

Global Production Sharing and Leontief Paradox: Evidence from Trade between two South Asian Countries

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The paper attempts to study the factor content of bilateral trade between the two developing countries of India and Sri Lanka. Given instances of production sharing between them and the extent of input trade that they engage in globally, it is only appropriate to use a framework which takes into account all these features. It uses the framework of Remier (2006) and Trefler and Zhu (2010) to find out if trade between them provides evidence of Heckscher-Ohlin pattern of trade. Results of the study provide evidence to support Leontief paradox with respect to this bilateral trade.

I Introduction

With deepening of economic integration of countries across the world, the pattern of international trade flows between nations and the factor content of such trade flows and models which have tried to reflect and predict such trade flows have become important and have been subject of several empirical tests.

Way back in 1933, two Swedish economists, namely, Eli Heckscher and Bertil Ohlin gave a trade model, known as the Heckscher-Ohlin (HO) model, which till date continues to be one of the most fundamental trade models. This model links the pattern of trade of countries to their pattern of comparative advantage. It postulates that in a world consisting of two countries, two goods and two factors of production, a country will export those commodities which require, for their production, relatively intensive use of those productive factors which are found locally in relative abundance. Thus, allowing for multiple factors of production, this model links factor endowments, trade flows and production technologies of a country and helps to predict the underlying factor content of the country's trade.

Later on, due to the contribution of Vanek (1968) this model has come to be referred also as the Heckscher-Ohlin-Vanek model (HOV model). Vanek's

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