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# Total factor productivity gap between internationalized and domestic firms: net premium or heterogeneity effect?

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**Key words:** TFP distribution, quantile treatment effect, gap decomposition.

## 1. Introduction and positioning within the literature

A number of studies in the last decade focused on the relationship between the internationalization of firms and total or partial productivity, prompted by the seminal empirical work of Bernard and Jensen (1995). The main results of these works is that productivity is positively related to firms' international involvement (for a complete and up-to-date review see Greenaway and Kneller, 2007, and Wagner, 2007).

From an applied perspective a number of different statistical and econometric tools have been adopted to evaluate the direction and extent of this relationship in the literature on the internationalization of firms. To briefly illustrate the main features of the different approaches, the international status of firms will be defined by considering two groups of firms: those operating in the international market (INT group), and those operating only in the domestic market (DOM group).

The analysis of the differences in productivity between INT and DOM groups was first carried out by comparing differences in average productivity (or average productivity growth). This approach, adopted in the pioneering study of Bernard and Jensen (1995), involves just the comparison of the first moment of productivity distributions, in this way neglecting the heterogeneity of productivity represented by the productivity distribution. Furthermore, the productivity differential evaluated in this way is "unconditional" as the DOM and INT groups may be different for a number of other characteristics linked to productivity. As a general consequence, differences in productivity may be due to differences in those firms' characteristics.

The first weakness outlined, i.e. the focus on the average, can be overcome by comparing the whole productivity distributions of groups of firms. To this purpose the concept of first order stochastic dominance has been used. Let  $F_{INT}(y)$  and  $F_{DOM}(y)$  denote the cumulative distribution function of the random variable  $y$  representing productivity, respectively for the INT and DOM groups. First order stochastic dominance of  $F_{INT}(y)$  with respect to  $F_{DOM}(y)$  is defined as  $F_{INT}(y) - F_{DOM}(y) \leq 0$ , uniformly in  $y$ , with strict inequality for some  $y$ . The hypothesis of first order stochastic dominance can be tested non-parametrically by using the one-sided and two-sided Kolmogorov-Smirnov test. The acceptance of the hypothesis means that INT productivity distribution stochastically dominates the DOM productivity distribution. Graphically, the empirical cumulative distribution function referring to INT firms lies entirely on the right of that referring to the DOM group. This testing approach was first used by Delgado et al. (2002) where productivity

distributions of exporters and domestic firms were compared. Girma et al. (2004), Arnold and Hussinger (2006) and Wagner (2006) extended the approach to a third group of multinational firms engaged in FDI. Note that this approach, as it accounts for the whole distribution, represents a more informative test of productivity difference with respect to the test which compares the averages. Obviously, if the hypothesis is accepted, the averages also significantly differ. Unfortunately this approach also focuses on unconditional productivity differences. Note that the unconditional comparison overlooks the most important finding of the recent micro econometric studies in this field: the representative firm does not exist in any industry and internationalized firms are heterogeneous.

As regard as the second weakness outlined, that is, the neglected role of covariates, a way to control for a number of firm characteristics, as summarized in Wagner (2007), is to estimate a regression model which expresses the expected value of the dependent variable (in general the log of the productivity) as a function of the variable defining the internationalization status (i.e. a dummy variable that distinguishes the groups of INT and DOM) and of a number of other so called “control variables” that we suspect could also predict the dependent variable (usually industry, region, firm size, capital intensity and so on). In this way, the internationalization “premium” could be estimated after controlling for the characteristics summarized by covariates. This approach has been adopted by Castellani and Zanfei (2007), Kimura and Kiyota (2006), Castellani et al. (2009). Note that this strategy offers a solution to the problem of conditioning the comparison to a vector of control variables but, given these controls, the comparison again only involves the (conditional) averages. In other words, if firms are largely (conditionally) heterogeneous in productivity, the relationship between international status and productivity is only roughly described by the effect on the (conditional) productivity average. This is mainly true if extreme observations of productivity are present in the dataset. To the best of our knowledge, in the stream of literature on the relationship between productivity and internationalization, only Yasar et al. (2006) refers the regression analysis to the whole conditional productivity distribution .

This paper contributes to the understanding of the relationship between firm productivity and internationalization from more perspectives. In fact it unifies the two main streams of the literature on the relationship between productivity and international status: the one based on (conditional) linear models and the one based on comparing distribution functions using the concept of the first order stochastic dominance.

First, we single out a “conditional” comparison between groups, that is we compare the “net” Total Factor Productivity (TFP) premium. In fact, the comparison of the TFP between groups can lead to biased conclusions if it is singled out without taking into account that compared groups can differ with respect to many characteristics defining heterogeneity of firms, including, for example, size, location and type of industry. Since each of these characteristics could have some association with the level of firm productivity, the evaluation of the productivity gap between groups (the so called “unadjusted” or “raw” comparison) would consist of a comparison neglecting the *ceteris paribus* condition. Then, we refer the comparison to the whole productivity distribution, that is, along its different quantiles, in order to not limiting the comparison to synthetic indicators (i.e. to the average).

The strategy above outlined allows answering to the following research questions:

- a) Is the TFP gap significantly different from zero? And if yes, does the gap amount depend on the TFP level? For example, is it lower or higher for firms with a lower or higher TFP?
- b) Is the relationship between TFP and variables describing firms’ heterogeneity different (in sign and amount) at different TFP distribution quantiles?
- c) Does the TFP gap “survive” conditionally for a number of characteristics of firms and, if the answer is affirmative, does the extent of this “surviving” gap depend on the TFP level?
- d) How much of the TFP gap is explained by characteristics of firms (self-selection hypothesis, as in Wagner (2007)) and how much by the net (so-called “adjusted”) productivity premium?

The statistical approach we adopt to deal with this multi-object task was proposed by Author et al. (2005), Machado and Mata (2005) and Melly (2005) in the framework of the comparison of wage

distributions in reference to different racial groups or genders. Based on the idea that a full understanding of the raw productivity premium requires a disentangling of the effects of differences in the structural characteristics of firms from the effects of differences in returns to the characteristics, this decomposition approach permits to evaluate what proportion of the productivity gap between INT and DOM is due to different characteristics of the firms and what proportion is due to their internationalization status.

The paper is organized as follows. In Section 2 we illustrate the methodology and show how differences in productivity distribution can be decomposed into three factors: coefficients, covariates and residuals. In Sections 3 and 4 we respectively describe the data and analyze the results obtained. In Section 5 some conclusions are drawn.

## 2. Methodology

The quantile regression approach (Koenker and Basset, 1978) is a methodology to estimate the regression coefficients at different quantiles of the distribution of the response variable. The coefficients of a specific covariate refer to different quantiles of the dependent variable allowing the evaluation of if and how the covariate impacts on the response variable at different quantiles. Then the regions of the support of the dependent variable where these effects are especially weak or strong or not present at all can be identified.

The quantile decomposition technique (here considered in the version proposed by Melly (2005)) uses the quantile regression model to provide an estimator of distribution function of the dependent variable in presence of covariates, which enables a calculation of counterfactual density. By comparing actual and counterfactual densities, it partitions the observed distribution of an outcome (usually wages, here TFP) into return components (coefficients), quantity components (group composition) and residuals and computes their impact on the overall outcome distribution. In other words, this technique provides information on differences between distributions evaluated moving from the lower to the upper tail of the conditional productivity distribution.

The rationale of the quantile decomposition technique develops as follows. Let  $\{y_i, \mathbf{x}_i\}_{i=1}^N$  be an independent sample from a population with  $y_i$  the outcome variable and  $\mathbf{x}_i = (x_{i1}, x_{i2}, \dots, x_{iK})$  a vector of  $K \times 1$  covariates, then the quantile regression model is defined as:

$$y_i = Q_\tau(y_i | \mathbf{x}_i) + u_i = \mathbf{x}_i' \boldsymbol{\beta}(\tau) + u_i \quad \forall \tau \in (0,1) \quad (1)$$

where  $Q_\tau(y_i | \mathbf{x}_i)$  is the  $\tau$ -th quantile of the distribution of  $y_i$  conditionally on the vector of covariates. Quantile regression enables the estimation of the relationship between a dependent variable and regressors along the whole distribution, imposing a minimal number of assumptions concerning the shape of the distribution function. For logged dependent variables the quantile regression coefficients may be interpreted as rates of returns to different characteristics at the specified quantile of the conditional distribution. If equation (1) is correctly specified,  $Q_\tau(y_i | \mathbf{x}_i)$ , as a function of  $\tau \in (0,1)$ , provides a full characterization of the conditional distribution of  $y$  given  $\mathbf{x}$ . On the other hand, by exploiting the knowledge of the dependence on the covariates, it is possible to construct counterfactual conditional distributions corresponding to different scenarios for covariates and coefficients. Since the conditional distribution does not reflect the variability of covariates in the population, the following step is required to marginalize the conditional distribution using alternative scenarios for the distribution of firm attributes, by integrating the estimated conditional quantile function over the distribution of  $\mathbf{x}$  and  $\tau$  in order to obtain an estimate of the counterfactual density, as follows:

$$\hat{f}(y) = \hat{f}(g(\mathbf{x}), y) = \iint_{\mathbf{x}, \tau} \hat{Q}_\tau(y_i | \mathbf{x}_i) g(\mathbf{x}) \partial \mathbf{x} \partial \tau$$

So far, by applying the covariates composition at state 0,  $g_0(\mathbf{x})$ , to the coefficients at state 1,  $\hat{\beta}_1(\tau)$ , it is possible to estimate the outcome counterfactual density  $\hat{f}(g_0(\mathbf{x}), y)$  which would happen if covariate composition were as at state  $s=0$  and returned as at state  $s=1$ . In other words, the density of output may be adjusted by group composition.

After adjusting for compositional effects, the residual difference is partly due to the difference in returns between groups and partly to the within group inequality due to residuals. Since the  $\tau$ -th quantile of the residual distribution of  $u$  given  $\mathbf{x}$  is consistently estimated by  $\mathbf{x}'[\beta(\tau) - \beta(0.5)]$ , according to Melly (2005), the within inequality component may be obtained by computing the distribution that would prevail if the median return to characteristics are as at state 1 but the residuals are at state 0, by using the return  $\beta^{1,r0}(\tau) = \beta^1(0.5) + \beta^0(\tau) - \beta^0(0.5)$ .

To estimate the unconditional quantile at operational level, the problem of lack of monotonicity, that is  $\tau_j \leq \tau_k \Rightarrow \mathbf{x}'\beta(\tau_j) \leq \mathbf{x}'\beta(\tau_k)$  may emerge. Here, the consistent and asymptotically normally distributed estimator of the population  $\theta$ -th quantile is used to this purpose:

$$\hat{Q}_\theta[f(g(\mathbf{x}), \beta)] = \inf \left\{ q : \sum_{i=1}^N \sum_{j=1}^J (\tau_j - \tau_{j-1}) I(\mathbf{x}_i' \hat{\beta}(\tau_j) \leq q) \geq \theta \right\} \quad (2)$$

This method allows for the simulation of counterfactual distributions that can be used to decompose differences in distribution. By using the equation (2), posing a regular grid of sufficiently small quantiles, for example  $(\tau_j - \tau_{j-1}) = 0.01$ , conditional distribution may be integrated to obtain marginal distribution.

Summing up, the observed difference between unconditional  $\theta$ -th quantiles of the outcome densities over two groups are decomposed as

$$\begin{aligned} & \hat{Q}_\theta[f(g_1(\mathbf{x}), \beta_1)] - \hat{Q}_\theta[f(g_0(\mathbf{x}), \beta_0)] = \\ & = \left[ \hat{Q}_\theta[f(g_1(\mathbf{x}), \beta_0)] - \hat{Q}_\theta[f(g_0(\mathbf{x}), \beta_0)] \right] + \\ & + \left[ \hat{Q}_\theta[f(g_1(\mathbf{x}), \beta_{1,r0})] - \hat{Q}_\theta[f(g_1(\mathbf{x}), \beta_0)] \right] + \\ & + \left[ \hat{Q}_\theta[f(g_1(\mathbf{x}), \beta_1)] - \hat{Q}_\theta[f(g_1(\mathbf{x}), \beta_{1,r0})] \right] \end{aligned}$$

where the first component is explained by changes in the composition of characteristics, the second difference measures the between-group inequality and it is explained by the difference in median coefficients, while the last difference measures the within-group inequality and is explained by residuals as covariates and coefficients are kept fixed.

For the purposes of this paper, the component due to characteristics may be interpreted as the observable effect of self-selection factors on the choice of openness to international markets, that due to coefficients, measuring the between-group difference may be interpreted as the net internationalization productivity premium, and the last component measures the residual within-group difference. As a further interpretation, if the total differences are considered as Quantile Treatment Effect of the openness to international market on productivity, the coefficient component is the Quantile Treatment on Treated effect.

### 3. The TFPs heterogeneity

The analysis is conducted on firm level data from the ninth Capitalia survey (covering the years 2001-2003), which contains accounting information from balance-sheets as well as information on geographical location, internationalization, sub-contracting, and innovation. The target population consists of Italian manufacturing firms with more than ten employees. It includes all Italian firms with more than 500 employees and a stratified sample of those with less than 500 employees. In this analysis, after a cleaning

procedure aiming at the exclusion of observations with missing data on outcome variable or on covariates, 3,431 manufacturing firms were selected.

Manufacturers involved in export during the three year period were about 75.3% of the whole, 20% of firms are involved in commercial penetration, 30.3% in agreements while other internationalization forms are less frequent. As a whole 76.7% of the firms are involved in at least one internationalization choice while the other 23.3% are purely domestic firms not involved in any form of internationalization. We consider firms as internationalized (INT) if they utilize at least one of the modes mentioned, whereas the remaining firms are domestic (DOM).

Firm heterogeneity may be found in compositional characteristics of INT versus DOM groups. Within the DOM group more than one third of firms (34%) operate within Mineral and Metal products industries, while only 19% in the INT group. Firms open to international markets more frequently operate in Textiles and Clothing, Non-electric Machinery, and Furniture industries. With respect to regional aspects, INT are more often found in district areas and in Northern or Central Italy. Other features associated with international openness are the skill intensity of employees, the presence of innovation or investments and group membership. Finally, international firms tend to be larger than domestic firms.

The TFP is measured at firm level by estimating nine Cobb-Douglas production functions by industry, with value added as output, total costs of labor as labor input and the book value of fixed and intangible assets as capital input by aggregation of industry. All nominal variables are deflated by proper index numbers. To take into account the simultaneity problem between input decisions and productivity shock, it is adopted the semi-parametric Levinson and Petrin (2003) estimator, in which deflated intermediate costs are assumed as proxy of capital. Since the level of TFPs cannot be measured in any meaningful units, movements relative to other firms or to a representative firm need to be computed. At the end firm-year specific TFPs, scaled respect industry means and log transformed, provide relative measures of how firm specific TFP diverges from the average during the three year period. The results on the estimated production function are available upon request<sup>1</sup>.

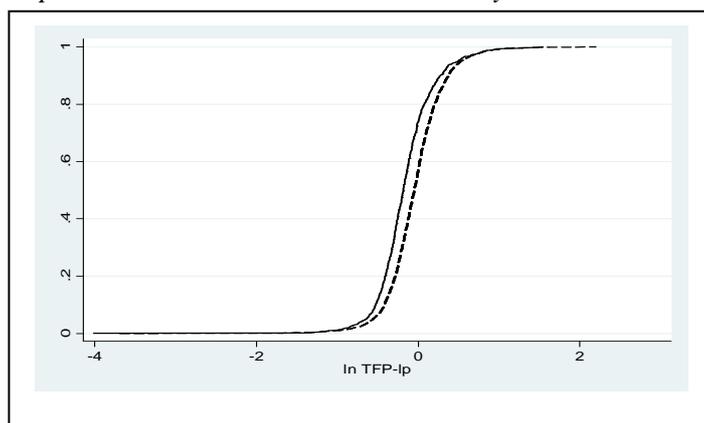
The main evidence emerging from the unconditional comparison (Tab. 1) is that a relevant productivity premium exists for INT firms with respect to DOM firms. The premium is quite uniform along the distribution, that is, of the same entity for more productive and less productive units in each group. DOM firms are found to be less productive than INT firms of 11.2% in mean. Stochastic dominance of TFP distribution for international firms is found as well (Fig. 1). The TFP gap between INT and DOM groups is quite stable along the distributions, from 12.1% at the first quartile to 13.1% at the third quartile.

Table 1. *Summary statistics of TFP distribution by international status*

$\ln(TFP)$	mean	1 <sup>st</sup> quartile	median	3 <sup>rd</sup> quartile
All firms	-0.070	-0.274	-0.086	0.122
Domestic	-0.156	-0.367	-0.183	0.015
International	-0.044	-0.245	-0.053	0.146
Export	-0.041	-0.242	-0.051	0.149
Commercial penetration	-0.024	-0.217	-0.020	0.151
Agreements	-0.042	-0.256	-0.047	0.142
FDI or Offshoring	0.040	-0.170	0.023	0.206
$\ln(TFP)$ : gap versus domestic	mean	1 <sup>st</sup> quartile	median	3 <sup>rd</sup> quartile
International	0.112	0.121	0.130	0.131
Export	0.115	0.125	0.132	0.134
Commercial penetration	0.132	0.149	0.163	0.136
Agreements	0.114	0.110	0.136	0.127
FDI or Offshoring	0.196	0.196	0.206	0.192

<sup>1</sup> To evaluate the sensitivity of results to the estimation approach, we also adopt the fixed effect panel estimator. Results are coherent with those presented here and available upon request.

Figure 1. Empirical cumulative TFP distributions by international status (DOM in solid line).



Looking at different internationalization modes (Tab. 1), the TFP premium is in mean 11% for firms which export or have commercial agreements, 13% for firms with commercial penetration and more than 19% for those with FDI or off-shoring. The ranking of firm productivity premium by internationalization mode presented in previous empirical works is then supported by this evidence. Moreover the TFP premia associated with each mode are quite stable along the distribution with absolute inter-quartile ranging always under 2%.

In order to adjust for the compositional effects observed for INT and DOM groups and to identify how much of the TFP gap is explained by characteristics of firms we run quantile regressions. For each international status, the log of the TFP is regressed on a set of influent attributes. To the aim of singling out the role of the different covariates, we run different model specifications in terms of regressors. Here the results of the specification with the covariates most used in the empirical literature on firm heterogeneity are presented (geographical, manufacturing district and sectoral dummies, features describing firm behavior such as labor skill intensity, innovations or realized investments and membership to groups and firm size).

In Table 2 the estimates of median and inter-decile regressions of the ln(TFP) are reported.

Table 2. Median regression and interdecile ranges coefficients by international status.

	$\beta(0.5)$		$\beta(0.9) - \beta(0.1)$	
	DOM	INT	DOM	INT
Constant	<b>-0.691</b>	<b>-0.652</b>	<b>0.871</b>	<b>0.691</b>
Food and beverages	<b>0.144</b>	0.041	-0.052	0.135
Textile, clothing and leather	-0.009	0.025	<b>-0.265</b>	0.031
Wood, paper, printer and publishing	0.032	<b>0.069</b>	<b>-0.274</b>	-0.101
Chemicals, rubber and plastic	-0.016	-0.035	0.074	-0.008
Non-electric machinery	0.001	-0.020	-0.191	-0.097
Electric electronic medical instruments	-0.060	-0.042	<b>-0.153</b>	0.013
Vehicles and transportation	<b>-0.141</b>	<b>-0.166</b>	0.030	<b>0.404</b>
Furniture	0.023	0.024	-0.236	-0.062
South	-0.031	-0.028	0.159	0.045
District	0.010	0.021	-0.050	-0.018
Skill intensity	<b>0.147</b>	<b>0.216</b>	0.211	<b>0.367</b>
Innovation	<b>-0.035</b>	0.019	-0.025	-0.042
Investment	0.011	0.016	-0.069	0.071
Group	<b>0.123</b>	0.008	<b>0.307</b>	<b>0.107</b>
Ln employment	<b>0.121</b>	<b>0.114</b>	-0.031	-0.042

In bold significant coefficients.

A significant coefficient in the median regression means that a significant effect of the specific variable on the median level of response is detected for that group. Significant coefficients are also observed in the inter-decile regression (denoted in bold). This means that a significant different impact between the ninth and first decile, that is between high and low values of response variable for the specific covariate, is detected in that group. The last outlined result confirms that the quantile regression approach is more suitable than the linear regression in order to explain heterogeneity.

All variables have expected signs. Location in the south of Italy has a negative association with productivity, while in manufacturing district area the impact is positive. Internationalized TFP increases in the presence of investment spending or innovations. As the skill intensity of labour increases, both median level of total productivity and heterogeneity in productivity distribution within the groups significantly increase. The same happens for membership to a company group.

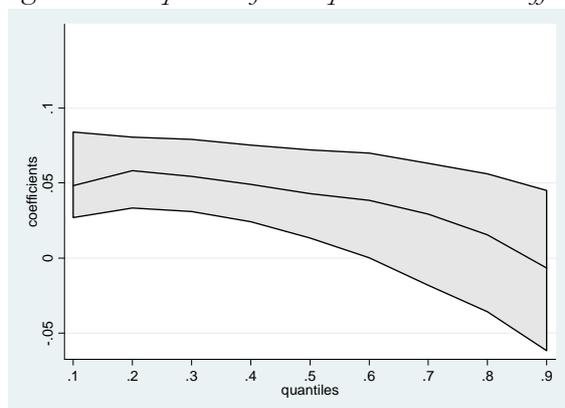
#### 4. Decomposition results

Basing on the results of previous quantile regressions, differences in TFP distributions are decomposed following the quantile decomposition methodology. Results are presented in Table 3. Raw productivity premium for internationalized firms ranges from 11.2% at the second decile in the bottom of distribution to 12.1% at the eighth decile in the higher part of distribution. When the covariates are considered, the firms' attributes explain an amount of gap of 7.1% at the second decile of the distribution, of 9.1% at the eighth decile of productivity distribution. The composition effect is then relevant along the whole TFP distribution. The component explained by the coefficient, which may be considered the adjusted internationalization productivity premium is around 5% for firms which belong to the less productive part of populations and is not significant from the bottom half of distribution (Fig. 2). The component explained by residuals is quite uniformly below 2% along the distribution.

Table 3. Components of total productivity premium due to residual, covariates and coefficients (net premium) at different quantiles.

Quantile	0.10	0.20	0.30	0.40	0.50	0.60	0.70	0.80	0.90
Total premium	.099	.112	.123	.135	.137	.137	.131	.121	.072
Premium due to:									
Residuals	-.018	-.017	-.006	.002	.008	.012	.016	.016	-.018
Covariates	.070	.071	.076	.084	.086	.086	.086	.091	.093
Coefficients	.047	.057	.054	.049	.043	.038	.029	.015	-.003

Figure 2. Component of TFP premium due to coefficients of the TFP gap with confidence bounds



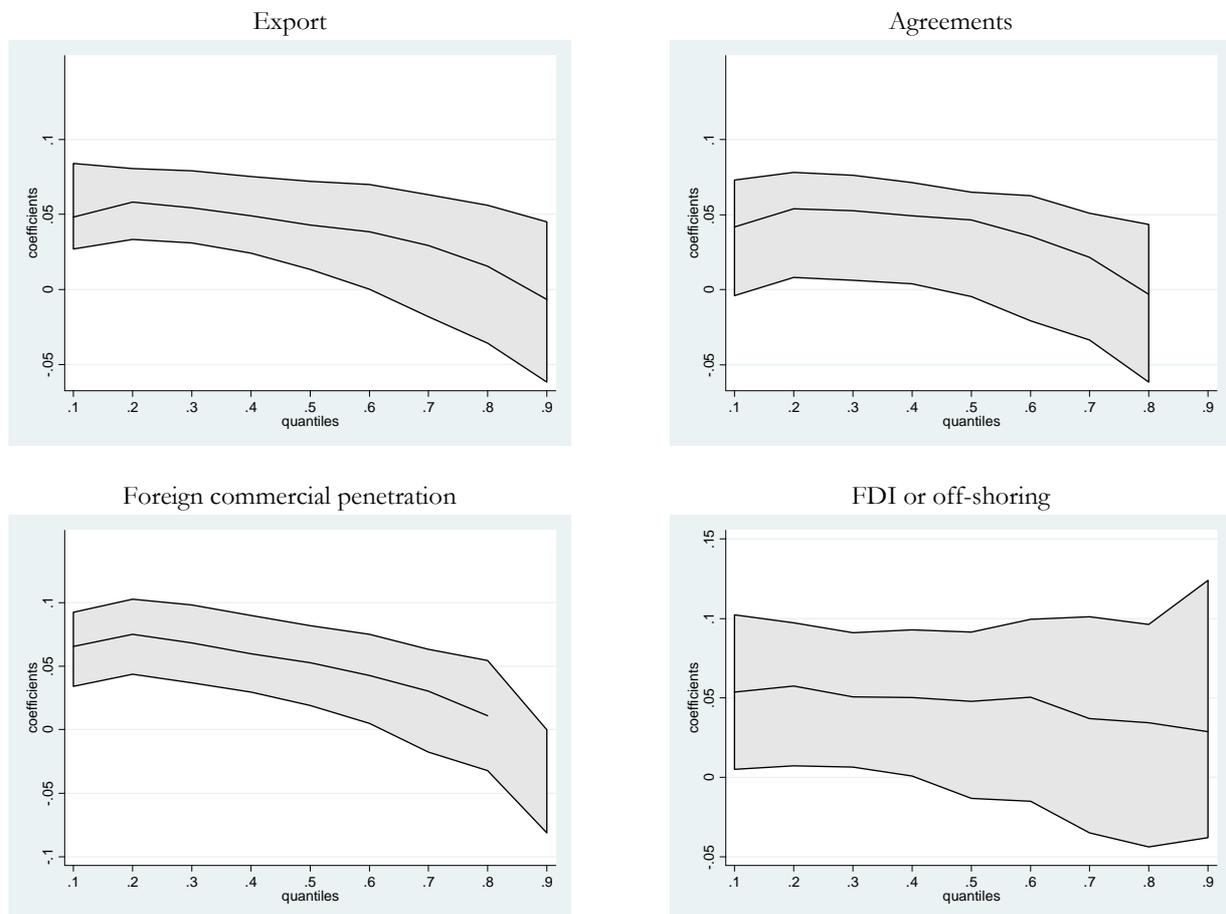
As in any method comparing two states (as for example index-numbers), the decomposition may change if the reference state changes. To control for these effects, results have been obtained by reversing the order of the decomposition and computing the productivity loss for domestic versus international firms. Changes observable in quantitative absolute results are negligible with no effects on the overall picture.

#### 4.1. Focusing on different internationalization modes

The main evidence emerging from the unconditional comparison in Section 3 is a relevant productivity premium for INT firms with respect to DOM firms, that is uniform along the entire distribution, i.e. for both more productive and less productive units. Estimators rank in ascending order the following internationalization modes with respect to TFP premium: at bottom although positive levels firms with export and commercial agreements, in the middle commercial penetration and at the top levels firms with FDI or off-shoring. These results seem to confirm the empirical evidence reported in literature. When the effect of firms' heterogeneity is controlled for, the previous analysis highlights that firms involved in internationalization still differ from domestic firms with respect to TFP, but with some variants: the net productivity premium is lower than the gross one and it entails only the less productive firms.

In order to evaluate if the net productivity premium and its link with TFP varies for different internationalization modes or for combination of them, we run quantile regression decompositions for groups of firms which distinctly perform export, foreign agreements, foreign commercial penetration, foreign direct investment or off-shoring versus DOM firms. In Figure 3 the components of the productivity gaps explained by coefficients, that is the net productivity premia, are depicted for each of the four analysed modes.

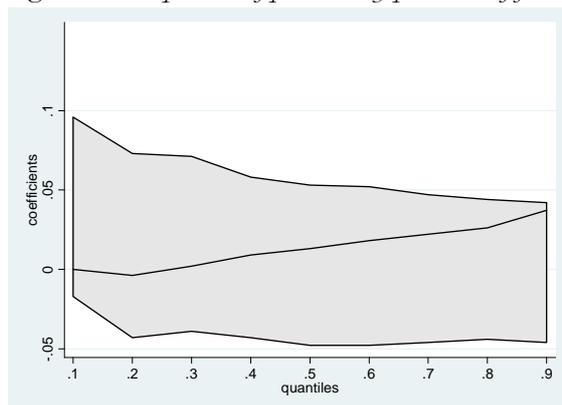
Figure 3. Components of productivity premium due to coefficients by internationalization mode



It is quite interesting to note that, after controlling for firm heterogeneity between each couple of groups (i.e. that one defined by each internationalization mode versus the DOM group) and within each group (that is at different quantiles) all the net productivity premia reduce to levels lower with respect to the unconditional gaps presented in Tab. 1.

Moreover, in general these premia are significantly different from zero for the less productive firms in each group, that is in the first parts of the distributions. The parts with non negligible net productivity premium vary from 40% for firms with foreign agreements to 60% for firms with export or foreign commercial penetration. An exception is given by the pattern of the premium for firms with FDI or off-shoring which does not decrease as quantiles increase. In a further control, the net premium of firms engaged in FDI or off-shoring versus exporter ones (Fig. 4) is found positive (although not significant) only for the firms with the highest level of TFP, that is on the top part of the TFP distribution. These two last findings support, also if only in qualitative terms since the confidence bounds are quite large due to limited size of the groups, the assumption widely discussed in literature that the productivity of firms engaged in FDI dominates the TFP of exporting firms which in turn dominates that of domestic ones. However this dominance is valid only for a part of the TFP distribution: the bottom part when exporter firms are compared to the domestic ones and the top part when firms engaged in FDI or off-shoring are compared to the exporters.

Figure 4. *Components of productivity premium of firms with FDI/Off-shoring versus exporting firms explained by coefficients*



## 5. Conclusions

Many papers in the empirical literature on the heterogeneity of firms find a productivity premium associated with international involvement. Two main questions are still open on this topic. The first entails the amount of the productivity premium which, although in relative terms, is rarely measured. The second entails the direction of the causality link between productivity and international openness. Does a self-selection mechanism induce the more productive firms to enter the international market or do internationalized firms, under the pressure of the global competition, become more productive by means of a learning-by-exporting type process?

The present paper does not provide a definitive answer to the above questions but certainly provides some useful insights. The analysis is conducted on micro-level data of a representative sample of Italian manufacturing firms. At first, as expected, the main evidence emerging from the unconditional comparison is that a relevant productivity premium for INT firms with respect to DOM firms exist and that it is uniform along the entire distribution, i.e. for more productive and less productive units. When the effect of firms heterogeneity is controlled for, by using quantile decomposition, firms involved in internationalization are found still differ from domestic firms with respect to TFP with some variants: the adjusted

internationalization premium is estimated positive and around 5% for the less productive firms, while it is negligible and not significant for the most productive ones. Clearly this finding does not give a definitive answer to the causality direction, but it restates the open question about the level and direction of the TFP gap, as we estimate that the TFP gap is 5% and it only regards the less productive firms.

In this framework, the self-selection hypothesis is only confirmed for the less productive firms. From this point of view, the internationalization policies should only target firms with a low level of TFP and they should foster the firms' performances and their productivity instead of promoting internationalization per se. Considering the learning-by-exporting hypothesis, our results may support previous evidence that this process mainly entails less productive (and often smaller) firms (Lileeva and Trefler, 2007). According to this hypothesis less productive firms seem to engage in a catching-up type behaviour and take more competitive advantage from openness to international markets. In this framework, policies targeting internationalization could result in an increase of firm productivity. To further understand the puzzle of causality, the time dimension in the data may no longer be neglected and future research will be focused on evaluating the pre-entry and post-entry (in the international markets) TFP differences.

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