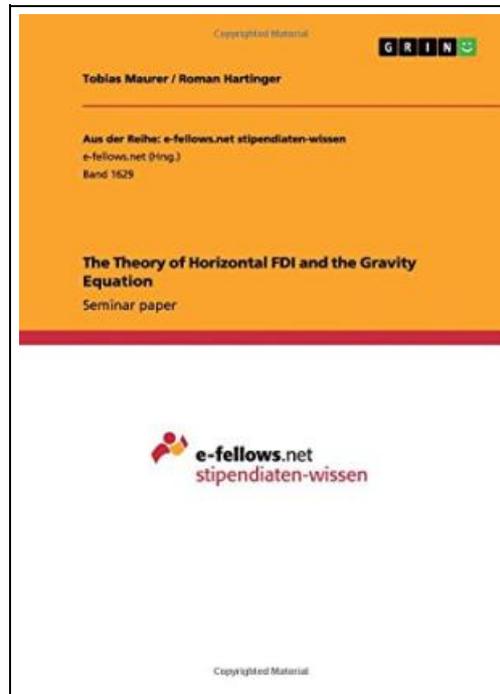


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THE THEORY OF HORIZONTAL FDI AND THE GRAVITY EQUATION



GRIN Publishing Nov 2015, 2015. Taschenbuch. Condition: Neu. Neuware - Seminar paper from the year 2015 in the subject Economics - Foreign Trade Theory, Trade Policy, grade: 2,0, University of Hohenheim (Institute of Economics), language: English, abstract: The gravity equation is a common and often used empirical technique to analyse bilateral trade. The relationship between the theoretical background of multinational firms and findings from the empirical research with the gravity equation, however, had not been proven to be strong. This results from the fact that gravity equations which try to explain foreign affiliate sales are ad hoc and therefore the coefficients estimated by them are hard to interpret. That is why Kleinert and Toubal (2010), from now on referred to as K&T, further elaborate the theoretical origin of the structural gravity equation by Redding and Venables (2003) which they use to analyse exports and FDI. In their paper they focus on three different theoretical models. Two models on horizontal FDI by Brainard (1997) and by Helpman et al. (2004) and one on vertical FDI by Venables (1999). After the theoretical part they try to apply the gravity equations they derived on a dataset on affiliate sales to analyse if these equations hold true in the empirical analysis. In our paper we will focus on the theoretical origins of the two models on horizontal FDI, since these are the models who hold in the empirical test. Our focus lies on the derivation of these models. We show the differences among the models themselves, as well as the similarities and differences between the original models and the revised models by K&T. We will further show how these models lead to the gravity equations by analysing its connections with the structural gravity equation by Redding and Venables (2003) in greater detail. Summing up,...



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