Abstract:

According to the Ricardian theory of trade, the productivity distributions of countries dictate what and how much a country exports in a product: countries should produce and export relatively more in industries in which they are relatively more productive. As there are many industries that countries could be economically active in, these theories could not tell much about whether there is a structure behind the industrial trade patterns of the countries. Moreover, if there is a structure, this would also affect the diversification patterns of the countries. We posit that this transformation is not random, but rather a path- dependent process, i.e., what a country effectively produces today is an important determinant of which industries it might be productive at tomorrow. We estimate productivity parameters for 128 countries in almost 500 industries using the methodology developed by Costinot et al. (2012). We test whether we can predict the productivity levels in an industry from the productivity in related industries by building different measures of relatedness between industries based on Input Output, Labor and Knowledge tables. We also test the dynamic aspects of the structure and find that structure of comparative advantage explains the growth in the extensive margin and intensive margin. We then explore whether this structure has a predictive power in determining which industries would grow after North American Free Trade Agreement. In all our tests, we confirm the importance of the structure in comparative advantage patterns of the countries.