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Direct and Indirect effects of Trade Liberalization: Evidence From Chile

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Abstract

Production networks can amplify the effects of trade reforms on firms performance. In this article, I examine the effect of a reduction of foreign tariffs on the productivity of supplier industries of exporters. Using a panel of Chilean plants during a period of trade liberalization with the European Union, the United States, and the Republic of Korea, I show that the average reduction in the foreign tariff faced by downstream industries (1.1 percentage points) increases the productivity of intermediate input suppliers industries by 1.5 percent. The increase in productivity among supplier industries accounts for 22.5 percent of aggregate productivity gains. I find that tariff cuts induce firms to acquire new machinery and pay higher wages to skilled workers. The results are robust when I control for the change in domestic competition and the access to foreign inputs that could potentially drive productivity growth following output and input tariff elimination.

Keywords: JEL Codes:, D21, F12, L60

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