

“Corruption, Resource Allocation Efficiency, and Exports”
(in English)

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ABSTRACT

Regarding institutions as “factor endowments”, recent literature has shown that good contract enforcement is a source of comparative advantage in international trade. This paper shows a different channel through which institutions can affect comparative advantage, that is, institutions can affect resource allocation efficiency. Building on the idea that a country’s comparative advantage is determined not only by its factor endowments, but also by its resource allocation efficiency, we investigate the role of corruption in affecting a country’s export after a shock to the country’s financial market (that is, the equity market liberalization). We find strong evidence that corruption distorts the financial resource allocation, which weakens substantially the comparative advantage gains of a country from liberalizing its equity market. The findings are robust to a series of tests. Following the latest trade literature of heterogeneous firms, we further find that the sand effect of corruption works mainly through limiting new firm entry but not through limiting the growth of existent firms, which is consistent with the arguments in the previous literature.