

*Trading Internationally*  
(Mike Peng & Klaus Meyer, International Business)

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Special Topics in Internationalization

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## **1. Introduction**

2. Why Do Nations Trade?

3. Theories of International Trade

4. National Institutions & International Trade

5. Implications for Practice



## ■ Learning Objectives

- Use the resource-based & institution-based views to explain **why nations trade**.
- Understand **classical & modern theories** of international trade.
- Appreciate how **economic & political institutions** influence international trade.
- Draw **implications for action** around the world.

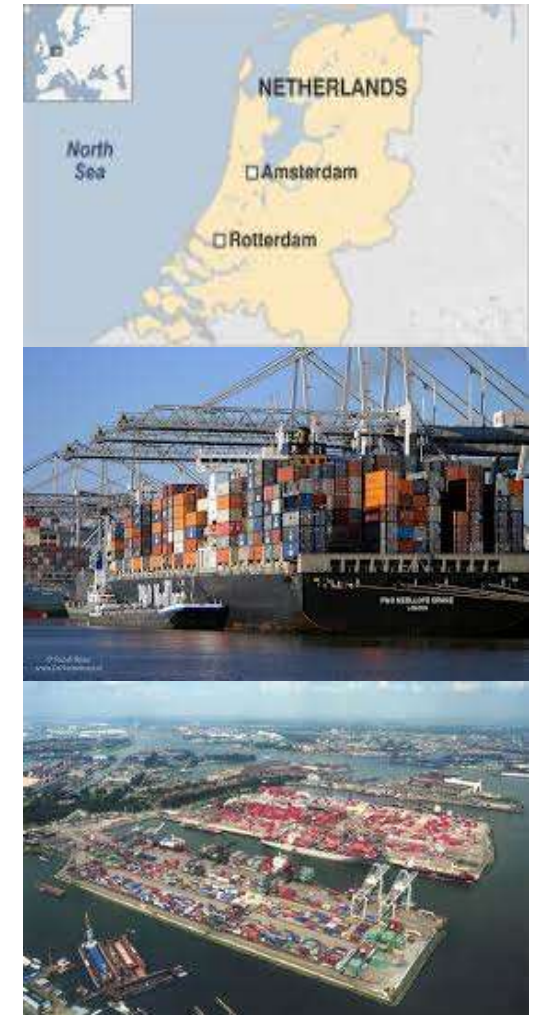


## ■ Port of Rotterdam: Gateway to the World

❖ What explains the economic success of the Netherlands over the centuries?

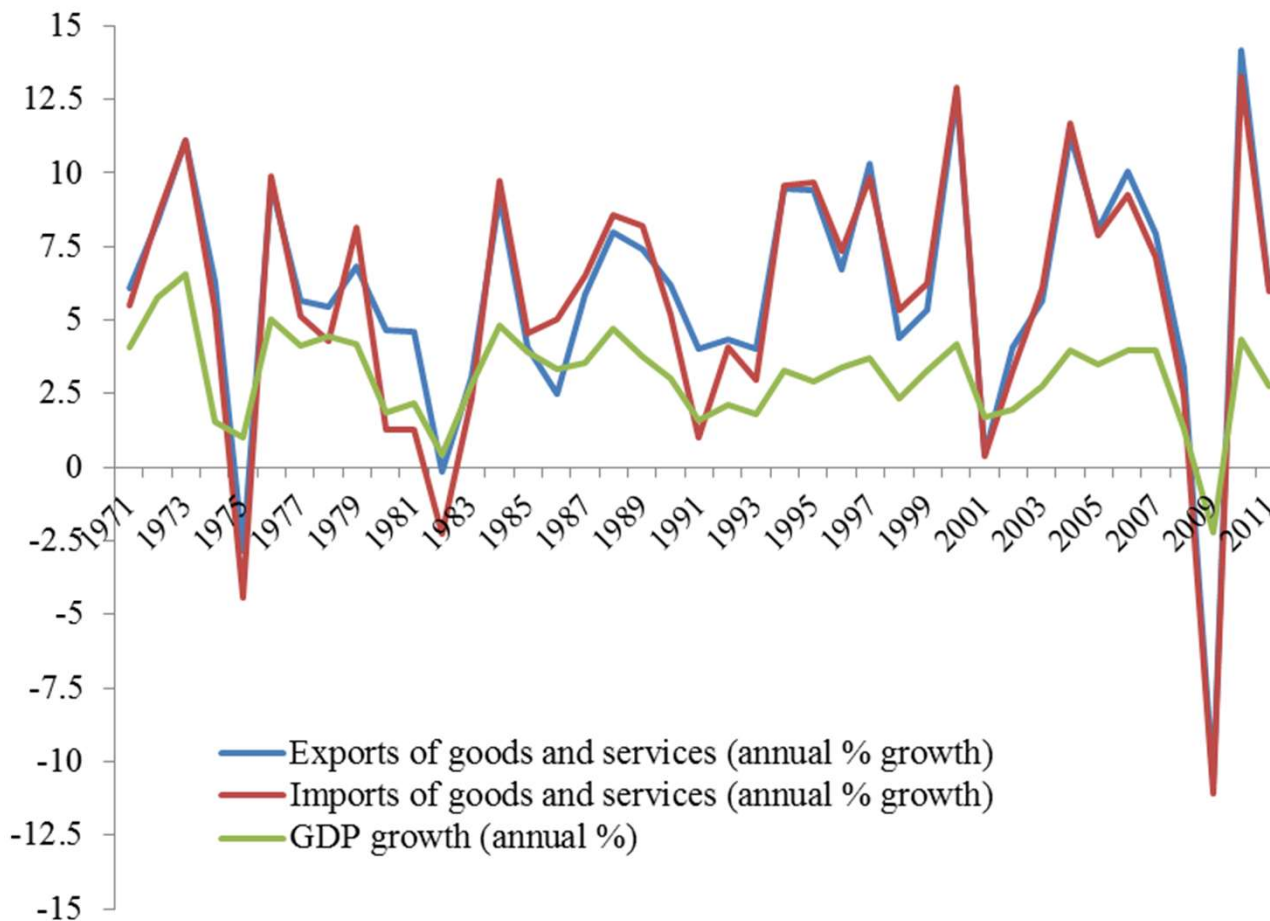
- **ANSWER:** International Trade !
- The Dutch East India Company in the **17<sup>th</sup>** century
- **Rotterdam:** Rank **4** (Shanghai/Ningbo/Singapore)
- The transportation business in the port: **€6.6** billion
- A main hub for sea-bound transportation for **500** million consumers in Europe
- Over **100** mega-cranes working every day
- Tank storage of **28.4** million cubic meters

> Many Japanese & American MNEs set up their European distribution centers near the port of Rotterdam.





## World Trade Growth vs. GDP Growth?



### KEY POINTS

- > **World export growth:**  
1998-2008: **+6.7%** (blue arrow up)  
2009: **-10.7%** (grey arrow down)
- > **World import growth:**  
1998-2008: **+6.6%** (red arrow up)  
2009: **-11.1%** (grey arrow down)
- > **World GDP growth:**  
1998-2008: **+3.3%** (green arrow up)  
2009: **-2.2%** (grey arrow down)

Source: Own illustration based on World Bank.



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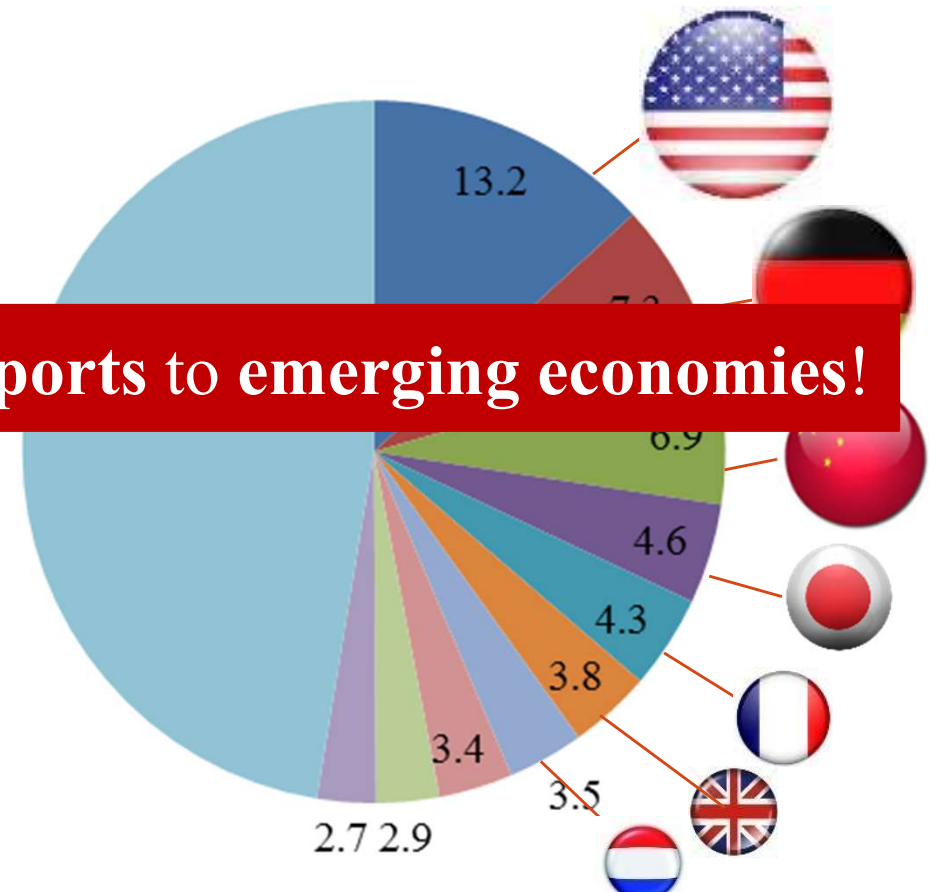
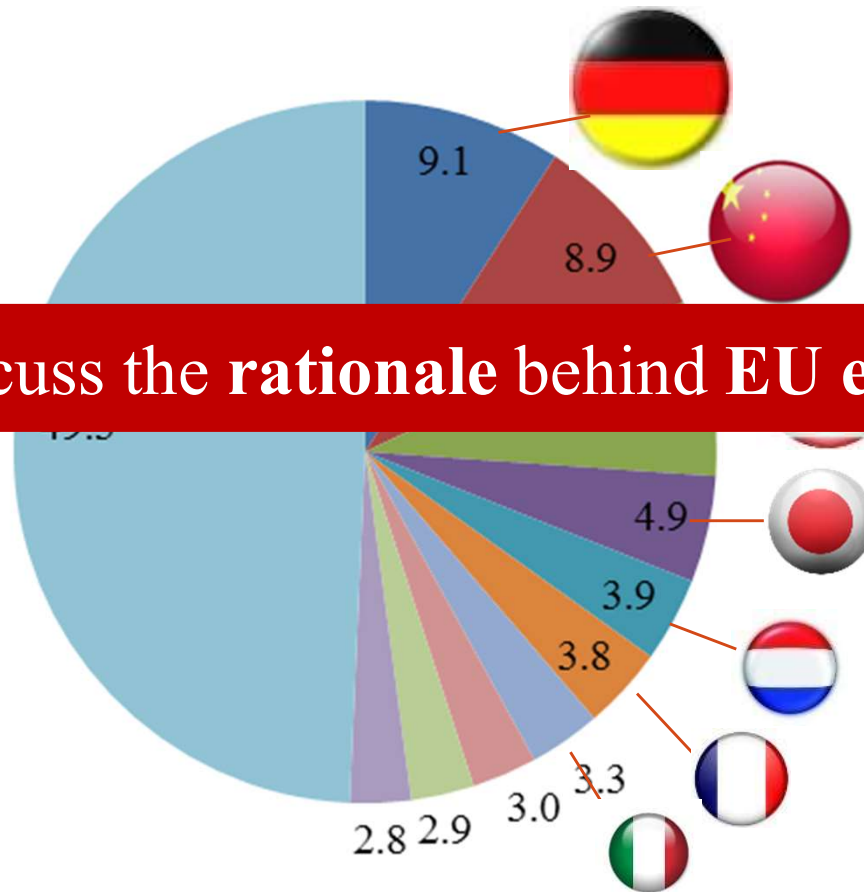
# Why Do Nations Trade?



## ■ Leading Trading Nations (Unit: %)

Top 10 Exporters of goods

Top 10 Importers of goods



Discuss the rationale behind EU exports to emerging economies!

# Why Do Nations Trade?



## ■ Key Questions


- ❖ **WHY** do nations go through greater complexities to trade internationally?
- ❖ **WHY** are there gains from international trade?
- ❖ **HOW** do nations benefit from such gains?

## ■ Key Words

- ❖ **Trade surplus:** An economic condition in which a nation **exports** more than it **imports**.
- ❖ **Trade deficit:** An economic condition in which a nation **imports** more than it **exports**.
- ❖ **Balance-of-trade:** Whether a nation has a trade **surplus** or **deficit**.





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# Theories of International Trade



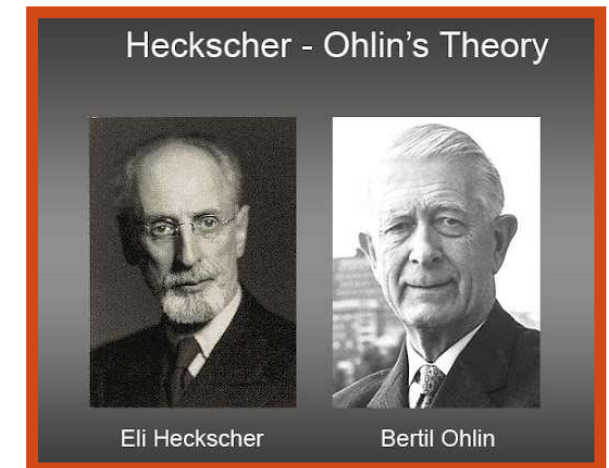
## ■ Theory of Comparative Advantage

- ❖ **David Ricardo**'s model is based on opportunity cost considerations.
- ❖ If the **opportunity cost** is lower in one nation than in another, *i.e.* relatively cheaper.
- ❖ ... focuses on **labor productivity**



## ■ Factor Endowment Theory

- ❖ ... indicates that nations develop comparative advantage based on their **locally abundant factors**.
- ❖ Labor, land, technology
- ❖ *e.g.* 🇧🇷 land, water, weather; 🇮🇳 human labor






# Theories of International Trade



## ■ Product Life Cycle Theory

❖ **Raymond Vernon** (Harvard) in the 1960s.

❖ **Basic Assumption:**

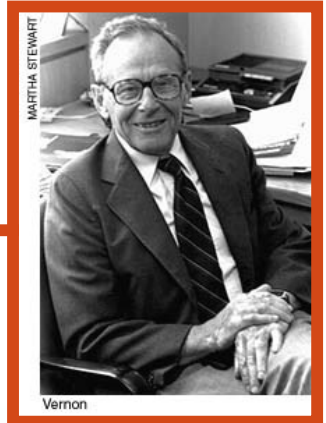
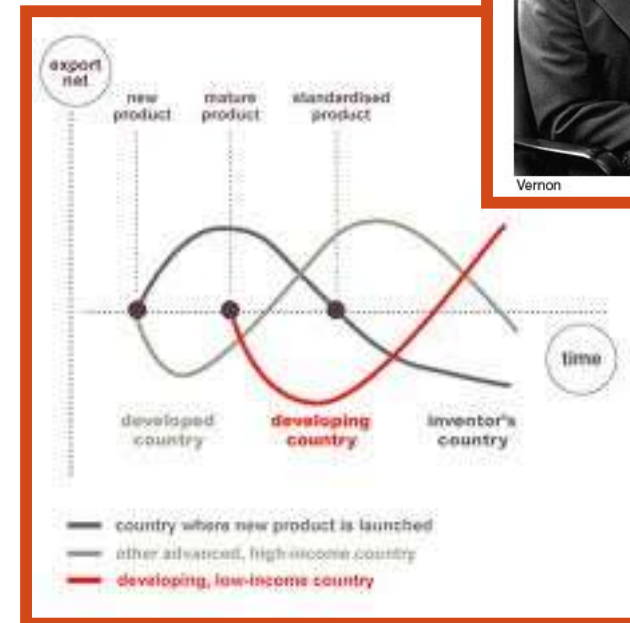
- Lead innovation nation. 
- Other developed nations.  
- Developing nations.
- Dynamic changes in patterns of trade.

❖ **‘3’ Stages:**

- (1) growth, (2) maturity, & (3) decline.

❖ **2 Major Limitations:**

- Innovation occurs not only in the USA but also in Asia & Europe.
- Simultaneously launching new products (e.g., iPods or game consoles) around the globe.





## ■ Strategic Trade Policy

- ❖ **Government intervention** is usually regarded by economists as **destroying value** because it distorts free trade.
- ❖ Can **government intervention** actually **add value**?
- ❖ ... indicates that strategic intervention by governments in **certain industries** can enhance their odds for international success.

## ■ Brander-Spencer Analysis (A game-theoretic framework )

- ❖ There are only ‘**2**’ firms (**Boeing & Airbus**) competing, each from a different country (**United States & Europe**).
- ❖ There is a new product, 150-seat aircraft, that both firms are capable of making.
- ❖ Each firm decides either to produce the new product or not.

# Theories of International Trade



## Strategic Trade Theory

How the profits earned by the 2 firms might depend on their decisions !

TABLE 11-1 Two-Firm Competition

		Airbus	
		Produce	Don't produce
Boeing	Produce	-5, -5	100, 0
	Don't produce	0, 100	0, 0

If Boeing has a **first-mover advantage**, there would be no incentive for Airbus to compete, & Boeing would enjoy huge excess returns !

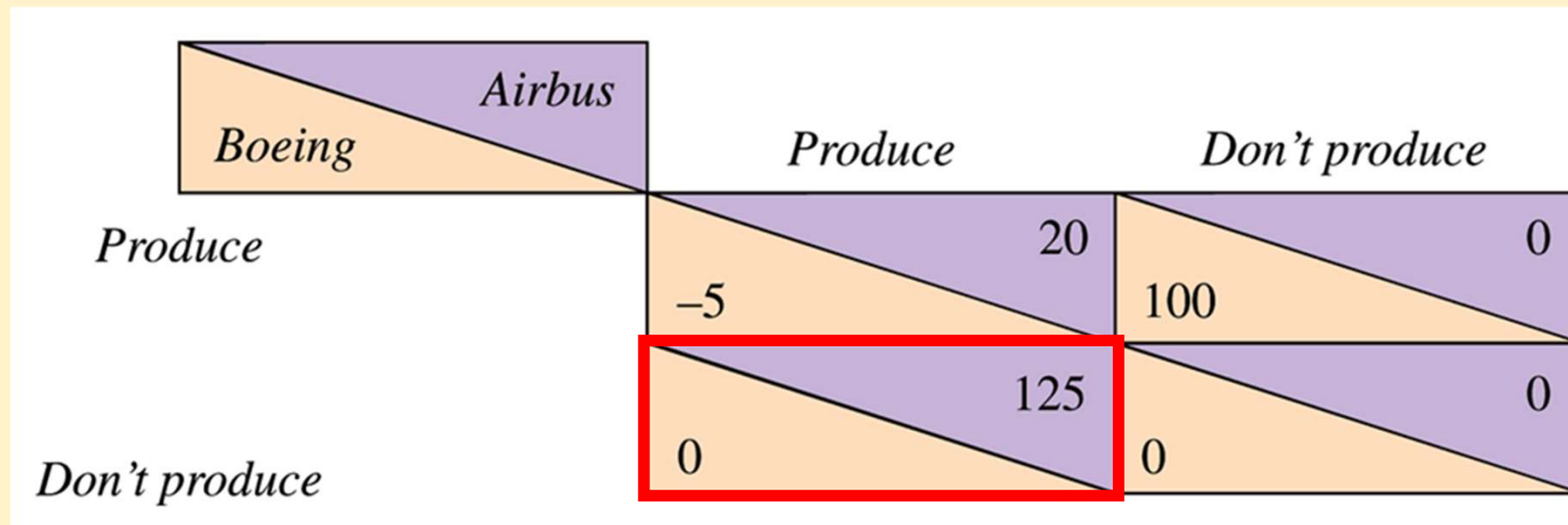
# Theories of International Trade



## Strategic Trade Theory

A subsidy of 25 by the EU alters the outcome.

TABLE 11-2 Effects of a Subsidy to Airbus



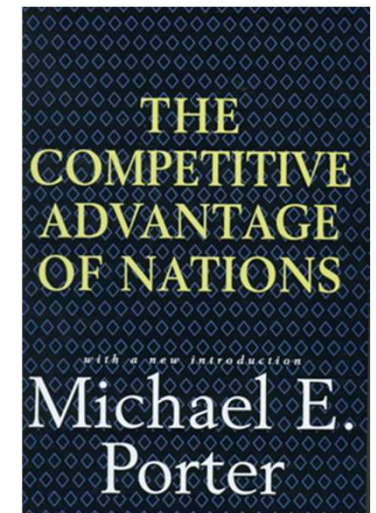
The subsidy raises profits by more than the amount of the subsidy itself.

# Theories of International Trade



## ■ The Competitive Advantage of Nations

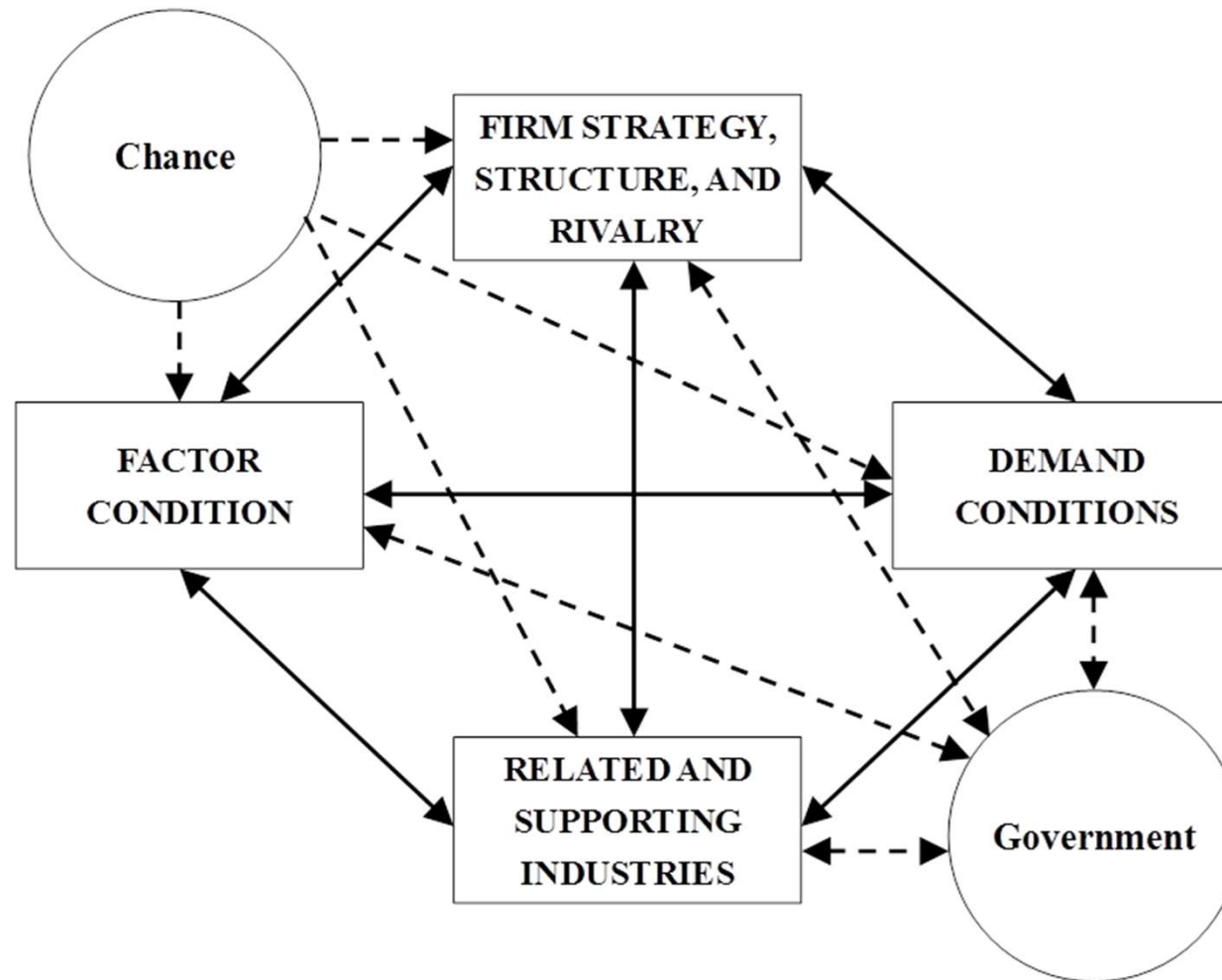
- ❖ Professor Michael Porter (Harvard Business School)
- ❖ **Diamond model:** The impact of a nation's location advantages on the competitiveness of a firm.
- ❖ **Why** are certain industries within a nation competitive internationally?
- ❖ For example, although **Japanese electronics & automobile industries** are global winners, Japanese service industries are notoriously inefficient.
- ❖ Porter argues that **4** elements play a central role in promoting the competitive advantage of the nation.



# Theories of International Trade



## ■ The Competitive Advantage of Nations



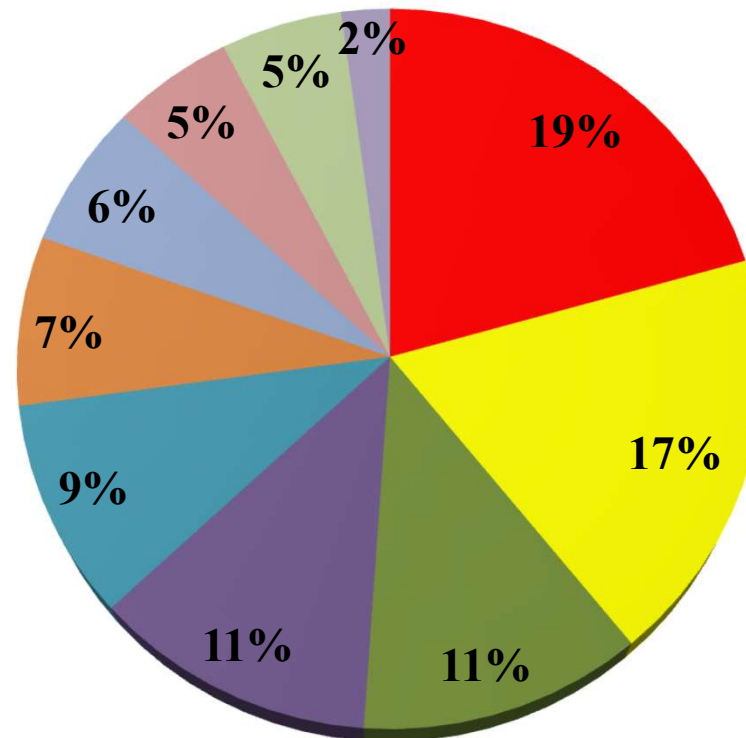
Source: Porter (1980)



# Theories of International Trade



## Japan's Digital Camera Industry



- Canon (JPN)
- Sony (JPN)
- Nikon (JPN)
- Samsung (KOR)
- Kodak (USA)
- Panasonic (JPN)
- Olympus (JPN)
- Fujifilm (JPN)
- Casio (JPN)
- Pentax (JPN)



## ■ Japan's Digital Camera Industry

### Resource endowments

- > Abundant supply of **electrical & mechanical engineers**

### Domestic demand

- > **Large, sophisticated home demand** due to Japanese obsession with taking photos.
- > Japanese love exchanging photos & taking group photos.

### Related & supporting industries

- > Strong electronics & equipment industries.
- > **Strong Japanese optical lens industry.**
- > **Gographical cluster** in the Suwa district of Nagano

### Firm strategy, structure & rivalry

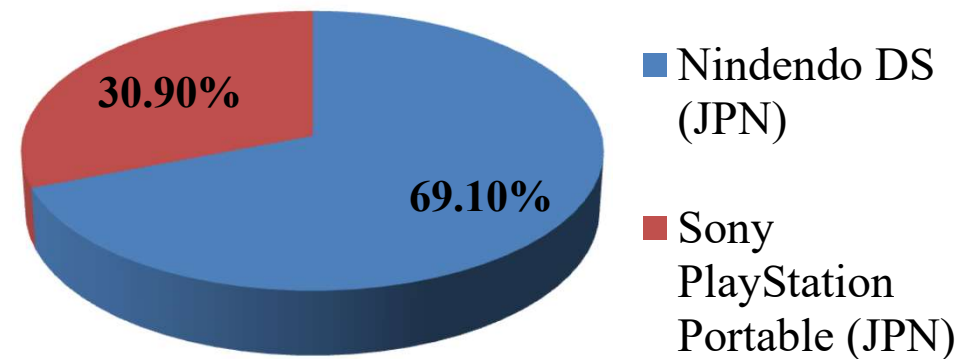
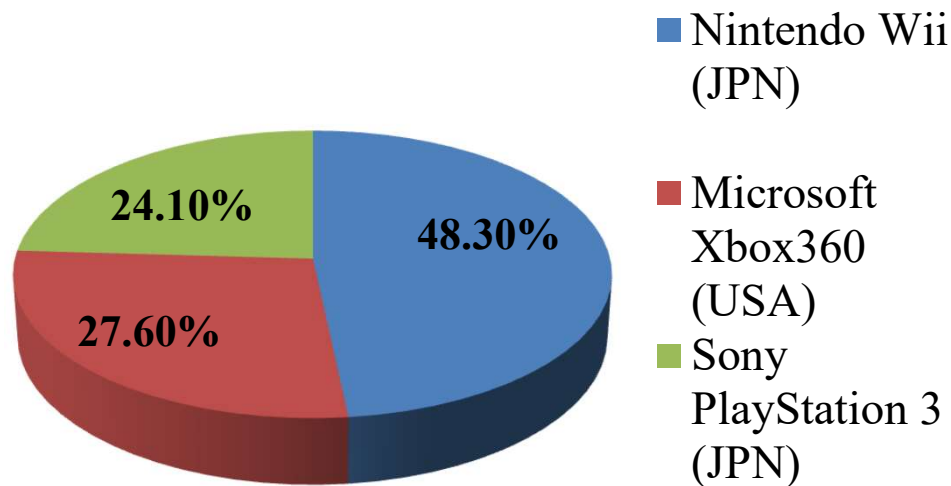
- > Many Japanese competitors.
- > **New entrants** came into the camera industry from other industries (*e.g.*, Film makers such as Fuji Film & Konica)

# Theories of International Trade



## Japan's Game Industry

### Home video game console



### Portable game console



## ■ Japan's Game Industry

### Resource endowments

- > Large pool of **skilled cartoon artists & game developers**.

### Domestic demand

- > **Demanding home customers** who were constantly looking forward new versions or new genres.
- > **High penetration of video games** in the Japanese market.

### Related & supporting industries

- > **Japanese comic book & animation industries** are world leaders.
- > Strong **cluster** about comic books, animation, games etc.

### Firm strategy, structure & rivalry

- > **Intense local rivalry** among many Japanese developers (more than 500 third-party software developers provide game software to Sony)



## ■ Limitations of Porter's Diamond Model

- ❖ The diamond model places **too much emphasis on domestic conditions** (*e.g.*, **Overseas demand** → India's IT industry).
- ❖ The model has **NOT** been comprehensively tested.
- ❖ Companies & countries do **NOT** depend on **domestic factor conditions** (*e.g.*, Capital & managers' international mobility)
- ❖ **Advancements in transportation & the relaxation of import restrictions** allow companies & countries to gain products & services from foreign markets.
- ❖ The lack of any of the **'4'** facets of the diamond does **NOT** necessarily prevent companies & countries from gaining competitive superiority internationally.



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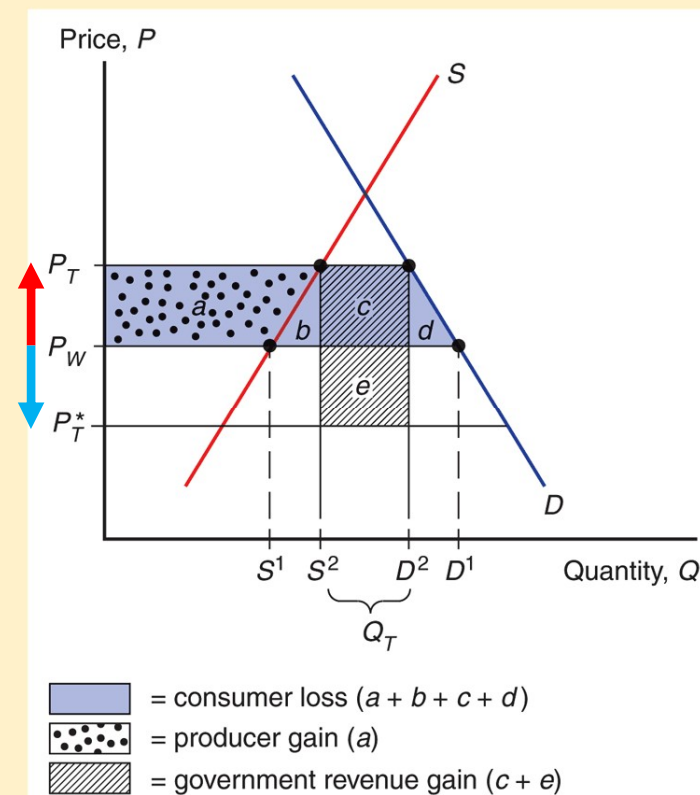
## ■ Tariff Barriers: 2 Economies Model) ■ Non-Tariff Barriers

- > **Subsidies:** Government payments to domestic firms.
- > **Import quotas:** Restrictions on the quantity of imports.
- > **Voluntary export restraints (VER):** An international agreement in which exporting countries voluntarily agree to restrict their exports.
- > **Local content requirement:** A requirement that a certain proportion of the value of the goods made in one country.

**Figure 8-9**

### Costs and Benefits of a Tariff for the Importing Country

The costs and benefits to different groups can be represented as sums of the five areas *a*, *b*, *c*, *d*, and *e*.





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## ■ Location, Location, Location !

- ❖ Discover & leverage **comparative advantage** of world-class locations.
- ❖ For instance, as managers aggressively tapped into **Argentina's comparative advantage in wine production**, its wine exports grew from \$6 million in 1997 to \$500 million in 2008.

## ■ Comparative Advantage is Not Fixed !

- ❖ **Monitor & nurture** the current comparative advantage of certain locations & take advantage of new locations.

## ■ Master the Game of Twisting Politicians' Arms

- ❖ **Be politically engaged** to demonstrate, safeguard, & advance the gains from international trade.

# The End of Today's Lecture



ご清聴有難う御座いました。

**Thank you so much!**

**Vielen Dank für Ihre Aufmerksamkeit!**

**Grazie mille !**

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