Heterogeneous Agent Trade

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ABSTRACT

This paper develops a model of heterogenous agents and international trade. Heterogenous agents are modeled as in the standard incomplete markets tradition with household's facing incomplete insurance against idiosyncratic productivity and taste shocks. Trade in goods follows the Armington tradition but is derived from the "bottom up" with micro-level heterogeneity shaping the aggregate pattern of trade. In the efficient allocation, I recover standard results regarding gravity and the gains from trade. In the decentralized allocation, the pattern of trade is distorted, the aggregate trade elasticity is non-constant and the benefits from globalization are distributed unequally. I use model to explore two issues: the ability of trade policy to improve outcomes and how financial globalization complements trade in goods.

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