Theories of International Trade

Assumes perfect in-country factor mobilities, but no factor mobilities between countries:

1) Ricardo's **comparative advantage** where source of advantage is labor productivity (Carbaugh Chpt. 2)
2) Heckscher-Olin **factor-endowment theory** expands Ricardo's theory to all factor inputs where advantage based on relative factor resource abundance (Chpt. 3)
3) **Factor-price equalization** where trade between countries equalizes returns to factors of production across countries (Ch. 3)

Removes perfect factor mobility assumption and introduces "asset specificity" (including knowledge capital) so is short-term model compared to long-term models above:

4) **Specific-factors theory** where capital in-country moves from "import-competing" industries to export industries because returns to capital in export industries is increasing relative to domestic industries (Ch. 3)
5) Increasing returns to scale theories:
   a) **Home market effect**, with large domestic demand a firm moves down along learning/cost curve so can export at comparative advantage
   b) **Overlapping demands**, consumer tastes are similar in countries with similar GDPs per person. Also explains "rich country" exports to the "rich" in "poor" countries (Ch. 3)

With “starting-point” of post-WWII “agglomeration” period of globalization:

6) **Intra-industry trade theory** (as opposed to inter-industry trade which is explainable by large differences in factor endowments between countries) is mostly between “advanced industrial nations”

    - *Homogenous products*: trade due to transportation costs and seasonal effects
    - *Heterogeneous products*: majority tastes met with domestic production but niche (“fat tail”) demand met with imports (Ch. 3)

Drops assumption of given and unchanging technology:

7) **Product life-cycle theory**, describes production moving from originating country (with higher than average profits) to “copy cat” country (with normal profits). (Ch. 3)
8) **MNEs and trade-theory**, similar to comparative advantage model (predicting that manufacturing will take place in low-cost country), however, firm factors of production not priced at market, so intra-firm pricing can be “nebulous” (or political / institutional) (Ch. 9).