

# MPRA

Munich Personal RePEc Archive

## **Innovation – source to obtain the competitive advantage in the global economy**

Sipos, Gabriela Lucia

West University from Timisoara (Romania), Faculty of  
Economics and Business Administration

April 2008

Online at <http://mpra.ub.uni-muenchen.de/13078/>  
MPRA Paper No. 13078, posted 30. January 2009 / 11:56

# INNOVATION – SOURCE TO OBTAIN THE COMPETITIVE ADVANTAGE IN THE GLOBAL ECONOMY

**Șipoș Gabriela Lucia**

*West University of Timisoara, Faculty of Economics and Business Administration*

*Pestalozzi 16, Timișoara, 300115, Romania, E-mail: [gabi.sipos@fse.uvt.ro](mailto:gabi.sipos@fse.uvt.ro) tel: 0744.284.855*

*A strong motivation to replace the comparative advantage theory with the competitive advantage theory is given by the significant change of the present economic conditions comparing with the old conditions that inspired the competitive advantage issues. The dynamic character of the market competition and the fact that, in the present, the competitiveness is located to enterprise's level and not to the level of the national economy are some important argues that sustain the necessity and the opportunity to move the economic thinking from the comparative advantage theory to the competitive advantage theory. In the past, the comparative advantage of an economy was given by the natural resources, by the geographical position or by the specific features of products or services. Nowadays the competitive advantage is created through innovation by all its forms.*

*Keywords: innovation, comparative advantage, competitive advantage*

## **Passing from the comparative advantage theory to the competitive advantage theory**

The competitiveness is a major preoccupation for all countries in the context of more free global economy. The perception on the competitiveness and on the mechanism to obtain it varies in time according with the development level of each country. The global economic situation at the first of the third millennium has a series of characteristics that must be considered in the process of making enterprise's strategy. Some of these issues are:

- The concept of the general and continue economic growth lost its viability, today every enterprise must count only on its own forces to win or even to survive on the competitive market;
- In the perspective of the unified European market will occur new business opportunities that in the conditions of stronger competition will force the managers to mobilize all the available resources. The first important resource is the technological resource that allows to enterprises to reduce the unit cost, to improve the product's performance and quality, to consolidate the position on the market and to gain new markets. In these conditions the "battlefield" will be transferred from the national to the international level and the winners will be the competitive enterprises with international vocation;
- It can be observed a strong development of the scientific research activities and, on the other hand, an accelerated process of practical implementation and application of the research results;
- The new adopted technologies spread in short time to domains that are very different by the initial domain that generated it;
- The industrial products market of more free because of gradual elimination of the all types of custom restrictions.

These economic realities are strong argues that sustain the necessity and the opportunity to pass from the comparative advantage theory to the competitive advantage theory. The comparative advantage theory gives explanations about favorable natural conditions from a national economy, given by the small cost of some production factors, comparative with other national economies based on the following elements:

- The existence of abundant and relative cheap natural resources that gives the orientation of the economy structure;
- The existence of a competitive business environment;
- The existence of neutral macroeconomic policies.

Michael E. Porter [2] supports that significant change and gives strong arguments for it. First argument aims that the majority of classic competitive theories put weight on product's cost, quality and diversification while the new theory sustains a more comprehensive competitiveness concept including the market segmentation, the technological differences and the scale economies. Innovation and the advantages generated by using the know-how and advanced technologies are superior to the advantages based on low cost of production factors.

The old theory has a static vision about the enterprise's competitiveness focused on cost – efficiency relation while the technical progress has considered an exogenous factor. The new theory includes the dynamic character of the competitiveness and the central element is the improving of the production methods and technological innovation. The static comparative advantage theory assumed that the production factors are constant and enterprises must focus on domains with superior efficiency. In the present situation, the competitiveness is facing a continue change and the essential criteria for enterprise's orientation are the innovation and changing. The enterprises are constrained to obtain profit from the new products based on new fabrication methods not only to move the resources to the most profitable domains. The new theory must have the capacity to focus the enterprises to new strategies that assures a stable position on the global competitive market.

In present days there are numerous examples about countries with low natural resources that register a strong economic and social progress or, in contrast with that, there are many undeveloped countries with very rich natural resources. This reality gives the consistence to the new theory that has microeconomic vision against the comparative theory that has macroeconomic vision. The competitive advantage theory underlines the role of the competitiveness level of the enterprises on the national market and, especially, on the international market. That competitiveness level gives the direction in the national economy's evolution and specialization. The new concept, competitive advantage, is based on active and selective policies that have the main goal to reach the targets in the global competitive market. There are four fundamental pillars: the enterprise, the competition, the favorable internal environment and the adequate economic policies applied by enterprises, ownerships, governments and international institutions.

The competitive advantage means the enterprise's capability to offer superior products and services for consumers comparing with the products and services offered by the competitors. The higher competitiveness level comparing with the competitors is given by price, product's quality, post-selling services quality, the enterprise's capability to adapt the offer to the market demand and technical progress. In Michael Porter's vision, the enterprise's competitive advantage means to assure a reduced cost or to create a distinct product or service that is clearly different through its quality by the competition's offer.

The enterprises are creating the competitive advantage in their branches and then the advantage is transferred to the national level in respect to accomplish the national economic targets. That means that it is a real necessity to elaborate and to apply a set of strategies at enterprise level and at governmental level based on the adopted theoretical premises. To be viable the competitive advantage has to be durable and sustainable on long-term. Contrary, the enterprise will benefit only by a temporary advantage based on an opportunity development.

The opportunities to create and support the competitive advantage are different according with development stage of each country. Considering these aspects, there are three different development stages [3]:

- The first development stage is the production factors based economy that assumes that the nation's competition is based on natural resources and unqualified or low qualified labor force. The enterprises assimilate the imported technology to manufacture basic products and consumer goods projected and designed in higher developed countries. The low level productivity is reflected in small amount of wages. At this development stage, the competition between enterprises is based exclusively on product's price and the direct access to foreign markets is almost inexistent;
- The second development stage is the efficiency based economy in which nation's advantages results from higher quality products manufactured in modern production processes assigned with increased efficiency. The growth of production processes efficiency is based on following factors: stimulating investment, major investment in infrastructure, increasing qualification of labor force, creating a favorable business environment, facilitating the access to investment financing capital. The increased labor

productivity is reflected in higher level of wages. The products and services are not different at global economy level and are still projected and designed in higher developed countries. The technologies are mostly assimilated from other developed countries through license agreements, joint-ventures, foreign direct investment but a part from the technologies are improved by internal effort. The enterprises extend their capabilities in the value chain and offer products addressed both to economic agents and final consumers. Although the competitiveness of efficiency based economy countries is more stable than the competitiveness of production factors based economy countries, is still sensitive to possible financial crises and brutal decreasing of foreign demand in certain domains;

- The innovation based economy is the third development stage and is superior to other previous stages. The main source of the competitiveness is the ability to manufacture innovative products based on high performance technologies and evolved production methods. Thus, to assure the success in the competitive market the enterprises have to create competitive advantage by manufacturing new products using modern production methods. These new products have to be clearly different by the competitor's products. In an innovation based economy the institutions and legal framework that stimulate the innovation are very well developed and promoted. Such type of economy is characterized by large elasticity against extern shocks and the most of producers are highly recognized at international level. Meanwhile, the services have a significant percent in the economy.
- To obtain durable economic development the enterprises from the entire world have to adapt their capabilities and competitive style to the specific development stage. Thus, enterprises have to renounce to compete based on cheap production factors and natural resources (the comparative advantage) and to create competitive advantaged induced by unique products, clearly different by the competitor's products obtained in maximum efficiency conditions.

### **The Romanian case**

A good exemplification of the comparative advantage theory application can be obtained analyzing the Romanian economy in the '90 decade. Based on action of comparative advantage theory, the most dramatic decreasing of the production and exports, while the imports was strongly increased had been registered in the computing manufacture, in the precision and medical care tools and machinery, drugs manufacture, electronic measure and control devices, fine chemistry, plains, car trucks and tractors construction, fine mechanics and so on. In the same time a rapid growth was registered by raw material exports like woods, timber, cement or basic chemistry materials [1].

It can be easy observed that the comparative advantage theory in the Romanian economy had been concretized in the developing of those domains with high consume of unqualified or low qualified labor force and, on the other hand, in restraining of the domains based on scientific research, technological development and innovation.

In these conditions, if the comparative advantage theory is let to freely act on a still not functional market characterized by large distortions, the results are stagnation, inflation and unemployment. The comparative advantage theory generated a vicious business environment, very expensive borrows, weak exchange rate of national currency, high level of taxation that affected not only the state enterprises with no chances to redress, but the viable enterprises. The specialization of the Romanian economies branches only based on the comparative advantage theory without any consideration for scientific research, inventions or innovation explain the poor situation of Romania in the last decade. It is a classic case that illustrates the comparative advantage theory limits. Nowadays it is appreciated that the Romania pass through comparative advantage stage and now is an efficiency based economy [4].

The evolution of the Romanian economy to a superior development stage had been determined by many factors like: major investment for improving infrastructure, elaboration of a legal and taxation framework that stimulates the foreign direct investment, increasing the investment credits accessibility and increasing the labor productivity by growth of qualification and competence level of the employees. The access to the efficiency based economy stage reflects a growth of national competitiveness induced by two major components: the increased national business environment quality and improved company operations and strategy. The key factors to increase the competitiveness in the present stage of Romania's economy

development are: higher education and training; goods market efficiency; labor market efficiency; financial market sophistication; technological readiness; market size.

• In a top score based on the global nation's competitiveness [4] quantified according with productive potential of 131 countries, Romania is on the 74<sup>th</sup> place with 3,97 points from a maximum possible 7 points score. The most important strong points of the Romania country identified in that survey are:

- Governmental stability;
- Low level of governmental debts;
- Low incidence of serious diseases (HIV, malaria);
- High level of primary education;
- Quality of math and science education;
- The Internet access in the schools;
- Small duration and relative simple procedures to establish a company;
- Reduced costs of dismissals;
- Flexibility of wage negotiations;
- Implying of women in work processes;
- High level of investment's protection;
- Dimension of internal market;
- Developing of business clusters;
- Availability of scientists and engineers.

• The weaknesses of the Romania country performance are: still low infrastructure, not fully restructured institutions, low level of business sophistication and innovation. In the category of business development obstacles can be enumerated: the high level of taxation, the instability of legal tax framework, the inefficient governmental offices, corruption, reduced access to financing, low infrastructure, political instability, lack of professional qualification and poor work ethic in national labor force. On the stimulating development of knowledge based domains the intensity of obstacle's manifestation will significantly decrease and Romanians enterprises will gain the competitive advantage due to innovation. In these conditions, Romania will be prepared to succeed to the superior development stage: innovation based economy.

### **Conclusion**

The changes of actual economic conditions of Romania country are strong argues to sustain the pass from the comparative advantage theory to the competitive advantage theory. It can be observed that the scale economies are extending, the consumer's needs are more complex and most of products are different one from each other. All these changes are induced by the technical progress and innovation. More than that, the present economic reality demonstrates the dynamic character of the competition and the fact that the competitiveness is not manifest at national economy level, but at the enterprise's level. The competitiveness is obtained at enterprise's level, than it is transmitted at branch level and finally at national economy level. The enterprises create and support the competitive advantage and are the tools to reach the economic targets at national level. To obtain the competitive advantage in the conditions of global economy and in permanently changing environment, there is a single chance for the enterprise: to innovate.

Innovation must be understood in the largest possible sense of the notion: the new products manufacture, the new production technologies, the new equipment acquisitions, the improved management or financing methods, the improved performance and qualification of the labor force, the improved informational system and so on. In the strategic enterprise's option must be inserted the innovation implementation methodology that is the main source and tool to gain the competitive advantage. In that context, the innovation process has to be a continuous preoccupation because the global economic environment changes bring opportunities only to enterprises prepared to face it.

## References

1. Iancu , A., Avantajul competitiv și accesul la Uniunea Europeană, Rev. "Adevărul Economic" nr. 14/2000
2. Porter, M. E., Avantajul concurențial – Manual de supraviețuire și creștere a firmelor în condițiile economiei de piață, Editura Teora, București, 2001
3. Porter, M. E., Ketels, C., Delgado, M., *The Global Competitiveness Report 2007-2008*, Part 1: The Competitiveness Indexes, 1.2 The Microeconomic Foundations of Prosperity: Findings from the Business Competitiveness Index, World Economic Forum
4. Sala-i-Martin, X., Blanke, J., Drzeniek Hanouz, M., Geiger, T., Mia, I., Paua, F., *The Global Competitiveness Report 2007-2008*, Part 1: The Competitiveness Indexes, 1.1. The Global Competitiveness Index: Measuring the Productive Potential of Nations, World Economic Forum