

Processing trade, Sunk Costs, Firm Heterogeneity and Export Behavior
——Theory and evidence from China

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There is debate that whether can the export behavior be explained by the firm heterogeneity and sunk costs, because more than half of the export of China are processing trade whose firms has been exporting when they were founded. This paper provides a theory framework and gives substantial evidence considering processing trade. We define the firms which only serve domestic market and only serve export market as single-market-firms, and the firms which serve both domestic and export market as integrated market firms. Then we use the firm-level data from Manufacture of Communication Equipment, Computers and other Electronic Equipment of China in 2004-2006 to construct a probit model. We find that the greater the TFP, the higher the probability of the firm to become an integrated market firm. At the same time, the sunk costs are significant to affect the export behavior of firms. This research makes the policy implication of trade of heterogeneity firm more obviously. Government should provide policy assistance for both of the firms wanted to export and the export firms wanted to enter domestic market to reduce costs to become integrated market firms.

Key Words: heterogeneous-firm trade model; full export enterprises; TFP; firm-level data; probit model