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INSTITUTIONAL BARRIER AND THE WORLD INCOME DISTRIBUTION

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Abstract

The objective of this paper is to discuss the relationship of the openness and the impact of institutional reforms in the participation of the product of individual countries in global output. Therefore, it is based on economic simulations, a type of alternative approach that uses mathematical techniques and deductions to solve an objective model. The economic simulation of this work reflects that the trade opening level is an important factor of weight for possible institutional alterations in the economies. It is noticeable that, in the countries with low opening level, the cost of the capital is the main setback for the economic growth. And, in those economies with high opening level, the largest dynamics would compensate the problems caused by the cost of the capital. When compared the two types of reforms (continuous versus punctual), the "continuous" reform will bring a more expressive gain quality of the relative product than the "punctual" reform.

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1. Introduction

There is a dominant perception that institutions are key for explaining the perennial technical progress, which gained a prominent role for explaining the large differences in output *per capta* among countries (Easterly and Levine, 2002; Barro, 1998; Ranis and Stewart, 2001). There is also a growing perception that we should examine the process of economic growth, its basis and its effects, taking into account the economic interpendence among countries (Helpman, 2004; Acemoglu and Ventura, 2002).

We examine the relationship between trade openness and the institutional quality upon countries' growth performance by working out some economic simulations based on Acemoglu and Ventura's (2002) growth model. In the present case, the numerical computational analysis, which have some advantages over the traditional comparative statistics, will enable us to work out interesting economic scenarios involving changes in trade liberalization and institutional reforms.

Institutions are, here, considered in a broad sense. No doubt, properties rights and the rule of law are crucial features for reducing the risks to investors, that is, for granting good contracts and enforcing them (Easterly and Levine, 2002). The same applies to the existence of undistorted prices for preventing misalocation of domestic resources and promoting market competition, (Helpman, 2004; North, 1990; Barro, 1998). Yet, despite the prominent role of sound microeconomic foundation over macroeconomic ones[1], in the long run, we should include the latter in a broad notion of institutional quality. That is why we rather use the concept of Institutional barrier, as better explained in the paper.

Acemoglu and Ventura (2002) consists of a global economy where countries trade intermediate goods based on Ricardian characteristics (differences in productivity) and the quality of institutions create conditions for sustained economic growth. Economic simulations enable us to better track behaviors of certain variables, and the main impact analysis are divided, in the present analysis, into two main groups: the first involving economies A (developed economy) and B (economy in the progressive development) and the second involving economies B and C (economy in the stagnant developing). These two main groups are further divided into four tests per group, in which changes in the variable "Institutional Barrier" (see section 1) and the level of trade openness are tested. All the simulations of the economic model will be rotated in Matlab, using the SOR iterative numerical method.

The remainder of this paper is structured into three parts. Section one presents the formulation of the economic model. The second section presents the economic simulations and their results. Finally, we conclude.

2. Structure of the Economic Model

We take Acemoglu and Ventura (2002) model for reference, which consists of an imperfectly

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[1] Even episodes of a general macroeconomic statibity among developing countries, which Rodrik (1999) assigns to external shocks amplified by delayed (domestic) stabilization policies, were found out to be better explained by delayed reforms (Cinquetti and Silva, 2008).