The University of Nottingham

GEP Leverhulme Centre for Research on Globalisation and Economic Policy

Newsletter

Issue 22 Summer 2007

In this issue:

www.gep.org.uk

GEP to open branch in Malaysia

The Globalisation and Economic Policy Centre is to practise its own form of globalisation by opening a GEP branch at the University of Nottingham's Malaysia campus.

'GEP in Malaysia' will be officially launched by the Vice-Chancellor, Sir Colin Campbell, at a ceremony at the purpose-built Semenyih campus, 30km from Kuala Lumpur, in January 2008.

GEP Centre Director, Professor David Greenaway said: "The Malaysia Campus was the first ever branch campus of a UK University abroad. The campus serves an international community of students from more than 50 countries with Nottingham's high educational standards. Opening up a branch of GEP in Malaysia will help us develop exciting research opportunities for GEP staff to generate and study new sources of data in Malaysia that could shed light on issues that affect many other countries in Asia and across the world."

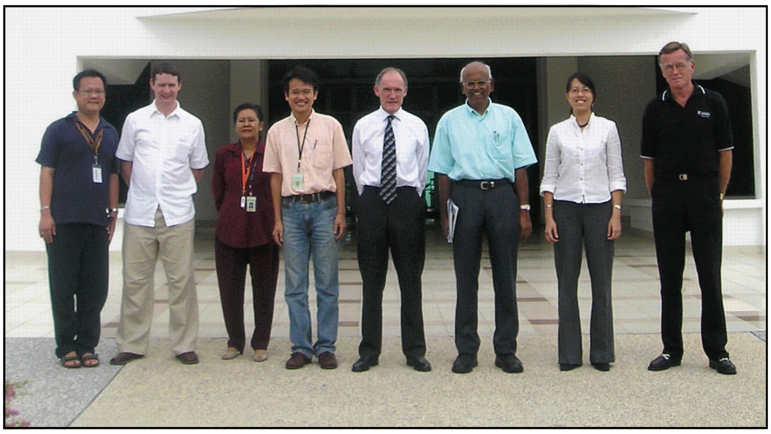
The launch will coincide with a two-day GEP conference at the Campus on "Asian Regionalism: Responding to Globalisation and China", on 16th and 17th January.

This Conference will include two keynote lectures, by Professor Richard Baldwin (Graduate Institute of International Studies, Geneva) and Professor Kym Anderson (World Bank and University of Adelaide), who will present the 2008 *The World Economy Annual Lecture*.

University of Nottingham speakers will be Daniel Bernhofen, Chris Milner, Shujie Yao and Zhihong Yu; and Lee Chew Ging from the Malaysia campus. Other international speakers will be: Ahmad Zubaidi Baharumshah, University Putra Malaysia;

University of Nottingham's Malaysia Campus

GEP to open branch in Malaysia



GEP's new branch collaborators

Peter Egger, University of Munich; Tomohiko Inui, Nihon University; Noor Aini Khalifah, Universiti Kebangsaan, Malaysia; Innwon Park, Korea University; Richard Pomfret, University of Adelaide; Euston Quah, Nanyang Technological University, Singapore; Shandre Thangavelu, National University of Singapore; Wing Thye Woo, University of California at Davis, and Eden Yu, City University Hong Kong.

Dr Cassey Lee, Associate Professor of Industrial Economics, at the Malaysia Campus, says the conference will be extremely useful. He said: "GEP's resources and network of researchers put it in a unique position to organise an event like this. The GEP Conference will provide an opportunity for scholars and policymakers in Malaysia to access and examine the latest research on trade-related issues."

The Globalisation Conference and GEP launch will be preceded by a Schools Conference at the Malaysian Campus, similar to the successful Sixth Form GEP conference held in Nottingham in July (featured on page 11 of this Newsletter).

GEP Conference at the University of Nottingham in Malaysia

16th and 17th January 2008 to include two Public Lectures:

Inaugural University of Nottingham in Malaysia Annual Globalisation Lecture

Richard Baldwin, Graduate Institute of International Studies, Geneva on 'The Three Bloc Dance'.

The World Economy Annual Lecture

Kym Anderson, University of Adelaide and World Bank on 'Agricultural Policies and Economic Development'.

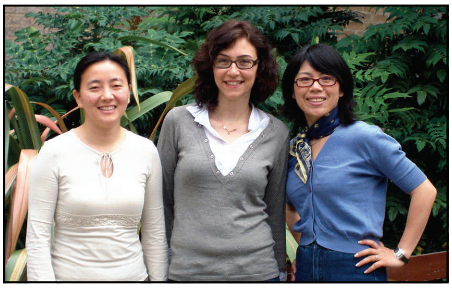
GEP News

Three new researchers join GEP

GEP has appointed three new Early Career Research Fellows, each taking up a two-year position:

Liza Jabbour, was formerly a PhD student at the Centre d'Economie de la Sorbonne. Her research topics include outsourcing, offshoring, multinational firms, industrial development, intellectual property rights and innovation.

Yundan Gong recently completed a PhD, *Essays on Firm Level Adjustment to Globalisation in China*, at the Nottingham University Business School. Her research focuses on industrial economics, particularly related to China, international trade and profitability and productivity analysis.



Xufei (Florence) Zhang, Liza Jabbour and Yundan Gong.

Xufei (Florence) Zhang takes up her Fellowship after submitting a GEP-sponsored PhD thesis, *Exchange Rates and Exports: Evidence from Manufacturing Firms in the UK*. Her fields include international trade and firm level adjustment to globalisation.

Teenagers step into world leaders' shoes

More than 200 students got a taste of some of the challenges facing world leaders when GEP hosted a prestigious conference for sixth-formers.

Teenagers from across Britain were invited to take part in a simulation in which they represented rich, poor and middle-income nations in a two-hour trading game designed to highlight the principles of global economics.

The exercise followed a morning of lectures from the GEP staff including GEP Director David Greenaway, who discussed the pros and cons of globalisation, and Associate Professor Richard Kneller, who spoke about the relationship between globalisation and economic growth.

Students from Nottinghamshire, Derbyshire, Leicestershire, Lincolnshire, South Yorkshire and Buckinghamshire took part in the day-long event on 26 June.

It proved so popular that next year's event will be run on two days to avoid over-subscription and allow more schools to take part.

Professor Dani Rodrik kicks-off Public Lectures Series

Professor Dani Rodrik, Professor of International Political Economy at Harvard University, starts GEP's public lecture programme for the coming months.

Professor Dani Rodrik

Professor Rodrik, whose work focuses on what constitutes sound economic policy and why some governments are better than others at adopting it, will deliver a lecture entitled *Saving Globalisation from its Cheerleaders* on 18 October.

On 15 November the guest speaker will be Professor Paul Collier, Professor of Economics at Oxford University. His Lecture, *The Bottom Billion*, will be based on his new book of the same title.

Udo Kreickemeier

Surely You Would Rather Work for a Successful Firm

More productive firms tend to pay higher wages and, therefore, attract many workers. However, not all workers will get their most preferred employment. With firm-specific wage rates, globalisation has previously unnoticed distributional implications. In this article, **Udo Kreickemeier** (Associate Professor in Economics and GEP Research Fellow, University of Nottingham) summarises the intuition and main results of his new research paper (co-authored by Hartmut Egger, University of Zurich and GEP External Research Fellow) on trade effects in the context of heterogeneous firms.

It is by now well established that firms in all sectors of the economy are heterogeneous with respect to key variables including productivity and size. There is strong evidence that this heterogeneity is also reflected in the export pattern across firms: Even in sectors that feature a lot of imports and exports, there are typically many small producers that only serve the local market. The exporters on the other hand tend to be the large and productive firms.

Trade theorists have struggled to come up with a model that accommodates the available evidence on firm heterogeneity. The most prominent, and arguably the most successful, outcome of this struggle, the model of Melitz (2003), suggests that firm heterogeneity is the source of a new type of gains from trade: Globalisation, by introducing foreign competition in each market, makes it tough for the least productive firms to survive, and they have to close down. The most productive firms gain and become larger, because for them it is worthwhile to incur the exporting cost and serve the larger world market. As a result, aggregate productivity goes up and so does welfare.

A seemingly straightforward question to ask in the context of the Melitz model, with its successful and unsuccessful firms that fare differently in the globalisation process, is the following: would you rather work for a successful or an unsuccessful firm? It seems natural to expect that workers should give preference to successful, i.e. high-productivity, firms. Perhaps surprisingly, a preference of this type would have no foundation in the model: a (rational) worker in the Melitz world would simply not care. This is because all firms pay the same wage and there is full employment.

Egger and Kreickemeier (2006) take the Melitz model as a starting point and develop a framework in which firm performance *does* matter for workers because more successful firms pay higher wages. This is possible because the labour market is imperfectly competitive, resulting in rent-sharing at the firm level. In this framework it is rational for workers to strive for a job in a successful firm. There is furthermore strong empirical support for the idea that larger, more productive producers indeed pay higher

It seems natural to expect that workers should give preference to (…) high-productivity firms. Perhaps surprisingly (…) a (rational) worker in the Melitz world would simply not care.

wages (Blanchflower, Oswald and Sanfey, 1996; Bayard and Troske, 1999).

Given that there is now a real benefit from working in a successful firm, why is it that not everybody is rushing to do just that? Also, how do the less successful firms that pay lower wages find workers? In the model of Egger and Kreickemeier, only some workers are lucky enough to find high-wage employment with the most productive firms. All firms ration employment, and those workers who are less lucky will end up with a less well paid job in a less productive firm. The most unlucky ones end up with no job at all. Firms do not lower wages, because this would jeopardise their existing employees' morale, thereby harming profits. A mechanism of this sort, which has been introduced into the theoretical literature by Akerlof and Yellen (1990) under the name "Fair Wage-Effort Hypothesis", is strongly supported by experimental as well as survey evidence (Bewley, 2005).

At the aggregate level, the model of Egger and Kreickemeier gives a simple theoretical framework that features equilibrium unemployment and wage differentiation between different firms, even if all workers are *ex ante* identical. In this setting, the selection effects identified by Melitz (2003) still lead to an increase in overall welfare, but globalisation now has distributional implications that would be considered undesirable by most: It gives rise to an increase in unemployment and an increase in *intra-group* wage inequality.

[Globalization] gives rise to an increase in unemployment and an intra-group wage inequality.

The link between the increase in aggregate output (and therefore welfare) on the one hand, and the increase in unemployment on the other hand is quite naturally provided by the increase in average productivity: firms that are on average more productive can produce a larger total output and at the same time employ fewer workers. This rather intuitive mechanism sheds new light on the impact of international competition on domestic employment – an issue which is a prime concern to policy makers and the general public alike.

The effect on intra-group wage inequality is notable for two reasons. First, there is strong empirical evidence across many countries that intra-group wage inequality is important and has increased (Barth and Lucifora, 2006). Second, although the observed increase in intra-group wage inequality has been parallel to the recent surge in intermediate goods trade the suggestion of a theoretical link between this two phenomena has previously been absent in the literature, which has primarily been concerned with inter-group wage inequality (between skilled and unskilled workers).

There are obvious ways in which the framework suggested by Egger and Kreickemeier (2006) can be extended in a number of directions. For one, it would be potentially fruitful to introduce trade policy instruments into the model and to look at their effect on welfare and the labour market. Another promising area for future research is the addition of a second factor of production that would allow the simultaneous discussion of within-group and between-group wage inequality.

Further Readings

Akerlof, G., Yellen, J. (1990), The Fair Wage-Effort Hypothesis and Unemployment, *Quarterly Journal of Economics*, vol. 105, pp. 255-283.

Barth, E., Lucifora, C. (2006), Wage Dispersion, Markets and Institutions: The Effects of the Boom in Education on the Wage Structure, *IZA Discussion Paper* 2181.

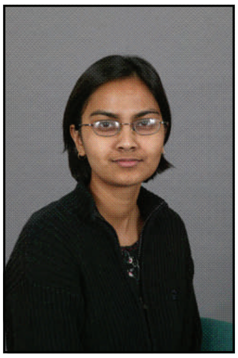
Bayard, K., Troske, K.R. (1999), Examining the Employer-Size Wage Premium in the Manufacturing, Retail Trade, and Service Industries Using Employer-Employee Matched Data, *American Economic Review* , vol. 89, pp. 99-103.

Bewley, T. (2005), Fairness, Reciprocity, and Wage Rigidity, in: Gintis, H., Bowles, S., Boyd, R., Fehr, E. (Eds.), Moral Sentiments and Material Interests: The Founda-tions of Cooperation in Economic Life. Cambridge/Mass., MIT Press, pp. 303-338.

Blanchflower, D.G., Oswald, A.J., Sanfey, P. (1996), Wages, Profits, and Wage Sharing, *Quarterly Journal of Economics* 111, 227-251.

Egger, H., Kreickemeier, U. (2007), Firm Heterogeneity and the Labour Market Effects of Trade Liberalisation, *GEP Research Paper* 2006/26.

Melitz, M.J. (2003), The Impact of Trade on Intra-Industry Reallocations and Aggregate Industry Productivity, *Econometrica* 71, 1695-1725.



Harshana Kasseeah

What Determines the Leverage Decisions of Chinese Firms?

The winner of the 2007 Conference of the Chinese Economic Association (CEA) UK Best Paper Award (2nd Prize) was **Harshana Kasseeah**. In this article Harshana summarises the main findings of her paper. Harshana is finishing a GEP-sponsored PhD thesisis at the University of Nottingham and her research focuses on the effect of financial constrains on the financing of firms in the UK and China.

Leverage measures the level of indebtedness of a firm. According to the pecking order theory as proposed by Myers and Majluf (1984), when firms need financing, they first use their internal funds, followed by debt and turn to equity as a last resort. Financing of firms in China is an interesting topic. Property rights are not well-defined and the financial system in China is not very efficient. The bond market is under-developed and firms are not able to issue new shares to raise capital as there are a number of restrictions imposed on them. However, despite this, China is the fastest-growing developing and transition economy in the world. This challenges the view that financial system development is an essential pre-requisite for growth.

The overall leverage [of Chinese firms] (...) is lower than Anglo-American firms and firms in Continental Europe. (...) It is also low when compared to firms in countries such as India, Thailand and Malaysia. [Moreover, Chinese firms] borrow more short term than long term.

The main issue that I investigate is whether the financing of Chinese firms is significantly different from their western counterparts. The dataset used is the China Stock Market and Accounting Research Database (CSMAR) that contains data on firms listed on the Shenzhen and Shanghai Stock Exchanges. This study is limited to the leverage decisions of only listed manufacturing firms over the 1994-2004 period. Leverage is defined as the sum of short term debt and long term debt where short term debt is debt with a maturity of less than one year while long term debt is debt with a maturity of more than one year.

We find that for the sample of firms that we have, the overall leverage (sum of short-term and long-term debt) is at 22% which is lower than Anglo-American firms and firms in Continental Europe (for example 27% for American and Italian firms according to Rajan and Zingales, 1995). It is also low when compared to firms in countries such as India, Pakistan, Thailand and Malaysia (67.1%, 65.6%, 49.4%, 41.8% respectively as documented by Booth et al, 2001). Another interesting feature is that these firms borrow more short term than long term as shown in Figure 1 above. This implies that either firms do not want to borrow long term or lenders do not want to lend long term.

The empirical specification that has been widely used in the literature and that I use in this study is from Rajan and Zingales (1995), where the ratio of leverage over assets is regressed on lagged leverage over assets, profitability, collateral, size and a growth measure. Profitability is measured as the ratio of net profit over assets, size is proxied for by the log of sales, collateral is measured as the ratio of tangible assets to total assets while the growth measure used is the growth in sales. All estimations are performed using the Arellano and Bond (1991) GMM estimator. Rather than concentrating on the signs of the coefficients, my focus is on the significance of the coefficients. The results that I obtain suggest that the leverage of listed Chinese manufacturing firms is influenced by their profitability and size while other variables like collateral and growth opportunities do not influence their leverage.

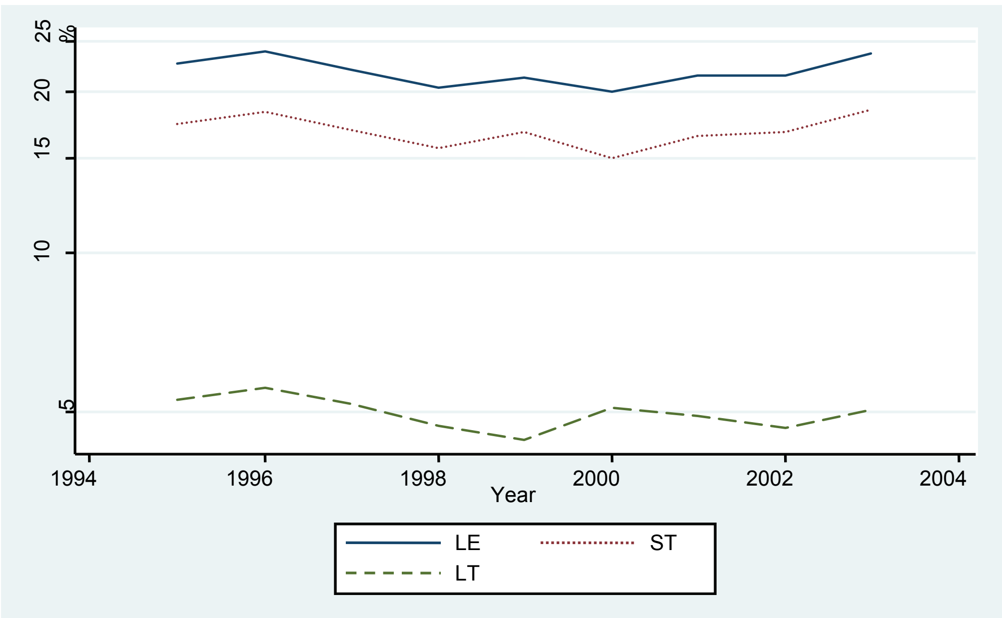
To further examine the leverage decisions of these firms, with particular emphasis on the sensitivity of leverage to profitability, I use a number of China-specific variables to distinguish among firms.

- I first take into account the location of a firm. China has many provinces and each province can operate as an independent state. These provinces can be sub-divided into three regions: the Eastern region, the Central region and the Western region. The Eastern region, due to its geographical positioning attracts much more productive resources and is more developed than the Central and Western regions. The results suggest that developments gaps among the Eastern, Central and Western provinces do not seem to influence the leverage decisions of Chinese firms. However, these results should be interpreted cautiously as I am here focusing solely on the behaviour of listed manufacturing firms that are only a tiny sample out of the population of Chinese firms.

- Second, I take into account the amount of FDI that different provinces receive. In the case of China, FDI could potentially act as an alternative source of financing, especially as the importance of FDI in China has been emphasized in the literature. Unfortunately, I do not have firm-level FDI so I use provincial level FDI obtained from the various issues of the China Statistical Yearbooks as a proxy to measure the level of FDI that a particular firm might be receiving. I hypothesize that the leverage of firms located in high FDI provinces would be less sensitive to their profitability while the leverage decisions of firms that are located in low FDI provinces would be more sensitive to their profitability. The results suggest that the leverage of firms that are located in high FDI provinces are not affected by their profitability, while profitability is an important determinant of the leverage decisions of firms located in low FDI provinces.

- Third, I account for the level of state intervention in the leverage decisions of the sample of Chinese firms that I examine. China was previously a communist economy where state intervention in firms' decisions was the norm. Although I do not have a variable to directly measure the level of state intervention in these firms, the dataset contains a subsidies variable, which is defined as "various subsidies received by a company such as subsidy for loss due to government policies and refund of value-added tax." I classify firms as either receiving high subsidies, or receiving low subsidies. The leverage of firms that receive high subsidies is expected to be less sensitive to their

Evolution of total (LE), short term (ST) and long term (LT) leverage of Chinese manufacturing firms, 1994-2004



What Determines the Leverage Decisions of Chinese Firms?

profitability (as subsidies are here acting as an additional source of financing). On the other hand, the leverage of firms which receive low subsidies is expected to be quite sensitive to their profitability. I find evidence suggesting that the level of subsidies obtained influences the leverage decisions of firms: the leverage of firms that receive high subsidies is in fact not affected by their profitability.

The accession of China to the World Trade Organisation (WTO) was an important event for Chinese firms especially for export-orientated firms as this implied that these firms could freely access their huge markets in the US. I examine whether this event has had any effect on the leverage decisions of Chinese firms by examining the leverage decisions of firms pre-WTO accession and post-WTO accession. I do not find any significant differences in the financing patterns of firms before or after this event suggesting that the WTO effect could possibly be a long term phenomenon.

In conclusion the results suggest that the single main determinant of leverage decisions of Chinese firms is the profitability of these firms. However, I find that for firms that are located in high FDI recipient provinces and that receive high subsidies, their leverage is not sensitive to their profitability. In addition, I find that the location of these firms does not influence the sensitivity of their leverage decisions to profit. This is probably due to the fact that the firms in my dataset are large and well-known firms. Hence the conclusion that can be drawn is that in some aspects Chinese firms are quite similar to their western counterparts while in other aspects they are quite unique.

Further Readings

Booth, L, Aivazian, V, Demirguc-Kunt, A, and Maksimovic, V., (2001). Capital structures in Developing Countries, The Journal of Finance, vol. LVI, pp. 87-130.

Myers, S., and N. Majluf. (1984). 'Corporate Financing and Investment Decisions when Firms have Information that Investors do not have.' Journal of Financial Economics, vol. 13, pp. 187-221.

Rajan, R., and Zingales, L., 1995. What Do Know about Capital Structure? Some Evidence from International Data, The Journal of Finance vol. 50, pp. 1421-1460.

GEP Forthcoming Conferences

GEP Schools Conference at the University of Nottingham Malaysia

15th January, Malaysia

Convenor: David Greenaway (GEP, University of Nottingham).

GEP Forthcoming Conferences

‘Globalisation and Migration’

19th October 2007, University of Nottingham

Speakers include:

- Marta Aloi (GEP, University of Nottingham)
- Giovanni Facchini (University of Illinois)
- Timothy Hatton (University of Essex)
- Tom Ivlevs (GEP, University of Nottingham)
- Willi Kohler (Eberhard Karls University, Tuebingen)
- Sharun Mukand (Tufts University)
- Giorgio Barba Navaretti (Universitâ degli Studi di Milano)

Conference Organizers: Daniel Bernhofen (GEP, University of Nottingham) and Giovanni Facchini (University of Illinois).

Leverhulme Globalisation Lectures

Paulo Collier, University of Oxford on 'The Bottom Billion'

15th November 2007, University of Nottingham

David Smith, Economics Editor of *The Sunday Times* on 'China and India'

4th December 2007, University of Nottingham

Danny Blanchflower, Dartmouth College and Bank of England Monetary Policy Committee

30th January 2008, University of Nottingham

Martin Wolf, Associate Editor and Chief Economics Commentator of *The Financial Times*

27th February 2008, University of Nottingham

Jo Morgan

Conference Report: Globalisation for Teenagers

In June GEP hosted its Sixth Form Conference on Globalisation. The event attracted teenager students from different parts of the UK . In this conference report **Jo Morgan** comments on the lectures and events included in the Conference's programme.

On June 26th 2007, GEP sponsored a sixth form conference on globalisation. Its purpose was to provide a stmulating and informative day for sixth formers from schools and colleges in counties from as far afield as Buckinghamshire. This venture, following last year's successful first conference, also allowed students to experience a taste of what it would be like to study economics at university.

The Programme of the lectures and events was as follows:

Globalisation: Opportunity or Threat?
David Greenaway

Trade and the Environment
Tim Lloyd

Globalisation and Growth
Richard Kneller

Transforming China and India: Challenges and Opportunities
Chris Milner

International Trade Game
Wyn Morgan

Against the backcloth of long term trends in globalisation, David Greenaway evaluated its benefits (which include more efficient use of resources, wider consumer choice and a stimulus to growth). Against this, however, has to be set appropriate consideration of adjustment issues and in particular those which result in workers being displaced. He then outlined the kinds of policies can be put in place which help smooth adjustment.

Tim Lloyd's lecture introduced students to the debate surrounding the impact of economic growth on the environment, challenging the view that growth leads to environmental degradation. Presenting theoretical and empirical evidence, he explained the role of markets in changing the relationship between growth and pollution as per capita income rises. On a more cautionary note, he argued that climate change represents a new kind of threat. Citing Sir Nicholas Stern's recent Climate Change Review, he emphasised the vital contribution economists can make to our understanding of global warming and the mechanisms via which potentially catastrophic projections can be averted.

Richard Kneller's talk was about the relationship between globalisation and economic growth. This relationship is important because it helps us understand differences in income levels between countries. It turns out that the evidence is mixed. It is possible to find countries such as Ireland and China that have become heavily globalised and grown very strongly, whereas others such as Argentina or countries in Africa that appear to have chosen the same set of policies towards globalisation yet have not grown quickly. Or if one takes a very rich country such as the US then you find that as the extent of its globalisation has risen, its growth rate has remained static, but in periods where policy has been against

Conference Report: GEP Sixth Post-Graduate Conference

globalisation its growth rate has fallen. All this suggests both economists and anti-globalisers are wrong: both provide a false message on the effect of globalisation on growth.

The afternoon session, organised by Wyn Morgan, took a very different approach to the morning. The students were organised into groups (unknown to them based on whether they were "rich", "poor" or "middle income" countries) and they spent the next two hours playing a trading game based on the principles of micro and international economics.

Chris Milner's talk on 'Transforming China and India: Challenges and Opportunities' explored the recent rapid integration of these two giant economies into the world economy, drawing attention to both the similarities and differences in the nature and impacts of their respective globalisation experiences. It considered also the structural and employment adjustment challenges for the UK and other industrial countries of rapid growth of China and India's exports, and the trade, investment and outsourcing opportunities created for industrial and developing countries of the growth of their economies.

The afternoon session, organised by Wyn Morgan, took a very different approach to the morning. The students were organised into groups (unknown to them based on whether they were "rich", "poor" or "middle income" countries) and they spent the next two hours playing a trading game based on the principles of micro and international economics. Students had to produce outputs using their differing endowments of capital and raw materials and then sell them onto the world market. As the game developed and it became clear all groups were not equal, bargaining and alliances started to be formed and as prices for the outputs changed the competition became ever more intense. While there was eagerness to see who had won, the main outcome was that students got to see key concepts in economics in action such as comparative advantage, price elasticity, imperfect competition and so forth. As for the result, not surprisingly the "rich" countries came out on top!

The theme of globalisation was a prime factor in the popularity of the conference as it now features strongly in the A level syllabus. Teachers were glad to have some extra input on this subject for their students, and all the talks were uploaded on the Leverhulme website to be accessible to all those who attended.

Feedback from both students and teachers was extremely favourable and everyone found it a valuable event, not only for the content of the lectures but also for the experience of coming to a university and being a student for the day. Nigel Bartlett from the Royal Grammar School in High Wycombe wrote: *A common apprehension, prior to the conference, amongst some of the students was that they would not understand university economics, having studied the subject for only a matter of months. These fears were allayed and a general consensus was that the boys were impressed both by the enthusiasm yesterday's speakers displayed for their subjects and their fluency of communication.*

GEP will repeat this event again next year. As demand was so high this year and we had to turn away some schools due to lack of space, the event may be run on two dates in future in order to accommodate more participants. In addition, given the establishment of a branch of GEP at the University's campus in Malaysia, a Conference for Schools will take place there in January 2008.

GEP will repeat this event again next year. As demand was so high this year and we had to turn away some schools due to lack of space, the event may be run on two dates in future in order to accommodate more participants. In addition, given the establishment of a branch of GEP at the University's campus in Malaysia, a Conference for Schools will take place there in January 2008.

Daniel Bernhofen

Ray Riezman

Conference Report: New Directions in International Trade Theory

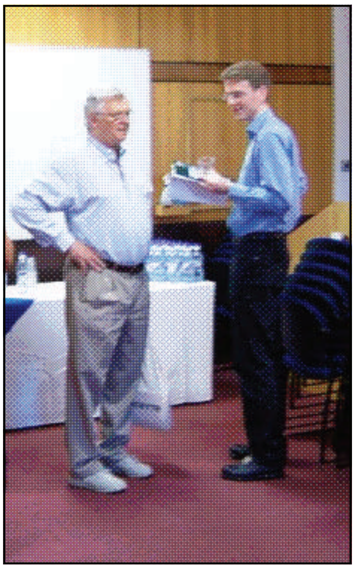
In June GEP hosted its residential conference on what are the new directions in International Trade Theory. In this conference report the organisers **Daniel Bernhofen** and **Ray Riezman** comment on the themes of the papers presented and their main findings. Daniel is Leverhulme Professor of International Economics, GEP, University of Nottingham and Ray is Henry B. Tippie Research Professor of Economics, University of Iowa, and GEP External Research Fellow.

This year's residential GEP conference took place on 8-9 June, 2007 and was organized by the Theory and Methods Programme under the theme of "**New Directions in International Trade Theory**". The conference participants came from Europe, North America and Asia. The 10 speakers were Peter Neary (Oxford University), Eric Bond (Vanderbilt University), James Anderson (Boston College), Udo Kreickemeier (University of Nottingham and GEP), John Whalley (University of Western Ontario), Yunfang Hu (Kobe University), Ronald Jones (University of Rochester), Carsten Kowalcyk (Tufts University), Mark Gibson (Washington State University) and Daniel Bernhofen (University of Nottingham and GEP).

The paper discussants were Arijit Mukherjee (University of Nottingham and GEP), Rod Falvey (University of Nottingham and GEP), Daniel Seidman (University of Nottingham), Peter Neary (Oxford University), Spiros Bougheas (University of Nottingham and GEP), Ronald Jones (University of Rochester), Jim Anderson (Boston College), Eric Bond (Vanderbilt University), Doug Nelson (Tulane University and GEP) and Catia Montagna (University of Dundee).

The conference was launched by two papers that focused on multi-lateral trade agreements. Peter Neary's paper (co-authored with Dermot Leahy) on **Multi-lateral subsidy games** examines the rationale for multi-lateral agreements to limit investment subsidies. This work is motivated by the prevalence of R&D subsidies within the European Union and the commonly held policy viewpoint that state aid in form of investment subsidies is more benign than aid in the form of production or export subsidies. The paper identifies several key factors which determine whether national governments have incentives to over- or under-subsidize from the point of view of union welfare.

In **Paths of self-enforcing trade agreements** Eric Bond adds to the discussion on whether preferential trade agreements are 'stumbling' or 'building blocks' towards a multilateral trade agreement by noticing that trade agreements must be enforceable. In most cases, "negotiated transfers" are promises on concessions (i.e. labour standards etc.) and



Ronald Jones and Udo Kreickemier

these promises can be broken. Bond's paper investigates expansion paths that go from bilateral to global agreements in the presence of no deviation constraints on transfers.

Traditionally, international trade theory has focused on the causes and consequences of international exchange without paying much attention to the institutional foundations that sustain international trade. In **Does trade foster contract enforcement?** Jim Anderson develops a model where trade can have positive and negative knock-on effects on institutional development. This model is capable of providing a possible explanation for the post 1500 divergence in institutional developments in Europe and China and also for more recent institutional developments in low-income and transition economies.

Udo Kreickemeier's paper (co-authored with Rod Falvey) on **Tariff reforms with rigid wages** extends the literature on the welfare and market access effects of tariff reforms by incorporating unemployment caused by rigid wages. The authors derive welfare increasing trade liberalizing strategies. A key result of their paper is that the tension between welfare and market access increasing reforms may be diminished if there are unemployment effects.

John Whalley's paper (co-authored with Hui Huang and Shunming Zhang) on **Exploring policy options in joint intertemporal-spatial trade models using an incomplete markets approach** develops and calibrates a computable general equilibrium model in which intertemporal intermediation services can only be provided by domestic firms. The authors identify the case for an optimal trade intervention for a small open economy when services remain unliberalized.

Yunfang Hu (in co-authorship with Murray Kemp and Koji Shimomura) develops **A multi-country dynamic Heckscher-Ohlin model with physical and human capital accumulation**. The authors investigate the relationships between long-run growth rates and trade and show how international differences in the efficiency of educational services can impact the pattern of international trade.

In **International models and real world features**, Ronald Jones (in co-authorship with Sugata Marjit) argues that competitive trade theory models are quite capable of explaining real world features like the increasing degree of international fragmentation of production. In competitive "middle product models" a heterogeneous labour force can be shown to produce the necessary "service link activities" which are required for the international fragmentation of production.

Carsten Kowalczyk's paper (co-authored with Ray Riezman) **Free trade: what are the terms-of-trade effects?** examines how trade policy agreements affect national welfare through terms-of-trade or volume-of-trade (or efficiency) effects. Building on the authors' prior work which has shown that global welfare can be reached if agreed side payments equal the terms-of-trade effects, this paper applies a computable general equilibrium model to estimate the magnitude of these terms-of-trade effects.

Mark Gibson's paper (co-authored with Claustre Bajona, Timothy Kehoe and Kim Ruhl) on **Trade liberalization, growth and productivity** is motivated by the popular perception that trade theory predicts that trade liberalization leads to a growth in a country's GDP. The authors shows that although all trade models predict that trade liberalization will increase national welfare; it will not necessarily increase a country's real GDP.

Daniel Bernhofen's paper **Predicting the pattern of international specialization in the neoclassical trade model model: A synthesis** aims to provide a unified framework for pattern of trade predictions in formulations of the neoclassical trade model that don't assume international factor price equalization. A key message of this paper is that pattern of trade predictions are directly linked to efficiency

Conference Report: New Directions in International Trade Theory (cont.)

gains. This means that if empirical tests confirm these predictions, they provide implicit evidence for aggregate efficiency gains resulting from international specialization.

Participants of the GEP Conference on New Directions in International Trade Theory.

All conference papers can be downloaded from the GEP conference website. Following some revisions, the papers are scheduled to appear in a special issue of Economic Theory with Daniel Bernhofen and Ray Riezman serving as the journal's guest editors.

Overall, the conference was characterized by well-organized presentations, thought provoking comments of assigned discussants and stimulating general audience discussions. The days' activities were rounded up by two conference dinners and a visit to a local Nottingham micro brewery accompanied by a sampling of the brewery's tasty beer.

The World Economy Annual Lecture

Dani Rodrik, Professor of International Political Economy, Harvard University

'Saving Globalisation From Its Cheerleaders'

18th October 2007, University of Nottingham.

New GEP Research Papers

http://www.gep.org.uk/research_papers

2007/28	Mirabelle Muûls and Mauro Pisu	Imports and exports at the level of the firm: Evidence from Belgium

Summary: This paper extends the stylised facts of international trading activities of firms offering a complete view of their export and import decisions. Our results point to the fact that companies that both export and import have superior characteristics than non-traders.

2007/27	Pedro E. Moncarz and Marcel Vaillant	MERCOSUR's role on the regional patterns of imports of its country members: a dynamic panel data approach

Summary: The results show that tariff preferences under MERCOSUR affected imports patterns in Argentina and Uruguay, to a less extent also those of Brazil and Paraguay. For the first two countries evidence of trade diversion is also found.

2007/26	Jürgen Bitzer, Ingo Geishecker and Holger Görg	Productivity spillovers through vertical linkages: Evidence from 17 OECD countries

Summary: This paper uses industry level data for 17 OECD countries to investigate the importance of horizontal and vertical spillovers. Results show that there is evidence for spillovers through backward linkages between multinationals and domestic firms for all countries, but that this effect is much higher for CEEC than other OECD countries.

2007/25	Rod Falvey, David Greenaway and Zhihong Yu	Market Size and the Survival of Foreign-Owned Firms
2007/24	Alexander Hijzen and Paul Swaim	Does Offshoring Reduce Industry Employment?
2007/23	Pedro Moncarz and Michael Bleaney	Trade Liberalization and the Spatial Distribution of Economic Activity Within A Country
2007/22	Arijit Mukherjee and Kullapat Suetrong	Unionisation structure and strategic foreign direct investment
2007/21	Arijit Mukherjee and Kullapat Suetrong	Privatisation, strategic foreign direct investment and the host country welfare
2007/20	Marta Aloi, Manuel Leite-Monteiro and Teresa Lloyd-Braga	Unions and Globalisation
2007/19	Shujie Yao and Chunxia Jiang	The Effects of Governance Changes on Bank Efficiency in China : A Stochastic Distance Function Approach
2007/18	Sourafel Girma, Holger Görg and Aoife Hanley	R&D and Exporting: A Comparison of British and Irish Firms
2007/17	Peter Egger and Douglas Nelson	How Bad is Antidumping?: Evidence from Panel Data
2007/16	Holger Görg, Oliver Morrissey and Manop Udomkerdmongkol	Investment and Sources of Investment Finance in Developing Countries
2007/15	Roberto Alvarez and Holger Görg	Multinationals as Stabilizers?: Economic Crisis and Plant Employment Growth

New GEP Research Papers (cont.)

http://www.gep.org.uk/research_papers

2007/14	Alexander Hijzen, Tomohiko Inui and Yasuyuki	Does Offshoring Pay? Firm-Level Evidence From Japan
2007/13	David Greenaway, Richard Kneller and Xufei Zhang	Exchange Rates and Exports: Evidence from Manufacturing Firms in the UK
2007/12	Richard Kneller and Mauro Pisu	Export Barriers: What Are They and Who Do They Matter To?
2007/11	Daniel M. Bernhofen	Predicting the Factor Content of Foreign Trade: Theory and Evidence
2007/10	David Greenaway, Joakim Gullstrand and	Live or Let Die? Alternative Routes to Industry Exit
2007/09	Andrew Burke, Holger Görg and Aoife Hanley	The Impact of Foreign Direct Investment On New Firm Survival in the UK : Evidence For Static v. Dynamic Industries
2007/08	Martyn Andrews, Lutz Bellmann, Thorsten Schank and Richard Upward	The Takeover and Selection Effects of Foreign Ownership in Germany : An Analysis Using Linked Worker-Firm Data
2007/07	Richard Kneller	Exporters and International Knowledge Transfer: Evidence From UK
2007/06	Paulo Bastos and Manuel Cabral	The Dynamics of International Trade Patterns
2007/05	Dermot Leahy and Catia Montagna	'Make-or-Buy' in International Oligopoly and the Role of Competitive
2007/04	Richard Kneller and Mauro Pisu	The Returns to Exporting: Evidence from UK Firms
2007/03	Holger Görg, Hassan Molana and Catia	Foreign Direct Investment, Tax Competition and Social Expenditure
2007/02	Daniel M. Bernhofen	On the Magic Behind David Ricardo's Four Mystical Numbers
2007/01	Alex Hijzen, Richard Upward and Peter Wright	Job Creation, Job Destruction and the Role of Small Firms: Firm-Level Evidence for the UK
2006/50	Marta Aloi and Teresa Lloyd-Braga	National Labour Markets, International Factor Mobility and Macroeconomic Instability
2006/49	Holger Gorg, Michael Henry, Eric Strobl and Frank Walsh	Multinational Companies, Backward Linkages and Labour Demand Elasticities
2006/48	Richard Kneller and Mauro Pisu	The Role of Experience in Export Market Entry: Evidence for UK Firms
2006/47	Shantanu Banerjee and Arijit Mukherjee	Joint Venture Instability Under Entry
2006/46	Simon Appleton, Lina Song and Qingjie Xia	Growing out of Poverty: Trends and Patterns of Urban Poverty in China 1988–2002
2006/45	Lina Song and Simon Appleton	Inequality and Instability: an Empirical Investigation into Social Discontent in Urban China.
2006/44	Holger Gorg, Michael Henry and Eric Strobl	Grant Support and Exporting Activity
2006/43	Sourafel Girma, Yundan Gorg, Holger Gorg and Zhihong Yu	Can production subsidies foster export activity? Evidence from Chinese Firm Level Data

Visitors to GEP in 2007

May 2007	June 2007	July 2007
Heather Booth di Giovanni *UK Trade and Investment* Professor Alan Deardorff *University of Michigan* Professor Jonathan Eaton *New York University* James Harrigan *NY Federal Reserve Bank* Professor Wilhelm Kohler *Eberhard Karls University Tübingen* Professor Xiaming Liu *Birkbeck College* Professor Jørgen Ulff-Møller Niel-sen, *Aarhus Business School* Jonathan Portes *Department of Work and Pensions* Ken Warwick *Department of Trade and Industry* Dr Niven Winchester *University of Otago*	Professor Ray Riezman *University of Iowa*	Dr. Naohiko Ijiri *Nihon University* Dr. Tomohiko Inui *Nihon University* Dr. Katsumi Matsuura *Hitotsubashi University*

October 2007	November 2007	December 2007
Professor Dani Rodrik *Harvard University* Professor Odd Rune Straume *University of Minho* Professor Nancy Chau *Cornell University*	Professor Paulo Collier *Oxford University* Professor Gabriel Felbermayr *Eberhard Karls University, Tubingen* Professor Dr. Josef Zweimuller *University of Zurich*	David Smith *Economics Editor , The Sunday Times*

GEP Researchers

Internal Research Fellows

Professor David Greenaway (Director), Dr Marta Aloi, Paulo Bastos, Professor Daniel Bernhofen, Dr Spiros Bougheas, Professor Richard Cornes, Agelos Delis, Dr Bouwe Dijkstra, Professor Rod Falvey, Dr Ben Ferrett, Dr Switgard Feuerstein, Dr Holger Görg, Dr Alessandra Guariglia, Dr Alex Hijzen, Dr Tom Ivlevs, Dr. Lisa Jabbour, Dr Richard Kneller, Dr Udo Kreickemeier, Professor Chris Milner, Dr Arijit Mukherjee, Professor Doug Nelson, Joana Silva, Professor Lina Song, Dr Richard Upward, Dr Peter Wright, Professor Shujie Yao, Dr Zhihong Yu.

External Research Fellows

Professor Bruce Blonigen (University of Oregon), Professor John Brown (Clark University), Professor Marius Brülhart (University of Lausanne), Professor Paul Collier (University of Oxford), Professor Carl Davidson (Michigan State University), Professor Alan Deardorff (University of Michigan), Dr Hartmut Egger (University of Zurich), Professor Peter Egger (University of Munich), Dr Robert Elliot (University of Birmingham), Professor Simon Evenett (University of St Gallen), Dr Joakim Gullstrand (Lund University), Professor Jonathan Haskel (Queen Mary, University of London), Professor Wilhelm Kohler (Eberhard Karls University), Dr Maurice Kugler (University of Southampton), Professor Steve Matusz (Michigan State University), Dr Daniel Mirza (University of Rennes), Dr Catia Montagna (University of Dundee), Professor Pascalis Raimondos-Møller (University of Copenhagen), Professor Ray Riezman (University of Iowa), Dr Frederik Sjøholm (Stockholm School of Economics), Professor Constantinos Syropoulos (Florida International University), Professor Mathew Tharakan (University of Antwerp), Professor Vitor Trindade (University of Missouri, Columbia), Professor Jim Tybout (Penn State University), Professor Rod Tyers (Australian National University), Professor Hylke Vandenbussche (Catholic University of Leuven), Professor Ian Wooton (University of Strathclyde), Dr Zhihao Yu (Carleton University)

Policy Associates

Mary Amiti (IMF), Kym Anderson (The World Bank), Bob Anderton (European Central Bank), Heather Booth di Giovanni (Department of Trade and Industry), Tony Clayton (Office for National Statistics), Cletus Coughlin (Federal Reserve Bank of St Louis), Adriaan Dierx (European Commission), Peter Dodd (DTI), Zdenek Drabek (World Trade Organisation), Andrew Gurney (HM Treasury), Tim Harcourt (Australian Trade Commission), Bernard Hoekman (The World Bank), Sébastien Jean (OECD), Nannan Lundin (Organisation for Economic Co-operation and Development), John Martin (Organisation for Economic Co-operation and Development), Beata Smarzynska Javorcik (The World Bank), Ken Warwick (Department of Trade and Industry)

Leverhulme Centre
for Research on Globalisation and Economic Policy

The Globalisation and Economic Policy Centre

GEP – the Globalisation and Economic Policy Centre – is the major centre in Europe studying the impacts of globalisation and economic policy, and one of the biggest of its kind in the world. The centre has an impressive international reputation; its academics have advised the Treasury, the OECD, the World Bank and WTO.

GEP was established in the School of Economics at the University of Nottingham in 2001. Its research and dissemination activities are structured around four Research Programmes, linked by the common theme of globalisation:

1. Theory and Methods
2. Globalisation and Labour Markets
3. Globalisation, Productivity and Technology
4. China and the World Economy

GEP supports both basic scientific and policy-focused research. Its core staff comprises a group of Research Fellows based at Nottingham, a network of External Fellows from a number of Universities in Western Europe, North America and Australia, and a Forum of Policy Associates based in the policy-making community. GEP publishes its own Research Paper Series, sponsors regular workshop programmes and conferences and supports a range of other outreach activities. For more information visit: **www.gep.org.uk**

GEP is substantially funded by grants from the Leverhulme Trust.

Further information

For more information on GEP and related research activities, please contact

Sue Berry
Leverhulme Centre for Research on Globalisation and Economic Policy
School of Economics
University of Nottingham
University Park
Nottingham NG7 2RD

Telephone: +44 (0) 115 951 5469

Email: sue.berry@nottingham.ac.uk

GEP Newsletter Editor: Joana Silva