chapter 1

# Globalization and International Business

## Objectives

1. To define *globalization* and *international business* and explain how they affect each other
2. To show why companies engage in international business and why its growth has accelerated
3. To discuss globalization's future and the major criticisms of it
4. To illustrate the different ways a company can accomplish its global objectives
5. To apply social science disciplines to understanding the differences between international and domestic business

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*Source:* Allstar Picture Library/Alamy

*The world's a stage;*
*each plays his part,*
*and takes his share.*

*—Dutch proverb*

# CASE

# Global Games for Fun and Business

The Fédération Internationale de Football Association (FIFA) has more country members than the United Nations has, and it administered the competition that brought 32 national teams to the 2010 World Cup in South Africa after months of qualifying games.[1] (The preceding photo shows part of the opening ceremony.) You were likely part of the record global television audience for at least some of the Cup and remember the droning of vuvuzela horns throughout the matches. While FIFA's membership has long been global, the 2010 Cup was the first in Africa, thus contributing toward the rapid global diffusion of major sports competition. In addition, the 2010 Commonwealth Games were played for the first time in India, the first Olympics in South America is scheduled for Brazil, and the first World Cup in the Middle East is confirmed for Qatar.

Sports, according to one political historian, is now "the most globalized [legitimate] business in the world." Historically, most players and teams in most sports competed only on their own home turf. Today, however, fans everywhere demand to see the best, and "best" has become a decidedly global standard. Satellite TV now brings live events from just about anywhere in the world to fans just about anywhere else in the world. Thus the key players in the sports-promotion business—team owners, league representatives, and sports associations—have broadened audience exposure, expanding fan bases and augmenting revenues, especially through advertising that cuts across national borders.

Likewise, because more fans expect to see the world's best teams and players, the search for talent has become worldwide. You can now find U.S. and European professional basketball scouts in remote areas of Nigeria looking for high-potential tall youngsters. Baseball agents have opened live-in training camps for teenagers in the Dominican Republic in exchange for a percentage of any of their future professional signing bonuses. However, keep in mind that assembling talent is necessary but insufficient to make a sports business successful. Shrewd marketing and financial management are crucial too. For instance, the Barcelona football club, arguably the best professional soccer team in recent years, nevertheless has had financial problems. It has turned to young business graduates to turn things around.

## THE INTERNATIONAL JOB MARKET

Today's top-notch players in just about every sport are willing to follow the money wherever it may take them. For instance, many of the best Brazilian soccer players are with European teams that offer much higher payrolls than their Brazilian counterparts. England's professional soccer league (Premiership) includes players from about 70 countries, which helps to improve the caliber of play and increase the TV fan base outside England. Interestingly, fans continue to follow national favorites even after they've taken their talents elsewhere. About 300 million Chinese tuned in to watch local basketball legend Yao Ming's first game in America's National Basketball Association (NBA).

### How the ATP Courts Worldwide Support

If you're a fan of individual sports, you've probably noticed that players are globe hoppers. Take tennis. No single country boasts enough interested fans to keep players at home for year-round competition. In any case, today's top-flight tennis pros come from every continent except Antarctica, and tennis fans everywhere want to see the top players compete on local courts. For 2012, the Association of Tennis Professionals (ATP) sanctioned 66 tournaments in 30 countries. It also requires member pros to play in a certain number of events—and thus stop over in a number of countries—to maintain international rankings.

Because no tennis pro can possibly play in every tournament, organizers must attract enough top draws to fill stadium seats and land lucrative TV contracts. Tournaments, therefore, compete for top-billed stars, not only with other tournaments but also with such regular international showcases as the Olympics and the Davis Cup. Prizes for two weeks' worth of expert serving and volleying can be extremely generous (about U.S. \$2.2 million for the 2011 singles champions of the Australian Open).

Remember, too, that tournaments earn money through ticket sales, corporate sponsorship agreements, television contracts, and leasing of advertising space. The more people in the stadium and TV audience, the more sponsors and advertisers will pay to get their attention. Moreover, international broadcasts attract sponsorship from international companies. The sponsor list for the 2011 Australian Open tennis tournament included a South Korean automaker (Kia), a Dutch brewer (Heineken), a Swiss watchmaker (Rolex), a French clothing company (Lacoste), and a U.S. sporting goods firm (Wilson).

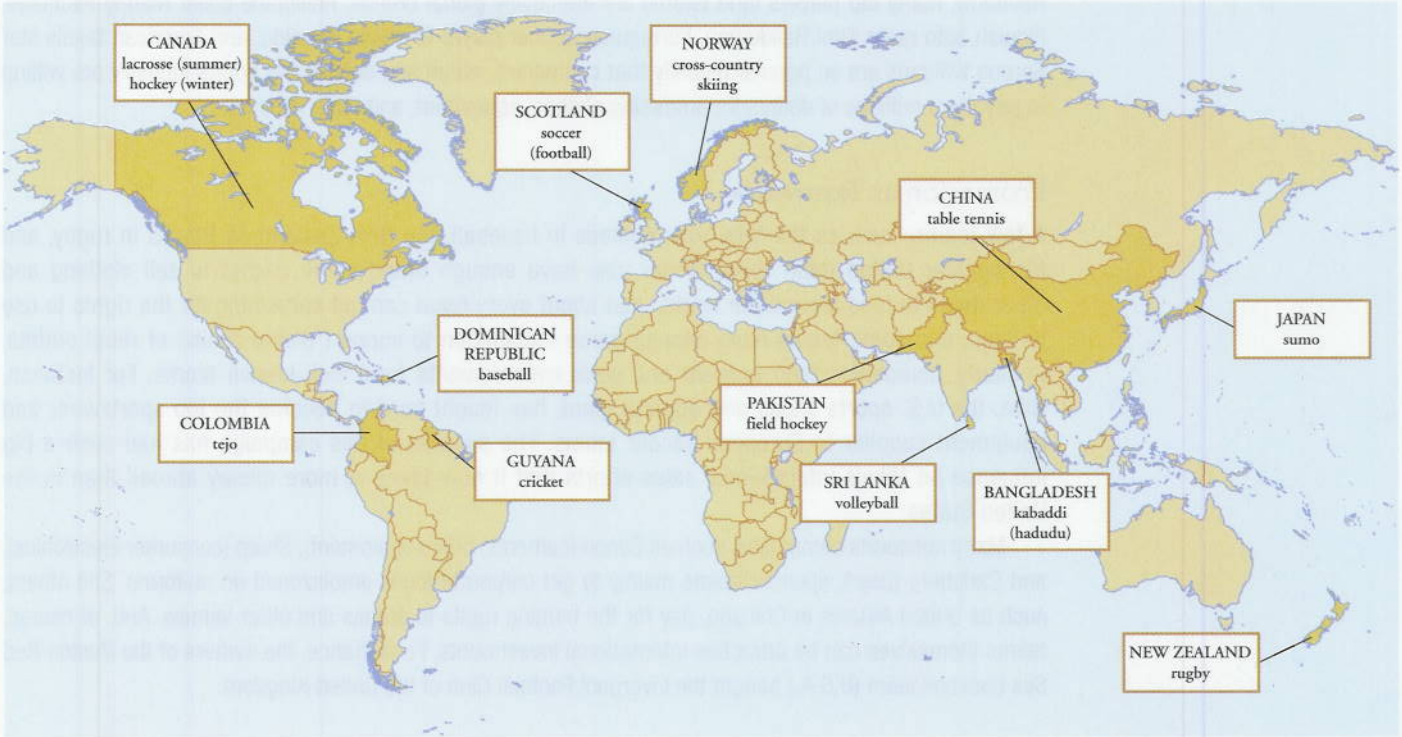
### From National to International Sports Pastimes

Some countries have legally designated a national sport as a means of preserving traditions, and some others effectively have one. Map 1.1 shows a sample of these. However,

## MAP 1.1 Examples of National Sports

Some 33 countries have either defined a national sport by law or de facto have a national sport. Some national sports are shared by more than one country, such as cricket by six former British colonies in the Caribbean. Some others have been established to protect an historical heritage, such as tejo in Colombia. Note also that Canada has two designations, one for winter and one for summer.

*Source:* The information on sports was taken from Wikipedia, http://en.wikipedia.org/wiki/National_sport (accessed March 3, 2009)




other sports have sometimes replaced national sports in popularity, such as cricket's replacement of field hockey as India's most popular sport.

Further, the International Baseball Federation now has over 100 member countries, even though baseball was popular only in its North American birthplace for most of its history. As TV revenues flattened in North America, Major League Baseball (MLB) began broadcasting games to international audiences. Increased exposure not only broadened the global fan base, but it also showed youngsters all over the world how the game was played. As late as 1986, only 14 percent of MLB players were born outside the United States; by 2010, that number had climbed to almost 28 percent. The average MLB clubhouse is now a bastion of multilingual camaraderie, with players and coaches talking baseball in Spanish, Japanese, and Korean as well as English.

## THE WIDE WORLD OF TELEVISED SPORTS

Not surprisingly, other professional sports groups have expanded their global TV coverage (and marketing programs). Most viewers of Stanley Cup hockey watch from outside North America. Fans watch National Association for Stock Car Auto Racing (NASCAR) races in more than 120 countries and NBA games in about 200. If you lived in Tunisia and enjoyed simultaneous access to multiple TV channels, you could watch more hours of NBA action than there are hours in the year.

And TV isn't the only means by which sports organizations are seeking foreign fan bases and players. For several years, the National Football League (NFL) of the United States sponsored a now-defunct professional league in Europe. It continues to underwrite flag-football programs in Chinese schools, and it is playing some regular NFL games in Europe. The NBA has appointed a director of basketball operations for India to help build youth leagues there. With the growth of broadband, we'll soon enter the realm of thousand-channel TV, where we'll be able to tune into sporting events that currently appeal only to highly localized niche markets. How about Thai boxing or Japanese sumo wrestling?

## The Top-Notch Pro as Upscale Brand

Relatedly, many top players (and teams) are effectively global brands. Philippine boxer Manny Pacquiao, Finnish auto racer Kimi Raikkonen, Portuguese soccer player Cristiano Ronaldo, and American tennis star Serena Williams are so popular globally that companies within and outside the sports industry are willing to pay them millions of dollars for endorsing clothes, equipment, and other products.

## Promotion as Teamwork

A few teams, such as the New York Yankees in baseball, the New Zealand All Blacks in rugby, and Manchester United (Man U) in soccer also have enough brand-name cachet to sell clothing and other items to fans around the world. Just about every team can get something for the rights to use its logo, and some teams have enough name recognition to support global chains of retail outlets. Similarly, companies both sponsor and seek endorsements from well-known teams. For instance, Nike, the U.S. sports shoes and apparel giant, has fought hard to become the top sportswear and equipment supplier to European soccer teams. The success of this campaign has had such a big influence on Nike's international sales efforts that it now takes in more money abroad than in the United States.

Many nonsports companies, such as Canon (cameras, office equipment), Sharp (consumer electronics), and Carlsberg (beer), sponsor teams mainly to get corporate logos emblazoned on uniforms. Still others, such as United Airlines in Chicago, pay for the naming rights to arenas and other venues. And, of course, teams themselves can be attractive international investments. For instance, the owners of the Boston Red Sox baseball team (U.S.A.) bought the Liverpool Football Club of the United Kingdom.

## Sports and You

What does all this mean to you as a sports fan? Chances are—especially if you're a male—you fantasized at one time about going pro in some sport, but you've probably given up that fantasy and settled into the role of spectator. Now that pro sports has become a global phenomenon (thanks to better communications), you can enjoy a greater variety—and a higher level of competition—than any generation before you.

That's the upside, but we must point out that people don't always take easily to another country's sport. Despite many efforts, cricket has never become popular in the United States. It became popular in many countries during centuries of British colonialism, but it has made no recent inroads internationally. Nor has American football gained much popularity outside the United States. A former NFL lineman expressed a reason: that rules for American football and cricket are so complicated that one must learn them as children. However, basketball and soccer have traveled to new markets more easily because they are easier to understand and require no specialized equipment.

Further, there is disagreement about the economic effect of successfully winning a bid to host big international competitions such as the World Cup and Olympics. On the one hand, the events bring in tourists and they publicize to the world (especially potential investors) the opportunities that might exist in the host location. They also help spur the construction of infrastructure that will speed future economic growth. On the other hand, hosts may spend on stadiums and facilities that have no use afterward. Finally, few competitions have ended without substantially increasing local and national debt.

Nor is everyone happy with the unbridled globalization of sports—or at least with some of the effects. Brazilian soccer fans lament the loss of their best players, and U.S. fans and public officials protested the sale of the MLB Seattle Mariners to a foreign investor.

# Introduction

In its broadest sense, **globalization** refers to the widening set of interdependent relationships among people from different parts of a world that happens to be divided into nations. The term can also refer to the integration of world economies through the elimination of barriers to movements of goods, services, capital, technology, and people.[2] Throughout recorded history, human connections over ever-wider geographic areas have expanded the variety of available resources, products, services, and markets. We've altered the way we want and expect to live, and we've become more deeply affected (positively and negatively) by conditions outside our immediate domains.

The opening case shows how far-flung global contact allows the world's best sports talent to compete—regardless of nationality—and the fans to watch them, from almost anywhere. The changes that have led firms to consider ever more distant places as sources of supplies and markets affect almost every industry and their consumers. We may not always know it, but we commonly buy products from all over the world. "Made in" labels do not tell us everything about product origins. So many different components, ingredients, and specialized business activities go into products that it's often a challenge to say exactly where they were made. For example, because Apple's iPhones are shipped from China they appear to be Chinese products, but less than 4 percent of their value is performed in China.[3]

Here's an interesting example of interdependent relationships. One of 2010's biggest stories and one that was watched on TV worldwide was the rescue of Chilean miners, but the rescue would have been impossible without the innovations and products from a variety of countries—the Center Rock drill bit from the United States, a high-strength cable from Germany, a super-flexible fiber optics communications cable from Japan, and a special cell phone from South Korea.[4]

## HOW DOES *INTERNATIONAL BUSINESS* FIT IN?

International business consists of all commercial transactions between two or more countries.

- The goal of private business is to make profits.
- Government business may or may not be motivated by profit.

Globalization enables us to get more variety, better quality, or lower prices. Our daily meals contain spices that aren't grown domestically and fresh produce that's out of season in one local climate or another. Our cars cost less than if all the parts were made and the labor performed in one place. All of these connections between supplies and markets result from the activities of **international business,** defined as all commercial transactions, including sales, investments, and transportation, that take place between two or more countries. Private companies undertake such transactions for profit; governments may undertake them either for profit or for other reasons.

**The Study of International Business** Why should we study international business? Simply, it comprises a large and growing portion of the world's total business. Global events and competition affect almost all companies, large and small, regardless of industry, as a result of selling output to and securing supplies and resources from foreign countries, as well as competing against products and services from abroad. Thus, most managers need to approach their operating strategies from an international standpoint. Recall the NBA teams in the opening case, which are looking globally for human resources—on-court talent—and additional markets that exist abroad. As a manager in almost any industry, you'll need to consider (1) where to obtain the inputs you need of the required quality and at the best possible price and (2) where you can best sell the product or service you've put together from those inputs.

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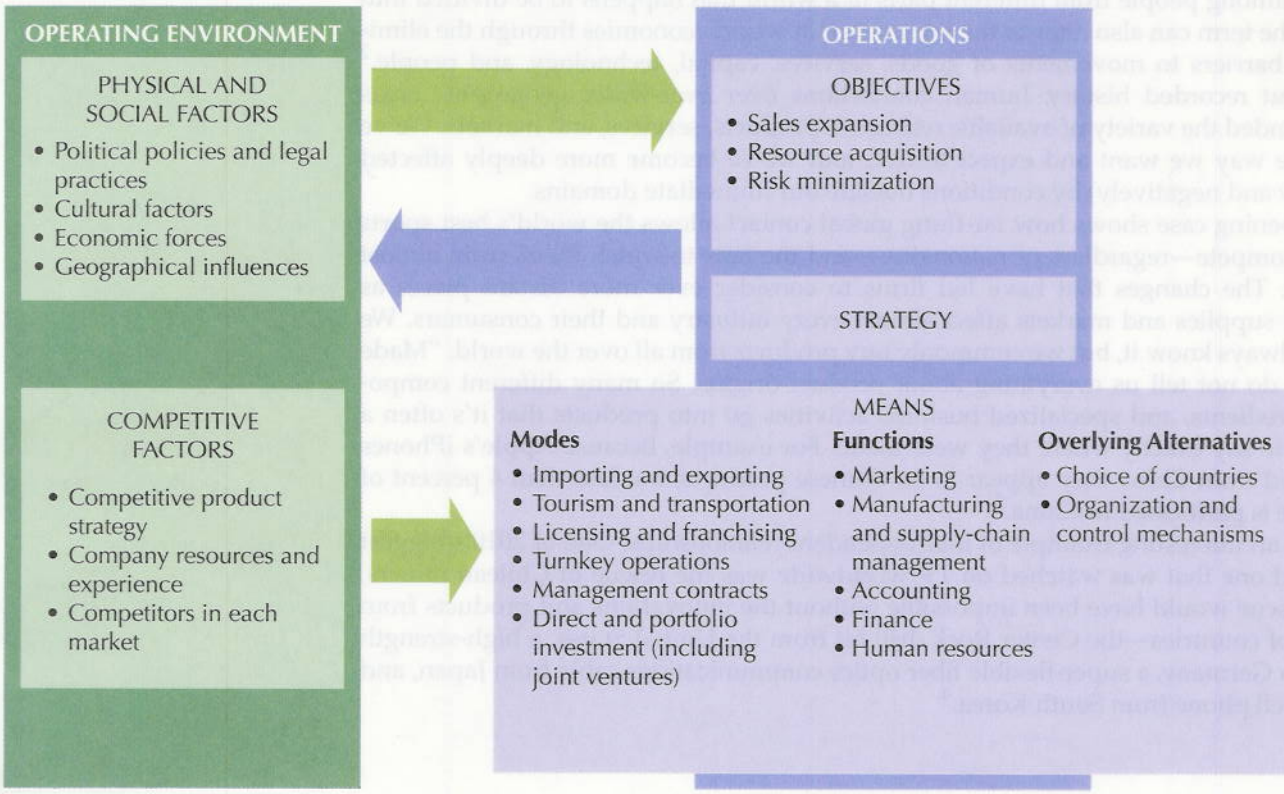
**Understanding the Environment/Operations Relationship** The best way of doing business abroad may not be the same as the best way at home. Why? First, when your company operates internationally, it will engage in *modes* of business, such as exporting and importing, that differ from those in which it engages domestically. Second, physical,

FIGURE 1.1 Factors in International Business Operations

The conduct of a company's international operations depends on two factors: its objectives and the means by which it intends to achieve them. Likewise, its operations affect, and are affected by, two sets of factors: physical/social and competitive.




Studying international business is important because

- Most companies either are international or compete with international companies.
- Modes of operations may differ from those used domestically.
- The best way of conducting business may differ by country.
- An understanding helps you make better career decisions.
- An understanding helps you decide what governmental policies to support.

social, and competitive conditions differ among countries and affect the optimum ways to conduct business. Thus, companies operating internationally have more diverse and complex operating environments than those that conduct business only at home. Figure 1.1 outlines the complex set of relationships among conditions and operations that may occur when a firm decides to conduct some of its business on an international scale.

Even if you never have direct international business responsibilities, understanding some of the complexities may be useful to you. Companies' international operations and their governmental regulations affect overall national conditions—profits, employment security and wages, consumer prices, and national security. A better understanding of international business will help you make more informed operational and civic decisions, such as where you want to operate and what governmental policies you want to support.

## The Forces Driving Globalization

Globalization

- Has been growing.
- Is less pervasive than generally thought.
- Has economic and non economic dimensions.
- Is stimulated by several factors.

Measuring globalization is problematic, especially for historical comparisons. First, a country's interdependence must be measured indirectly.[5] Second, when national boundaries shift, such as in the breakup of the former Soviet Union or the reunification of East and West Germany, domestic business transactions can become international transactions and vice versa. Nevertheless, various reliable indicators assure us that globalization has been increasing, at least since the mid-twentieth century. Currently, over 20 percent of world production is sold outside its country of origin, compared to about 7 percent in 1950. Restrictions on imports have generally been decreasing, and output from foreign-owned investments as a percentage of world production has increased. In almost every year since World War II, world trade has grown more rapidly than world production. However, in recessionary periods, global trade and investment contract even more than the global economy, such as a fall in world trade of 21 percent between April 2008 and May 2009.

At the same time, however, globalization is less pervasive than you might suppose. In much of the world (especially poor rural areas), people lack the resources to establish more than the barest connection with anyone beyond the outskirts of their isolated domains. Only a few countries—mainly very small ones—either sell over half their production abroad or depend on foreign output for more than half their consumption. This means that most of the world's goods and services are still sold in the countries in which they're produced. Moreover, the principal source of capital in most countries is domestic rather than international.

Granted, these measurements address only *economic* aspects of global interdependence. Various studies have relied on different indicators for comparison.[6] One of the most comprehensive is the A.T. Kearney/Foreign Policy Globalization Index, which shows not only that some countries are more globalized than others but also that a given country may be highly globalized on one dimension and not another. This index ranks countries across four dimensions:

- *Economic*—international trade and investment
- *Technological*—Internet connectivity
- *Personal contact*—international travel and tourism, international telephone traffic, and personal transfers of funds abroad
- *Political*—participation in international organizations and government monetary transfers

In recent years, the index has ranked Singapore and Hong Kong as the most globalized countries and India and Iran as the least. The U.S. ranking shows how globalization can differ by dimension: first on the technological scale but almost last on the economic.[7]

## FACTORS IN INCREASED GLOBALIZATION

What factors have contributed to the growth of globalization in recent decades? Most analysts cite the following seven factors:

1. Increase in and application of technology
2. Liberalization of cross-border trade and resource movements
3. Development of services that support international business
4. Growing consumer pressures
5. Increased global competition
6. Changing political situations
7. Expanded cross-national cooperation

These factors are, of course, interrelated, and each deserves a closer look.

**Increase in and Application of Technology** Many of the proverbial "modern marvels" and efficient means of production have come about from fairly recent advances in technology that have occurred in many different countries. Thus, much of what we trade today did not exist a decade or two ago and cannot easily be produced in our own countries. The increased demand due to rising productivity means, on average, people produce and can buy more by working the same number of hours. In addition, more than half the scientists who have ever lived are alive today. One reason, of course, is population growth. But another is economic growth, which frees up more people to *develop* new products because fewer people can *produce* them. As the base of our technology expands, new product development accelerates and we need more scientists and engineers to work on technical applications.

Further, much new technical innovation takes so much financial and intellectual resources that companies must cooperate to take on portions of development. These efforts may necessitate collaboration among firms in different countries that have financial resources and specialized capabilities. Once new products are developed, the optimum scale size of production seldom corresponds with the market demand in a single country. Consequently, companies must sell both domestically and internationally in order to spread the fixed developmental and production costs over more units of production.

***Advances in Communications and Transportation*** Strides in communications and transportation now permit us to learn about and want products and services developed in other parts of the world. Moreover, the costs of these improvements have risen more slowly in most years than costs in general. A three-minute phone call from New York to London that cost $10.80 in 1970 costs less than $0.20 today, while a call using Voice over Internet Protocol (VoIP) is virtually free.

Innovations in transportation mean that more countries can compete for sales to a given market. For example, the sale of foreign-grown flowers in the United States used to be impractical; today, however, flowers from as far away as Ecuador, Israel, the Netherlands, and New Zealand compete with each other for the U.S. market because growers can ship them quickly and economically.

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Or recall the opening case. Innovations allow individual athletes and teams to go head to head at venues around the world and sports media to broadcast competitions to fans everywhere. If it weren't for modern means of transportation, a tennis pro couldn't play in Morocco right after finishing a tournament in Miami. And if it weren't for modern means of advertising to fans around the globe, the prize money wouldn't be big enough to induce players to do all that traveling.

Improved communications and transportation not only speed up interactions, they also enhance a manager's ability to oversee foreign operations. Thanks to the Internet, even small companies can reach global customers and suppliers. Atlanta's Randy Allgaier, for example, has established a partnership in Taiwan that contracts a Chinese factory to manufacture lighting fixtures for him—all this without his need for costly on-site contact with people in either Taiwan or China.[8]

**Liberalization of Cross-Border Trade and Resource Movements** To protect its own industries, every country restricts the movement across its borders of not only goods and services but also the resources—workers, capital, tools, and so on—needed to produce them. Such restrictions, of course, set limits on international business activities and, because regulations can change at any time, contribute to a climate of uncertainty. Over time, however, most governments have reduced such restrictions, primarily for three reasons:

1. Their citizens want a greater variety of goods and services at lower prices.
2. Competition spurs domestic producers to become more efficient.
3. They hope to induce other countries to lower their barriers in turn.

**Development of Services That Support International Business** Companies and governments have developed a variety of services that facilitate international business. Take the sale of goods and services in a foreign country and currency. Today, because of bank credit agreements—clearing arrangements that convert one currency into another and insurance that covers such risks as nonpayment and damage en route—most producers can be paid relatively easily for goods and services sold abroad. What happens, for instance, when Nike sells sportswear to a French soccer team? As soon as the shipment arrives at French customs (probably from somewhere in Asia), a bank in Paris collects payment in euros from the soccer team and pays Nike in U.S. dollars through a U.S. bank.

**Growing Consumer Pressures** Not only do consumers know more today about products and services available in other countries, but also many more can afford to buy products that were once considered luxuries. We want more, newer, better products, and we want them more finely differentiated. As usually occurs, such greater affluence is spread unevenly, both among and within countries as well as from year to year, but more and more companies are now responding to those markets where incomes and consumption are growing most rapidly, such as China.

Greater affluence has also spurred companies to spend more heavily on research and development (R&D) and to search worldwide—via the Internet, industry journals, trade fairs, and trips abroad—for innovations and products they can sell to ever-more-demanding consumers. By the same token, consumers are more proficient today at scouring the globe for better deals; such as U.S. consumers' Internet-searches for lower-priced prescription drugs abroad.

**Greater Global Competition** The present and potential pressures of increased foreign competition can persuade companies to buy or sell abroad. For example, a firm might introduce products into markets where competitors are already gaining sales, or seek supplies where competitors are getting cheaper or more attractive products or the means to produce them.

In recent years, many companies have merged or acquired firms to gain operating efficiencies that enable them to compete with or become global leaders, such as the merger between the Brazilian firms Perdigão and Sadia to create BRF-Brasil Foods, a major exporter of chilled and frozen foods.[9] So-called **born-global companies** start out with a global focus because of their founders' international experience[10] and because advances in communications give them a good idea of where global markets and supplies are. Many new companies locate in areas with numerous competitors and suppliers—a situation known as **clustering** or **agglomeration**—where they quickly learn of foreign opportunities and gain easier access to the resources needed for international moves.[11]

Regardless of industry, firms and individuals have to become more global; in today's competitive business environment, failure to do so can be catastrophic. (Figure 1.2 shows this humorously.) Once a few companies have responded to foreign opportunities, others inevitably follow suit. And they learn from each other's foreign experiences. As the opening case suggests, for example, the early success of foreign-born baseball players in U.S. leagues undoubtedly spurred American basketball and football organizations to begin looking for and developing talent abroad.[12]

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FIGURE 1.2 International Business as a Two-Edged Sword

Although global competition promotes efficiency, it obliges both companies and their employees to spend time and effort on a greater range of activities.

*Source:* © 1998 The New Yorker Collection, Roz Chast, from cartoonbank.com. 

**Changing Political Situations** A major reason for growth in international business is the end of the schism between Communist countries and the rest of the world. For nearly half a century after World War II, business between the two camps was minimal. Today, only a few countries do business almost entirely within a political bloc.

Another political factor is the willingness of governments to support programs, such as improving airport and seaport facilities, that have fostered speed and cost efficiencies for delivering goods internationally. Governments now also provide an array of services to help domestic companies sell more abroad, such as collecting information about foreign markets, furnishing contacts with potential buyers, and offering insurance against nonpayment in the home-country currency.

**Expanded Cross-National Cooperation** Increasingly, governments have come to realize that their own interests can be addressed through international cooperation by means of treaties, agreements, and consultation. The willingness to pursue such policies is due largely to these three needs:

1. To gain reciprocal advantages
2. To attack problems jointly that one country acting alone cannot solve
3. To deal with areas of concern that lie outside the territory of any nation

***Gain Reciprocal Advantages*** Essentially, companies don't want to be at a disadvantage when operating internationally, so they petition their governments to act on their behalf. Thus, governments join international organizations and sign treaties and agreements for a variety of commercial activities, such as transportation and trade.

Some treaties and agreements allow the countries' commercial ships and planes to use certain seaports and airports in exchange for reciprocal port use. Some cover commercial-aircraft safety standards and flyover rights; some protect property, such as foreign-owned investments, patents, trademarks, and copyrights. Countries also enact treaties for reciprocal reductions of import restrictions (remaining prepared, of course, to retaliate when another party interferes with trade flows by raising trade barriers or cutting diplomatic ties).

***Multinational Problem Solving*** Countries often act to coordinate activities along their mutual borders, building highways and railroads or hydroelectric dams that serve the interests of all parties. They also cooperate to solve problems that they either cannot or will not solve by themselves, for several reasons. First, the resources needed to solve the problem may be too great for one country to manage; sometimes no single country is willing to pay for a project that will also benefit another country, as witnessed by Japan and the United States sharing the costs of ballistic-missile defense technology. In any case, many problems are inherently global—think of, for example, global climate change or nuclear proliferation—and can't be easily addressed by a single country. That's why cooperative efforts have developed to fight the spread of diseases such as malaria, to set warning systems against such natural disasters as tsunamis, and to take actions affecting environmental problems such as global warming.

Second, one country's policies may affect those of others. Higher real-interest rates in one country, for example, can attract funds very quickly from individuals and firms in countries with lower rates, thus creating a shortage of investment funds in the latter. Similarly, companies may change suppliers in one country for those in another as costs change, thus contributing to unemployment in the country where they abandon suppliers. To coordinate economic policies in these and other areas, the most economically important countries meet regularly to share information and pool ideas.[13]

***Areas Outside National Territories*** Three global areas belong to no single country: the noncoastal areas of the oceans, outer space, and Antarctica. Until their commercial viability was demonstrated, they excited little interest for either exploitation or multinational cooperation. The oceans, however, contain food and mineral resources and constitute the surface over which much international commerce passes. Today, we need agreements to specify the amounts and methods of fishing to be allowed, to address questions of oceanic mineral rights (such as on oil resources below the Arctic Ocean), and to deal with piracy of ships.

Likewise, there is disagreement on the commercial benefits to be reaped from outer space. Commercial satellites, for example, pass over countries that receive no direct benefit from them but argue that they should. If that sounds a little far-fetched, remember that countries do charge foreign airlines for flying over their territories.[14]

Antarctica, with minerals and abundant sea life along its coast, attracts thousands of tourists each year, has a highway leading to the South Pole, and has thus been the subject of agreements to limit commercial exploitation. However, there is still disagreement about the continent's development—how much there should be and who does it.

Much of the cooperation we've described has been undertaken by international organizations, which we discuss in more detail in later chapters, especially in Chapter 8.

## The Costs of Globalization

Although we've discussed seven interrelated reasons for the rise in international business and globalization, we should remember that the consequences of the rise remain controversial. To thwart the globalization process, *antiglobalization* forces regularly protest international conferences and governmental policies—sometimes violently. The adjacent photo shows such a protest. We focus here on three issues: *threats to national sovereignty, growth and environmental stress,* and *growing income inequality and personal stress.* We revisit these and others in more depth later; watch for them also in several of our Point-Counterpoint features.


This is part of an anti-globalization protest in London, England in 2011.
*Source:* © photocritical/iStockphoto.com

Critics of globalization claim

- Countries lose sovereignty.
- The resultant growth hurts the environment.
- Some people lose both relatively and absolutely.

## THREATS TO NATIONAL SOVEREIGNTY

You've probably heard the slogan "Think globally, act locally." In essence, it means that local interests should be accommodated before global ones. Some observers worry that the proliferation of international agreements, particularly those that undermine local restrictions on how goods are produced and sold, will diminish a nation's **sovereignty**—its freedom to "act locally" and without externally imposed restrictions.

**The Question of Local Objectives and Policies** Countries seek to fulfill their citizens' economic, political, and social objectives by setting rules reflecting national priorities, such as those governing worker protection and environmental practices. However, some critics argue that individual countries' priorities are undermined by opening borders to trade. For example, if a country has stringent regulations on labor conditions and requires clean production methods, companies may produce where they can cut costs because of less rigorous rules. The result, if imports can enter freely, may be that the strict country must forgo its priorities or face the downside of fewer jobs and tax receipts.

**The Question of Small Economies' Overdependence** In addition, critics say that small economies depend so much on larger ones for supplies and sales that they are vulnerable to foreign demands, including everything from defending certain positions at the United Nations to supporting a large economy's foreign military or economic actions. Nobel economist George Akerlof has noted that consequences of this dependence are intensified by poor countries' inadequate administrative capacity to deal with globalization.[15] These countries are also concerned that large international companies are powerful enough to dictate their operating terms (say, by threatening to relocate), exploit legal loopholes to avoid political oversight and taxes, and counter the small economies' best interests by favoring their home countries' political and economic interests.

**The Question of Cultural Homogeneity** Finally, critics charge that globalization homogenizes products, companies, work methods, social structures, and even language, thus undermining the cultural foundation of sovereignty. In Chapter 2 we'll see that, as international differences diminish, countries find it harder to maintain the traditional ways of life that unify and differentiate their cultures. Recall in our opening case that despite countries' designation of national sports to maintain tradition, some are losing out to imported sports anyway. Fundamentally, many critics feel helpless when it comes to stopping the incursion of foreign influences by such means as satellite television, print media, and Internet sites.[16]

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## ECONOMIC GROWTH AND ENVIRONMENTAL STRESS

Much criticism of globalization revolves around the economic growth it brings. According to one argument, growth consumes more nonrenewable natural resources and increases environmental damage—despoliation through toxic runoffs into rivers and oceans, air pollution from factory and vehicle emissions, and deforestation that can affect weather and climate.

**The Argument for Global Growth and Global Cooperation** Not everyone agrees with such a conclusion. Others argue that globalization has positive results for both sustaining natural resources and maintaining an environmentally sound planet. Global cooperation, they say, fosters superior and uniform standards for combating environmental problems, while global competition encourages companies to seek resource-saving and eco-friendly technologies, such as automobiles that use less gas and emit fewer pollutants. However, unless the positive results of globalization are seen as outpacing the negative, sustaining economic growth will remain a problem in the future.

The pursuit of global interests may even conflict with what a country's citizens think is best for themselves. Consider, for instance, the effect of global pressure on Brazil to curtail logging activity in the Amazon region to help protect the world's climate. Unemployed Brazilian workers have felt that job creation in the logging industry is more important than climate protection outside Brazil.

## GROWING INCOME INEQUALITY AND PERSONAL STRESS

In measuring economic well-being, we look not only at our absolute situations but also compare ourselves to others. We generally don't find our economic status satisfactory unless we're doing better *and* keeping up with others.

**Income Inequality** By various measurements, income inequality has been growing both among and within a number of countries. Critics claim that globalization has affected this disparity by helping to develop a global superstar system, creating access to a greater supply of low-cost labor, and developing competition that leads to winners and losers.

The superstar system is especially apparent in sports, where global stars earn far more than the average professional player or professionals in sports with a more limited worldwide following. It also carries over to other professions, such as business, where charismatic top people can command many times what others can.

Although globalization has brought unprecedented opportunities for firms to profit by gaining more sales and cheaper or better supplies, critics argue that profits have gone disproportionately to the top executives rather than to the rank and file. Nobel economist Robert Solow supports this criticism by arguing that greater access to low-cost labor in poor countries has reduced the real wage growth of labor in rich countries.[17] And even if overall worldwide gains from globalization are positive, there are bound to be some losers in either an absolute or relative sense (who will probably become critics of globalization). The speed with which technology and competition expand globally affects the number of winners and losers along with the relative positions of individuals, companies, and countries. As an example, relocation of U.S. manufacturing jobs to China and India have helped the latter grow more rapidly than the United States, thus lessening the U.S.'s *relative* economic leadership over those countries.[18] Likewise, some displaced workers have lost economic and social standing relative to workers whose jobs were not moved. The challenge, therefore, is to maximize the gains from globalization while simultaneously minimizing the costs borne by the losers.

**Personal Stress** Certain repercussions of globalization can't be measured in strictly economic terms. What about the stress imposed on the people whose relative economic and social status suffers, or those who fear the loss of their jobs?[19] There is some evidence that the growth in globalization goes hand in hand not only with increased insecurity about job and social status but also with costly social unrest.[20] Further, although few of the world's problems are brand new, we may worry about them more now because globalized communications bring exotic sagas of misery into living rooms everywhere.[21]

**Point** **Is Offshoring Good Strategy?**

**Point** **Yes** **Offshoring** is the shifting of production to a foreign country. *If offshoring succeeds in reducing costs, it's good.* This is happening with many companies. Most branded clothing companies offshore to have work done by cheaper sewing machine operators. Many investment companies, such as Fidelity in India, are hiring back-office workers in poor countries to cut the cost of industry research. What good are cost savings? It's basic. If you can cut your costs, you can cut your prices or improve your product. For example, by offshoring work to India, Claimpower, a small U.S. medical-insurance billing company, cut costs, lowered the prices it charges doctors, quadrupled its business in two years, and hired more U.S. employees because of the growth.[22]

What's the main complaint about offshoring? Too many domestic jobs end up abroad. As we discuss this, keep in mind that employment results from offshoring are difficult to isolate from other employment changes. Sure, unemployment in most high-income countries increased substantially in the 2008–2009 period, but this was probably due mainly to improvements in production technology and the global recession. However, I'll try to pinpoint direct results of offshoring.

IBM is a good example. Over 70 percent of its nearly 400,000 employees are based outside the United States.

By shipping some of its programming work abroad, IBM saves a tidy $40 an hour per worker—which comes out to $168 million a year.[23] Analysts agree that IBM's competitors in low-wage countries, such as Infosys from India, can underprice IBM with competitive products and services if IBM fails to offshore.[24] Moreover, when you become price-competitive, you sell more at home and in foreign countries by exporting to them. You may also increase sales abroad if you locate near foreign customers. As you *create* jobs in this process, you improve your chances of survival.[25] For instance, IBM is actually saving jobs by offshoring. Again, it's basic business: Cost savings generate growth, and growth creates more jobs.[26]

And not just any jobs: This process lets companies create more *high-value* jobs at home—the ones performed by people like managers and researchers, who draw high salaries. When that happens, demand for qualified people goes up. In the United States, that process has already resulted in a higher percentage of white-collar and professional employees in the workforce. These are *high-income* people, and more of them are employed as a result of sending *low-income* jobs to countries with lower labor costs.[27]

Further, offshoring is a natural extension of *outsourcing,* the process of companies contracting work to other companies so that they can concentrate on what they do best.[28] This contributes to making a company more efficient. What is the difference, then, of outsourcing to a domestic versus a foreign company?

Admittedly, workers do get displaced from offshoring, but *aggregate* employment figures show that these workers find other jobs the same as do workers who get displaced for other reasons. In a dynamic economy, people are constantly shifting jobs. Doing so because of outsourcing is no different from doing so for any other reason, such as a company deciding to invest in some laborsaving technology. In any case, because there are bound to be upper limits on the amount of outsourcing work a country can do, the direst predictions about job loss are exaggerated: There simply aren't enough unemployed people abroad who have the needed skills *and* who will work at a sufficiently low cost.

Offshoring isn't for all companies or all types of operations. Some companies are bringing many operations *back* from abroad because of such factors as poor quality, consumer pressure, and concerns about competitive security. In fact, about a fifth of the companies that have gone to offshoring now say that the savings are less than they expected.[29] And that brings us back to what we said explicitly at the outset: Offshoring works when you cut operating costs *effectively.*

**Is Offshoring Good Strategy?**

## Counterpoint

**No** Some things are good for some of the people some of the time, and that's *almost* the case with offshoring, which unfortunately is good for only a *few* people but not for *most.* I keep hearing about the cost savings, but when I buy goods or services I rarely find anything that's cheaper than it used to be. Whether buying a Ralph Lauren shirt, getting medical services from a doctor who is saving money through Claimpower, or having Fidelity manage my assets, I have seen no lower prices for me. Further, Claimpower's growth had to be at the expense of other companies in the business, not because of growth in the number of people getting medical services because of price decreases.

I know of one study that took a close look at 17 high-income countries and found that, in aggregate, the percentage of national income going to labor has gone down while the percentage of national income going to profits has gone up.[30]

Here's one of the key problems: When you replace jobs by offshoring, you're exchanging *good* jobs for *bad* ones. Most of the workers who wind up with the short end of the offshoring stick struggled for decades to get reasonable work hours and a few basic benefits, such as healthcare and retirement plans. More important, their incomes allowed them to send their kids to college, and the result was an upwardly mobile—and productive—generation.

## Counterpoint

Now many of these employees have worked long and loyally for their employers and what do they have to show for it in the offshoring era? Yes, I know that governments give them unemployment benefits but these never equal what the employees had before, and they run out.[31] On top of everything else, they may have no other usable skills, and at their ages, who's going to foot the bill for retraining them? The increase in what you call "high-value jobs" doesn't do *them* any good.

Offshoring may lead to short-term cost savings, but many studies indicate that it merely diverts companies' attention from taking steps to find innovative means of more efficient production, such as better operating techniques and machinery.[32] Concentrating on these latter alternatives may cut costs, increase production, and maintain the jobs that are going abroad.

While we're on the subject of job "value," what kinds of jobs *are* we creating in poor countries? Because countries are competing with lower wages, it encourages them to keep wages from rising, a sort of race to the bottom. However, MNEs no doubt pay workers in low-wage countries more than they could get otherwise, and I'll grant that some of these jobs—the white-collar and technical jobs—are pretty good. But for most people, the hours are long, the working conditions are barbaric, and the pay is barely enough to survive on. There is also little job security. As salaries creep up where companies are offshoring, the companies merely move to even cheaper places to get the job done. For instance, this is what happened to workers in the island country of Mauritius. As soon as Mauritians began to think they might expect a better way of life, MNEs found workers elsewhere to do their sewing.[33]

Admittedly, in a dynamic economy, people have to change jobs more often than they would in a stagnant economy—*but not to the extent caused by offshoring.* There's still some disagreement about the effects of off-shoring on a country's employment rate. Researchers are still looking into the issue, but what they're finding are that more of the so-called better jobs are also being outsourced. A study of 2,700 major U.S. and European organizations showed that 700,000 finance, IT, and other high level jobs were outsourced in 2009 and that another 250,000 per year will be outsourced through 2014.[34] Researchers are finding data like these: About 11 percent of U.S. jobs are at risk of being offshored—nearly 2 million of them in accounting-related fields alone.[35] So are we really creating higher-level jobs? Here's the bottom line: In countries like the United States, workers simply aren't equipped to handle the pace of change when it means that jobs can be exported faster than the average worker can retrain for different skills.

# Why Companies Engage in International Business

Let's now focus on some of the specific ways firms can create value by going global. Take another look at Figure 1.1, where you'll see three major operating objectives that underlie the reasons for engaging in international business:

- Expanding sales
- Acquiring resources
- Reducing risk

Normally, these three objectives guide all decisions about whether, where, and how to engage in international business. Let's examine each of them in more detail.

## EXPANDING SALES

A company's sales depend on the desire and ability of consumers to buy its goods or services. Obviously, there are more potential consumers in the world than found in any single country. Now, higher sales ordinarily create value, but only if the costs of making the additional sales don't increase disproportionately. Recall, for instance, the opening case. Televising sports competitions to multiple countries increases costs only marginally while generating advertising revenue in excess of these marginally increased costs. In fact, additional sales from abroad may enable a company to reduce its per-unit costs by covering its fixed costs—say, up-front research costs—over a larger number of sales. Because of lower unit costs, it can boost sales even more.

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So increased sales are a major motive for expanding into international markets, and many of the world's largest companies—such as Volkswagen (Germany), Ericsson (Sweden), IBM (United States), Michelin (France), Nestlé (Switzerland), and Sony (Japan)—derive more than half their sales outside their home countries.[36] Bear in mind, however, that international business is not the purview only of large companies. In the United States, 41 percent of export value is by small and mid-sized firms (SMMs) from a combination of their direct exports plus their sales of components to large companies, which install them in finished products slated for sale abroad.[37]

Pursuing international sales usually increases the potential market and potential profits.

## ACQUIRING RESOURCES

Producers and distributors seek out products, services, resources, and components from foreign countries—sometimes because domestic supplies are inadequate (as with crude oil shipped to the United States). They're also looking for anything that will create a

Foreign sources may give companies
- Lower costs.
- New or better products.
- Additional operating knowledge.

competitive advantage. This may mean acquiring a resource that cuts costs, such as Rawlings' reliance on labor in Costa Rica—a country that hardly plays baseball—to produce baseballs.

Sometimes firms gain competitive advantage by improving product quality or differentiating their products from those of competitors; in both cases, they're potentially increasing market share and profits. Most automobile manufacturers, for example, hire design companies in northern Italy to help with styling. Many companies establish foreign R&D facilities to tap additional scientific resources.[38] Companies also learn while operating abroad. Avon, for instance, applies know-how from its Latin American marketing experience to help sell to the U.S. Hispanic market.[39]

### REDUCING RISK

International operations may reduce operating risk by

- Smoothing sales and profits.
- Preventing competitors from gaining advantages.

Operating in countries with different business cycles can minimize swings in sales and profits. The key is the fact that sales decrease or grow more slowly in a country that's in a recession and increase or grow more rapidly in one that's expanding economically. During 2008, for example, General Motors' U.S. sales fell 21 percent, but this was partially offset by its sales growth of 30 percent in Russia, 10 percent in Brazil, and 9 percent in India.[40] Moreover, by obtaining supplies of products or components both domestically and internationally, companies may be able to soften the impact of price swings or shortages in any one country.

Finally, companies often go international for defensive reasons. Perhaps they want to counter competitors' advantages in foreign markets that might hurt them elsewhere. By operating in Japan, for instance, Procter & Gamble (P&G) delayed foreign expansion on the part of potential Japanese rivals by slowing their amassment of resources needed to expand into other international markets where P&G was active.

Similarly, British-based Natures Way Foods followed a customer, the grocery chain Tesco, into the U.S. market. This move expanded its sales and its relationship with Tesco. Moreover, it reduced the risk that Tesco would find an alternative supplier who might then threaten Natures Way's relationship with Tesco in the U.K. market.

## Modes of Operations in International Business

When pursuing international business, an organization must decide on one of the suitable *modes of operations* included in Figure 1.1 In the following sections, we discuss each of these modes in some detail.

### MERCHANDISE EXPORTS AND IMPORTS

Merchandise exports and imports are usually a country's most common international economic transactions.

Exporting and importing are the most popular modes of international business, especially among smaller companies. **Merchandise exports** are tangible products—goods—that are sent *out* of a country; **merchandise imports** are goods brought *into* a country. Because we can actually *see* these goods as they leave and enter the country, we sometimes call them *visible exports* and *imports*. The athletic shoes that an Indonesian plant sends to the United States are exports for Indonesia and imports for the United States. For most countries, the export and import of goods are the major sources of international revenues and expenditures.

### SERVICE EXPORTS AND IMPORTS

The terms *export* and *import* often apply only to *merchandise*. For non-merchandise *international earnings*, we use the terms **service exports** and **service imports.** The provider and receiver of payment makes a *service export;* the recipient and payer makes a *service* *import*. Services constitute the fastest growth sector in international trade. Service exports and imports take many forms, and in this section we discuss the most important:

- Tourism and transportation
- Service performance
- Asset use

Service exports and imports are international nonproduct sales and purchases.

- Examples of services are travel, transportation, banking, insurance, and the use of assets such as trademarks, patents, and copyrights.
- Service exports and imports are very important for some countries.
- They include many specialized international business operating modes.

**Tourism and Transportation** Let's say that the Williams sisters, Venus and Serena, take Air France from the United States to Paris to play in the French Open tennis tournament. Their tickets on Air France and travel expenses in France are service exports for France and service imports for the United States. Obviously, then, tourism and transportation are important sources of revenue for airlines, shipping companies, travel agencies, and hotels.

The economies of some countries depend heavily on revenue from these sectors. In Greece and Norway, for example, a significant amount of employment and foreign-exchange earnings comes from foreign cargo carried by Greek and Norwegian shipping lines. Tourism earnings are more important to the Bahamian economy than earnings from export of merchandise. (As we'll see in our closing case, year-round good weather enables Caribbean countries to benefit from passengers arriving on cruise ships.)

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**Service Performance** Some services, including banking, insurance, rental, engineering, and management services, net companies earnings in the form of *fees:* payments for the performance of those services. On an international level, for example, companies may pay fees for engineering services rendered as so-called **turnkey operations,** which are construction projects performed under contract and transferred to owners when they're operational. The U.S. company Bechtel currently has turnkey contracts in Peru and Saudi Arabia to build respectively a copper concentrator and aluminum smelter. Companies also pay fees for **management contracts**—arrangements in which one company provides personnel to perform general or specialized management functions for another. Disney receives such fees from managing theme parks in France and Japan.

**Asset Use** When one company allows another to use its assets—such as trademarks, patents, copyrights, or expertise—under contracts known as **licensing agreements,** they receive earnings called *royalties*. For example, Adidas pays a royalty for the use of the Real Madrid football team's logo on jackets it sells. **Royalties** also come from franchise contracts. **Franchising** is a mode of business in which one party (the *franchisor*) allows another (the *franchisee*) to use a trademark as an essential asset of the franchisee's business. As a rule, the franchisor (say, McDonald's) also assists continuously in the operation of the franchisee's business, perhaps by providing supplies, management services, or technology.

## INVESTMENTS

Dividends and interest paid on foreign investments are also considered service exports and imports because they represent the use of assets (capital). The investments themselves, however, are treated in national statistics as different forms of service exports and imports. Note that *foreign investment* means ownership of foreign property in exchange for a financial return, such as interest and dividends, and it may take two forms: *direct* and *portfolio*.

**Direct Investment** In **foreign direct investment (FDI),** sometimes referred to simply as *direct investment*, the investor takes a controlling interest in a foreign company. When, for example, U.S. investors bought the Liverpool Football Club, the football club became a U.S. FDI in the United Kingdom. Control need not be a 100 percent or even a 50 percent interest; if a foreign investor holds a minority stake and the remaining ownership is widely dispersed, no other owner may effectively counter the investor's decisions. When two or more companies share ownership of an FDI, the operation is a **joint venture.**

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Although the world's 100 largest international companies account for a high proportion of global output, the vast number of companies using FDI indicates that it's also common among smaller firms. Today, about 79,000 companies worldwide control about 790,000 FDIs in all industries.[41]

Key components of portfolio investment are

- Noncontrolling interest of a foreign operation.
- Financial benefit (e.g., loans).

**Portfolio Investment** A **portfolio investment** is a *noncontrolling* financial interest in another entity. It usually takes one of two forms: stock in a company or loans to a company (or country) in the form of bonds, bills, or notes purchased by the investor. They're important for most companies with extensive international operations, which routinely move funds from country to country for short-term financial gain.

## TYPES OF INTERNATIONAL ORGANIZATIONS

Basically, an "international company" is any company that operates internationally, but we have a variety of terms to designate different types of operations. Highly committed international companies usually draw on multiple operating types. Companies work together—in *joint ventures, licensing agreements, management contracts, minority ownership,* and *long-term contractual arrangements*—all of which are known as **collaborative arrangements.** The term **strategic alliance** is sometimes used to mean the same, but it usually refers either to an agreement that is of critical importance to one or more partners or to an agreement that does not involve joint ownership.

An MNE (sometimes called MNC or TNC) is a company with foreign direct investments.

**Multinational Enterprise** A **multinational enterprise (MNE)** usually refers to any company with foreign direct investments. This is the definition we use in this text. However, some writers reason that a company must have direct investments in some minimum number of countries to be an MNE. The term **multinational corporation or multinational company (MNC)** is often used as a synonym for MNE, while the United Nations uses the term **transnational company (TNC).**

***Does Size Matter?*** Some definitions require a certain size—usually giant. A small company, however, can have foreign direct investments and adopt any of the operating modes we've discussed. Of course, a small international company, if successful, becomes a large company. Vistaprint is a good example. Founded in 1995, its sales in 120 countries for 2010 were U. S. $670 million, of which 45 percent came from outside its U.S. domestic market.

# Why International Business Differs from Domestic Business

Managers in international business must understand social science disciplines and how they affect all functional business fields.

Let's now turn to the conditions in a company's *external environment* that may affect its international operations. Smart companies don't form or develop the means to implement international strategies without examining these conditions indicated in the left-hand side of Figure 1.1 and organized into the following categories:

- *Physical factors* (such as a country's geography or demography)
- *Social factors* (such as its politics, law, culture, and economy)
- *Competitive factors* (such as the number and strength of a company's suppliers, customers, and rival firms)

In examining these categories, we delve into the realm of the *social sciences,* which helps in explaining how external conditions affect patterns of behavior in different parts of the world.

## PHYSICAL AND SOCIAL FACTORS

The physical and social factors we show above can affect how companies produce and market products, staff operations, and even maintain accounts. Remember that any of these factors may require a company to alter its operation abroad (compared to domestically) for the sake of efficiency.

**Geographic Influences** Managers who are knowledgeable about geography are in a position to determine the location, quantity, quality, and availability of the world's resources, as well as ways to exploit them. The uneven distribution of resources throughout the world helps explain why different products and services are produced in different places. Further, countries differ in size of landmass and population. Because smaller countries have less access to varied domestic resources and large markets, they are usually more dependent on international trade than larger countries are.

Natural conditions affect where different goods and services can be produced.

Again, take sports. Norway fares better in the Winter Olympics than in the Summer Olympics because of its climate, and except for the well-publicized Jamaican bobsled team (whose members actually lived in Canada), tropical countries don't even compete in the Winter Olympics. East Africans' domination in distance races is due in part to their ability to train at higher altitudes than most other runners.

Geographic barriers—mountains, deserts, jungles, and so forth—often affect communications and distribution channels. And the chance of natural disasters and adverse climatic conditions (hurricanes, floods, droughts, earthquakes, volcanic eruptions, tsunamis) can make business riskier in some areas than in others, while affecting supplies, prices, and operating conditions in far-off countries, such as the one illustrated in the photos on page 20. Again, we can look ahead to our ending case, which shows that cruise-line operators must adjust their ports-of-call when hurricanes threaten. Keep in mind also that climatic conditions may have short- or long-term cycles. For instance, recent melting of Arctic ice floes along with new ship technologies have allowed more ships to use a Northwest Passage to cut transport costs by saving as much as 15 days at sea.[42]

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Finally, population distribution and the impact of human activity on the environment may exert strong future influences on international business, particularly if ecological changes or regulations cause companies to move or alter operations.

**Political Policies** Not surprisingly, a nation's political policies influence how international business takes place within its borders (indeed, *whether* it will take place). For instance, Cuba once had a minor-league baseball franchise, which went the way of diplomatic relations between Cuba and the United States back in the 1960s. Several Cuban baseball players are now members of professional U.S. teams, although most of them had to defect from Cuba to play abroad.

Obviously, political disputes—particularly military confrontations—can disrupt trade and investment. Even conflicts that directly affect only small areas can have far-reaching effects. The terrorist bombing of a hotel in Indonesia resulted in a decrease in tourism revenue and investment capital because individuals and businesses abroad perceived Indonesia as too risky.

Politics often determines where and how international business can take place.

**Legal Policies** Domestic and international laws play a big role in determining how a company can operate overseas. *Domestic law* includes both home- and host-country regulations on such matters as taxation, employment, and foreign-exchange transactions. British law, for example, determines how the U.S.-investor owned Liverpool Football Club is taxed and which nationalities of people it employs. Meanwhile, U.S. law determines how and when the earnings from the operation are taxed in the United States.

Each country has its own laws regulating business. Agreements among countries set international law.

*International law*—in the form of legal agreements between countries—determines how earnings are taxed by *all* jurisdictions. International law may also determine how

*Source:* © Jon Helgason/iStockphoto.com

A 2010 volcanic eruption in Iceland (above) affected business over a wide area, such as closing the airport in Zurich, Switzerland (below).


*Source:* Fedor Selivanov/Shutterstock.com

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(and whether) companies can operate in certain places. As we point out in our closing case, for example, agreements permit ships' crews to move about virtually anywhere without harassment.

Finally, the ways in which laws are *enforced* also affect a firm's foreign operations. In the realm of trademarks, patented knowledge, and copyrights, most countries have joined in international treaties and enacted domestic laws dealing with violations. Many, however, do very little to enforce either the agreements or their own laws. This is why companies not only must understand agreements and laws but must also determine how fastidiously they're enforced in different countries.

The interpersonal norms of a country may necessitate a company's alteration of operations.

**Behavioral Factors** The related disciplines of anthropology, psychology, and sociology can help managers better understand different values, attitudes, and beliefs. In turn, such understanding can help managers make operational decisions abroad.

Let's return once again to the opening case. Although professional sports are spreading internationally, the popularity of specific sports differs among countries. Interestingly, these differences affect the way the U.S. film industry treats sports as subject matter. As a rule, U.S. producers spare no expense to ensure that movies generate the greatest possible international appeal (and revenue). When it comes to sports-themed movies, however, they typically cut costs. Why? Because people in one country are usually lukewarm about other countries' sports, and moviemakers see little point in spending extra money trying to attract foreign audiences and revenues with these films.[43]

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We should also point out that sports rules sometimes differ among countries. The Japanese *do* care about U.S. baseball, but Japanese culture values harmony more than U.S. culture does, whereas U.S. culture values competitiveness more than the Japanese do. This is reflected in different baseball rules: A game in the United States continues until there is a winner, while Japanese are content with a tie if neither team is ahead after 12 innings.

**Economic Forces** Economics explains why countries exchange goods and services, why capital and people travel among countries in the course of business, and why one country's currency has a certain value compared to another's. Recall from our opening case that the percentage of non-U.S.-born players on major-league rosters has been increasing. Players from the Dominican Republic form the largest share of non-U.S.-born players, but even though baseball is quite popular in the Dominican Republic, the idea of putting a major-league baseball team there simply isn't feasible. Why? Because too few Dominicans can afford the ticket prices necessary to support a team. Obviously, higher incomes in the United States and Canada enable major league teams to offer higher salaries that attract Dominican players.

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Economics also helps explain why some countries can produce goods or services for less. And economics provides the analytical tools to determine the impact of an international company's operations on the economies of both host and home countries, as well as the impact of the host country's economic environment on a foreign firm.

Economics explains country differences in costs, currency values, and market size.

## THE COMPETITIVE ENVIRONMENT

In addition to its physical and social environments, every globally active company operates within a competitive environment. Figure 1.1 highlights the key competitive factors in the external environment of an international business: product strategy, resource base and experience, and competitor capability.

**Competitive Strategy for Products** Products compete by means of *cost* or *differentiation strategies*, the latter usually by:

- Developing a favorable *brand image*, usually through advertising or from long-term consumer experience with the brand; or
- Developing *unique characteristics*, such as through R&D efforts or different means of distribution.

Using either approach, a firm may mass-market a product or sell to a niche market (the latter approach is called a *focus strategy*). Different strategies can be used for different products or for different countries, but a firm's choice of strategy plays a big part in determining how and where it will operate. Take Fiat, an Italian automobile brand that competes mostly with a cost strategy aimed at mass-market sales. This strategy has influenced Fiat to locate engine plants in China, where production costs are low, and to sell in India and Argentina, which are cost-sensitive markets. Interestingly, Fiat also owns Ferrari, which competes with a focus strategy toward very high-income consumers. Whereas the competitive U.S. market has not been conducive to a mass-market Fiat brand strategy, Fiat sells over a quarter of all its Ferraris in the United States. With Fiat's

A company's situation may differ among countries by

- Its competitive ranking.
- The competitors it faces.

investment in Chrysler, it plans to also sell the Fiat 500 (a sort of boutique car) with a focus strategy.

**Company Resources and Experience** Other competitive factors are a company's size and resources compared to those of its competitors. A market leader, for example—say, Coca-Cola—has resources for much more ambitious international operations than a smaller competitor like Royal Crown. Royal Crown sells in about 60 countries, Coca-Cola in more than 200.

In large markets (such as the United States), companies have to invest many more resources to secure national distribution than in small markets (such as Ireland). Further, they'll probably face more competitors in large markets; in a European country, especially in retailing, a firm is likely to face three or four significant competitors, compared to the 10 to 20 it will face in the United States.[44]

Conversely, national market share and brand recognition have a bearing on operating in a given country. A company with a long-standing dominant market position uses operating tactics quite different from those employed by a newcomer. Such a company, for example, has much more clout with suppliers and distributors. Remember, too, that being a leader in one country doesn't guarantee being a leader anywhere else. In most markets, Coca-Cola is the leader, with Pepsi-Cola coming in a strong second; in India, however, Coke is number three, trailing both Pepsi and a locally owned brand called *Thums Up*.[45]

**Competitors Faced in Each Market** Finally, success in a market (whether domestic or foreign) often depends on whether the competition is also international or local. Commercial aircraft makers Boeing and Airbus, for example, compete almost only with each other in every market they serve. What they learn about each other in one country is useful in predicting the other's strategies elsewhere. In contrast, the British grocery chain Tesco faces different competition in almost every foreign market it enters.

## Looking to the Future: Three Ways of Looking at Globalization

At this juncture, there's a big difference of opinion on the future of international business and globalization. Basically, there are three major viewpoints:

- Further globalization is inevitable.
- International business will grow primarily along regional rather than global lines.
- Forces working against further globalization and international business will slow down the growth of both.

### Globalization Is Inevitable

The view that globalization is inevitable reflects the premise that advances in human connectivity are so pervasive that consumers everywhere will know about and demand the best products for the best prices regardless of their origins. Those who hold this view also argue that because MNEs have built so many international production and distribution networks, they'll pressure their governments to place fewer restrictions on international movements of goods and means to produce them.

Even if we accept this view, we must still meet at least one challenge to riding the wave of the future: Because the future is what we make of it, we must figure out how to spread the benefits of globalization equitably while minimizing the hardships placed on those parties—both people and companies—who suffer from increased international competition.

The *Wall Street Journal* posed a question to all living Nobel Prize winners in economics: "What is the greatest economic challenge for the future?" Several responses addressed globalization and international business. Robert Fogel said it's the problem of getting available technology and food to people who are needlessly dying. Both Vernon Smith and Harry Markowitz specified the need to bring down global trade barriers. Lawrence Klein called for "the reduction of poverty and disease in a peaceful political environment." John Nash felt we must address the problem of increasing the worldwide standard of living while the amount of the earth's surface per person is shrinking.[46] Clearly, each of these responses projects both managerial challenges and opportunities.

### More Regional Than Global Growth

The second view—that growth will be largely regional rather than global—is based on studies showing that almost all of the companies we think of as "global" conduct most of their business in home and neighboring countries.[47] Most world trade is regional, and many treaties to remove trade barriers are regional. Transport costs favor regional over global business. And regional sales may be sufficient for companies to gain scale economies to cover their fixed costs adequately. Nevertheless, regionalization of business activity may be merely a transition stage. In other words, companies may first promote international business in nearby countries and then expand their activities once they've reached certain regional goals.

### Globalization and International Business Will Slow

The third view argues that the pace of globalization will slow down, or may already have begun collapsing.[48] In light of the antiglobalization sentiments mentioned earlier, it's easy to see that some people are adamant and earnest in voicing their reservations. The crux of the antiglobalization movement is the perceived growing schism between parties (including MNEs) who are thriving in a globalized environment and those who aren't. For example, during 2009, hungry (undernourished) people increased by about 100 million from 2008 and reached about 20 percent of the world's population.[49]

Antiglobalists pressure governments to promote nationalism by raising trade barriers and rejecting international organizations and treaties. Historically, such groups have often succeeded (at least temporarily) in obstructing either technological or commercial advances that threatened their well-being. Recently, antiglobalization sentiments have grown in many countries, such as a state law change in Arizona to restrict undocumented aliens, the deportation by France of ethnic Roma (gypsies), the evacuation in Italy of immigrants to protect them against local residents, and gains by Sweden's anti-immigration Democrat's Party.[50] In Brazil and South Africa, voters have authorized domestic companies to copy pharmaceuticals under global patent protection. Bolivia and Venezuela have nationalized some foreign investments, and the United States prevented China from purchasing a U.S. oil company. The sparring between pro- and anti-globalists is one of the reasons why the globalization process has progressed in fits and starts.

Other uncertainties may hamper globalization. First is the question of oil prices, which affect international transportation because they can constitute more than 75 percent of operating costs on large ships.[51] In early 2008 global oil prices rose 44 percent, fell 74 percent by the end of the year, and then more than doubled by the end of 2010. Many U.S. companies, such as furniture manufacturers, have responded by returning to domestic production bases rather than facing transport cost uncertainty.[52] Second, the economic recession and lingering unemployment since 2008 have led countries to enact measures to protect their work forces. Third, safety concerns—property confiscation, terrorism, piracy of ships, and outright lawlessness—may inhibit companies from venturing as much abroad.

Finally, one view holds that for globalization to succeed, efficient institutions with clear-cut mandates are necessary; however, there is concern that neither the institutions nor the people working in them can adequately handle the complexities of an interconnected world.[53]

### Going Forward

Only time will tell, but one thing seems certain: If a company wants to capitalize on international opportunities, it can't wait too long to see what happens on political and economic fronts. Investments in research, equipment, plants, and personnel training can take years to pan out. Forecasting foreign opportunities and risks is always challenging. Yet, by examining different ways in which the future may evolve, a company's management has a better chance of avoiding unpleasant surprises. That's why each chapter of this book includes a feature that shows how certain chapter topics can become subjects for looking into the future of international business. ■