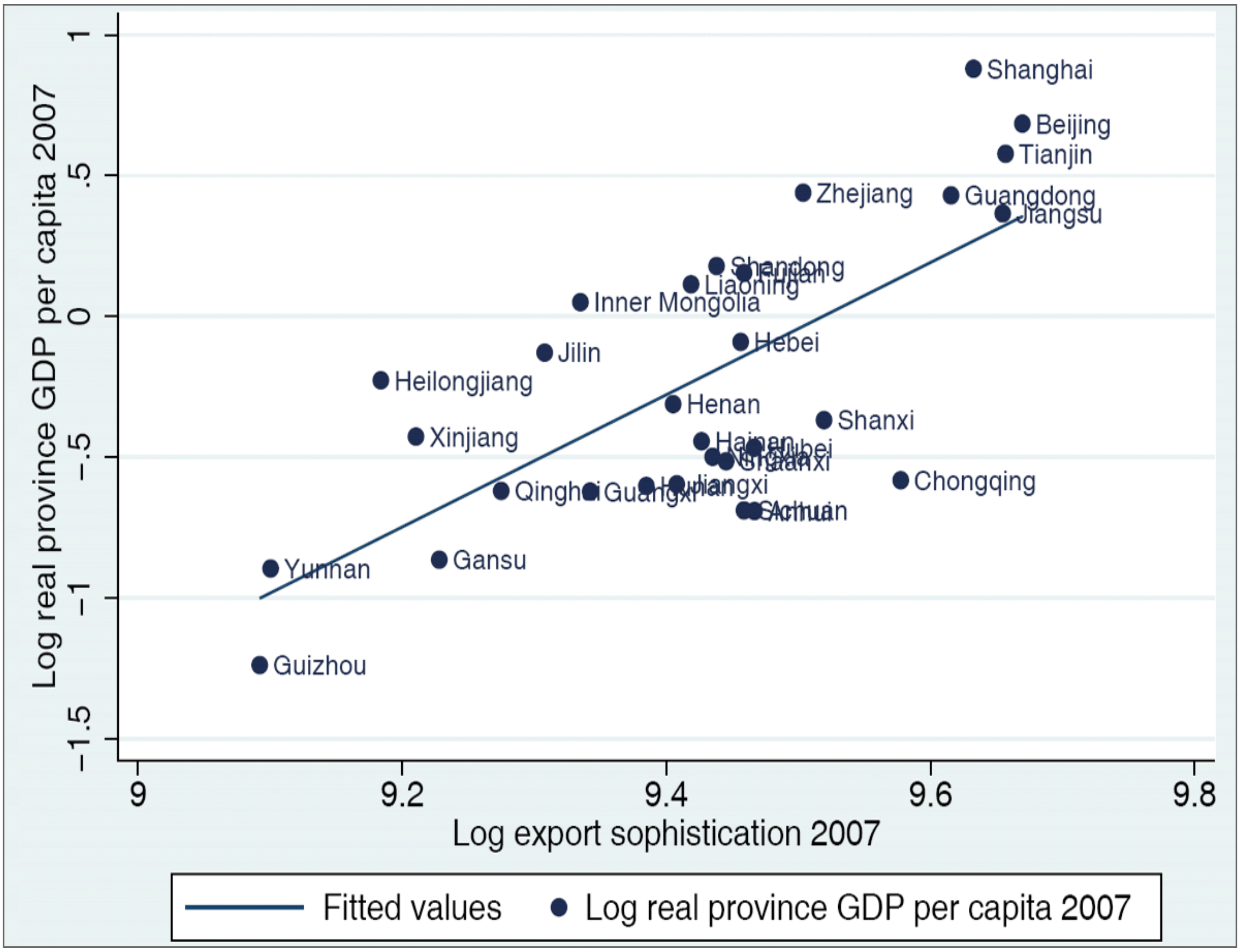


Source: Authors' computations based on BACI and WDI data.

Considering the evolution of China's sophistication over time, distinguishing between domestic and foreign firms, the recent upgrading of China's exports is not confined to foreign entities (which typically operate in processing trade), but also concerns domestic producers. The export sophistication of both types of exporters has risen rapidly. The income level associated with exports by domestic entities increased by 15.5% between 1997 and 2007. Over the same period that of foreign entities however rose even faster, by 25.7%, so that the gap between domestic and foreign export sophistication doubled from 1720$ to 3266$. A similar message comes from the consideration of the share of high-tech products in exports as a measure of export sophistication.

Figure 2 shows the relationship between real income per capita (in constant 2000 dollars) and export sophistication across provinces in 2007. The correlation between these two variables in our sample of 30 provinces is positive, with a figure of 0.70.

Figure 2: Export sophistication and real GDP per capita, 2007



Source: Authors' computations based on Chinese customs and China Statistical Yearbooks data.

Empirical results based on econometric evaluations of growth regressions relating variation in export sophistication and growth across China show that the gains in growth only occur when the improved technology is developed by domestic-owned firms and embedded in ordinary trade. This suggests that the different sources (export regime and firm type) of Chinese upgrading export must be identified for the true measurement of the improvement in technology and its implications for economic growth.

Sandra Poncet

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WORKING PAPERS

Does Importing more Inputs Raise Exports? Firm Level Evidence from France

N° 2011-15, June 2011

Why would an increase in imported inputs rise exports? We argue that importing more varieties of intermediate inputs increases firm's productivity and thereby makes the firm able to overcome the export fixed costs. Whereas the literature evidences the positive effect of an increase in imported inputs on firms' productivity and shows that only the most productive firms export, the link between imported intermediate inputs and export scope has not been made. This paper bridges the gap by studying the impact of imported inputs on the margins of exports. We use a firms' level database of imports at the product (HS6) level provided by French Customs for the 1995-2005 period. Access to new varieties of inputs may increase productivity, and thereby exports, through better complementarity of inputs and transfer of technology. We test for these different mechanisms by distinguishing the origin of imports (developing vs. developed countries). We find a significant impact of higher diversification and increased number of imported inputs varieties on firm's TFP and export scope. Both the complementarity and transfer of technology mechanisms seem to matter.

Maria Bas & Vanessa Strauss-Kahn

Joint Estimates of Automatic and Discretionary Fiscal Policy: the OECD 1981-2003

N° 2011-14, May 2011

Official calculations of automatic stabilizers are seriously flawed since they rest on the assumption that the only element of social spending that reacts automatically to the cycle is unemployment compensation. This puts into question many estimates of discretionary fiscal policy. In response, we propose a simultaneous estimate of automatic and discretionary fiscal policy. This leads us, quite naturally, to a tripartite decomposition of the budget balance between revenues, social spending and other spending as a bare minimum. Our headline results for a panel of 20 OECD countries in 1981-2003 are .59 automatic stabilization in percentage-points of primary surplus balances. All of this stabilization remains following discretionary responses during contractions, but arguably only about 3/5 of it remains so in expansions while discretionary behavior cancels the rest. We pay a lot of attention to the impact of the Maastricht Treaty and the SGP on the EU members of our sample and to real time data.

Julia Darby & Jacques Melitz

Migration: Burden or Benefit from Welfare State Financing

N° 2011-13, Mai 2011 (in french)

Immigration is often perceived as an instrument of adaptation for aging countries. In this paper, we evaluate, using a dynamic general equilibrium model, the contribution of migration policy in reducing the tax burden associated with the aging population in France. Four variants, compared to a baseline scenario based on official projections for France (INSEE, COR, etc.), are simulated with the aim to quantify the immigration effects on the French social protection finances. The first variant assesses the economic effects of immigration in France as projected into official forecasts. The three other variants are built on the same more ambitious annual quantitative flows of immigrants (corresponding to net inflows that have characterized the second great wave of immigration in France in the twentieth century). These three variants only distinguish in terms of the skill structure of new migrants. We show that the age and skill structure of immigrants is the key feature that mainly determines the effects on social protection finances. Overall, these effects are all the more positive in the short-medium term that the migration policy is selective (in favor of more skilled workers). In the long term, beneficial effects of a selective policy may disappear. But the financial gains from more consequent migration flows are relatively moderated in comparison of demographic changes it implies.

Xavier Chojnicki & Lionel Ragot

The Performance of Socially Responsible Funds: Does the Screening Process Matter?

N° 2011-12, May 2011

This paper is about the financial performance of mutual funds that practice Socially Responsible Investing (SRI). First, we measure the financial performance of a sample of 116 French SRI mutual funds over the period 2004-2007. As expected, and according to previous studies, our results show that SRI funds do not outperform the market, whatever the performance measure considered. Then, we assess the financial performances within our sample of SRI funds, as suggested by Barnett and Salomon (2006). Precisely, we examine whether the financial performances of these funds are related to the features of the SRI selection process. We find evidence that a greater screening intensity reduces SRI financial performance, but the relationship runs in the opposite direction when screening gets tougher. Further, we show that only sectoral screens – such as avoiding "sin" stocks – decrease financial performance, while transversal screens – commitment to UN Global Compact Principles, ILO/Rights at Work, etc. – have no impact. Other characteristics of the screening process like shareholder activism, or the overall quality of the SRI process do not have any significant impact either.

Gunther Capelle-Blancard & Stéphanie Monjon

Market Size, Competition, and the Product Mix of Exporters

N° 2011-11, May 2011

We build a theoretical model of multi-product firms that highlights how market size and geography (the market sizes of and bilateral economic distances to trading partners) affect both a firm's exported product range and its exported product mix across market destinations (the distribution of sales across products for a given product range). We show how tougher competition in an export market induces a firm to skew its export sales towards its best performing products. We find very strong confirmation of this competitive effect for French exporters across export market destinations. Trade models based on exogenous markups cannot explain this strong significant link between destination market characteristics and the within-firm skewness of export sales (after controlling for bilateral trade costs). Theoretically, this within firm change in product mix driven by the trading environment has important repercussions on firm productivity and how it responds to changes in that trading environment.

Thierry Mayer, Marc Melitz & Gianmarco Ottaviano

The Trade Unit Values Database

N° 2011-10, April 2011

Trade unit values are commonly used as proxies for trade prices in empirical research in international economics. Existing datasets providing international trade unit values for a large number of countries typically suffer from a number of statistical biases, due to the aggregation of unit values and the harmonization of quantity information. These biases reduce the reliability of unit values as a proxy for trade prices. This paper presents the Trade Unit Values dataset, a new database developed to circumvent these statistical issues. Bilateral trade unit values are computed at a very high level of disaggregation before aggregation into Harmonized-System 6-digits categories to allow for cross-country comparability. Our processing strategy improves the differentiation of trade prices within product categories, as compared to existing worldwide datasets. A simple econometric analysis shows that unit values in our database are well explained by economic aggregates.

Antoine Berthou & Charlotte Emlinger

Carbon Price Drivers: Phase I Versus Phase II Equilibrium?
N° 2011-09, April 2011

The aim of this paper is to investigate the determinants of the carbon price during the two phases of the European Union Emission Trading Scheme (EU ETS). More specifically, relying on daily EU allowance futures contracts, we test whether the carbon price drivers identified for Phase I still hold for Phase II and evolve toward a long-run relationship. Using cointegration techniques and accounting for the 2006 structural break on the carbon market, we show that while a cointegrating relationship exists for both phases of the EU ETS, the nature of this equilibrium relationship is different across the two subperiods, with an increasing role of fundamentals in Phase II. Deriving equilibrium values, we show that the carbon price tends to be undervalued since the end of 2009.

Anna Creti, Pierre-André Jouvet & Valérie Mignon

Rebalancing Growth in China: An International Perspective
N° 2011-08, April 2011

Based on simulations of an original DGE model of the US, Chinese and Euro area economies with financial frictions and various monetary regimes, the paper shows that the contribution of China in global rebalancing should primarily rely on structural policies aiming at reducing aggregate savings in China. The role of the exchange-rate regime would be minor under standard monetary policies, although more important if monetary policies in advanced countries are constrained, as they are today. Finally, relying only on a change in China’s monetary regime (without structural reforms) could end up in delaying rather than accelerating the rebalancing, depending on China’s policy regarding accumulated reserves.

Agnès Bénassy-Quéré, Benjamin Carton & Ludovic Gauvin

Economic Integration in the EuroMed: Current Status and Review of Studies
N° 2011-07, March 2011

This article draws a picture of the current status of the liberalization process in the Euro-Mediterranean region, and reviews existing studies of this process. Economic integration among the South-Med countries (SMCs) has started in the middle 1990s through intra-regional agreements (GAFTA, Agadir Agreement) and bilateral agreements with the EU. Econometric studies using gravity models generally found important trade creation effects for intra-regional trade, but smaller and asymmetric effects from EU-Med agreements, with an increase of export flows from the EU but no increase of flows in the other direction. Simulations with CGE models shows the main sources of gains (trade creation) and of losses (trade diversion, terms of trade) for SMCs. Studies also suggest that a dismantling of non-tariff barriers and of barriers in services trade could yield substantial gains for SMCs. A table with existing agreements and a picture of economic flows in the region can be found in the annex.

Joachim Jarreau

The Decision to Import Capital Goods in India: Firms' Financial Factors Matter
N° 2011-06, March 2011

Are financial constraints preventing firms from importing capital goods? Sourcing capital goods from foreign countries is costly and requires internal or external financial resources. A simple model of foreign technology adoption shows that credit constraints act as a barrier to importing capital goods under imperfect financial markets. In our study, we investigate this prediction using detailed balance-sheet data from a sample of about 5,500 Indian manufacturing firms per year, having reported information on financial statements and imports by type of good over the period 1996-2006. Our empirical findings shed new light on the micro determinants of firms’ choice to import capital goods. Baseline estimation results show that firms with a lower leverage and higher liquidity are more likely to source their capital goods from foreign countries. Quantitatively, an improvement of the liquidity or leverage ratio by 10% increases the probability of importing capital goods by 3% to 5% respectively, independently of productivity. These findings are robust to alternative measures of foreign technology. The effect of leverage is also robust with respect to specifications dealing directly with reverse causality.

Maria Bas & Antoine Berthou

FDI from the South: the Role of Institutional Distance and Natural Resources

N° 2011-05, March 2011

This study explores location choices for investors stemming from emerging economies (often referred to as the South), with a particular emphasis on institutions and natural resources. Relying on a novel dataset of bilateral FDI flows between 1996 and 2007, we demonstrate that FDI from the South has a more regional aspect than investment stemming from the North. Institutional distance has an asymmetric effect on FDI depending on whether investors choose countries with better or worse institutions. In the latter case, a large institutional distance between source and destination countries discourages FDI inflows, but the growing attractiveness of the primary sector outweighs this deterring effect for emerging investors. We also attest to the complementary relationship between capital flows from the North and South in developing recipient countries, which we attribute to different FDI patterns of these investors.

Mariya Aleksynska & Olena Havrylchyk

What International Monetary System for a Fast-Changing World Economy?

N° 2011-04, March 2011

Though the renminbi is not yet convertible, the international monetary regime has already started to move towards a 'multipolar' system, with the dollar, the Chinese currency and the euro as its key likely pillars. This shift corresponds to the long-term evolution of the balance of economic weight in the world economy. Such an evolution may mitigate some flaws of the present (non-) system, such as the rigidity of key exchange rates, the asymmetry of balanceof- payments adjustments or what remains of the Triffin dilemma. However it may exacerbate other problems, such as short-run exchange rate volatility or the scope for ‘currency wars’, while leaving key questions unresolved, such as the response to capital flows global liquidity provision. Hence, in itself, a multipolar regime can be both the best and the worst of all regimes. Which of these alternatives will materialise depends on the degree of cooperation within a multilateral framework.

Agnès Bénassy-Quéré & Jean Pisani-Ferry

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RECENT PUBLICATIONS

LA LETTRE DU CEPII, MONTHLY

Reform of the International Monetary System: Some Concrete Steps

N° 309, 28 March 2011

Reform of the international monetary system is under discussion after three decades of apathy. However, in the short term, there is little chance of a grand redesign of the international monetary system. Nevertheless, concrete steps should be taken. First, consensus is needed on exchange rates, capital flows and reserves. This consensus is closer than often assumed, and should be codified in some form of soft law, with provisions for surveillance agreed on. Second, financial safety nets must be improved so that countries do not have to self-insure by accumulating reserves. The least difficult route could be a new regime for deciding on Special Drawing Right allocations that would facilitate more frequent use of this instrument. Third, a change in the composition of the SDR should be planned for, to strengthen the multilateral framework by including the renminbi. These reforms would be a partial move, and would prepare the ground for further developments.

Agnès Bénassy-Quéré, Jean Pisani-Ferry & Yu Yongding

Limiting Greenhouse Gas Emissions: the Sooner the Better

N° 306, 30 December 2010

The objective set by the IPPC of limiting the increase in average global temperature to +2°C compared to the preindustrial era is now accepted by all concerned. This ambitious objective was recognised at the Copenhagen Conference in 2009 and confirmed at Cancun in 2010. There are still no restrictive measures, but to achieve this objective, the main countries contributing to the emissions have already announced their commitment to reducing their emissions by 2020. The aim of this Newsletter is firstly to gain a better understanding of what this objective involves in terms of reducing global emissions over the next ten years. It will be then go on to assess whether the measures taken by the various countries are sufficient.

Stéphanie Monjon

FORTHCOMING

PPP (Partenariats Public-Privé) et croissance en Europe

Organized by Le Club du CEPII.

Paris, June 28, 2011

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