

specialization of production still seems appropriate in light of the GVC phenomenon, the paper will consider whether the "drivers" of GVCs and offshore outsourcing are fundamentally different from the traditional determinants of international production and trade patterns. As a related issue, the report will identify and evaluate recent policy recommendations that have been made to enhance the "home country" economic benefits of GVCs and offshore outsourcing. In particular, we will consider whether recent recommendations differ substantively from those made in the past with respect to increasing the net economic benefits of international trade and foreign direct investment (FDI).

1.2 Outline of Report

The paper proceeds as follows. Section 2 contains a relatively condensed statistical overview of recent changes in international trade involving intermediate inputs, including service inputs, as well as offshore outsourcing. The focus of this section is both on the absolute growth of these activities, as well as growth relative to global international trade flows. Among other things, attention will be paid to whether and to what extent activities traditionally carried out at corporate headquarters, particularly research and development, are being partly or wholly relocated geographically, as well as the extent to which the international relocation is accompanied by outsourcing.⁴ Section 2 will also address whether and how recent Canadian experience with trade in intermediate inputs and offshore outsourcing differs from that of other OECD countries.

Section 3 presents an overview of conventional theories of international production, particularly the determinants of the international specialization of production encompassing the allocation of value chain activities across firms, i.e. make-or-buy decisions. Section 4 provides an evaluation of whether and how conventional theories of international production need to be modified or extended in order to explain in a satisfactory manner the phenomena of increased trade in intermediate inputs (including services) and offshore outsourcing. This evaluation includes a consideration of whether new drivers of international trade and outsourcing have emerged in recent years. Relevant theoretical contributions to the literature on international production will be reviewed, as well as empirical studies identifying the main determinants of international production specialization and trade. Recent theoretical and empirical studies of offshore outsourcing will also be reviewed and assessed.

Section 5 will identify and assess policy recommendations that have been made to enhance the home country economic benefits derived from the GVC and offshore outsourcing phenomena. Section 6 provides a brief summary and conclusions.

2. The Growth of GVCs and Offshore Outsourcing

There is no consistent time series evidence on the extent to which trade in intermediate inputs has changed over time. Nor is there consistent evidence on the magnitude of offshore outsourcing activities over time. Furthermore, the evidence that is available is largely based on surveys that are specific to particular time periods and/or locations.

⁴ As Markusen (2005) notes, the loss of domestic service jobs associated with corporate head offices are among the biggest concerns in the trade policy area, so a particular focus on vertical specialization and offshore outsourcing of traditional headquarters' services seems appropriate.