ANNALES D'ÉCONOMIE ET DE STATISTIQUE. – N° 47 — 1997

RECENT DEVELOPMENTS IN INTERNATIONAL ECONOMICS

Foreword

Denis PÉGUIN and Antoine SOUBEYRAN*

The world trading system is changing, so are international trade and trade policy theories. As a by-product of a conference organized under the auspices of ADRES, this special issue brings together a range of papers which show how researchers are concerned by the real world and constantly try to explain observed facts with theory. Unless facts give rise to new theoretical developments. It's not new. One remembers the effect produced by the Leontief's paradox on research in international trade theory in the 50s and the 60s. The same phenomenon appears in the 80s and the 90s.

Nevertheless, we cannot say that all traditional propositions developed over two centuries in trade theory are obsolete. Comparative advantage is still prominent in explaining trade structure, but its dynamic nature has been highlighted. It can be modified by trade, it can be moulded by appropriate trade policies. Likewise, free trade can still be considered as the preferred solution but without a too rapid and onerous transition period.

The most striking advances in theoretical developments during the last two decades undoubtedly are the consideration of the organizational dimension of trade and the spatial aspect of activities. It is no longer the market for products or factors which is the only determinant of the world comparative advantage and trade structure. State intervention and bilateral or multilateral agreements are now prominent. These interventions or agreements no longer only affect trade flows, to restrain or promote them, they have impact on market access for foreign products and increasingly influence the structure of comparative advantage.

A rapid examination of conflicts presented before the World Trade Organisation since its creation in 1995 is significant. They deal increasingly with problems related to restrictions to market access for imported goods (see for instance the conflict between the United-States and Japan in the automobile sector or the one between the United-States and Venezuela and Brazil on gasoline) or problems related to technology of production used by exporting countries (see the conflict between the United- States and Mexico on sea mammals) and less and less with problems related to trade barriers.

* D. PÉGUIN: Université de Provence, UFR LAG-LEA, GREQAM; A. SOUBEYRAN: Université de la Méditerranée, Faculté des Sciences Économiques, GREQAM.

Concerning the spatial dimension of activities, there again a significant evolution of theory has taken place. The second wave of regional integration in the 80s and the multiplication of multinational agreements (70% of regional agreements existing up to now have been signed after 1990) have contributed to this renewal. Economic geography has become a full field of research in international economy and the analysis of factor movements is being reevaluated.The papers presented in this special issue deal with these developments. The order in which they are introduced has no relation with the importance given to a particular theme of research.

The dynamic aspect of comparative advantage formation is considered in the first article. R. Mendez develops the argument that international trade of goods or direct investments carry within themselves convergence forces via the voluntary technological diffusion (production under license) or unintentional (imitation): the exchange of goods implies a certain exchange of ideas, but commercial trade also carries within itself divergent forces. Trade leads to specialization which modifies the dynamics of factors through reinforcing comparative advantage which strengthens economies' specialization. The author illustrates this idea with an endogenous growth model where the dynamics (i.e. convergence or divergence of standards of living) depends on the process of ideas spreading (international transfers of technology) and of economies' history (via their initial relative endowment).

The role of the multilateral trade organization, with its rule-oriented framework, is developed in the two following articles.

The Multi-Fibre Arrangement (MFA) is a system of bilateral voluntary export restraints on textile and clothing items between importing and exporting countries. The exporting countries manage entirely the allocation of quota licenses and the granting of export visas. The importing countries are only responsible for ensuring that the quota limits are not exceeded. K. Krishna and L.H. Tan examine the implications of quota subcategorization by an exporting country like India. They show that, depending on the environment and the objective of the authorities, subcategorization may be theoretically desirable. However they do not advocate subcategorization in practice because the informational requirements necessary for its success are not likely to be met.

The paper by V. Ginsburgh and S. Weber examines the issues raised by Article XIX of the GATT and its revision. Article XIX permits government to raise tariffs to protect their producers, but only temporarily, with no discrimination, and with compensation or retaliation. This article has been the object of some controversy. The Uruguay Round redrafted Article XIX in several aspects, but the main idea remains: a country may take action, but has to make concessions to its trading partners that are "equivalent" to their loss in exports. This paper analyzes situations in which a country may retaliate to protective measures taken by one of its trade partners. The authors formalize the compensating mechanism and show that the built-in retaliation mechanism prevents countries from initiating a tariff war. The retaliation mechanism is modified to yield the free trade as a unique equilibrium of the associated tariff game.

Strategic trade policy is still a prolific field of research. P.-Ph. Combes, B. Caillaud and B. Jullien examine the role of national subsidy policies in a common market under imperfect competition and information. They clarify the costs and benefits of integration in regulated industries, as well as the interaction between national regulations in a common market. The basic model with perfect information describes an economy with two countries. In each country a single regulated firm produces to satisfy the local demand (before the Common Market creation) or the Common Market demand (once it is created) on the market for a particular good. Each firm is regulated by a national agency through a linear tariff: a unitary subsidy and a lump-sum transfer. Like in Brander-Spencer, competition in the common market is modeled through a two-stage game: governments set first subsidy policies simultaneously and non cooperatively to their firms, firms accept or reject these policies. Then firms compete in quantities in the common market. They consider the cases where the regulation schemes are secret or not. Then they examine the case of imperfect information when the agencies lack information about unit firm costs. The authors show that it is optimal to allow states to subsidize their domestic firms: a common market creation improves the allocative efficiency and reduces the agency costs of regulation.

Economic geography certainly retrieved its theoretical position thanks to the questions raised by the regional integration wave of the 80s. Two articles contribute to this research.

At the European community level, an important problem is to analyze the effects of European integration (as a fall in transport costs) on the location of industries. Many analysts (like Krugman and Venables) think that integration may lead to agglomeration for sufficiently low levels of trade costs, favoring the development of regions that are already rich. F. Trionfetti extends the Krugman-Venables model of economic geography to show that public expenditures (like the European Union's Structural Funds program) can create a new source of "backward" linkage that tends to favour dispersion over agglomeration. Three types of international transfers are examined: pure transfers, tied aid, and joint expenditure.

The paper of H. Erkel-Rousse extends the monopolistic competition framework of Dixit-Stiglitz, Krugman and Helpman-Krugman in three directions to provide a theoretical foundation for empirical trade equations which underlines the role played by product differentiation in comparative advantage and export performances of industrial countries. To derive trade equations requires geographically differentiated products (to identify separate import demand), market segmentation as a consequence, and differences across countries (to isolate factors of comparative advantage), three features not modeled in the Dixit-Stiglitz, Krugman model. The author introduces endogenous horizontal differentiation strategies for individual multi-product firms and she partly endogenises the source of comparative advantage by allowing firms to influence the brand image of their products.

International factor movements become more and more important in our changing world. For example migrations flows in the Western part of Europe generate tensions in Germany, not only from fear of increasing unemployment, but also from the use of publicly provided goods by immigrants. N. Leiner examines how non-migrants are affected by an international migratory movement in the presence of public goods. She compares costs and benefits of migration in a two country-trade model with public goods in a one period and multi-period model, where she clearly identifies additional investments and changes in tax revenue; migration policy is examined.

C. Matthieu proposes a model of product differentiation based on an extension of the spatial approach proposed by Hotelling, to determine the equilibrium on two markets (one market by country) where domestic and foreign differentiated products can be traded. Firms decide sequentially on their plant localization, on technical specification of their products and on prices. In this framework the author shows that the market can have a monopoly or a duopoly structure according to the trade barrier and sunk cost levels. At equilibrium the multinationalisation of both firms is always achieved in a prisoner's dilemma game. Moreover, cross-hauling direct investments and intra-industry trade can also be realized but they are exclusive like production abroad and exportation.

Even if trade liberalization is always desirable, it nevertheless seriously threatens countries because of its consequences on employment and production, or because of the fact that the transition period from autarchy to free trade is a matter of fact.

Output and employment perspectives implied by trade liberalization in a common economic space appear as a major field of research. E. Petit provides general equilibrium estimates of the welfare gains and unemployment changes that may be expected from the single European market. He uses a multi-country, multi-sector applied model with imperfect competition based on Mercenier. The novelty is to enrich the model with an unemployment rate that is determined endogenously in an efficiency-wage framework. Introducing imperfection in the labor market allows the author to exhibit new features on the consequence of integration on employment in Europe.

M. Gasiorek assesses the paths of factor prices and welfare as trade is liberalized, via reduction in trade transport costs, within a general equilibrium model consisting of a perfectly competitive sector, an imperfectly competitive sector producing under conditions of increasing returns to scale and a sector producing the resources employed in trading. It is not the case that trade liberalization entails monotonic changes in factor prices and welfare. The introduction of trade costs is an important step in trying to improve the realism of the theoretical literature on the gain from trade.

The paper of G. Fuchs gives support to those who consider that progressive liberalization can have more virtues than a brutal elimination of all trade barriers. Traditional models of international trade favor free trade as an optimal organization but do not examine the question of the "acceptability" of free trade in term of majority support – especially for example for countries where social rigidities such as a minimal wage prevail, free trade may generate unemployment and be rejected on this basis. Too often the classical literature ignores the problem of the redistribution of income induced by trade. In the framework of a very simple model (two zones, two factors of production, two goods), where a system of quota permits the analysis of a continuum of situations between autarky and free trade, it is shown that many configurations occur where there exists a maximal level of import, maximal meaning with respect to a progressive opening of the economy with at each step majority approval. It is shown also that when a dynamic process is introduced where unskilled manpower is trained over time, then, after a sufficient lapse, the pure free trade situation may be obtained and accepted.