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THE NEW REALITIES



FIFTH EDITION

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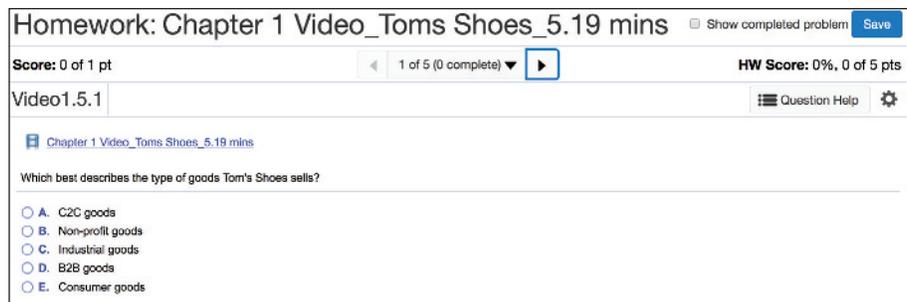
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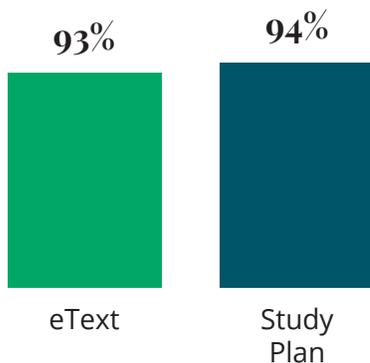
The screenshot shows a homework question interface. At the top, it says "Homework: Chapter 1 Video\_Toms Shoes\_5.19 mins" with a "Show completed problem" checkbox and a "Save" button. Below that, it shows "Score: 0 of 1 pt" and "1 of 5 (0 complete)" with navigation arrows. The "HW Score: 0%, 0 of 5 pts" is also visible. The question is "Which best describes the type of goods Tom's Shoes sells?" and the options are: A. C2C goods, B. Non-profit goods, C. Industrial goods, D. B2B goods, and E. Consumer goods.

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# **International Business**

## **The New Realities**

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# International Business

## The New Realities

Fifth Edition

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**Dedicated to...**

This book is dedicated to all those who feel passionate about cross-border business, our readers around the world. I trust that this edition will inspire and help you discover the magic of international business. Since any journey is much more rewarding when you are accompanied by others, I also dedicate this edition to my students of four decades whom I had the opportunity to mentor over the years.

**S. Tamer Cavusgil**  
**Atlanta, Georgia**

This book is dedicated to my wife, Mari, for her intellect, patience, and adventurous spirit; to Bill and Audrey, and to Hiroshi and Hisako, for being great parents and role models; and to the many students I have had the good fortune to influence over the years.

**Gary Knight**  
**Salem, Oregon**

This book is dedicated to my parents, Richard and Marie Riesenberger, for their example, many sacrifices, and love. To my wife and best friend, Pat, for her enthusiasm and loving support. To my daughters, Chris and Jen, of whom I am so very proud and thankful. To Byron, Ann-Marie and Terry, who enrich my life. To my amazing grandchildren, Ryan, Paige, Ethan, and Emma—the future of the New Realities.

**John R. Riesenberger**  
**Scottsdale, Arizona**

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# Preface

## New to This Edition

Our aim is to keep the text fully up-to-date and at a reasonable length. Thus, we have dropped some items and added new ones. From Chapter 1, we dropped the Opening Case on Facebook. From Chapter 4, we dropped the Closing Case on Bribery and Corruption at Siemens. From Chapter 4, we dropped the Closing Case on Bribery and Corruption at Siemens. From Chapter 5, we dropped the Closing Case on Hyundai and the Global Auto Industry. From Chapter 6, we dropped the Opening Case on Risks in Russia's Political and Legal Systems. From Chapter 9, we dropped the Closing Case on Financial Contagion and the Global Financial Crisis. From Chapter 17, we dropped the Opening Case on International Human Resource Management at Johnson & Johnson.

To replace the above dropped items and maintain currency, we have created new or greatly revised opening and closing cases in the fifth edition of Cavusgil, Knight, and Riesenberger (CKR 5e) as follows:

- Chapter 1: A new Opening Case on *Instagram: A Global Phenomenon*
- Chapter 2: A heavily revised Opening Case on *Spotify and the Rise of Born Global Firms*
- Chapter 4: A new Closing Case on the recent *Scandal at Volkswagen*
- Chapter 5: A new Closing Case on *Unilever's Comparative and Competitive Advantages*
- Chapter 6: A new Opening Case on *Odebrecht and Risks in Brazil's Political and Legal Systems*
- Chapter 7: A heavily revised Closing Case on *Government Intervention at Airbus and Boeing*
- Chapter 8: A heavily revised Closing Case on *Tata Group: India's Top Global Challenger*
- Chapter 9: A new Closing Case on *Tesco, the European Debt Crisis, and Brexit*
- Chapter 15: A heavily revised Closing Case on *Subway and the Challenges of Franchising in China*
- Chapter 16: A heavily revised Opening Case on *Michael Kors: The Global Affordable Luxury Market*
- Chapter 17: A new Opening Case on *International Human Resource Management at Google*

In addition, for our feature *You Can Do It: Recent Grad in IB*, we have added new biographies of young graduates with careers in international business. In Chapter 1, we added *Mary Lyles*, who works in global sourcing for Starbucks; and in Chapter 15, we added *Juanita Velez*, who works in international social media at Delta Air Lines.

In various chapters, we also added several new exhibits and significant new material on such contemporary topics as preparing for international travel, the rise of digital technologies, the trade and GDP growth relationship, the meaning of colors worldwide, workplace harassment, Brexit and the UK, populism, national governance, blockchain and cryptocurrencies, carbon taxes, cross-national project management, the Global Connectedness Index, global sourcing for smartphones, reshoring and nearshoring, the best global companies to work for, and women in international business, among numerous others.

## Solving Teaching and Learning Challenges

Today's students—often called Generation Z, Post Millennials, or the iGen—have grown up in a constantly connected world. To address the unique wants, needs and learning style of Generation Z students, we have designed CKR 5e to emphasize the following features:

- **Visual learning.** CKR 5e emphasizes interactive media and videos as well as exhibits, maps, and other visual learning aids. The MyLab Management provides access to a wide variety of additional visual resources.
- **Relevant knowledge and job-related skills.** CKR 5e includes more relevant examples and activities, concise foundational course content, Intangible Soft Skills, and Tangible Process Skills that prepare Generation Z students for the work world.

- **Contemporary issues that matter to Generation Z.** CKR 5e emphasizes the new international business environment, in-depth coverage of contemporary international business topics such as emerging markets, developing economies, growth of the service sector, risks in international business, digital technologies, women in international business, and other important trends.
- **Meaningful content.** CKR 5e provides substantial content on ethics, corporate social responsibility, and sustainability in international business.
- **Digital platform.** Generation Z learners prefer content that they can read or access digitally at a time and place of their choosing. Digital learning enhances engagement, self-pacing, and the ability to customize content to individual needs. Digital platforms help ensure timely, up-to-date content and the ability to collaborate with peers. In these and other ways, CKR 5e provides such digital options. To improve Generation Z students results, we recommend pairing the text content with MyLab Management, which is the teaching and learning platform that empowers you to reach every student. By combining trusted author content with digital tools and a flexible platform, MyLab personalizes the learning experience and will help your students learn and retain key course concepts while developing skills that future employers are seeking in their candidates. From Mini Sims to Personal Inventory Assessments, MyLab Management helps you teach your course, your way. Learn more at [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management).

Some of the main features of the textbook and MyLab are as follows:

**HIGHLY ACCESSIBLE WRITING AND EXPLANATIONS THAT ENGAGE STUDENTS.** Opening and closing cases appeal to students, featuring firms and subjects such as Apple, IKEA, Harley-Davidson, H&M, Instagram, born global firms, social media in China, and the global movie industry. The content stimulates student desire to learn more about international business.

**Constantly fluctuating exchange rates require international managers to keep in mind three facts:**

- The prices the firm charges can be quoted in the firm’s currency or in the currency of each foreign customer.
- Because several months can pass between placement and delivery of an order, fluctuations in the exchange rate during that time can cost or earn the firm money.
- The firm and its customers can use the exchange rate as it stands on the date of each transaction, or they can agree to use a specific exchange rate.

**MORE EXERCISES AND ACTIVITIES THAT ENABLE STUDENTS TO ACQUIRE CRITICAL THINKING AND PROBLEM-SOLVING SKILLS.** CKR 5e contains 174 exhibits (about three times more than leading competitors). Students like exhibits because they help clarify complex material and facilitate reading the chapters.

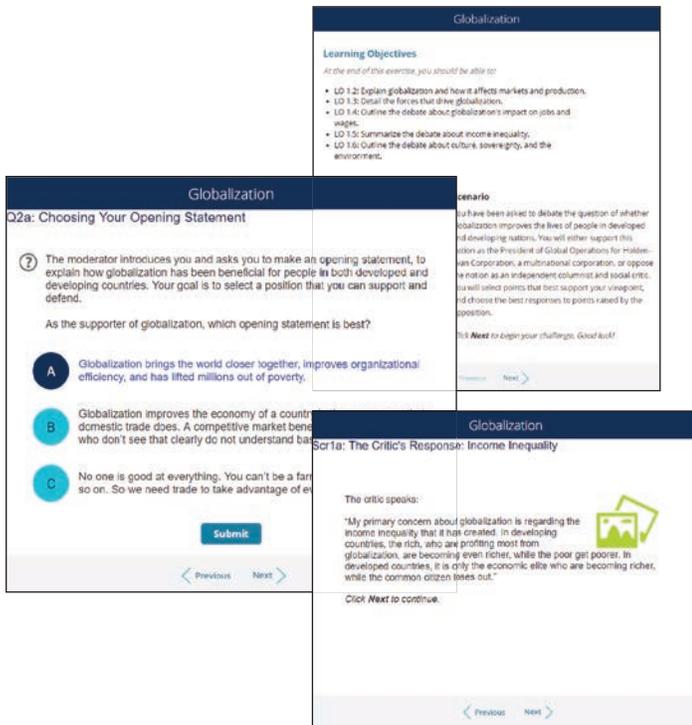
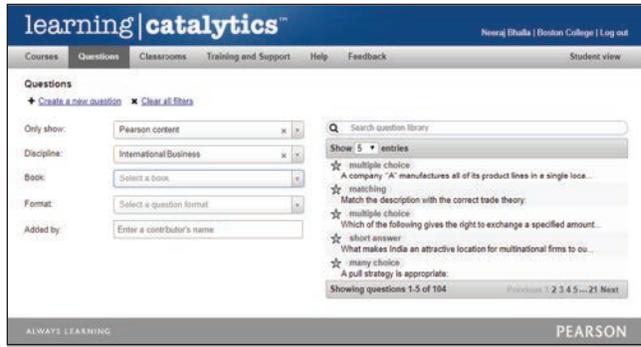
**TANGIBLE PROCESS TOOLS.** They are designed to simulate real-world decision making that will help increase effectiveness in the workplace.

**GROUP PROJECT ON INTERNATIONAL CORPORATE SOCIAL RESPONSIBILITY.** CKR 5e contains a comprehensive activity in which students debate corporate social responsibility (CSR) in international business. In this extended exercise, located in the *Instructor’s Manual*, students debate the merits and consequences of CSR as executives, consumers, or activists.

**YOU CAN DO IT—RECENT GRAD IN IB BIOGRAPHIES.** CKR 5e offers eleven biographies of actual university graduates who have embarked on fascinating careers in international business. These biographies include comments concerning the specific intangible soft skills that have helped them be successful in work.

<b>You Can Do It</b>	<b>RECENT GRAD IN IB</b>
	<p><b>TERRANCE ROGERS</b></p> <p><b>Terrance’s Majors:</b> Finance and international business</p> <p><b>Objectives:</b> Exploration, international perspective, self-awareness, career growth, and learning about foreign markets</p> <p><b>Internships during college:</b> Deutsche Bank</p> <p><b>Jobs held since graduating:</b></p> <ul style="list-style-type: none"> <li>• Business analyst at Deutsche Bank, New York</li> <li>• Management associate at Deutsche Bank, New York</li> <li>• Executive management rotation at Deutsche Bank, New York</li> <li>• Executive management associate at Deutsche Bank, London and New York</li> </ul>

**LEARNING CATALYTICS™.** With this tool, you'll hear from every student when it matters most. You pose a variety of questions that help students recall ideas, apply concepts, and develop critical-thinking skills. Your students respond using their own smartphones, tablets, or laptops.



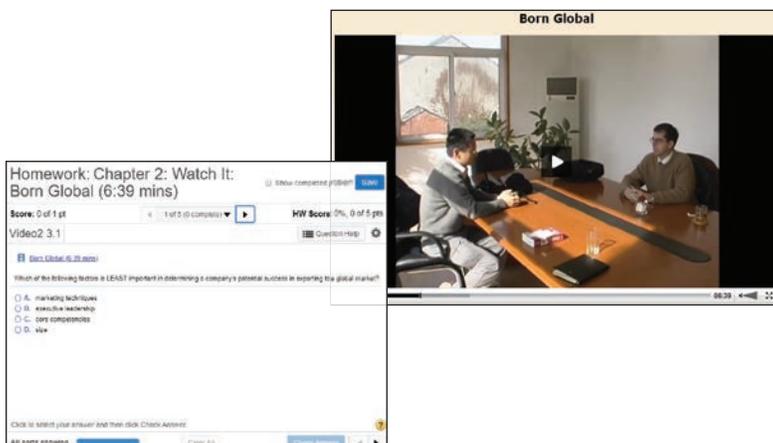
**NEW MINI SIMS.** Mini Sims put students in professional roles and give them the opportunity to apply course concepts and develop decision-making skills through real-world business challenges.

The simulations use each student's decisions to create various scenario paths that help them understand the impact their decisions can have on an organization.

These branching Mini Sims strengthen a student's ability to think critically, help students understand the impact of their decisions, engage students in active learning, and provide students with immediate feedback on their decisions.

Each decision point remediates to the Learning Objective in the eText.

**CHAPTER WARM-UP.** These questions help you hold your students accountable for learning key concepts in each chapter before coming to class.



**VIDEOS EXERCISES.** Engaging Videos explore a variety of business topics related to the theory students are learning in class.

Exercise Quizzes assess students' comprehension of the concepts in each video.



## Developing Employability Skills

The Association to Advance Collegiate Schools of Business (AACSB) International increasingly advocates a more skills-oriented, practical approach in business books, which this text provides, rather than a theory-based approach.

For students to succeed in a rapidly changing job market, they should be aware of their career options and how to develop various critical skills. In this book and MyLab Management, we focus on developing these skills.

The CKR 5e Career Preparation Kit™ incorporates CKR Tangible Process Tools™ as well as CKR Intangible Soft Skills™, which constitute guidelines of the Association to Advance Collegiate Schools of Business (AACSB). CKR Intangible Soft Skills focus on the skills employers have identified as needed for employability and success in the marketplace today. The CKR Tangible Process Tools will help students increase their effectiveness in the workplace.

The Employability Skills Table below provides students with a guide to features that support the development of skills employers are looking for in today’s business graduates, helping students to see from the start of class the relevance of the course to their career goals. This table identifies which features and end-of-chapter materials will help students to develop these skills.

Employability Skills Table			
Skills	Sections in the text and MyLab covering these skills		
<b>Written and oral communication</b>	Global Edge Internet Exercises - End of chapter box element	Test Your Comprehension - Chapter End exercises	EOC Writing Assignment - MyLab Management
<b>Critical thinking and problem solving</b>	Chapter Opening and Chapter Closing Cases	Apply Your Understanding - short, essay-style questions at the end of the chapter	New Mini Sims - MyLab Management
<b>Teamwork and collaboration</b>	Chapter Opening and Chapter Closing Cases	Apply Your Understanding - short, essay-style questions at the end of the chapter	
<b>Leadership</b>	Chapter 11, “Strategy and Organization in the International Firm”		
<b>Creativity</b>	Apply Your Understanding	Chapter Opening and Chapter Closing Cases	
<b>Ethics</b>	Chapter 4, “Ethics, Corporate Social Responsibility, Sustainability, and Governance in International Business”	Chapter 4 Watch It Video Exercises - MyLab Management	
<b>Information technology skills</b>	Global Edge Internet Exercises - End of chapter box element		

**OPENING CASE.** Each chapter begins with a brief case study that illustrates chapter topics and asks key questions about real-world companies and situations covered in the case.

**CLOSING CASE.** Every chapter closes with an extensive case study that addresses the learning objectives highlighted in the chapter. The cases help students build managerial skills by applying chapter material to a situation faced by real-world managers. Questions accompany the case for assignment as homework. Class discussion helps students sharpen their analytical and decision-making skills.

**TEST YOUR COMPREHENSION.** A list of 6 to 12 short questions assesses student learning of chapter learning objectives and other chapter concepts.

**APPLY YOUR UNDERSTANDING.** An additional collection of three short, essay-style questions aims to have students apply chapter material to real-world international business practice.

## CLOSING CASE Internationalization at Harley-Davidson

Considered an American icon by many, Harley-Davidson (Harley) is a U.S. motorcycle manufacturer founded in 1903 and offers 32 models through a network of about 1,500 dealers. Its global motorcycle revenue was about \$6 billion in 2017, continuing a three-year downward trend. Total sales have been relatively flat since 2012, with U.S. sales declining and international sales rising. Harley earns about two-thirds of its total sales in the United States, where it also manufactures almost all its bikes to support its brand image and quality control. The firm is embarked on a course to build the next generation of Harley riders globally; international markets are crucial to the firm's survival and growth. The CEO recently announced a bold goal to grow international sales to 50 percent of annual volume by 2027.

Harley is the only U.S.-based global motorcycle manufacturer and makes four distinctive groups of models:

- **Standard:** Practical bikes used for low-cost commuting
- **Performance:** Sleek, sport-style racing bikes built for speed and easy handling
- **Custom:** Stylized bikes customized to customer tastes
- **Touring:** Long-distance, large-capacity, comfort bikes that typically include cruise control, stereos, and luggage racks

quality management and empowered its production workers. Management increased marketing efforts, improved the dealer network, and undertook various cross-branding ventures. By the mid-1990s, management had repositioned Harley more strongly in the performance motorcycle market. The enhancements paid off in sharp improvements in company image and sales. However, the volume of Harley motorcycle shipments peaked in 2006. Shipments flattened or declined during the global financial crisis and ensuing recession and still had not recovered by 2018.

### International Expansion

Harley management resolved that future success would come from expansion into foreign markets. The firm had established a distribution network and local subsidiary in Japan, and by 2016, it was selling more than 16,000 motorcycles annually. It continued to sell heavyweight motorcycles in Japan at a price of more than \$20,000, substantially more than Honda's standard lightweight model. Harley's foreign saw a sustained growth.

Harley also made inroads in Europe, a vast marketplace and home to dozens of countries with diverse needs and tastes. In Europe, performance bikes are the top seller by far, accounting for more than one-third of Harley sales, followed by touring, standard



## INTERNET EXERCISES

Access globalEDGE™ at [www.globalEDGE.msu.edu](http://www.globalEDGE.msu.edu)

### AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Information Technology, Application of Knowledge, Diverse and Multicultural Work Environments, Written and Oral Communication, Analytical Thinking and Reflective Thinking

#### Knowledge Portal

globalEDGE™ is a leading knowledge portal for professionals in international business. It is a gateway to specialized knowledge on countries, international business transactions, culture, and firm practice. globalEDGE™ was developed at Michigan State University under the direction of Professor S. Tamer Cavusgil. Consult the globalEDGE™ portal to complete the Internet exercises at the end of each chapter.

1-20. You can gain valuable insights into international business by examining how countries compare to each other. Various research groups and international agencies systematically examine economic, political, and other features of nations. Visit globalEDGE™ Tools and Data, scroll down, and click Interactive Rankings. Select Countries. You will find dozens of criteria ranking countries based on GDP per capita; Education—literacy rate; People—population total; People—population density; Health—mortality rate; Energy—electricity production; Infrastructure—mobile cellular subscriptions; Infrastructure—roads, total network; Trade and Investment—foreign direct investment net inflows; and many other factors. Choose the ranking criteria that interest you most, and then examine the following three countries: Germany, India, and South Africa. Based on your analysis, explain why they rank where they do. Do

their relative positions make sense to you? Does each country seem like a good place to do business? Why or why not? **Hint:** Evaluate countries on a per-capita basis by dividing each criterion by the country's population.

1-21. In this chapter, we reviewed the four major risks that firms face in international business: cross-cultural risk, country risk, currency risk, and commercial risk. Identify one or more countries that interest you, and then visit globalEDGE™ and research the countries to uncover examples of each of the four types of risks. For example, China is characterized by various cultural differences and a national government that tends to intervene in business. Research by entering the country name in the search engine. Visit Global Insights and Market Potential Index. Illustrate each risk with examples.

1-22. You have recently been hired by a smaller firm that is beginning to expand internationally. When first starting out, most firms choose exporting as their main foreign market entry strategy. However, no one in your firm knows how to conduct exporting. Therefore, your boss has given you an assignment: Prepare a presentation for your coworkers on how to engage in exporting. Using globalEDGE™, find and review Guide to Exporting, which you can use to create your presentation.

**GLOBALEDGE INTERNET EXERCISES.** GlobalEDGE™ (<https://globaledge.msu.edu>) was developed by CKR author S. Tamer Cavusgil and is the leading knowledge portal for professionals in international business. It provides a gateway to specialized knowledge on countries, cross-border ventures, culture, and company practice. Each chapter provides several globalEDGE exercises as the basis for student assignments and projects.

**CKR TANGIBLE PROCESS TOOLS™.** These practical exercises familiarize students with key managerial challenges and decision making that professionals typically encounter in international business. By completing CKR Tangible Process Tools™ exercises, students can acquire real-world skills that will help them perform better in their careers.

### CKR Tangible Process Tools™

#### What is a CKR Tangible Process Tool Exercise?

CKR Tangible Process Tools consist of practical exercises and work processes designed to familiarize you with key managerial challenges and decisions that professionals typically encounter in international business. Completing CKR Tangible Process Tool exercises in this text enables you to acquire practical, real-world work processes that will improve employability and success in the workplace. Each exercise presents a managerial challenge in a real-world scenario, the skills you will acquire in solving the exercise, and a methodology and the resources to use in solving it. The second half of the exercise is provided at the Pearson MyLab Management website ([www.pearson.com/mylab/management](http://www.pearson.com/mylab/management)).

**AACSB TAGGING.** This book and MyLab Management support AACSB international accreditation. In every chapter, after each section of questions, specific AACSB tagging is provided to help instructors identify which AACSB Intangible Soft Skills that activity supports. AACSB tagging is also part of all questions in the Test Item File that accompanies the book.

## Instructor Teaching Resources

At the Instructor Resource Center, [www.pearsonhighered.com](http://www.pearsonhighered.com), instructors can easily register to gain access to a variety of instructor resources available with this text in downloadable format. If assistance is needed, our dedicated technical support team is ready to help with the media supplements that accompany this text. Visit <https://support.pearson.com/getsupport> for answers to frequently asked questions and toll-free user support phone numbers.

Supplements available to instructors at <a href="http://www.pearsonhighered.com/irc">www.pearsonhighered.com/irc</a>	Features of the Supplement
<b>Instructor’s Resource Manual</b> authored by Marta Szabo White, S. Tamer Cavusgil, Gary Knight, and John Riesenberger	<ul style="list-style-type: none"> <li>• Chapter-by-chapter summaries</li> <li>• Examples and activities not in the main book</li> <li>• Teaching outlines</li> <li>• Teaching tips, including openers to help launch lectures</li> <li>• Solutions to all questions and problems in the book</li> </ul>
<b>Test Bank</b> authored by John Capela	1,600 multiple-choice, true/false, short-answer, and essay questions with the following annotations: <ul style="list-style-type: none"> <li>• Difficulty level (1 for straight recall, 2 for some analysis, 3 for complex analysis)</li> <li>• Type (multiple-choice, true/false, short-answer, essay)</li> <li>• Learning objective</li> <li>• AACSB learning standard (Written and Oral Communication, Ethical Understanding and Reasoning, Analytical Thinking, Information Technology, Interpersonal Relations and Teamwork, Diverse and Multicultural Work Environments, Reflective Thinking, and/or Application of Knowledge)</li> </ul>
<b>TestGen® Computerized Test Bank</b>	TestGen allows instructors to: <ul style="list-style-type: none"> <li>• Customize, save, and generate classroom tests</li> <li>• Edit, add, or delete questions from the Test Item Files</li> <li>• Analyze test results</li> <li>• Organize a database of tests and student results</li> </ul>
<b>PowerPoints Presentations</b> authored by S. Tamer Cavusgil, Gary Knight, and John Riesenberger	<ul style="list-style-type: none"> <li>• Cover all concepts, explanations, and major examples in each chapter</li> <li>• Include all exhibits in the textbook</li> <li>• Meet accessibility standards for students with disabilities. Features include, but not limited to:                             <ul style="list-style-type: none"> <li><input type="checkbox"/> Keyboard and Screen Reader access</li> <li><input type="checkbox"/> Alternative text for images</li> <li><input type="checkbox"/> High color contrast between background and foreground colors</li> </ul> </li> </ul>
<b>Image Library</b>	<ul style="list-style-type: none"> <li>• A collection of photos and other images for use in enhancing PowerPoints and other teaching materials related to CKR 5e</li> </ul>

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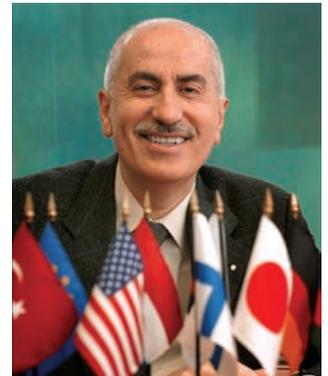
Tamer is an elected fellow of the Academy of International Business (AIB), a distinction earned by a select group of intellectual leaders in international business. He also served as vice president of the AIB and on the Board of Directors of the American Marketing Association.

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Tamer was awarded an honorary doctorate, *Doctor Honoris Causa*, by The University of Hasselt, Belgium, in May 2014 and an honorary doctorate from the University of Southern Denmark in October 2017. In 2018, Tamer was named an honorary professor by Atilim University in Ankara, Turkey.

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Gary has been Helen Simpson Jackson Chair in International Management at Willamette University since 2012. He was a professor at Florida State University for 15 years, where he directed the school's International Business Program. He also has been a visiting professor at the University of Southern Denmark and Nihon University in Japan.



Gary has been an invited speaker at institutions worldwide and developed study abroad programs in Asia, Europe, and Latin America. He has won several awards, including the Jerry Hudson Award for Excellence in Teaching, Willamette University, and Best Teacher in the MBA Program, Florida State University.

Gary has coauthored six books and more than 100 refereed articles in academic journals and conference proceedings. His research emphasizes international business strategy, international services, emerging markets, and internationalization of small and medium-sized firms.

Gary won the Hans Thorelli Best Paper Award for his article “Entrepreneurship and Strategy: The SME Under Globalization.” Along with S. Tamer Cavusgil, he won the 2014 Decade Award at the *Journal of International Business Studies* for their article on born global firms.

Gary is ranked in the top 5 percent of scholars who have published in the *Journal of International Business Studies* since 1995, based on number of articles published. He is ranked among the top five scholars in the United States and top 15 worldwide in international business research impact based on Google Scholar citation data. He is on the editorial review boards of several international journals. He has provided expert testimony on global commerce and small business to the U.S. House of Representatives.

Gary is chair of the Academy of International Business, Western United States Chapter. Prior to joining academia, he was export manager of a medium-sized enterprise, directing the firm’s operations in Canada, Europe, Japan, and Mexico and supervising some 50 distributors. He enjoyed a brief career in banking and as a teacher in Japan.

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## John R. Riesenberger

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John is an accomplished author, consultant, and international executive with senior executive positions in major pharmaceutical firms, biotechnology firms, and pharmaceutical agencies. John’s international business career spans more than three decades in the global pharmaceutical industry. He has conducted business transactions in 22 countries.

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He worked for 30 years with Pharmacia & Upjohn and The Upjohn Company as a senior international executive. His experience covered a diverse range of divisional, geographic, and functional accountabilities. His most recent position was as vice president of Global Business Management. He also served as corporate vice president and chief commercialization officer for a biotechnology firm and as the executive vice president of a pharmaceutical science agency.

John serves as a member of the board of directors of the Ontario Institute for Cancer Research. He was a member of the Global Advisory Board of the American Marketing Association. He served as an executive in residence at the Michigan State University Center for International Business Education and Research. He served on the editorial review board of the *Journal of International Marketing*. He served as chairman of the Industry Advisory Board’s Value of Marketing Program, SEI Center for the Advanced Studies in Management at the Wharton School of

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John holds a bachelor of science degree in economics–business and an MBA in management from Hofstra University. He attended the Harvard Business School’s International Senior Management Program.

# Chapter 1

## Introduction: What Is International Business?

**Learning Objectives** *After studying this chapter, you should be able to:*

- 1.1** Describe the key concepts in international business.
- 1.2** Understand how international business differs from domestic business.
- 1.3** Identify major participants in international business.
- 1.4** Describe why firms internationalize.
- 1.5** Appreciate why you should study international business.
- 1.6** Learn the CKR Intangible Soft Skills™ and the CKR Tangible Process Tools™ to improve your employability and success in the workplace.

## Instagram: A Global Phenomenon

**G**lobalization refers to ongoing economic integration and growing interdependency of countries worldwide. It implies rising economic, political, and personal interconnectedness among countries, companies, and consumers. Widespread adoption of smartphone apps like Facebook and Instagram exemplifies globalization and converging lifestyles around the world. The number of smartphone users worldwide has reached 3 billion, about 40 percent of world population. Smartphone ownership is common in the advanced economies—especially in Australia, Europe, and North America—where 65 percent of residents own such devices. The phones are increasingly popular in emerging markets—countries such as Chile, China, Poland, and Russia—where the ownership rate is more than 50 percent. Developing economies—countries such as Bangladesh, Nigeria, Pakistan, and Ukraine—have low

smartphone penetration rates, mainly due to lower incomes and underdeveloped infrastructure.

Founded in 2010, Instagram is a photo- and video-sharing network that smartphone owners use to share photos and short videos with others. The site has more than 700 million active monthly users, the majority of whom are women, and most are under age 35. Instagram was acquired by Facebook in 2012 for about US\$1 billion.

Available in 33 languages, Instagram has a dual identity—a for-profit business *and* a vehicle for our personal lives. Instagram is the sixth most popular social media platform worldwide, after Facebook, Twitter, LinkedIn, YouTube, and Google+. Instagram emphasizes sharing photographs and enjoys a very enthusiastic following from visually oriented social media users. The app is popular worldwide, especially in countries like Russia,



Source: Dmytro Kosmenko/123rf

Brazil, Turkey, the United Kingdom, Poland, and the United States.

Instagram is a truly global platform—more than 80 percent of users are outside the United States, where the app is based. Management has used foreign direct investment to establish offices around the world. The most photographed countries among Instagram users are Italy, Japan, Indonesia, Kuwait, Thailand, and France. Tourist destinations such as Rome, Kyoto, Dubai, Paris, and the Grand Canyon are popular subjects. Pizza is the most Instagrammed food, followed by sushi.

The Instagram platform allows people to take and share high-quality photographs using low-resolution phones, which appeals to users in less-developed economies. Users in such countries often cannot afford sophisticated phones or access fast cellular networks that allow conveniently downloading the Instagram app. Many lack enough phone storage to easily download the

app. To get around these problems, Instagram launched an expanded web version that allows users to skip the app's wait time, data costs, and storage needs while still providing basic functionality.

Retailers and other companies leverage Instagram to market their products and services at low cost. Instagram first launched advertising, along with its photo feed, to subscribers in Australia, Canada, and the United Kingdom in 2014. Most of the world's top brands—for example, Apple, BMW, and Sony—have established Instagram pages, and many actively share photos or videos every week. Today, Instagram earns more than \$5 billion in annual advertising revenue worldwide.

German sportswear company Puma contracts with Instagrammers who have many followers to capture photos that showcase the firm's products. The Danish brewing company Carlsberg launched a marketing strategy called "Happy Hour" that offers half-priced beers in

exchange for Instagram posts. In Japan, Instagram's most popular influencer is a dog, Marutaro, who promotes pet food, real estate, and other ventures through the app. Sports teams use Instagram to promote themselves in Brazil. The Instagram phenomenon illustrates how converging lifestyles, communications technology, and imaginative entrepreneurship are facilitating the emergence of global enterprises.

### **AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Written and Oral Communication, Reflective Thinking and Application of Knowledge**

#### **Questions**

- 1-1.** What advantages does Instagram obtain from doing business in international markets?
- 1-2.** What attributes of Instagram have allowed it to gain rapid acceptance in countries around the world?
- 1-3.** How do companies use Instagram to market their products and services?

**SOURCES:** B. Ahmadinejad and H. Asli, "E-business through Social Media: A Quantitative Survey (Case Study: Instagram)," *International Journal of Management, Accounting and Economics*, 4, No. 1 (2017), [www.ijmae.com](http://www.ijmae.com); S. Aslam, "Instagram by the Numbers: Stats, Demographics & Fun Facts," *Omnicores*, August 10, 2017, [www.omnicoreagency.com](http://www.omnicoreagency.com); J. Constone, "Instagram Launches Mobile Web Sharing to Pursue Global Growth," *Techcrunch*, May 8, 2017, <https://techcrunch.com>; E. Hamburger, "Instagram Shoots for Global Expansion with Big Android Update," *The Verge*, March 11, 2014, [www.theverge.com](http://www.theverge.com); E. Hancock, "The 23 Most Instagrammed Countries of All Time," *Business Insider*, December 1, 2016; J. Hempel and A. Nyantakyi, "Instagram Is Ready to Take Its Shot," *Fortune International (Europe)*, July 21, 2014, pp. 72–77; S. Joseph, "Carlsberg Offers Drinkers Half-Priced Beers in Exchange for Instagram Posts," *Marketing Week*, March 17, 2014, [www.marketingweek.com](http://www.marketingweek.com); Newzoo, "Top 50 Countries by Smartphone Users and Penetration," April 2017, <http://newzoo.com>; M. Swant, "This Instagram Timeline Shows the App's Rapid Growth to 600 Million," *Adweek*, December 15, 2016, [www.adweek.com](http://www.adweek.com).

#### **International business**

Performance of trade and investment activities by firms across national borders.

As revealed in the opening case, international business touches our daily experiences. **International business** refers to firms' performance of trade and investment activities across national borders. Because it emphasizes crossing national boundaries, we also refer to international business as *cross-border business*. Firms organize, source, manufacture, market, and conduct other value-adding activities on an international scale. They seek foreign customers and engage in collaborative relationships with foreign business partners. Although international business is performed mainly by individual firms, governments and international agencies also conduct international business activities.<sup>1</sup> Firms and nations exchange many

#### **CKR Career Preparation Kit™**

In this textbook, *International Business: The New Realities*, by Cavusgil, Knight, and Riesenberger ("CKR"), we will present guidance on how best to prepare for a career in international business, the CKR CAREER PREPARATION KIT™.

##### **The Unmet Need**

Numerous surveys of employers, educators, and students suggest that today's graduates are not adequately prepared for the job market. Students need to acquire intangible soft skills and tangible process tools to improve their employability and succeed in the workplace.

##### **The Solution**

*International Business: The New Realities CKR CAREER PREPARATION KIT* has been specifically designed to integrate and advance your learning of intangible soft skills and tangible process tools.

### CKR Intangible Soft Skills™

Surveys and the findings of the Association to Advance Collegiate Schools of Business (AACSB) identify the following Intangible Soft Skills as necessary for success in today's workplace:

- *Written and oral communication*
- *Ethical understanding and reasoning*
- *Information technology*
- *Analytical thinking*
- *Diverse and multicultural work environments*
- *Reflective thinking*
- *Application of knowledge*
- *Interpersonal relations and teamwork*

Each chapter of CKR has been specifically designed to integrate and advance your learning of these intangible soft skills. End-of-chapter exercises—Test Your Comprehension, Apply Your Understanding, and globalEDGE Internet Exercises—help you develop these critical skills.

### CKR Tangible Process Tools™

Understanding and applying these tools will help you increase your effectiveness in the workplace. “Tangible Process Tools” appear at the end of selected chapters and consist of process tools that will enable you to address real-world challenges often encountered by managers in the workplace. Some of the tools consist of helpful checklists. Others will present a real-world management scenario, methodology, and the resources to solve it. Please visit the Pearson MyLab Management at [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) to access the “CKR: Travel Abroad Preparation Checklist™,” which will assist you in gathering necessary documents, as well as tools and aids for health care, telecommunications, funds, customs, and other requirements for visiting different countries.

For a more detailed treatment of this topic, visit the Pearson MyLab Management website ([www.pearson.com/mylab/management](http://www.pearson.com/mylab/management)).

physical and intellectual assets, including products, services, capital, technology, know-how, and labor. In this book, we are mainly concerned with the international business activities of the individual firm.

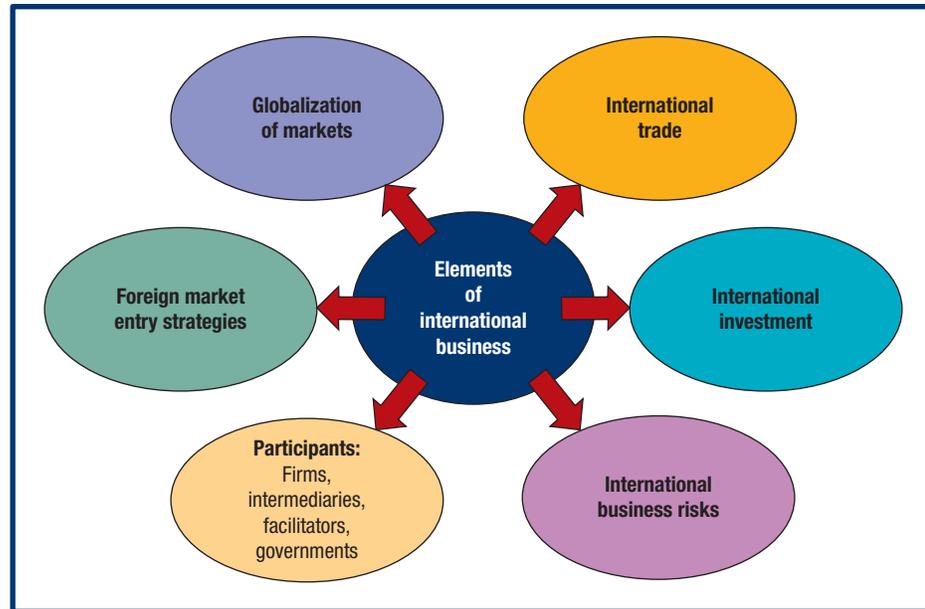
International business is characterized by six major dimensions, as shown in Exhibit 1.1. Firms' growing international activities give rise to the globalization of markets. As they venture abroad, firms undertake international trade and investment activities. In doing so, they encounter various types of risks and challenges that occur to a lesser degree, or not at all, in the home country. Participants in international business are diverse and include firms, distribution channel intermediaries, and facilitators. When they expand abroad, firms employ such international market entry strategies as exporting and direct investment. We explore each of the six dimensions in detail in this chapter.

Although trading across borders has been around for centuries, contemporary international business has gained much momentum and complexity over the past few decades. Firms seek international market opportunities more than ever before. Like Instagram, international business affects the everyday lives of people worldwide. Daily activities such as shopping, listening to music, watching a movie, or surfing the Internet involve interactions and transactions that connect you to the global economy. Internationalization of business gives you access to products and services from around the world. It profoundly affects your quality of life and economic well-being.

Online platforms such as Amazon, Alibaba, Facebook, and Instagram are all expressions of ongoing economic integration and growing interdependency of countries worldwide, known as the **globalization of markets**. Globalization is a macro-trend of intense economic interconnectedness among the nations of the world. A parallel trend is the ongoing internationalization of countless firms and dramatic growth in the volume and variety of cross-border transactions in

#### Globalization of markets

Ongoing economic integration and growing interdependency of countries worldwide.

**EXHIBIT 1.1****Elements of International Business****Internationalization**

The tendency of *companies* to deepen their international business activities systematically.

goods, services, and capital flows. **Internationalization** refers to the tendency of companies to deepen their international business activities systematically. It has led to widespread diffusion of products, technology, and knowledge worldwide.

Globalization both compels and facilitates firms to expand abroad. Simultaneously, company internationalization has become easier than ever before. A few decades ago, international business was largely the domain of large, multinational firms. Recent developments have created a more level playing field that allows all types of firms to benefit from active participation in international business. In this book, you will read about the international activities of smaller firms and those of large, multinational enterprises. You will learn about companies in the services sector that are internationalizing in such industries as banking, engineering, insurance, and retailing.

### The globalization of markets is evident in several related trends.

- *Unprecedented growth of international trade.* In 1960, cross-border trade was modest—about \$300 billion per year. Today, it accounts for a substantial proportion of the world economy, with world exports alone amounting to some \$16 trillion annually—that is, \$16,000,000,000,000!
- *Trade between nations, accompanied by substantial flows of capital, technology, data, and communications.* In 2004, total cross-border bandwidth in digital data transfer and communications was practically zero. Today, total cross-border bandwidth flows now exceed 400,000 gigabits per second. Virtually every type of international transaction now includes a digital component.
- *Development of highly sophisticated global financial systems and mechanisms* that facilitate the cross-border flow of products, money, technology, and knowledge.
- *Greater collaboration among nations* through multilateral agencies such as the World Trade Organization (WTO, [www.wto.org](http://www.wto.org)) and the International Monetary Fund (IMF, [www.imf.org](http://www.imf.org)).

Source: McKinsey Global Institute, *Digital Globalization: The New Era of Global Flows* (2016), [www.mckinsey.com](http://www.mckinsey.com); UNCTAD, *World Investment Report*, New York: United Nations (2017), [www.unctad.org](http://www.unctad.org); World Trade Organization, *World Trade Report*, Geneva: World Trade Organization (2017), [www.wto.org](http://www.wto.org).

## What Are the Key Concepts in International Business?

**International trade** describes the exchange of products (merchandise) and services (intangibles) across national borders. Exchange can occur through **exporting**, the sale of products or services to customers located abroad from a base in the home country or a third country. Exchange also can take the form of **importing or global sourcing**—the procurement of products or services from suppliers located abroad for consumption in the home country or a third country. While exporting represents the outbound flow of products and services, importing is an inbound activity. Both finished products and intermediate goods (for example, raw materials and components) can be imported and exported.

**International investment** refers to the transfer of assets to another country or the acquisition of assets in that country. Economists refer to such assets as *factors of production*; they include capital, technology, managerial talent, and manufacturing infrastructure. Trade implies that products and services cross national borders. By contrast, investment implies that the firm itself crosses borders to secure ownership of assets located abroad.

The two essential types of cross-border investment are international portfolio investment and foreign direct investment. **International portfolio investment** refers to the passive ownership of foreign securities such as stocks and bonds to gain financial returns. It does not entail active management or control over these assets. The foreign investor has a relatively short-term interest in the ownership of these assets.

**Foreign direct investment (FDI)** is an internationalization strategy in which the firm establishes a physical presence abroad through acquisition of productive assets such as land, plant, equipment, capital, and technology. It is a foreign-market entry strategy that gives investors partial or full ownership of a productive enterprise typically dedicated to manufacturing, marketing, or management activities. Investing such resources abroad is generally for the long term and involves extensive planning.

### The Nature of International Trade

Overall, export growth has outpaced the growth of domestic production during the past few decades, illustrating the fast pace of globalization. Exhibit 1.2 contrasts the growth of total world exports with the growth of total world *gross domestic product (GDP)* since 1980. GDP is defined as the total value of products and services produced in a country in the course of a year. As reflected in the exhibit, world trade declined in 2009 due to the global recession, following a 27-year boom. Trade revived and returned to normal levels by 2012. Trade was a key factor in reducing the impact of the global recession.<sup>2</sup> What is remarkable is that throughout most of the

**1.1** Describe the key concepts in international business.

#### International trade

Exchange of products and services across national borders, typically through exporting and importing.

#### Exporting

Sale of products or services to customers located abroad from a base in the home country or a third country.

#### Importing or global sourcing

Procurement of products or services from suppliers located abroad for consumption in the home country or a third country.

#### International investment

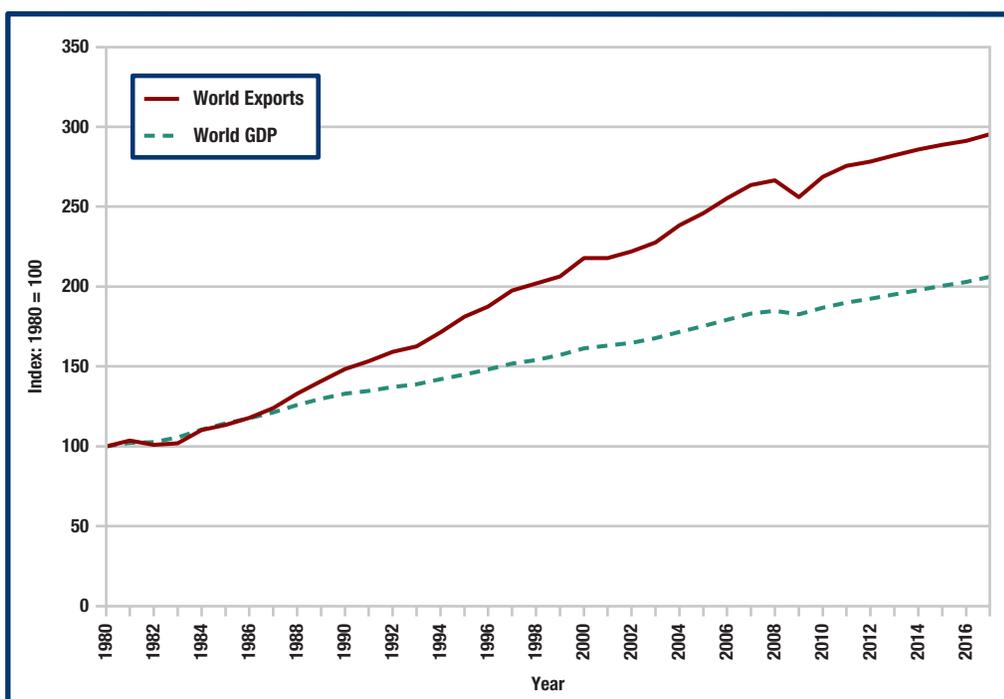
The transfer of assets to another country or the acquisition of assets in that country.

#### International portfolio investment

Passive ownership of foreign securities such as stocks and bonds to generate financial returns.

#### Foreign direct investment (FDI)

An internationalization strategy in which the firm establishes a physical presence abroad through acquisition of productive assets such as capital, technology, labor, land, plant, and equipment.



#### EXHIBIT 1.2

#### Comparing the Growth Rates of World GDP and World Exports

Source: Based on data from the International Monetary Fund, *World Economic Outlook Database October 2017*, [www.imf.org](http://www.imf.org).

past few decades, average annual growth rate in world exports has surpassed that of world GDP by a factor of almost two (5.3 versus 2.8 percent).

Three factors have been especially notable in explaining why trade growth has long outpaced GDP growth. First is the rise of emerging markets during the past three decades. These rapidly developing economies are home to swiftly growing middle-class households possessing substantial disposable income. Second, advanced (or developed) economies such as the United States and the European Union are sourcing many of the products they consume from such low-cost manufacturing locations as China, India, and Mexico. Third, advances in information and transportation technologies, decline of trade barriers, and liberalization of markets all have contributed to rapid growth of trade among nations.

Exhibit 1.3 identifies leading nations in exports of merchandise (and not services). Panel (a) shows the total annual value of merchandise exports and imports in billions of U.S. dollars. Panel (b) shows the annual value of products traded as a percentage of each nation's GDP. Total merchandise trade (exports plus imports) of the countries in panel (a) is nearly \$18,000 billion and accounts for about half of world merchandise trade. To get a better sense of the structure of international trade, Exhibit 1.4 presents the world's top trading countries. It reveals that China, the United States, Germany, and Japan are the world's leading international traders. China and the United States are close competitors in total trade, but trade accounts for about 31 percent of China's GDP as opposed to 19 percent for the United States. Merchandise trade is a much larger component of economic activity in countries such as the Netherlands (126 percent) and South Korea (69 percent). These percentages suggest that some countries depend very heavily on international trade relative to the value of all goods and services they produce domestically.

In some cases, countries' total trade surpasses 100 percent of the nation's GDP. How can this be? The answer is that countries such as Singapore, Hong Kong, and the Netherlands are known as *entrepôt* economies. *Entrepôt* is from the French for "intermediate depot." Such countries import a large volume of products, some of which they process into higher value-added products and some of which they simply re-export to other destinations. They often arise in locations that enjoy especially advantageous access to larger, adjacent markets. For example, Singapore is a major *entrepôt* for Southeast Asia, e.g., for transshipping petroleum products that it receives from the Middle East. Hong Kong is an *entrepôt* for China. The Netherlands is an *entrepôt* for the greater European Union.

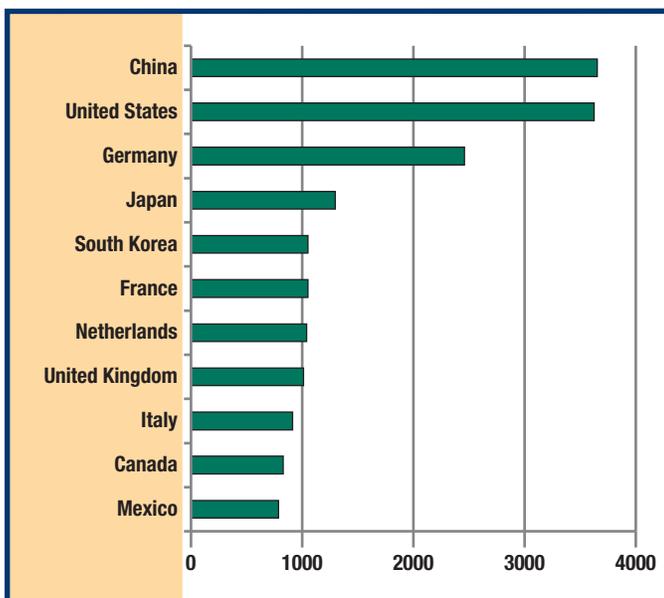
### EXHIBIT 1.3

#### Leading Countries in International Merchandise Trade

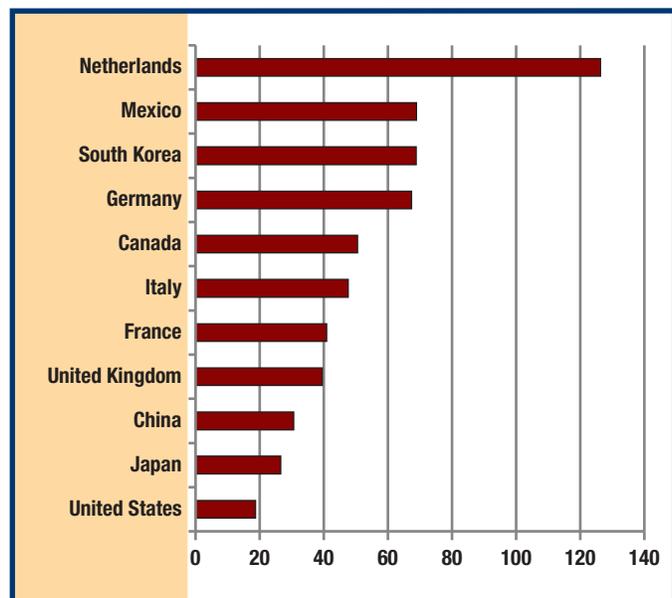
Sources: Based on data from the World Bank, *World Development Indicators*, Washington, DC: World Bank (2017), [www.worldbank.org](http://www.worldbank.org); World Trade Organization, *Statistics Database*, Geneva: World Trade Organization (2017), [www.wto.org](http://www.wto.org); UNCTAD, *World Investment Report*, New York: United Nations (2017), [www.unctad.org](http://www.unctad.org).

#### The Nature of International Investment

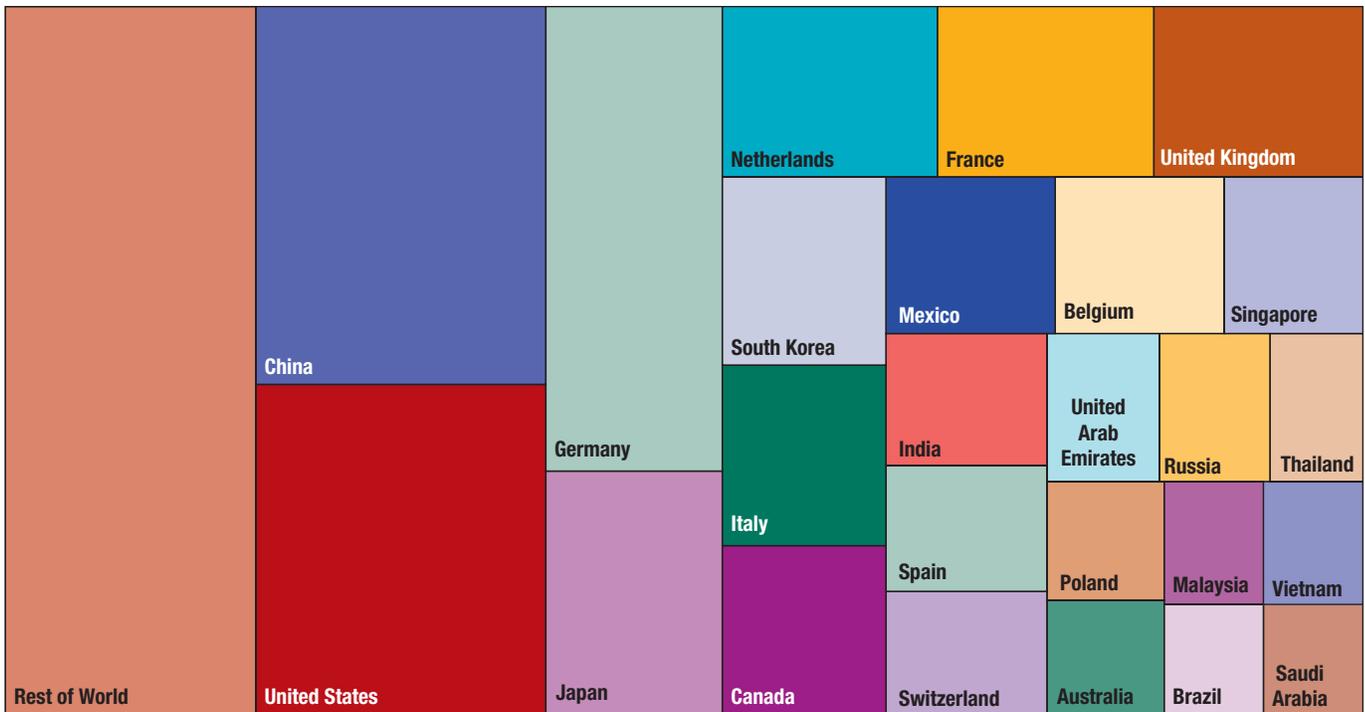
Of the two types of investment flows—portfolio investment and foreign direct investment—we are concerned primarily with foreign direct investment (FDI) in this text because it is the ultimate form of internationalization and encompasses the widest range of international business



(a) Total annual value of products trade (exports + imports) in billions of U.S. dollars



(b) Total annual value of products trade (exports + imports) as a percentage of nation's GDP



#### EXHIBIT 1.4

#### The Top 25 Countries in International Merchandise Trade

Sources: Based on data from the World Bank, *World Development Indicators*, Washington, DC: World Bank (2017), [www.worldbank.org](http://www.worldbank.org); World Trade Organization, *Statistics Database*, Geneva: World Trade Organization (2017), [www.wto.org](http://www.wto.org); UNCTAD, *World Investment Report*, New York: United Nations (2017), [www.unctad.org](http://www.unctad.org).

Note: The exhibit reflects the value of each country's combined exports and imports as a percentage of total world trade.

involvement. FDI is the foreign entry strategy practiced by the most internationally active firms. Companies usually undertake FDI for the long term and retain partial or complete ownership of the assets they acquire. In the process, the firm establishes a new legal business entity in the host country, subject to the regulations of the host government.

FDI is especially common among large, resourceful companies with substantial international operations. For example, many European and U.S. firms have invested in China, India, and Brazil to establish plants to manufacture or assemble products, taking advantage of low-cost labor or natural resources in these countries. At the same time, companies from these rapidly developing economies have begun to invest in Western markets. In 2012, for example, the Haier Group from China acquired New Zealand's appliance manufacturing company Fisher & Paykel. Then, in 2016, Haier purchased General Electric's appliance division for \$5.4 billion.<sup>3</sup>

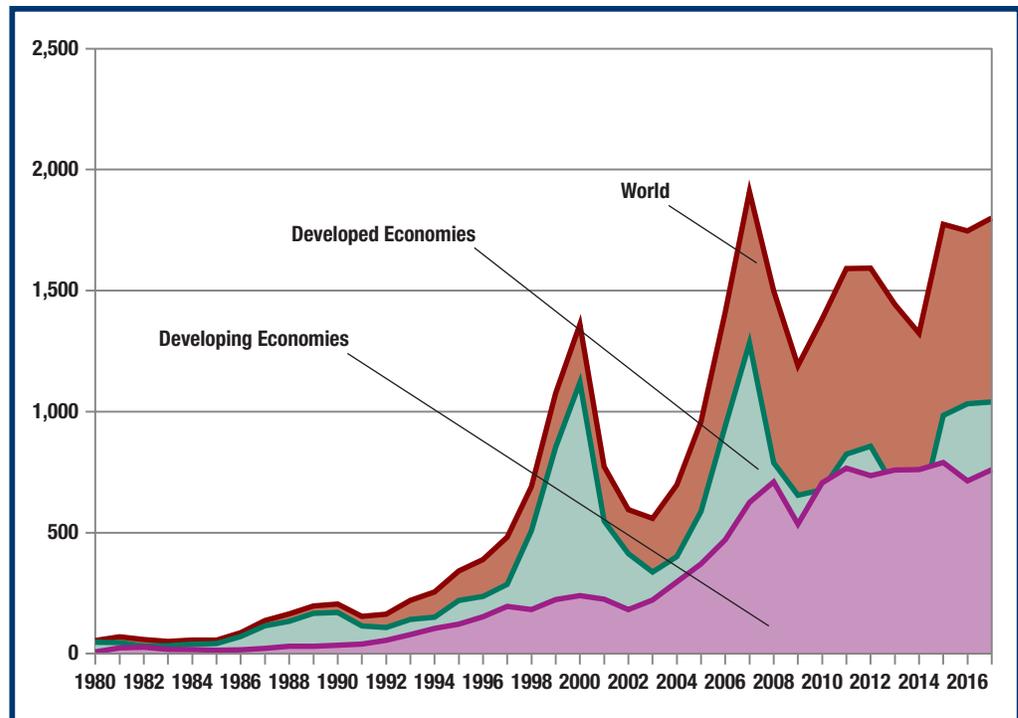
Exhibit 1.5 illustrates the dramatic growth of FDI since the 1980s. The exhibit reveals that the dollar volume of FDI has grown immensely since the 1980s, especially in developed (advanced) economies such as Japan, Europe, and North America. FDI inflows to the developing economies began to surpass those to the advanced economies in about 2010. FDI inflows were interrupted in 2001 as investors panicked following the September 11 terrorist attacks in the United States. The inflows were interrupted again in 2008 by the global recession but then rose sharply in subsequent years. These dips underscore the importance of maintaining stability in the world economy. Despite these setbacks, the overall trend remains strong and growing over time. Particularly significant is the growth of FDI into developing economies, much of which results from their need for modern industrial infrastructure. It reflects the importance of developing economies and emerging markets as target markets and sourcing bases.

### Services as Well as Products

Historically, international trade and investment were mainly the domain of companies that make and sell products—tangible merchandise such as clothing, computers, and motor vehicles. Today, firms that produce *services* (intangibles) are key international business players as well. Services are deeds, performances, or efforts performed directly by people working in banks, consulting firms, hotels, construction companies, retailers, and countless other firms in the services sector. International trade in services accounts for about one-quarter of all international trade and is growing rapidly.

**EXHIBIT 1.5****Foreign Direct Investment (FDI) Inflows into World Regions (in Billions of U.S. Dollars per Year)**

Sources: UNCTAD, *UNCTADSTAT Database*, Inward FDI Flows, Annual (2017); OECD, *FDI Flows* (2017), <https://data.oecd.org/fdi/fdi-flows.htm>; World Bank, *Foreign Direct Investment, Net Inflows (BoP, Current US\$)* (2017), <http://data.worldbank.org>.

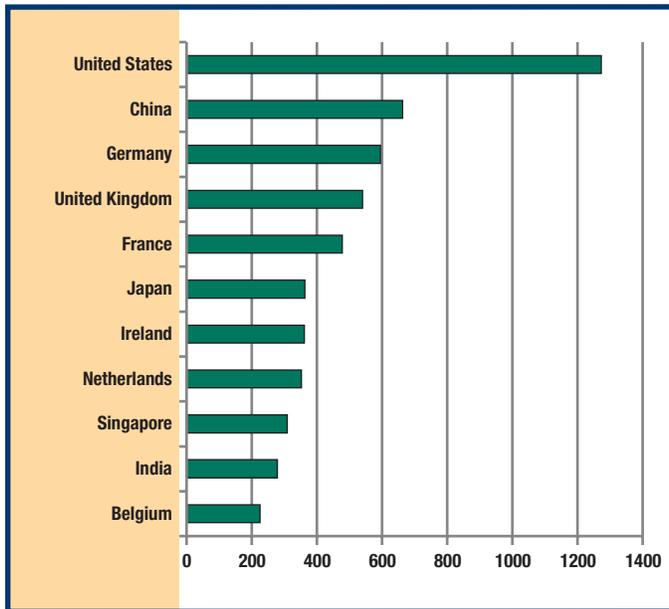


Instagram in the opening case is a leading services firm that has internationalized rapidly. If you own a house, your mortgage might be underwritten by the Dutch bank ABN Amro. Perhaps you eat lunch in a cafeteria owned by the French firm Sodexho, which manages the food and beverage operations on numerous university campuses. Recently, Riot Games expanded its operations into Germany, Ireland, China, Turkey, and numerous other countries to meet rapidly rising demand for its online video games. Demand for the firm's *League of Legends* game has spread rapidly, prompting the need to establish offices at gamer locations worldwide. The 2017 League of Legends World Championship attracted fans from around the world for two weeks of competition and more than 100 hours of live content broadcast in more than 20 languages.<sup>4</sup>

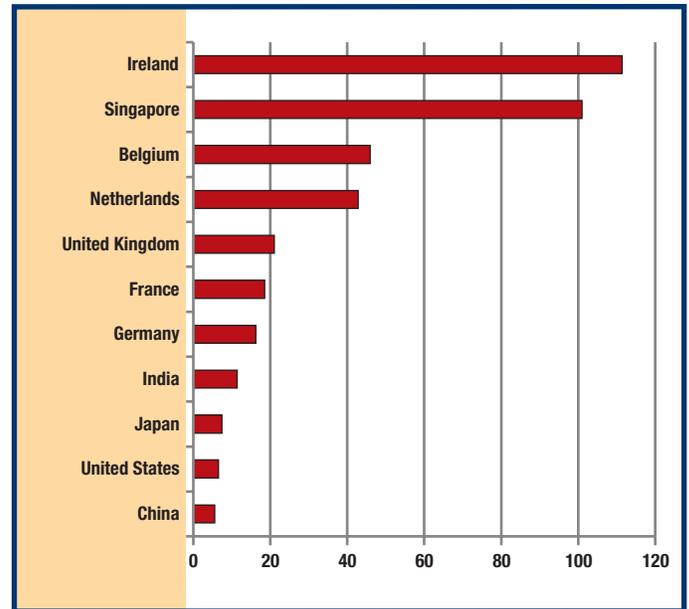
Exhibit 1.6 identifies countries leading in total international services trade. Panel (a) shows the total annual value of services exports and imports in billions of U.S. dollars. Panel (b) shows the total annual value of services trade as a percentage of each nation's GDP. As with products, larger advanced economies account for most world services trade. This is expected because services typically comprise more than two-thirds of the GDPs of these countries. Recently, the emerging markets of China and India have gained strong reputations in this area. Ireland has emerged as the leader in world services trade as a percentage of GDP. Compare the value of merchandise trade in Exhibit 1.3 with the value of services trade in Exhibit 1.6 for each country. Although services trade is growing rapidly, the value of merchandise trade is still much larger. One reason is that services face greater challenges and barriers in cross-border trade than merchandise goods.

Not all services can be exported. Examples are repair work done on your bicycle or the experience of eating a meal in a restaurant. Although some services can be digitized and moved across borders, most service providers can operate internationally only by establishing a physical presence abroad through direct investment. Firms invest abroad to set up restaurants, retail stores, and other physical facilities through which they sell billions of dollars' worth of services every year.

There are numerous industries in the services sector with strong potential for internationalization. The giant Internet retailer eBay earned about \$9 billion in 2017, of which more than 50 percent came from international sales. The company expects that most future revenue growth will come from abroad. When developing its business in India, eBay acquired the Mumbai-based e-retailer Baazee, which followed eBay's expansion into China, Korea, and Europe. Vendors in Russia now constitute a big portion of eBay's business.<sup>5</sup>



(a) Total annual value of services trade (exports + imports) in billions of U.S. dollars



(b) Total annual value of services trade (exports + imports) as a percentage of nation's GDP

### EXHIBIT 1.6

#### Countries Leading in International Services Trade

Sources: Based on data from the World Bank, *World Development Indicators*, Washington, DC: World Bank (2017), [www.worldbank.org](http://www.worldbank.org); World Trade Organization, *Statistics Database*, Geneva: World Trade Organization (2017), [www.wto.org](http://www.wto.org); UNCTAD, "International Trade in Goods and Services," *UNCTADSTAT* (2017), [www.unctad.org](http://www.unctad.org).

A recent development in the services sector is the rise of the *sharing economy*, in which firms and individuals undertake online peer-to-peer exchange of all types of goods and services. Uber and Airbnb are examples of a growing number of global firms that allow people to borrow or rent assets from others. Uber lets people bypass taxis to go places, and Airbnb allows them to book rooms in private homes around the world. Uber is based in San Francisco and operates in more than 600 cities worldwide. The firm has faced controversy in various nations, as municipal authorities deal with legal issues related to driver qualifications, licensing, and fares. In Australia, people use Freelancer to hire needed workers. Streetbank is a UK-based firm that helps neighbors share tools, appliances, and other household items and has expanded to Australia, Canada, and numerous other countries.<sup>6</sup>

Exhibit 1.7 illustrates the diversity of service industries that are internationalizing, extending their reach beyond the countries where they are based. If you are considering a career in international business, keep these industries in mind.

### The International Financial Services Sector

International banking and financial services are among the most internationally active service industries. Explosive growth of investment and financial flows since about 2000 has led to the emergence of capital markets worldwide. It resulted from two main factors: the internationalization of banks and the massive flow of money across national borders into pension funds and portfolio investments

In the developing economies, meanwhile, banks and other financial institutions have fostered economic activity by increasing the availability of local investment capital, which stimulates the development of financial markets and encourages locals to save money.

International banking is primarily conducted by very large banks. Governments around the world have imposed many new regulations in the banking industry following the global financial crisis that arose in 2007–2008. Consumers and local businesses generally prefer to deal with local banks, obtaining financial services from homegrown “brick-and-mortar” branches and personnel who understand local conditions. Smaller, local banks usually work with larger, international banks to process cross-national payments, exchange currencies, and fulfill other international functions. Banks in Asia and North America have seen the most growth in recent years in their home markets. China is now home to three of the world’s five largest banks, specifically ICBC, China Construction Bank, and the Agricultural Bank of China. London long has been the banking hub of Europe, a status bolstered by the United Kingdom’s membership in the European Union (EU). However, the 2016 vote to exit the EU may reduce London’s competitive advantages in banking and may result in a growing role for Dublin, Frankfurt, and Paris as leading European banking centers.<sup>7</sup>

**EXHIBIT 1.7****Service Sector Industries That Are Rapidly Internationalizing**

Source: Based on International Trade Administration, *Service Industries* (Washington, DC: U.S. Department of Commerce, 2018).

<i>Industry</i>	<i>Representative Activities</i>	<i>Representative Companies</i>
<b>Architectural, construction, and engineering</b>	Construction, power utilities, design, engineering services, for airports, hospitals, dams	ABB, Bechtel Group, Kajima, Philip Holzman, Skanska AB
<b>Banking, finance, and insurance</b>	Banks, insurance, risk evaluation, management	Bank of America, CIGNA, Barclays, HSBC, Ernst & Young
<b>Education, training, and publishing</b>	Management training, technical training, language training	Berlitz, Kumon Math & Reading Centers, NOVA, Pearson, Elsevier
<b>Entertainment</b>	Movies, recorded music, Internet-based entertainment	Time Warner, Sony, Virgin, MGM
<b>Information services</b>	E-commerce, e-mail, funds transfer, data interchange, data processing, computer services	Infosys, Google, Hitachi, Qualcomm, Cisco
<b>Professional business services</b>	Accounting, advertising, legal, management consulting	Leo Burnett, EYLaw, McKinsey, A.T. Kearney, Booz Allen Hamilton
<b>Transportation</b>	Aviation, ocean shipping, railroads, trucking, airports	Maersk, Santa Fe, Port Authority of New Jersey, SNCF (French railroads)
<b>Travel and tourism</b>	Transportation, lodging, food and beverage, aircraft travel, ocean carriers, railways	Carlson Wagonlit, Marriott, British Airways

**1.2** Understand how international business differs from domestic business.

## How Does International Business Differ from Domestic Business?

Firms operate in countries characterized by distinctive economic, cultural, and political conditions. For example, the economic environment of Colombia differs sharply from that of Canada, the legal environment of Saudi Arabia does not resemble that of Japan, and the cultural environment of China is very distinct from that of Kenya. Not only does the firm find itself in unfamiliar surroundings, it encounters many *uncontrollable variables*—factors over which management has little control. These factors introduce new or elevated business risks. As exemplified by Instagram in the opening case, distinctive conditions in each country require firms to adapt their products and approaches from country to country.

### The Four Risks in Internationalization

Globalization is not without risks. When companies undertake international business, they are routinely exposed to four major types of risk, as illustrated in Exhibit 1.8. These are cross-cultural risk, country risk, currency risk, and commercial risk. The firm must manage these risks to avoid performance breakdowns, reputation loss, or other adverse consequences.

**Cross-cultural risk** occurs when a cultural misunderstanding puts some human value at stake. Cross-cultural risk arises from differences in language, lifestyles, mind-sets, customs, and religion. Values unique to a culture tend to be long-lasting and transmitted from one generation to the next. Values influence the mind-set and work style of employees and the shopping patterns of buyers. Foreign customer characteristics can differ significantly from those of buyers in the home market.

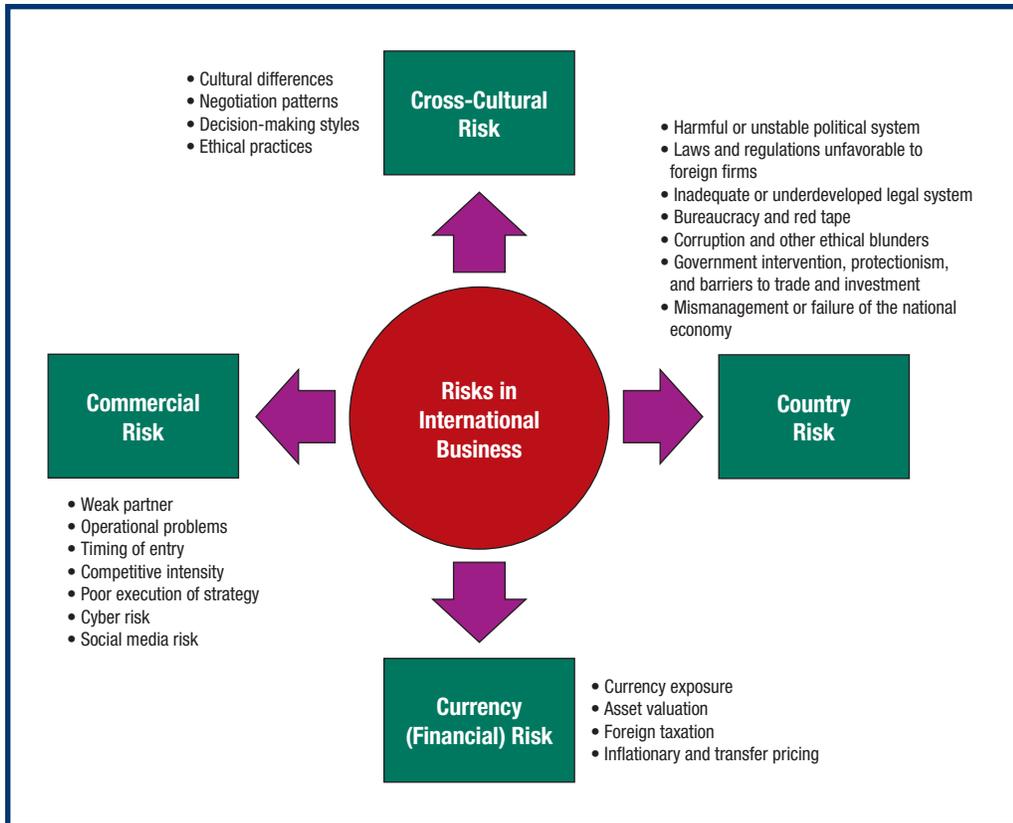
Language is a critical dimension of culture. In addition to facilitating communication, language is a window on people's value systems and living conditions. For example, Inuit (Eskimo) languages have various words for snow, whereas the South American Aztecs used the same basic word stem for snow, ice, and cold. When translating from one language to another, it is often

#### Cross-cultural risk

A situation or event in which a cultural misunderstanding puts some human value at stake.

## EXHIBIT 1.8

## The Four Risks of International Business



difficult to find words that convey the same meanings. For example, a one-word equivalent to *aftertaste* does not exist in many languages. Such challenges impede effective communication and cause misunderstandings. Miscommunication due to cultural differences gives rise to inappropriate business strategies and ineffective relations with customers. Cross-cultural risk most often occurs in encounters in foreign countries. However, the risk also can occur domestically, as when management meets with customers or business associates who visit company headquarters from abroad.

**Country risk** (also known as *political risk*) refers to the potentially adverse effects on company operations and profitability caused by developments in the political, legal, and economic environment in a foreign country. Country risk includes the possibility of foreign government intervention in firms' business activities. For example, governments may restrict access to markets, impose bureaucratic procedures on business transactions, and limit the amount of income that firms can take home from foreign operations. The degree of government intervention in commercial activities varies from country to country. Singapore and Ireland are characterized by substantial economic freedom—that is, a fairly liberal economic environment. By contrast, the Chinese and Russian governments regularly intervene in business affairs.<sup>8</sup> Country risk also includes laws and regulations that potentially hinder company operations and performance. Critical legal dimensions include intellectual property protection, product liability, and taxation policies. Nations also experience potentially harmful economic conditions, often due to high inflation, national debt, and unbalanced international trade.

**Currency risk** (also known as *financial risk*) refers to the risk of adverse fluctuations in exchange rates. Fluctuation is common for *exchange rates*—the value of one currency in terms of another. Currency risk arises because international transactions are often conducted in more than one national currency. For example, when U.S. fruit processor Graceland Fruit Inc. exports dried cherries to Japan, it is normally paid in Japanese yen.

When currencies fluctuate significantly, the value of the firm's earnings can be reduced. The cost of importing parts or components used in manufacturing finished products can

**Country risk**

Potentially adverse effects on company operations and profitability caused by developments in the political, legal, and economic environment in a foreign country.

**Currency risk**

Risk of adverse fluctuations in exchange rates.

increase dramatically if the value of the currency in which the imports are denominated rises sharply. Inflation and other harmful economic conditions experienced in one country may have immediate consequences for exchange rates due to the interconnectedness of national economies.

Rising value of the U.S. dollar during 2015 and 2016 relative to most currencies has cut into revenues of U.S. multinational firms such as Apple, Caterpillar, and Pfizer. Procter and Gamble's Duracell battery business experienced a 31 percent decline in profits due to weaker currencies in its foreign markets.<sup>9</sup>

### Commercial risk

Firms' potential loss or failure from poorly conceived or executed business strategies, tactics, or procedures.

**Commercial risk** is encountered by all firms, whether operating domestically or internationally. It refers to the firm's potential loss or failure from poorly conceived or executed business strategies, tactics, or procedures. Managers may make poor choices in such areas as the selection of business partners, timing of market entry, pricing, creation of product features, and promotional themes. Although such failures also exist in domestic business, the consequences are usually costlier when committed abroad. For example, in domestic business, a company might terminate a poorly performing distributor simply with advance notice. In foreign markets, however, terminating business partners can be costly due to regulations that protect local firms. Marketing inferior or harmful products, falling short of customer expectations, or failing to provide adequate customer service can also damage the firm's reputation and profitability. Furthermore, commercial risk is often affected by currency risk because fluctuating exchange rates can affect various types of business deals.

In recent years, two types of commercial risk have become an important source of concern for firms—cyber risk and social media risk. Both are the result of vulnerabilities in affected organizations. *Cyber risk* results from attacks on, or breaches of, the firm's information systems. Cyber risk arises from failures in the firm's information technology systems. Recent data breaches have afflicted such companies as eBay, Uber, Tesco Bank, and Sony Playstation Network. Even government organizations are vulnerable to data breaches.<sup>10</sup>

*Social media risk* refers to rapid and widespread circulation of unfavorable "buzz" about the firm. Such negative news is accelerated and amplified by social media. In 2015, for example, regulators announced that Volkswagen had installed software in its vehicles aimed at evading environmental regulations intended to reduce engine pollutants. When the scandal went viral on Twitter, Facebook, and other sites, Volkswagen's brand image was damaged. By late 2015, Volkswagen's buzz score had descended to its lowest point in several years. A single negative post about corporate events can travel globally at lightning speed and damage stakeholder trust in the firm's brand even before management has time to react.<sup>11</sup>

The four types of international business risks are omnipresent; the firm may encounter them around every corner. Some international risks, such as global financial disruptions, are extremely challenging. In Greece, the nation's debt crisis has lingered for several years and affects not only the European Union but creditors elsewhere.<sup>12</sup>

Although risk cannot be avoided, it can be anticipated and managed. Experienced international firms constantly assess their environments and conduct research to anticipate potential risks, understand their implications, and take proactive action to reduce their effects. This book is dedicated to providing you, the future manager, with a solid understanding of these risks as well as managerial skills and strategies to counter them effectively.

**1.3** Identify major participants in international business.

### Focal firm

The initiator of an international business transaction, which conceives, designs, and produces offerings intended for consumption by customers worldwide. Focal firms are primarily MNEs and SMEs.

## Who Participates in International Business?

International business requires numerous organizations, with varying motives, to work together as a coordinated team, contributing different types of expertise and inputs. There are four major categories of participants.

- A **focal firm** is the initiator of an international business transaction; it conceives, designs, and produces offerings intended for consumption by customers worldwide. Focal firms take center stage in international business. They are primarily large multinational enterprises (MNEs; also known as multinational corporations, or MNCs) and small and medium-sized enterprises (SMEs). Some are privately owned companies; others are public, stock-held firms; and still others are state enterprises owned by governments. Some focal firms are manufacturing businesses; others are in the service sector.

- A **distribution channel intermediary** is a specialist firm that provides various logistics and marketing services for focal firms as part of international supply chains, both in the focal firm's home country and abroad. Typical intermediaries include independent distributors and sales representatives, usually located in foreign markets where they provide distribution and marketing services to focal firms on a contractual basis.
- A **facilitator** is a firm or an individual with special expertise in banking, legal advice, customs clearance, or related support services that helps focal firms perform international business transactions. Facilitators include logistics service providers, freight forwarders, banks, and other support firms that assist focal firms in performing specific functions. A **freight forwarder** is a specialized logistics service provider that arranges international shipping on behalf of exporting firms, much like a travel agent for cargo. Facilitators are found in both the home country and abroad.
- *Governments*, or the public sector, are also active in international business as suppliers, buyers, and regulators. **State-owned enterprises (SOEs)** account for a substantial portion of economic value added in many countries, even rapidly liberalizing emerging markets such as Russia, China, and Brazil. Governments in advanced economies such as France, Australia, and Sweden have significant ownership of companies in telecommunications, banking, and natural resources. The recent global financial crisis led governments to step up their involvement in business, especially as regulators.

The activities of firms, intermediaries, and facilitators in international business overlap to some degree. The focal firm performs certain activities internally and delegates other functions to intermediaries and facilitators when their special expertise is needed. In other words, the focal firm becomes a client of intermediaries and facilitators who provide services on a contractual basis.

Whereas focal firms, intermediaries, and facilitators represent the supply side of international business transactions, customers or buyers make up the demand side. Customers consist of:

- *Individual consumers and households.*
- *Retailers*—businesses that purchase finished goods for the purpose of resale.
- *Organizational buyers*—businesses, institutions, and governments that purchase goods and services as inputs to a production process or as supplies needed to run a business or organization. Governments and nonprofit organizations such as CARE ([www.care.org](http://www.care.org)) and UNICEF ([www.unicef.org](http://www.unicef.org)) also often constitute important customers around the world.

## Focal Firms in International Business

Imagine a typical theatrical production. It has script writers, stage managers, lighting technicians, musicians, set directors, business managers, and publicity staff in addition to performing actors. Each participant contributes in different ways, and much coordination is required among them. Advanced planning, preparation, timeliness, and synchronization are critical to ultimate success. In the same way, international business transactions require the participation of many specialist organizations, exact timing, and precision.

Focal firms are the most prominent international players. They include well-known multinational enterprises and small and medium-sized exporting firms as well as contemporary organizations such as the born global firms. Let's learn more about each of these key actors in international business.

A **multinational enterprise (MNE)** is a large company with substantial resources that performs various business activities through a network of subsidiaries and affiliates located in multiple countries. Leading MNEs are listed in the *Fortune Global 500* (<http://fortune.com>). Examples include well-known companies such as Nestlé, Sony, Citibank, Unilever, Nokia, Ford, Barclays, DHL, Four Seasons Hotels, and Shell Oil. In recent years, the largest MNEs have been firms in the oil industry (such as Exxon-Mobil and Royal Dutch Shell) and the automotive industry (General Motors and Honda) as well as in retailing (Walmart).<sup>13</sup>

Although MNEs employ a range of foreign market entry strategies, they are best known for their foreign direct investment (FDI) activities. They operate in multiple countries, especially in Asia, Europe, and North America, by setting up production plants, marketing subsidiaries, and regional headquarters. MNEs such as Exxon, Honda, and Coca-Cola derive much of their total

### Distribution channel intermediary

A specialist firm that provides various logistics and marketing services for focal firms as part of international supply chains, both in the home country and abroad.

### Facilitator

A firm or an individual with special expertise in banking, legal advice, customs clearance, or related support services that assists focal firms in the performance of international business transactions.

### Freight forwarder

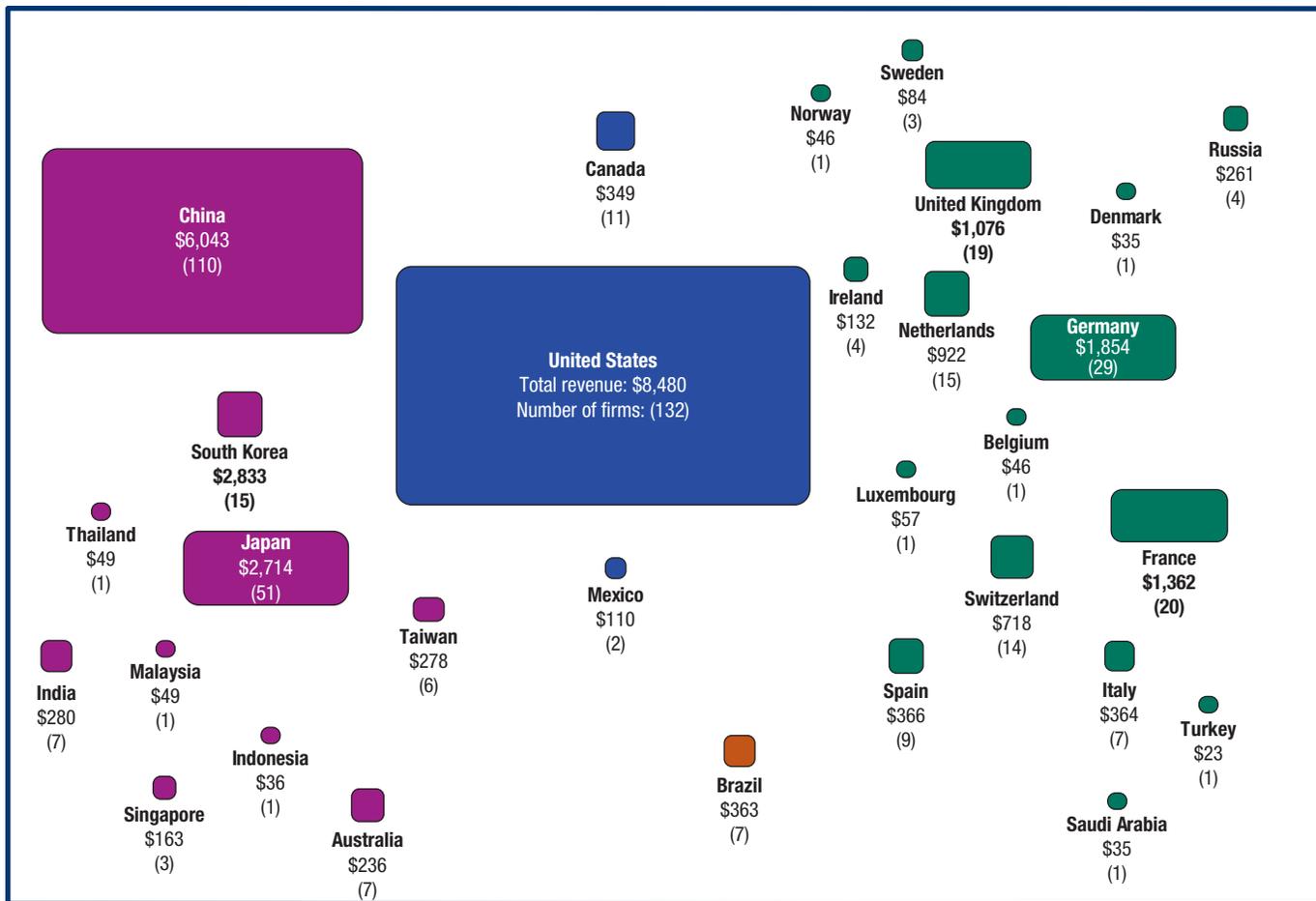
A specialized logistics service provider that arranges international shipping on behalf of exporting firms.

### State-owned enterprise (SOE)

A company that is founded and owned by a government in order to undertake commercial activities on the government's behalf.

### Multinational enterprise (MNE)

A large company with substantial resources that performs various business activities through a network of subsidiaries and affiliates located in multiple countries.



### EXHIBIT 1.9

#### Geographic Distribution of the Headquarters of the World's 500 Largest MNEs

Sources: Scott Decarlo, "Global 500," *Fortune* (2017), <http://fortune.com>, pp. 18–19; *Fortune*, "Global 500," Special Section, July 21, 2014, pp. F1–F8. Note: The exhibit shows country name, total revenues of Global 500 firms in U.S. dollars, and total number of Global 500 firms.

sales and profits, often more than half, from cross-border operations. Although there were fewer than 7,500 MNEs worldwide in 1970, today there are at least 75,000, a tenfold increase.<sup>14</sup>

Exhibit 1.9 displays the geographic distribution of the world's largest MNEs, drawn from *Fortune's* Global 500 list. These firms are concentrated in the advanced economies. The United States was home to 132 of the top 500 MNEs in 2017, a number that has declined over time as firms from other countries increase in size. China has the second most MNEs (110 firms), and Europe is home to many top MNEs: Germany (29 firms), France (20 firms), and the United Kingdom (19 firms).<sup>15</sup>

In recent years, large MNEs have begun to appear in emerging market countries, such as China, Mexico, and Russia. China currently hosts 110 of the top 500 MNEs, a number that has increased from only 20 countries in the past decade. Nearly all of China's top firms are state enterprises—wholly or partly owned by the Chinese government—which provides them substantial advantages.<sup>16</sup>

The new global challenge firms from emerging markets are fast becoming key contenders in world markets. For example, the Mexican firm Cemex is one of the world's largest cement producers; in Russia, Lukoil has big ambitions in the global energy sector; and China Mobile dominates the cell phone industry in Asia. These companies make best use of home-country natural resources and low-cost labor to succeed in world markets. Thousands of firms from emerging markets have big global dreams and pose competitive challenges to companies from the advanced economies.<sup>17</sup>

#### Small and medium-sized enterprise (SME)

A company with 500 or fewer employees (as defined in Canada and the United States).

#### Small and Medium-Sized Enterprises

Another type of focal firm that initiates cross-border business transactions is the SME. As defined in Canada and the United States, **small and medium-sized enterprises (SMEs)** are manufacturers or service providers with fewer than 500 employees. (In the European Union and

numerous other countries, they are defined as having fewer than 250 employees.) SMEs now make up the majority of companies active in international business. Nearly all firms, including large MNEs, started out small. Compared to large multinationals, SMEs can be more flexible and quicker to respond to global business opportunities. They are usually less bureaucratic, more adaptable, and more entrepreneurial and often sustain entrepreneurship and innovation in national economies.

Being smaller organizations, SMEs are constrained by limited financial and human resources. This explains why they usually choose exporting as their main strategy for entering foreign markets. Their limited resources prevent them from undertaking FDI, an expensive entry mode. As their operations grow, some gradually establish company-owned sales offices or subsidiaries in key target markets.

Due to their smaller size, SMEs often target specialized products to market niches too small to interest large MNEs. SMEs owe much of their international success to support provided by intermediaries and facilitators in foreign markets and to globe-spanning logistics specialists such as FedEx and DHL. Smaller firms also rely on information and communications technologies that allow them to identify global market niches and efficiently serve specialized buyer needs. SMEs are gaining equal footing with large multinationals in marketing sophisticated products around the world.

### Born Global Firms

One type of contemporary international SME is the **born global firm**, a young entrepreneurial company that initiates international business activity very early in its evolution, moving rapidly into foreign markets. Despite the scarce resources typical of most small businesses, born globals usually internationalize within three years of their founding and may export to 20 or more countries, generating more than 25 percent of their sales from abroad.

One example is Logitech ([www.logitech.com](http://www.logitech.com)), a born global firm based in Switzerland specializing in accessories for mobile phones and personal computers. The firm is well known as a worldwide leader in mice and keyboards. Within a few years of founding, Logitech expanded its sales to countries around Asia, Europe, and North America. Today Logitech has more than 7,000 employees in some 30 countries.<sup>18</sup>

The born global phenomenon represents a new reality in international business. In countries like Australia, Denmark, Ireland, and the United States, born globals account for a substantial proportion of national exports. They use the Internet and communications technologies to facilitate early and efficient international operations. In many cases, born globals offer leading-edge products with strong potential to generate international sales.

The emergence of born globals is associated with *international entrepreneurship*, in which innovative, smaller firms pursue business opportunities everywhere, regardless of national borders. Communications and transportation technologies, falling trade barriers, and the emergence of niche markets worldwide have increased the ability of contemporary firms to view the whole world as their marketplace. Entrepreneurial managers are creative, proactive, and comfortable dealing with risk. They are usually quick to adapt company strategies as circumstances evolve. The widespread emergence of born globals implies that any firm, regardless of size or experience, can succeed in international business.<sup>19</sup>

### Governments and Nongovernmental Organizations

In addition to profit-seeking focal firms, governments are central participants in international trade and investment. Their role is so important that we

#### Born global firm

A young entrepreneurial company that initiates international business activity early in its evolution, moving rapidly into foreign markets.



Source: Iakov Filimonov/123rf

Born global firms are international from their founding. Vix Technology is an Australian born global that makes fare management equipment for public transit systems worldwide.



Source: Oksana Kuzmina/123rf

The British Wellcome Trust funds nongovernmental organizations (NGOs) and research initiatives to work in collaboration with private businesses to develop remedies for diseases in Africa and other less developed areas.

devote later chapters to government intervention, political systems, and other government-related topics. In addition, numerous *nonprofit organizations* conduct cross-border activities, including charitable groups and *nongovernmental organizations (NGOs)*. They work on behalf of special causes, such as education, research, health care, human development, and the natural environment, operating internationally either to conduct their activities or to raise funds. Examples of nonprofit organizations include the Bill and Melinda Gates Foundation and the British Wellcome Trust, both of which support health and educational initiatives. CARE is an international nonprofit organization dedicated to reducing poverty. Many MNEs operate charitable foundations that support various initiatives. GlaxoSmithKline (GSK), the giant pharmaceutical firm, operates several small, country-based foundations in Canada, France, Italy, Romania, Spain, and the United States.

#### 1.4 Describe why firms internationalize.

### Why Do Firms Internationalize?

There are multiple motives for international expansion, some strategic in nature, others reactive. An example of a strategic, or proactive, motive is to tap foreign market opportunities or to acquire new knowledge. An example of a reactive motive is the need to serve a key customer that has expanded abroad. Specific motivations include the following:

- *Seek opportunities for growth through market diversification.* Substantial market potential exists abroad. Many firms—for example, Facebook, Gillette, Siemens, Sony, and Biogen—derive more than half of their sales from international markets.<sup>20</sup> In addition to offering sales opportunities that often cannot be matched at home, foreign markets can extend the marketable life of products or services that have reached maturity in the home market. One example is the internationalization of automatic teller machines (ATMs). The first ATMs were installed in London by Barclays Bank. The machines were adopted next in the United States and Japan. As growth of ATMs began to slow in these countries, they were marketed throughout the rest of the world. There were more than 3 million ATMs worldwide in 2017; a new one is installed somewhere every few minutes.
- *Earn higher margins and profits.* For many types of products and services, market growth in mature economies is sluggish or flat. Competition is often intense, forcing firms to get by on slim profit margins. By contrast, most foreign markets may be underserved (typical of high-growth emerging markets) or not served at all (typical of developing economies). Less intense competition, combined with strong market demand, implies that companies can command higher margins for their offerings. For example, compared to their home markets, bathroom fixture manufacturers American Standard and Toto (of Japan) have found more favorable competitive environments in rapidly industrializing countries such as Indonesia, Mexico, and Vietnam. Just imagine the demand for bathroom fixtures in the thousands of office buildings and residential complexes going up from Taiwan to Turkey!
- *Gain new ideas about products, services, and business methods.* International markets are characterized by tough competitors and demanding customers with various needs. Unique foreign environments expose firms to new ideas for products, processes, and business methods. The experience of doing business abroad helps firms acquire new knowledge for improving organizational effectiveness and efficiency. For example, Japan's Toyota refined just-in-time inventory techniques, which other manufacturers and foreign suppliers around the world then applied to manufacturing in their own countries.

- *Serve key customers better that have relocated abroad.* In a global economy, many firms internationalize to better serve clients that have moved into foreign markets. For example, when Nissan opened its first factory in the United Kingdom, many Japanese auto parts suppliers followed, establishing their own operations there.
- *Be closer to supply sources, benefit from global sourcing advantages, or gain flexibility in product sourcing.* Companies in extractive industries such as petroleum, mining, and forestry establish international operations where raw materials are located. One example is the aluminum producer Alcoa, which established operations in Brazil, Guinea, Jamaica, and elsewhere to extract aluminum's base mineral bauxite from local mines. Some firms internationalize to gain flexibility from a greater variety of supply bases. Dell Computer has assembly facilities in Asia, Europe, and the Americas that allow management to shift production quickly from one region to another. This flexibility provides Dell with competitive advantages over less agile rivals—a distinctive capability that allows Dell to outperform competitors and skillfully manage fluctuations in currency exchange rates.
- *Gain access to lower-cost or better-value factors of production.* Internationalization enables the firm to access capital, technology, managerial talent, and labor at lower costs, higher quality, or better value. For example, some Taiwanese computer manufacturers established subsidiaries in the United States to access low-cost capital. The United States is home to numerous capital sources in the high-tech sector, such as stock exchanges and venture capitalists, which have attracted many firms from abroad seeking funds. More commonly, firms venture abroad in search of skilled or low-cost labor. For example, the Japanese firm Canon relocated much of its production to China to profit from that country's inexpensive and productive workforce.
- *Develop economies of scale in sourcing, production, marketing, and R&D.* Economies of scale reduce the per-unit cost of manufacturing by operating at high volume. For example, the per-unit cost of manufacturing 100,000 cameras is much cheaper than the per-unit cost of making just 100 cameras. By expanding internationally, the firm greatly increases the size of its customer base, thereby increasing the volume of goods it produces. On a per-unit-of-output basis, the greater the volume of production, the lower the total cost. Economies of scale are also present in R&D, sourcing, marketing, distribution, and after-sales service.
- *Confront international competitors more effectively or thwart the growth of competition in the home market.* International competition is substantial and increasing, with multinational competitors invading markets worldwide. The firm can enhance its competitive positioning by confronting competitors in international markets or preemptively entering a competitor's home market to destabilize and curb its growth. One example is Caterpillar's entry in Japan to confront its main rival in the earthmoving equipment industry, Komatsu. Caterpillar's preemptive move hindered Komatsu's international expansion for at least a decade. Had it not acted proactively to stifle Komatsu's growth in Japan, Komatsu's home market, Caterpillar would certainly have had to face a more potent rival sooner.
- *Invest in a potentially rewarding relationship with a foreign partner.* Firms often have long-term strategic reasons for venturing abroad. Joint ventures or project-based alliances with key foreign players can lead to the development of new products, early positioning in future key markets, or other long-term, profit-making opportunities. For example, Black and Decker entered a joint venture with Bajaj, an Indian



Source: Coleman Yuen/Pearson Education Asia Ltd.

A vibrant workforce is driving economic development and buying power in emerging markets. Here consumers flock to a popular shopping street in Beijing, China.

retailer, to position itself for expected long-term sales in the huge Indian market. The French computer firm Groupe Bull partnered with Toshiba in Japan to gain insights for developing the next generation of information technology.

At the broadest level, companies internationalize to enhance competitive advantage and find growth and profit opportunities. Throughout this book, we explore the environment within which firms seek these opportunities, and we discuss the strategies and managerial skills necessary for achieving international business success.

### MyLab Management Watch It!

If your professor has assigned this, go to the Assignments section of [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) to complete the video exercise titled MINI Globalization.

**1.5** Appreciate why you should study international business.

## Why Study International Business?

There are many reasons to study international business. We examine them from the perspectives of the global economy, the national economy, the firm, and you as a future manager.

### Facilitator of the Global Economy and Interconnectedness

International business is transforming the world as never before. In the past 50 years, international trade and investment have experienced unprecedented growth. Since the 1980s, *emerging markets* have provided new impetus to worldwide economic interconnectedness. These fast-growth developing economies—some 30 countries, including Brazil, Russia, India, and China, the so-called BRICs—are experiencing substantial market liberalization, privatization, and industrialization, which are fueling global economic transformation.

### Contributor to National Economic Well-Being

International business contributes to economic prosperity, helps countries use their resources more efficiently, and provides interconnectedness to the world economy and access to a range of products and services. Consequently, governments have become more willing to open their borders to foreign trade and investment.

International trade is a critical engine for job creation. It is estimated that every \$1 billion increase in exports creates more than 20,000 new jobs. In the United States, cross-border trade directly supports at least 11 million jobs. One of every seven dollars of U.S. sales is made abroad. One of every three U.S. farm acres and one of every six U.S. jobs is producing for export markets. On average, exporting firms create jobs faster and provide better pay than nonexporting firms.<sup>21</sup>



Source: satina/123rf

International trade is encouraging faster diffusion of consumer products and brands around the world.

### A Competitive Advantage for the Firm

To sustain a competitive advantage in the global economy, firms must readily participate in cross-border business and acquire the necessary skills, knowledge, and competence. Procter & Gamble sells shampoo, disposable diapers, and other consumer products in more than 150 countries. MTV broadcasts its programming in some 140 countries. Nestlé sells its food and beverage products worldwide, obtaining nearly all its revenue from foreign operations. As these examples imply, going international offers countless opportunities for firms to grow and earn additional profits.



### MARY LYLES

**Mary's Degrees:** Bachelor's degree in Spanish, master's in international business

**Internships during college:** World Trade Center of Atlanta; purchasing intern, Diaz Foods

**Jobs held since graduating:**

- Buyer and private label project manager, Diaz Foods, Atlanta, USA
- Sourcing analyst, Starbucks, Rancho Cucamonga, California, USA
- Senior sourcing analyst, Starbucks, Seattle, USA

When she first enrolled in college, Mary considered becoming a dentist. But after pondering the long list of science courses required in dentistry, Mary had a change of heart. Her natural enthusiasm for learning about cultures, languages, and religions pushed her toward a career in international business. Mary majored in Spanish. A study abroad program in Granada, Spain, inspired her to pursue a master's degree in international business.

In graduate school, Mary sought the guidance of advisors and mentors. She undertook two internships: one at the World Trade Center in Atlanta and another at Diaz Foods, a Hispanic food distributor in Atlanta. At Diaz Foods, Mary developed a passion for sourcing and supply chain management. Upon graduation, the firm hired Mary to develop the food brand D'Sabor. Mary worked diligently to locate and source manufacturers worldwide. Around this time, Diaz Foods acquired La Cena Fine Foods, a distributor of Hispanic foods. Mary was part of the acquisition team tasked with ensuring synergy with the acquired firm. After two years at Diaz Foods, Mary was feeling adventurous and sought a change of scene.

She next took a position with the Starbucks Coffee Company at its Evolution Fresh juice plant in California. There, she worked as a sourcing analyst for fresh produce, puree, and other juice ingredients. She managed order placement and production of domestic and international crops

such as pineapple and coconut. She traveled regularly to production sites in Mexico and the United States for sourcing and to conduct safety and quality audits.

Within two years, Mary was promoted to senior sourcing analyst on the food ingredient sourcing team and moved to Starbucks headquarters in Seattle. There she manages bread, condiment, and sauce commodities for prepared foods. In this role, Mary supports new food innovation, product launches, category strategy, and supplier relationships. For her next career goal, Mary aims to support Starbucks' international expansion efforts.

### Mary's Advice for an International Career

"Develop a global mind-set. Globalization has changed the way business is done, and more than ever, firms need talent with a global mind-set. Realize that your dreams will not happen overnight. If you keep your mind focused on the end goal, you will get there! Cultivating relationships with a diverse group of associates and friends will expose you to different cultures, increasing your knowledge of the global community."

### Success Factors

Mary says networking and diversity have been key success factors in her career so far. "Network! I cannot overstate the

importance of it. Without networking, I would not be where I am today. You never know who will help you meet your goals or get you the next job. Be sure to maintain relationships along the way, and do not reach out only when you need something. Good managers and true leaders will always want to help you achieve success and exceed your goals. Set clear goals from the onset, and communicate with your boss openly and objectively about any issues that may arise." Mary surrounds herself with a diverse group of individuals in her professional and personal life. She believes diversity is critical for generating new ideas and producing extraordinary outcomes.

### Challenges

"Dealing with cultural differences can be tricky! When working on a project in another country, you have to adapt the product, but you also need to keep it true to the brand."

Mary aspires to leverage the knowledge gained at Starbucks to pursue an international assignment to support Starbucks's food platform in one of the firm's international locations. Mary's passion for international business is paying off.

*Source:* Courtesy of Mary Lyles

## A Competitive Advantage for You

Although most international careers are based in one's home country, managers travel the world and meet people from various cultures and backgrounds. Traveling abroad leads to exciting challenges and learning experiences. Managers rising to the top of most of the world's leading corporations honed their managerial skills in international business.

The *CKR CAREER PREPARATION KIT* has been specifically designed to integrate and advance your learning of “CKR Intangible Soft Skills” and “CKR Tangible Process Tools” to improve your employability and success in the workplace.

In this text, you will read about recent graduates who describe how they have applied CKR Intangible Soft Skills and CKR Tangible Process Tools in their career development in a special feature called *You Can Do It: Recent Grad in IB*. Read about Mary Lyles, a recent graduate who is enjoying her early experiences in international business.

### **An Opportunity to Support Ethics, Sustainability and Corporate Citizenship**

As the world’s population grows, so do pressures to meet consumer demand in an ethical and sustainable way. Increasingly, companies operate in environments characterized by limited resources, vulnerable human conditions, and stakeholder consciousness on issues that affect all society. In response to this trend, companies are expanding their awareness about the social and environmental implications of their actions. Rather than being caught off guard, firms increasingly develop ethical, sustainable, and socially responsible policies and practices. For example, Starbucks began selling coffee only from growers certified by the Rain Forest Alliance ([www.rainforest-alliance.org](http://www.rainforest-alliance.org)), a nonprofit organization that promotes the interests of coffee growers and the environment. Such multinational enterprises as Philips, Unilever, and Walmart follow business practices that promote sustainable development. McDonald’s buys beef from farmers who meet special standards on animal welfare and environmental practices. Its outlets in Austria, Germany, Sweden, and the United Kingdom sell only organic milk.<sup>22</sup> Internationally active firms must embed corporate citizenship in their strategic decisions as well as their ongoing processes and practices. Ethics and responsible behavior in firms’ international activities are of such importance that we devote Chapter 4 to this topic.

**1.6** Learn the CKR Intangible Soft Skills™ and the CKR Tangible Process Tools™ to improve your employability and success in the workplace.

### **CKR Career Preparation Kit: Tangible Process Tools and Travel Abroad Preparation Checklist**

Traveling internationally requires thorough, early preparation and entails numerous requirements not needed for domestic travel.

Documents required for international travel include a passport, a traveler’s visa issued by the embassy of some host countries, proof of return trip, and hotel reservations. Requirements of customs authorities vary by country.

It is vital to understand and comply with security, safety, and health care requirements for the specific countries that you visit.

Electricity standards vary around the world. Investigate and obtain appropriate plug adapters and converters prior to travel. Mobile telephone standards often vary, and international calling costs can be substantial. Check with your service provider to identify and choose the best phone plan to minimize calling costs abroad.

Most countries use different currencies. Learn about currency exchange rates and the feasibility of using credit and debit cards prior to travel. You may wish to obtain the appropriate foreign currency(s) prior to departure. Banks and credit card companies usually require their customers to notify them in advance of anticipated card usage abroad.

It is wise to familiarize yourself with laws in the destination country(s) and comply with them. If you plan to drive a car overseas, it is usually best to obtain an International Driving Permit (IDP) prior to departure. Cultural awareness is critical and is addressed in Chapter 3 of this textbook.

Please consult the Pearson MyLab Management at: [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) for a link to the “CKR: TRAVEL ABROAD PREPARATION CHECKLIST” ©, a comprehensive list of these details prior to traveling outside your home country.

## CLOSING CASE

### Internationalization at Harley-Davidson

Considered an American icon by many, Harley-Davidson (Harley) is a U.S. motorcycle manufacturer founded in 1903 and offers 32 models through a network of about 1,500 dealers. Its global motorcycle revenue was about \$6 billion in 2017, continuing a three-year downward trend. Total sales have been relatively flat since 2012, with U.S. sales declining and international sales rising. Harley earns about two-thirds of its total sales in the United States, where it also manufactures almost all its bikes to support its brand image and quality control. The firm is embarked on a course to build the next generation of Harley riders globally; international markets are crucial to the firm's survival and growth. The CEO recently announced a bold goal to grow international sales to 50 percent of annual volume by 2027.

Harley is the only U.S.-based global motorcycle manufacturer and makes four distinctive groups of models:

- *Standard*: Practical bikes used for low-cost commuting
- *Performance*: Sleek, sport-style racing bikes built for speed and easy handling
- *Custom*: Stylized bikes customized to customer tastes
- *Touring*: Long-distance, large-capacity, comfort bikes that typically include cruise control, stereos, and luggage racks

In the United States, Harley competes primarily in the custom and touring segments, which account for about 85 percent of heavy-weight sales. However, US sales have suffered recently, mainly because millennials and other potential buyers are relatively price-conscious. Its numerous competitors are all headquartered outside the United States and include Honda, Suzuki, Yamaha, and Kawasaki in Japan and BMW, Ducati, and Triumph in Europe. New competitors are emerging from China.

Harley heavyweight bikes sell for \$19,000 or more, which puts them beyond the reach of many buyers. The median age of a motorcycle owner is 47, up from 40 in 2009. One key to Harley's success is the Harley Owners Group (HOG), a club of loyal Harley owners with more than a million members, including 100,000 in Europe. HOG is an important marketing tool for promoting sales. In the United States, brand loyalty is fierce, and switching costs for Harley owners are high. Over time, the firm has created a mystique around its heavyweight bikes that helps drive sales. Indeed, many owners get Harley tattoos.

#### Threat of Foreign Competitors and Revival

Some years ago, Harley faced financial ruin. By the 1980s, Honda, Kawasaki, Suzuki, and Yamaha were selling millions of motorcycles in the United States by specializing in inexpensive, lightweight models. Initially, Harley paid little attention to the competition and continued to focus on heavyweight bikes, but the market for lightweights continued to grow. Meanwhile, Harley began to experience major problems with the quality of its bikes and poor productivity in its factories. Over time, the firm's image suffered and sales declined sharply; Harley nearly went bankrupt.

For its turnaround strategy, Harley adopted Japanese-style management techniques—updating manufacturing methods, improving quality, and expanding model offerings. In its factories, Harley instituted just-in-time inventory systems and total

quality management and empowered its production workers. Management increased marketing efforts, improved the dealer network, and undertook various cross-branding ventures. By the mid-1990s, management had repositioned Harley more strongly in the performance motorcycle market. The enhancements paid off in sharp improvements in company image and sales. However, the volume of Harley motorcycle shipments peaked in 2006. Shipments flattened or declined during the global financial crisis and ensuing recession and still had not recovered by 2018.

#### International Expansion

Harley management resolved that future success would come from expansion into foreign markets. The firm had established a distribution network and local subsidiary in Japan, and by 2016, it was selling more than 16,000 motorcycles annually. It continued to sell heavyweight motorcycles in Japan at a price of more than \$20,000, substantially more than Honda's standard lightweight model. Harley's foreign saw a sustained growth.

Harley also made inroads in Europe, a vast marketplace and home to dozens of countries with diverse needs and tastes. In Europe, performance bikes are the top seller by far, accounting for more than one-third of Harley sales, followed by touring, standard, and custom bikes. In the United States, customers strongly prefer custom and touring bikes, which account for about half and one-third of U.S. sales, respectively. Performance and standard models produce much smaller revenues in the United States. European tastes are distinctive, often differing by region. Some buyers prefer Italian styling, which is dominated by Ducati. Others prefer the German styling of BMW.

Compared to U.S. customers' tastes, European preferences are varied. Freeways in much of Europe have high speed limits that necessitate high-performance bikes. Most Europeans do not relate to Harley's U.S. image of rugged individualism, freedom, and rebellion. Harley's big bikes are difficult to maneuver in narrow streets and impractical for daily commuting. Fortunately, Harley sells a broad range of bikes that suit European tastes. To enhance its European presence, Harley launched an overseas branch of the HOG club. To further its presence in Europe, Harley also bought the Italian motorcycle firm MV Agusta Group for \$109 million in 2008, but economic conditions forced it to divest its interest in Agusta in 2010. The firm grew annual European sales at about 8 percent from 2013 to 2017. Major European economies returned to growth and Harley enjoyed good results in 2018.

Emerging markets such as Brazil, China, India, and Russia have large populations, a fast-growing middle class, and increased disposable incomes. By 2017, Harley had opened 15 new dealerships in South Korea, Thailand, and Russia, and the firm plans to expand its dealer network, with a focus on China, India, and Malaysia. India is home to millions of households with annual incomes over \$80,000. Honda, Yamaha, and Kawasaki all have a strong presence there. Despite trade and investment barriers including local emission regulations, Harley established a subsidiary near Delhi, but competition remains fierce. Presently, India accounts for only 2 percent of Harley's sales.

Tariffs on motorcycles are relatively high in the Asia-Pacific region. For example, China and Malaysia maintain a 30 percent tariff on motorcycles, while Thailand's tariff is 60 percent. In 2018, Harley developed a factory in Thailand to serve the Southeast Asia market and avoid Thailand's high tariff. China is home to 1.3 billion people and central to Harley's internationalization drive. But wages are low, and the majority of Chinese riders prefer small motorcycles and use them mainly for commuting. China is characterized by counterfeiting and other intellectual property violations. The government restricts motorcycles in some areas to reduce noise and drive-by thefts.

Harley's entry into the large Brazilian market was fraught with challenges. Initially, Brazil's government imposed high import tariffs that doubled the cost of bikes to Brazilian buyers. To address this dilemma, Harley established an assembly plant in Brazil, a step that avoids import barriers and reduces costs thanks to the availability of low-cost workers. Despite recent political and economic instability, Harley remains optimistic about Brazil, the largest market in Latin America. Harley opened a plant in Manaus and expanded its network to 12 dealerships. These efforts helped the firm capture a fifth of the motorcycle market. Harley aims to attract younger buyers, especially women who make up one-quarter of Brazil's motorcyclist market. The EMEA Region (Europe, Middle East, and Africa) was a bright spot in 2017 with increased sales and projected growth.

## Environmental Sustainability

Motorcycles pollute the natural environment, and Harley is vulnerable to regulation because it makes large bikes. Most of Harley's greenhouse gas (GHG) emissions emanate from its manufacturing plants, and management is moving to reduce pollution as well as energy and water usage. In 2016, Harley paid a \$12 million fine for sales of after-market devices that increase air pollution from motorcycles. Harley is developing an electric motorcycle and other environmentally friendly products. As regulations continue to evolve, the firm's sustainability initiatives appeal to governments in China, Europe, India, and elsewhere around the world.

## The Future

A sluggish global economy is threatening sales. Harley's share of the U.S. market for heavyweight motorcycles declined from 58 to 50 percent in the past three years. For management, a big question is how best to position the firm given declining demand in its home markets and challenges abroad. Management believes the keys to sustainable growth will be (1) a heightened focus on foreign markets, (2) an appeal to lighter-weight, performance-based markets, (3) improved and larger dealer networks, and (4) strategic control of distribution.

Management believes it must balance production and sales for domestic and foreign markets. To diversify its revenue streams and reduce its dependence on the U.S. market, Harley wants to increase international sales and needs to figure out a strategy to achieve this goal. Management sees emerging markets as key to future growth.

## AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Reflective Thinking, Analytical Thinking, Written and Oral Communication, Application of Knowledge and Ethical Understanding and Reasoning

### Case Questions

- 1-4. Describe the international business environments Harley faces. What types of risks does Harley face?
- 1-5. How does Harley benefit by expanding abroad? What types of advantages can the firm obtain? What advantages acquired abroad can help Harley improve its performance in its home market?
- 1-6. How can Harley effectively compete with rivals from Japan and Europe? What strategies should management apply to grow the firm's sales in those regions?
- 1-7. Competitors such as Lifan and Zongshen are beginning to emerge from China, where they enjoy competitive advantages such as low-cost labor and extensive experience with emerging markets. How can Harley compete against such firms? Should Harley more aggressively pursue emerging markets such as Brazil, China, and India? If so, what strategies will help them succeed in those markets?
- 1-8. Evaluate Harley's environmental sustainability initiatives in the evolving regulatory environment on global greenhouse gas. What advantages does Harley gain by attempting to produce environmentally safe and sustainable products?

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This case was prepared by Dr. Marta Szabo White and updated by Dr. Mourad Dakhli, both of Georgia State University.

# END-OF-CHAPTER REVIEW

## MyLab Management

Go to [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) to complete the problems marked with this icon .

## Key Terms

born global firm 17	focal firm 14	international trade 7
commercial risk 14	foreign direct investment (FDI) 7	internationalization 6
country risk 13	freight forwarder 15	multinational enterprise (MNE) 15
cross-cultural risk 12	globalization of markets 5	small and medium-sized enterprises (SMEs) 16
currency risk 13	importing or global sourcing 7	state-owned enterprise (SOE) 15
distribution channel intermediary 15	international business 4	
exporting 7	international investment 7	
facilitator 15	international portfolio investment 7	

## Summary

In this chapter, you learned about:

- **Key concepts in international business**

**International business** refers to the performance of trade and investment activities by firms across national borders. **Globalization of markets** is the ongoing economic integration and growing interdependency of countries worldwide. International business is characterized by international trade and investment. **International trade** refers to exchange of products and services across national borders, typically through exporting and importing. **Exporting** is the sale of products or services to customers located abroad from a base in the home country or a third country. **Importing** or **global sourcing** refers to procurement of products or services from foreign suppliers for consumption in the home country or a third country. **International investment** refers to international transfer or acquisition of ownership in assets. **International portfolio investment** is passive ownership of foreign securities such as stocks and bonds to generate financial returns. Using **foreign direct investment**, the firm establishes a physical presence abroad through acquisition of productive assets such as capital, technology, labor, land, plant, and equipment.

- **How international business differs from domestic business**

International firms are constantly exposed to four major categories of risk that must be managed. **Cross-cultural risk** refers to a situation or event when some human value has been put at stake due to a cultural misunderstanding. **Country risk** refers to the potentially adverse effects on compa-

ny operations and profitability caused by developments in the political, legal, and economic environment in a foreign country. **Currency risk** refers to the risk of adverse fluctuations in exchange rates. **Commercial risk** arises from the possibility of a firm's loss or failure from poorly developed or executed business strategies, tactics, or procedures. The risks are ever-present in international business, and firms take proactive steps to reduce their effects.

- **Who participates in international business**

A key participant in international business is the **multinational enterprise (MNE)**, a large company with many resources whose business activities are performed by a network of subsidiaries located in multiple countries. Also active in international business are **small and medium-sized enterprises (SMEs)**, companies with 500 or fewer employees. **Born global firms** are entrepreneurial firms that initiate international business from or near their founding. Nongovernmental organizations (NGOs) are nonprofit organizations that pursue special causes and serve as an advocate for the arts, education, politics, religion, and research.

- **Why firms internationalize**

Companies internationalize for various reasons. These include the ability to increase sales and profits, serve customers better, access lower-cost or superior production factors, optimize sourcing activities, develop economies of scale, confront competitors more effectively, develop rewarding relationships with foreign partners, and gain access to new ideas for creating or improving products and services.

- **Why you should study international business**

There are many reasons to study international business. It enhances a firm's competitive positioning in the global market, facilitates development of the global economy and of the interconnectedness among nations, and contributes to national economic well-being. From a career standpoint, learning about international business will provide you with a competitive edge and enhance your ability to thrive in the job market. Firms have various opportunities for ethical corporate citizenship abroad.

- **Learn the CKR Intangible Soft Skills™ and the CKR Tangible Process Tools™ to improve your employability and success in the workplace.**

International travel requires early preparation and entails specific requirements such as a passport and a visa for some countries. Understand the security, safety, and health care requirements of the destination country. Check local standards for electricity and mobile telephones. Learn about currencies, exchange rates, and usage of credit and debit cards. Familiarize yourself with local laws and comply with them.

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## Test Your Comprehension

### AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Written and Oral Communication, Analytical Thinking, Reflective Thinking, Diverse and Multicultural Work Environments

- 1-9. Distinguish between international business and globalization of markets.
- 1-10. What is the difference between exporting and foreign direct investment?
- 1-11. What makes international business different from domestic business?
- 1-12. What are the various types of risks that firms face when they conduct international business?
- 1-13. Who are the major participants in international business?
- 1-14. What is the difference between a multinational enterprise (MNE) and a small and medium-sized enterprise (SME)?
- 1-15. What are some of the key motivations for firms to engage in international business?
- 1-16. Why should you care about international business?

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## Apply Your Understanding

### AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Application of Knowledge, Written and Oral Communication, Analytical Thinking, Diverse and Multicultural Work Environments, Interpersonal Relations and Teamwork

- 1-17. Richard Bendix is the marketing manager at a firm that makes and sells high-quality prefabricated houses. He believes there is little difference between his home-country market and foreign markets and that he can use the same methods for selling in Asia or Latin America as he does in his home country. Write a memo in which you explain to Richard the differences between domestic and international business. Explain the risks and other differences that Richard's firm will likely encounter if it expands abroad.
- 1-18. Suppose that after graduation you get a job with Cottonwood Corporation, a small firm that does business only in its domestic market. You have just completed coursework in international business, are aware of various business opportunities abroad, and believe that Cottonwood should internationalize. Write a memo to your boss in which you explain why your company should pursue international business. What are the benefits to Cottonwood of venturing abroad? Explain why firms internationalize.
- 1-19. You have become the president of the International Business Club at your school. You are trying to recruit new members and find that many students do not recognize the importance of international business or the career opportunities available to them. You decide to give a presentation on this theme. Prepare an outline of a presentation in which you explain what types of companies participate in international business, why students should study international business, and what career opportunities they might find.



## INTERNET EXERCISES

Access globalEDGE™ at [www.globalEDGE.msu.edu](http://www.globalEDGE.msu.edu)

### AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Information Technology, Application of Knowledge, Diverse and Multicultural Work Environments, Written and Oral Communication, Analytical Thinking and Reflective Thinking

#### Knowledge Portal

globalEDGE™ is a leading knowledge portal for professionals in international business. It is a gateway to specialized knowledge on countries, international business transactions, culture, and firm practice. globalEDGE™ was developed at Michigan State University under the direction of Professor S. Tamer Cavusgil. Consult the globalEDGE™ portal to complete the Internet exercises at the end of each chapter.

1-20. You can gain valuable insights into international business by examining how countries compare to each other. Various research groups and international agencies systematically examine economic, political, and other features of nations. Visit globalEDGE™ Tools and Data, scroll down, and click Interactive Rankings. Select Countries. You will find dozens of criteria ranking countries based on GDP per capita; Education—literacy rate; People—population total; People—population density; Health—mortality rate; Energy—electricity production; Infrastructure—mobile cellular subscriptions; Infrastructure—roads, total network; Trade and Investment—foreign direct investment net inflows; and many other factors. Choose the ranking criteria that interest you most, and then examine the following three countries: Germany, India, and South Africa. Based on your analysis, explain why they rank where they do. Do

their relative positions make sense to you? Does each country seem like a good place to do business? Why or why not? **Hint:** Evaluate countries on a per-capita basis by dividing each criterion by the country's population.

- 1-21. In this chapter, we reviewed the four major risks that firms face in international business: cross-cultural risk, country risk, currency risk, and commercial risk. Identify one or more countries that interest you, and then visit globalEDGE™ and research the countries to uncover examples of each of the four types of risks. For example, China is characterized by various cultural differences and a national government that tends to intervene in business. Research by entering the country name in the search engine. Visit Global Insights and Market Potential Index. Illustrate each risk with examples.
- 1-22. You have recently been hired by a smaller firm that is beginning to expand internationally. When first starting out, most firms choose exporting as their main foreign market entry strategy. However, no one in your firm knows how to conduct exporting. Therefore, your boss has given you an assignment: Prepare a presentation for your coworkers on how to engage in exporting. Using globalEDGE™, find and review Guide to Exporting, which you can use to create your presentation.

### MyLab Management

Go to [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) for Auto-graded writing questions as well as the following Assisted-graded writing questions:

- ★ 1-23. What role do distribution channel intermediaries fulfill?
- ★ 1-24. What risks do companies typically engage in with international business?
- ★ 1-25. MyLab Management Only—comprehensive writing assignment for this chapter.

## Endnotes

1. We use the term *international business* to refer to the cross-border business activities of individual firms, whereas economists use *international trade* to refer to aggregate cross-border flows of products and services between nations. Although international business describes an enterprise-level phenomenon, international trade describes the macrophenomenon of aggregate flows between nations.
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# Chapter 2

## Globalization of Markets and the Internationalization of the Firm

**Learning Objectives** *After studying this chapter, you should be able to:*

- 2.1 Understand market globalization as an organizing framework.
- 2.2 Learn the driving forces of globalization.
- 2.3 Understand the impact of technological advances on globalization.
- 2.4 Learn the dimensions of globalization.
- 2.5 Understand firm-level consequences of market globalization.
- 2.6 Understand the societal consequences of globalization.

### Spotify and the Rise of Born Global Firms

**S**potify is a music and video streaming service founded in Sweden in 2008. The firm's emergence coincided with a global shift in the way people listen to music. From the beginning, Spotify's strategy was to enter many international markets quickly. A few months after its founding, Spotify was launched in Finland, France, Norway, and Spain. It then established operations in the United Kingdom and the United States. Today, Spotify has more than 150 million regular users throughout Europe, the Americas, and the Asia-Pacific region, more than 60 countries in all. The firm has offices in 14 countries, established through direct investment.

Spotify grew quickly by offering a huge selection of music at no cost. Personalized content, easy ways to discover new music, and customer-tailored marketing are

just some of the ways Spotify differentiated itself in a global music marketplace dominated by Apple. This start-up has leveraged partnerships with firms like Coca-Cola and Vodafone to broaden its customer appeal worldwide.

Spotify is one of a growing number of small and medium-sized enterprises (SMEs) active in international business. SMEs make up the majority of all firms. In contrast to large multinational enterprises (MNEs) that historically have dominated cross-border business, most SMEs have far fewer financial and human resources. International business was often beyond their reach. Globalization and recent technological advances now have made venturing abroad more feasible and much less expensive. This has created a commercial environment in which many more small firms can participate in international business.



Source: bowie15/123rf

Spotify is an example of “born global” firms, start-ups that enter numerous international markets within a few years of founding and build substantial global presence. Spotify exemplified agility and flexibility characteristic of young, smaller ventures, which helped the firm serve the global marketplace more effectively. Other born globals include Airbnb (lodging), Cochlear (medical devices), Mavi (clothing), HTC (smartphones), Skype (Internet-based communications), Uber (transportation), and many others.

Born global firms internationalize early for various reasons, some specializing in a product category for which demand is universal. Geo Search ([www.geosearch.co.jp](http://www.geosearch.co.jp)) is a Japanese born global that developed high-technology equipment to help engineers survey ground surfaces for cavities and build safe roads, airports, and underground utility lines. The firm developed a land-mine detector to find buried bombs and discovered a ready market in countries such as Afghanistan, Cambodia, and Libya.

Smaller companies such as Spotify and Geo Search demonstrate that even new ventures with limited experience and resources can participate actively in cross-border trade and investment. More companies undertake international business today than ever before.

**AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Analytical Thinking, Reflective Thinking**

### Questions

- 2-1.** What are the main characteristics of born global firms?
- 2-2.** What driving forces and causes of globalization have allowed born global firms such as Spotify to internationalize at or near their founding?
- 2-3.** What advantages do you think a young company can gain by entering international markets soon after its founding?

**SOURCES:** S. Tamer Cavusgil and Gary Knight, "The Born-Global Firm: An Entrepreneurial and Capabilities Perspective on Early and Rapid Internationalization," *Journal of International Business Studies*, 46, No. 1 (2015), pp. 3–16; Mindi Chahal, "Putting the Spotlight on Spotify," *Marketing Week*, April 7, 2016, pp. 26–27; Thomas Hobbs, "Spotify on Driving Personalised Ads, Dealing with Tidal and Its Plans for Global Domination," *Marketing Week*, April 20, 2015, www.marketingweek.com; Gary Knight and S. Tamer Cavusgil, "Innovation, Organizational Capabilities, and the Born-Global Firm," *Journal of International Business Studies* 35, No. 2 (2004), pp. 124–141; B. Oviatt and P. McDougall, "Toward a Theory of International New Ventures," *Journal of International Business Studies* 25, No. 1 (1994), pp. 45–64; Jonathan Ringen, "Listen Up!," *Fast Company*, September 2015, pp. 34–37; Spotify, company information, www.spotify.com, retrieved January 12, 2018.

### Globalization of markets

Ongoing economic integration and growing interdependency of national economies.

### Value chain

The sequence of value-adding activities the firm performs in the course of developing, producing, marketing, and servicing a product.

The opening case highlights important driving forces and causes of market globalization. These include worldwide reduction of barriers to trade and investment, market liberalization and adoption of free markets, and advances in technology.

**Globalization of markets** refers to the gradual integration and growing interdependence of national economies. Declining trade barriers and rapid changes in communications, manufacturing, and transportation technologies are enabling firms to internationalize much more rapidly and easily than ever before.

Globalization allows companies to outsource value-chain activities to the most favorable locations worldwide. A **value chain** is the sequence of value-adding activities the firm performs in the course of developing, producing, marketing, and servicing a product. Firms source raw materials, parts, components, and service inputs from suppliers around the globe. Globalization has also made it easier for companies to sell their offerings worldwide. These trends are transforming national economies. Growing world trade and foreign direct investment (FDI) provide buyers with a wider choice of products than ever before. Global competition and innovation frequently help to lower consumer prices. Firms with cross-border business create millions of jobs that raise living standards around the world.

Globalization is not new. In early history, civilizations in the Mediterranean, Middle East, Asia, Africa, and Europe all contributed to the growth of cross-border trade. Globalization evolved out of a common desire of civilizations to reach out and touch one another.<sup>1</sup> It is a culmination of people's recognition, thousands of years ago, of the wonders of difference and discovery. Cross-border trading opened the world to innovations and progress by giving societies the opportunity to expand and grow. Trade through the ages fostered civilization; without it, the world would consist of warring tribes bent on getting what they need through combat.<sup>2</sup>

## Phases of Globalization

We can identify five distinct phases in the evolution of globalization since the 1800s. As illustrated in Exhibit 2.1, each phase was accompanied by radical technological advances and internationalization trends.

- *The first phase of globalization* began in about 1830 and peaked around 1880.<sup>3</sup> It was associated with the use of water and steam power to mechanize production and power ships and trains. International business became widespread due to the growth of railroads, efficient ocean transport, and the rise of large manufacturing and trading firms. Invention of the telegraph and telephone in the late 1800s enabled information flows between and within nations and aided early efforts to manage companies' supply chains.
- *The second phase of globalization* began around 1900 and was associated with the rise of electricity and steel production. Electric power was widely used to drive mass production. This phase reached its height just before the Great Depression, a worldwide economic downturn that began in 1929. In 1900, Western Europe was the most industrialized world region. Europe's colonization of countries in Asia, Africa, and the Middle East led to the establishment of some of the earliest subsidiaries of multinational enterprises (MNEs). European companies such as BASF, Nestlé, Shell, Siemens, and British Petroleum established foreign manufacturing plants by 1900.<sup>4</sup> In the years before World War I (pre-1914), many firms operated globally. The Italian manufacturer Fiat supplied vehicles to nations on both sides of the war.

### EXHIBIT 2.1 Phases of Globalization Since the Early 1800s

Phase of Globalization	Approximate Period	Triggers	Key Characteristics
First phase	1830 to late 1800s, peaking in 1880	Introduction of railroads and ocean transport	Rise of manufacturing: cross-border trade of commodities, largely by trading companies
Second phase	1900 to 1930	Rise of electricity and steel production	Emergence and dominance of early MNEs (mainly from Europe and North America) in manufacturing, extractive, and agricultural industries
Third phase	1948 to 1970s	Formation of General Agreement on Tariffs and Trade (GATT); conclusion of World War II; Marshall Plan to reconstruct Europe	Focus by industrializing Western countries to reduce trade barriers; rise of MNEs from Japan; development of global capital markets; rise of global trade names
Fourth phase	1980s to about 2006	Privatization of state enterprises in transition economies; revolution in information, communication, and transportation technologies; remarkable growth of emerging markets	Rapid growth in cross-border trade of products, services, and capital; rise of internationally active SMEs and services firms; rising prosperity of emerging markets
Fifth phase	2007 to present	Rise of digital technologies, and other new technologies, which are boosting manufacturing productivity and the efficiency of international trade in services	Leveraging technology to facilitate trade and local production; rising trade in digitally enabled services but slowing growth of trade in merchandise goods

- *The third phase of globalization* began after World War II. This phase was associated with reconstruction efforts after the war and the dismantling of trade barriers. By the war's end in 1945, substantial pent-up demand fueled markets for consumer and industrial products to rebuild Europe and Japan. Leading industrialized countries, including Australia, the United Kingdom, and the United States, sought to reduce international trade barriers to supply goods to meet this demand.

In 1947, the Bretton Woods Conference of 23 nations created the *General Agreement on Tariffs and Trade (GATT)*, which reduced barriers to international trade and investment. Participating governments recognized that liberalized trade would stimulate industrialization, modernization, and better living standards. In turn, the GATT led to the formation of the **World Trade Organization (WTO)** ([www.wto.org](http://www.wto.org)), which grew to include about 164 member nations. The WTO aims to regulate and ensure fairness and efficiency in global trade and investment. Global cooperation in the postwar era also gave birth to the International Monetary Fund and the World Bank.

Early multinationals from the third phase of globalization originated in the United States, Western Europe, and Japan. European firms such as Unilever, Philips, Royal Dutch-Shell, and Bayer organized their businesses by establishing subsidiaries around

#### World Trade Organization (WTO)

A multilateral governing body empowered to regulate international trade and investment.

the world. Many companies developed internationally recognized trade names, including Nestlé, Kraft, Lockheed, Caterpillar, Coca-Cola, and Levi's. Foreign subsidiaries of such companies operated as small versions of the parent firm, marketing their products around the world. MNEs began to seek cost advantages by locating factories in developing countries with low labor costs. International trade and investment expanded significantly in the 1960s. Recovered from World War II, MNEs in Europe and Japan began to challenge the dominance of U.S. multinationals. Growing international trade coincided with increased cross-national flows of capital, leading to integration of global financial markets.<sup>5</sup>

- *The fourth phase of globalization* began in the early 1980s and featured the use of electronics and information technology to automate production. The phase was characterized by enormous growth in cross-border trade and investment. It was triggered by the development of personal computers, the Internet, and web browsers. It was also characterized by the collapse of the Soviet Union and the market liberalization of Central and Eastern Europe. Impressive industrialization and modernization in East Asian economies followed. International prosperity began to develop in the emerging markets, including Brazil, India, and Mexico. The 1980s witnessed huge increases in FDI, especially in capital- and technology-intensive sectors. Technological advances in information, communications, and transportation supported the rise of internationally active small and medium-sized enterprises. These advances increased the ability to organize and manage exports more efficiently and at lower cost. Modern technologies also enabled the globalization of the service sector in such areas as banking, entertainment, tourism, insurance, and retailing.
- *The fifth phase of globalization* began around 2007 with the rise of digital technologies. Technological breakthroughs in fields such as quantum computing, the Internet of Things, artificial intelligence, robotics, autonomous vehicles, 3D printing, nanotechnology, and biotechnology are blurring the lines between the physical, digital, and biological spheres. Digital and other new technologies are boosting the efficiency of international trade, especially in services. For example, much retailing is now done through giant firms such as Amazon and Alibaba, which sell their offerings around the world via online platforms. From Africa to South Asia to Latin America, as more people become digitally connected, they consume more international services. The value of world exports of services rose from about \$3 trillion in 2007 to more than \$5 trillion in 2017. Thanks to technological advances, national borders and traditional country-based business models are losing much of their relevance.

Meanwhile, growth in international trade of goods has slowed during this phase. Just as new technologies support international services trade, they also increase the productivity of local manufacturing. This tendency reduces firms' cost of domestic operations and increases the attractiveness of homegrown, local manufacturing. FDI as a share of total investment has declined. Emerging market countries increasingly focus on developing local markets for locally manufactured products.<sup>6</sup>

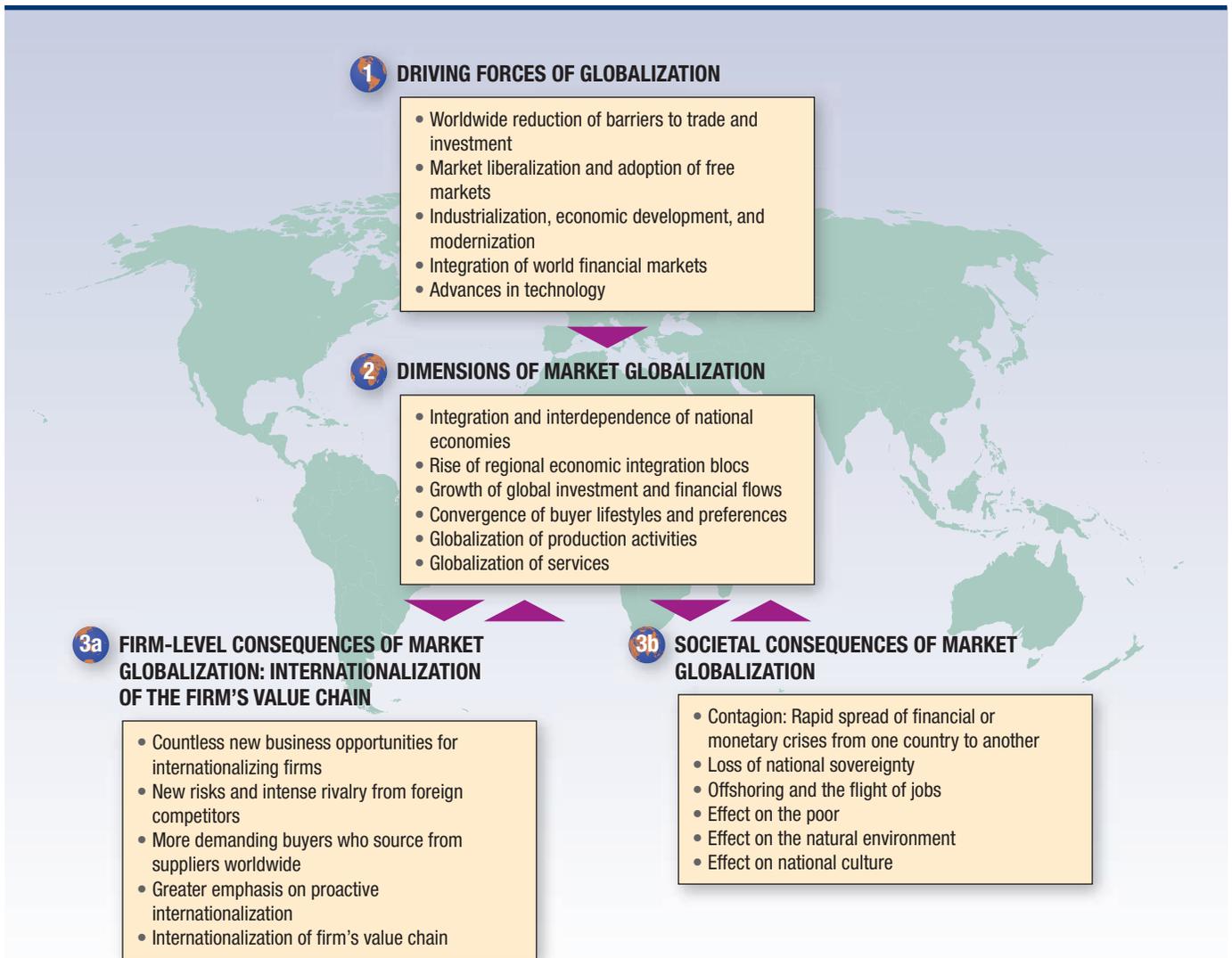
**2.1** Understand market globalization as an organizing framework.

## Market Globalization: Organizing Framework

Firms expand abroad proactively to increase sales and profit through new markets, find lower-cost inputs, or obtain other advantages. Firms may also internationalize reactively because of unfavorable conditions in the home market such as regulation or declining local industry sales. Exhibit 2.2 presents an organizing framework for examining market globalization. The exhibit makes a distinction among:

- *driving forces* or causes of globalization.
- *dimensions* or manifestations of globalization.
- *firm-level consequences* of globalization.
- *societal consequences* of globalization.

In the exhibit, the double arrows illustrate the interactive nature of the relationship between globalization and its consequences. As globalization intensifies, individual firms respond to the challenges and new advantages that it brings.

**EXHIBIT 2.2****The Driving Forces, Dimensions, and Consequences of Globalization**

America Movil ([www.americamovil.com](http://www.americamovil.com)) is a leading wireless phone service provider, with more than 225 million subscribers in 18 countries, that has pursued internationalization as a growth strategy. Based in Mexico, America Movil internationalized mainly through foreign direct investment (FDI) with initial operations in Brazil and Colombia. It then expanded to Ecuador, Chile, the Netherlands, and numerous other foreign markets. The firm entered into a joint venture with Citigroup to fund expansion in South America. It acquired Verizon's telephone operations in Puerto Rico. In each case, America Movil took advantage of such globalization trends as harmonizing communications technologies, converging buyer characteristics, and reduced trade and investment barriers. As emerging markets transform into sophisticated economies, they leapfrog older telecom technologies and embrace contemporary mobile phone technology—a boon to America Movil.

To minimize costs, many of the firm's cell phones are essentially identical worldwide. They are adapted only to accommodate for local languages, regulations, and telephone standards. America Movil's positioning emphasizes a global brand that is recognized everywhere. Worldwide convergence of buyer lifestyles and incomes help facilitate this transnational approach. Management coordinates operations on a global scale and applies common business processes in procurement and quality control. The strategies of product standardization, global branding, and selling to customers worldwide owe much of their success to the globalization of markets.<sup>7</sup>

## MyLab Management Watch It! 1

If your professor has assigned this, go to the Assignments section of [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) to complete the video exercise titled Born Global.

**2.2** Learn the driving forces of globalization.

## Driving Forces of Globalization

Various trends have converged in recent years as causes of globalization. The following are particularly notable:

- *Worldwide reduction in barriers to trade and investment.* The tendency of national governments to reduce trade and investment barriers has accelerated global economic integration. For example, tariffs on the import of industrial and medical equipment and countless other products have declined nearly to zero in many countries, encouraging freer international exchange of goods and services. Falling trade barriers are facilitated by the WTO. After joining the WTO in 2001, China has made its market increasingly more accessible to foreign firms. The decrease in trade barriers is also associated with the emergence of regional economic integration blocs. The recent rise of nationalistic politicians in some countries has tended to hinder ongoing reduction of trade and investment barriers. However, the overall trend of increasing free trade continues.<sup>8</sup>
- *Market liberalization and adoption of free markets.* In the past three decades, free-market reforms have smoothed the integration of China, India, Russia and other formerly protectionist countries into the global economy. Numerous Asian economies—for example, India, Indonesia, Malaysia, and South Korea—embraced free market norms. These events opened much of the world to freer international trade and investment. China, India, and Eastern Europe have become some of the most cost-effective locations for producing goods and services worldwide. Privatization of previously state-owned industries in these countries has encouraged economic efficiency and attracted massive foreign capital to their national economies.
- *Industrialization, economic development, and modernization.* Many emerging markets—rapidly developing economies in Asia, Latin America, and Eastern Europe—have now moved from being low value-adding commodity producers to sophisticated, competitive producers and exporters of premium products such as electronics, computers, and aircraft.<sup>9</sup> For example, Brazil is now a leading manufacturer of Embraer commercial aircraft. The Czech Republic excels in producing automobiles. India is a leading supplier of software. Economic development results in increased incomes and living standards, an important measurement of which is *gross national income (GNI)* per person.<sup>10</sup> Exhibit 2.3 maps the levels of GNI worldwide. It reveals that Africa and several countries in Asia and Latin America are the lowest-income countries. These areas are also characterized by lower levels of globalization. A critical driver of rising income levels is the nation's volume of international trade. Exhibit 2.4 highlights the relationship between trade and gross domestic product (GDP). In this exhibit, trade is expressed as the volume of merchandise exports, and GDP measures the volume of goods and services production. The exhibit suggests that countries that undertake the most international trade, and whose trade levels have sharply increased in the past decade, also enjoy high and rapidly rising GDP.
- *Integration of world financial markets.* Financial market integration makes it possible for internationally active firms to raise capital, borrow funds, and engage in foreign currency transactions. Financial services firms follow their customers to foreign markets. Cross-border transactions are made easier because of the ease with which funds can be transferred between buyers and sellers. This takes place through networks of international commercial banks. For instance, the SWIFT network connects more than 11,000 financial institutions in some 200 countries. This global financial connectivity assists firms in developing and operating world-scale production and marketing operations. It enables companies to pay suppliers and collect payments from customers worldwide.
- *Advances in technology.* Technological advances are a remarkable facilitator of cross-border trade and investment. This is an important megatrend that requires greater elaboration.

## Technological Advances and Globalization

Perhaps the most important driving force of market globalization has been technological advances in information, communications, manufacturing, and transportation. Technological advances provide the *means* for market globalization to happen.

### Information Technology

Information technology (IT) is the science and process of creating and using information resources. Its effect on business has been revolutionary. The cost of computer processing fell by more than 30 percent per year during the past three decades and continues to fall. IT creates competitive advantages by giving companies new ways to outperform rivals.<sup>11</sup> Geographically distant subsidiaries of a multinational firm are now interconnected by intranets that facilitate instant sharing of data, information, and experience across company operations worldwide. MNEs use collaboration software to connect widely dispersed product development teams.

IT benefits smaller firms, too, allowing them to design and produce customized products they can target to narrow, cross-national market niches. Online search engines provide easy access to unlimited data for researching markets, competitors, and other key information. At a higher level, IT supports managerial decision making, such as the selection of qualified foreign business partners, by allowing firms to access key information and intelligence quickly.

Technology enables firms to interact with foreign partners and value-chain members in a more timely and cost-effective way. Such productivity advances provide substantial competitive advantages for the firm.<sup>12</sup> One result is the increased early internationalization by SMEs. Emerging markets and developing economies benefit from technological leapfrogging. For example, numerous African countries are adopting cell phone technology directly, bypassing the landline technology common to some advanced economies.

Panel (a) of Exhibit 2.5 reveals how the cost of international communications has fallen since 2000, expressed as the dramatic rise in the volume of international traffic in Voice over Internet Protocol (VoIP) calls. VoIP is the mother technology of Skype, FaceTime, and numerous other platforms that facilitate very low-cost international voice and video communications. Panel (b) of Exhibit 2.5 reveals the growth in Internet users in various regions since 2000. Africa has the fewest Internet users, whereas Europe and North America have the most, reflecting the level of economic and infrastructural development in each region.

### Digitalization

*Digitalization* refers to enabling or transforming business functions, operations, and activities by leveraging digital technologies and digitized data. Digital connectivity has become possible because of advanced IT and telecommunications technologies. Digital networks provide a global platform through which people and organizations interact, collaborate, obtain information, and develop strategies. Digital flows of information and commerce are connecting the world more than ever before. E-commerce now encompasses a vast range of platforms and applications that facilitate international buying and selling of goods and services online. For example, sharing-economy firms such as Uber and Airbnb use specialized software and the Internet to facilitate the joint creation of value and services between asset users and asset owners. Around the world, Uber allows people who need temporary transportation to hire drivers and vehicles owned by others. Airbnb allows travelers to rent other people's homes.

Digitalization is transforming interactions among customers, employees, business partners and investors by connecting locations, products, services, and data.<sup>13</sup> Large-scale data analysis helps uncover breakthrough business insights and develop products, services, and experiences tailored to specific customer needs. For example, automakers continuously collect data on how customers use their cars and then utilize the data to improve product quality and the driving experience. Leveraging emergent technologies such as virtual reality and artificial intelligence helps to create innovative products and services that provide competitive advantages. Robots, artificial intelligence, and IT-based automation improve operational efficiency and deliver more engaging customer experiences. For example, MNEs are introducing sensors into manufacturing operations to improve production efficiency, predict maintenance problems, and perform repairs from remote locations.

**2.3** Understand the impact of technological advances on globalization.

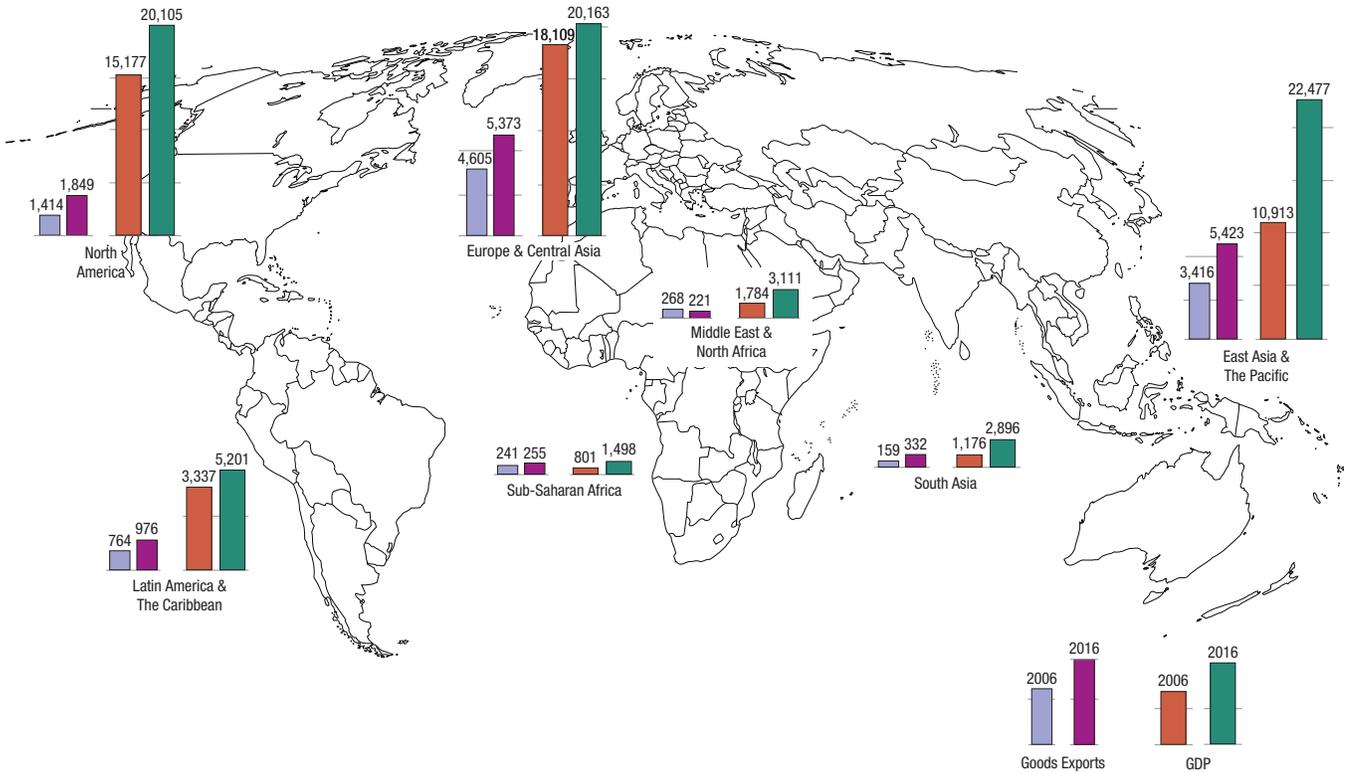


**EXHIBIT 2.3**

**Gross National Income, in U.S. Dollars**

Source: Based on World Bank (2018); World Bank Development Indicator database, GNI per capita, Atlas method (current US\$), [www.data.worldbank.org](http://www.data.worldbank.org).





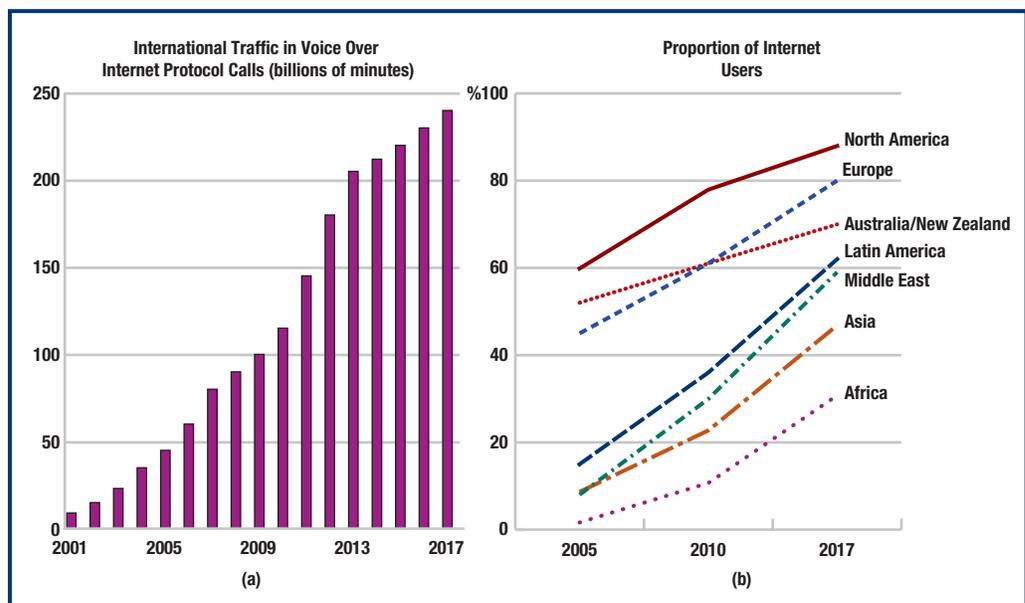
**EXHIBIT 2.4**  
**Relationship Between Trade and GDP Growth, in Billions of U.S. Dollars**

Source: Based on World Bank, Data, 2018, www.worldbank.org.

Digitalization has numerous consequences. The marginal cost of transmitting data and information worldwide is now essentially zero. Digitalization has reduced both the importance of geographic boundaries and the costs of international interactions and transactions. Companies extensively use digital tools to support innovation and improve productivity and the effectiveness of value chains worldwide. All kinds of firms use digital platforms to connect with customers and suppliers around the world. Competition is becoming more sophisticated and global. For example, Alibaba and Amazon are connecting global suppliers and imposing competitive pressures on traditional retailers worldwide.<sup>14</sup>

**EXHIBIT 2.5**  
**Growth of Global Communication and the Internet**

Sources: BridgeVoicePluto, "Disrupting Wholesale Telecom: VoIP Market Trends and Predictions," 2017, www.bridgevoice.com; IMF, *World Economic Outlook* (Washington, DC: International Monetary Fund, 2017); United Nations International Telecommunications Union, *ICT Statistics*, 2017, www.itu.int; Internet World Stats, *Internet Usage Statistics*, 2018, www.internetworldstats.com.



## Communications

The Internet and Internet-dependent systems such as intranets, extranets, social media, and email connect billions of people and companies. Marketers use the Internet to promote the widest range of products and services to customers worldwide. Transmitting voice, data, and images is essentially costless, making Seoul, Stockholm, and San Jose next-door neighbors. South Korea has nearly 100 percent Internet access, with one of the fastest broadband networks worldwide. Koreans use their phones to pay bills, do banking, and watch news programs.

The Internet opens the global marketplace to SMEs and other firms that would normally lack the resources to do international business. By establishing a presence on the web, even tiny enterprises can take the first step to become multinational firms. Services as diverse as designing an engine, monitoring a security camera, selling insurance, and doing secretarial work are easier to export than car parts or refrigerators. In China, thousands of rural farmers use Internet sites such as [www.taobao.com](http://www.taobao.com) to market their produce to urban consumers.<sup>15</sup>

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## Ethical Connections

In six years, Nigeria increased its telecom infrastructure from just 500,000 phone lines to more than 30 million cellular subscribers. The result has been a dramatic rise in productivity and commerce, which has helped improve living standards. Greater access to cell phones saves wasted trips, provides access to education and health care services, and facilitates communication between suppliers and customers. MNE telecom investment in Africa allows firms to fulfill social responsibilities and improve the lives of millions of poor people.

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Countries need modern infrastructure in communications, such as reliable telephone systems, to support economic development. Mobile phones are the most transformative technology in developing economies. Fortunately, cell phone infrastructure is inexpensive and relatively easy to install.

The *Internet of Things* refers to machine-to-machine connectivity online. Worldwide, mobile telephony and app development have grown enormously, creating millions of jobs, increasing productivity, and producing big GDP gains. The number of smartphone users reached 3 billion in 2017, double the figure in 2013. People everywhere are now online.<sup>16</sup>

Social media such as Snapchat, Instagram, and WeChat facilitate the free flow of information, deepening the pace and impact of globalization. Global communities created by platforms such as YouTube and Twitter help mobilize audiences that transcend borders and geographic distance. The “Arab Spring” in the Middle East was facilitated in large part by social media. In view of this, in some authoritarian countries, national governments restrict access to social media, fearing the role it can play in accelerating social movements. Many companies and other organizations leverage social media to communicate with their publics through direct sales, advertising, and public relations. Social media provide the means to communicate directly with millions of connected individuals in new markets. Puma uses Twitter and other platforms to market sportswear to customers in Europe and Latin America ahead of the World Cup games. McDonald’s used the social media site Renren.com to market burgers and sundaes to customers in China. Social media provide various means to reach important audiences in markets around the world.<sup>17</sup>

## Manufacturing

Digitalization and computer-aided design (CAD) of products, robotics, and production lines have transformed manufacturing, mainly by reducing production costs. Revolutionary developments facilitate low-scale and low-cost manufacturing; firms can make products cost-effectively even in short production runs. Online platforms are increasing the productivity of business and industrial activity. Such developments benefit international business by allowing firms to adapt products more efficiently to individual



Source: © Gilles Paire/Fotolia

Increasing availability of cell phones in Africa has helped spur economic growth there.



Source: federico rostagno/123rf

Advances in transportation and low freight costs have helped spur market globalization. Triple E class ships can carry thousands of shipping containers.

foreign markets, profitably target small national markets, and compete more effectively with foreign competitors that enjoy cost advantages.<sup>18</sup>

### Transportation

Firms consider the cost of transporting raw materials, components, and finished products when deciding to either export or manufacture abroad. If transport costs to an important market are high, management may decide to manufacture merchandise in that market. The development of fuel-efficient jumbo jets, giant ocean-going freighters, and new transportation technology has greatly reduced shipping times and costs. In recent decades, the volume of international shipping has increased dramatically. For example, world traffic in shipping containers increased from 225 million 20-foot equivalent containers in 2000 to more than 700 million such containers in 2017, a rise of 210 percent. Containers are the big boxes, usually 40 feet long (about 12 meters), loaded on top of ships, trucks, and

rail cars that carry the world's cargo. Today's ocean-going container ships hold more than 2,500 containers.<sup>19</sup>

Transportation of products has been revolutionized over time. However, growing transportation poses an increasing threat to the natural environment in terms of the usage of energy and other resources.

Shipbuilders, such as Maersk, have recently introduced container ships that can carry upward of 9,000 40-foot shipping containers. The vessels are so massive that only a handful of international ports can handle them, including Shanghai in China and Rotterdam in the Netherlands. These ships are used mainly to transport goods between Europe and Asia because they are too wide to pass through the Panama Canal. Technological advances in these Triple E vessels provide economies of scale that reduce the cost of transportation dramatically. They are energy efficient and environmentally friendly.<sup>20</sup>

#### 2.4 Learn the dimensions of globalization.

### Dimensions of Market Globalization

The globalization of markets can be characterized by several major dimensions.

- *Integration and interdependence of national economies.* Internationally active firms develop multi-country operations through trade, investment, geographic dispersal of company resources, and integration and coordination of value-chain activities. The collective activities of such firms give rise to *economic integration*, that is, increased trade and other commercial activities among the nations of the world. Governments assist this integration by lowering barriers to international trade and investment, harmonizing their monetary and fiscal policies within *regional economic integration* blocs, and creating *supranational* institutions. These include such organizations as the World Bank, International Monetary Fund, and World Trade Organization.
- *Rise of regional economic integration blocs.* Regional economic integration blocks consist of groups of countries that facilitate reduced trade and investment barriers among themselves. Examples include the North American Free Trade Agreement area (NAFTA), the Asia Pacific Economic Cooperation zone (APEC), and Mercosur in Latin America. In more advanced arrangements, such as a common market, the barriers to the cross-border flow of labor and capital are completely removed. A notable example is the European Union ([www.europa.eu](http://www.europa.eu)). The European Union has adopted free trade among its member countries and harmonized fiscal and monetary policies and business regulations.
- *Growth of global investment and financial flows.* In the process of conducting international transactions, firms and governments buy and sell large volumes of national currencies (such as dollars, euros, and yen). The free movement of capital around the world—the globalization of capital—extends economic activities across the globe. It further increases interconnectedness among world economies. The bond market has gained worldwide scope, with foreign bonds representing a major source of debt financing for governments and firms.

- *Convergence of consumer lifestyles and preferences.* Consumers around the world increasingly spend their money and time in similar ways. Many aspects of lifestyles and preferences are converging. Shoppers in New York, Paris, and Shanghai increasingly demand similar household goods, clothing, automobiles, and electronics. Teenagers everywhere are attracted to iPhones, Levi's jeans, and Hollywood movies. Major brands enjoy a global following encouraged by movies, global media, and the Internet. Movies such as *Transformers* and *The Hunger Games* have developed global audiences of fans. Convergence of preferences is also occurring in industrial markets, where professional buyers source raw materials, parts, and components that are increasingly *standardized*—that is, similar or identical in design and structure.
- *Globalization of production.* Intense global competition is forcing firms to reduce their costs of production. Companies cut their costs and selling prices through economies of scale, standardization of finished products, and shifting manufacturing and procurement to foreign locations with less expensive labor. For example, firms in the auto and textile industries have relocated their manufacturing to low labor-cost locations such as China, Mexico, and Poland.
- *Globalization of services.* The services sector—banking, hospitality, retailing, and other service industries—is undergoing widespread internationalization. The real estate firm REMAX has established more than 6,500 offices in some 100 countries. Firms increasingly outsource business processes and other services in the value chain to vendors located abroad. In a relatively new trend, many people go abroad to undergo medical procedures, such as cataract and knee surgeries, to save money.<sup>21</sup>



Source: Robert Harding Picture Library Ltd/Alamy

Google is one of many multinational enterprises that contribute to convergence of consumer lifestyles and preferences.

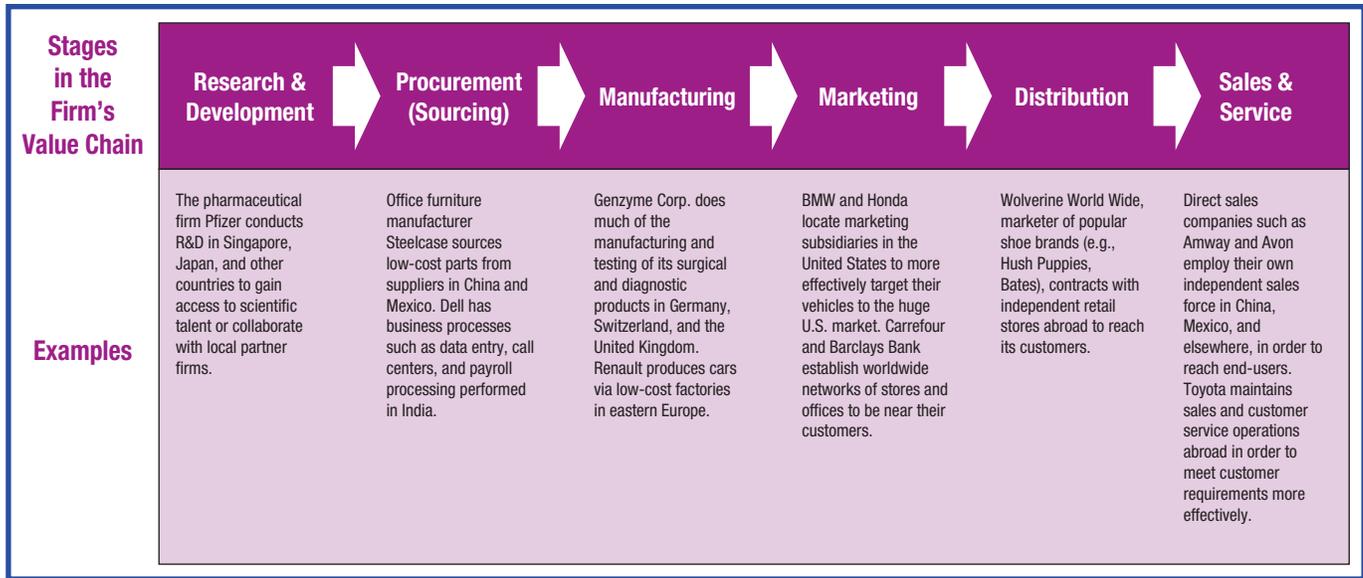
## Firm-Level Consequences of Market Globalization: Internationalization of the Firm's Value Chain

The most direct consequence of market globalization is on the firm's value chain. Globalization compels firms to organize their sourcing, manufacturing, marketing, and other value-adding activities on a global scale to achieve cost advantages and time efficiencies. In a typical value chain, the firm conducts research and product development (R&D), purchases production inputs, and assembles or manufactures a product or service. Next, the firm performs marketing activities such as pricing, promotion, and selling, followed by distribution of the product in targeted markets and after-sales service. The value-chain concept is useful in international business because it helps clarify *what* activities are performed *where* in the world. For example, exporting firms perform many upstream value-chain activities (e.g., R&D and production) in the home market and many downstream activities (e.g., marketing and after-sales service) abroad.

Each value-adding activity in the firm's value chain is subject to internationalization; that is, it can be performed in locations outside the home country. Exhibit 2.6 illustrates a value chain in a typical international firm. As examples in the exhibit suggest, companies have considerable latitude regarding where in the world they can locate or configure key value-adding activities. The most typical reasons for locating value-chain activities in particular countries are to reduce the costs of R&D and production or to gain closer access to customers. Through offshoring, the firm relocates a major value-chain activity by establishing a factory or other subsidiary abroad. A related trend is global outsourcing, in which the firm delegates performance of a value-adding activity to an external supplier or contractor located abroad.

In the same month that German carmaker BMW launched a new factory in South Carolina, an aging textile plant a few miles away, Jackson Mills, closed its doors and shed thousands of workers. Globalization created a new reality for both these firms. By establishing operations in the United States, BMW found it could manufacture cars cost-effectively while more readily accessing

**2.5** Understand the firm-level consequences of market globalization.



**EXHIBIT 2.6**

**Examples of How Firms' Value-Chain Activities Can Be Internationalized**

the huge U.S. market. In the process, BMW created thousands of high-paying, better-quality jobs for U.S. workers. Simultaneously, Jackson Mills had discovered it could source textiles of comparable quality more cost-effectively from suppliers in Asia. Globalization drove these firms to relocate key value-adding activities to the most advantageous locations around the world.

Without a doubt, globalization has created a crowded and intensely competitive global marketplace. As illustrated in Exhibit 2.7, globalization has meant that firms face intense rivalry from foreign competitors. This exhibit shows that in 1989 General Motors, Ford, and Chrysler together held nearly three-quarters of the market share in passenger car sales in the United States. By 2017, the percentage had fallen to 44 percent, and Chrysler had been acquired by the Italian automaker Fiat. The market shares of competitors such as Toyota, Hyundai, and others rose dramatically. Over time, the services sector also has been internationalizing at a fast pace. See the *You Can Do It: Recent Grad in IB* below featuring Terrance Rogers, who is working in the global banking industry.

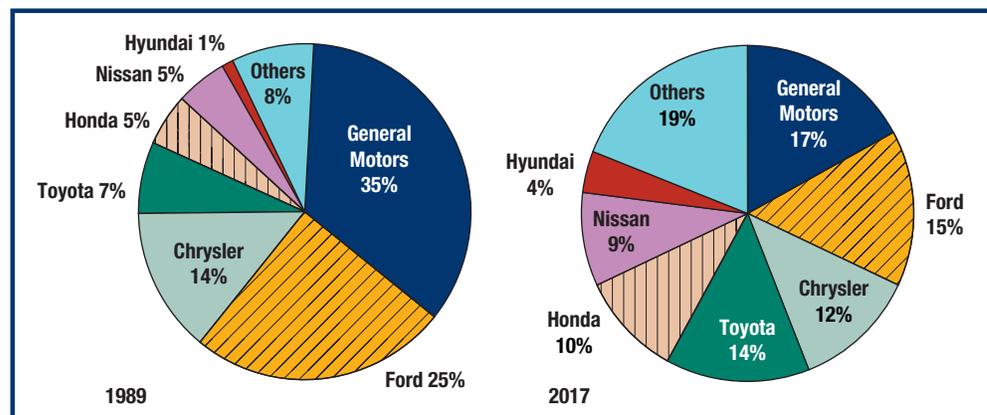
**MyLab Management Watch It! 2**

If your professor has assigned this, go to the Assignments section of [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) to complete the video exercise titled Rudi's Bakery Management in the Global Environment.

**EXHIBIT 2.7**

**Market Shares of Automakers in Passenger Car Sales in the United States, 1989 and 2017**

Sources: Based on Craig Trudell, "U.S. Automakers Seen Losing Market Share amid 2012 Growth: Cars," *Bloomberg BusinessWeek*, February 8, 2012, [www.businessweek.com](http://www.businessweek.com); J. Muller, "Automakers Gold Rush," *Forbes*, June 8, 2009, pp. 70–77; *Wall Street Journal*, "Sales and Total Share of Market by Manufacturer," February 1, 2018, [www.wsj.com/mdc/public/page/2\\_3022-autosales.html](http://www.wsj.com/mdc/public/page/2_3022-autosales.html).





### TERRANCE ROGERS

**Terrance's Majors:** Finance and international business

**Objectives:** Exploration, international perspective, self-awareness, career growth, and learning about foreign markets

**Internships during college:** Deutsche Bank

**Jobs held since graduating:**

- Business analyst at Deutsche Bank, New York
- Management associate at Deutsche Bank, New York
- Executive management rotation at Deutsche Bank, New York
- Executive management associate at Deutsche Bank, London and New York

After taking his first international business course, Terrance became fascinated with the idea of working abroad. As a university student, he enrolled in his college's International Business Certificate program. The program allowed Terrance to combine his passion for finance with his appetite for learning about culture and doing business abroad. Terrance took his first international trip through a short study abroad course. The course, "Financial and Managerial Issues in the EU," brought him to Paris and Brussels. Terrance and his classmates visited prominent businesses and the European Union offices to hear from leaders across multiple sectors. The experience allowed Terrance to believe that working abroad could be a real possibility for him.

After graduation, Terrance started his career as a business analyst with Deutsche Bank in New York. The position gave him experience in regulatory change, process improvement, and crisis management. Terrance got the opportunity to work on several global projects. After being promoted to management associate, Terrance worked directly with the chief operations officer of the Americas for his division.

After spending four years gaining experience in various areas of the bank,

Terrance took a position with numerous international responsibilities. Today, Terrance is an executive management associate, leading business strategy, finance analysis, and communications for the United Kingdom Executive Team. In this role, he splits his time between London and New York. He is responsible for interpreting financial drivers, product strategy, and operational issues that shape each business line in the region. He works directly with the head of Marketing and Communications to craft and execute communication strategy for the chief executive officer.

### Terrance's Advice for an International Career

Terrance owes his success to early exposure at his university to international business and study abroad. Terrance says that "international careers are a requirement for today's business leaders. Major clients don't just reside in the U.S. anymore, so if you want to have a long impactful career, you must find a way to gain some international exposure. Your boss will rely on you to be able to work with business associates from different cultures. Your clients will expect you to understand issues with a global perspective, and if you don't have

any global experience, your competitors (for jobs and clients) will be one step ahead of you."

### Success Factors

"If you want to work abroad, do the following things to increase your chances at securing an international role: (a) Work on projects that expose you to people in different regions across the globe; (b) mention your interest in working abroad early and bring it up in your annual review; and (c) find a way to impress the people who can make the decision. It becomes easier to make the move when the 'right people' know that you can deliver."

### Challenges

"Challenges like language barriers and cultural differences are things that should be faced as soon as you can in your career. Don't be afraid to make a mistake. It's much better to learn from cultural missteps now so that you can be a better business leader tomorrow." Globalization is a major dimension of business today.

*Source:* Courtesy of Terrance Rogers.

**2.6** Understand the societal consequences of globalization.

## Societal Consequences of Globalization

Our discussion so far has highlighted the far-reaching, positive outcomes of globalization. Major advances in living standards have been achieved in virtually all countries that have opened their borders to increased trade and investment.<sup>22</sup> Yet the transition to a global marketplace also poses challenges to individuals, organizations, and governments. Low-income countries have not been able to integrate with the global economy as rapidly as others have. Poverty remains a major problem in Africa and in populous nations such as Brazil, China, and India.<sup>23</sup> Let's consider some of the unintended consequences of globalization.

## Contagion: Rapid Spread of Monetary and Financial Crises

The world economy has experienced numerous financial and monetary crises. In 2008, for example, a major financial crisis was triggered by unsustainably high prices in housing and commodities. As real estate prices tumbled, many owners were left with mortgage debts greater than the value of their homes. Tens of thousands of those mortgages had been bundled and sold as investments on stock markets worldwide. As the value of these homes and securities plunged or became uncertain, stock markets also plunged.<sup>24</sup> The crisis began in the United States and spread around the world, like a contagious disease.

### Contagion

The tendency of a financial or monetary crisis in one country to spread rapidly to other countries due to the ongoing integration of national economies.

In international economics, **contagion** refers to the tendency for a financial or monetary crisis in one country to spread rapidly to other countries due to integrated national economies.<sup>25</sup> For example, excessive consumer borrowing can give rise to instability or overheating of national economies. Resultant crises can be aggravated by insufficient or ill-conceived regulation of the financial and banking sector or of the economy at large. As we will see later in this text, having a strong legal and regulatory framework is critical to national economic well-being.<sup>26</sup>

Financial or economic crises may weaken consumer confidence and reduce spending on consumer goods, services, and other consumables. Decreased spending, in turn, affects global commerce and international trade.<sup>27</sup> Following the crisis that began in 2008, global growth declined to levels not seen since World War II. Many national economies did not begin to recover until 2010. Economies in Japan and several countries in Europe have remained sluggish.<sup>28</sup>

Exhibit 2.8 shows how GDP growth in advanced, developing, and emerging economies varies over time. GDP in all three of these economies declined substantially during the recent global recession and financial crisis. One lesson of the exhibit is that, even following deep recessions, the global economy has always rebounded, and countries' GDPs have returned to growth.

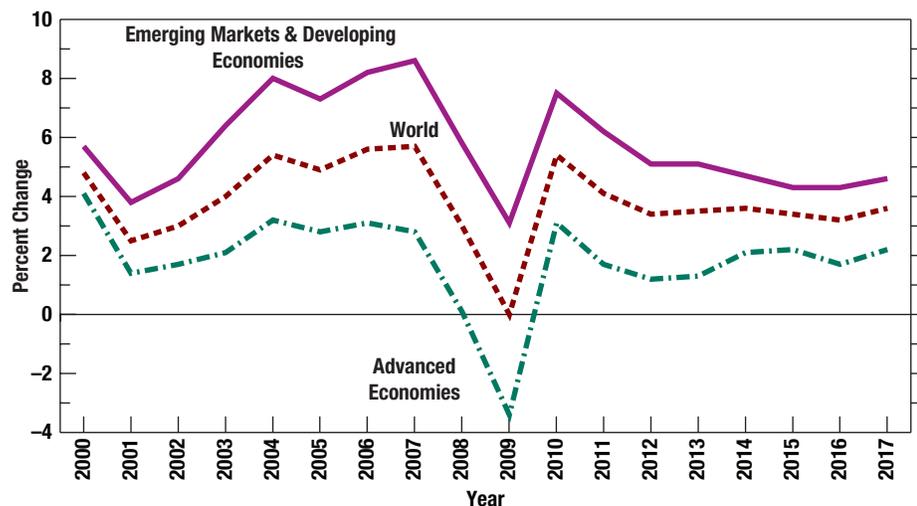
## Loss of National Sovereignty

*Sovereignty* is defined as the ability of a nation to govern its own affairs; normally one country's laws cannot be applied or enforced in another country. Globalization, however, can threaten national sovereignty in various ways. MNE activities can interfere with a government's ability to control its own economy, social structure, and political system. Some corporations are bigger than the economies of small nations; Walmart's internal economy—its total revenues—is larger than the GDP of many of the world's nations, including Israel, Greece, and Poland. Large multinational firms can apply much pressure on governments through lobbying or campaign contributions and can frequently influence the legislative process.

The largest firms are constrained by market forces. In countries with many competing firms, one company cannot force customers to buy its products or force suppliers to supply it with raw materials and inputs. Resources that customers and suppliers use are made through free choice.

### EXHIBIT 2.8 Percentage of Change in Annual GDP Growth

Sources: World Bank, Data, GDP Growth (Annual %), <http://data.worldbank.org>, 2017; IMF, *World Economic Outlook* (Washington, DC: International Monetary Fund, September 2017); IMF, *World Economic Outlook Database, 2017*, [www.imf.org](http://www.imf.org); United Nations, UNData, "GDP Growth (annual %)," 2017, <http://data.un.org>.



Company performance depends on the firm's skill at winning customers, working with suppliers, and dealing with competitors. Corporate dominance of individual markets is rare. In reality, market forces generally dominate companies. For example, Ford, Chrysler, and General Motors once dominated the U.S. auto market. Today, many more automotive firms—Toyota, Honda, Hyundai, Nissan, and Volkswagen—compete in the United States, along with newcomers such as Tesla. Volkswagen now leads the global market in annual unit sales. Home-country market shares of domestic U.S. automakers have tumbled.<sup>29</sup>

To minimize globalization's harm and reap its benefits, governments should ensure the freedom to enter and compete in markets, protect private property, enforce the law, and support voluntary exchange through markets rather than through political processes. Banks and financial institutions should be regulated appropriately. Transparency in the affairs of business and regulatory agencies is critical.

### Offshoring

Globalization has created countless new jobs and opportunities worldwide, but it also has cost many people their jobs. Ford and General Motors have laid off thousands of workers in the United States, partly the result of competitive pressures posed by carmakers from Europe, Japan, and South Korea. Ford, GM, and Volkswagen all have transferred thousands of jobs from their factories in Germany to countries in Eastern Europe.<sup>30</sup> *Offshoring* is the relocation of manufacturing and other value-chain activities to cost-effective locations abroad. For example, the global accounting firm Ernst & Young relocated much of its accounting support work to the Philippines. Massachusetts General Hospital has its CT scans and X-rays interpreted by radiologists in India. Many IT support services for customers in Germany are based in the Czech Republic and Romania.<sup>31</sup>

High-profile plant closures and manufacturing relocation have received much media attention. For example, Polaris, the U.S. manufacturer of all-terrain vehicles, moved its Wisconsin factory to Mexico to reduce production costs. In Australia, Toyota closed a Camry factory, resulting in the loss of thousands of jobs. Such closures disrupt local communities in various ways.<sup>32</sup>

Simultaneously, however, MNEs create millions of jobs abroad, which help raise living standards. For example, U.S. MNEs now employ about a million workers in each of Canada, China, Mexico, and the United Kingdom.<sup>33</sup> In developing economies and emerging markets, such positions help raise living standards.

### Reshoring

MNEs sometimes engage in *reshoring*—the return of manufacturing and services back to the home country. It is the opposite of *offshoring* which refers to the relocation of manufacturing to a foreign country, usually to take advantage of low-cost labor. For example, Ford and Boeing have reshored thousands of jobs back to the United States. Reshoring is done for various reasons, including the rise of wages and other business costs in emerging market countries as well as the desire to manage operations more effectively and locate value-chain activities closer to customers. General Electric reshored the production of energy-efficient water heaters from China back to the United States in order to manage inventory and transportation costs better. Symington's, a British food company, moved noodle production from China back to England in order to improve product quality, increase delivery speed, and manage the supply chain more effectively.<sup>34</sup>

### Effect on the Poor

Globalization has affected the poor in areas related to income distribution and worker exploitation by MNEs. *Income distribution* refers to the allocation of GDP and national income among the members of a society. In some countries, a relatively small minority, often less than 10 percent, holds most of the country's wealth, and the great majority of citizens live in poverty. This income inequality is substantial in several nations in Southern Africa and in Latin America, for example. Among the advanced economies, income inequality is less of a factor in Japan and most countries in Northern Europe due mainly to cultural factors and public policies. Income inequality is relatively more common in the United States, which is home to many highly paid executives and other wealthy individuals.

As nations' economies develop and per-capita incomes rise, globalization can worsen income inequality because many good-paying jobs in the manufacturing sector are lost as companies shift



Source: Peter Cook/Dorling Kindersley

Media attention and consumer concern are helping to improve wages and sweatshop conditions slowly in developing economies, such as those in South Asia.

production to low-wage countries. In the advanced economies, growing international trade coincided with falling wages in many industries as firms transferred manufacturing jobs to lower-cost countries, such as China and Mexico. However, income inequality is a complex and dynamic phenomenon. While the creation of new manufacturing jobs has increased wages for many individuals in China, Mexico, and other emerging markets, income levels among other, often larger groups in such countries have remained relatively stagnant.

In addition, automation and technology, to a large extent, have resulted in lower incomes for many people. Just as demand for high-skill workers has increased, demand for lower-skill or less-educated workers has decreased. This arises because many jobs that historically were done by low-skill workers are now performed by machines and digital platforms.<sup>35</sup>

Many MNEs have been criticized for paying low wages, exploiting workers, and employing child labor. Child labor is particularly troubling because it denies

children educational opportunities. It is estimated there are more than 215 million children aged 5 to 17 at work around the world. About 73 million children are believed to work in hazardous conditions.<sup>36</sup>

Bangladesh, China, Colombia, Egypt, and the Philippines are examples of countries often characterized by poor working conditions. In Egypt, employees who strike or protest poor working conditions can be jailed. In China, many factory workers earn less than \$3 per day and may have to work long hours. Companies ranging from Nike to H&M to the Gap have been accused of tolerating sweatshop conditions in their factories overseas.<sup>37</sup>

### MyLab Management Watch It! 3

If your professor has assigned this, go to the Assignments section of [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management) to complete the video exercise titled Save the Children Social Networking.

Labor exploitation and sweatshop conditions are major concerns in many developing economies.<sup>38</sup> But some ask, “What other employment choices are available to poorly educated people?” A low-paying job is usually better than no job at all. Studies suggest that banning products made using child labor may produce unintended negative consequences such as reduced living standards for families.<sup>39</sup> Legislation passed to reduce child labor in the formal economic sector (the sector regulated and monitored by public authorities) may have little effect on jobs in the informal economic sector, sometimes called the *underground economy*. In the face of persistent poverty, abolishing formal sector jobs does not ensure that children leave the workforce and go to school.

Work conditions and salaries tend to improve, over time, in many developing countries. The growth of the footwear industry in Vietnam translated into a fivefold increase in wages. While still low by advanced economy standards, those growing wages are improving the lives of millions of workers and their families. Globalization tends to support a growing economy. Countries that liberalize international trade and investment enjoy faster per-capita economic growth. Developing economies that seek to integrate with the rest of the world tend to have faster per-capita GDP growth than those that fail to participate in the world economy.<sup>40</sup>

Exhibit 2.9 shows the global GDP growth rate from 2009 to 2018. Most nations are experiencing positive growth. The fastest-growing large economies are China and India. Exhibit 2.10 reveals that, on average, global poverty is declining over time.<sup>41</sup> This exhibit

illustrates the income status of people in developing economies. Poverty remains a major factor in South Asia and sub-Saharan Africa (that part of Africa below the Saharan Desert), but even those areas have made much progress in the past decade. The Middle East and North Africa, Latin America, and East Asia are home to billions of people whose daily incomes have risen substantially. Much of these improvements are due to international trade and investment activities.<sup>42</sup>

### Effect on Sustainability and the Natural Environment

Globalization promotes manufacturing and economic activity that result in increased pollution, habitat destruction, and deterioration of the ozone layer. In China, for example, economic development is attracting much inward FDI and stimulating the growth of numerous industries. The construction of factories, infrastructure, and modern housing can spoil previously pristine environments. In eastern China, growing industrial demand for electricity led to construction of the Three Gorges Dam, which flooded agricultural lands and permanently altered the natural landscape. See the *Apply Your Understanding* exercise at the end of this chapter, which presents an Ethical Dilemma problem on the environmental damage done by a large oil company in Nigeria.

As globalization stimulates rising living standards, concerned citizens focus on improving their environment. Over time, governments pass legislation that promotes improved environmental conditions. For example, Japan endured polluted rivers and smoggy cities in the early decades of its economic development following World War II. As its economy grew, the Japanese passed tougher environmental standards to restore their natural environment.

Evolving company values and concern for corporate reputations have led many firms to reduce or eliminate practices that harm the environment.<sup>43</sup> In Mexico, for example, big automakers such as Ford and General Motors have gradually improved their environmental standards. Alcan in Canada (aluminum), Kirin in Japan (beverages), and Google in the United States (Internet services) are examples of firms that embrace practices that protect the environment, often at the expense of profits.<sup>44</sup> The Conservation Coffee Alliance has committed approximately \$2 million to environmentally friendly coffee cultivation in Central America, Peru, and Colombia.

### Effect on National Culture

Globalization exerts strong pressures on national culture because market liberalization exposes local consumers to global brands, unfamiliar products, and different values. People worldwide are exposed to movies, television, the Internet, and other information sources that promote lifestyles of people in the United States and other advanced economies. Appetites grow for Western products and services, which are seen to signal higher living standards. For example, despite low per-capita income, many Chinese buy consumer electronics such as smartphones and TV sets. Advertising disseminates societal values modeled on Western countries. Hollywood dominates the global entertainment industry.

The flow of cultural influence often goes both ways, too. Cafe Spice is an Indian food company whose founder hails from Mumbai. The firm is transforming American tastes by selling curry dishes and other Indian favorites in cafeterias and supermarkets. Cafe Spice is helping to make Indian cuisine mainstream in the United States.<sup>45</sup> As the influence of the Chinese economy grows over time, Western countries will likely adopt some of China's cultural attitudes and behaviors. Chinese restaurants and some Chinese traditions are already a way of life in much of the world. Similar influences are evident from Latin America and other areas in the developing world.



Source: Sergey Zhukov/Shutterstock

Western companies can influence food preferences, but cultural values tend to remain stable over time. This Burger King is in Bangkok, Thailand.



**EXHIBIT 2.9**

**The Growth of World GDP, Average Annual GDP Growth Rate, 2009–2018 (%)**

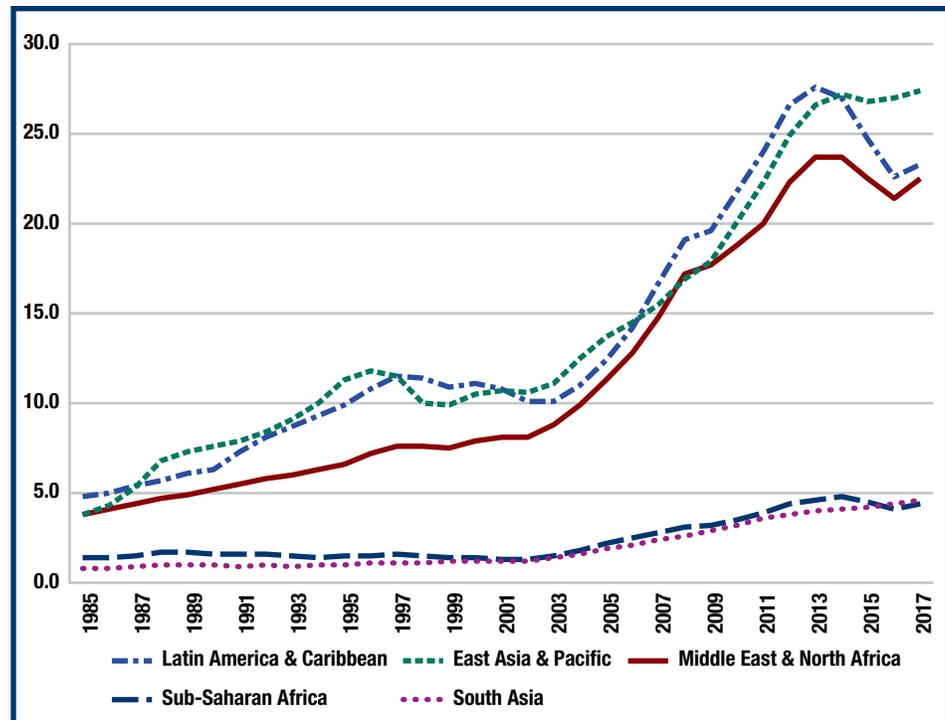
Source: International Monetary Fund, World Economic Outlook database, 2018, [www.imf.org](http://www.imf.org).



**EXHIBIT 2.10****The Rise of Daily Income Levels, by Region, in U.S. Dollars**

Sources: L. Chandy, N. Ledlie, and V. Penciakova, *The Final Countdown: Prospects for Ending Extreme Poverty by 2030*, Policy Paper 2013–14 (Washington, DC: Brookings Institution); *Economist*, “Poverty’s Long Farewell,” February 28, 2015, p. 68; World Bank, GNI per capita, Atlas method (current US\$), 2017, <http://data.worldbank.org>.

Note: The figures show average daily income per capita, in U.S. dollars, adjusted for inflation.



Cultural imperialism is offset by the countertrend of local nationalism. Although many products and services have become largely universal, people’s behaviors and attitudes remain relatively stable over time. Religious differences are as strong as ever. Language differences are steadfast across national borders. As globalization standardizes superficial aspects of life across national cultures, people resist these forces by insisting on their national identity and taking steps to protect it. For example, laws exist to protect national language and culture in Belgium, Canada, and France.

**Globalization and Africa**

Africa is home to the poorest countries. The majority of its 1 billion people live on less than \$5 a day. It is the area least integrated into the world economy and accounts for less than 5 percent of world trade. Although it has abundant natural resources, Africa remains underdeveloped due to many factors, including an inadequate commercial infrastructure, lack of access to foreign capital, high illiteracy, government corruption, wars, and the spread of AIDS.

Experience of the past half century suggests that traditional methods of trying to help Africa—mainly foreign aid provided by advanced economies—have achieved little success. Despite billions of dollars of aid to Africa, per-capita income is increasing relatively slowly.<sup>46</sup>

One of the most effective ways to alleviate African poverty is to develop more business-based models of development.<sup>47</sup> Several sub-Saharan African countries have recently experienced significant economic growth by increasing international trade in commodities. Africa is a major supplier of petroleum to Europe and the United States. Angola is among the top oil suppliers to China. This activity has developed a ripple effect of economic development. Because of the boom of certain sectors in Africa, there has been an increase in foreign banks, retailers, and MNE operations in the continent.<sup>48</sup>

Rwanda had developed business opportunities in sectors as diverse as mining, tourism, telecommunications, and real estate. China and India are beating out U.S. firms and quickly increasing their business dealings in Africa. Chinese companies are investing billions of dollars in the continent. All this international trade and investment is helping to address many of Africa’s most pressing development needs.<sup>49</sup> Samsung has set a goal of \$10 billion in African sales and is committed to training 10,000 African engineers and technicians to develop the capabilities

needed for success. Even so, it will take many more years for Africa to achieve a critical mass of infrastructure and business culture sufficient to raise average incomes substantially across the continent.

Technology plays an increasing role in reducing poverty. Increasing use of mobile phones, satellite technology, and IT is helping farmers in Africa to increase crop yields and agricultural productivity. IT is being used to develop databases of information that support farmers in minimizing crop damage and improve farming methods. Data obtained from satellite technology helps farmers assess the likelihood of draught and prepare accordingly.<sup>50</sup>

## CLOSING CASE

### A Debate on the Good and Harm of Globalization

People around the world are concerned about the impact of globalization, which they associate with job losses, declining national sovereignty, mass migration, and an intrusion of foreign values. Globalization has become a central theme in political, economic, and academic discourse. Recently, a major university sponsored a roundtable on the broader implications of globalization. The participants were an anti-globalization activist, a business executive, and a government trade official. Excerpts from the exchange provide diverse perspectives on globalization and international business.

#### Activist

“One problem with international business is that it often ignores human rights and basic labor standards. Low-wage factories abroad create substandard working conditions. The activities of multinational companies not only result in job losses here at home, but also in low wages and exploited workers around the world. Just think of the sweatshops in Asia that make imported clothing. Think of the autoworkers in Mexico who live in horrible conditions and make only a few dollars a day. Also consider the poverty caused worldwide by the recent global financial and economic crisis.”

#### Business Executive

“Our country needs to participate in the global economy. Companies that export provide better-paying jobs, have more profits, pay higher taxes, and stimulate purchases from local suppliers. Foreign companies that invest here create new jobs, enhance local living standards, and pressure our firms to stay competitive in a challenging global marketplace. Exporters pay higher wages and provide better benefits than non-exporting firms do. Many companies need access to foreign markets because of the huge, upfront research and development costs they accumulate. One more pill is cheap; it’s the cost of research to find a cure for AIDS that is prohibitive. Pharmaceutical firms can’t do the necessary R&D unless they can amortize those costs over a huge, global marketplace. In the long run, uninterrupted international commerce is good.”

#### Trade Official

“The current administration believes in the value of free trade. The government strongly supported NAFTA, and this has already had a positive effect on the economy through increasing exports to Mexico, creating jobs, and leading to improved investment opportunities. Countries are forging ahead with international trade ties.

Canada has completed a free trade agreement with Chile. Economic ties lead to cultural ties and more peaceful relations. Also, it’s hard for our government to promote freedom and democracy around the world if we’re not promoting free trade.”

#### Activist

“We cannot overlook the detrimental effects of globalization on the natural environment. The more we trade internationally, the more irreparable harm will be done to the environment. International business means more environmentally damaging development. Companies internationalize so they can become more efficient. But if countries have weak environmental standards, then factories will be built with minimal environmental standards.”

#### Business Executive

“If we trade internationally, then living standards will increase everywhere. As living standards rise, awareness of and care for the environment will also increase. International business is good for the world because it creates wealth. The more affluent the people, the more they will care about their environment and pass laws to protect it. We are also becoming more responsive to concerns over social responsibility and environmental degradation. We have shown that a good economy and a clean environment are not mutually exclusive. We can have it both ways: a clean planet and a better quality of life.”

#### Trade Official

“I think part of the solution is to negotiate trade agreements that take environmental factors into account. International trade that disregards legitimate environmental concerns is counterproductive and defeats the political agendas of most governments around the world. It is clear that international trade must take environmental concerns into account.”

#### Activist

“International trade interferes with the sovereignty of national governments. When Apple or Toyota are bigger than most countries in Africa, it is harder for governments to manage policies regarding taxes, monetary policy, social issues, and exchange rates. And who are we, trying to impose our own cultural standards on the world? When I travel in Asia or Latin America, I see McDonald’s all over the place. They see Western powers exploiting globalization, harming the economic, cultural, and environmental interests of the rest of the world.