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CONTENTS:

FOCUS

Trade in services: New horizon for globalization

In 2004, services represented 69% of world GDP, and 72% of total workforce of OECD countries. In contrast, the share of services in international trade is astonishingly low: it is only one fifth of world trade, and about 23% for OECD countries. Of course, many services are hardly tradable because their delivery requires face to face relationships. But, the persistence of political barriers to trade also plays a major role in explaining this relatively low contribution to world trade. Since 1995, the GATS (General Agreement on Trade in Services) lays the framework for the multilateral negotiations in services. In parallel, liberalization progresses also within the European Union. To eliminate trade barriers in service sectors, countries must reform the domestic regulations (including those controlling migrations). That explains why negotiating free trade is particularly difficult and controversial, as proved recently by the sharp opposition to the European directive on services (i.e. the so-called "Bolkestein directive"). Agnès Bénassy-Quéré, Cyrille Schwellnus & Deniz Ünal-Kesenci (2006) and Deniz Ünal-Kesenci (2006) present the key issues of multilateral and regional trade negotiations. Similarly, an analysis of the expected consequences of the directive on services is given by Cyrille Schwellnus (2006). To shed light on these topics that are at the top of the agenda of trade negotiators, one need reliable data and accurate economic analyses.

In order to picture the pattern of world trade in services, Isabelle Bensidoun and Deniz Ünal-Kesenci (Ünal-Kesenci, 2006; Bensidoun and Ünal-Kesenci, 2007) gathered several database. Working with data on trade in services is not easy. Balance of payments data is hardly compatible with data recording supply of services by affiliates on foreign markets (FATS), which is available for some OECD countries. Moreover, bilateral trade flows are scarce and they are not harmonized. Isabelle Bensidoun and Deniz Ünal-Kesenci had to deal with these issues to provide an original study based on relevant data. They show that, even if trade in services has not grown significantly faster than trade in goods, its structure has deeply changed during the last decades. The share of transport activities has fallen dramatically, while trade in some specific services (such as insurance and finance, or information technology) has risen sharply. Moreover this analysis shows clearly that the USA and the European Union are the two main exporters of services. The EU is relatively specialized in insurance, finance and computer and information services, while the USA has a strong advantage in cultural and recreational services and royalties and license fees. Even if some other countries, like India or Israel have a growing market share in some service industries, the leading position of the EU and the USA explains why they consider trade negotiations in services as a key issue. Finally, these studies point out that trade in services that is reported in current accounts of balances of payments represents only a minor share of total trade. Indeed, considering the countries for which FATS data are available, they show that the largest part of countries exports is actually direct sales by foreign affiliates.

A first step to evaluate the impact of trade liberalization in services consists in estimating empirically the effect of domestic regulations on countries' exports. Cyrille Schwellnus (2007) uses previously unexploited data to perform a panel estimation of a gravity equation that partly controls for unobserved country heterogeneity. His estimates of the elasticities of services trade with respects to domestic regulations are approximately 1/2 of the ones proposed in previous literature. Even with such relatively small elasticities, the consequence on multilateral trade of removing domestic regulations is still rather large. However, it is also shown that these elasticities decrease with the level of domestic regulation. In other words, any further progress in deregulation should have less impact on trade flows than previous ones.

Following a different but complementary strategy, Yvan Decreux and Lionel Fontagné (2006) rely on a Computable General Equilibrium assessment to evaluate the impact of freer trade in services. They use the MIRAGE model, to simulate the consequences of the implementation of trade facilitation that are contemplated by trade negotiators of the Doha round. As usual in this kind of exercise, the consequences on world welfare of liberalizing trade in goods are relatively modest. But when services are introduced in the picture, a very interesting outcome appears. With a 50% reduction of the obstacles to trade in services, welfare gain doubles for the world economy. For the European Union, an ambitious liberalization of services would translate into large increases in exports of services: a 15% increase of exports of business services, a 10% increase for transport, and 8% for financial and insurance services. Besides these direct analyzes of trade in services, Thierry Mayer, Anne-Célia Disdier, Silvio Taï and Lionel Fontagné (2006) show that liberalizing trade in some kinds of services may also have an indirect positive consequence on manufacturing trade. They test whether bilateral trade of cultural goods and services contributes to ease cultural differences between trade partners and thus fosters trade of more traditional goods. They conclude that a 10% increase in bilateral trade of cultural goods and services should increase trade in other goods up to 4.25%.

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ON THE RESEARCH AGENDA

Fiscal policy in real time

The active use of fiscal policy to stabilize the business cycle remains a controversial issue among economists. The traditional Keynesian school generally recommends that governments should actively intervene to smooth economic fluctuations. In particular, during phases of weak economic growth, they should adopt measures, such as tax cuts or new public investments, to foster a recovery in the economic activity. In contrast, when growth is above potential, they should cut public expenditures or increase taxation. In other words, they should act counter-cyclically over the economic cycle.

The Keynesian view has been criticized over the last thirty years by economists in the ''New Classical'' tradition. According to the "New Classical" view the market takes itself the steps to recover from a recession. Then, any active use of fiscal policy is useless, or even harmful.

Yet some empirical papers have recently found that fiscal policy, rather than being counter-cyclical, as Keynesian theories suggest, or a-cyclical, as advocated by the New Classical macroeconomics, has shown a tendency towards pro-cyclicality. This would occur in developing economies in particular, but also, though in a weaker way, in industrialized countries.

These studies, though insightful in that they allow to evaluate the "ex-post" or "realized" stance of fiscal policy, are not suitable to assess the "true" or "intentional" policy stance since they are based on revised data and not on the information available in real-time when policy-makers make their decisions.

This paper shows that when real-time data is used in the estimation of fiscal policy reaction functions relating a discretionary fiscal policy indicator, the structural primary balance, to the output gap and the debt-GDP ratio in OECD countries, the stance of fiscal policy seems to have been counter-cyclical over the last thirteen years. Interestingly, this would occur especially during economic expansions.

Jacopo Cimadomo

Differentiation and competitiveness of Latin American exports abroad

There is increasing empirical evidence that international specialisation in trade is done within varieties, rather than products. At the most detailed product level, large and systematic differences in unit values are observed. These differences can be related to factor endowments and development level of the exporting country (Schott, 2004; Fontagné et al, 2007). For developing countries, these differences in unit values can be of great importance: nowadays Mexico, Central America and Brazil seem to compete on a wide range of products with China and other Asian countries. It is often suggested that Latin American countries do not have a cost advantage over emerging Asian countries, and that they should consider an increase in the quality of their products to stay competitive. To find out whether Latin American products are in fact competing on the same quality segment of those of Asian goods and to shed some light on this policy debate, the analysis has to be conducted at a highly desegregated level.

This study, developed in collaboration with the ECLAC (United Nations Economic Commission for Latin America and the Caribbean), explores the pattern of specialisation across traded varieties for Latin American and Asian countries. The CEPII has recently conducted research on these issues, with a focus on North-South competition across varieties, with special attention to the European Union. The methodology can be extended to consider the specificity of Latin American countries (where we observe a strong presence of resource-based varieties in the exported goods). The study uses BACI, the new CEPII database (available from July 2007 on the CEPII website), providing the most detailed and comprehensive trade information at world level for the 1995-2004 period. The analysis considers, among others, the generation of indices of similarity at industry, product and variety level, as well as market shares for the exports by quality segment, and technological content.

Rodrigo Paillacar

The erosion of colonial trade linkages after independence

The dismantling of European empires after World War II led to sweeping changes in the governance of developing countries in Africa and Asia. Recent research in economics has investigated the long-run consequences of colonial rule. La Porta et al. (1998) argue that the British endowed their colonies with a legal system that produces superior economic outcomes. Acemoglu et al. (2001, 2002) find that colonizers were more likely to establish pro-growth institutions in sparsely populated areas with lower settler mortality. Banerjee and Iyer (2004) find that 50 years after India abolished land revenue systems imposed in the mid-19th century by British rule, the"institutional overhang" can be seen in agricultural productivity differences. In this study, we investigate a different legacy of colonial rule: the bias in post-colonial bilateral trade patterns.

The impetus for writing this paper came from the example of Algeria's exports to France. In 1960, two years before independence, Algeria accounted for 8.5% of French imports. Over the succeeding 42 years, that share fell to just 0.73% in 2002.

We compile a large data set on annual bilateral trade between almost every country in the world from 1948 to 2003. Employing a sequence of gravity-based specifications, we assess the impact of independence on colonial trade patterns. We estimate a semi-parametric specification in which years since independence are divided into seven intervals. Independence effects are identified from within-dyad variation in trade.

Our paper relates to several strands in the literature. First, unlike the work cited in the opening paragraph, we take as given any change in per capita income caused by evolving institutions. Second, we also use institutions (membership in regional trade agreements, GATT, and currency unions) as controls because our goal is to measure the effects of unobserved institutions on trade. We chiefly have in mind the role of business and social networks put forward by Rauch (1999). We also conduct two additional exercises to investigate mechanisms that underlie the post-independence erosion of trade with the former metropole. First, we exploit a data set showing the number of French nationals living in different countries which we consider as a proxy for the metropole's social and business network. We find the population of French expatriates in former colonies to decline in much the same way as bilateral trade. The declining expatriate presence explains a substantial portion of the diminished trade between France and its former colonies. Second, hypothesizing that war of independence will likely lead to more abrupt and permanent decline in bilateral business networks, we also categorize independence effects into amicable and hostile separations and find that the latter are more destructive to trade---although the gap between amicable and hostile separations seems to disappear after 50 years.

Thierry Mayer

Costs and benefits of membership to the Euro Zone: A counterfactual analysis

From the very beginning of the nineties until today, the European Monetary Union (EMU) has been indeed a quite debated idea. Many academics from different fields of international macroeconomics have predicted serious troubles for the central bank which would have to set the common monetary policy for such "ill-matched" countries.

Now that monetary integration is effective, this article aims at providing a quantitative assessment of the adequacy (or the inadequacy) of the single monetary policy to each euro area member over the 1999-mid-2006 period. Indeed, while economic analysis generally accepts that agents can know and analyze the potential outcomes of alternative scenarios, empirical works dealing with economic policy practice rarely use the so-called counterfactual approach. One main exception is the contribution of Pesaran et al. (2005) who use a global macroeconometric framework (Global Vectorial AutoRegressive, GVAR) to investigate the interdependencies between countries belonging to the euro area.

Our contribution in this paper is twofold. First, to our knowledge, it has never been tried before to gauge quantitatively the macroeconomic costs or gains of EMU membership. Second, by reversing the problematic of Pesaran et al. (2005), we modify the GVAR in order to test different scenarios related to the absence of the euro after January 1999. Echoing a short but intense debate which occurred in Italy in 2005, we also study the potential outcomes if Italy had not participated to EMU Stage 3 in 1999.

Emmanuel Dubois, Jérôme Héricourt & Valérie Mignon

DATABASES

What's going on with hourly labour productivity? Stylised facts from the EUKLEMS database

The good news in 2006 regarding the revival of productivity in Europe relative to the United States after the gloomy years of European productivity sluggishness needs to be confirmed over time. Past experience can teach some lessons as to the reasons of this new success.

Trends in output per hour growth show an acceleration in the US and a deceleration in Europe between the 1981-95 and 1996-2004 periods (Graph). In the US, output per hour growth jumps from 1.5% over 1981-95 to 3% in the 1996-2004 years. Only Finland and the eastern European countries exhibit such a performance over the last years, the former country on account of a bigger Information and Communication Technology (ICT) production sector and faster ICT use like in the US and the latter because of a catch-up effect.

The UK and France still enjoy growth rates above 2% over the 1995-2004 period but the deceleration of output per hour growth is steeper in France than in the UK, due to the fact that labour composition has changed more rapidly in the UK than in France. The largest decelerations of output per hour growth are experienced by Spain, Italy and Denmark. The gap can be explained by a big slump in the contribution of total factor productivity (TFP), that is a combination of labour and capital productivity. TFP is one of the contributions that adds up to the use of capital and labour services per hour to explain output per hour growth.

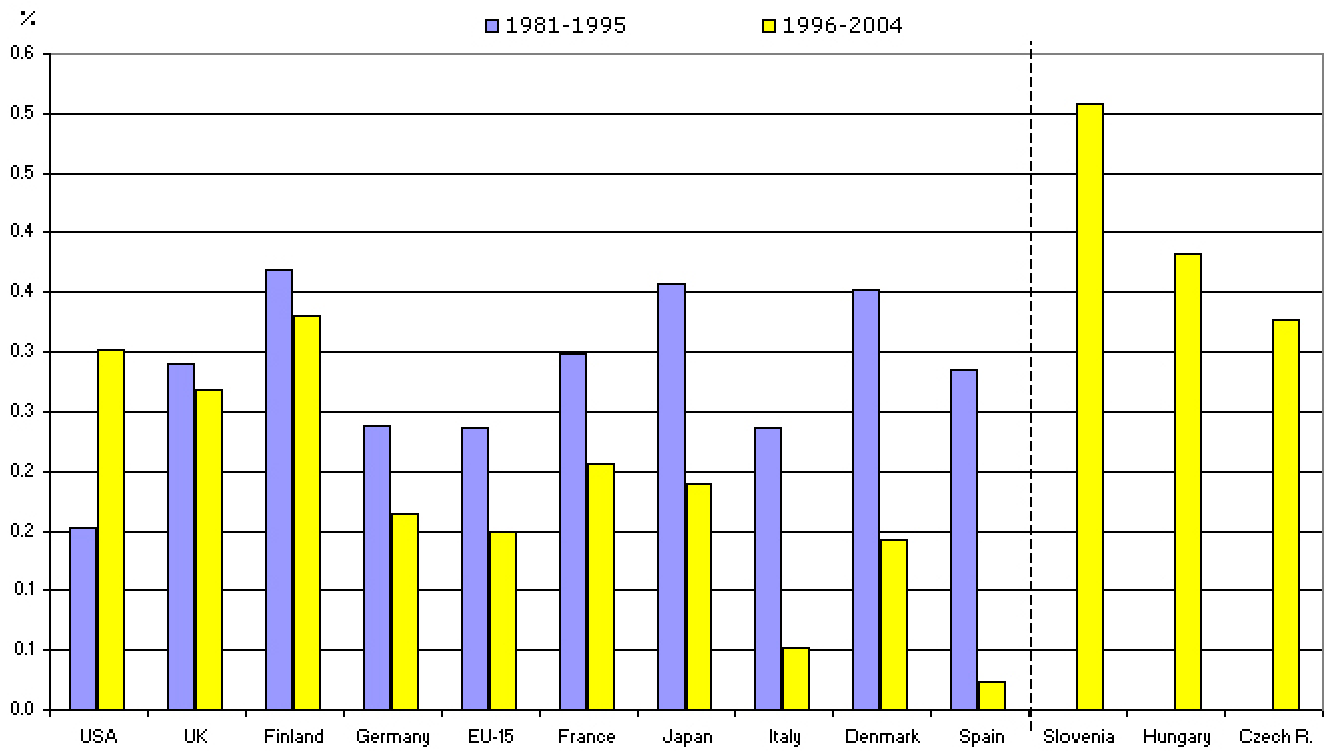
TFP is also the major candidate to investigate the difference of output per hour growth between the US and EU, as it explains two thirds of the US acceleration and about 40% of the EU hourly labour productivity deceleration. The decrease in TFP is the result for some European countries of using more intensively and less efficiently labour and capital. For example, in Spain and Italy, output per hour would have increased by 1.1% instead of 0.2% and 0.5% respectively per year over 1996-2004 had TFP growth been equal to 0.

Some big countries benefit from a larger TFP growth, UK and France (0.8 and 0.7 percentage point), and to some extent, also Germany and Japan (0.4 point) in the 1996-2004 years, along with an increase in the use of factors of production. In the UK, the contribution of capital deepening in ICT is even larger than in the US (1 point against 0.8 point). Labour composition changes are more significant in France (0.5 point) than in the US or in the EU (0.2 point). In Germany and Japan, non-ICT capital (0.7 point) contributes the most to output per hour growth (1.9% and 1.4%).

To sum up, the upturn of output per hour in Europe may may now come from the assimilation of past investments in the context of an increasing world demand.

Stylised facts are drawn from the EUKLEMS database on growth and productivity from 1970 to 2004 (released in March 2007). The EUKLEMS project, is funded by the Research-DG as part of the sixth Framework Programme, Priority 8. For each EU member country, national data have been processed in 72 industries, along the same template, by a national team. For France, this work has been carried out by the CEPII. “Sister datasets” have been constructed for the United States and Japan.

Graph
Output per hour growth in the market economy
(in %)



Source: EUKLEMS database
http://www.euklems.net

Laurence Nayman

EVENTS

Globalization and Big Emerging Countries

May 29, 2007

That was the theme for the 7th Rendez-vous de la mondialisation.

Integration of China and India into the world economy brought huge reserves in labour forces onto the market, increasing the number of potential workers from 1.5 billion to 3 billion people. This "big doubling" changes drastically the balance of power between capital and labour to the benefit of capital and pushes down employment and wages. The Chinese and Indian competition is real not only in traditional production sectors, intensive in unskilled labour, but more and more frequently in industry and services requiring skilled labour force. The two countries welcome more and more R&D units of multinationals.

Opening and innovation on financial emerging markets

March 27-28, 2006

CEFI (university of Aix-Marseille II), CEPII, NATIXIS and the French Embassy in Beijing organized the conference. It lasted two days and was structured in ten sessions, intertwining round tables amongst regulators and academic presentations.

The mix of participants made the conference lively and stimulating. Participants were academics, researchers from international institutions and from international banks, and officials from banking and securities market regulatory institutions.

A first topic encompassed the diversification of growth financing from bank to market finance, bank modernization and capital market development. A second topic involved regulation and supervision with a focus on Asia, highlighted by views on the European experience. A third topic gathered the international side of financial markets: balance of payment disequilibria, binding capital controls, exchange rate misalignments and adjustments, prospects on policy coordination and regional currency areas amongst emerging market countries. China's financial reform was a core focus. Chinese regulators underlined past achievements and challenges ahead to build a robust and efficient financial system. A particular emphasis was made on the development of bond markets at the present stage. The priority of establishing a strong legal and institutional infrastructure before opening markets was heralded.

Substantial discussion also arose on Asian integration. Trade integration in Asia is a long-standing process that builds foundations for an economic coordination on a regional basis. The Chiang Mai initiative is a forerunner opening ways for more ambitious achievements. The decoupling of Asian currencies from the dollar could incite East Asian governments to set a mechanism for mutual surveillance on exchange rates and to launch Asian bonds denominated in a basket of Asian currencies.

WORKING PAPERS

Global Ageing and Macroeconomic Consequences of Demographic Uncertainty in a Multi-Regional Model

N°2007-09, May 2007

In this paper, we investigate the impact of demographic uncertainty in a multi-regional general equilibrium, overlapping generations model (INGENUE 2). Specifically, we will consider the level of uncertainty in each of the ten major regions of the world, and their correlation across regions. In order to address these issues, we produce stochastic simulations of the world population for the ten regions until 2050. Then, we will analyse the economic consequences on a path by path basis over the period 2000-2050. These simulations allow us to assess the uncertainty induced into key macro-economic variables, the GDP growth rate and the world interest rate in particular, by uncertain future demographics. We show that the assumptions regarding interregional correlations of forecast errors are important in our model: they have a large impact on the uncertainty of the macroeconomic variables, and it appears that the macroeconomic adjustments can differ substantially if we consider independence or high correlation across the regions. In particular, the macroeconomic behaviour of the agents in the current account/saving problem differs significantly across regions according to the degree of interregional correlation.

Juha Alho & Vladimir Borgy

The Effect of Domestic Regulation on Services Trade Revisited
N°2007-08, May 2007

This paper uses the previously unexploited Eurostat ITS dataset and the latest release of the OECD Product Market Regulation indicators to reevaluate the effect of domestic regulation on cross border services trade. The empirical analysis is guided by recent theoretical advances in the theoretical derivation of the gravity equation which allows to avoid common sources of bias in previous studies. Once these common sources of bias are eliminated, the support for the claim that the domestic level of regulation reduces services trade is weakened.

Cyrille Schwellnus

The Location of Domestic and Foreign Production Affiliates by French Multinational Firms
N°2007-07, May 2007

Economists explaining location choices of foreign affiliates usually focus on country-level determinants. Costs of production, the size of expected demand, proxies for agglomeration effects, and various policy-related incentives form the usual set of covariates. Two dimensions of those choices are usually omitted. Multinational entreprises (MNEs) usually have more than one affiliate abroad and they also continue to invest domestically during their international expansion. We add to the literature on location choice by accounting for i) the entire network of affiliates of each French MNE over the 1992-2002 period, and ii) the entire set of possible choices by including the home country. Our results show that the interdependence between affiliates of the same MNE matters a great deal for location, both for the choice between different foreign countries and for the choice between investing at home or abroad. Moreover, French firms' propensity to invest abroad is shown to be positively linked to their productivity and the size of their intangible assets.

Thierry Mayer , Isabelle Méjean & Benjamin Nefussi

Specialisation across Varieties within Products and North-South Competition
N°2007-06, May 2007

There has been repeated evidence in the trade literature that international specialisation is taking place within products, across varieties, rather than across products or across industries. Using a new database which draws on United Nations COMTRADE data covering trade between 1995 and 2004 for more than 200 countries and 5,000 products, we systematise this evidence and ask what are the precise patterns and determinants of such specialisation between North and South. Although the two groupings of countries are quite similar when specialisation is considered across broadly defined sectors, they are very dissimilar when the differentiation of products, reflected in differences in unit values across varieties, is taken into account. We systematise Schott's relation between the unit values of varieties shipped and the level of development of the exporter. Lastly, we use a gravity equation accounting for the market positioning of varieties and for the direction of trade in order to shed light on the determinants of trade in varieties. We observe that supply and demand related determinants contemplated in the literature offer a coherent framework in which Linder's hypothesis combines with factor endowments. Overall, our analysis confirms that advanced economies are maintaining their advantage in the upper segment of product markets: North and South are not competing head on within industries. However, this conclusion does not exclude a likely impact on the advanced economies' labour markets of a systematic repositioning on up-market varieties.

Lionel Fontagné, Guillaume Gaulier & Soledad Zignago

Trade Costs and the Home Market Effect
N°2007-05, March 2007

Most of the theoretical and empirical studies on the Home Market Effect (HME) assume the existence of an "outside good" that absorbs all trade imbalances and equalizes wages. We study the consequences on the HME of removing this assumption. The HME is attenuated and, more interestingly, it becomes non-linear. The non-linearity implies that the HME is more important for very large and very small countries than for medium size countries. The empirical investigation conducted on a database comprising 25 industries, 25 countries, and 7 years confirms the presence of the HME and of its non-linear shape.

Matthieu Crozet & Federico Trionfetti

RECENT PUBLICATIONS

ECONOMIE INTERNATIONALE, QUARTERLY

Issue 108, 4th Quarter 2006

La crise monétaire turque de 2000/2001 : une analyse de l'échec du plan de stabilisation par le change du FMI
Jérôme Héricourt Julien Reynaud

Similarité institutionnelle, qualité des institutions et commerce international
Emmanuelle Lavallée

Real Equilibrium Exchange Rates: a Panel Data Approach for Advanced and Emerging Economies
Antonia López Villavicencio

Divergence, Wage-Gap and Geography
Frédéric Andres

Débats

La politique migratoire française à un tournant (full text)
Martine Durand & Georges Lemaître

Revisiter l'aide publique au développement
Pierre Jacquet

France and International Environmental Policy
Alain Ayong Le Kama, Mouez Fodha & Pierre-André Jouvet

Economie Internationale publishes papers dealing with a wide range of issues in applied international economics. Papers cover topics like macroeconomics, money and finance, trade, transition, European integration and regional studies. *Economie internationale* especially encourages the submission of articles which are empirical in nature and emphasises the rigor of empirical analyses and data processing. With articles being submitted from economists in various universities, central banks and private financial institutions worldwide, the journal achieves an extraordinary diversity and provides many viewpoints on international economic and financial questions. Articles should be readable by non-specialists. *Economie Internationale* is indexed in Econlit.

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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@cepii.fr *Economie Internationale* makes every effort to provide authors with timely reports from referees. Authors will be informed within four months.

NEWS IN BRIEF

Lionel Fontagné (Professor of economics at the University Paris I and former Director of the CEPII) is awarded the GTAP Research Fellow distinction (2007-2010) "in recognition of his outstanding contributions to border protection measurement and innovative research in the broader field of international economics".

Riccardo Magnani joined the CEPII as an economist in June. His research interests mainly concern the analysis of the population ageing phenomenon and its consequences at the macroeconomic level and on the pension system.

The CIREM has a new Vice-Chairman and a new Executive Director: Martine Carré-Tallon (Deputy Director of the CEPII) and Laurence Nayman (economist), since April.

FORTHCOMING

L'économie mondiale 2008
CEPII
September 12, 2007

Africa in a the World Economy
AFD, CEPII & French Minister of Foreign Affairs
September 15, 2007

Mondialisation, transports et logistique
September 20, 2007

L'Europe : quelle attractivité financière ?
Groupama Asset Management & CEPII
September 25, 2007

Fifth ELSNIT Annual Conference on Integration and Trade
IADB
October 26-27, 2007

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