

Some key quantified “stylized facts” concerning trade-inhibiting factors that have been identified in the gravity model literature are as follows:²⁴

1. *Borders*: two firms located on opposite sides of a national border trade two thirds less than if they were located in the same country.
2. *Distance and Contiguity*: if two countries are not adjacent, trade falls by half, with a further 1 percent decline in trade for each 1 percent increase in distance between them.
3. *Currencies*: use of different currencies (even if fixed exchange rates are used) reduces trade by two thirds, with a further 13 percent reduction due to exchange rate variability.
4. *Culture*: if two countries speak different languages, trade falls by half.
5. *Trade Rules*: if two countries do not belong to a free trade area, trade falls by two thirds—and even further if tariff and non-tariff barriers are at the heights typical of developing countries.

Even ignoring the effects of distance, tariffs, and other factors such as being landlocked versus having access to a coast and/or shared colonial history, if two countries are not immediate neighbours, have different currencies, speak different languages and are *not* parties to an FTA—in other words the typical situation facing most pairs of nations—the chance of an international transaction taking place is less than one percent of that of a domestic transaction. An FTA increases this propensity to about 2½%.²⁵ This indicates a powerful trade-generating effect. Table 1 summarizes these effects.

²⁴ These assessments are taken from Jeffrey A. Frankel, “Assessing the Efficiency Gain from Further Liberalization,” paper delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Harvard University (June 1-2, 2000). This paper is available online at <http://www.ksg.harvard.edu/cbg/trade/frankel.htm>.

²⁵ The implied “border effect” for Canada-US merchandise trade from these stylized values is 10.6. This accords well with John Helliwell’s estimate of about 12 post-FTA. See John F. Helliwell, *How Much do National Borders Matter?* (Washington: Brookings Institution, 1998); pg 115.