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## *FOCUS*

### **China in the Global Economy**

The rise of China has been the most outstanding phenomenon in the world economy over the last ten years. China has become the world's third largest trading power, the second host-country for foreign direct investment, and the second holder of international official reserves.

The CEPII's research has amply shown that China's trade expansion is the result of its strong involvement in the international segmentation of production processes. China has become an assembly country and international processing activities account for 55% of its exports. Production sharing with industrialised Asian economies (Japan, Taiwan, South-Korea, Hongkong) has allowed China to diversify its exports rapidly from textiles to electronics, as industrial firms have transferred the final, labour intensive, stages of production to their affiliates on the mainland. Foreign affiliates in China account for an ever-increasing share of China's trade (almost 60% in 2004).

This integration in Asian production networks also accounts for the rapid technological upgrading of China's trade. The overwhelming share of China's high-tech exports (75% in 2002) is handled by firms with foreign capital: most of China's high-tech imports come from Asian countries (70% in 2002) and consist of parts and components. China has thus taken advantage of the globalisation process. But China's rising importance in world markets, including in technology-intensive products, should not hide the dualism that characterises its manufacturing industries.

China's internationally competitive industries, which benefit from foreign capital and technology, remain distinct from its traditional industries. They are also largely based on

assembly activities, using foreign components. In contrast, China's traditional industries are run by wholly Chinese-owned enterprises and lag significantly behind international competition.

China's emergence has also led to the reorganisation of production in Asia and has fostered regional integration. China's exports of final goods to the US and the EU have expanded rapidly and have given rise to large trade surpluses, while East Asian advanced economies have lost ground in Western markets and have increased their exports of intermediate goods and capital goods to China.

Overall, the rising share of China's exports in world markets, together with the accumulation of massive foreign reserves, has harboured increasing suspicions about the potential misalignment of the Chinese currency. Since 1994, the Chinese authorities have maintained a fixed exchange rate regime against the dollar. The bilateral real exchange rate of the yuan has also been rather stable, despite rapid productivity gains and the accumulation of net foreign assets. Yet, a consistent, effective appreciation was recorded up to 2003.

In order to investigate both the hypothetical misalignment of the yuan and its global impact, the CEPII has developed a project for evaluating real exchange rate misalignments within the Group of Twenty (made up of the G7 countries and large emerging economies). It can be concluded that by the end of 2001, the yuan was indeed undervalued, a situation that has probably continued in the following years. For the time being, it has not been possible to detect Balassa-Samuelson effects in China, probably because of the structural segmentation of the labour market. As a consequence, the effective undervaluation of the yuan is rather limited (5% in 2001), when measured using Chinese data. However, if China were to behave as other major economies (the G20 countries), the yuan would have been undervalued by 16% in 2001. Moreover, the Chinese yuan appears to be especially undervalued against the US dollar, which is also a consequence of the peg on the dollar.

Pushing the analysis further, this work suggests that the dollar/euro exchange rate would have been close to equilibrium in 2003, had the yuan and other Asian currencies also been close to their equilibrium level. It also shows that the lack of adjustment in China and more generally in Asia tended to magnify the dollar overvaluation in 2001, and to a lesser extent in 2003.

The diagnosis of Chinese undervaluation is therefore controversial. The country's exchange rate policy is under pressure, as both official and business constituencies put forward disparate arguments: overheating of the economy, ongoing catching-up that calls for real exchange-rate appreciation, "unfair" cost advantages benefiting the country, or capital controls that artificially back-up the exchange rate regime.

However, the peg on the dollar has served the country well regarding its economic performance over the last two years. China has achieved strong growth with moderate inflation, and a modest current account surplus. Furthermore, it does not suffer from overall pent-up demand. Its over-investment can better be cured by domestic demand management. The prospect of an appreciation of the real exchange rate is a long-run phenomenon that will come out of a rise in non-traded goods prices accompanying more balanced growth. Due to concerns about the pitfalls inherent in reforming its domestic financial system, however China will rightly open its capital accounts with great care. It will not consider changing the peg too soon and too abruptly.

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## ON THE RESEARCH AGENDA

### The INGENUE 2 Model

The initial goal of the INGENUE project was to analyse quantitatively international flows and growth dynamics induced by the differential ageing of the various regions of the world. To this end, a long-term model for the world economy was built jointly by the CEPII, the CEPREMAP and the OFCE. The model describes a multi-region world along the lines of models developed by Obstfeld and Rogoff [1996], in which the structure of each regional economy is similar to that of other applied, overlapping-generations, general equilibrium models (such as Auerbach and Kotlikoff [1987]).

Several studies were performed with the first version of the INGENUE model, notably in order to analyse the macroeconomic consequences of pension reforms in Europe. Nevertheless, the first version of the model had several shortcomings and it was decided to build a new version. The INGENUE 2 model is now operational and displays several major improvements. In particular, the world is divided into ten regions (compared to six in the previous model) and the demographic part of the model is now built on our own demographic forecasts, based on UN data. The baseline scenario describes the macroeconomic and demographic evolution of the ten regions during the first half of the 21st century.

Several studies based on the new model are on the research agenda of the INGENUE team. Among them, a reassessment of the macroeconomic implications of the pension reforms in Europe is scheduled. Our purpose is also to shed some light on the debate about immigration into Western Europe. To this end, we will study the macroeconomic consequences of several labour migration scenarios, from the Southern Mediterranean countries especially into Western Europe. The worldwide consequences of a faster increase of total factor productivity (than the one selected in the baseline scenario) in China and India, in particular, will also be forecast.

With the INGENUE model, we should be able to provide insight into the "standard" macroeconomic consequences of such scenarios (for instance, GDP growth, investment and saving dynamics) but the model also allows us to study the long run consequences for the public pension systems in the different regions.

Vladimir Borgy

### A Quantitative Assessment of the Impact of the Doha Development Agenda (DDA)

The agreement reached in Geneva last summer re-launched the WTO's multilateral negotiations. Following on from work already carried out using Computable General Equilibria for assessing trade liberalisation, the CEPII has launched a study which aims to evaluate fully the economic impact of the trade round in the field of agriculture (market access,

domestic support, export subsidies), of market access in industry and services, as well as in the field of trade facilitation.

Compared to studies which have already been undertaken on this subject, this work will make it possible to assess the overall impact of the multilateral negotiations based on the use of detailed information regarding the bound, MFN, as well as preferential tariffs. Also, we aim at providing realistic simulations of the effects of an agreement on trade facilitation.

In addition to providing results for the EU25 as a whole and for its main trade partners, the study will provide significantly detailed results for 89 European regions. Accordingly, the economic adjustments which will follow on from trade openness may be tackled and accompanied at the regional level.

Yvan Decreux & Lionel Fontagné

## **Institutional Determinants of Foreign Direct Investment**

Since the late 1990s, the literature on economic development has been renewed by focusing on the quality of domestic institutions as a key explanation of cross-country differences in both growth rates and income per capita (see IMF, 2003 and Acemoglu *et al.*, 2004, for recent surveys). The degree of protection of civil and property rights, the level of economic and political freedom, as well as low levels of corruption have been shown, in particular, to be associated with higher prosperity.

At the same time, there has been a growing interest in the determinants of foreign direct investment (FDI) in developing countries, as FDI is considered as the most stable component of capital flows to developing countries and can also be a vehicle for technological progress through the use and dissemination of improved production techniques. Not surprisingly, a number of authors have therefore also studied the link between institutions and FDI. Such a link could be seen as one channel through which institutions promote development in the modern era.

In this study, we contribute to the literature on the determinants of FDI in developing countries, and re-evaluate the role of the quality of institutions on FDI. We improve upon the existing literature in several ways. First, we re-examine the role of governance infrastructure in the host and in the source country, by estimating a gravity equation for bilateral FDI stocks that includes governance indicators for the two countries. Second, we tackle multicollinearity and endogeneity biases by systematically comparing estimations with and without GDP per capita which is likely to be correlated to various measures of institutional quality. This is done by using two-stage estimations, and by instrumenting governance variables when necessary. Third, we look into the detail of institutions by using a new database constructed by the French Ministry of Finance's network in 52 foreign countries. This database is used to point out in some detail relevant institutional features. For comparability, we look for the most proximate variables in existing databases and compare results when these are used. When possible, panel data estimations are also carried out. Finally, we study the impact of institutional distance on bilateral FDI.

Agnès Bénassy-Quéré, Maylis Coupet & Thierry Mayer

## **A New Assessment of the Impact of Regional Agreements on Trade Patterns: The Case of the EU**

The influence of regional agreements on trade patterns has been the primary subject of the huge literature using gravity equations to study bilateral volumes of trade. There are dozens of papers in this literature dating back to the early seventies, that is soon after the gravity equation had been applied to international trade for the first time. Researchers have investigated almost all possible regional trading agreements (RTA), looking for positive deviations from the "norm of trade" given by gravity.

For a while, technical progress in this area has mostly consisted in adding covariates to the set of explanatory variables, in order to provide better control for unobserved characteristics of the bilateral trade between two countries. This is indeed important for the assessment of the impact of an RTA, which usually involves a large proportion of contiguous countries. Omitting this variable, while putting an RTA dummy in a cross-section regression can generate fallacious, positive estimates of trade policy due to an omitted-variable bias.

More recently, decisive progress has been made in the link between the empirical gravity equation and the different modelling frameworks available in trade theory. Many authors have had tried to take into account the remoteness of trading partners, that is not only their bilateral distance, but also their location with respect to third countries. The improved link with theory should allow such problems to be sorted out by radically improving the norm of trade to which exchanges within an RTA is compared.

Yet, even with such progress, the reference group to which members of an RTA are compared must be considered. We envision solving this reference group issue using two different methods. First, as what has already been done in the border effect literature, we will consider international trade inside an RTA, not with respect to trade with third countries solely, but will compare these two flows to a third one: trade within countries, which seems to be the natural benchmark of a perfectly integrated economy. Second, we will apply score matching techniques, recently introduced in the trade literature. This involves a two step procedure. In the first step, the probability of becoming a member of the RTA is actually modelled, and in the second step, the trade volumes of actual RTA members are compared to a counterfactual consisting of the most proximate countries possible. That is the situation of a country which is likely to enter the RTA in question, but then does not.

Lionel Fontagné, Thierry Mayer & Soledad Zignago

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## *DATABASES*

### **The Worldwide Distribution of *Ad Valorem* Equivalent, Applied Tariff Duties for Agricultural Products**

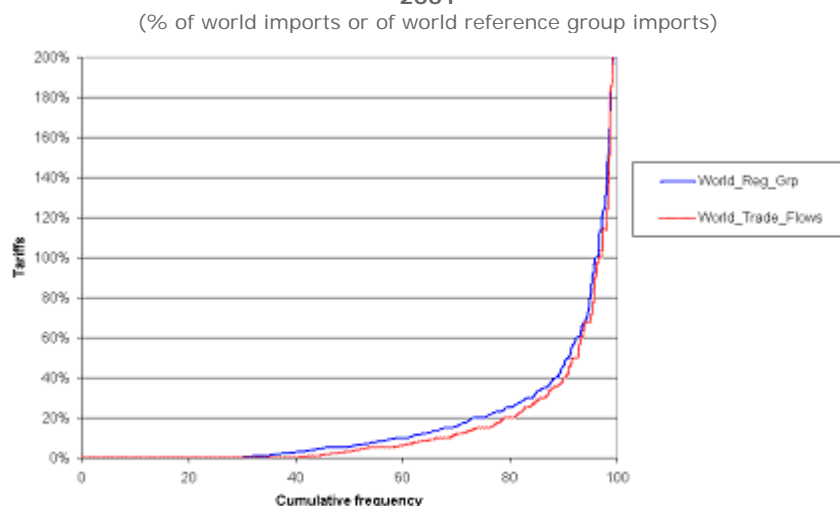
The MACMap-HS6 database, built in cooperation with the ITC (UNCTAD-WTO, Geneva), provides an exhaustive and consistent assessment of *ad valorem* equivalent (AVE) applied duties for 5,111 products (at the six-digit level of the Harmonised System covering agricultural and non-agricultural products), for 163 countries with 208 partners, taking into account all preferential agreements (see Bouët, A., Decreux, Y., Fontagné, L., Jean, S. & Laborde, D. *CEPII Working Paper N° 2004-22*). *Ad valorem* tariffs are taken into account, but so are specific, mixed and compound tariffs, as well as tariff rate quotas. This unique database allows the landscape of world protection to be characterised in detail, not only in terms of average levels, but also in terms of distribution. This is illustrated in the graph below, which represents the worldwide, cumulative distribution of AVE tariff duties for agricultural products in 2001, based on the measurement of AVE protection applied by each country to each partner, separately for each product (for a similar graph on non-agricultural products, see Bouët *et al.*, *op.cit.*). This is done using two different metrics. The first one (the red curve) measures the share of world agricultural imports facing less than a given level of AVE tariff. The graph below shows, for instance, that approximately 40% of world agricultural imports are free of duty.

But imports are not independent of protection, and it is likely that the remaining 60% of world agricultural imports that face non-zero duties would be larger, were protection to be removed. This is why the distribution is also characterised using the MACMap weighting scheme. This weighting scheme is built up in MACMap for the sake of aggregation, based on a clustering of countries into five reference groups, gathering similar countries in terms of GDP and openness. Instead of bilateral flows from the importer to the exporter, MACMap weights are calculated as trade flows from the exporter towards the reference group the

importer belongs to. The endogeneity bias is thus minimised. Using this weighting scheme, the share of duty-free imports for agricultural products worldwide appears to be only slightly above 30%.

The way this distribution is measured thus makes a significant difference. Whatever the metric used, however, this graph highlights the strong skewness of protection across the world, with a small proportion of world products and markets accounting for a large part of world average protection. This is especially clear in agriculture, and this finding suggests that granting even limited flexibility (as measured through the number of goods) can strongly undermine the impact of any liberalisation agreement.

**Worldwide Cumulative Frequency of *Ad Valorem* Equivalent, Applied Tariff Duties for Agricultural Products, 2001**



Source: Bouët, A., Decreux, Y., Fontagné, L., Jean, S. & Laborde, D., "A Consistent, Ad-Valorem Equivalent Measure of Applied Protection Across the World: The MACMap-HS6 Database" *CEPII Working Paper N°2004-22*, Graph 3.

Note: The red curve measures cumulative frequency in % of world trade. The blue curve measures cumulative frequency in % of the world total of MACMap weighting schemes. All calculations are made at the six-digit level of the Harmonised System, individually for each country and each partner.

Sébastien Jean

## *EVENTS*

### **Tax Competition in the EU25**

The lively debate on tax competition in the European Union illustrates a vast academic literature discussing the risk of a sub-optimal production of public goods (including inter-personal redistribution), in a world where capital is perfectly mobile whereas labour, especially low-skilled labour, is not. This risk is to be balanced against the gains from putting some pressure on national governments to raise public sector efficiency. The issue of tax harmonisation was re-launched by the European Commission's proposal, in 2001, to move towards a harmonisation and a consolidation of corporate tax bases within the European Union, and more recently by EU enlargement to low-tax countries. The CEPII and its Business Club felt that the existing theoretical as well as empirical literature on the subject were perhaps not used enough in the policy debate. This was the prime reason for bringing together high-level researchers working on these issues at both the academic and the policy-relevant levels. The conference took place in Prague on December 16-17, 2004, hosted by CERGE-EI. It was organised within the TAXBEN project held under the 6th Framework Programme of the European Commission, and also received support from the CEPII's Business Club and from the *Institut CDC pour la Recherche*.

During the first day the results of the academic literature were examined on the basis of four different themes: the scope for tax competition, the impact of taxation on the location of firms, tax avoidance and the scope for tax harmonisation. Detailed analyses of the nature of tax competition, on its extent, on its consequences as well as on the scope for tax harmonisation were provided by: Alexander Klemm (Institute for Fiscal Studies, London), Patrick Artus (IXIS, Paris), Clements Fuest (University of Cologne), Jouko Ylä-Liedenpohja (University of Tampere), Ruud de Mooij (CPB, The Hague), Amina Lahrèche-Révil (CEPII), Marius Brülhart (University of Lausanne), Andreas Haufler (University of Munich), Sam Bucovetsky (University of York) and Jacques Thisse (CORE, Université Catholique de Louvain).

The second day was devoted to policy issues. It started with a view of taxation in the EU15 and in new member states. Then, the pros and cons of the EC proposal (concerning the harmonisation and consolidation of tax bases) were discussed. Henk Vording (University of Leiden), Ludomir Lizal (CERGE-EI, Prague), Witold Orłowski (NOBE, Warsaw) and Olev Raju (University of Tartu) provided EU-wide as well as country views of tax strategies in the EU. Carola Maggiulli (DG Taxud), presented the European Commission two-tier proposal issued in 2001. Marcel Gérard (Fucam, University of Mons) discussed the proposal through illustrative simulations. The day ended with a roundtable discussion on tax coordination which brought together Thiess Buettner (Munich University), Steve Bond (Institute for Fiscal Studies, London), Michaela Erbenova (Czech National Bank, Prague), Daniele Franco (Banca d'Italia, Rome), Witold Orłowski (NOBE, Warsaw) and Jean Pisani-Ferry (University Paris-Dauphine). Lionel Fontagné (CEPII) was the moderator.

Agnès Bénassy-Quéré

### **East Asian's *de Facto* Economic Integration**

The IDE Workshop held on the 19 January 2005 was an occasion to compare the processes of regional integration in East Asia and Europe. Up to the 1990s, regionalisation in East Asia was more a *de facto* phenomenon than the result of an institutional process. Papers presented at the conference show that East Asian economic regionalisation is based more on a vertical division of labour rather than on a horizontal division of labour as in Europe, and that the emergence of China has led to a far-reaching reorganisation of production within the region. Even tariffs seem to be higher within Asia than with America or Europe, showing an inverse preferential treatment of Asian Countries. The papers presented will be the object of a joint IDE-CEPII publication in 2005. Further cooperation between IDE-CEPII for 2006 is being discussed.

Michel Fouquin

### **Productivity and Monetary Policy**

The 4th Economic Policy Forum, organised by the CEPII, the *Banque de France* and the IDEP, took place on the 19 January, 2005 at the *Banque de France*.

The meeting was focused on the policy implications of a (stable) rise in the productivity growth rate, in the light of the recent experience of the US economy. The invited speakers were Professor Alan Blinder (Princeton University), Christian Noyer (Banque de France Governor) and Olivier Garnier (Director of the Strategy and Research Department, SGAM).

Prof. Blinder identified three different conceptual issues: i) the rise in productivity growth is recognized by everyone: in this case the money supply should grow at the same rate as productivity. An expansionary monetary policy should not then be inflationary since demand effects are completely offset by supply ones. ii) The rise in productivity growth is recognized only by the Central Bank: nominal wages do not increase faster than usual, the Central Bank faces a (pleasant) choice between lower unemployment and lower inflation. iii) The rise in productivity growth is recognized by no one: the Central Bank does not provide enough

liquidity, employment falls. Prof. Blinder argued that the US experience of the 1990's was somewhat comparable to the second case above.

Governor Noyer stressed that, generally, productivity shocks are identified with a lag. However, the monetary authority should avoid making the opposite mistake, which proves to be even more costly: *i.e.* identifying a shock that did not occur. Thus, from a normative point of view, he suggested that a "pragmatic practice" should be favoured, relying on the monitoring of a broad set of inflationary sources.

Olivier Garnier stressed that Central Bankers should not only be concerned with the impact of productivity growth on inflation. In the medium term, in fact, a productivity shock may result in a wedge between the actual real interest rate and the 'natural' real interest rate. The gap between the two might be a cause for financial imbalances (*i.e.* asset price bubbles, over-investment and under-savings), albeit with contained inflation.

## The CEPII Business Club's Meetings

### Fault Lines in the Chinese Economy and Society

For 25 years or so, China has been one of the world's fastest growing economies and its population has experienced an unprecedented rise in average living standards. For the most part, this has gone together with social stability and political continuity, particularly over the 15 years since June 1989, when the military cleared the centre of Beijing by force and the "Party elders" dismissed then the General Secretary of the Party. To the extent that there is a causal relationship between them, the massive reduction in poverty in the train of economic growth has enhanced social stability. However, historically the relationship between economic growth and stability has not been one-way (see Huntington, 1968). The dramatic economic performance has also been accompanied by the appearance of fault lines running through the society, with development producing stresses and strains of varying magnitudes. Among others, these include the emergence of wide and visible economic inequalities, a sharp rise in unemployment, as well as the appearance of a large population of migrants in towns and cities who are treated as "outsiders". Furthermore, protests and defiance of authority, albeit localised, are a commonplace.

This meeting, held on 14 January 2005, opened the **CEPII Business Club's series of conferences on China**. Dr. Athar Hussain, Deputy Director of the Asia Research Centre of the London School of Economics has been researching the Chinese economy for more than 20 years. He has frequently visited China, Hong Kong and Taiwan and has been a counsellor to the government of the People's Republic of China, as well as to several international organisations such as the World Bank, the Asian Development Bank and the United Nations Programme on Development. He is a member of the group of experts nominated by the World Bank to see through: i) reform projects of state enterprises; and ii) the reorganisation of the electricity industry. Dr Hussain is presently a counsellor to a British government project on unemployment insurance in China.

Dr. Hussain set out the various sources of tensions which are accompanying China's economic development: the aggravation of income inequalities, massive migration and urbanisation, a banking system saddled with bad debts, ethnic divisions, environmental degradation, as well as the coexistence of single-party rule and a market economy. He concluded by outlining the probabilities of a crisis and the government's capacity to manage it.

### Low Cost, Low Fare

There are ever-more "low cost" airline companies and the price wars they have triggered across the world are fiercer and fiercer, leading to risks of a major restructuring of the air transport sector and its allied services, with on-line reservations becoming the rule.



Tougher competition is however not limited to the airline companies. Rail companies are also now offering "low cost" TGV trains, with attractive prices.

This is likely to lead to a complete reorganisation of transport systems over the next fifteen years, in France, in Europe and throughout the world, benefiting new customers.

Are "low cost" / "low fare" services at a long-standing turning point which will lead these sectors to restructure? Or will some of the low cost companies go out of business, as has already happened to Aëris and Air Lib?

On 9 February 2005, the CEPII's Business Club invited several experts to discuss these issues. Michel Lénéz (Air France) analysed the new environment facing air travel, and its consequences for all transport activities and for users. Antoine Cachin (ITAC) and Stéphane Fargette (Easyjet) also gave the points of view of passengers and "low cost" carriers.

### Turkey and the European Economy

On the 17th December 2004, the European Council announced its decision to open membership negotiations with Turkey. For months, the public debate has focused on the political aspects of this decision, both in France and in the rest of Europe. But the issue at stake is also crucial for the Turkish economy.

The opening of negotiations indeed prolongs a remarkable process of stabilisation and reform, and participates in the consolidation of a new growth regime. The trust which has been reinforced by the prospects of membership has created a favourable climate for foreign direct investment. This in turn is likely to provide Turkey's dynamic manufacturing sector with new strengths and help its international economic integration. At the same time, the adoption of the *acquis communautaire*, to which Turkey has committed itself under the Customs Union Treaty of 1996, signifies that the country is in the process of adopting far more advanced economic standards.

To gauge the implications of these issues and inform public opinion in France, the CEPII Business Club and TÜSIAD, along with the CEPII and the BIAC, organised a conference on the 10th December 2004, which allowed Turkish and European experts to debate the integration of Turkey into the European economy and the country's transformations within the perspective of membership.

### The Future of the World Economy: What Is the Place for European Industry?

The issue of new competition emerging is not new. Nevertheless, there are several factors which are currently creating a radical break in the logic of the international division of labour: the strong reduction of transaction, transport and communication costs; the opening up of large economies with low cost labour; the possibility of mobilising such labour across foreign affiliates and multinational firms through the use of advanced technology.

Given these factors, it is not sure that traditional economic analysis of the costs and benefits of openness is still adapted. The sudden arrival of competitors in industry (such as China), or in services (such as India) has led to renewed worries about a destructive shock hitting industry and employment in the industrialised countries. Faced with such competition from low-wage countries, will Europe be able to retain its industrial activities? If yes, then which activities? Or should Europe abandon its industrial base to become, on the one hand, a large market for imported products and, on the other hand, a major producer of services, even though these too are threatened by relocation to low labour-cost countries? What policies could help Europe meet these challenges? Will it be sufficient to pursue measures concerning the economic environment or is it better to return to more active measures?

A CEPII Business Club meeting was held on 11 February 2005, to address these issues.

Lionel Fontagné began by recalling the mechanisms leading to deindustrialisation and placed the phenomenon of industrial relocation within firms' competitive strategy framework. He went on to examine economic policy options and set out scenarios for the world economy, for the medium term. Marc Deluzet (CFDT) and Pierre Gattaz (FIEEC, Radiall) gave their opinions concerning this new industrial environment and the policies which should be pursued by France to remain competitive and to deal effectively with the economic insecurity that is presently affecting it.



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## WORKING PAPERS

### Market Access in Global and Regional Trade

No 2005-02 January

This paper develops a method for assessing market access difficulties with an application to manufactured trade patterns between developing and developed countries. The method also allows the assessment of the impact of regional trading arrangements to be renewed. A micro-founded, gravity-type model of trade patterns is used to estimate the impact of national borders on revealed access to Northern markets by Southern producers. The results reveal that the difficulties faced by developing countries' exporters in accessing developed countries' consumers are higher than vice versa. At the same time, the EU, CUSA/NAFTA, ASEAN/AFTA and MERCOSUR agreements all tend to reduce the estimated degree of market fragmentation within these zones.

Thierry Mayer & Soledad Zignago

### Real Equilibrium Exchange Rate in China

No 2005- 01 January

In this paper, we try to measure the size of a possible misalignment in the Chinese real exchange rate in two ways. On the one hand, we address the issue of the "Balassa effect", by which the real exchange rate of a catching-up country should appreciate. On the other hand, we follow the FEER (Fundamental Equilibrium Exchange Rate) approach. Both methods suggest that the renminbi is undervalued.

Virginie Coudert & Cécile Couharde

### A Consistent, *Ad Valorem* Equivalent Measure of Applied Protection Across the World: The MAcMap-HS6 Database

No 2004- 22 December

MAcMap-HS6 is a database providing a consistent, *ad valorem* equivalent measure of tariff duties and tariff rate quotas for 163 countries and 208 partners, at the six-digit level of the Harmonised System (5,111 products). Based on a joint effort by ITC (UNCTAD-WTO, Geneva) and CEPII (Paris) to collect systematically and harmonise the relevant information, we describe here the methodology used in MAcMap-HS6 to compute and aggregate an *ad valorem* equivalent of applied protection, which is well suited for analytical purposes (in particular computable general equilibrium analysis).

Antoine Bouët, Yvan Decreux, Lionel Fontagné, Sébastien Jean & David Laborde

### IMF in Theory: Sovereign Debts, Judicialisation and Multilateralism

No 2004- 21 December

The paper argues that the successive regimes for restructuring sovereign debts have been shaped by the linkages existing between three institutional functions: information gathering

and economic expertise, then third-party mediation, and lastly policy enforcement, also called conditionality. While these functions were integrated within the Fund during the 1980s' debt crisis, mediation has now been outsourced, under the pressure of the demand by the private sector for a thorough judicialisation of the restructuring process. Two responses to this demand have been formulated: the creation of a supra-national "bankruptcy court"; and the reliance upon national courts, specifically those under the jurisdiction of which the initial debt contracts had been signed.

Jérôme Sgard

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The CEPII's Working Papers are available free, on-line, in PDF format; hard copies are also available on request.

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## *RECENT PUBLICATIONS*

### *ECONOMIE INTERNATIONALE*, QUARTERLY

*To mark the 100th anniversary issue of Economie Internationale, the CEPII is very pleased to welcome contributions by leading authors in international economics and by key policymakers.*

#### **No 100, 4th Quarter 2004**

##### **Présentation**

Lionel Fontagné

##### **Declining international inequality and economic divergence: Reviewing the evidence through different lenses**

François Bourguignon, Victoria Levin & David Rosenblatt

##### **Croissance endogène et réduction de la pauvreté**

Philippe Aghion & Beatriz Armendariz de Aghion

##### **Global imbalances and the lessons of Bretton Woods**

Barry Eichengreen

##### **The dollar/euro exchange rate**

John Williamson

##### **Architecture financière internationale: au-delà des institutions de Bretton Woods**

Michel Aglietta

##### **Recent developments in macroeconomic analysis: Reviving the case for stabilisation policies**

Jean-Philippe Cotis

##### **New perspectives on the benefits of exporting**

David Greenaway & Richard Anthony Kneller

##### **La politique commerciale de l'Union européenne**

Pascal Lamy

##### **The dilemma of globalisation: A German perspective**

Hans-Werner Sinn

*Economie Internationale* publishes original contributions in applied international economics, dealing either with finance, macroeconomics, or trade. Submissions of interest in the public debate, to policy makers or to help understand current economic issues, are most welcome, in English or in French.  
Publisher: *La Documentation Française*, price: €18.50 per issue, €65.50 annual subscription in Europe and €68.50 outside Europe.  
Issues published more than 2 years ago are available in full text on the web site. For more recent issues, only selected articles are available in full text.

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## **LA LETTRE DU CEPII**, MONTHLY

### **Turkey-Europe : From a Customs Union to the European Union**

N° 240, December 2004

The European Council held on 15 December 2004 opened the way to membership negotiations between the European Union and Turkey. *La Lettre du CEPII* published last September indicated how this process was likely to consolidate the macroeconomic stabilisation and reforms presently underway. It should also deepen Turkey's regional integration. This integration, which was reinforced by the customs union of 1996, is taking place in an original way that is different from that of the other new Member States of the Union or other candidate countries. The two sectors which account for most of Turkey's exports – textiles & clothing and vehicles – are experiencing a transformation of competitive conditions in the national and international markets. In both cases, trade liberalisation within the Euro-Mediterranean area and the adoption of the *acquis communautaire* will play a key role in defining Turkey's new trade specialisations.

Agnès Chevallier, Guillaume Gaulier & Deniz Ünal-Kesenci

### **Exceptional Circumstances**

N° 239, November 2004

The drafters of the Euro area's Stability and Growth Pact provided for the possibility that "exceptional circumstances" could allow member states' budget deficits to exceed the 3% limit. But the definition they gave has shown itself to be too restrictive: none of the countries facing deficit problems while suffering from poor growth has been able to use this justification. The clause therefore appears as virtual and the European Commission is proposing to change it. What could the new definition of exceptional circumstances be? Should a rate of growth be used, as is presently the case, but at what level? Or should a "threshold of exceptionality" be considered? Should an absolute standard be defined for all member states or should a standard be adapted to the potential growth levels of different countries? The various possibilities are examined here: they would have led to exceptional circumstances being invoked for between 20% and 50% of the excessive deficit cases which arose from 1997 to 2003.

Agnès Bénassy-Quéré & Alexis Penot

### **The Dollar in the G20**

N° 238 October 2004

The swelling of the United States' foreign debt is weakening the international monetary system and feeding expectations of a long term depreciation of the dollar. The required adjustment of the US current account thus appears as a burden to be distributed between the US and its trade partners, via adjustments in the exchange rate. The greater exchange rate flexibility which the G7 has called for concerns mainly the large emerging economies that are not included in it. The G20 may therefore appear as a forum better suited to furthering international monetary co-operation. This article evaluates the adjustments required, and their distribution within the G20, on the basis of an econometric description of the behaviour of the real exchange rate over the long term. If all countries had gone along with flexibility, then the Euro would have been close to its equilibrium rate against the dollar in 2003. But a simulation of Asia' strategy for pursuing monetary stability vis-à-vis the dollar

suggests that the Euro needed to appreciate a further 10-15%.

Agnès Bénassy-Quéré, Amina Lahrèche-Révil & Valérie Mignon

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*La Lettre du CEPII* (monthly) is published in French. Publisher: *La Documentation Française*, price: €48.40 outside France (on subscription only). The English version of this publication is available on the CEPII's web:  
<http://www.cepii.fr/anglaisgraph/news/accueilengl.htm>

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## **BOOKS**

### **Politique économique**

**Agnès Bénassy-Quéré, Benoît Coeuré, Pierre Jacquet & Jean Pisani-Ferry**  
Editions De Boeck, 2004

How can unemployment be brought down? Is the European Central Bank's inflation target too low? Is the public debt excessive? Is it better to have a fixed or a floating exchange rate? Which taxes need reforming? Can Europe's living standards catch up with the United States? All these questions are part of the economic policy debate, and economic analysis can and indeed should provide them with some precise and reasoned answers.

Economists actually work on these issues constantly. But they are not always heard within the political and social debate. To be sure, the tools are spread over a range of distinct disciplinary fields, such as macroeconomics, public economics, labour economics or international economics. This book seeks to overcome this problem, by bringing together for the first time in one volume the essential issues at stake, the main theoretical learnings, along with analysis of the current debates in economic policy.

The approach sets out first to be methodological (What is economic policy? What are its objectives? How is it to be conducted?). Then it is thematic, ranging from fiscal policy to employment policy, while passing by money, exchange rates, long term growth and taxation. Without casting aside scientific rigour (the book draws on reference models, the major classical authors and more recent research), it stresses the practical use of tools of economic policy. Much attention is paid to the experiences of different countries, and especially of the European Union and the euro area. Disagreements over doctrine and methods are not obscured, while the sometimes-passionate debates among political policy-makers are put into perspective.

The book is based on a seminar which the authors have given for a number of years at the *Ecole Polytechnique*. Formalisation of relationships is put in boxes, which makes the book accessible at different levels. Each subject chapter is structured in three parts – the issues at stake, theory and policies – so that reading can be conducted individually. The book aims to meet the needs of a varied readership: students at bachelor's or master's levels in economics, management or political sciences, policy-makers and observers of economic policy, economic actors and interested readers who wish to know what economists have to say about major issues affecting their daily lives.

### **European Integration and the Functioning of Product Markets**

European Communities, 2004

Europe's achievements in economic integration have attracted world-wide interest and are seen as an example for other regions to follow. Ten years after the completion of the Single Market Programme, this book is able to utilise empirical data not available to previous studies, and can also build on research by reputed academic experts and staff at the European Commission. Michel Fouquin co-authored, with Khalid Sekkat, a contribution focused on the sensitivity of European sectors to exchange rate fluctuations. Combining an exposure indicator and the elasticity estimates, a sectoral classification emerges where the three sectors having the highest elasticity and being the most exposed are machinery &

equipment, electrical & optical products and transport equipment.

### **Dollar Adjustment: How Far? Against What?**

C. Fred Bergsten and John Williamson, ed.

Institute for International Economics, November 2004

Building on the scholarship of the highly successful 2003 volume, *Dollar Overvaluation and the World Economy*, this book assesses the progress made to date in correcting the sizeable misalignments of key national currencies that developed in the late 1990s and early 2000s. The book examines whether a dollar decline is needed for the United States and the rest of the world to achieve sustainable current account positions and what the impact of a major dollar realignment would be on economies around the world. It also features new ideas on the effectiveness of intervention in moving exchange rates in a desired direction. The book brings together perspectives from government, industry, and academia. Agnès Bénassy-Quéré, Pascale Duran-Vigneron, Amina Lahrèche Révil and Valérie Mignon co-authored a contribution suggesting that the dollar-euro exchange rate was close to equilibrium in 2003, conditional on the acceptance, by China and other Asian countries, of a rather large underevaluation of their own currencies against the US dollar.

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## *NEWS IN BRIEF*

Christian Deubner joined the CEPII to collaborate on the management of the ENEPRI network and work on European issues. He will also organise the CEPII's collaboration with the DIW, within the framework of the German-French Council of Economic Advisors, which has recently been established. He will assist Lionel Fontagné in the French Planning Agency's MIDI research group.

Houssein Boumellassa joined the CEPII to work on the CHELEM Balance of Payments database and CGE Models.

Xavier Chojnicki joined the CEPII to work on pensions system in Europe.

Antoine Bouët has left the CEPII to join the International Food Policy Research Institute, in Washington DC, where he will work as a Senior Research Fellow on Global Trade Modelling, to measure the impact of trade liberalisation on Less Developed Countries.

Sophie Chauvin has left the CEPII for the French Treasury Directorate at the Ministry of Finance, where she will work on Latin America.

Isabelle Bensidoun is being seconded to the Council of Economic Analysis, as a Scientific Advisor.

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## *FORTHCOMING*

### **China's Growth: Is the Agricultural Sector Being Left Behind ?**

10 March 2005

Meeting organized by the CEPII Business Club

### **The New Frontiers of European Union**

16-17 March 2005

Conference organized by the CDC Institute for Economic Research, the *Caisse des Dépôts et Consignations*, the CEFI, the CEPII and the *Revue Economique*

## **Can Germany Sustain Locational Competition?**

14 April 2005

Conference organized by the ARGE and the CEPII

## **Globalisation and Growth**

21 April 2005

Conference organized by the CAE and the CEPII

## **German-French Council of Economic Advisors**

25 April 2005

## **OECD Forum**

2-3 May 2005

With the scientific support of the CEPII

## **2005 Asia Conference**

12 May 2005

Conference organized by the CEPII Business Club, Ubifrance and the French Senate

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