Origins of International Factor Structures

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We show that exchange rate correlations tend to be explained by the global trade network while consumption correlations tend to be explained by productivity correlations. Sharing common trade linkages with other countries increases exchange rate correlations beyond bilateral linkages. We explain these findings using a model of the global trade network with market segmentation. Interdependent global production generates international comovements, while market segmentation disconnects the drivers of exchange rate correlations from the drivers of consumption correlations. Moreover, we show that the trade network generates common factors found in exchange rates. Our findings offer a trade-based account of the origins of international comovements and shed light on important frictions in international markets.