

markets. This may involve a range of activity, such as providing firm-specific information services, facilitating trade shows, and whatever other types of assistance that would more firms make the transition into foreign trade. This is not an argument for increasing the flow of exports or investment per se. Rather, the key is to encourage firms to try new ideas, new markets, and new strategies because the information spillovers come from learning about what works and what doesn't.

There are a couple of weaknesses in this argument which suggest caution in its implementation. The first is that the empirical evidence on the magnitude and importance of this spillover effect is limited and mixed—some studies have found evidence of spillovers; others have not. The second is that the argument that firms do not experiment enough with new strategies and new markets applies to domestic market activity as well. A policy that provides too much inducement to export and invest abroad runs the risk of drawing too many resources away from production for domestic consumers.

A third type of information spillover arises from externalities affecting the foreign demand for goods and services from a particular country. This arises when either (1) there are spillovers in reputation for product quality—that is, the quality of products from a particular country is difficult to measure and is correlated across firms so that one firm's good or bad reputation can affect the demand for products from other firms from that country; or (2) when there are linkages in demand, such as for tourism, where one firm's advertising to attract tourists will generate business for other firms in the same region. Some of these spillover effects will be internalized by intermediaries who have an incentive to seek out high quality products to sell in their local markets. However, in some sectors (such as wine, tourism and education), the market failure arising from demand externalities is likely to persist, and this can provide some justification for government support in marketing efforts. Policies such as support for trade shows and advertising and promotion efforts would address the externalities.