

Economic Integration and Welfare: Manufacturing Market vs. Agricultural Market

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Abstract

In the literature of new trade theory, most papers study the industrial location by imposing the assumption of free transportation in the agricultural sector. This paper explicitly incorporates arbitrary transport costs in both the manufacturing and the agricultural sectors into the Helpman-Krugman-Davis model of two countries and one production factor. The following results are obtained. First, we find a necessary and sufficient condition for the home market effect (HME) to be observed. Secondly, we find that integrating manufacturing markets has contrastive impacts on two countries to integrating the agricultural markets. Being derived from a general equilibrium framework, our results are suggestive for the analysis of various international trade agreements.

Key words: Transport costs, Firm location, Home market effect, Welfare.

JEL Classification: F12, Q17, R1.

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