

**Abstract:** I consider how heterogeneity in capital goods affects international trade patterns, and I show a novel source of comparative advantage: the magnitude of capital goods heterogeneity. Capital goods are heterogeneous in their productivity, and due to capacity constraints, only productive capital goods are activated in the equilibrium. Through this selection, the distribution of capital goods determines the industry-level productivity: industry-level productivity is higher in an industry with relatively larger variation in capital goods, and hence in a perfectly competitive two-country, two-good, two-factor equilibrium, the industry has Ricardian comparative advantage. An empirical examination using cross-country industry-level data shows that larger heterogeneity, which is empirically captured by a lower average capacity utilization rate, is positively correlated with higher international competitiveness of the industry. An extension of the model, including fixed trade cost, describes a sorting situation in which the most productive production units export, the moderately productive units serve domestic market, and the least productive units do not operate.