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CONTRACTING INSTITUTIONS AND DIFFERENTIATED EXPORTS

Abstract:

Institution has been shown to be important determinants for economic growth and development. Contracting institution represents a major institution governing economic transactions between private agents and thus affects economic activities most directly. This paper examines how quality of contracting institutions in source and destination countries influence exports of homogeneous and heterogeneous goods. Using a large sample of cross-country bilateral disaggregate export data, we control for endogeneity and establishing causality between contracting institutions and exports and show that competitive advantages of firms in exports of both homogeneous goods (such as agricultural and mineral commodities) and heterogeneous goods (such as manufactured goods) are eroded by weak contracting institutions in their source countries. We also find that weak contracting institutions in the destination countries exert significant negative impacts on heterogeneous but not homogeneous exports. To explain for the differential source and destination countries' contracting institutional constraints on differentiated exports, we extend the conventional institutional cost theory which implicitly posits that contract enforcement weakness in any country impedes the flows of all types of goods by taking the differences in relationship specificity of heterogeneous and homogeneous goods into account. Our analysis has policy implications for countries on institutional reform and provides practical location and production strategies for exporting firms.

Keywords:

Contracting Institutions; Differentiated Exports; Multinational firms

JEL Classification: F10, F23