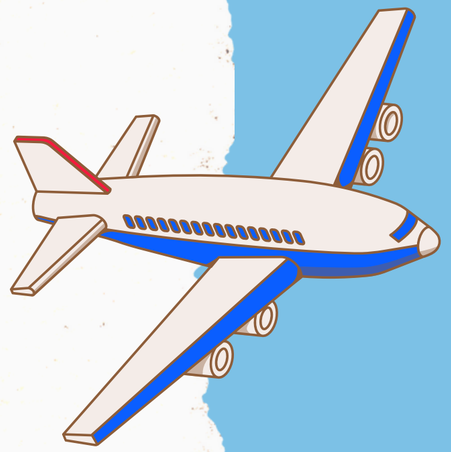
Chinese Firms in Global Markets

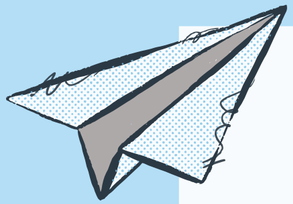


Round 5

Transaction Cost Theory
Chinese Firms in Global Aviation

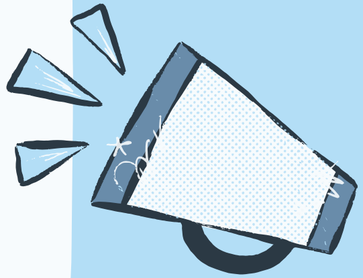
Benedikt Lasar

23.05.2025



Presentation Schedule

Any team, topic, or date preferences?



Transaction Cost Theory

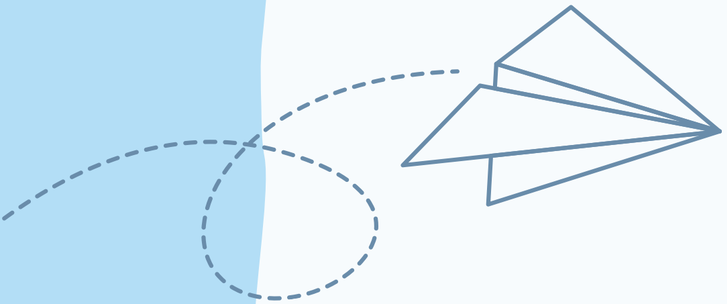
1. Coase
2. North
3. Williamson

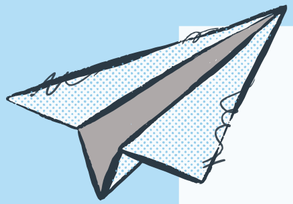
Aviation Industry

4. Global Industry
5. COMAC

TCT: Coase

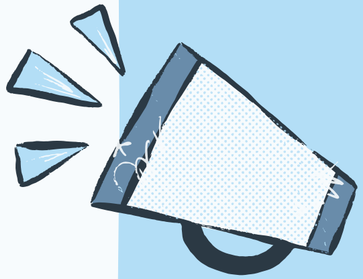
- Ronald Coase, father of TCT
- Nobel price in economics
- Why do firms exist?





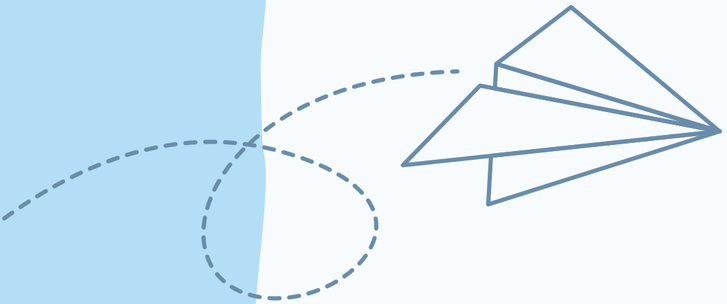
Question

Why do firms exist?



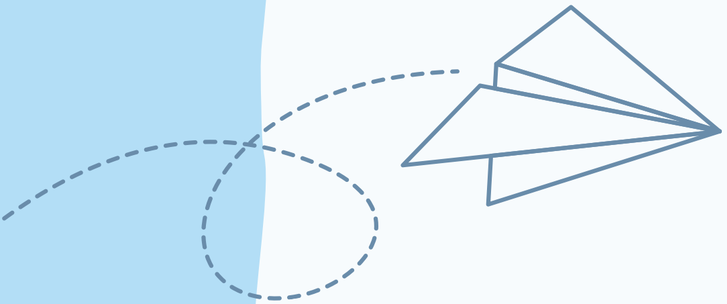
TCT: Coase

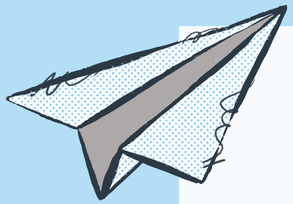
- There are more costs to market transactions than the price of goods and services
- Firms can avoid market costs by producing in-house
- There's a limit to economically rational in-house production



TCT: Coase

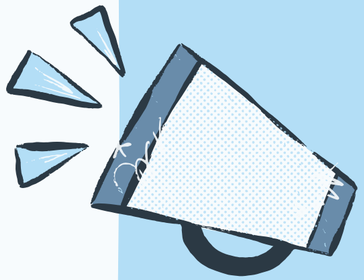
- Coase develops Adam Smith's idea of the division of labor: what tasks should be performed by firms, what tasks by the market?
- Firms need to consider both production and transaction costs





Question

What costs arise when a company engages in market transactions apart from production costs?



TCT: Coase

Search and information costs

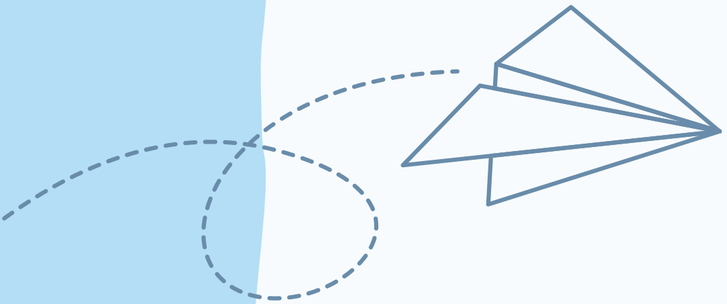
Who offers what at which price?

Bargaining and decision costs

Negotiation costs

Policing and enforcement costs

compliance and dispute resolution



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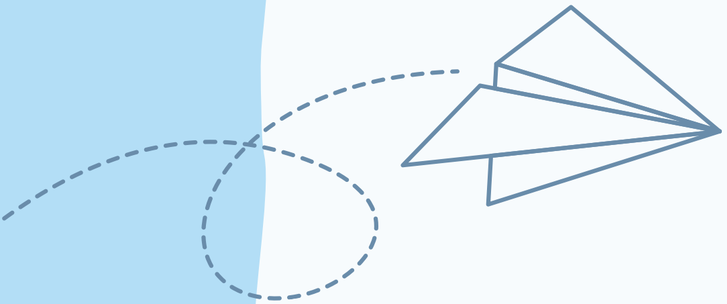
TCT: North

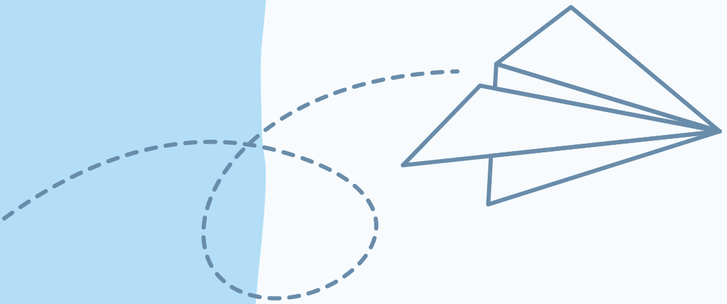
- TCT assumes humans are opportunistic but constrained by bounded rationality

- This is contrary to hyperrationality in classical economics (homo oeconomicus)



TCT: North

- Douglas North argues that we are bound by institutions
- Institutions govern society, they are the rules of the game
- Transaction costs are influenced by institutions



TCT: North

- Institutions that facilitate transaction costs boost economic growth

"The more complex an economy the more individuals will be engaged in coordinating and operating that system."

North, D.C. (1992): *Transaction costs, institutions, and economic performance*. p.6

Four Factors

of transaction costs

Measurement

It is necessary to consider all aspects of the good or service that is being transactioned

Enforcement

A third party is needed to ensure that neither party violates the terms of the transaction

Four Factors

of transaction costs

Market Size

Impersonal exchanges bring forth the need of a third party arbitrator

Ideology and perception

The individual perception of the economic and political system affect performance

Transaction Cost Theory

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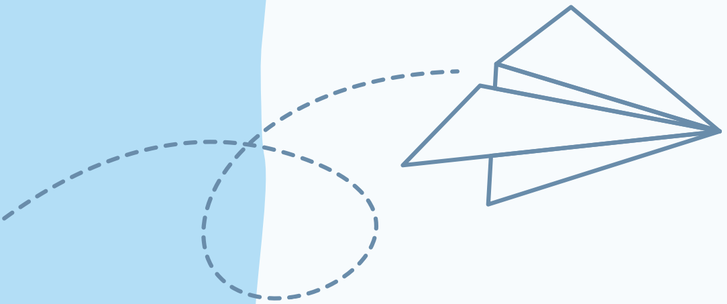
TCT: Williamson

- Oliver Williamson regards transactions as an exchange of tangible or intangible resources between two or more parties

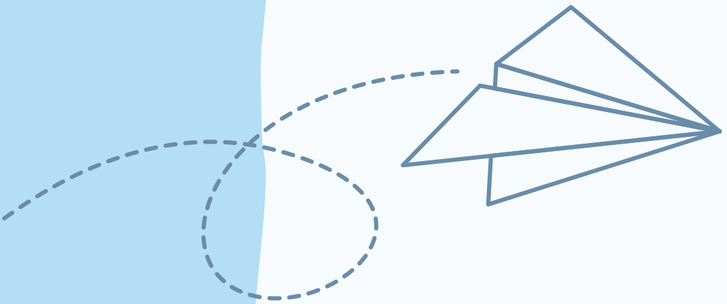
- Four categories of transaction costs: origination, agreement, control, and adjustment costs

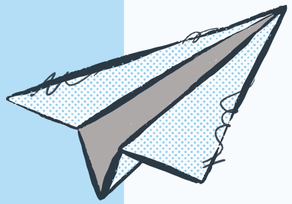


TCT: Williamson

Williamson's three indicators for transaction cost decisions:

- Specificity
- Uncertainty
- Frequency

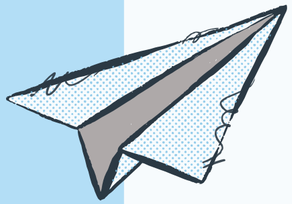




Specificity

- When a resource is specific (hard to substitute), then the company should produce the resource itself

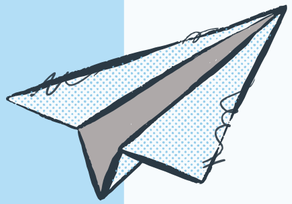
- Outsourcing could cause problems in bragaining in the future



Uncertainty

- Unpredictability before and during the transaction process

- Caused by externalities interfering in the negotiation and fulfillment of transactions or in-house production



Frequency

- Frequent transactions can establish trust between the parties involved

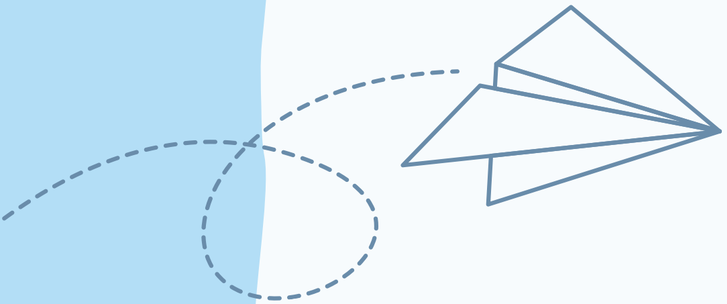
- In-house production can build expertise and avoids the costs of frequently occurring transactions

TCT: Williamson

Williamson concludes:

The higher the factors are, the more likely in-house production becomes

A company should outsource if the factors are low



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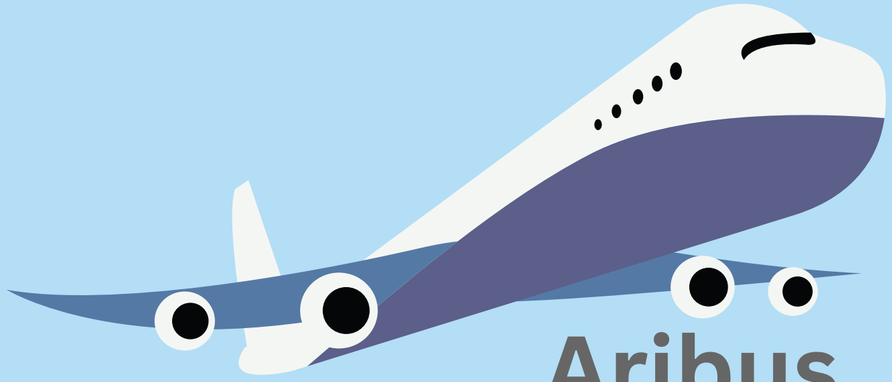
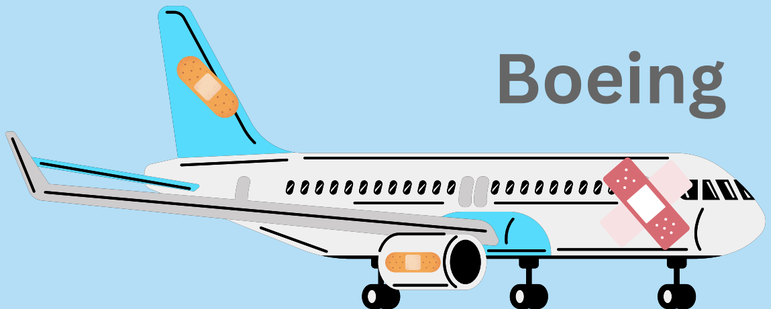


Aribus

Global Aviation Industry

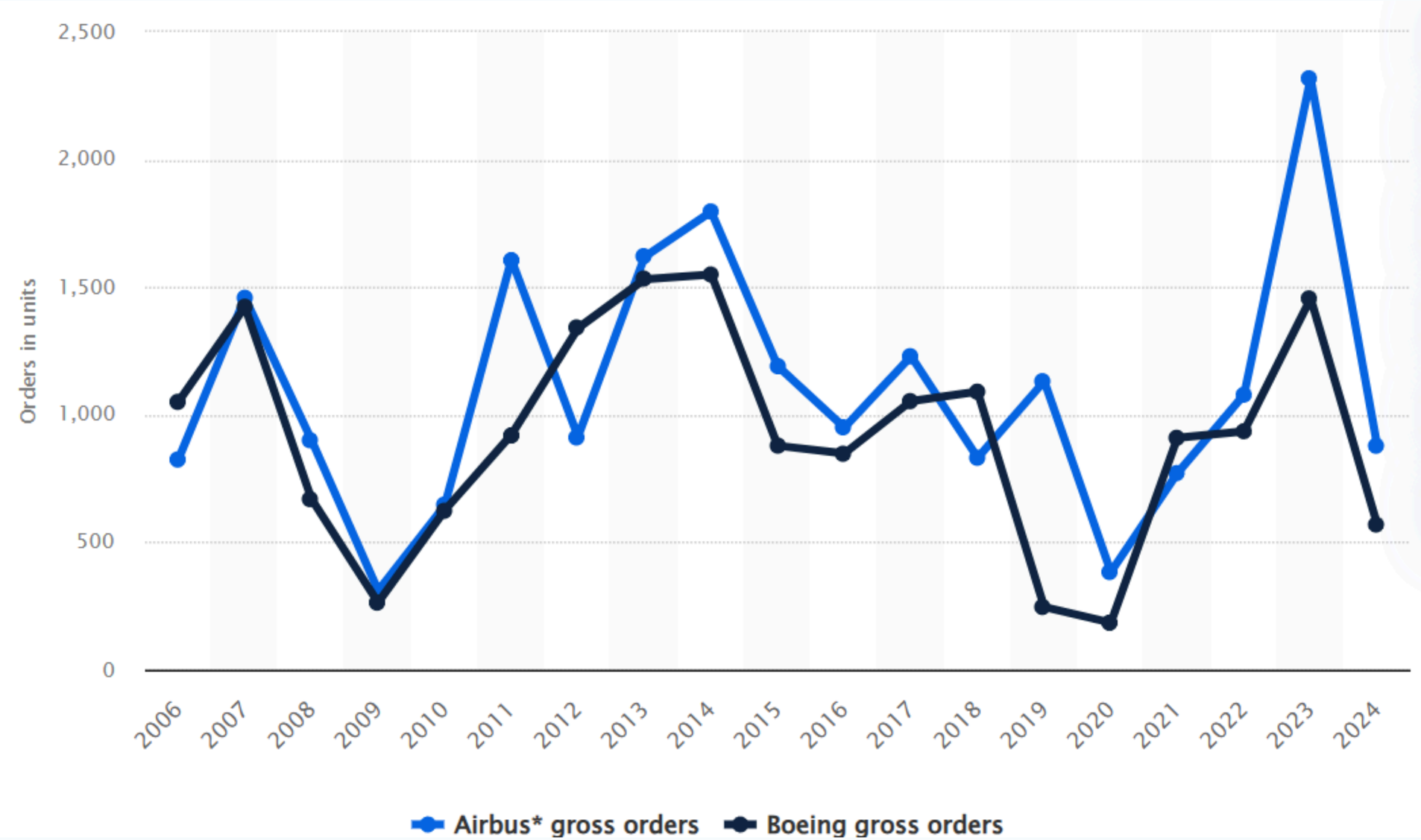
COMAC



Boeing

Global Aviation Industry

- Dominated by Airbus and Boeing
  → Duopoly (A-B-C oligopoly soon?)
- Aircraft orders dropped drastically during the pandemic
- Boeing has been in crisis for several years



Source: statista.com/statistics/264492/aircraft-orders-from-airbus-and-boeing/

- Possibility for new competitors to enter the market
- But: barriers to market entry are high
- Barely any company even tries to enter

Barriers to Entry

- Technological advantages
- Economics of scales
- Product differentiation
- Sunk costs
- Returns on investment take time
- Transaction costs

- Component manufacturers compete for contracts with Airbus and Boeing

- The Boeing 787 relies on 50 suppliers from ten countries (70 percent)

- Trend towards in-house production in response to delays and failures to fulfill contracts

Market Segments

- Helicopters
- Business jets
- Regional jets
- Small and large commercial aircraft

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- Established in Shanghai in 2007
- No prior Chinese aviation industry
- Zhongyun No.1, the first fully Chinese made airplain built in 1944
- Strong reliance on the USSR

COMAC

Picture: en.wikipedia.org/wiki/Comac

- Specializes in large passenger aircraft (150+ passengers)
- Airbus and Boeing make up 99 percent of all orders in the segment
- China sees building an aircraft industry as an ideological necessity

COMAC

Picture: en.wikipedia.org/wiki/Comac

- ARJ21: noise problems and delays in construction

- C919: first test flights in 2020

- The C919 is remarebly similar to the Airbus A320 in both looks and functions

COMAC

Picture: en.wikipedia.org/wiki/Comac

- Orders mostly from Chinese state-owned carriers (Air China, China Southern, China Eastern)

- Advanced talks mostly happen with countries in Southeast Asia (Vietnam, Indonesia, Brunei)

COMAC

Picture: en.wikipedia.org/wiki/Comac

- International expansion hampered by legal barriers

- COMAC plains only allowed to fly in China and some other countries

- Still waiting for green light from the EU and US (political decision)

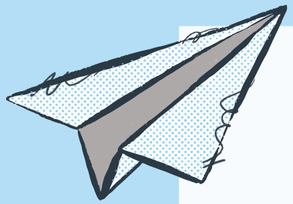
COMAC

Picture: en.wikipedia.org/wiki/Comac

- Cost advantages (C919 approximately half of the Airbus A320 neo)
- Price could convince poorer nations despite security concerns
- BRI includes an aviation strategy

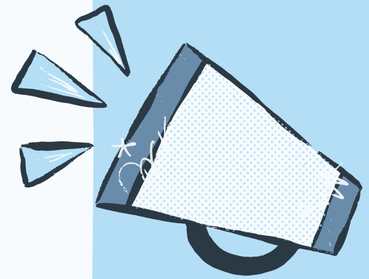
COMAC

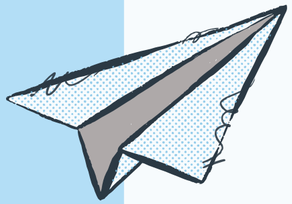
Picture: en.wikipedia.org/wiki/Comac



Question

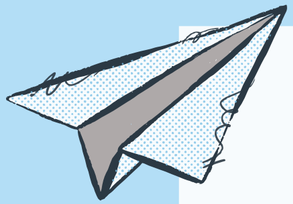
What advantages and disadvantages does COMAC have in terms of transaction costs? What challenges connected to specificity, uncertainty, and frequency do you see?



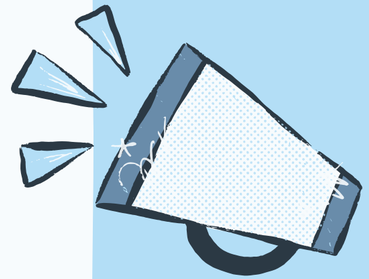


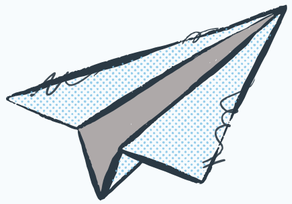
S-U-F

- How specific is a resource?
- Are there uncertainties connected to the transactions?
- How frequently do transactions happen?



Questions





Homework

Not text to read for week!

Instead, please write a one to two-page analysis of Bytedance's globalization using one of the internationalization theories you have learned about so far. Deadline is the **28th of May**. Please use **proper citation and referencing** as you would expect to do in your term papers.

Theory References

Coase, R.H. (1937): *The Nature of the Firm*. Economica (4), pp. 386-405.

North, D. C. (1990): *A Transaction Cost Theory of Politics*. In Journal of Theoretical Politics 2 (4), pp. 355–367.

North, D. C. (1992): *Transaction Costs, Institutions, and Economic Performance - An Economic Appraisal*. San Francisco, CA.: ICS Press.

Williamson, O. E. (1998): *Transaction Cost Economics: How It Works; Where It is Headed*. In De Economist 146 (1), pp. 23–58.