How to best to address the fast-changing nature of the global economy?

Paola Conconi
ULB (ECARES), CEPR, and CESifo

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Geneva, December 11, 2018
Major trends in international trade since the “Washington Consensus”

- Proliferation of regional trade agreements
- Surge in the number of RTAs
- Increasing depth of RTAs (World Bank, 2018)

Global value chains:
- Advances in information and communication technology and falling trade barriers → fragmentation of production process across countries

- A Honda is made of 20,000 to 30,000 parts produced by hundreds of different firms (Bartelme and Gorodnichenko, 2015)
- iPhone’s software and product design are done by Apple, most parts are produced by independent suppliers around the world (Xing, 2011)
- Intermediates account for 2/3 of total trade (Johnson and Noguera, 2012)
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The role of large firms

- Heterogeneity in productivity and fixed costs lead to selection into:
  - Exporting (Bernard and Jensen, 1999; Melitz, 2003)
  - FDI (Helpman et al., 2004)
  - Importing (Antràs et al., 2017)

Granularity of international trade, which is dominated by a few large firms:
- 0.4% of US firms account for 96% of exports (Bernard et al., 2007)
- Multinationals account for 2/3 of international trade flows (UNCTAD, 2013)

Are the winners from trade dominating the political economy of trade agreements?
- Rodrik (2018): “trade agreements are the result of rent-seeking, self-interested behavior of politically well-connected firms

However, no systematic empirical evidence and no theory
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- Are the winners from trade dominating the political economy of trade agreements?
  - Rodrik (2018): “trade agreements are the result of rent-seeking, self-interested behavior of *politically well-connected firms* on the export side
  - However, no systematic empirical evidence and no theory
Using detailed information from lobbying reports available under the Lobbying Disclosure Act, we construct a new dataset on firms' lobbying on US FTAs. We uncover new facts:

- Individual firms are the key players in the political economy of FTAs.
- Virtually all lobbying firms are in favor of FTAs.
- Larger firms are more likely to lobby on FTAs.
- Firms engaged in international trade are more likely to lobby on FTAs.

To rationalize these findings, we develop a new theoretical model of endogenous lobbying by heterogeneous firms on a proposed FTA under political uncertainty.

We assess the validity of the model's predictions on firms' lobbying expenditures:

- Larger firms spend more lobbying in favor of an agreement.
- Individual firms spend more on agreements that generate larger gains—in terms of reduction in tariffs on their final goods and inputs, depth of FTA, export and sourcing potential of FTA partners.
- When legislators are less likely to be in favor of ratification.
Blanga-Gubbay Conconi and Parenti (2018)

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The backlash against trade

Notwithstanding strong support by large firms, there seems to be a decline in political support for trade agreements (e.g. US withdrawal from TPP, public opposition to TTIP and CETA in the EU).

Possible reasons:
- Firms have gone global, but politics remains local: by fragmenting their production processes across countries, large corporations have "diluted" their political power. Some firms have started reshoring activities.
- Politicians care about re-election and trade policy is more salient to protectionist voters (Conconi et al., 2014).

Understanding the distributional effects of trade across and within countries is key for the political feasibility of future regional/plurilateral/multilateral negotiations.
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• Understanding the **distributional effects** of trade across and within countries is key for the **political feasibility** of future regional/plurilateral/multilateral negotiations
Thank you!
Number of agreements over time

More than 20
Between 10 and 20
Less than 10
Not in force
Cumulative
Source: Hofmann, Osnago and Ruta (2017)
Lobbying expenditures on the ratification of FTAs negotiated by the U.S.
Lobbying expenditures on the ratification of FTAs negotiated by the U.S.

![Bar chart showing lobbying expenditures on FTAs]

- **Firms**: Significant expenditure on supporting FTAs.
- **Associations**: Small expenditure on supporting FTAs.
- **Trade Unions**: Minimal expenditure, no opposition shown.

Legend:
- **Support**: Blue
- **Oppose**: Red
In virtually all cases (99.25%), lobbying firms are in favor of FTAs.
Larger firms are more likely to lobby on FTAs

Sales distribution (lobbying vs non-lobbying firms)
Employment distribution (lobbying vs non-lobbying firms)
## Probability of lobbying on FTAs and firm size

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>log(Sales(_{f,t}))</td>
<td>0.004***</td>
<td>0.004***</td>
</tr>
<tr>
<td></td>
<td>(0.0002)</td>
<td>(0.0003)</td>
</tr>
<tr>
<td>log(Employment(_{f,t}))</td>
<td></td>
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</tr>
<tr>
<td>FTA FE</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Industry FE (SIC2)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>N</td>
<td>67,716</td>
<td>67,716</td>
</tr>
<tr>
<td>pseudo R(^2)</td>
<td>0.504</td>
<td>0.463</td>
</tr>
<tr>
<td>Predicted probability</td>
<td>0.0037</td>
<td>0.0037</td>
</tr>
</tbody>
</table>

A 1% increase in firm size leads to a 1% increase in the predicted probability of lobbying.
Firms engaging in trade are more likely to lobby on FTAs

Probability of lobbying on FTAs and trade participation

<table>
<thead>
<tr>
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<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
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</thead>
<tbody>
<tr>
<td>Tradable sector, (f)</td>
<td>0.005*** (0.0001)</td>
<td>0.007*** (0.0003)</td>
<td>0.010*** (0.0006)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Exporter and/or importer, (f,t)</td>
<td>0.031*** (0.0065)</td>
<td>0.017*** (0.0053)</td>
<td>0.018*** (0.0052)</td>
<td></td>
<td></td>
<td></td>
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<td>(\log(Sales, f,t))</td>
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</tr>
<tr>
<td>N</td>
<td>64,112</td>
<td>64,112</td>
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<td>12,429</td>
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<tr>
<td>Pseudo R²</td>
<td>0.203</td>
<td>0.521</td>
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<td>0.0035</td>
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Operating in tradable sectors increases the probability of lobbying on FTAs by 143%

Trade participation increases the probability of lobbying on FTAs by 278%
Firms engaging in trade are more likely to lobby on FTAs

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Lobbying expenditures increase with firm size
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<tr>
<td>( \log(\text{Sales}_{f,t}) )</td>
<td>0.257** (0.1080)</td>
<td>0.276** (0.1140)</td>
<td>0.299** (0.1085)</td>
<td></td>
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<tr>
<td>( \log(\text{Employment}_{f,t}) )</td>
<td>0.285** (0.0900)</td>
<td>0.351** (0.1249)</td>
<td>0.411*** (0.1132)</td>
<td></td>
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<td>Yes</td>
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<tr>
<td>Industry FE (SIC1)</td>
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<td>No</td>
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<td>Yes</td>
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<tr>
<td>N</td>
<td>1,731</td>
<td>1,731</td>
<td>1,731</td>
<td>1,731</td>
<td>1,731</td>
<td>1,731</td>
</tr>
<tr>
<td>( R^2 )</td>
<td>0.076</td>
<td>0.077</td>
<td>0.080</td>
<td>0.082</td>
<td>0.096</td>
<td>0.099</td>
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Lobbying expenditures increase with the level of pre-agreement tariffs

Lobbying expenditures on FTAs, variation in pre-agreement tariffs

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<tr>
<td>log(Tariff applied by FTA partners on the final good $j,a,t-1$)</td>
<td>0.304**</td>
<td></td>
<td></td>
<td>0.507**</td>
</tr>
<tr>
<td></td>
<td>(0.0935)</td>
<td></td>
<td></td>
<td>(0.1048)</td>
</tr>
<tr>
<td>log(Tariff applied by US on inputs $j,a,t-1$)</td>
<td></td>
<td>2.239***</td>
<td></td>
<td>3.354***</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(0.1941)</td>
<td></td>
<td>(0.2873)</td>
</tr>
<tr>
<td>log(Tariff applied by US on the final good $j,a,t-1$)</td>
<td></td>
<td></td>
<td>0.092</td>
<td>-0.021</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.3768)</td>
<td>(0.3474)</td>
</tr>
</tbody>
</table>

| Firm FE | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| N       | 1,150 | 1,323 | 878 | 645 |
| $R^2$   | 0.203 | 0.227 | 0.242 | 0.283 |
Lobbying expenditures increase with depth of the agreement

Lobbying expenditures on FTAs, variation in the depth of the agreements

<table>
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<tr>
<th></th>
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</tr>
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<tbody>
<tr>
<td>Depth DESTA (index)</td>
<td>0.185*</td>
<td>0.0789</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depth DESTA (latent)</td>
<td></td>
<td>4.372***</td>
<td>(0.8072)</td>
</tr>
<tr>
<td>Depth World Bank</td>
<td></td>
<td></td>
<td>0.148***</td>
</tr>
</tbody>
</table>

Firm FE | Yes | Yes | Yes
Year FE | Yes | Yes | Yes
N | 1,732 | 1,732 | 1,732
R² | 0.221 | 0.226 | 0.230
Lobbying expenditures increase with the size of the FTA partners’ market

Lobbying expenditures on FTAs, variation in the size of FTA partners

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<tbody>
<tr>
<td>log(GDP of FTA partners(_{a,t-1}))</td>
<td>0.310***</td>
<td></td>
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</tr>
<tr>
<td></td>
<td>(0.0637)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>log(Export potential of FTA partners(_{j,a,t-1}))</td>
<td></td>
<td>0.259**</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>(0.0924)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>log(Sourcing potential of FTA partners(_{j,a,t-1}))</td>
<td></td>
<td></td>
<td>0.076*</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.0371)</td>
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<tr>
<td>Firm FE</td>
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<td>Yes</td>
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<tr>
<td>Year FE</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>N</td>
<td>1,821</td>
<td>1,294</td>
<td>1,327</td>
<td>863</td>
</tr>
<tr>
<td>R(^2)</td>
<td>0.202</td>
<td>0.204</td>
<td>0.225</td>
<td>0.244</td>
</tr>
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</table>
Lobbying expenditures increase with probability that legislators are against ratification

Lobbying expenditures on FTAs, variation in expected political support for ratification

<table>
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<th>(2)</th>
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</tr>
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<tbody>
<tr>
<td>Share of Democrats in Congress1&lt;sub&gt;t&lt;/sub&gt;</td>
<td>11.567**</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(4.0433)</td>
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