

The implications of Global Value Chain for Measuring the Effect of Trade Costs Using Gravity Equation

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International trade is important factor for developing process for any country. At earlier, international trade was limited and most luxury goods were traded. After industrial revolution, trade expanded all over the world. The most recent trend of international trade was Global Value Chain (GVC) which became main feature of international trade in twenty first century. Rapidly declined trade cost as a result of the improvement of transportation and information communication technology is one of main factor for expanding GVC. Most studies apply gravity model to analyse determinants of the trade activities. Traditional gravity model shows that the trade flow from origin country to destination country depends on the economic size of each partners and distance between countries and mainly considers the gross term of trade flow. However, intermediate good trade flows became more important with GVC. So, applying traditional gravity model to analyse the intermediate trade flows were criticised by many studies. This study analysed the implication of GVC for measure the trade cost using gravity model by an empirical study based on Sri Lankan garment and apparel export. The result of study did not confirm the predicted relationship of gravity model. Tariff and GDP variable showed the expected sign but not statistically significant, also, distance variable was statistically significant, however, it showed a positive relationship. Accordingly, it revealed that Sri Lanka as a developing small open economy, the factors for apparel trade are differ than the factors describe in the gravity model. Apart from the variable of traditional gravity model, the labour cost or average wage level, international trade negotiations are some of important factors for trade flows for developing counties like Sri Lanka.

Keywords: Global Value Chain; intermediate goods; trade cost; textile trading