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978-1-107-03672-7 - International Economics and Business: Nations and Firms in the Global Economy:  
Second Edition

Sjoerd Beugelsdijk, Steven Brakman, Harry Garretsen and Charles Van Marrewijk

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From the first edition: ‘This book is a remarkable achievement. It covers all the pressing international economic issues of our day in an accessible yet thorough manner. The authors adroitly combine illustrative data and essential theory to explain the hows and whys of trade and trade liberalization, the delocation of firms and multinational activity, capital flows, currency and financial crises, and the role of international organisations such as the IMF and WTO. It is appropriate for students without an economics specialization both at the undergraduate and non-specialists graduate level, e.g. MBA and Masters of Public Administration. The facts and real-world feel of the book make it interesting as a supplement for specialist students as well.’

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Second Edition

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University of Groningen

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University of Groningen

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CONTENTS

List of figures	<i>page</i> xi
List of tables	xv
List of boxes	xvii
Preface	xix

**Part I**      **Introduction**      **1**

<b>1</b>	<b>The global economy</b>	<b>3</b>
1.1	Introduction	3
1.2	A sense of time: the universe and population	4
1.3	Income levels: GNP and GDP	10
1.4	What is the global economy?	17
1.5	Globalization and income	20
1.6	Globalization and international trade	24
1.7	Analysing the global economy	27
1.8	Conclusions	35
<b>2</b>	<b>Getting the numbers right</b>	<b>38</b>
2.1	Introduction	38
2.2	Trade and multinational activity	39
2.3	Trade data and the current account	41
2.4	FDI data and the capital account	46
2.5	Sales and value added data	58
2.6	The right type of data	66
2.7	Measuring international capital mobility	69
2.8	Conclusions	75
	Appendix	76

**Part II**      **Firms, trade, and location**      **79**

<b>3</b>	<b>Trade, comparative advantage, and competition</b>	<b>81</b>
3.1	Introduction	81
3.2	Comparative advantage: David Ricardo’s fundamental insight	82
3.3	Comparative advantage versus competitiveness	88
3.4	Comparative advantage: the neo-classical answer	92

3.5	The closed economy	94
3.6	Open economy international trade: the Heckscher–Ohlin result	98
3.7	Factor endowments and competitiveness	103
3.8	Conclusions	104
<b>4</b>	<b>Modern trade theory: the role of the firm</b>	<b>105</b>
4.1	Trade and imperfect competition	105
4.2	Understanding intra-industry trade: imperfect competition	109
4.3	The trading equilibrium	112
4.4	Monopolistic competition	114
4.5	Trade with monopolistic competition	118
4.6	Empirical support for intra-industry trade	121
4.7	Firm heterogeneity	123
4.8	Conclusions	131
<b>5</b>	<b>Trade restrictions and trade policy</b>	<b>132</b>
5.1	Introduction	132
5.2	Tariffs and trade restrictions	133
5.3	Effects of tariffs	136
5.4	World welfare effects of trade restrictions	140
5.5	Additional effects of protectionism	141
5.6	Trade agreements	145
5.7	Strategic interaction between firms: the Airbus–Boeing example	151
5.8	Evaluation of the demand for and supply of trade protection	156
<b>6</b>	<b>Firms, location, and distance</b>	<b>157</b>
6.1	Introduction	157
6.2	Transport costs	158
6.3	Modelling distance at the firm level	164
6.4	Modelling distance at the country level: the gravity model	174
6.5	Liability of foreignness and multiple types of distance	177
6.6	Integrative frameworks linking firm and country	184
<b>7</b>	<b>Managing across borders</b>	<b>190</b>
7.1	Introduction	190
7.2	Firm-specific advantages	191
7.3	Multi-locational or multinational?	193
7.4	Managing the global–local paradox	196
7.5	Three illustrations of managing the global–local challenge	199
7.6	Entry modes	212
7.7	Choosing the optimal entry mode	215
7.8	Conclusions	221



<b>Part III</b>	<b>Capital, currency, and crises</b>	<b>223</b>
<b>8</b>	<b>Exchange rates</b>	<b>225</b>
	8.1 Introduction	225
	8.2 Exchange rates	229
	8.3 Exchange rates and prices	237
	8.4 Effective exchange rates	241
	8.5 Arbitrage and interest parity	246
	8.6 Conclusions	254
<b>9</b>	<b>Currency crises and exchange rate policy</b>	<b>256</b>
	9.1 Introduction	256
	9.2 What is a currency crisis?	257
	9.3 Characteristics of currency crises	261
	9.4 First-generation models of currency crises	264
	9.5 Second-generation models of currency crises	269
	9.6 Expectations and contagion	273
	9.7 The exchange rate and the policy trilemma	276
	9.8 Looking ahead	281
<b>10</b>	<b>Gains from international capital mobility</b>	<b>282</b>
	10.1 Introduction	282
	10.2 International allocation of savings and investment	284
	10.3 The degree of international capital market integration and a puzzle	289
	10.4 Does capital flow in the wrong direction?	292
	10.5 Capital flows and risk diversification	299
	10.6 Firm investment and asymmetric information	304
	10.7 Conclusions	310
<b>11</b>	<b>Financial crises, firms, and the open economy</b>	<b>311</b>
	11.1 Introduction and terminology	311
	11.2 An asymmetric information view of financial crises	313
	11.3 A financial crisis framework	316
	11.4 Financial crises in an open economy	317
	11.5 Wake-up call and perverse savings	322
	11.6 Twin crises	325
	11.7 Bad fundamentals or malicious investors?	328
	11.8 Synthesis and conclusions: a vicious circle	331
<b>12</b>	<b>The Great Recession</b>	<b>333</b>
	12.1 Introduction	333
	12.2 Seeds of the crisis	335

Contents

12.3	A banking crisis	340
12.4	Financial crisis and real impact I: trade collapse	341
12.5	Financial crisis and real impact II: output decline	346
12.6	Global value chains and the bullwhip effect	350
12.7	Policy and public debt in the wake of the current crisis	353
12.8	European currency crisis	356
12.9	International capital mobility, crises, and policy	362
12.10	Two examples of capital restrictions	368

<b>Part IV</b>	<b>Consequences of globalization</b>	<b>373</b>
----------------	--------------------------------------	------------

<b>13</b>	<b>Globalization and growth</b>	<b>375</b>
13.1	Introduction	375
13.2	Catching up	376
13.3	Production, capital, and investment	378
13.4	Empirical implications	382
13.5	Technology, knowledge, innovation, and TFP growth	390
13.6	Open economies, TFP, and economic growth	392
13.7	A historical example: Japan	399
13.8	A recent example: China	402
13.9	Conclusions	408
<b>14</b>	<b>Globalization and inequality</b>	<b>409</b>
14.1	Introduction	409
14.2	Globalization and income growth: the big picture	410
14.3	Trade, skills, wages, and technology	414
14.4	Globalization and labour migration	419
14.5	Globalization and income distribution	422
14.6	Global income inequality	429
14.7	Outsourcing, skills, and development	433
14.8	Conclusions	437
	Bibliography	438
	Author index	459
	Subject index	463

FIGURES

0.1	Firm decision tree and book overview	<i>page</i> xxi
1.1	‘Big Bang’ and beyond	5
1.2	Development of world population over the last 2,500 years	6
1.3	Development in world population, UN projection to 2100	7
1.4	GDP and GNP, current \$, 2010	11
1.5	Correction of GDP per capita for purchasing power, 2010	15
1.6	Development of world per capita income over the last 2,000 years, logarithmic graph	20
1.7	Advantages and disadvantages of logarithmic graphs	21
1.8	Leaders and laggards in GDP per capita: a widening perspective	23
1.9	Carrying capacity of European merchant fleets, 1470–1780, metric tons	25
1.10	Two ‘waves’ of globalization, merchandise exports, per cent of GDP	26
1.11	Trade and market integration	28
1.12	London external bond spread, 1870–1940, 14 core and empire bonds	32
1.13	Foreign capital stocks, assets/world GDP, 1860–2000	32
1.14	Relative migration flows, Western Europe and Western offshoots, 1870–2010, per 1,000 inhabitants	34
1.15	Traditional and globalized fragmented production processes	35
1.16	Change in night light intensity on the Korean peninsula, 1992–2008	36
2.1	Home firm decision tree	39
2.2	Horizontal and vertical multinational activity	40
2.3	US export shares in 2010	41
2.4	A country’s balance of payments	46
2.5	Current account balance, per cent of GDP, 1980–2012	47
2.6	FDI flows, 2005–2011	51
2.7	Value added export (VAX) as a share of GDP, 1995 and 2008 (per cent)	61
2.8	Value added distribution of an Apple iPad, 2011	62
2.9	Global net capital flows, average for 15 countries, 1870–2010	70
2.10	Capital outflows for selected countries (per cent of national savings)	70
2.11	Evolution of British and American share in foreign assets	72
2.12	Net private financial flows to developing economies, \$ bn, 1992–2009	73
3.1	Labour productivity and GDP per capita, 2009	86
3.2	Ratio of productivity in wheat (tonnes/ha) to productivity in sugarcane (tonnes/ha)	87
3.3	Knowledge spillovers in developing countries, 1971–1990	94
3.4	An isoquant	96
3.5	Cost minimization	97

List of figures

3.6	Lerner diagram, <i>a</i> goods prices and <i>b</i> factor prices	97
3.7	The impact of international trade	99
4.1	Intra-industry trade: Grubel–Lloyd index for different income groups	107
4.2	Increasing returns to scale and perfect and imperfect competition, demand and costs	112
4.3	A trading equilibrium: monopoly versus duopoly, demand and costs	113
4.4	Intra-industry trade as a result of transportation costs	115
4.5	The varieties approach of monopolistic competition	116
4.6	Monopolistic competition, demand and costs	117
4.7	Monopolistic competition and foreign trade pressure, demand and costs	120
4.8	Export orientation of US manufacturing firms, 2002	124
4.9	Distribution by number of products and export destinations, USA, 2000	125
4.10	Simultaneous exporting and importing, US manufacturing, 1997	126
4.11	Firm heterogeneity, prices, and profits	127
4.12	Firm heterogeneity and trade	128
4.13	Productivity and firm type in Latin America, 2006	129
5.1	Worldwide applied tariff rate, 1988–2010	133
5.2	US average tariffs, 1820–2010	134
5.3	Applied tariff rate, simple mean, all products, 2010	135
5.4	Domestic welfare effects of imposing a tariff	138
5.5	The world welfare effects of a tariff	140
5.6	‘Predicted’ duration of the Doha round	147
5.7	Customs union: trade creation	149
5.8	Customs union: trade creation and diversion	151
5.9	Additional trade costs of NTM measures in EU–US trade, 2010 (per cent)	155
6.1	<i>Ad valorem</i> trade costs by exporting country, 2008 (per cent)	160
6.2	Container port traffic, mn TEU 20-foot equivalent units, 2000–2010	161
6.3	Developments in world air transport freight, mn ton-km, 1975–2010	162
6.4	Home firm decision tree	164
6.5	Profits in the Home and Foreign market: national exporting firm	166
6.6	Going multinational: the horizontal case	167
6.7	Going multinational: the vertical case	168
6.8	Geographic distance and foreign sales of US multinationals	178
6.9	Cultural distance and foreign sales of US multinationals	180
6.10	Institutional quality and foreign sales of US multinationals	182
6.11	Liability of foreignness for a horizontal multinational	184
6.12	Porter’s diamond model	185
7.1	Transferring subsidiary resources to the multinational	198
7.2	Correlation in cultural characteristics	201
7.3	Increase in taxes if used to prevent environmental pollution	206
7.4	Acquisition waves, 1895–2012	214
7.5	Distance distribution of IKEA’s first stores over time, 1963–2011	220
8.1	Exchange rates, trade, and multinational activity	227
8.2	Some exchange rates, daily data, 2000–2011	231

List of figures

8.3	Australia–USA, spot and forward exchange rates of US dollar, 1976–2011	235
8.4	Global foreign exchange market turnover, 1998–2010	236
8.5	Most used currencies on the foreign exchange market, 1998–2010	237
8.6	Exchange rates and prices, 1960–2009	238
8.7	Exchange rates and intervention	241
8.8	<i>De facto</i> exchange rate arrangements, 30 April 2010	242
8.9	US dollar: effective exchange rates, 1973–2011	243
8.10	Out-of-sample exchange rate forecasting	246
8.11	Canada, interest rates and inflation rate (CPI), 1970–2011	247
8.12	UK, interest rates and term structure, 1980–2011	248
8.13	Two investment options	249
8.14	Australia–USA; 12-month covered interest parity	250
9.1	The Asian crisis: rapid drop in the value of some currencies, 1985–2002	258
9.2	Currency crashes since 1800	259
9.3	The Asian crisis: current account balance, 1990–2009 (per cent of GDP)	261
9.4	The Asian crisis: developments of GDP per capita, 1990–2009	264
9.5	Interest rates for selected euro area countries, 1993–2012	270
9.6	The policy trilemma	277
10.1	International capital mobility is welfare enhancing	286
10.2	Capital reallocation between Home and Foreign	293
10.3	Firm investment, supply of funds, and asymmetric information	305
10.4	Bank efficiency scores, per cent rank and score (%)	307
11.1	Stylized balance sheets of firms and banks	315
11.2	Financial crisis in an asymmetric information framework	316
11.3	Current account balance of selected EU countries, 2006–2012	318
11.4	Global imbalances, current account balance (\$US bn), 1970–2011	319
11.5	Foreign-held US government debt (US\$ bn), 2011	320
11.6	Perverse savings and the backward-bending savings curve	325
11.7	Currency crises and ongoing banking crises, 1970–2012	326
11.8	The unfolding of a financial crisis	327
11.9	The vicious circle of financial crises	331
12.1	American house prices, 12-month moving average, 1987–2012	336
12.2	Stock market index, monthly data, 1987–August 2012	341
12.3	Maximum loans by Federal Reserve to selected banks (\$US bn), 2008–2009	341
12.4	Great Recession: real world trade flows (index), 1970–July 2012	342
12.5	Trade volumes and the Great Recession, 2004–July 2012	344
12.6	Surprise! OECD’s changing world trade growth projections for 2009	346
12.7	Industrial production, monthly growth rates, 2007–July 2012	347
12.8	GDP per capita (PPP), countries with growth and decline (per cent), 2000–2011	348
12.9	USA retail and manufacturing sales, index (1992 = 100), 1992–August 2012	351
12.10	USA inventory/sales ratio, index (period average = 100), 2002–July 2012	352

List of figures

12.11	Government net lending/borrowing (per cent of GDP), 2012–2017	355
12.12	Expected general government gross debt (per cent of GDP), 2012	356
12.13	Emerging markets, 20 largest foreign exchange reserves, mid-2011 (\$ bn)	357
12.14	Total factor productivity index, 1989 = 100, 1989–2011	358
12.15	Sovereign ratings in Europe since 2005, long-term foreign currency	359
12.16	Sovereign ratings since 1997, long-term foreign currency	361
13.1	France, share of income invested, 1950–2010, per cent	381
13.2	Income levels and capital accumulation (Solow)	382
13.3	USA, GDP per capita, 1870–2010 (log scale)	383
13.4	Income per capita and secondary schooling rate, 2010	384
13.5	Income per capita and years of schooling, World Bank regions, 1960–2010	385
13.6	Japan and Indonesia, income per capita, 1970–2010	386
13.7	Overview of technology spillovers in an open developing economy	389
13.8	Inter-temporal adjustments in Singapore, 1972–2010, current account balance, per cent of GDP	393
13.9	Rapid growth in Europe–Asia trade, 1500–1800	395
13.10	Multinational trade composition	396
13.11	A Dutch ship in Nagasaki, 1859	400
13.12	The Japanese economy, 1500–2008, GDP and exports, per cent of world total	401
13.13	Developments in Chinese income and trade flows, 1960–2011	403
13.14	The Dupuit triangle	406
13.15	Dynamic costs of trade restrictions	407
14.1	Income levels, growth rates, and population, 1980–2010	411
14.2	Total factor productivity index, 1989 = 100, 1989–2011	417
14.3	Changes in US real income, working adults, by education, 1991–2010	418
14.4	Workers’ remittances received, per cent of GDP, 2010	420
14.5	Labour reallocation between Home and Foreign	421
14.6	Number of poor people in the developing world, 1981–2008	423
14.7	Poverty headcount ratio at \$1.25 a day (PPP), per cent of population, 1981–2008	424
14.8	Global income distribution, 1970 and 2006	425
14.9	The Lorenz curve and the Gini coefficient	428
14.10	Income inequality, Gini coefficient, selected countries, 1981–2010	430
14.11	Global income inequality, Gini coefficient, 1970–2006	431
14.12	Income inequality decomposition, across and within countries, 1970–2000	432
14.13	Development and income inequality, some historical examples	433

TABLES

1.1	The twenty countries with highest population and population density, 2010	<i>page 7</i>
1.2	Population projections, 2000–2050, the world and continents	8
1.3	The twenty most powerful economies, 2010	12
1.4	Assumed labour productivity, Australia and Botswana	14
1.5	Price convergence and declining transport cost, 1870–1913	30
1.6	Tariffs on manufactures for selected countries, 1820–2010 (per cent)	31
2.1	US imports and exports (US\$ bn), 2010	42
2.2	A firm’s statement of income	43
2.3	Funding options for multinationals	49
2.4	Inward FDI stock (US\$ bn), 2009	52
2.5	FDI stocks and flows (US\$ bn) (per cent), 2011	53
2.6	Analytic presentation: balance of payments (US\$ bn), 2007	55
2.7	FDI inflows and outflows, as percentage of total flows	58
2.8	US outward multinational activity in 2010	59
2.9	Top ten non-financial multinationals, 2011	60
2.10	Country of origin of global 500 between 2005 and 2010	63
2.11	GDP, sales and profits in 2009 (US\$ bn)	67
2.12	Size of net capital flows for selected countries, 1870–2010	69
2.13	Gross financial stocks, ratios, and shares	71
2.A1	Overview of tax havens	76
2.A2	Global 500: top 20 largest firms of the world (US\$ bn), 2010	77
3.1	Hypothetical labour productivity, production per hour	83
3.2	Production of cloth and wine in the EU and the USA	84
3.3	Sign tests of factor abundance	102
4.1	Intra-industry trade per country in 2006, ranked from high to low	107
4.2	Cross-country determinants of intra-industry trade, 2006	123
4.3	Exporter premia in US manufacturing, 2002	124
4.4	Productivity, exports, and foreign ownership	130
5.1	GATT and WTO rounds since 1947	146
5.2	Airbus–Boeing strategic interaction pay-off matrix	153
5.3	Strategic interaction pay-off matrix after Airbus subsidy	153
6.1	Regional trade pattern of Europe, percentage of total, 1860–2009	159
6.2	The world’s largest container ports, mn TEU, 1989 and 2009	162
7.1	Brand name and technology as firm-specific advantages	194
7.2	Multinationals as a special case of multi-locational firms	194
7.3	Integration-responsiveness framework	197

List of tables

7.4	International cultural diversity in four dimensions, index scores	200
7.5	Effectiveness of downsizing	204
7.6	Stock exchange reactions to downsizing announcements	205
7.7	Nature, motives, strategies, and modes of business activity	212
8.1	Some international currency symbols	230
8.2	Some spot exchange rates on 24 July 2012, at 8.29 a.m. ET	231
8.3	Cross exchange rates, spot, 3 August 2011	232
9.1	Real income growth from before to after the crisis	263
9.2	Coordination of a speculative attack	268
9.3	The incidence of global contagion, 1970–1998	275
9.4	Looking for the trilemma: estimates of $\beta$	279
10.1	Respondents mentioning thrift as an important quality to teach children (per cent)	289
10.2	Correlation between national savings and investment, 1960–2010	291
10.3	The Feldstein–Horioka test	291
10.4	Shareholder and creditor protection in countries with different legal origins	298
11.1	Costs and duration of banking crises, 1970–2011	312
11.2	Possible relationships between signals and crises	327
11.3	Percentage of crises accurately predicted	328
12.1	Time line of main events during the Great Recession, 2007–2012	334
12.2	Extent and duration of per capita income decline during Great Recession	349
12.3	Classification of policy measures	354
12.4	Credit ratings of main agencies	360
12.5	Gross capital inflows to Chile (millions of \$US)	370
13.1	GDP per capita growth projections, 2000–2010	377
13.2	GDP per capita growth rates per decade, 1950–2010	377
13.3	GDP per capita growth projections, 1950–2010	378
13.4	European output and TFP growth, 1870–2008	387
13.5	Firm-level impact of importing intermediates on total factor productivity	398
14.1	Trade policy adjustment, time trend of $\ln$ (income per capita), 1950–2001	414
14.2	Income inequality	427



BOXES

1.1	Purchasing power parity (PPP) corrections	<i>page</i> 14
1.2	Logarithmic graphs	21
1.3	Measuring economic growth from outer space	36
2.1	Dutch GAAP versus US GAAP	44
2.2	Inter- and intra-firm trade and transfer pricing	48
2.3	FDI data criticized	56
2.4	A transnationality index	60
2.5	Who earns what when an iPad is sold?	62
2.6	Global value chain specialization	64
2.7	Why accounting is useful and why accounting is not explaining	68
3.1	Wages and productivity	86
3.2	The world is flat	91
3.3	Knowledge spillovers	93
3.4	Isoquants	96
3.5	Empirical tests of factor abundance: Ricardo revisited?	101
4.1	Intra-industry trade	106
4.2	Profit maximization	111
4.3	Alternative explanations for intra-industry trade	115
4.4	Models compared	119
4.5	Firm heterogeneity: data for USA	123
4.6	Firm heterogeneity in Latin America	129
5.1	The costs of protection	137
5.2	The EU–USA steel conflict	143
5.3	WTO and GATT trade rounds	145
5.4	The politics of free trade zones: how many trade blocs?	152
5.5	Non-tariff measures	154
6.1	The death of distance or a spiky world?	163
6.2	Nasty econometrics	176
6.3	Measuring cultural distance	180
6.4	Regional clusters	187
7.1	The home-country effect on multinational behaviour	202
7.2	Americanization?	204
7.3	Institutional theory	211
7.4	Real option theory	216
7.5	IKEA’s internationalization over time	219
8.1	Foreign exchange risk, hedging, and multinational firms	228
8.2	Black markets	236

8.3	Forecasting exchange rates and random walks	245
8.4	The empirics of covered interest parity	250
8.5	How to test for uncovered interest parity (UIP)	253
9.1	A game-theoretic illustration of speculative coordination	267
9.2	The second-generation model of currency crises	272
10.1	Important qualities to teach children: thrift and saving money	288
10.2	A legal origin view of financial institutions	296
10.3	Insurance against shocks through portfolio diversification	301
10.4	The home and foreign bias	303
10.5	The financing of firm investment and the external finance premium	309
11.1	Moral hazard and over-investment: an example	323
11.2	Are foreign subsidiaries better at handling financial crises?	329
12.1	The Great Moderation	339
12.2	The OECD’s big surprise	345
12.3	Credit rating agencies	359
12.4	Asset-price inflation	365
12.5	Banking policy options and moral hazard behaviour	366
12.6	Political risk and the multinational firm’s investment strategy	370
13.1	Growth accounting and growth modelling	379
13.2	Human capital (schooling) and development	384
13.3	Technology spillovers and development	388
13.4	VOC – the world’s first multinational	394
13.5	Firm-level productivity, imports, policies, and development	397
13.6	Dynamic costs of trade restrictions	405
14.1	Open-to-closed or closed-to-open economies and (asymmetric) growth	413
14.2	The economic effects of international migration	421
14.3	Measuring income inequality	426
14.4	Development and income inequality	432
14.5	Terms of trade: the Prebisch–Singer hypothesis	436

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978-1-107-03672-7 - International Economics and Business: Nations and Firms in the Global Economy:  
Second Edition

Sjoerd Beugelsdijk, Steven Brakman, Harry Garretsen and Charles Van Marrewijk

Frontmatter

[More information](#)

## PREFACE

*International Economics and Business* offers an integrated perspective on the (changing) role of nations and firms in the global economy. It is partially based on an earlier book published by Cambridge University Press in 2006, written by three of the present four authors (in conjunction with Arjen van Witteloostuijn) and entitled *Nations and Firms in the Global Economy*. Although the basic idea has remained the same, the underlying philosophy and overall organization of this book are more explicit and pronounced. We discuss aspects of the global economy typically found in international economics and in international business. The book is targeted at first- or second-year undergraduate students, and we have written the book in such a way that students familiar with basic calculus and mathematics are able to understand the material we present. In terms of a typical economics or business curriculum, this means that you have probably had introductory courses on statistics and microeconomics. If you are a student enrolled in an economics programme, this book serves as an introduction to international economics, including a discussion on the most essential theories of international business. If you are a student following a business programme, this book serves as an introduction to international business, including a discussion of the essentials of international economics. Having successfully mastered the material we present to you in this book, an economics student may subsequently follow an intermediate international economics course, while a business student may continue by taking an intermediate international strategy course. We provide common ground for both undergraduate communities.

### Teaching philosophy

This book is based on a teaching philosophy developed in approximately 80 years of cumulative teaching experience in international economics and international business, including a substantial number of years in undergraduate programmes. Over the years we have become more and more convinced of the need to focus on the explanation of the big picture in international economics and business. Sure, you need to learn about intricate details of balance of payments, internationalization process models, and exchange rate developments, to mention just a few aspects, but in the end the added value of a course on international economics and business is the ability to *link* the different concepts and understand the relationships that allow you to ‘get the big picture’. From the start of this project, our goal has been to provide this picture. Moreover, instead of providing just another introduction on international economics or on international business as separate topics, we explicitly integrate these two fields of inquiry (more on that below). Whilst writing and developing our

book, we followed two educational principles (see below). The first principle is taken from Ed Leamer (2009), an econometrics professor at the University of California in Los Angeles. The second principle cannot be attributed to anyone in particular, although Nobel laureate George Stigler is sometimes mentioned.

1. People are pattern-seeking story-telling animals.
2. The plural of anecdote is not evidence.

The first principle relates to the need for human beings to structure the world around them in order to understand it. This is exactly what we offer you in this book; we structure the world of international economics and business in such a way that it helps you to understand the contemporary global economy. *Patterns* have a history, however, which means that in order to understand the contemporary global economy you need to have some historical knowledge because patterns in the social sciences tend to be path-dependent. The position of nations and firms today (at time  $t$ ) is related to their position yesterday (at time  $t-1$ ). Throughout this book, we therefore discuss the relevant historical background when necessary. We use a variety of instruments to clarify. First, we introduce a decision tree in the next section for a firm that considers going abroad and describe the different options this firm has. This decision tree is used in Chapter 2 when discussing types of multinational activity, in Chapter 6 when discussing the central role of distance in international economics and business, and again in Chapter 8 when explaining the role of exchange rates. Using the same instrument at these occasions supports the integration and discovery process, and facilitates the learning process. Second, whereas international economics books tend to focus on nations and international business books on firms, we combine the two in one consistent framework. We do so by taking a bottom-up perspective in which trade and investment patterns emerge as firms make internationalization decisions that are driven by their wish to generate value added abroad, subsequently affecting home and host countries. This perspective is also reflected in the decision tree used throughout.

The second principle implies that our book is *research driven*. It is not a collection of anecdotes, but based on research in international economics and international business. What we present to you is not just a set of examples, but the combination of relevant insights and theories based on and derived from fundamental research. We think that cases and examples are helpful, but that they should not be the starting point for getting the big picture. For that reason, we start from theory and use case insights as complementary pieces of information, thus balancing analytical reasoning and discussions on data and numbers. Related issues are discussed in additional boxes.

### Organization

To discuss international economics and international business in an integrated way, we use a decision tree as our starting point (see Figure 0.1). It depicts a set of choices for a firm considering going abroad, usually driven by the wish to generate additional value added. Even if a firm goes abroad for strategic reasons, it still has to do so in the most

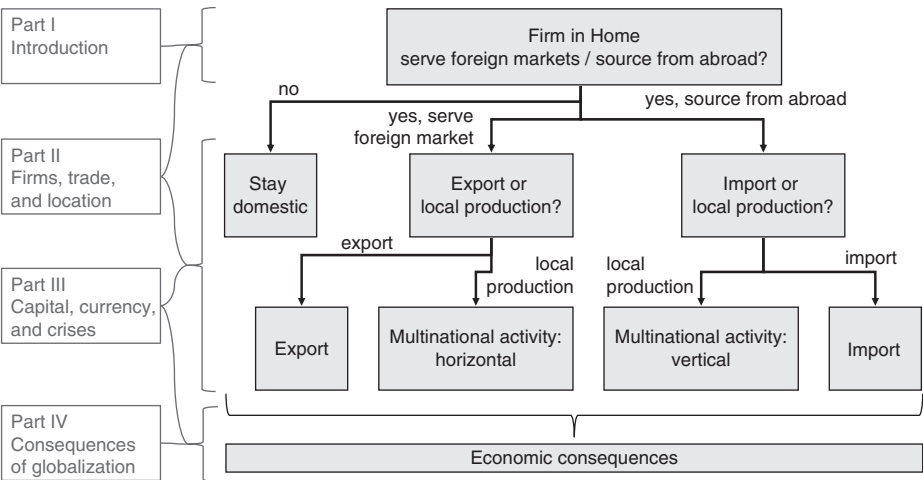


Figure 0.1 Firm decision tree and book overview

efficient and effective way. A firm may go abroad either to *sell* or to *buy* goods or services (see the first stage of the decision tree). If the firm decides to sell abroad it has two basic options, namely (i) to produce at home and export goods to serve the market in the other country or (ii) to start production in the host country and serve the foreign market from that production facility. In the second case, the firm becomes a (horizontal) multinational, that is, a firm which owns and controls activities in more than one country. If a firm decides to source from abroad there are also two options, namely (i) import from abroad or (ii) start local production in the host country and send these goods back to the home country for use in the local production process (intra-firm trade). In the second case the firm becomes again a (vertical) multinational. This summarizes the second stage of the decision tree in Figure 0.1, used throughout the book to discuss aspects of international economics and business.

The book is organized in four parts, largely in line with the flow through the firm’s decision tree illustrated in Figure 0.1, including the consequences for nations and firms.

- Part I: ‘Introduction’, consists of two chapters. Chapter 1 discusses the history and structure of the globalization process and introduces the global economy in terms of population, income, trade flows, and capital flows. Chapter 2 discusses the motivations for internationalization and the data that are used to measure the resulting flows of international business activity at the country level (the balance of payments).
- Part II: ‘Firms, trade, and location’, consists of five chapters in which we elaborate on the core of the decision tree that can be used to explain trade flows (Chapters 3–5) and multinational activity (Chapters 6 and 7). Chapter 3 focuses on comparative advantages through technology differences and factor abundance, leading to competitive advantages and outsourcing. Chapter 4 focuses on the role of heterogeneous firms in modern trade theory based on economies of scale, leading to intra-industry

trade, gains through love-of-variety and market size, and strategic advantages. Using the insights gained from Chapters 3 and 4, Chapter 5 then evaluates the effectiveness of trade restrictions and trade policy. The notion of firm heterogeneity is relevant when discussing multinational firms. Chapter 6 discusses how firms deal with all sorts of additional costs that they face when starting activities abroad, measured by geographic, cultural, institutional, and linguistic distance. Part II concludes in Chapter 7 with a discussion of how firms effectively and efficiently manage the firm-specific advantages they need to overcome the ‘liability of foreignness’ when going abroad.

- Part III: ‘Capital, currency, and crises’, also consists of five chapters. This part focuses on the financial dimension of international economics and business, consisting of problems that firms have to deal with in the core of the decision tree and the associated resulting consequences for trade- and capital flows that nations have to deal with. Chapter 8 discusses exchange rates and how to manage risks and uncertainty using forward markets, arbitrage, and interest rate parity. Chapter 9 focuses on currency crises and (the limitations of) exchange rate policy. Chapter 10 reviews the benefits of international capital mobility and discusses the problems of moral hazard, asymmetric information, and adverse selection. Chapter 11 brings together the issues discussed and learned in Part III in a consistent framework analysing financial crises and firms in the open economy. Chapter 12 concludes the financial part of our book by analysing in detail the causes and consequences of the current ‘Great Recession’ and putting this in a broader perspective.
- Part IV: ‘Consequences of globalization’, consists again of two chapters and brings together the most important implications of what we have learned in Parts II and III for the nations, firms, and people of the global economy. Chapter 13 focuses on the implications of globalization for economic growth by discussing the links between open economies and capital accumulation, technology, innovation, knowledge spillovers, and productivity. Chapter 14 concludes our book by reviewing the evidence on the links between globalization and inequality, including poverty, remittances, skill bias, the global income distribution, and the impact of outsourcing.

### Supporting website

We have made supporting material available on the website associated with this book ([www.cambridge.org/ieb](http://www.cambridge.org/ieb)). In line with our two educational principles, we provide review exercises and data exercises allowing students to familiarize themselves with the right numbers. We also make available all tables and colour versions of the figures used in the book. For instructors, we provide (PowerPoint) presentations of the chapters of the book and brief, indicative answers for the exercises.

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The authors

As already mentioned, we have a cumulated teaching experience of approximately 80 years. All of us have been teaching courses at undergraduate and graduate levels, at all major economics and business faculties in the Netherlands. All of us are active as researchers in the field of international economics and business and have numerous publications dealing with trade, investment, and globalization. Sjoerd Beugelsdijk is professor of international business and management at the University of Groningen, where he also serves as the academic director of the IB undergraduate programme. Steven Brakman is professor of international economics at the University of Groningen and academic director of the master programme in international economics and business. Harry Garretsen is professor of international economics and business at the University of Groningen, as well as dean of the faculty of economics and business. Finally, Charles van Marrewijk is professor of international macroeconomics at Utrecht University and director of the Tjalling Charles Koopmans Institute.