

Politically Induced Internal Trade Barriers in China ^{*}

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Abstract

Competition among subnational governments generates internal trade barriers, fragmenting markets within nominally integrated economies. In China's decentralized system, where provincial authorities evaluate city leaders on relative economic performance, politicians face incentives to maximize locally appropriable gains while minimizing spillovers to rivals. This domestic geopolitics creates systematic distortions in resource allocation. Exploiting exogenous variation in promotion incentives driven by the age of city party secretaries (1996–2018), I show that intensified within-province competition significantly reduces inter-city trade flows, dampens international exports, and restricts firm access to intermediate inputs. Under competitive pressure, politicians reallocate resources toward non-tradable sectors, specifically real estate, while underinvesting in connective infrastructure near jurisdictional borders. Individually rational responses to career incentives thus produce collectively suboptimal market fragmentation, demonstrating that internal trade costs are endogenous to political institutions.

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