

Comments on “The Efficiency of Global Markets for
Final Goods and Productive Capabilities”
by Georg Strasser

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Contributions of the paper

- Extends Dumas (1992) model of real exchange rate to allow for differences in mean productivities of capital across countries
- Develops novel measure of real exchange rate in terms of “productive capabilities”
- Uses ESTAR model to capture drift and diffusion of the exchange rate process
- Obtains measure of relocation costs of final goods and productive capabilities

The Model

- One good model of trade with
 - AK production technology
 - Country specific shocks to depreciation of capital
 - Cost of trading goods across countriesArbitrage trade is triggered if relative capital stocks are sufficiently far from parity level

Value Function

$$V(K, K^*) = K^{*\gamma} I(\omega)$$

$$\omega = K / K^*$$

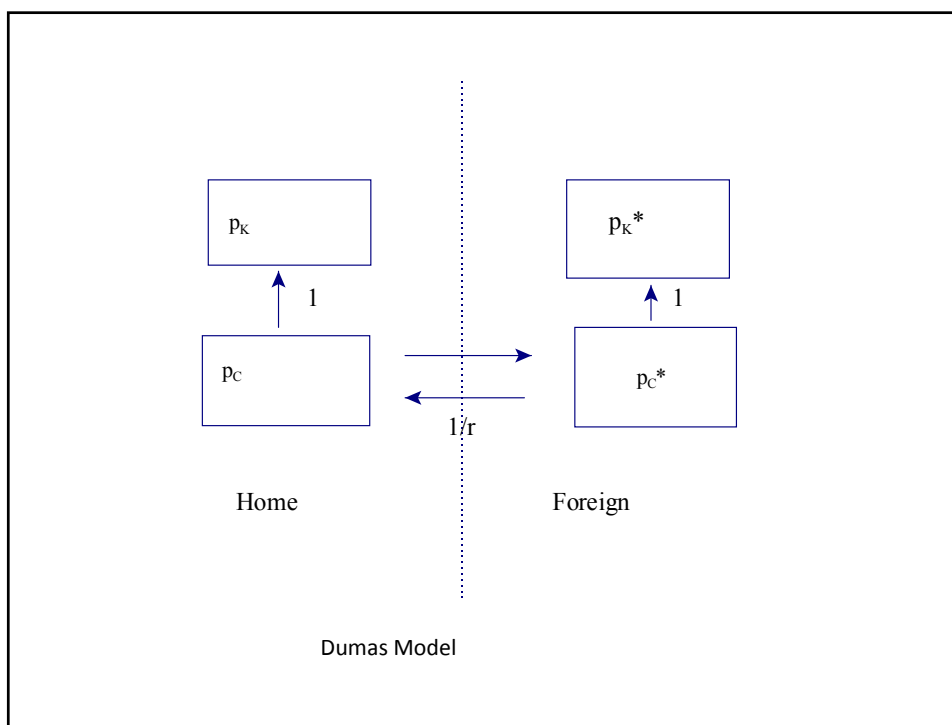
Real Exchange Rate

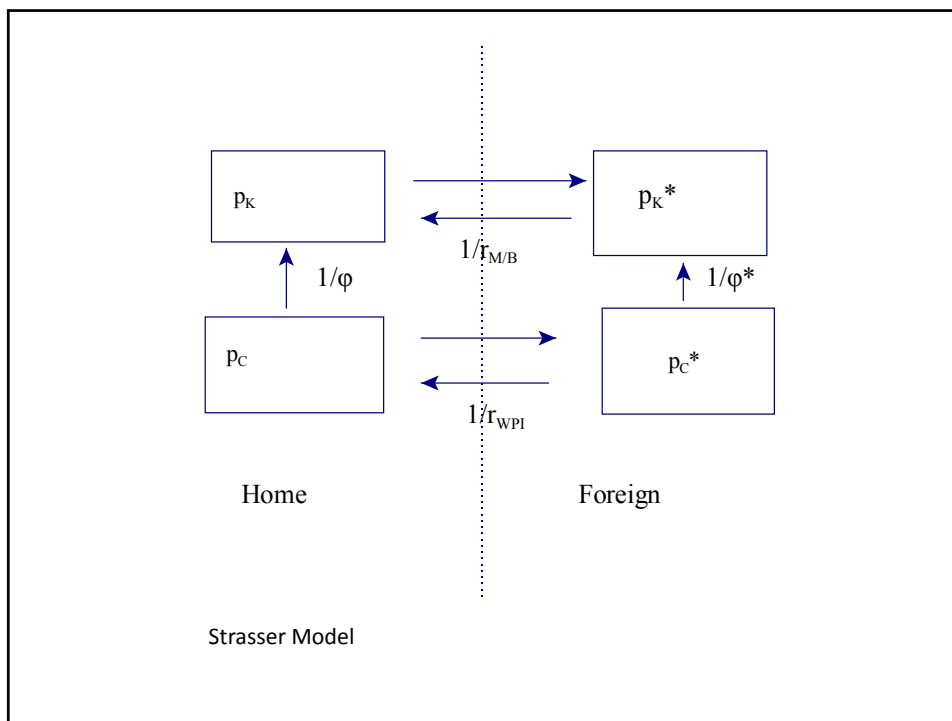
$$p(\omega) = \frac{V_K(K, K^*)}{V_{K^*}(K, K^*)}$$

Real Exchange Rate

1. Goods market interpretation : WPI

2. Productive Capabilities
Interpretation: M/B





Role of Knowledge capital

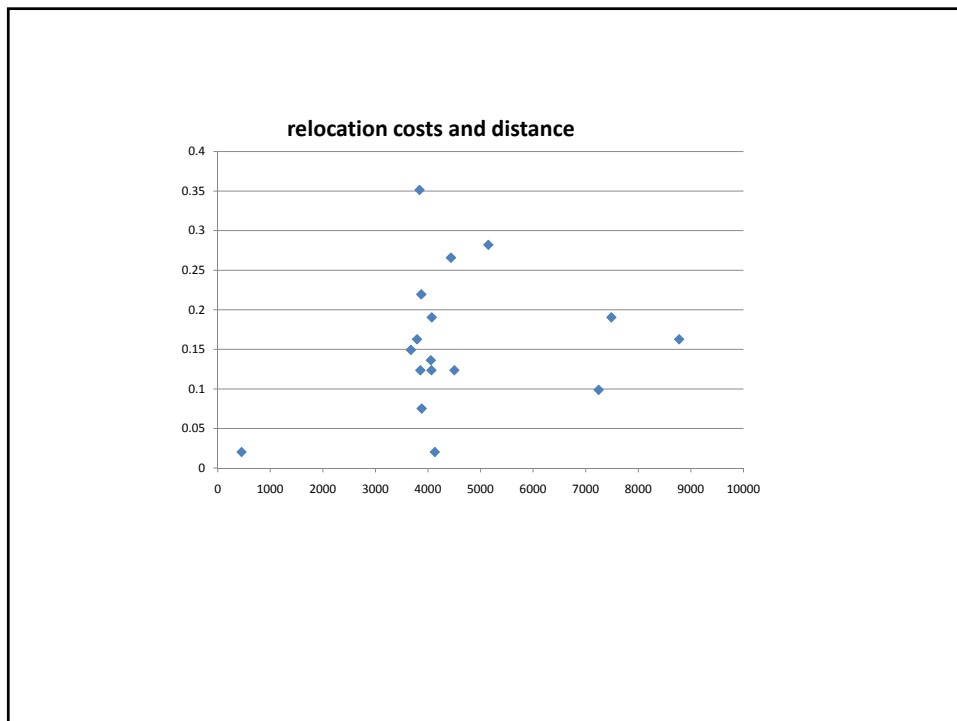
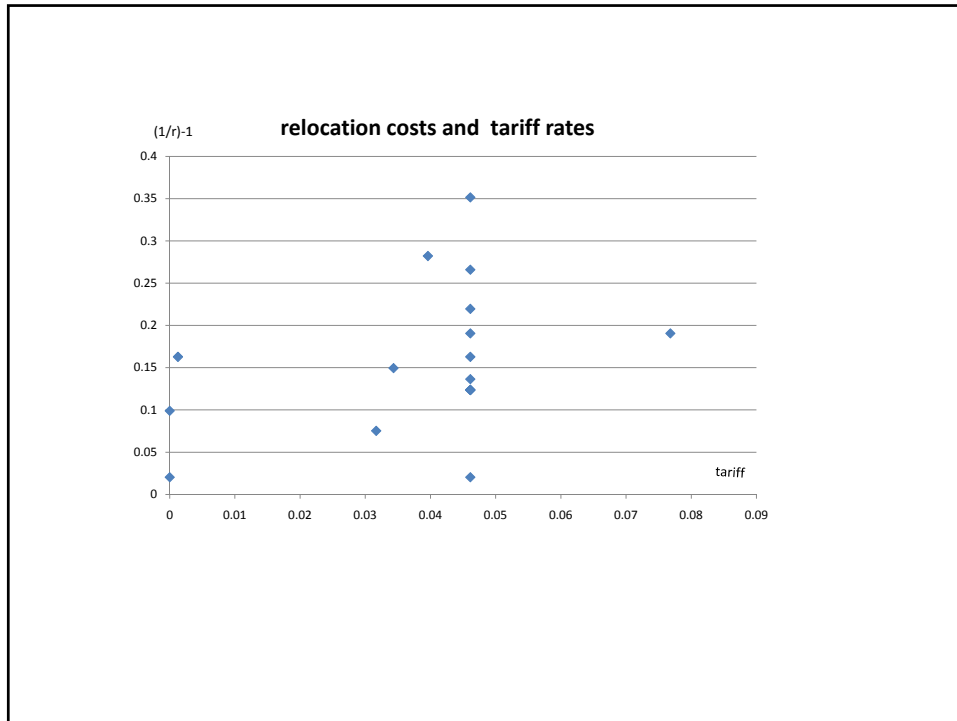
- Public good nature of knowledge capital that may be reflected in foreign investment
- M&A activity may reflect firms specific productivity advantages, rather than capital market returns

How reasonable is the relocation cost model?

- Are the measures correlated with things that we think represent transactions costs
- Is arbitrage trade associated with the level transactions costs

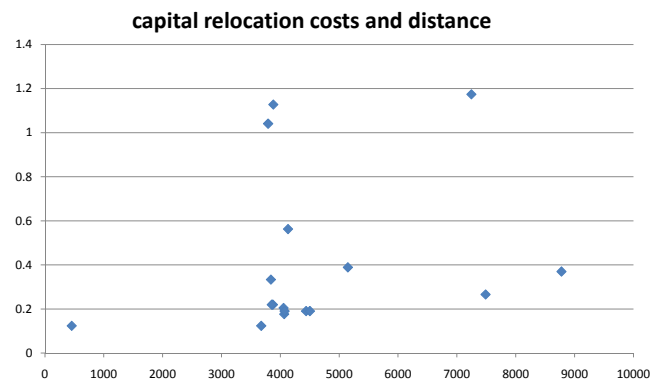
What does r_{WPI} represent?

- Trade costs
- Transport costs
- Administrative costs



What does r_{CAP} measure?

- Presumably greater costs of moving capital than of moving goods
- Does M and A activity represent arbitrage?



Things I'd like to see

- Comparisons with predictions in terms of terms of real interest rate differentials
- Modeling with differentiated products