

Discussion on “Learning the Wealth of Nations”

by Francisco J. Buera, Alexander Monge-Naranjo and Giorgio E. Primiceri

Ruben Segura-Cayuela

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STRUCTURE OF THE DISCUSSION

- **Motivation**

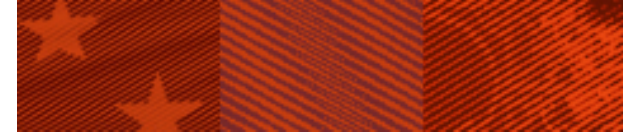
- Their motivation
- My motivation

- **Theory**

- A couple of technical issues
- How good is the fit?
- Counterfactuals

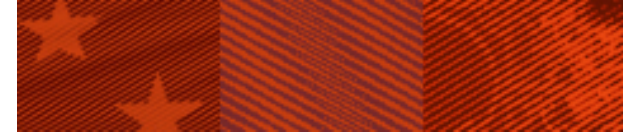
- **Summing up**

Motivation



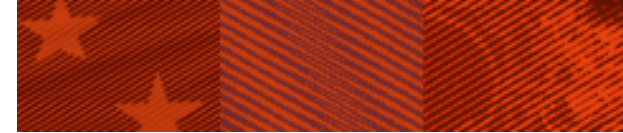
- **Despite common objectives, policies adopted differ across countries**
- **This differences are persistent in time**
- **In particular, if we look at trade policies for the period 1950-1998:**
 - Western Europe, U.S. and Canada open
 - Asia starts opening fast in 1960's
 - ROW displays fast and late (mid 1980's) opening

Motivation (II): Questions

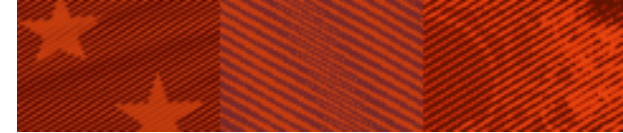


- **Can these patterns be explained through rational learning about the desirability of trade opening?**
- **If yes, is learning localized?**
- **And how disperse are beliefs today?**
- **How likely is a massive policy reversal (towards protectionism)**

Preview of the results



- **Rational learning does a good job: explains 92% of policy choices**
- **Learning is very localized: how much we learn from others declines by 40% for each 1000km**
- **Despite convergence of beliefs, still dispersion**
- **Large shocks (great depression) can cause policy reversals: 10% of countries would close borders within 5 years, and it would take almost 40 years to correct this**



How would I motivate this paper: a trade economist perspective

- **Historically (last 50 years), most trade has taken place between the North, some North-South, almost none (until recently) South-South**
- **Also, very hard to form new trade links [HMR\(2007\)](#)**
- **Uncertainty about policies and local learning can explain this**
- **Another alternative: This paper provides a “microfoundation” based on uncertainty for the stubborn role of distance in the gravity equation**

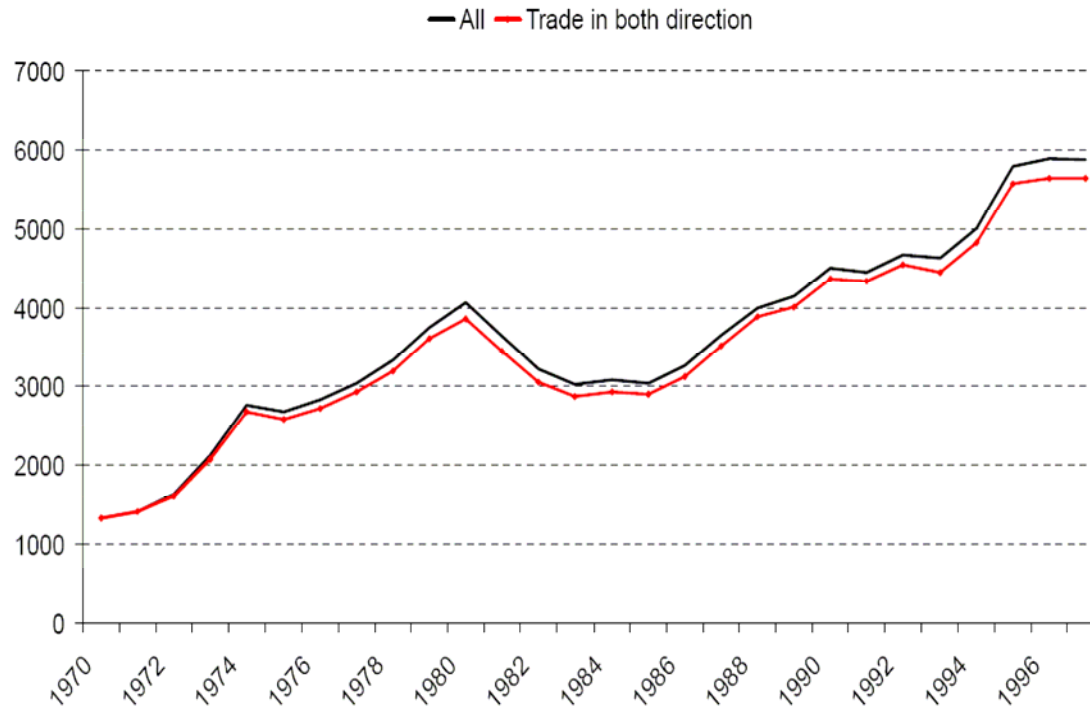
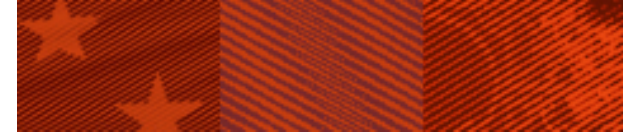


Figure 2: Aggregate volumes of exports, measured in billions of 2000 U.S. dollars, of all country pairs and of country pairs that traded in both directions in 1970, 1970-1997.

The Model



- **Very elegant and simple. Fresh (agnostic) approach:**
 - No need to take a stand on trade vs growth
 - Model has no trade theory content
 - No need of heterogeneity on fundamentals across countries
 - No political economy
- **Benevolent policymakers with priors about the relationship between trade and growth**
- **Being open to trade has exogenous and random political/ social costs/benefits**
- **They use own and others past experience to update their beliefs on that relationship. They may weight others experience differently than own if they are too different culturally or too far away.**

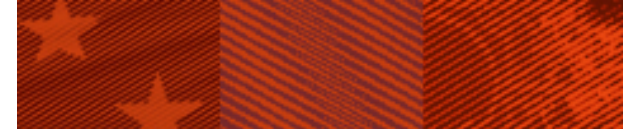
The model

- Thus, policy makers open the country whenever, once they update their priors, the expected growth rate in an open economy is large enough (compared to being closed) as to compensate for the political costs
- Optimal updating in the sense of Bayes:

$$w_{ij} = \frac{\sigma_i}{\sigma_j} \exp[z'_{ij}\gamma]$$

- A couple of technical notes:
 - Experimentation is not allowed
 - Can they learn more from switchers?
- They estimate using SW index from 1950 to 1998 (SW has some problems, are ex-socialists included?)

How important is learning?(I)



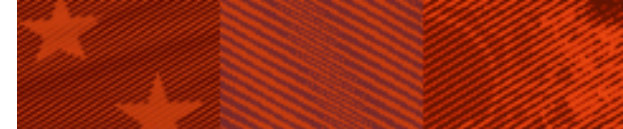
- **To evaluate the importance of learning in explaining the policy choices, they switch off the political cost**

- How many times does the model give the right policy choices?

- **Learning explains 92% of policy choices. Is this a large percentage?**

- Not clear

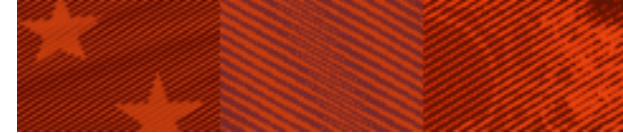
How important is learning?(I)



■ A simple example:

- 128 countries, 1950-1998
- 30% always open. 20% always close. Assume the remaining 50% all open in 1985.
- Set political cost to 0 and assume that there is no learning and that initial situation reveals their prior
- Without learning nobody switches. We get policies wrong $0.5 \times 128 \times 13 = 960$ times. Total is $48 \times 128 = 6144$
- That is, we get it right aprox. 85% of the time

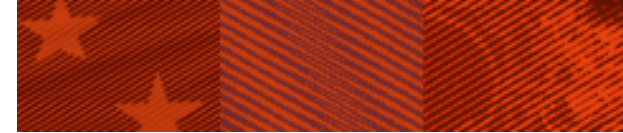
How important is learning?(II)



- **We should evaluate the relevance of learning on how well it predicts policy switches:**

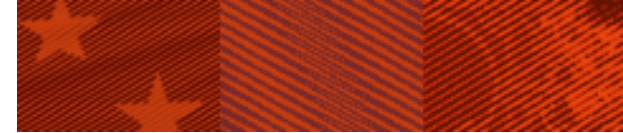
- it explains 60% of trade openings on the last part of the sample (when most of the action occurs)
- This number looks much better, but hard to get a sense of how much, particularly because this is when all the action takes place.
- It would be nice to know where and when are the errors located, and the direction of the error
- Do they have anything to do with exogenous shocks (for instance, stabilization plans in Africa around that time, the spread of the Washington Consensus)

How important is learning?(III)



- **The claim of the paper is that learning helps explain the dynamic and regional evolution of trade policies**
- **Evaluate learning precisely on that:**
 - I would compare the time path predicted by learning with the SW indicator, both in the aggregate and by region
- **Same applies for the dispersion of beliefs**
 - Which regions have a more positive view of trade?(my guess, Western Europe)

Counterfactuals



- **Large shock (calibrated to Great Depression) in 1998: 10% of countries revert to protectionism and the effect washes out in 40 years**
 - Is it large? How does it compare with the real Great Depression?
 - Given the small dispersion of beliefs, the size of the shock, and that by 1998 beliefs about growth are quite similar for both regimes, 10% seems small. Who reverts to protectionism?

Summing up

- **A simple model of rational and localized learning about the benefits of trade opening may help explain the observed patterns of trade liberalization over time and across regions.**
- **And it does so with uncertainty and learning as the main ingredients. No need for:**
 - Self interested policy makers and or special interest groups
 - Trade content
 - A relationship between trade and growth
 - Different levels of development

Summing up

- **Is this story more appealing than other existing ones that do not rely on uncertainty and/or learning?**
 - It may be, most other stories of trade policy do a good job in the regional dimension but not such a good one on the (endogenous) dynamic evolution
 - And uncertainty is an ingredient that has been largely overlooked in the trade literature
- **Some Self Publicity: There are other models of trade and uncertainty that can generate similar dynamics for trade flows and are probably hard to differentiate from this one on the data (Segura-Cayuela and Vilarrubia, 2008). All we need is:**
 - Firms uncertain about the profitability of markets but with the ability to observe and learn from the experiences of other firms in those markets
 - Fixed costs
 - Transport costs that depend on distance

Ruben Segura-Cayuela

Thank you for your attention

BANCO DE **ESPAÑA**



150 AÑOS DE HISTORIA
1856 - 2006

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