Prospects for Trade in Intermediates and Trade in Services: What Does the Gravity Model of Bilateral Trade Tell Us?

by Haruka Yane

Master's Thesis

Osaka School of International Public Policy

Osaka University

January 2013

Abstract

This study uses product-level international bilateral trade panel data for the period 1995 to 2009, covering 40 countries from the recently released World Input-Output Database (WIOD). Constructing this dataset into a standard gravity model, this paper aims to compare the magnitude of coefficients across two pairs of equations with different dependent variables: trade in intermediates in comparison with trade in final products, and total trade in goods as opposed to total trade in services. So as to investigate these differences further, this study also analyzes the models by sector. This paper applies the sample selection model in order to account for the zero trade flows. Estimation results confirm that trading partners in East Asia engage much more in both trade in intermediate inputs and assembled final products, especially the former, compared to EU and NAFTA blocs. Trade in services presents remarkable resilience to the current financial crisis. Intermediate services trade, in particular, is affected less by trade costs and market size. By liberalizing trade and increasing economic freedom, there will be a highly significant, positive effect on nearly all kinds of trade flows.