

Advantages and disadvantages of importing and exporting



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Introduction

International business is the core theme in conducting business in current era of globalization. In the competitive environment, businesses are competing at global level. In international business a company can engage in either of the two ways such as import or export. Import and export are the two basic and primary ways of conducting the business (Dunning, 2007). Whenever a company engages into the international business, there are lot many factors which impact the business. Hence there are advantages and disadvantages of both import and export. Considering this view, this assignment report addresses the critical analysis of two primary ways of occurring international business and respective advantages and disadvantages. In addition to this the assignment report also discusses the international business and free trade (Fortanier, 2008).

International Trade:

International trade is also known as global trade where the traders can exchange the goods or services and raw material across the borders. International trade was first started by the industrial revolution in US and spread across the globe in the late 18th and early 19th century. A drastic change in the communication, transportation and logistics has changed the way of conducting international business and simplified the process. The technological advancement and change in the communication and transportation facilities has surged the international trade in the 20th century. The present form of international trade has been transformed into the outsourcing and multinational companies(Gupta and Govindarajan, 2008). A dramatic rise has been noted in the trading volume from the mid of <https://assignbuster.com/advantages-and-disadvantages-of-importing-and-exporting/>

20th century. In the year 1928 the total export value in the world was approximately \$31.7 billion while after 70 years this figure is \$4,215,000.2 billion. In order to maintain the stability and equilibrium among the countries the formation of World Trade Organization came into existence (Hennart, 2004). The organization not only solves the trade matters but also support the developing countries in export their product and service to foreign countries. The commanding position in WTO is left with G-7 countries which include US, France, Germany, the UK, Italy, Japan and Canada. The organization controls the dynamics of international trade which also support in preparing the trade agreement between the nations. There are few trade theories which provide the overall view of international trade as discussed below:

Absolute Advantage Theory:

The absolute advantage theory provided the view about the capacity and control in terms of competitive landscape for international trade among the countries. According to this theory, if any country A can produce the products and service of same quality at lower cost of resources than the other country B then country A has absolute competitive advantage over country B. also for other commodities country B can have the absolute competitive advantage over country A. the great economist Adam Smith has put this theory forward to understand the international trade (Johanson and Wiedersheim-Paul, 2008).

Comparative Advantage Theory

Comparative advantage theory is the extension of absolute advantage

theory which stated that a country should produce only those items in which
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it has expertise and specialization for the purpose of developing the comparative advantage in terms of resources. In order to govern the pattern of trade the relative factor endowment has a key role ((Jones, 2006).

Heckscher-Ohlin Model

Heckscher Ohlin theory is some what different from absolute advantage and comparative advantage theory since it emphasizes only on the production factors in which the company has expertise and from that produce the goods. This theory stated that a country should export only those goods which are abundance in the country and for which the means of production factors can be utilized more intensively. In contrast the country should import only those goods in which the country is less capable for its means of production factors and also not available in abundance (Nelson and Winter, 2007). Therefore it has been observed that the factor of endowment and relative variation has key role in the pattern of international trade. As against this statement, Wasily Leontieff tested this theory empirically in which he found that the Hecksher Ohlin theory may not always be true. In support of this statement he stated that the export in US is for the commodities which are labor intensive however the country has abundance capital and this example is famous by the name as Leontief Paradox ((Jones, 2008).

Specific Factors Model

The specific model theory stated that for producing the goods and exports them to other country, the capital should be fixed for the short run and labor should be mobile. It would help to minimize the cost of production i. e. in case the price of a commodity increase then the producer an get the benefit

by using the labor which is available at low cost. This model is suitable only for some specific industries (Easterly, 2008).

Gravity Model

As per the gravity model theory, the pattern of trade between the countries is affected by the distance between the countries and these findings are also supported by the economics (Hennart, 2007).

International Equities:

International equities are the assets of the country in which the country transact with the other country. In the international equity a country has greater or lesser value transaction over the other country. There are few theories comes under international equity which provides the better idea to understand the international equity. These theories are provided in the following section (Hennart, 2007).

Balance of Trade:

Whenever, a country export to other country or import from other country, then the difference between the export and import is known as balance of trade. If the export of goods is greater than the import of goods then the different between the export and import is positive and said that the country has positive balance of trade. On the other hand if the export is less than the import then the balance of trade will be negative and this situation is called trade deficit (Casson, 2008).

Balance of Payment:

Balance of payment is the record of all the transaction which has been done by the country with rest of the world. The transaction may include the import, export, financial capital, goods of services, and the financial transfers of the funds. The balance of payment is prepared in a single currency and usually prepared for specific period as like the financial year of a company. The receipts of loan, investments receipts and export sources of funds are recorded as surplus or positive items. On the other hand the usage of funds as like the investments, import and payable are recorded as negative or deficit items (Dunning, 2006). There must be balance when all the components of balance of payment are recorded as like balance sheet of a company. Ideally balance of payment is the difference between the current account and capital account and the balance item are added or subtracted depending on the value it holds. There is a point of concern for the countries having deficit in current account since it generates the long term liability for the country (Bartlett and Ghoshal, 2007).

Advantages and Disadvantages of International Trade:

There are some advantages and disadvantages of international trade for both the export and import.

Advantages of Exporting:

One of the major advantages of export is the ownership advantage which is specific to the firms' international experience, asset and ability of the exporter to either develop the differentiated product or low cost product with in the values chain (Hertner and Jones, 2007). A combination of investment

risk and market potential is known as the location benefit of the particular market combination. In order to retain the core competencies within the organization and stitching it throughout the country without retaining the license, selling or outsourcing is the international advantage in export (Amatori and Jones, 2003).

Some of the organizations having lower level of ownership advantage may do not enter into the foreign markets. In case a company's products and company's ownership equipped with the international advantage and ownership advantage, the entry can be made through low risk model known as exporting under the eclectic paradigm. There is low investment requires in exporting of goods than the other modes of international trade and expansion such foreign direct investment. Some how it is recognized that the lower level of risk result in , lower level of rate of return than possibly the other modes of international trade (Khanna, 2007). On the other hand the usual return on international trade in export sales might not have greater potential but also there will be no risk. In export of goods the managers are allowed to exercise the various operational control however it does not have the option over the control of marketing activities of the company. The end consumer of exported goods is far away from the exporter though the various intermediaries can mange the risk (Jones, 2008).

Disadvantages of Exporting:

The exporting of goods is specifically difficult and disadvantageous for the small and medium size firms having employees less than 250. The sale of services and goods into the foreign market is difficult for them rather serving the domestic market. A lack of knowledge of different languages, difference
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in culture, exchange regulations and trade regulations having the major impact on exporting the goods for SMEs. In addition to this the staff interaction and strain of resources is a major block of exporting the goods. Despite this disadvantage, some of the SMEs are still exporting however two third of them sold out to the foreign markets (Jones, 2008).

In addition to this there are some major disadvantages highlighted in the export of goods such as financial management, communication technology improvements, and customer demand and management mistakes. In order to minimize the risk of transaction process of exporting the goods and exchange rate fluctuation, it is essential to have more capacity for managing the financials for coping up the efforts (Nelson and Winter, 2007). Customers can now interact with the suppliers due to the recent development is the communication technology has improved the way of purchasing goods, since the communication is much cheaper than what it was two decades ago. It leads more transparency in transaction and purchasing of goods and vendors are responsible for following the real time demand for submitting the transaction details (Hennart, 2007). The customers are becoming advance due to the improvement in the technology and they demand more support and services from the vendor such as startup and equipment installation and startup, delivery service and maintenance which are difficult for the exporter to provide. There might be some pitfalls in the organization occurred by some of the management mistakes such as oversea a distributor, an agent or chaos in the global organization (Johanson and Wiedersheim-Paul, 2008).

Advantages of Importing:

Importing raw materials and goods is one of the paths of increasing the profit margins. There are number of benefits in importing the goods, such as high quality, low prices, and benefits related to the international trade. An importer can have the comparative advantage which means lower prices (Jones, 2006). Also the importer can have the much cheaper products from the foreign market due to low labor cost, low taxes etc. in terms of quality, the importer can have the higher quality goods and produce the finished goods with high quality and extend the business profit margins. In some countries, government provides the support to the importer for developing the trade relations (Nelson and Winter, 2007).

Government provides the information of the manufacturers and producers in the foreign country so that the importer can purchase the high quality and low price goods. Also due to the government involvement reduces the transaction risk. An importer can access to the regionally exclusive resources and cheap labor for producing the goods. These resources are required in the manufacturing process that have specialized skills and can be sound in certain countries. For example in electronic items, Japanese people are highly efficient and manufacturer in UK use the labor from Japanese market for producing goods. The importing of resources includes everything starting from labor to technology (Fortanier, 2008).

Disadvantages of Importing:

There are many governments and economists who believe that the importing goods have numerous disadvantages. For example importing of goods could lead the erosion of the domestic markets and national economies specifically <https://assignbuster.com/advantages-and-disadvantages-of-importing-and-exporting/>

when there is trade deficit occurrence i. e. the import is higher than the export. Some of the goods like cars; appliances lead a higher level of domestic automobile and electronic markets and also loss of jobs in the respective markets (Hennart, 2007).

Some other problems can also be increased due to import of goods such as conflict in the domestic values due to the acceptance of social values. The domestic industries can also be crippled due to the import of the countries where the wages are low and the domestic industries are unable to compete since they cannot lower down their prices of goods than the cost of goods and also they have the obligation to the worker union (Hertner and Jones, 2007).

Free Trade Concept:

The concept of free trade was introduced in the system to benefit the country and improving the condition of poor by providing them high quality and cheaper products. However as an economist, in my opinion free trade is erosion the domestic players for example if UK government lower down the import duty on sugar then the demand for the imported sugar will increase and domestic player will not be able to compete with the foreign player (Johanson and Wiedersheim-Paul, 2008). On the other hand the economic category argues that free trade promote the environmental degradation, supporting the child labor, income inequality and wage labor, slavery, harming the national defense, enforcement of cultural change and accentuating the poverty in the country.

The economists also argued that the importing goods under free trade are opposed by the domestic industries due to rise in competition in terms of product quality and cheaper prices (Nelson and Winter, 2007). A maximum exploitation of workers due to the free trade is also opposed by the socialists. Free trade generally do not reduce the poverty or improve the condition of working class in the country but frequently make them more poor. It also supports the colonialism and imperialism in the country. On the other hand I believe that in free trade consumer could gain more than the industrialists and the domestic producers are more likely to mobilize their products without lifting the tariffs (Jones, 2006).

Conclusion and Suggestions:

The competitive business environment enforces the businesses in both the international and domestic markets to retain their business and remain competitive. However depending on the need and potential of the business, it is essential to understand whether the company should indulge into the export or import activity (Gupta and Govindarajan, 2008). It is recommended to the businesses specially the medium and small companies to extend their business potential at domestic market first and then extend into the international market collaboration, joint venture or business partnership. Prosperity in the country cannot be achieved through protectionism since it increases only the poverty and also do not protect the domestic industries or jobs but harm the export business and industries which has belief on imports (Hennart, 2007).