I take a new look at both long-run and short-run effects of trade on economic growth purely through comparative advantage. I propose a second generation growth model with two industries, which are asymmetric in productivities. Surprisingly, opening two countries to trade need not increase the initial output of either country because of an externality absent from static models, though in practice the externality seems likely to be small enough that initial output rises in both countries. In the long run, trade could either increase or decrease the growth rate, depending on the research and development (R&D) productivities of the types of goods imported but not the types exported. For example, you might notice most goods in Wal-Mart are made in China. Qualities of Chinese goods might not be as good as those made in the U.S., but we still import them since they are much cheaper, which means they have lower quality-adjusted prices. Importing the low-quality goods from China could decrease output levels for the U.S. if the quality is low enough. And the growth rate effect of Chinese goods on the U.S. economy depends on the R&D productivity of China on that good. Even if the current quality level of that Chinese good is low, as long as China has a higher productivity in doing R&D in that industry, trade will increase the growth rate of the U.S. Otherwise, it causes a lower growth rate for the U.S.. The effect of trade on the U.S. is the same as if the U.S. had adopted the R&D productivity used by its trade partner, China, on the goods that the U.S. imports. The model is a theoretical model based on certain assumptions, and focuses only
on pure comparative advantage, so the effect of trade here excludes technology spillovers and direct investment. All those effects are present in reality, of course, but the purpose here is to isolate the phenomenon of interest - the growth effects of trade arising purely through comparative advantage - rather than constructing a “realistic” model ready for estimation.