# The CEPII NEWSLETTER

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CENTRE D'ÉTUDES PROSPECTIVES
ET D'INFORMATIONS INTERNATIONALES


## *Focus*

### *The Challenges of a Multi-Speed Europe*

***The multi-speed approach to European integration has become a necessity because of the heterogeneity of European countries. However, this raises problems because it makes the long term characteristics of integration dependent on the path taken to achieve the union.***

Economic integration in Europe has, *de facto*, become a multi-speed process. As far as monetary integration is concerned, this has come as a response to concerns (mostly German) that the integration with some countries having weak monetary and fiscal records is too risky. As for the Central and Eastern European Countries (CEECs), the multi-speed process stems from the challenge of integrating up to twenty five countries of very different income levels into the Union, without blocking the deepening of integration altogether.

From a conceptual point of view, the effect of this new time dimension on regional integration is unknown. It is vital to ask whether the existence of different integration speeds may have an impact on the long term nature of integration itself. In short, is the process of integration path dependent?

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Excluding high-inflation countries from monetary union may modify their optimal monetary policies.

This would be the case if the dynamics of progressive integration generate strategic implications. A multi-speed approach could then endanger the very process of integration. In the case of monetary union, the gains of participation for the high inflation countries would decrease over time, and are likely to modify their optimal monetary policies. This is because entry into EMU will eliminate all possibilities for countries to use their exchange rates to export shocks to their partners. Outside the union, however, the excluded countries will be able to take advantage of the more restricted monetary policy within the EMU, by making strategic use of exchange rate movements against the single currency. If the exclusion lasts too long, or if the conditions for entry remain too stringent, then the credibility gains of joining the union may turn out to be less than the gains of adopting a free-rider strategy based on possible devaluations. In this case, a multi-speed integration is dangerous, as it may lead to a partial EMU, even though a full EMU is optimal *ex ante*.

A multi-speed approach may also be dangerous if the creation of a partial EMU makes it more difficult for the excluded countries to fulfil the convergence conditions for entry, should the differential in inflation rates (and in credibility) between the two groups of countries increase as a direct result of the partial EMU. This may happen as monetary policy within the union will be more stringent as members cannot use competitive devaluations against each other anymore. The inflation differential which is at the origin of the decision to exclude certain countries is reinforced by the exclusion. An EMS-type agreement between the EMU and the non-EMU countries has been proposed as a solution to this problem. However, the credibility differential between the two groups of countries will be widened because of the creation of a partial EMU, so that such an agreement would be even more difficult and costly to implement than the current EMS.

Partial integration of the CEECs may lead to their using environmental, labour and industrial policies to free-ride on market liberalisation.

As for the integration of the CEECs into the European Union, further free-rider problems may emerge under a multi-speed scenario, if these countries can use their environmental policies, labour standards, and industrial policies etc. to attract industries from the EU countries. If the CEECs are excluded for a long period of time they could be tempted to benefit from cooperation with the EU in certain areas, and so become free-riders of the EU's overall integration.

In addition to its strategic implications, sequential integration may also have a long term impact if it affects the location of economic activities in a permanent way. Countries that are, even temporarily, excluded from an integrated core could face a relocation of their firms to the integrated area, because lower transaction costs in the integrated area make trade within it cheaper, when compared to trade with the excluded countries. The latter are then likely to prefer that there is no regional integration in the core area.

Yet, this does not readily imply that the excluded countries should insist on entering the core as soon as possible. If 'agglomeration processes' do not set in (for example, because there is no significant migration), the decrease of transaction costs accompaning integration will make income divergence a stronger determinant of industrial location. If a poor country joins the integrated area, its firms will relocate to the richest markets which are in the core. If the transition period is associated with income convergence, then a multi-speed approach could be a good idea, as it will enable the 'peripheral' countries to join the integrated area when the income differentials are not too large, and so will not generate a massive relocation of activities to the core countries.

'Agglomeration effects' could permanently widen the gap between the hard-core and the 'periphery' of the Union.

This conclusion is reversed if agglomeration economies set in. In this case incomes are not fixed geographically, so that the temporary exclusion of the poor country may be accompanied by agglomeration in the rich, integrated core during the transition. This would result in increasing returns to sectors in the rich integrated countries, thus aggravating income divergence between the core and the periphery. This may occur even where convergence between the rich and poor countries was taking place before integration among the first-track countries. This could be called the 'agglomeration effect' of multi-speed integration. If the length of the transition period is determined by income convergence, a country 'temporarily' excluded may never be able to integrate the union.

Both scenarios have policy implications. If policy-makers do not believe that migration of human capital, and more generally agglomeration economies will set in, then a multi-speed approach to integration makes sense, because income differentials between countries are the main determinant of industry location. However, if agglomeration does set in, this approach is dangerous because the attraction of the core area during the transition period is self-reinforcing, and will likely lead to a widening income differential. Excluded, poor countries will then never be able to bridge the income differential, and will be excluded permanently.

In conclusion, it is possible to identify various economic mechanisms which make European integration path dependent. Either free-rider problems or agglomeration mechanisms could result from the progressive nature of integration. A multi-speed Europe may have become a necessity in view of the heterogeneity of European countries. Identifying some of its possible, adverse effects is nevertheless vital, especially as they require transitory institutional and economic agreements to be devised to help reduce them.

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FOR FURTHER INFORMATION SEE:

• 'THE GEOGRAPHY OF MULTI-SPEED EUROPE', P. MARTIN AND G. OTTAVIANO, *CEPII WORKING PAPER*, NO 95-10, NOVEMBER 1995.

• 'L'IMPORTANCE DES EXCLUS DE L'INTÉGRATION MONÉTAIRE EN EUROPE', P. MARTIN, *CEPII WORKING PAPER*, NO 95-08, NOVEMBER 1995.

• 'L'EUROPE À GÉOMÉTRIE VARIABLE, UNE ANALYSE ÉCONOMIQUE', J. PISANI-FERRY, *CEPII WORKING PAPER* NO 95-04, APRIL 1995.

• 'A SEQUENTIAL APPROACH TO REGIONAL INTEGRATION: CENTRAL AND EASTERN EUROPE AND THE EU', P. MARTIN, *CEPR DISCUSSION PAPER*, NO 1070, NOVEMBER 1994.

• 'FREE-RIDING, CONVERGENCE AND TWO-SPEED MONETARY UNIFICATION IN EUROPE', P. MARTIN, *EUROPEAN ECONOMIC REVIEW*, VOLUME 39, NO 7, 1994.

# RESEARCH SUMMARY

## Exchange Rate Regimes and Policies in Asia

***The CEPII is about to complete a study of the exchange rate regimes of the Asian countries, supported by the French Planning Agency and the European Commission (DGII). It shows that despite the growing importance of Japan in the world economy, and the development of Asia as a whole, the dollar continues to play a major role as an anchor in the exchange rate policies of the region.***

The large depreciation of the US dollar (USD) since 1985 has been of great concern to the European economies, which have seen their price competitiveness decline compared not only to the United States, but also to the East Asian countries. The latter were already benefiting from price advantages, which have been enhanced as the Asian currencies have followed the dollar in its depreciation against the yen. Frankel (1993) found some evidence for the increased influence of the yen in the nominal exchange rate policy of some Asian countries since the early 1980s. The present study shows that this movement was not confirmed in the early 1990s, and that the dollar has remained a real anchor for Asian currencies.

Only Hong Kong officially pegs its currency to the USD (Table 1), whereas the exchange rate regimes of most Asian currencies are 'managed floats', i.e. flexible regimes with frequent, official interventions. Thus the official regimes are rather vague, and include a wide range of *de facto* policies.

Table 1: Exchange rate regimes at end-1994

| | |
|---|---|
| Hong Kong | Pegged to the USD |
| Korea | Managed float |
| Singapore | Managed float |
| Taiwan | Not an IMF member |
| Indonesia | Managed float with USD reference |
| Malaysia | Managed float |
| Philippines | Free float |
| Thailand | Pegged to a basket |
| China | Managed float |
| India | Free float |
| Myanmar | Pegged to the SDR |
| Pakistan | Managed float |
| Sri-Lanka | Managed float |

Source: IMF, *Exchange Arrangements and Exchange Restrictions*, 1995.

Nominal exchange rate policies can be examined by comparing the volatility of nominal exchange rate variations against the dollar and against the yen (Table 2). The volatility of Asian currencies is much more limited against the dollar than it is against the yen (except for China during 1994-1995), and this implicit link has been reinforced in recent years.

Table 2: Relative volatility of nominal exchange rates against the dollar, as a percentage of their volatility against the yen

| | 1989-1993 | 1994-1995(05) |
|---|---|---|
| Korea | 18.6 | 20.8 |
| Singapore | 46.2 | 19.6 |
| Indonesia | 11.4 | 3.3 |
| Malaysia | 31.7 | 50.0 |
| Philippines | 51.3 | 41.3 |
| Thailand | 21.4 | 14.0 |
| China | 70.6 | 100.0 |
| India | 75.7 | 8.8 |
| Pakistan | 43.9 | 5.0 |
| Sri-Lanka | 68.6 | 14.3 |

Source: Author's calculations based on monthly variations of exchange rates (IFS data).

In brief, the Asian countries appear to stabilise their exchange rates against the USD. A regression equation may be used to show whether they follow all dollar fluctuations, or whether they partially stabilise fluctuations against other currencies[1] : $\dot{S}_{k,\$} = a_0 + a_1\dot{S}_{DM,\$} + a_2\dot{S}_Y$; where $\dot{S}_{k,i}$ stands for the monthly log-variation of the nominal exchange rate of currency i against j. A positive estimate for a1 (or a2) means that the monetary authorities partially stabilise the fluctuations of their exchange rate against the DM (or the yen). Estimates are given in Table 3. From 1974 to May 1995, the majority of Asian countries gave a significant, positive weight to the DM/$ rate in their implicit basket peg (Table 3). This weight ranged from 0.1 to 0.3, meaning that a 1% depreciation of the DM against the USD would lead to a 0.1 to 0.3% depreciation of the domestic currency against the USD. Conversely, only four countries gave a positive (but smaller) weight to the yen (0.07 to 0.2). Over the 1991-95 sub-period, fewer countries tried to stabilise their nominal exchange rates against the DM or the yen.

The link between short run nominal volatility and long run real fluctuations depends on the drift of the nominal exchange rate compared with cumulative inflation differentials. Pegging an international currency leads to a real appreciation if cumulative inflation differentials are not compensated by nominal devaluations. But in pegging the nominal exchange rate, monetary authorities hope that inflation will converge towards the foreign inflation rate. Thus,

(1) Frankel (1993) carried out similar regressions, but exchange rates were defined in terms of the purchasing power of local goods in the numeraire.

Table 3: Implicit nominal basket pegs

| | 1974-1995:05 | | | 1991:05-1995:05 | | |
|---|---|---|---|---|---|---|
| Country | a1 | a2 | SE (%) | a1 | a2 | SE (%) |
| Bhutan | 0.282* | -0.034 | 1.9 | 0.181 | -0.187 | 3.8 |
| China | 0.223* | 0.036 | 3.4 | 0.239 | 0.207 | 5.8 |
| Korea | -0.003 | 0.057 | 1.5 | -0.001 | 0.066 | 0.6 |
| India | 0.282* | -0.034 | 1.9 | 0.181 | -0.187 | 3.8 |
| Indonesia | -0.008 | 0.143 | 3.2 | 0.007 | 0.002 | 0.1 |
| Malaysia | 0.200* | 0.070* | 1.1 | 0.118 | 0.013 | 1.3 |
| Myanmar | 0.269* | 0.198* | 1.5 | 0.344* | 0.353* | 1.0 |
| Pakistan | 0.112* | 0.026 | 0.9 | 0.152* | -0.060 | 1.0 |
| Philippines | -0.005 | -0.076 | 2.4 | 0.065 | -0.191 | 1.6 |
| Singapore | 0.219* | 0.124* | 0.8 | 0.201* | 0.075* | 0.5 |
| Sri Lanka | 0.049 | -0.007 | 3.2 | -0.012 | 0.183 | 1.8 |
| Thailand | 0.050 | 0.075* | 1.1 | 0.075* | 0.093* | 0.1 |

* Not equal to 0, at 5% significance.

nominal and real pegs should be consistent in the long run, though contradictory in the short run. This study shows that Asian countries follow a real dollar peg along with a nominal peg[2]:

(i) The volatility of the real exchange rate is lower against the dollar than against the yen, and this has been reinforced in recent years (Table 4).

Table 4: The relative volatility of real exchange rates against the dollar as a percentage of their volatility against the yen.

| | 1989-1993 | 1991-1995 |
|---|---|---|
| Korea | 31.1 | 21.8 |
| Singapore | 44.4 | 25.5 |
| Indonesia | 21.3 | 13.8 |
| Malaysia | 71.0 | 64.3 |
| Philippines | 50.0 | 60.9 |
| India | 51.2 | 41.2 |
| Pakistan | 25.0 | 42.9 |
| Sri-Lanka | 47.9 | 22.0 |

Source: Author's calculations based on IFS data of producer prices.

(ii) Asian countries almost never give weight to real fluctuations of the DM/$ or Yen/$ rates in their implicit real basket peg. This conclusion arises from the estimation of the following equation:

$$E_{i,\$} = a + b_0(L)E_{i,\$} + b_1(L)E_{DM,\$} + b_2(L)E_{Y,\$} + \varepsilon$$

where Eij is the real exchange rate of currency i against currency j and L is a lag operator. The sum of the lagged coefficients for each variable is estimated using a Wold decomposition (Table 5).

In brief, most Asian currencies seem to be pegged to the USD both in nominal and in real terms. The appreciation of the yen has recently put this choice into question, since several countries in the region are heavily indebted in yen[3]. But a single country will unlikely switch its exchange rate policy towards a yen peg in a context of yen appreciation, because it would loose market shares in the US to the benefit of its Asian and Latin American competitors. A switch towards a yen peg would necessitate regional coordination in order to resolve this Nash-equilibrium problem.

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FOR FURTHER INFORMATION SEE:

- 'NI CHANGE FIXE, NI CHANGE FLEXIBLE', A. BENASSY, *LA LETTRE DU CEPII*, NO 133, MARCH 1995.
- 'LA CONCURRENCE POUR LE STATUT DE MONNAIE INTERNATIONALE DEPUIS 1973', A. BÉNASSY, P. DEUSY-FOURNIER, *ECONOMIE INTERNATIONALE*, NO 59, 3RD QUARTER 1994.

Table 5: Implicit real basket pegs

| Country | b0(1) | b1(1) | b2(1) | SE(%) | Autocorrel. of errors |
|---|---|---|---|---|---|
| India | 0.105 | 0.287 | 0.064 | 2.2 | No |
| Indonesia | -0.221 | -0.127 | -0.278 | 2.6 | No |
| Korea | 0.256 | 0.088 | 0.148 | 1.3 | No |
| Singapore | 0.265 | 0,188 | -0.027 | 1.4 | No |
| Thailand | 0.103 | 0.372* | -0.088 | 1.4 | No |
| Philippines (1) | 0.792* | - | 0.035* | 2.0 | Yes |

* Not equal to 0, at 5% significance.

** For the Philippines, exchange rates against the USD and the yen are taken to be level because they are stationary. The exchange rate against the DM is not included because its level is not stationary.

(2) Bhutan and Myanmar are left aside because of their low share in world exports; as in China, because price data are not available.

(3) The share of the yen in the long-term external debt at end-1993 was 40.7% in Indonesia, 37.5% in Malaysia, 38.3% in the Philippines and 52.1% in Thailand (source: World Bank, *World Debt Tables*).

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FRANCE

# *Conference Summaries*

## *DIFFERENT ROADS TO THE MARKET: A COMPARISON BETWEEN CHINA AND CENTRAL AND EASTERN EUROPE*

*BUDAPEST, 6-7 OCTOBER 1995*

This conference was organised by the CEPR, the CEPII and the OECD Development Centre, in collaboration with the Institute for World Economics of the Hungarian Academy of Sciences. It was financed by the European Community (ACE).

Fan Gang and Laslo Csaba pointed out that the different economic and political situations of China and the Central and East European Countries (CEECs) have led not just to a different pace of reforms, but also to contrasting priorities and performances.

The adjustment policies of state enterprises were analysed by Gérard Roland and Olivier Bouin, who noted that Chinese enterprises are lagging behind those of the CEECs, though even the latter have implemented largely gradualist strategies.

Foreign exchange policies have also been very different. Charles Wyplosz presented work on the use of fixed or floating exchange rate regimes in the macroeconomic stabilisation in the CEECs. This contrasts Zhaohui Zhen's analysis of China's exchange rate policy of pursuing convertibility, rather than stabilisation.

Kiichiro Fukasaku, Henri-Bernard Solignac and Françoise Lemoine stressed the very different trade policies implemented by these countries. For the CEECs, liberalising trade and especially imports has been a corner stone of domestic liberalisation, while China has pursued export-led growth and the decentralisation of economic activity and exports.

The transition has led to a destabilisation of public finances in both the CEECs and China. But according to Fabrizio Coricelli and Bert Hofman policy responses have been very different. In the CEECs, deficits rose to meet the social costs of restructuring enterprises, whereas in China (lower) deficits were brought about by tax decentralisation, and have reflected structural reforms, notably in the financial system.

Francesca Cornelli, Richard Portes and Wing Thye Woo analysed the situation facing financial intermediaries. In the CEECs, financial problems have led to banks rationing credit to companies. In contrast, the absence of reforms in China has led to the uncontrolled expansion of credit and the fragmentation of the financial system associated with powerful mechanisms for financial repression, which may cause difficulties in the long term.

The proceedings of this conference will be published by the OECD, in 1996.

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## *INTERNATIONAL TRADE AND EMPLOYMENT: THE EUROPEAN EXPERIENCE*

*PARIS, 25-26 SEPTEMBER 1995*

This conference was organised by the CEPII and the European Centre for Advanced Research in Economics (ECARE), and was supported by European Commission (DGV).

The studies presented were innovative, and based on data that has been little used so far, each looking at a particular dimension of this pressing issue. Although both the specific fields of investigation and the methods used differed considerably, the results demonstrated a notable homogeneity.

Mathias Dewatripont, André Sapir and Khalid Sekkat presented findings concerning the impact of trade with the LDCs, based on data from four European countries relating to long term unemployment, employment and wages according to qualification. Having tested various specifications they concluded that the impact of trade is negligible.

To obtain a better international overview, Anna Revenga and Richard Freeman used data from various international sources which they had rendered consistent. The econometric analysis suggests that trade with low labour-cost countries has only had a limited impact on labour markets in the OECD. However, trade within the zone has far stronger consequences.

For France, Olivier Cortes, Sébastien Jean and Jean Pisani-Ferry analysed the impact of trade on the structure of production, noting that there is no link between trade and the qualification structure of sectors which appears to stem only from the level of initial qualifications held by employees. They stressed, however, that penetration rates seem to have a negative impact on the employment content of value added, but this is so only for trade with developed countries.

As for Germany, Klaus Zimmermann's work concentrated as much on the impact of immigration on employment and salaries as that of trade, using data for the ex-FRG. But he concluded that trade, rather than immigration, has played an important role in labour market trends, in terms of wages and labour mobility.

Overall, these innovative, empirical studies suggest that the impact of trade on European employment is not negligible, but that it stems from trade within the developed countries rather than with the LDCs.

For further information regarding these papers please contact the CEPII.

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# Recent Publications

## ECONOMIE INTERNATIONALE, QUARTERLY

• NO 64, 4ND QUARTER 1995, 125 P.

• *'L'avenir des institutions de Bretton Woods : Halifax et après'*, Christian Chavagneux

• *'Croissance et marchés financiers : Une approche empirique'*, Arnaud Laroche, Emmanuel Lemoine, Arnaud Millien, Florent Prats, Yun Jie Zhang

• *'L'évaluation du risque dans les prêts internationaux'*, Ephraïm Clark

• *'Les échanges commerciaux entre les pays à bas salaire et l'Union européenne'*, Pierre-André Buigues, Alexis Jacquemin

Discusion

• *'Remarques relatives aux effets de la stratégie britanique de sortie du SME'*, Claude Leroy

• *'Divergences par rapport à Claude Leroy'*, Andrew Hughes Hallett, Simon Wren-Lewis

Book review

• *'Lectures sur la Russie actuelle'* Georges Sokoloff

Seminars

• *'Commerce international et emploi : l'expérience européenne'*, Olivier Cortes, Sébastien Jean

• *'Des voies différentes vers l'économie de marché : la Chine et les Pecos'*, Françoise Lemoine

• NO 63, 3RD QUARTER 1995, 120 P.

*LIFE OUTSIDE THE EMS*

• *'Quelques faits saillants après la crise du SME'*, Pierre Villa

• *'Y a-t-il une vie hors du SME ? L'expérience du Royaume-Uni'* Andrew J. Hughes Hallet, Simon Wren-Lewis

• *'L'Italie après la dévaluation : au delà des idées reçues'*, Alberto Locarno, Salvatore Rossi

*GLOBALISATION & REGIONALISATION*

• *'Quel cadre juridique pour l'activité des firmes multinationales ?'*, Fabrice Hatem

• *'Que penser des accords de commerce régionaux ?'*, François Benaroya

Price:
FF 110 per issue,
FF 480 annual subscription in Europe, and FF 580 outside Europe.
Publisher: la Documentation française

## LA LETTRE DU CEPII, MONTHLY

• *'L'APEC : un mariage forcé ?'*, Michel Fouquin
NO 141, DECEMBER.

• *'Quand les marchés triomphent... Une projection de l'économie mondiale à l'horizon 2002'*, Equipe MIMOSA, CEPII-OFCE
NO 140, NOVEMBER.

• *'Combien coûte un redressement budgétaire ?'*, Philippine Cour, Jean Pisani-Ferry
NO 139, OCTOBER.

• *'Faut-il payer ses dettes ? Hongrie et Pologne cinq ans après'*, Jérôme Sgard
NO 138, SEPTEMBER.

• *'L'affrontement commercial Etats-Unis Japon : le cas du secteur automobile'*, Evelyne Dourille-Ferr
NO 137, JULY-AUGUST.

Price:
FF 350 annual subscription in Europe, FF 440 outside Europe.
Publisher: la Documentation française



## BOOKS, BY CEPII RESEARCHERS

• *L'ECONOMIE MONDIALE 1996*
M. Fouquin, D. Pineye (eds.)
125 P., COLL REPÈRES, LA DÉCOUVERTE, FF.45.
This is an anual CEPII publication outlining major events in the world economy for a wide readership.

• *ECONOMIA MUNDIAL 1990-2000 : EL IMPERATIVE DE CRECIMIENTE*, report by the CEPII, published by Corregidor, Buenos Aires. (Translation of *Economie mondiale 1990-2000 : l'impératif de croissance*, 1992, 521 p. Economica, Paris, FF 200)

## CEPII WORKING PAPERS

• *'Why NAFTA might be Discriminatory'*, L. Fontagné
NO 95-12, DECEMBER 1995.

• *'Régionalisation et échanges de biens intermédiaires'*, L. Fontagné, M. Freudenberg, D. Ünal-Kesenci
NO 95-11, NOVEMBER 1995.

• *'The Geography of Multi-Speed Europe'*, P. Martin, G. Ottaviono
NO 95-10, NOVEMBER 1995.

• *'The Political Economy of French Economic Policy and the Transition to the EMU'*, C. de Boissieu, J. Pisani-Ferry
NO 95-09, OCTOBER 1995.

• *'L'importance des exclus de l'intégration monétaire'*, P. Martin
NO 95-08, NOVEMBER 1995.

• *'Asymétries financières en Europe et transmission de la politique monétaire'*, V. Coudert, B. Mojon
NO 95-07, SEPTEMBER 1995

• *'La mesure du capital éducatif'*, P. Villa
NO 95-06, SEPTEMBER 1995.

## *Events: Seminars and Meetings*

**• Europe and the Mediterranean: Economic and Political Issues for the Barcelona Conference**
I. Bensidoun, A Chevallier (CEPII), R. Dubertrand (Ministry of foreign Affairs)
*23 November 1995*

**• International Trade and Competition from the Emerging Countries**
A day's discussion organised with the French Centre for Foreign Trade
*15 November 1995*

**• Foreign Exchange Policies in Asia**
A. Bénassy, H. Delesssy. J. Pisani-Ferry (CEPII), S. Collignon (AUME) R. Barrell (NIESR)
*9 November 1995*

**• Evaluations of Market Risks by Banks and Prudential Control**
M. Aglietta (CEPII), P. Thoraval (Bank Commission), C. Tran (Crédit Lyonnais)
*18 October 1995*

**• Outside the EMS: the Experience of Italy and the UK**
A. Hughes Hallet (University of Strathclyde), A. Locarno, S. Rossi (Banca d'Italia), P. Villa (CEPII)
*22 september 1995*

**• Different Roads to the Market: a Comparison between China and Central and Eastern Europe**
See page 5.

**• International Trade and Employment: the European Experience**
See page 5.

## *News in Brief*

• Francis Mer has been appointed as the chairman of the CEPII's Board. He is the CEO of France's recently privatised steel company Usinor-Sacilor, and Chairman of the European Association of Steel Producers. Mr. Mer takes over from Michel Albert, who was appointed to the Monetary Policy Council of the Banque de France in 1994. The Board of the CEPII sets the centre's research programme. It is made up of leading government officials, business personalities, trade unionists and academics.

• Virgine Coudert and Benoît Mojon presented a paper on the transmission channels of monetary policy, at a conference held by the Association for the Monetary Union of Europe, in Frankfurt, on 30 Nov - 1 Dec 1995.

• A workshop was jointly held by the CEPII and the Russian Institute of World Economy and International Relations (Moscow), at the CEPII, on the 8-9 December 1995. It examined company management and international economic relations from a comparative point of view. The workshop was supported by the French Ministry of Foreign Affairs and the French Ministry of Higher Education and Research.

• The CEPII has entered an agreement with *The WEFA Group* which will share responsibility for the distribution of the CHELEM database.

• Philippine Cour joined the CEPII in September, to work as an economist on the MIMOSA model.

• Jean-Bernard Châtelain and John Baude left the CEPII during the summer, to work for the Banque de France. Frédéric Busson also left the CEPII for EDF, France's electricity company. The staff of the CEPII wish them all the best for the future.



## *Forthcoming*

• Two seminars that were to have taken place in December 1995 have been postponed until January 1996. They are:

- **The Single Market and the Adaptation of Industrial Structures**
L. Fontagné, M. Freudenberg, D. Unal-Kesenci (CEPII)
12 January 1996.

- **The Transition of Central and Eastern Europe and the ex-USSR**
P. Mordacq, N. Stern (EBRD)
30 January 1996.

• On 19 January, the CEPII and the CEPR will organise a roundtable in Paris to present and discuss the recent CEPR report (Monitoring European Integration n°6) *Flexible Integration: Towards a More Effective and Democratic Europe.* The speakers will be M. Dewatripont (ECARE-ULB and CEPR), G. Tabellini (Università commerciale Luigi Bocconi and CEPR), R. Boyer (CEPREMAP, CNRS, and EHESS), M. Dehove (CGP), J. Pisani-Ferry (CEPII).

• A seminar on 'The Effects of Exchange Rate Changes on Intra-EU Trade' will also take place in Paris on the 22 February. The speakers will be Henri Delessy of the CEPII, and Pierre-André Buigues of the European Commission (DGII).

• The CEPII, the French Institue of International Relations, Sciences Po and Chatham House will hold a one-day conference on trade policy, during the first quarter of 1996. Subjects to be included are: competition from low labour-cost countries, agriculture, trade in audio-visual products, exchange rates and the EU trade policy.

• The CEPII, the Caisse des Dépôts et Consignations, the OECD Development Centre, CEFI (University of Aix-Marseille II), and the Department of Foreign Economic Relations of the French Ministry of Economics and Finance are organising an international conference on 'Strategies of Growth and Emerging Markets'. The subjects to be addressed include: the financing of growth and development, industrial strategies, foreign investment, privatisation, exchange rate policies etc. This conference is to be held in Ho Chi Minh City (Saigon), on the 12 and 13 November 1996.

The organisers welcome any proposals for papers to be presented at the conference, but authors should note that travel expenses to Ho Chi Minh City cannot be covered. For further information please contact Jérôme Sgard at the CEPII (E-mail: SGARD@CEPII.FR).

• The Cepii and the Japanese Foundation for Advanced Information and Research (FAIR) will co-organise a high-level meeting on monetary and financial issues, to be held in Paris in May.

# THE MIMOSA MODEL

## A Projection of the World Economy to the Year 2002

The latest medium-term projection by MIMOSA was presented at a conference organised by the French Senate in October 1995. It suggests that growth in the OECD is likely to slowdown over the next two years, due to the investment cycle. Generally, demand will be restrained, because of high interest rates, and rather sluggish household consumption, which in turn results from fiscal tightness and limited wage rises. Firms' high profit margins will thus be only partially converted into investment. Meanwhile, inflation should be moderate, in most of the major OECD countries, and even in the United States and Germany, which should be close to full employment by 2002. Elsewhere in Europe, unemployment will decrease only slowly.

Long term real interest rates should fall slightly, yet still remain above growth rates, and so prevent any significant reduction of the public debts which built up rapidly in the 1980s and during the 1991-1993 recession. Containing deficits is therefore a wide-ranging priority, especially in the European Union, where the Member States are committed to meeting the Maastricht convergence criteria. The projection assumes that Germany, Austria, Benelux, Denmark, France and Ireland will achieve monetary unification, given a realistic interpretation of the Maastricht criteria, and a progressive erosion of their risk premia *vis-à-vis* the DM along the path to convergence. Inflation in Italy and the United Kingdom should be sufficiently low by 2002 for them to join EMU, but Spain and Portugal are likely to remain excluded.

Lastly, the projection suggests that world trade will keep expanding, at an average annual rate of 7%, mostly under the impulse of the Pacific zone. The durable weakness of the dollar should permit the United States to raise its market share in world trade, but the US current account deficit will persist, because of increasing outflows for interest payments. Japan's current surplus is expected to fall slightly, while the current account surplus of the European Union will persist, due to weak internal demand, and in spite of its decreasing share in world trade.

*Mimosa*

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Major Industrialized Countries: Some Significant Results

| | Average 1995-1997 | Average 1997-2002 |
|---|---|---|
| *GDP Growth - Annual Rates in %* | | |
| Germany | 2,6 | 3,3 |
| France | 2,4 | 2,0 |
| Italy | 2,6 | 1,7 |
| United Kingdom | 2,2 | 2,0 |
| Other EU 'North' | 2,9 | 2,8 |
| Other EU 'South' | 3,8 | 3,2 |
| United States | 2,7 | 1,8 |
| Japan | 2,1 | 2,6 |
| *Annual Inflation Rate* | | |
| West Germany | 2,4 | 2,3 |
| France | 2,6 | 2,9 |
| Italy | 4,3 | 3,4 |
| United Kingdom | 3,7 | 3,4 |
| Other EU 'North' | 2,2 | 2,7 |
| Other EU 'South' | 6,4 | 8,9 |
| United States | 2,8 | 3,3 |
| Japan | 0,0 | 1,5 |
| *Unemployment Rate* | | 2002* |
| West Germany | 8,3 | 5,9 |
| Germany | 9,7 | 7,5 |
| France | 11,9 | 11,1 |
| Italy | 10,3 | 8,4 |
| United Kingdom | 8,0 | 7,2 |
| Other EU 'North' | 9,2 | 9,5 |
| Other EU 'South' | 17,4 | 17,2 |
| United States | 4,9 | 5,8 |
| Japan | 3,1 | 2,0 |
| *Budget Balance (in % of GDP)* | | 2002* |
| Germany** | -2,3 | -1,0 |
| France | -5,2 | -1,2 |
| Italy | -7,8 | -3,8 |
| United Kingdom | -4,8 | -2,8 |
| Other EU 'North' | -3,4 | -4,3 |
| Other EU 'South' | -6,7 | -1,7 |
| United States | -1,9 | -2,1 |
| Japan | -4,2 | 0,8 |
| *Current Account Balance (in % of GDP)* | | 2002* |
| Germany** | -0,6 | -1,2 |
| France | 1,3 | 0,6 |
| Italy | 1,5 | 2,2 |
| United-Kingdom | -0,3 | 1,2 |
| Other EU 'North' | 3,5 | 1,6 |
| Other EU 'South' | -1,0 | -1,2 |
| United States | -2,6 | -2,5 |
| Japan | 2,4 | 2,0 |

* Rate in the year 2002

** As of mid-1990, includes operations in former East Germany.

*Source*: Model MIMOSA CEPII-OFCE.



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