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SK, Shanthi and Sircar, Sanjoy and Reddy, Kotapati  
Srinivasa

India Development Foundation, Great Lakes Institute of  
Management

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# Global Trade/Capital Flows and Competitiveness

SK Shanthi, Sanjoy Sircar, K. Srinivasa Reddy

2015

## *Guest Editors*

### **SK Shanthi**

Director,  
India Development Foundation,  
Gurgaon (Haryana, India).

### **Sanjoy Sircar**

Professor and Director-PGPM,  
Great Lakes Institute of Management, Chennai,  
Dr V Balachandar Campus, ECR Road, Manamai,  
Tirukazhukundram Taluk, Kanchipuram – 603102 (Tamil Nadu, India).

## *Handling Editor*

### **K. Srinivasa Reddy**

Independent Researcher–Management,  
Amaravathi (New Capital City of Andhra Pradesh),  
Guntur (Andhra Pradesh, India).

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# Global Trade/Capital Flows and Competitiveness

(Special Issue Editorial)

## Abstract

**Purpose:** The purpose of this special issue is to get a deeper understanding of global trade and investment flows and how they affect the competitiveness of economies. There have been some tectonic shifts in global flows both in terms of actual goods and services and also in terms of financial capital. The emerging economies have been aggressively competing in markets, which were hitherto dominated by the so-called developed world. This has been facilitated by the increased orientation towards openness in the emerging economies as also the other developing countries. These developments have been essential for strategically positioning them in the global marketplace and have been instrumental in improving the well-being of citizens across the globe.

**Design/Methodology/Approach:** The papers in this issue have a focused approach towards the various issues related to the over-arching theme of '*Global Trade/Capital Flows and Competitiveness*.' One of the important issues discussed in economic literature is that of the link between 'openness' and economic growth. This issue is explored in the context of India. It is also well known that some developing countries (most notably China) have benefited a great deal from the inward remittances of its diaspora. This issue is explored in the context of Sub-Saharan Africa in another paper. Another issues discussed is that of risks to shareholders in cross-border acquisitions. Some emerging economies have also gained financial strength and are exporting capital abroad. This and the issue of pricing strategies for optimization in service exports are also discussed.

**Findings:** The papers offer rich insights in to the different angles of the global trade and capital flows and are nuanced to specific countries or regions. They will contribute to a better understanding of the various issues and will be of great use to academics for further research and practitioners in their new policy initiatives in the area of improving their performance be it in terms of improving growth and exports or in terms of attracting capital from the capital surplus countries.

**Originality/Value:** All the papers are original contributions and it is our view that they will lead to better understanding of the implications of these trades and capital flows on individual country performance and to calibration of policies initiated by governments in this area.

**Keywords:** Economic growth, Openness, Capital flows, Remittances, Trade flows, Emerging markets, Competitiveness

**Paper type:** General review

We are honored to be the guest editors of this special issue on ‘*Global Trade/Capital Flows and Competitiveness*.’ This vast area abounds in rich contributions from academics the world over. In this special issue, we present an eclectic set of papers that address some specific and very important and current questions relating to globalization. Answering these questions to some extent, pave the way for strategically positioning emerging and other developing economies in the global marketplace and are instrumental in improving the well-being citizens across the globe.

Trade and business activities have increased significantly between countries, regions and continents in the light of liberalization of economic policies in developing economies. In the same vein, technology development, cross-culture integration, migration, improvement in education and income levels have contributed to the current economic growth of the world (Fatehi *et al.*, 2008). This two-way process has increased the competitiveness faced by the liberalizing countries from global corporates. Protectionism has been phased out systematically by most countries and they have thrown open their doors for global trade and investment flows. As a result, there has been a phenomenal growth in trade among developed and developing economies. The capital flows across countries have grown even faster, both in terms of foreign direct investments and in terms of institutional investments in the primary and secondary financial markets of countries around the world. However, the market for cross-border capital flows across the world has been declined around the 2007-08 global financial crisis (Reddy *et al.*, 2014). While protecting local firms from international competition, many developing economies have drafted and altered various institutional and/or trade laws, provisions and guidelines (Dima *et al.*, 2008; Pillania, 2009; Reddy, 2015a, 2015b). In fact, the entry of multinationals and the global investments have boosted the local competition in many of the host countries: India and China. In particular, Fatehi *et al.* (2008, p. 78) explain 11 major factors that affect international business environment (IBE): decreasing trade barriers; developing countries' attitude changes; adoption of export-oriented strategies by developing countries; spread of regional trade agreements; technological developments; global demand for capital; diminishing effectiveness of national borders; investments required in new technologies; effect of the internet; international terrorism; and increasing interdependence among nations. By contrast, they suggest that ease of cross-border travel and the information explosion ushered in by the web have also raised globalization and global competition (p. 88). Therefore, this special edition will answer some important issues raised in the current IBE and related literature.

Motivated by these factors, the special issue invited academic professionals to submit their research output on various assorted themes. Following the double blind review system, we have accepted six articles out of 31 submissions. We believe that the selected papers would add new knowledge to the existing literature on global trade and capital flows. We hope readers will enjoy reading them. Herewith, we present research summary for five selected articles and remaining article will be published in future issues of the journal.

Rudra P. Pradhan, Mak B. Arvin, and Neville R. Norman in their paper titled, '*A quantitative assessment of the trade openness–Economic growth nexus in India*', use progressive statistical techniques to study interactions between economic growth, openness to international trade and the coverage of equity markets and banking in India. They focus on whether causality runs both ways, one way, the other way or not at all, between these variables. They advance on previous studies for India and many other countries with (i) novel estimation approaches, and (ii) the inclusion of all four potentially two-way interacting variables. The mixture of some bi-directional and some uni-directional causality warns policy makers seeking to foster growth to check multi-causal studies involving all these variables before setting their policy stances. They, further, demonstrate the applications of the findings to trade liberalization, financial education related monetary policy improvements and reforms and direct growth incentives.

Reena Kohli in the paper titled, '*Financing strategies and shareholders' risk in cross border acquisitions in India*,' examines the effect of financing strategies employed in outbound cross border acquisitions on the risk structure of the acquiring companies. For this average  $\alpha$ 's (measuring the unsystematic risk) and average  $\beta$ 's (measuring the systematic risk) have been calculated for different event periods (viz. pre estimation, post estimation and pooled estimation periods) and across different modes of payment (viz. cash offers, stock offers and earnouts). The analysis reveals that across all the modes of payment, substantial shifts are visible in systematic risk of the acquiring companies in post and pooled acquisition periods whereas shifts in unsystematic risk are negligible. Further, the systematic risk has shown substantial decline in case of earnout offers whereas stock offers have shown a significant increase in the same. Cash offers are accompanied with a statistically insignificant reduction in systematic risk. The paper recommends earnout offers as a tool to mitigate the risk of adverse selection in case of cross border acquisitions where the acquiring companies are prone to such risk due to the lack information about the true worth of the target companies' resources.

Avik Sinha in the paper titled, '*Conceptualizing service export price optimization,*' studies the issue from the perspective of a profit-maximizing producer. The paper finds that considering the profit maximization objective of a service providing firm, optimization of the service price in international market can prove out to be a critical decision to make. This paper takes into consideration the demand and supply side aspects of the entire scenario and presents a comprehensive mathematical model for optimization of export price of services, along with a set of simulations for demonstrating the working of the model. In order to carry that out, both academic and applied implications of the model have been explored, with a hypothetical example for the academic purpose and another from the Indian IT industry.

Khanindra Das and Nilanjan Banik in their paper titled, '*What motivates Indian firms to invest abroad?*' study the increased capital flows, in the form of outward foreign direct investment from developing countries, with specific reference to India. India has emerged as one of the leading developing countries in terms of outward foreign direct investment. These investments are spearheaded by market-driven emerging multinationals, originating from both manufacturing and non-manufacturing sectors and motivated by various factors. The paper presents a detailed econometric analysis of foreign investment motives of emerging multinational firms from India during 2008-09 to 2011-12. The analysis shows that there are multiple motives for outward investment by Indian firms, both in the form of equity and in the form of debt, to different host countries. These motives of investment include but are not limited to the access to energy resources, technology and strategic assets, and a quest for efficiency. The findings challenge the conventional understanding that emerging multinationals from India primarily seek markets in their international foray, and bring to the fore several implications that are relevant for policy concerning capital outflows from India.

Daniel Tarus in the paper titled, '*Do diaspora remittances affect banking sector development in Sub Saharan Africa?*' looks into the role of inward remittances from diaspora and how they have contributed to strengthen the banking sector services in Sub-Saharan Africa. Diaspora remittances to countries of origin constitute the largest source of foreign capital flows after foreign direct investment. The paper contributes to the extant literature by looking specifically at the effect of diaspora remittances on banking sector development in Sub-Saharan Africa. The paper draws data from 23 Sub-Saharan African countries over the period 1994-2009, giving a sample of 345 country-year observations. Fixed effects regression was used to achieve this objective. It is concluded that increasing remittances to Sub-Saharan Africa enhances the development of the banking sector. The paper further concludes that the

capital flows from remittances have the potential to influence the competitiveness of emerging markets through the improved credit base of the market.

**Nominated Paper from this Special Issue to the Journal Annual Awards**

*Title:* What motivates Indian firms to invest abroad?

*Authors:* Khanindra Das and Nilanjan Banik

**Nominated Reviewer from this Special Issue to the Journal Annual Awards**

*Imlak Shaik, Assistant Professor, Department of Management Studies, BITS Pilani, India*

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