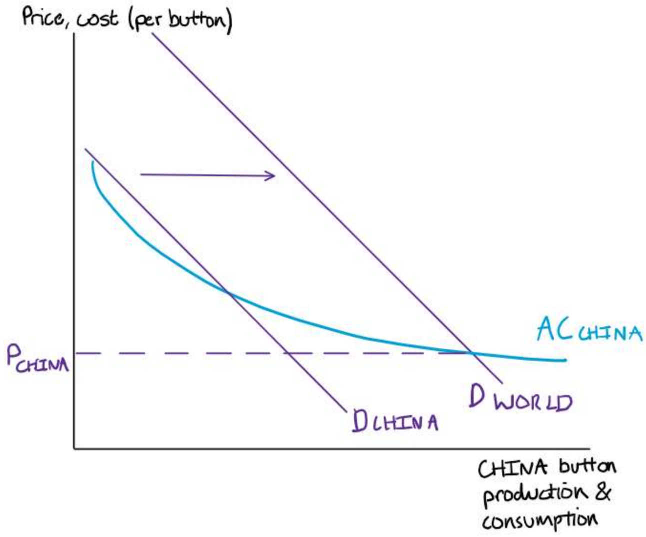
External Economies After Trade

Now as the USA and China trade, **China faces increased demand** from both USA and China consumers **as they can produce buttons more cheaply.** Therefore:

- The US industry **contracts.**
- The Chinese industry **expands.**

Until all production is in China.



As a result, **prices are lower** due to China's **larger industry** - **External Economies of Scale**

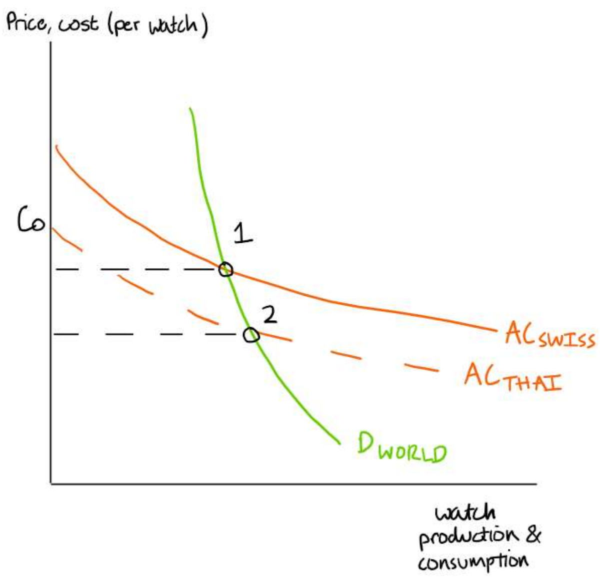
Now china provides buttons for **both** Chinese and US consumers.

RECAP

In Ricardian Model and H&O, prices converge, however with external economies, **prices are reduced everywhere.**

Initial Advantage

Historical Accidents leads to certain industries remaining in certain countries despite lower costs of production elsewhere. Consider Thailand and Switzerland producing watches



Production **may not be in the ideal location all the time.**

- Thailand price is less than Switzerland.
- 2 < 1
- Ideally Thailand would supply the market.
- However, at **the current price at 1, Thailand cannot enter the market** as their start production cost is **Co.**