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A Dynamic North-South Model of Demand-Induced Product Cycles*

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Abstract

This paper presents a dynamic North-South general-equilibrium model where per capita incomes shape demand patterns across regions. Innovation takes place in a rich North while firms in a poor South imitate products manufactured in North. Allowing a role for per capita incomes in determining demand delivers a complete international product cycle as described by Vernon (1966), where the different stages of the product cycle are not only determined by supply-side factors but also by the distribution of income between North and South. We analyze how changes in the gap between North and South due to changes in Southern labor productivity, population size in South and inequality across regions affect the international product cycle. In line with presented stylized facts, we predict a negative correlation between adoption time and per capita incomes.

JEL classification: F1, O3

Keywords: international product cycles, inequality, international trade

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