Porter's Diamond Theory, developed by Michael E. Porter, provides a framework for understanding why certain nations achieve international success in particular industries. The theory identifies four interrelated determinants that create the environment in which companies are born, grow, and achieve competitive advantage on a global scale. Here's a breakdown of each determinant:

1. Factor Conditions

Factor conditions refer to a country's resources, such as labor, land, natural resources, capital, and infrastructure. However, Porter emphasizes that the most important factors are those created by investment and innovation, not just inherited natural resources. These include skilled labor, technological sophistication, and advanced research facilities. The theory suggests that countries will excel in industries where they have the most favorable factor conditions.

2. Demand Conditions

Demand conditions pertain to the nature and size of the home market demand for an industry's products or services. When local customers have high standards and expectations, companies are pushed to meet these demands, leading to a more competitive industry. High-quality home market demand encourages firms to innovate and improve, which can lead to competitive advantages internationally.

3. Related and Supporting Industries

The presence of competitive and innovative related and supporting industries can enhance the competitiveness of firms in an industry. For example, a strong automotive industry may benefit from competitive suppliers and related industries such as precision engineering. These relationships encourage the development of new technologies, efficient processes, and cost-effective inputs, fostering a more competitive environment for the primary industry.

4. Firm Strategy, Structure, and Rivalry

The ways in which companies are created, organized, and managed, as well as the nature of domestic rivalry, influence competitiveness. Different nations will develop unique management ideologies and structures, which can lead to competitive advantages. Furthermore, intense domestic rivalry breeds efficiency and innovation, as companies are forced to find new ways to gain a competitive edge. This constant drive for improvement prepares domestic companies to compete on a global scale.

The Diamond as a System

Importantly, these four determinants do not work in isolation; they are part of a dynamic system where each element influences and is influenced by the others. Additionally, the model is supplemented by two external variables:

- Government: Although not a part of the diamond, the role of government in shaping these determinants through policies and regulations is significant.
- Chance: Events outside of control (such as scientific breakthroughs or geopolitical shifts) can disrupt the status quo, impacting the national diamond.

Porter's Diamond Theory provides a useful lens for analyzing and understanding the competitive advantage of nations, helping to explain why some countries become global leaders in certain industries.