Discussion of Balistreri, Hillberry, and Rutherford (2007): 
“Structural Estimation and Solution of International Trade 
Models with Heterogeneous Firms”

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EIIT, 12-14 Oct 2007
Overview and contributions

- Structural estimation of a multi-region Melitz model with heterogeneous firm industries
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- Propose a solution method for computing the world trading equilibrium:
  - PE module: Solve for industry equilibrium taking general equilibrium variables (aggregate incomes, factor prices) as given
  - GE module: Solve for general equilibrium taking industry equilibrium variables (average industry productivity, prices, measure of firms) as given
  - Iterate between PE and GE modules until convergence.

Calibration strategy: Pin down some parameters based on the literature. Estimate the remaining structural parameters ($\theta$, $a$, fixed costs of exporting) by NLLS to fit bilateral manufacturing trade flows in the GTAP database.
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Overview and contributions (cont.)

- **Implementation:** Relatively aggregate observational units
  - 9 regions (CHN, NAF, LAM, EUR, EER, JKT, ROA, ANZ, ROW)
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- **Counterfactuals:** Reduction of ad valorem tariff barriers versus fixed cost barriers to trade in manufactures
  - Welfare gains much larger (4 times) with reduction of fixed costs of trade
  - Complementarity of reducing both fixed and variable trade costs
  - Interesting point: Biggest gainers appear to be developing regions as opposed to developed regions (presumably because of higher initial barriers)
General comments

▶ An important research agenda: Quantifying the welfare gains from trade liberalization in a setting with heterogeneous firms.

Theoretical set-up is a natural extension of Melitz (2003)

▶ Numerical computation of general equilibrium is conceptually neat.

Facilitated by neat aggregation in the Melitz model

▶ Plausible that gains from reducing fixed exporting costs are larger given relatively low level of recorded tariff barriers in GTAP (9.3%)

Consistent with prior evidence that the extensive margin (number of exporting firms) matters more than the intensive margin (exports per firm) in accounting for the magnitude of trade flows (Eg Eaton, Kortum and Kramarz (2004))
Specification choices

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- Does this parsimonious specification provide a good fit to the data?
  Would like to see plots of predicted trade flows when setting $f_{rs}^r = 0$
  against actual trade flows.
  Are there dimensions along which the estimated model does a relatively
  poor job of fitting trade flows? (Possible mis-specification)
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▶ For eg: \( f_{rs}^{r} \) much larger in magnitude for EER and ROW (Table 5), so a lot more residual variance in trade flows unexplained for these regions.

Is it all due to fixed exporting costs, or is there something else systematically different about these regions?
Specification choices (cont.)

- One possibility: Differences in technological capabilities

  Minimum productivity in Pareto distribution: \( b \) could be allowed to vary by exporting country (ie \( b_r \))
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Two side points:

- Presentation of fixed cost barriers: prefer if convert to monetary units (\( f_{rs} c_r \) instead of \( f_{rs} \)).

- Some parameters already calibrated.
  Why not also calibrate \( \theta \) and \( a \) from the literature, and leave only the fixed cost parameters to estimation?
Specification choices (cont.)

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▶ Less keen on disaggregating sectors: Would have to worry about how parameters such as fixed costs might differ systematically across sectors.
Additional exercises

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  - Sensitivity of the welfare results to heterogeneity parameter (vary $a$)
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  - Would like to see welfare gains in a hypothetical zero-gravity exercise (reducing $\tau_{rs}(1 + t_{rs})$ to 1, and $f_{rs} \to 0$)
Minor comments

1. Mention non-convexities: Natural question is uniqueness. Experimenting with different initial values in the algorithm should ease this concern.

2. A little more description of the variables taken from GTAP