Discussion of:
"The Cost of Non-Europe, Revisited"

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A Key Question

- what are the economic gains from the EU?
  - ▸ MVZ (2018): quantification of the trade-related gains relative to alternative scenarios
- two stages:
  1. gravity regressions
     - ★ regress bilateral trade on a number of FEs plus dummy for EU and other RTAs
     - ★ identify direct trade effect of EU
     - ★ both for goods and service
  2. counterfactual simulations
     - ★ use (1) + ACR (2012) formulas + estimates of trade elasticity
     - ★ evaluate trade and welfare effects of moving from EU to RTA or MFN
- additional counterfactuals
  - ▸ unilateral exit (Brexit), domino effects

General Comments

- great paper!
  - ▶ important question
  - ▶ very clean empirical analysis
  - ▶ state-of-the-art quantitative approach
  - ▶ very elegant

- my comments
  1. gravity: pros and cons
  2. structural approach: pros and cons
  3. results: interpretation and beyond

Gravity: Comments

- empirical analysis very solid and transparent
- bilateral trade explained by host of FEs
  - destination-time, origin-time, destination-origin
- and yet, EU has a large trade effect
  - *triples* trade
    - ⋆ effect much larger than what implied by fall in tariffs
- main advantages
  - EU dummy captures *all* aspects of integration
    - ⋆ can identify the effects of various EU treaties
- limits of gravity:
  - results somewhat sensitive to estimation method (OLS vs PPML)
  - once you remove the EU dummy, all the FEs will change, but how?
  - cannot be used for counterfactuals

Counterfactuals: Pros

- structural model
    - ▶ turns the EU dummy into GE counterfactuals
        - ★ "exact hat algebra"
    - ▶ turns trade effects into welfare (GFTs)
        - ★ "trade elasticity"
- elegant
    - ▶ a microfoundation for gravity
- simple
    - ▶ low data requirement
    - ▶ just need to solve a simple system of equations
- quite general
    - ▶ holds across different workhorse trade models (ACR, 2012; Costinot & Rodriguez-Clare, 2014)

Counterfactuals: Cons

- yet the "trade elasticity" is *not* estimated
- and model *is* restrictive
  - ► imports across firms/products are not Pareto
    - ★ can double the GFTs
    - ★ Head, Mayer & Thoenig (2014); Melitz & Redding (2015); Redding & Weinstein (2018)
  - ► distributions are not the same *across countries*
    - ★ 25% of US imports explained by differences in variances across origins
    - ★ Bonfiglioli, Crino' and Gancia (2018a,b), Redding & Weinstein (2018)
  - ► trade elasticity varies *across sectors*
    - ★ easy to accommodate, can triple the GFTs
    - ★ Caliendo & Parro (2015); Costinot & Rodriguez-Clare (2014), Ossa (2015)
  - ► some other missing factors
    - ★ pro-competitive effects, MNF and GVC, dynamic effects missing
- most likely, GFTs are a lower bound

An Alternative Use for the Structural Model

- perhaps, there is an alternative use for the structural model
  - ▸ to *interpret the data* rather than to make quantitative predictions
- how?
  - ▸ by opening up the gravity equations
- what is inside the time-varying FEs?
  - ▸ the model can tell us:
    - ★ GDP, size, price indexes, globalization, infrastructure
- year by year, they capture all macroeconomic variables explaining trade flows
  - ▸ would be fascinating to look inside!
- can we use the model to do an ex-post quantification?
  - ▸ could be compared with observables to make it more credible

Interpreting the Results

- welfare gain from EU over RTA
    - mean gain +6.6%
    - but large heterogeneity
- which countries gain the least?
    - GBR (2.3%), Greece (2.4%), Italy (2.8%)
        - ⋆ maybe the model is not so far off!!!
- lessons for Europe
    - the Euro had no trade effects → is Europe going too far?
    - 2004 enlargement → big gainers are entering countries
        - ⋆ Cyprus (3.5%), Czech Republic (10.8%), Estonia (10.4%), Hungary (14.2%), Latvia (8.7%), Lithuania (6.4%), Malta (8.2%), Poland (6%), Slovakia (12%), and Slovenia (10.5%)
- maybe things could have been done differently...

The Future of the EU

- domino effects after Brexit are small
    - but what if Greece and Italy exit?
- if EU collapses, what would be the real costs of Non-Europe?
    - probably far greater than 6.6%
- globalization cannot be stopped
    - will missed GFT grow?
- maybe not: despite temporary setbacks, markets have always grown
- but how?
    - before WWII, empires made markets
    - after WWII, trade agreements replaced empires
        - ★ Findlay & O'Rourke (2007), Gancia, Ponzetto & Ventura (2018)
- if the EU collapses, could a new age of economic imperialism follow?

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