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PART

The Global Manager's Environment

PART OUTLINE

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Assessing the Environment—Political,
Economic, Legal, Technological

World Map

Chapter 2

Managing Interdependence: Social
Responsibility, Ethics, Sustainability



Assessing the Environment

Political, Economic, Legal, Technological



OUTLINE

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OBJECTIVES

1. To understand the global business environment and how it affects the strategic and operational decisions which managers must make.
2. To critically assess the developments, advantages, and disadvantages of globalization.
3. To review the role of technology in international business.
4. To develop an appreciation for the ways in which political, economic, legal and technological factors and changes impact the opportunities that companies face.
5. To discuss the complexities of the international manager's job.

OPENING PROFILE: THE GLOBALIZATION OF RISK¹

Firms' risk analysts were certainly scratching their heads going into 2012 after the confluence of events in 2011 caused such a global ripple effect of business risk. The World Economic Forum Global Risks 2012 Report (based on 469 social experts and industry leaders) highlighted the world's interconnected and rapidly developing socio-economic risks. The report points out that severe income disparity and chronic fiscal imbalances would be the top two risks facing business leaders and policy makers for 2012 and the next decade; it also raises the concern that those macro risks will reverse the gains of globalization. Contributing largely to those escalating risks, the global debt crisis continued unabated; in Europe, in particular, problems in major debtor countries such as Greece, Italy, and Ireland threatened to break up the eurozone and implode the euro. Leaders in stronger countries such as Germany and France struggled to put together a rescue plan. As the global recession, started in 2008, continued to eat away at business profits and people's jobs, homes, and lifestyles, the observation quoted below is still relevant.

A perilous global crisis of confidence has revealed both the scale and the limitations of globalization.²

People around the world made their fears known as they sought redress for their various situations. Most surprising were the massive "Arab Spring" protests, which spread like wildfire through social media and Internet technology. Their long-term effects are not yet known. Following those, the protest movement spread in the West and was known in the United States as the "Occupy" movement, in which people were protesting what they perceived as "Wall Street" excesses and income inequality.

It is clear that the global credit crunch has hit consumers and businesses alike as uncertainty about the future cripples spending and investment, and has a ripple effect around the world. Firms are reluctant to expand their business in troubled countries, consumers are reluctant to spend, and so the global economy retracts. Even the rapidly developing emerging economies are adversely affected by the reduced demand from developed economies.

Add to this the political uncertainty of leadership changes around the world, such as in China, and increasing tensions with Iran, and you have a cauldron of political, economic, and financial risks.

In 2011 it also became apparent to risk analysts that there are natural disasters that can cripple business activities in far-flung countries from where the disaster occurs, and these cannot be anticipated, although back-up plans can be put in place. This realization came after the Japanese 9.0 magnitude earthquake killing 20,000 people. The resulting tsunami and problems in the nuclear reactors was devastating to Japan's people and economy. Supply chains around the world were disrupted from the shutdown of manufacturing plants and infrastructure in Japan; this disaster and the devastating flooding in Thailand in November 2011 highlighted the need for resilient business models in response to crises of unforeseen magnitude. "The question now is, has the quest for lowest-cost production and hyper-lean supply chains overridden and exposed vulnerability to significant business risk?"³

Clearly, globalization has compounded the types and level of business risks to which firms are exposed and the speed with which they might be impacted. Managers around the world must be attuned to what types of situations make their firms vulnerable and plan accordingly. Carlos Ghosn, the CEO of Nissan, told an audience in New York:

There's going to be another crisis. We don't know what kind of crisis, where it is going to hit us, and when it is going to hit us, but every time there is a crisis we are going to learn from it.

FORTUNE,
December 26, 2011.⁴

Half of the global growth now comes from emerging markets.

ROBERT ZOELICK, PRESIDENT, WORLD BANK,
SEPTEMBER 19, 2011.⁵

As evidenced in the opening profile, managers in the twenty-first century are being challenged to operate in an increasingly complex, interdependent, networked, and changing global environment. In a globalized economy, developments such as those described in the opening profile can have repercussions around the world almost instantaneously. Clearly, those involved in international and global business have to adjust their strategies and management styles to those kinds of global developments as well as to those regions of the world in which they want to operate, whether directly or through some form of alliance.

Typical challenges that managers face involve politics, cultural differences, global competition, terrorism, and technology. In addition, the opportunities and risks of the global marketplace increasingly bring with them the societal obligations of operating in a global community. An example is the dilemma faced by Western drug manufacturers of how to fulfill their responsibilities to stockholders, acquire capital for research and development (R&D), and protect their patents while also being good global citizens by responding to the cry for free or low-cost drugs for AIDS in poor countries. Managers in those companies are struggling to find ways to balance their social responsibilities, their images, and their competitive strategies.

To compete aggressively, firms must make considerable investments overseas—not only capital investment but also investment in well-trained managers with the skills essential to working effectively in a multicultural environment. In any foreign environment, managers need to handle a set of dynamic and fast-changing variables, including the all-pervasive variable of culture that affects every facet of daily life. Added to that “behavioral software” are the challenges of the burgeoning use of technological software and the borderless Internet, which are rapidly changing the dynamics of competition and operations.

International management, then, is the process of developing strategies, designing and operating systems, and working with people around the world to ensure sustained competitive advantage. Those management functions are shaped by the prevailing conditions and ongoing developments in the world, as outlined in the following sections.

THE GLOBAL BUSINESS ENVIRONMENT

Following is a summary of some of the global situations and trends that managers need to monitor and incorporate in their strategic and operational planning.

Globalization

The World Trade Organization (WTO) warned in September 2011 that the expansion in global trade had slowed sharply, and that “the slowdown in trade was concentrated in the advanced economies, particularly Europe, suggesting that it was related to the sovereign debt crisis in the eurozone.”⁶ Clearly, the financial linkages around the world are just one phenomenon of globalization. Business competitiveness has now evolved to a level of sophistication commonly called **globalization**—global competition characterized by networks of international linkages that bind countries, institutions, and people in an interdependent global economy. Economic integration results from the lessening of trade barriers and the increased flow of goods and services, capital, labor, and technology around the world. The invisible hand of global competition is being propelled by the phenomenon of an increasingly borderless world, by technological advancements, and by the rise of emerging markets such as China and India—a process that Thomas Friedman refers to as “leveling the playing field” among countries—or, the “flattening of the world.”⁷

Emerging economies now produce as much trade, capital, and knowledge flow as do developed economies.⁸ Sirkin et al. use the term “globality,” stating that business these days is all about “competing with everyone from everywhere for everything.”⁹ On a more strategic level, Ghemawat argues, rather, that the business world is in a state of “semi-globalization”—that various metrics show that only 10 to 25 percent of economic activity is truly global. He bases this conviction on his analysis that “most types of economic activity that can be conducted either within or across borders are still quite localized by country.”¹⁰ Ghemawat poses that we are in an “unevenly globalized world” and that business opportunities and threats depend on the individual perspective of country, company, and industry.¹¹ He observes that, as emerging market countries have gained in wealth and power and increasingly call their own shots, there is a reverse trend of globalization taking place—evolving fragmentation—which he says is, ironically, a ripple effect of globalization.¹² Examples of such localization trends are the activities of firms such as Alibaba, Infosys, Carrefour, General Motors, and Pizza Hut that now focus on tailoring their products to emerging-market consumers.

GLOBAL TRENDS

The rapid development of globalization is attributable to many factors, including the burgeoning use of technology and its accompanying uses in international business; political developments that enable cross-border trade agreements; and global competition for the growing numbers of

consumers around the world. From studies by Bisson et al. and others, we can also identify five key global trends that provide both challenges and opportunities for companies to incorporate into their strategic planning:¹³

- The changing balance of growth toward emerging markets compared with developed ones, along with the growing number of middle-class consumers in those areas.
- The need for increased productivity and consumption in developed countries in order to stimulate their economies.
- The increasing global interconnectivity—technologically and otherwise, as previously discussed, and in particular the phenomenon of an “electronically flattened earth” that gives rise to increased opportunity and fast-developing competition.
- The increasing gap between demand and supply of natural resources, in particular to supply developing economies, along with the push for environmental protection.
- The challenge facing governments to develop policies for economic growth and financial stability.¹⁴

Globality and Emerging Markets

*Nestlé said on July 11, 2011 that it had agreed to pay \$1.7 billion for a 60 percent stake in a big Chinese confectioner, in one of the biggest deals ever by a foreign company in China.*¹⁵

It is clear that globalization—in the broader sense—has led to the narrowing of differences in regional output growth rates, driven largely by increases led by China, India, Brazil and Russia (often called the BRICs, which together accounted for over 18 percent of global gross domestic product (GDP) as of 2011¹⁶). There is no doubt that the global economic turmoil has curtailed investment, and company executives remained wary of investment in 2012. However, global trade is increasingly including those developing nations judged to have significant growth potential, with investments from developed economies to emerging economies of over \$1,000 billion a year as of 2011.¹⁷ Exhibit 1-1 shows the 2012 results from research by the A. T. Kearney Company of the Foreign Direct Investment (FDI) intentions and preferences of the leaders of top companies in 17 industry sectors spanning six continents; the companies participating in the survey account for over \$2 trillion in global revenue. The exhibit shows the top 25 countries in which those executives have confidence for their investment opportunities. Their results show that China, India, and Brazil continue to rank at the top of the FDI Confidence Index, along with the United States (although the U.S. rank dropped two places since 2010, burdened by debt and financial instability).¹⁸ In fact over half of global FDI inflows were from emerging markets for the first time in history, and now comprise more than half of the Index’s top 25 countries. South Africa, which was unranked in 2010, rebounded to 11th place. Russia fell from 9th place in 2007 to 12th in 2012. Overall, it is clear that the phenomenon of such rapidly developing economies, says Fareed Zakaria, is something much broader than the much-ballyhooed rise of China or even Asia. Rather, he says:

*It is the rise of the rest—the rest of the world.*¹⁹

“The rest,” he says, include countries such as Brazil, Mexico, South Korea, Taiwan, India, China, and Russia. He states that, as traditional industries in the United States continue to decline, “the rest” are picking up those opportunities. Even so, the United States remains dominant in many “new age” industries such as nanotechnology and biotechnology. It is clear, also, that as emerging markets continue to grow their countries’ economies, they will provide growth markets for the products and services of developed economies.

Evidence of the growing number of companies from emerging markets can be seen in the Fortune 500 rankings of the world’s biggest firms. The Global 500 is increasingly global. While the U.S. still dominates the list, with 133 companies, that number is down from 185 a decade ago. China continues to move up the list, with 61 companies—versus just 12 in 2001—while many companies from India, Russia, Brazil, and other growth economies are moving up in the rankings. Examples of “emerging giants” are, from China, Huawei Technologies, Lenovo Group, and Baosteel; those from India include Infosys Technologies, Tata Group, and Bharti Airtel;

MAP 1.1 Emerging Economies

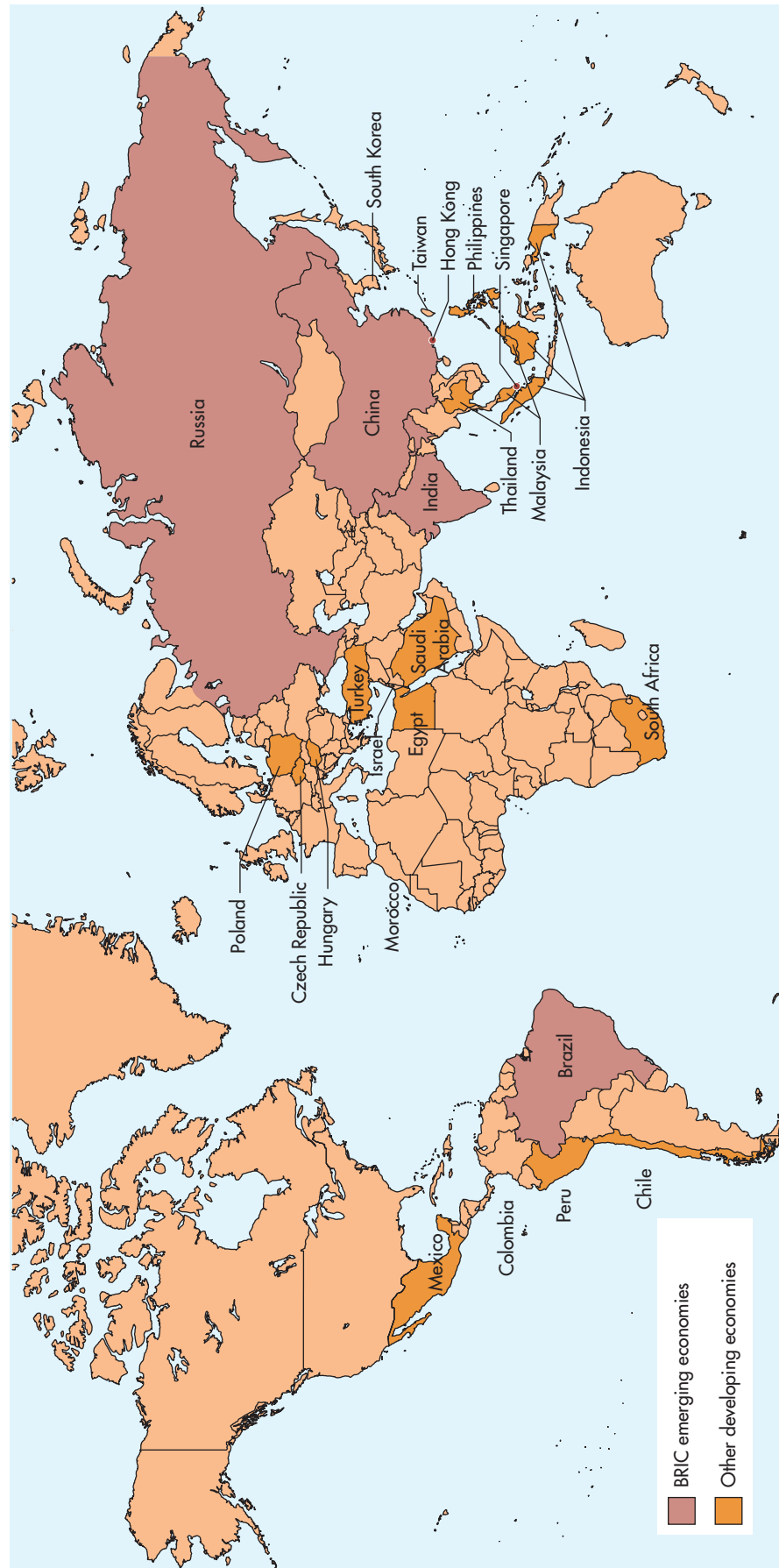
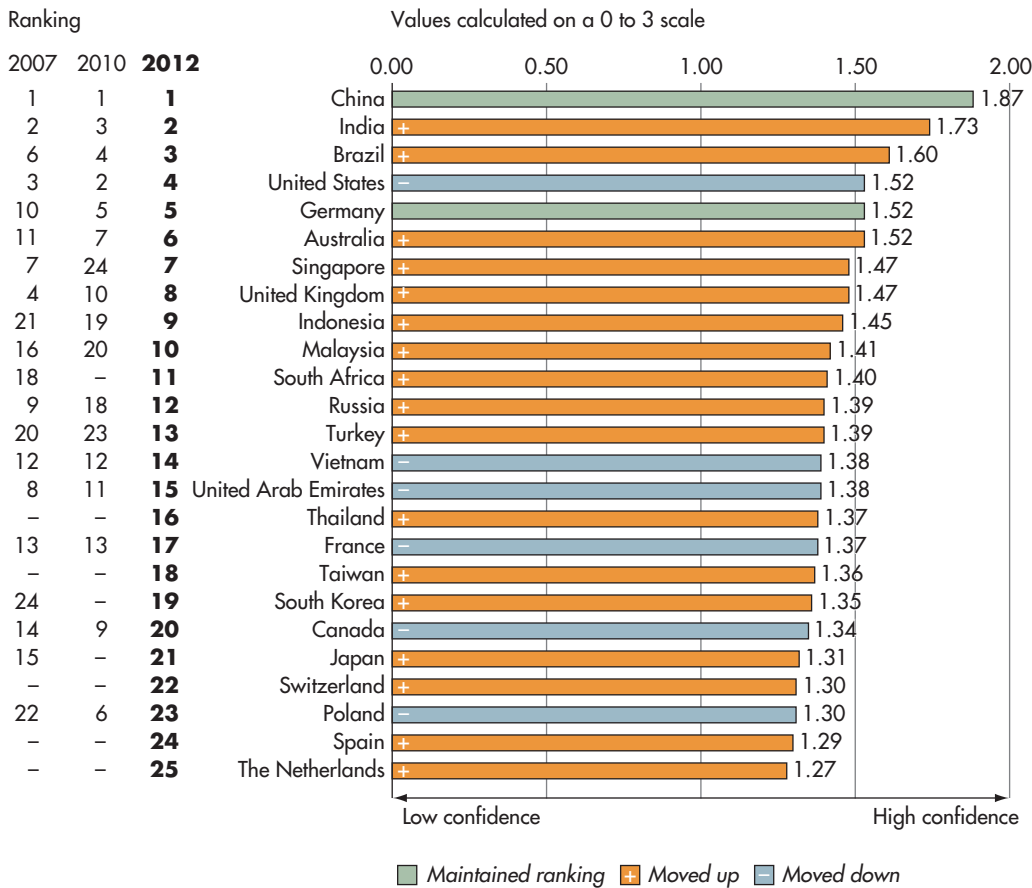


EXHIBIT 1-1 2012 Foreign Direct Investment Confidence Index Top 25 Targets for FDI The main types of FDI are acquisition of a subsidiary or production facility, joint ventures, licensing, and investing in new facilities or expansion of existing facilities.



Source: 2012 FDI Confidence Index, Copyright A. T. Kearney, 2012. All rights reserved. Reprinted with permission.

from Brazil they include Embraer and Votorantim Group; from Mexico, Group Bimbo; Gazprom from Russia, and Bumi Resources from Indonesia—to name a few.

Simply put: If you're doing business with the biggest companies in the world, you're not just spending time in New York, London, and Hong Kong.²⁰

FORTUNE,
JULY 25, 2011.

Further evidence that “globalization” is no longer just another word for “Americanization” is the increase in the number of emerging-market companies acquiring established large businesses and brands from the so-called “developed” countries. For example, in 2008 the Budweiser brand, America’s favorite beer, was bought by InBev, a Belgian-Brazilian conglomerate, and also in 2008, “several of America’s leading financial institutions avoided bankruptcy only by going cap in hand to the sovereign-wealth funds (state-owned investment funds) of various Arab kingdoms and the Chinese government.”²¹ Clearly, companies in emerging markets are providing many tangible business opportunities for investment and alliances around the world, as well as establishing themselves as competitors to reckon with.

Backlash against Globalization

As we consider the many facets of globalization and how they intertwine, we observe how economic power and shifting opinions and ideals about politics and religion, for example, result in an increasing backlash against globalization and a rekindling of nationalism. Globalization has been propelled by capitalism and open markets, most notably by Western companies. Now

“economic power is shifting fast to the emerging nations of the south. China and India are replacing the U.S. as the engines of world economic growth.”²²

The rising nationalist tendencies are evident as emerging and developing nations—wielding their economic power in attempted takeovers and inroads around the world—encounter protectionism. There is hostility to takeovers such as the Indian company Mittal Steel's bid for Europe's largest steel company, Arcelor. In particular, as the demand on energy resources burgeons with heightened industrial activity in China, we see increased protectionism of those resources around the world as Russia, Venezuela, and Bolivia have privatized their energy resources.

The backlash against globalization comes from those who feel that it benefits advanced industrial nations at the expense of many other countries and the people within them who are not sharing in those benefits. Joseph Stiglitz, a Nobel Laureate, for example, argues that such an economic system has been pressed upon many developing countries at the expense of their sovereignty, their well-being, and their environment. Critics point to the growing numbers of people around the world living in poverty.²³ Recently, globalization has also become increasingly unpopular with many in the United States as growth in emerging markets raises prices for energy and commodities; as their jobs are being lost overseas, driving down wages; and as the weak dollar makes companies in the United States vulnerable to foreign buyers.²⁴

While the debate about the effects of globalization continues, it is clear that economic globalization will be advanced by corporations looking to maximize their profits with global efficiencies, by politicians and leaders wishing to advance their countries' economies, and by technological and transportation advances that make their production and supply networks more efficient. However, pressure by parties against those trends, as well as the resurgence in nationalism and protectionism, may serve to pull back those advances to a more regional scope in some areas, or limit them to bilateral pacts.²⁵

In addition, while competition to provide the best and cheapest products to consumers exerts pressure on corporations to maximize efficiencies around the world, there is also increasing pressure and publicity for them to consider the social responsibility of their activities (discussed further in Chapter 2).

Effects of Institutions on Global Trade²⁶

Two major groups of institutions (supranational and national) play a differing role in globalization. Supranational institutions such as the World Trade Organization (WTO) and the International Labor Organization (ILO) promote the convergence of how international activities should be conducted. For example, the WTO promotes the lowering of tariffs and a common set of trade rules among its member countries. Similarly, the ILO promotes common standards of how workers should be treated. While many supranational institutions frequently promote rules or laws favorable to foreign firms (e.g., requiring intellectual property rights protections in China), others have been criticized for infringing on national sovereignty (e.g., challenges to certain environmental laws in the United States).

National institutions, in contrast, play a role in creating favorable conditions for domestic firms and may make it more difficult for foreign firms to compete in those countries. For example, the stringent drug testing rules required by the U.S. Food and Drug Administration (FDA) and the anti-dumping rules enforced by the U.S. Department of Commerce's International Trade Administration (ITA) act as entry barriers for foreign firms (see Chapter 6 for a more detailed discussion of these entry barriers).

Some supranational institutions represent the interests of a smaller group of countries. For example, the European Commission acts in the interest of the 27 EU members as a whole rather than the interest of individual member countries. The European Commission is the executive arm of the EU and is responsible for implementing the decisions of the European Parliament and the European Council. Of relevance to international business, the European Commission speaks for the EU at the World Trade Organization, and is responsible for negotiating trade agreements on behalf of the EU.²⁷

Effects of Globalization on Corporations

In returning to our discussion at the corporate level, we can see that almost all firms around the world are affected to some extent by globalization. Firms from any country now compete with companies at home and abroad, and domestic competitors are competing on price by outsourcing

or offshoring resources and services anywhere in the world. Often it is difficult to tell which competing products or services are of domestic or foreign origin. Examples abound—for example, do you really drive an American car?

*Look at your vehicle identification number (VIN): If it starts with 1 it is made in America, 2, Canada, 3, Mexico, 4, anywhere else in the world. The only cars allowed to park in a UAW plant are those with VIN numbers beginning with 1 and 2.*²⁸

Hondas are made in Ohio; Buicks are made in Germany. In contrast, Japan's Toyota Sienna model is far more American, with 90 percent local components being assembled in Indiana.²⁹ This didn't happen overnight. Toyota has been investing in North America for 20 years in plants, suppliers, and dealerships, as well as design, testing, and research centers. Toyota became the largest auto manufacturer in the world in sales in 2009. In fact, on June 1, 2009, General Motors filed for Chapter 11 bankruptcy, pushed into a temporary partial nationalization by the U.S. government in order to save the company in a drastically downsized form.³⁰

Clearly, competition has no borders, with most global companies producing and selling more of their global brands and services abroad than domestically. Cisco Systems gets 55 percent of its revenues from overseas and CEO John Chambers predicted that 70 percent of the firm's growth will come from overseas.³¹ Avon, for example, estimates it employs 5 million sales representatives globally; Nestlé has 50 percent of its sales outside of its home market; Coca-Cola has 80 percent; and Procter & Gamble has 65 percent. The Tata Group, a conglomerate originating in India, has operations in 85 countries and has made a number of acquisitions of large firms around the world.

Investment by global companies around the world means that this aspect of globalization benefits developing economies—through the transfer of financial, technological, and managerial resources, as well as through the development of local allies that later become self-sufficient and have other operations. Global companies are becoming less tied to specific locations, and their operations and allies are spread around the world as they source and coordinate resources and activities in the most suitable areas and as technology facilitates faster and more flexible interactions and greater efficiencies. In fact, as noted in discussions in the 2012 World Economic Forum: “it is that the world's largest companies are moving beyond governments and countries that they perceive to be inept and anemic. They are operating in a space that is increasingly supranational—disconnected from local concerns and the problems of their home markets.”³²

It is essential, therefore, for managers to look beyond their domestic market. If they do not, they will be even further behind the majority of managers who have already recognized that they must have a global vision for their firms, beginning with preparing themselves with the skills and tools of managing in a global environment. Companies that desire to remain globally competitive and to expand their operations to other countries will have to develop a cadre of top management with experience operating abroad and an understanding of what it takes to do business in other countries and to work with people of other cultures. Many large firms around the world are getting to the stage of evolution known as the stateless multinational, where work is sourced wherever it is most efficient; the result of this stage of development is that

*for business leaders, building a firm that is seamlessly integrated across time zones and cultures presents daunting obstacles.*³³

Already it is clear that top managers are locating anywhere in the world where the firm has operations or is looking for opportunities, rather than trying to run the show from a headquarters building in the home country. Jeff Immelt, for example, who is Chairman and CEO of General Electric (GE), calls himself a “globalist.” GE is clearly a global company—half of GE's 300,000 employees are overseas, and 60 percent of its revenues come from overseas. “Petropolis,” for example, GE's company town plant in Brazil, has 8,000 employees and is growing at a rate of 35 percent a year, compared to one percent in the United States. When Leslie Stahl, in an interview on October 9, 2011 for the CBS program *60 Minutes*, pressured Mr. Immelt about GE's many jobs overseas that could be in the United States, he responded that those plants order components from GE's U.S. plants, and he defended the company's global strategy as being responsible to the shareholders and responsible to grow the company's revenues.

SMALL AND MEDIUM-SIZED ENTERPRISES (SMEs)

SMEs are also affected by, and in turn affect, globalization. They play a vital role in contributing to their national economies—through employment, new job creation, development of new products and services, and international operations, typically exporting. The vast majority (about 98 percent) of businesses in developed economies are small and medium-sized enterprises, which are typically referred to as those companies having fewer than 500 employees. Small businesses are rapidly discovering foreign markets. Although many small businesses are affected by globalism only to the extent that they face competing products from abroad, an increasing number of entrepreneurs are being approached by potential offshore customers, thanks to the burgeoning number of trade shows, federal and state export initiatives, and the growing use of Web sites that ease making contact and placing orders online.³⁴

There has never been a better time for SMEs to go global; the Internet is as valid a tool for small companies to find customers and suppliers around the world as it is for large companies. By using the Internet, email, and web-conferencing, small companies can inexpensively contact customers and set up their global businesses. One example of a very small start-up that went global quickly is that of Groupon Inc., a local e-commerce marketplace that connects merchants to consumers by offering goods and services at a discount through on-line coupons. The idea was conceived by Groupon's CEO Andrew Mason and rapidly caught on. Groupon has quickly become one of the success stories of the new generation of Internet start-ups. As of September 30, 2011, the Company featured deals from over 190,000 merchants worldwide across over 190 categories of goods and services. Mason employs people in a number of countries to tailor their approach locally to the local commerce markets worldwide in the leisure, recreation, food-service, and retail sectors.³⁵

Regional Trading Blocs

Much of today's world trade takes place within three regional free-trade blocs (Western Europe, Asia, and the Americas). These trade blocs are continually expanding their borders to include neighboring countries, either directly or with separate agreements.

THE EUROPEAN UNION The European Union (EU) comprises a 27-nation unified “borderless” market of approximately 500 million people, as shown in Map 1.2. Countries around the world trade with the EU countries. The United States, for example, had a two-way trade of \$560 billion and a \$3 trillion two-way investment relationship as of 2011. Although trade continued to grow in 2010 despite the 2008 global financial crisis, the EU GDP growth was only at 1.8 percent that year and economic problems in some member states continuing into 2012 were adversely affecting the EU as a whole, resulting in global financial repercussions. Many were questioning the stability of the euro, as discussed in the Financial Times:

*The future of the eurozone, and the capacity of the 17-nation currency union to recover from the debt crisis among its peripheral members, depends on the performance of the German economy more than on any other in Europe.*³⁶

The importance of Germany to the eurozone is clear, but it is also a two-way street. “Germany’s prosperity is inextricably linked with the success and survival of the single currency, with more than 38 percent of German exports going to its eurozone partners, and almost 58 percent to the 27 members of the European Union.”³⁷ The strength of the German manufacturing model is evidenced by the fact that, while Germany has about a quarter of the population of the United States, and a quarter of the U.S. GDP (Gross Domestic Product), it exports more than the United States.³⁸ Germans were concerned, however, that their economic strength would be diluted by the need to help prop up weaker economies in the eurozone, such as Greece.

In spite of those problems, the World Economic Forum’s 2012–2013 Global Competitiveness Index (GCI) shows that six out of the top ten countries are in Europe (see Table 1–1). Interestingly, the United States had slipped to seventh from second place in 2010. The GCI is based on twelve pillars of competitiveness that provide attractive conditions and incentives for both local and foreign companies to do business there.³⁹ However, the elimination of internal tariffs and customs, as well as financial and commercial barriers has not eliminated national pride. Although most people in Europe are thought of simply as Europeans, they still think of

MAP 1.2 European Union



themselves first as British, French, Danish, Italian, etc., and are wary of giving too much power to centralized institutions or of giving up their national culture. The continuing enlargement of the EU to include many less prosperous countries has also promoted divisions among the “older” members.⁴⁰ In addition, continuing eurozone problems in 2012 prompted skepticism of any further enlargement.

Global managers face two major tasks. One is strategic: how firms outside of Europe can deal with the implications of the EU and of what some have called a “Fortress Europe”—that is, a market giving preference to insiders. While firms must have a pan-European business strategy, they must realize that suitable market entry strategies must be considered on a country-by-country basis.

*While the European Union continues to move in the direction of a Single Market, the reality today is that U.S. exporters in some sectors continue to face barriers to entry in the EU market. In the world of the Internet and e-commerce, some of these barriers are still pronounced.*⁴¹

TABLE 1-1 2012–2013 Global Competitiveness Index (7 is highest score)

Rank	Country	Score
1	Switzerland	5.72
2	Singapore	5.67
3	Finland	5.55
4	Sweden	5.53
5	Netherlands	5.50
6	Germany	5.81
7	U.S.	5.47
8	U.K.	5.45
9	Hong Kong	5.41
10	Japan	5.40

Source: Based on selected data from www.worldeconomicforum.org, September 7, 2012.

The other task is cultural: How to deal effectively with multiple sets of national cultures, traditions, and customs within Europe, such as differing attitudes about how much time should be spent on work versus leisure activities.

ASIA

It would be difficult to overstate the power of the fundamental drivers of Asian growth. First, Asian economies have been enjoying a remarkable period of “productivity catch-up,” adopting modern technologies, industrial practices, and ways of organizing—in some cases leapfrogging Western competitors.⁴²

Manufacturing accounts for approximately 30 percent of GDP in Asia’s emerging markets, helping to fuel the demand for materials and supplies from the developed world, and lending hope for a quick global economic recovery.⁴³ Japan and the Four Tigers—Singapore, Hong Kong, Taiwan, and South Korea have provided most of the capital and expertise for Asia’s developing countries. Now the focus is on China’s role in driving closer integration in the region through its rapidly growing exports. Japan continues to negotiate trade agreements with its neighbors; China is negotiating with the entire thirteen-member Association of Southeast Asian Nations (ASEAN), while ASEAN is negotiating for earlier development of its own free trade area, ASEAN Free Trade Area (AFTA).

The Chinese market offers big opportunities for foreign investment, but you must learn to tolerate ambiguity and find a godfather to look after your political connections.⁴⁴

China has enjoyed success as an export powerhouse, a status built on its strengths of low costs and a constant flow of capital. Its growth phenomenon is further discussed in the accompanying feature “Comparative Management in Focus—China Helps Prop Up the Global Economy.”



COMPARATIVE MANAGEMENT IN FOCUS

China Helps Prop Up the Global Economy

Headline GDP numbers won’t tell the real story, even if that number is 8% or 9%. The growth rate in many cities is well above that, in the range of 15% to 20%, and that is what matters for the global system.⁴⁵

If I say I want to open a campus in China . . . they’ll say, “What do you need?”

JOHN CHAMBERS, CISCO SYSTEMS CHAIRMAN AND CEO,
April 2012.⁴⁶

Indeed, in spite of some recent pullback, there is no doubt that the rise in China’s GDP has helped prop up the global system. While China’s growth rate in 2011 was 8.9 percent, down from

9.1 percent in 2010, it was “hardly a sign of a ‘hard’ landing.”⁴⁷ U.S. exports to China rose 542 percent to \$103.9 billion in 2011 from \$16.2 billion in 2000, making it the third-largest U.S. export market.⁴⁸ China is the second-largest trading partner with the United States, after Canada, and it is the world’s second largest recipient of FDI after the United States—investment largely coming from MNCs (Multinational Corporations). China’s gross domestic product (GDP) growth rate—over 9 percent a year for thirty years—has been the fastest in the world.⁴⁹ Its economy has doubled every eight years for thirty years and the income of its people has increased sevenfold. With most of the world in an economic downturn, China has continued to grow because of its aggressive approach to the slowdown by committing \$586 billion—9 percent of GDP—to infrastructure projects, and because its banking system remained relatively unscathed compared with others around the world. Indeed, China surpassed Germany in 2009 as the world’s largest exporter.⁵⁰ Continuing its aggressive long-term approach, China stepped up to the plate to take advantage of the economic downturn by going on a major shopping spree, investing in energy and other natural resources that could give it an economic advantage it has never had before. Examples were lending the Brazilian oil giant Petrobras \$10 billion in exchange for a long-term commitment to send oil to China, and similar deals with Russia and Venezuela.⁵¹

In March 2012, however, Chinese Premier Wen Jiabao raised eyebrows when he announced the government is targeting only 7.5% growth for 2012. This announcement signaled that Beijing is willing to tolerate slower growth in the name of better growth. Indeed, many welcomed such a goal, hoping that China will be able to contribute to global “rebalancing” by shifting away from export- and investment-dependence and toward domestic consumption. However, it also signaled more government intervention rather than a market-based approach.⁵² In addition, the announcement of China’s new leadership, set for November 2012, was being anxiously awaited.

Nevertheless, China has become a battleground for companies wanting a piece of the action in this rapidly growing economy. In fact, over 400 of the *Fortune* Global 500 companies are operating there. China’s rapid rise—and the burgeoning opportunities for foreign businesses—is partly attributable to its membership in the WTO and its actions taken for structural reforms and the opening of many of its industries to foreign investment. However, foreign companies are increasingly protesting the protectionism that the Chinese government uses by taking advantage of its original WTO membership, which gave concessions to a then-categorized less-developed economy. China is now a hybrid/market-driven economy—driven by competition, capital, and entrepreneurship.

In addition to the large companies that continue to earn considerable returns on their investments in and exports to China, SMEs are also active and gaining ground in this complex country; but all companies are advised to do their homework first, as advised by the Foreign Commercial Service (FCS):

*FCS counsels American companies that to be a success in China, they must thoroughly investigate the market, take heed of product standards, pre-qualify potential business partners and craft contracts that assure payment and minimize misunderstandings between the parties.*⁵³

What accounts for China’s rapid rise? China’s recent exports in a single day have been more than it exported in all of 1978. With its 1.3 billion people, China benefits greatly from its large and rapidly growing foreign and domestic market size, which provides significant economies of scale. Innovation is becoming another competitive advantage, with rising company spending on R&D coupled with strong university-industry research collaboration, and an increasing rate of patenting. In addition, China has the world’s largest foreign-exchange reserves—U.S. \$3.2 trillion in 2011, although at a slowing trend in 2012 because of its narrowing trade surplus.⁵⁴ Not to be overlooked is the fact that the Chinese government often subsidizes and supports its manufacturing base.

China’s vast population of low-wage workers and massive consumer market potential has attracted offshoring of manufacturing from companies around the world. In fact there are 49,000 U.S. companies alone operating in China. It is this low-cost manufacturing base that has contributed greatly to its exports and growth, as a major factor in China’s uniqueness, making it the world’s largest manufacturer, second-largest consumer, largest saver, and probably the second-largest military spender. China has the world’s largest shipped goods port capacity. For these reasons, China would seem well positioned to expand globally as long as global demand for its products and manufacturing continues. However, in 2012, some firms were noting that their Chinese labor costs were increasing, energy and shipping costs were rising, and the Chinese currency was appreciating—making it less advantageous to manufacture there than in the past.⁵⁵ In fact, in April 2012, the Boston Consulting Group reported on the results of their survey of companies with over \$1 billion sales, which indicated that “more than a third of large manufacturers are considering reshoring from China to the U.S.,” citing labor costs and product quality as primary considerations.⁵⁶

(Continued)

In all, China is still a developing country, with considerable differences between urban and rural areas making for quite varied markets. The great diversity is indicated by China's eight major languages, several dialects, and several other minority languages. Mandarin is the main language in the north; Cantonese in the south, in particular in Hong Kong. Each language reflects its own history and culture, and therefore markets and economies. Generally speaking, it is clear that China is aggressively opening its doors. However, the fact remains that, in virtually all industrial sectors, state firms play a significant or dominant role. Sixteen state-owned enterprises (SOEs) make up about half of GDP. In addition, central, regional, and local political influences create unpredictability for businesses, as do the arbitrary legal systems, suspect data, and underdeveloped infrastructure.⁵⁷ The FCS cautions investors to beware of the following factors:

- China's legal and regulatory system is arbitrary. Protection of intellectual property rights is critical.
- In spite of its progress toward a market economy, China still leans toward protecting its local firms, especially the state-owned ones, from imports, and promotes their exports.
- Political goals and agendas often take precedence over commercially-based decisions.
- Discrepancies of business practices make it difficult for SMEs with limited budgets to get started. The FCS advises those firms to start with fostering a sales network through regional agents or distributors who can assist in keeping track of policy and regulation updates and have local contacts.⁵⁸

How to negotiate with the Chinese is the subject of a further feature in Chapter 5. Presented here are ten basic tips for doing business in China, published by Mia Doucet in CanadExport:

TEN TIPS FOR DOING BUSINESS IN CHINA

When doing business in China, the ability to navigate cross-cultural issues is just as important as the goods and services you bring to the marketplace. This is true whether your company is just now considering the China market, recently gained its first sale or maintains an in-country presence.

Tip #1: Never underestimate the importance of existing connections. You need to be dealing with a Chinese person of influence. If that person feels you are trustworthy enough, and if they can get their network of contacts to trust you, there is a chance you will succeed. Asians want to do business with people they trust. But there is no real trust unless a person is in their circle. At first, they don't know if you will be a good partner. Show respect by keeping some distance. Focus on building the relationship before talking business. Do not go for big profit on your first contract.

Tip #2: To protect your intellectual property, use the same due diligence you would in the West.

Tip #3: Never pressure your Asian colleagues for a decision. To speed up the decision process, slow down. Start from the beginning and work through to a solution in a logical, step-by-step fashion. Then stand your ground.

Tip #4: The negotiation process will be anything but smooth. Your best strategy is a walk away mentality. You have to go in trying not to make the deal. Explain your position in clear, concise words. State your terms clearly. Respectfully. Then be prepared to walk away if your terms are not met.

Tip #5: Respect face. Never argue or voice a difference of opinion with anyone—even a member of your own team. Never make the other person wrong. Never say "no" directly, as that is considered rude and arrogant.

Tip #6: Account for the fact that most Asians understand less spoken English than we think they do. The easiest thing in the world is for a Chinese to say yes. Their smiles and nods have more to do with saving face than getting your meaning. Talk in short sentences. Listen more than you speak. Pause between sentences. Find four or five easy ways to say the same thing. Never ask a question that can be answered with a simple yes. Avoid all slang. Skip humour altogether.

Tip #7: Manage the way you present written information. Document everything in writing and in precise detail. Present your ideas in stages. Write clearly, using plain English text. In order to appeal to Asian visual bias, use sketches, charts, and diagrams.

Tip #8: Prepare for every interaction. Do not count on your ability to wing it. A lack of preparedness can cause loss of face and trust. Do not give or expect to receive partial answers from your Chinese colleagues, as that is considered offensive.

Tip #9: Make sure your facts are 100% accurate in every detail, or you will lose credibility. Do not present an idea or theory that has not been fully researched, proven, or studied beforehand. If you make a mistake, you are not to be trusted.

Tip #10: Everyone on your team needs to know how to avoid costly gaffes.

Most of us are not by nature sensitive to the differences in culture—we have to be taught. Time-honoured passive resistance could bring your company to its knees. It makes sense to teach people the cross-cultural factors that have a direct impact on your profits.

Source: Mia Doucet, author of the award-winning book *China in Motion*, prepared these tips for *CanadExport*, “Ten Tips for Doing Business in China,” February 5, 2009. Used with permission of CanadExport, Foreign Affairs and International Trade Canada, September 15, 2011.

India: the 2011 GDP growth for India was 7.4 percent (down from 9.9 percent in 2010). Clearly there is much opportunity for foreign businesses in India, with its one-billion-plus population and a great potential for continued growth. Total bilateral trade with the U.S. for 2010 was \$48.8 billion.⁵⁹ However, in early 2012, a proposed raft of new taxes led a group of 250,000 global companies to warn that India would “lose significant ground as a destination for international investment” if it adopted the tax changes.⁶⁰ With its slow pace of reform, as well as continuing corruption cases, India is losing opportunities to other emerging markets which are more investor friendly. Nevertheless, India ranked second on the A.T. Kearney FDI Confidence Index as shown in Exhibit 1-1.

While China is known as the world’s factory, India has become known as the world’s services supplier, providing highly skilled and educated workers to foreign companies. India is the world’s leader for outsourced back-office services, and increasingly for high-tech services, with outsourcing firms such as Infosys becoming global giants themselves. India is the fastest-growing free-market democracy, yet its biggest hindrance to growth, in particular for the manufacturing sector, remains its poor infrastructure, with both local and foreign companies experiencing traffic gridlocks and power outages. However, much of India’s growth has been in technology industries that have not been affected by poor roads, compared with China’s manufacturing-based growth. Nevertheless, with growth second only to China, optimism abounds in India about the country’s prospects. The expanding middle class of almost 300 million is fuelling demand-led growth. Increasing deregulation is allowing whole sectors to be competitive. Here, too, there is considerable diversity in markets, incomes, and economies; there are fifteen major languages and over 1,600 dialects. Yet India’s rise is largely fueled by family firms that often maintain pyramid structures and grow vertically out of convenience because of problems with red-tape, erratic supply chains, and infrastructure:

*Adaptable, ingenious and combustible, the family firm remains the backbone of India’s private sector; not an anachronism. . . . The oldest, such as Aditya Birla, Tata and Bajaj, stretch back over three or more generations and are wily survivors.*⁶¹

Even so, approximately 40 percent of the profits of India’s 100 biggest listed firms come from state-controlled firms; an estimated two-thirds of production from India’s finance, energy, and natural resources firms is state controlled, despite India’s moves toward further privatization.⁶²

A common comparison between China and India notes that China’s economy grows because of its government, while India’s economy grows in spite of it. However, with its one billion people, many are still mired in poverty. Per capita GDP is below \$1,000, although the poverty rate is half that of twenty years ago. While India’s large upcoming youth bulge—compared with China—will bring a wave of workers for the economy, it will also bring many more mouths to feed. (India has the largest working-age population in the world, with about one-third under age 25, and one-third under age 15, while China is experiencing the results of its one-child policy.)

In many areas in India the economic transformation is startling, with growth fed by firms like the Tata Group—a global conglomerate producing everything from cars and steel to software and consulting systems. In August 2008, India joined a free-trade agreement with the ten fast-growing countries in the Association of South-East Asian Nations (ASEAN)—making it clear that a regional deal was preferable to a compromise to protect its farmers by saying “no” to

the multilateral trading system in the Doha trade talks.⁶³ Further discussion of doing business in India is included in Chapter 4.

In **South Asia**, an agreement was signed to form the South Asia Association of Regional Cooperation (SAARC), a free trade pact among seven South Asian nations: Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan, and Sri Lanka, effective January 1, 2006. The agreement was to lower tariffs to 25 percent within three to five years, and to eliminate them within seven years. The member nations comprise 1.5 billion people, with an estimated one-third of them living in poverty. Officials in those countries hope to follow the success of the other Asian regional bloc, the ASEAN.

Australia—although not regarded as part of Southeast Asia, but rather of the region called Oceania, which also includes New Zealand and neighboring islands in the Pacific Ocean—did sign an ASEAN friendship treaty with Southeast Asia. Australia is one of the richest countries in the world, with the mining industry responsible for attracting about a third of its investment inflows. Over 50 percent of her exports go to East Asia, with more transported through the region to markets around the world. Australia ranks 6th in the 2012 FDI Confidence Index shown in Exhibit 1-1—actually with the same score as the United States and Germany.

THE AMERICAS NAFTA: The goal of the North American Free Trade Agreement (NAFTA) between the United States, Canada, and Mexico was to bring faster growth, more jobs, better working conditions, and a cleaner environment for all as a result of increased exports and trade. This trading bloc—“one America”—has 421 million consumers. The Canada-United States trade is the largest bilateral flow between two countries. In addition, the vast majority—around 84 percent—of both Canadian and Mexican exports goes to the United States. Mexico is the United States’ 3rd largest trade partner (after Canada and China) and 2nd largest export market for U.S. products. From Mexico’s perspective, the country’s exports have exploded under NAFTA; U.S.-Mexico bilateral trade increased from \$88 billion in 1993, the year prior to the implementation of NAFTA, to \$383 billion (estimated) in 2010, an increase of 335 percent.⁶⁴ However, Mexico’s dependence on the United States for its exports—NAFTA’s greatest success—was shown to be a liability in the global economic downturn as Mexico felt the full brunt of declining consumption in the United States. The auto industry, for example, which has flourished under NAFTA, ground to a virtual standstill early in 2009. Mexican auto exports fell more than 50 percent in the first two months of 2009 compared with 2008, and production dropped almost 45 percent. However, in 2011 and 2012, Mexico’s growth rate picked up from increasing exports to the U.S. and was on track at around 4 percent growth.⁶⁵ Nevertheless Mexico fell off the 2012 FDI Confidence Index; indeed Canada fell from 9th place in 2010 to 20th in 2012, clearly suffering the impact of a decline in the U.S. economy.⁶⁶

Mexican trade policy is among the most open in the world, and the country has become an important exporting and importing power. While the Mexican economic cycles are very dependent on the American economy, she has signed 12 trade agreements with 43 nations, putting 90 percent of its trade under free trade regulations.⁶⁷

Recently, considerable violence among drug gangs, especially in border areas, has created insecurity for businesspeople. In addition, competition from China for offshored jobs from foreign firms has put downward pressure on opportunities for Mexico, as manufacturing facilities and some service facilities migrate from Mexico to China in a race for the lowest cost operations.⁶⁸

MERCOSUR is the fourth largest trading bloc after the EU, NAFTA, and ASEAN. Established in 1991, it comprises the original parties—Brazil, Argentina, Paraguay, and Uruguay; Venezuela is an applicant country awaiting ratification. This regional trading bloc comprises 250 million people and accounts for 75 percent of South America’s GDP.

Brazil

*Foreign companies are turning to Brazil not just for the size of its booming domestic market, but also as a platform to its Spanish-speaking neighbors. Fiat’s factory in Brazil, for example, is the second biggest in the world.*⁶⁹

The Federal Republic of Brazil is Latin America’s biggest economy and is the fifth largest country in the world in terms of land mass and population, with about 193 million people. According to the U.S. Department of Commerce, Brazil is the 7th largest economy in the world. Bolstered by demand from China and elsewhere for its raw materials, by strong domestic demand, and by a growing middle class, Brazil’s economy grew by 7.3 percent in 2010, and ranked 3rd in the 2012 FDI Confidence Index (see Exhibit 1-1).

While most of the developed world has been mired in debt and stunted growth prospects, Brazil's economy is stable and growth prospects are bright. Yet poor infrastructure remains an obstacle (less than 10 percent of roads are paved), and drastic inequality among Brazil's people hampers domestic growth. However, there will be considerable investment and export opportunities as Brazil spends billions in infrastructure development while it prepares for the World Cup in 2014 and the Olympics in 2016. Further discussion regarding doing business in Brazil is included in Chapter 3.

CAFTA: Modeled after the NAFTA agreement, the goal of the U.S.-Central America Free Trade Agreement (**CAFTA**) was to promote trade liberalization between the United States and five Central American countries: Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua. In 2004, the Dominican Republic joined the negotiations, and the agreement was renamed DR-CAFTA. Since then, U.S. exports to those countries have grown considerably because of the phase-out of most tariffs. CAFTA is considered to be a stepping-stone to the larger Free Trade Area of the Americas (FTAA) that would encompass 34 economies, but which has met with considerable resistance.⁷⁰

Other recent agreements include three trade agreements between the United States and South Korea, Colombia and Panama, all passed on October 12, 2011, bringing to 20 the total number of free trade agreements with the United States.⁷¹

Other Regions in the World

Sweeping political, economic, and social changes around the world present new challenges to global managers. The move toward privatization has had an enormous influence on the world economy. Economic freedom is a critical factor in the relative wealth of nations.

One of the most striking changes today is that most nations have suddenly begun to develop decentralized, free-market systems in order to manage a global economy of intense competition, the complexity of high-tech industrialization, and an awakening hunger for freedom.

THE RUSSIAN FEDERATION

Coca-Cola Co. and Coca-Cola Hellenic Bottling Company SA, plan to invest \$3 billion in Russia over the next five years as part of an ongoing push into emerging markets.

AP IN *NEW YORK TIMES*,
SEPTEMBER 26, 2011.⁷²

Foreign investment in Russia, as well as its consumers' climbing confidence and affluence, bode well for the economy. GDP growth for 2011 was about 4.3 percent. Membership in the WTO in 2011 promised additional trade liberalization. Until recently, Russia has been regarded as more politically stable. New land, legal, and labor codes have encouraged foreign firms to take advantage of opportunities in that immense area, in particular the vast natural resources and the well-educated population of 145 million. Moscow, in particular, is teeming with new construction sites, high-end cars, and new restaurants. Export opportunities abound in Russia, with a growing middle class and vast infrastructure needs. However, corruption and government interference persist, along with excessive regulations, lack of the rule of law, and infrastructure problems. The protests of the people in 2011 and 2012 indicated considerable unrest about political procedures that resulted in the return of President Putin. Further discussion of the business environment in Russia is in Chapter 7.

THE MIDDLE EAST

*"You start to differentiate in a post-Arab spring world and you look at the different markets that were affected," says Mustafa Abdel-Wadood, chief executive at Abraaj.*⁷³

FINANCIAL TIMES U.K.,
SEPTEMBER 22, 2011.

The changing geopolitical landscape due to the revolutions across the region, which toppled leaders in Tunisia and Egypt and ousted the regime of Colonel Muammar Gaddafi in Libya, have made investors wary, but looking for opportunities. Egypt, where the political landscape has been redrawn in recent months, is beginning to attract interest from Gulf, Western, and Asian international investors. "I think the main theme when considering whether to enter these markets is the potential for long-term growth that will ultimately lead to a more positive outcome."⁷⁴

According to *The Arab World Competitiveness Report* by the World Economic Forum, the United Arab Emirates is the most competitive economy in the Arab world among the countries at

the third and most advanced stage of development. It is followed by Qatar and Kuwait. Among countries at the second stage of development, Tunisia and Oman are the best performing Arab economies while Egypt is the regional best performer in the third group of countries. The Forum predicted there will be prosperity with challenges for the Middle East:

*Oil and gas revenues provide unique investment opportunities, but the region's greatest challenges are likely to be in managing expectations, lowering trade and investment barriers and educating the next generation to handle the wealth that is now being produced. Education is the biggest challenge.*⁷⁵

DEVELOPING ECONOMIES

Developing Economies are characterized by change that has come about more slowly as they struggle with low gross national product (GNP) and low per capita income, as well as the burdens of large, relatively unskilled populations and high international debt. Their economic situation and the often-unacceptable level of government intervention discourage the foreign investment they need. Many countries in Central and South America, the Middle East, and Africa desperately hope to attract foreign investment to stimulate economic growth.

THE AFRICAN UNION (AU)

The AU comprises the 53 African countries and was formed from the original Organization of African Unity (OAU) primarily to deal with political issues. According to the International Monetary Fund (IMF), as of 2012, seven of the world's ten fastest growing economies are in Africa. However, there continue to be many major problems in the region. Unfortunately, Africa has received little interest from most of the world's investors, although it receives increasing investment from companies in South Africa, which has the region's biggest economy. On the bright side, however, trade between China and Africa has risen from \$10 billion in 2000 to well over \$100 billion today. In fact, China's appetite for commodities has led to a \$12 billion FDI in 2011.⁷⁶ At a growth rate of over 5.2 percent in 2011, more than double that predicted for the U.S. or Europe, prospects for Africa are improving. For example, Coca-Cola's chief executive has targeted the African continent as one of the company's top investment priorities.⁷⁷

South Africa: The South African economy has been growing continuously since 1998, amid a more stable political environment since the defeat of apartheid. This is the longest economic upswing in the country's history although unemployment remains very high.⁷⁸ South Africa is a country of 48.7 million people that is rich in diverse cultures, people, and natural resources. "Enjoying remarkable macroeconomic stability and a pro-business environment, South Africa is a logical and attractive choice for U.S. companies to enter the African continent."⁷⁹

The rapid growth of consumer demand, along with increasing tourism and foreign business investment, has made the country's outlook very positive. Foreign investment is encouraged through the Strategic Industrial Project, which provides approved companies with substantial tax reductions as well as other incentives. These incentives, along with more political stability, encouraged the return of most of the foreign companies that had left during the apartheid era. In addition, companies in South Africa no doubt realize that they have a competitive edge on the African continent that they do not have in more developed parts of the world.⁸⁰ There is further discussion of the business climate in South Africa in the Chapter 6 opening profile.

For firms willing to take the economic and political risks, developing economies offer considerable potential for international business. Assessing the risk-return trade-offs and keeping up with political developments in these developing countries are two of the many demands on international managers. Among proactive managers taking advantage of such opportunities are those at Intel—a corporation that epitomizes the ways in which "globalization" is affecting less-developed countries (LDCs) and developing economies such as Vietnam, as discussed in the accompanying Management Focus.

The Globalization of Information Technology

Of all the developments propelling global business today, the one that is transforming the international manager's agenda more than any other is the rapid advance in information technology (IT). The explosive growth of IT is both a cause and an effect of globalism. The role of IT in international management is discussed under a later heading "The Technological Environment."



MANAGEMENT IN ACTION

*Intel Brings Changes to Vietnam's Economy and Culture*⁸¹

Intel Plant Put Vietnam on High-Tech Map

*Intel CEO Paul Otellini, Bloomberg News—October 29, 2010*⁸²

The United States opened trade relations with Vietnam in 2000, opening the way for that country's expansion. Although Vietnam is a communist country, its rapid growth can be attributed to its entrepreneurial traditions and those aspects of globalization that attract corporations such as Intel to take advantage of new markets and lower costs of production. While the debate continues about whether globalization brings overall positive or negative effects to less developed countries, the inevitable march of trade and investment has led Daniel Altman to believe that "the more relevant question today is whether these multinational relationships can be managed in a way that benefits both guests and hosts." Intel's success in this regard started with the awareness of the tight control of the Vietnamese government in all aspects of society and on foreign companies wishing to do business there.

After painstaking and secret negotiations with Vietnamese government officials who were unused to market economics, Intel's general manager, Rick Howath, decided to build its biggest semiconductor manufacturing plant ever along the Hanoi Highway in Vietnam, a nation of 85 million with limited higher education opportunities. This is Intel Corporation's seventh assembly site of its global network. (Other sites include Penang and Kulim, Malaysia; Cavite, Philippines; Chengdu and Shanghai, China; and San Jose, Costa Rica.) The plant has provided thousands of jobs and training for local workers to produce chips for the company's extensive global supply chain. In this way Intel has demonstrated how multinationals which are industry leaders can change the economic and cultural dynamics in a developing country by the decision to locate a plant there. However, this was no light decision. Intel's company strategic decision-makers spent years investigating and evaluating the benefits and constraints of locating in Vietnam and considerable effort in working with the government in Hanoi. The company's investigations were relentless, evaluating school curricula, traffic congestion, the poor infrastructure, and the size of the average adult in order to tailor the factory to them. Their main concern was finding enough qualified engineers.

In the end, the Vietnamese government's desire to attract multinationals, along with the country's proximity to China and its young, low-cost workforce, convinced Intel to invest \$1 billion there for its 115-acre construction site in the new Saigon Hi-Tech Park (Saigon is now called Ho Chi Minh City). The company called the project A-9. (Nine is regarded as a lucky number in Vietnam.) However, this was not until the government-owned Saigon Hi-Tech Park signed a pact with Intel to fight against corruption and improper business conduct. This was the first time a state agency had made such a pact and also a first for Intel, which was concerned about Vietnam's reputation as one of the world's most corrupt countries.

Changes resulting from Intel's investment in Vietnam are already evident. The Vietnamese government is giving Intel's managers unprecedented access to high-ranking officials, and other global giants are showing interest in investing there. The plant will create a higher-end manufacturing base beyond garment assembly lines and create desperately needed professional jobs for its youth. Intel is also bringing its culture to Vietnam. Executives work alongside the workers, with no big offices for the bosses—contrary to Vietnam's hierarchical culture. It also sponsors team-building exercises like karaoke Fridays. Intel's company buses shuttle workers to the plant, passing low-slung shacks, which house so many Vietnamese.

In all, the Vietnamese view the new plant in Ho Chi Minh City with patriotic pride and hope for further economic emergence. For its part, Intel's success is largely attributable to cultivating government officials and to understanding the government's goals and working towards them. These include the desire to increase the use of personal computers and the Internet, and also to build a reputation for Vietnam to export high-tech items. Focusing on local traditions and working with the government's Communist youth group, Intel developed a program under the brand Thanh Giong, a Vietnamese hero, with the goal of beating back the enemy of illiteracy.

The Globalization of Human Capital

Firms around the world have been offshoring manufacturing jobs to low-cost countries for decades. An increasing number of firms have been producing or assembling parts of their products in many countries; that is, outsourcing by contracting to a local firm, and then integrating them into their global supply chains. Although, with the recent much higher cost of fuel greatly increasing shipping rates, some firms were fearful that their cost advantage of producing abroad was being lost. Paul Fichter, owner of Taphandles, for example, made a decision in October 2011

to bring back some of its manufacturing to the United States because of the narrowing advantage of producing in China. Taphandles (beer taps for breweries) was employing 33 people in Seattle and 450 in China. His reasons included the increasing labor costs and benefit costs for competing for employees there, the higher shipping costs because of the rise in oil prices, and the increasing appreciation of the renminbi against the dollar.⁸³ In addition, hundreds of textile manufacturers, for example, have been diversifying their business to countries such as Cambodia, Vietnam, and Indonesia, where wages are lower than those in China, which have risen around 20 percent in the last three years.⁸⁴

But shipping costs do not affect non-manufacturing jobs, and more and more firms are outsourcing white-collar jobs to India, China, Mexico, and the Philippines: customer support, medical analysis, technical work, computer programming, form filling, and claims processing—all these jobs can now move around the globe in the same way that farming and factory jobs could move a century ago.⁸⁵ We have all experienced talking to someone in India when we call the airlines or a technology support service; now increasingly sophisticated jobs are being outsourced, leaving many people in developed economies to worry about job retention. For example, General Electric has about 14,500 employees in India, IBM more than 74,000, and Citigroup more than 10,000.⁸⁶ MoFirst provides programming services—a part of India's \$88.1 billion per year information technology services and outsourcing industry. The company's office in Bangalore houses twenty or so programmers coding on laptops. Most of its clients are in the U.S., Europe, and the Middle East, and MoFirst bills them \$15 to \$20 an hour—considerably less than the developers in the U.S. charge. India is experiencing considerable demand for its mobile-app development shops, such as for Apple's iPhone and iPad and for devices for running Google's Android software.⁸⁷

In Bangalore, India, MNCs such as Intel, Dell, IBM, Yahoo!, and AOL employ workers in chip design, software, call centers, and tax processing.⁸⁸ Dell has four call centers in India, where the bulk of its 10,000 employees work, as well as software development and product testing centers. Overall, the Indian IT-enabled services (ITES) sector has an estimated 700,000 people worldwide and comprises 35 percent of the Business Process Outsourcing (BPO) market.⁸⁹ Recently, however, large Indian IT outsourcing companies such as Infosys Limited and the Tata Group were hiring their staff in the United States.

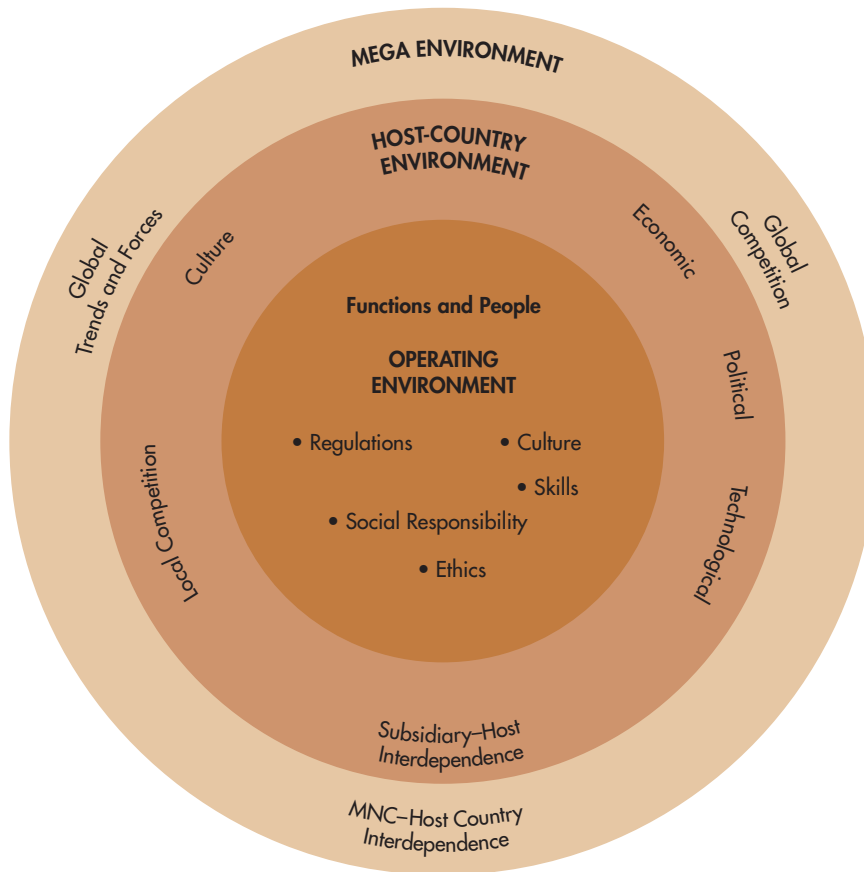
In China—long the world's low-cost manufacturing hub—jobs are on the upswing for back-office support for financial services and for telecom and retail companies in Asia. Such employees communicate with people in Hong Kong and Taiwan in local languages. While backlash from some European and U.S. firms' clients has resulted in them repatriating high-end jobs, white-collar job migration is still on the rise for firms around the world, bringing with it a new phase in economic globalization and competition. For global firms, winning the “war for talent” is one of the most pressing issues, especially as hot labor markets in emerging markets are causing extremely high turnover rates.⁹⁰ However, the shift in economic power to the East presents considerable opportunity for companies and economies in the West because of the rising buying power of the 2.5 billion or so people in those developing countries. In addition, firms from China and India, for example, are expanding overseas, bringing their investment and providing jobs, so that. . .

You might just find, for example, that your biggest customers are in Chengdu, not Chicago, or that your boss sits in New Delhi, not New York City. Your paycheck could come in renminbi or rupees instead of in euro or dollars.

TIME,
MARCH 28, 2011.⁹¹

The Global Manager's Role

Whatever your level of involvement, it is important to understand the global business environment and its influence on the manager's role. This complex role demands a contingency approach to dynamic environments, each of which has its own unique requirements. Within the larger context of global trends and competition, the rules of the game for the global manager are set by each country (see Exhibit 1-2): its political and economic agenda, its technological status and level of development, its regulatory environment, its comparative and competitive advantages, and its cultural norms. The astute manager will analyze the new environment, anticipate how

EXHIBIT 1-2 An Open Systems Model

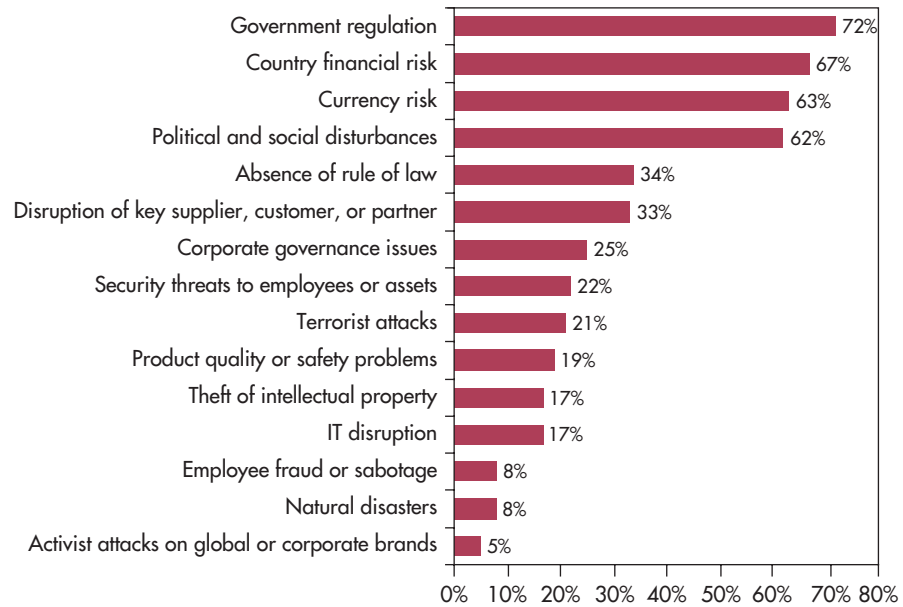
it may affect the future of the company, and then develop appropriate strategies and operating styles. She or he will need to take into account the business practices and expectations of varying sets of suppliers, partners, customers, and local managers. These factors in the manager's role are the subjects of the rest of this book.

THE POLITICAL AND ECONOMIC ENVIRONMENT

Proactive globally-oriented firms maintain an up-to-date profile of the political and economic environment of the countries in which they maintain operations (or have plans for future investment). Surveys of top executives around the world show that **sustainability**—economic, political, social, and environmental—has become a significant worldwide issue. Executives who recognize that fact are leading their companies to develop new policies and to invest in sustainability projects with the purpose of benefiting the environment as well as profitability.⁹² The opening profile described the general global risk environment. Among the strategic and operational risks reported by global companies were government regulation, country financial risks and currency risk, and political and social disturbances. These concerns and other risks, as reported by those companies, are shown in Exhibit 1-3.

From a separate survey in 2011 by the Aon Risk Solutions Company, we can see the top ten risks as reported by 960 companies from 58 countries, giving us an overview of how concerns can change over time. The risk of economic slowdown was the number one risk in 17 out of 27 industries surveyed, and across all countries reporting.

Those risks have different relative levels of priority and concern depending on the region. The risk of economic slowdown is the first concern across all regions, while subsequent risks vary across those regions. For example, “failure to attract/retain top talent” is far higher on the list for the Asia Pacific region than for the others. In addition, the Aon report noted that “Senior management's intuition and experience remains the primary method used by survey respondents

EXHIBIT 1-3 Greatest Risks Affecting FDI Decisions, as Reported by Global Companies

Source: www.atkearney.com, September 12, 2008. Copyright A. T. Kearney, Inc., 2007. All rights reserved. Reprinted with permission.

to identify and assess major risks facing their organizations.”⁹³ That led the researchers to conclude that formal risk management using business analytical tools would be more useful than experience in identifying new risks. The top ten risks overall were:

1. Economic slowdown.
2. Regulatory/legislative changes
3. Increasing competition
4. Damage to reputation/brand
5. Business interruption
6. Failure to innovate/meet customer needs
7. Failure to attract or retain top talent
8. Commodity price risk
9. Technology failure/system failure
10. Cash flow/liquidity risk.⁹⁴

An additional important aspect of the political environment is the phenomenon of ethnicity—a driving force behind political instability around the world. In fact, many uprisings and conflicts that are thought to be political in nature are actually expressions of differences among ethnic groupings. Often, religious disputes lie at the heart of those differences. Uprisings based on religion operate either in conjunction with ethnic differences (as probably was the case in the former Yugoslavia) or as separate from them (as in Northern Ireland). Many terrorist activities are also based on religious differences, as in the Middle East and other parts of the world. Managers must understand the ethnic and religious composition of the host country in order to anticipate problems of general instability, as well as those of an operational nature, such as effects on the workforce, on production and access to raw materials, and on the market.

Political Risk

Clearly, as evidenced by the 2011 “Arab Spring” uprisings in Egypt and elsewhere, major political changes can affect the business environment and risk level almost overnight. As far as political risk is concerned, a 2011 survey—based on 211 countries and territories—by Aon Risk Solutions (the firm discussed earlier), found that the political risk level is rising in more countries than it is declining. That conclusion was based on the level of exposure to factors such as currency inconvertibility and transfer; strikes, riots, and civil commotion; war; sovereign

nonpayment; political interference; supply chain interruption; and legal and regulatory risk.⁹⁵ It is clear from the past that firms operating in some countries are exposed to political risks that can drastically affect them with little warning, as illustrated by the following example:

After firms from Europe and the United States had moved their factories to China to avoid the taxes and quotas on rare earth exports, China closed the door on them in September 2011.⁹⁶

*By closing or nationalizing dozens of the producers of rare earth metals . . . China is temporarily shutting down most of the industry and crimping the global supply of the vital resources.*⁹⁷

The managers of a global firm need to investigate the political risks to which they expose their company in certain countries—and the implications of those risks for the economic success of the firm. **Political risks** are any governmental action or politically motivated event that could adversely affect the long-run profitability or value of a firm. The Middle East, as we have seen, has traditionally been an unstable area where political risk heavily influences business decisions.

Nationalization In unstable areas, multinational corporations weigh the risks of nationalization or expropriation. In April 2012, Argentina, under President Cristina Fernandez de Kirchner, announced plans to nationalize Repsol YPF, the Spanish oil company, taking a 51 percent stake in YPF, which accounts for a third of Argentina's oil production.⁹⁸ In retaliation, Spain announced that it would restrict imports of biodiesel from Argentina. **Nationalization** refers to the forced sale of an MNC's assets to local buyers, with some compensation to the firm, perhaps leaving a minority ownership with the MNC. As the fallout from the financial meltdown spread around the world in 2009, nationalist impulses gathered storm as government moves to take stakes in ailing industries were verging on partial or full nationalization—though, for the most part, not forcing it. Japan, for example, took a cue from the United States in taking majority stakes in major banks; while in Russia, the Kremlin was exploiting the economic crisis to establish more control over industries that it had long coveted, such as energy.⁹⁹

Expropriation occurs when a local government seizes and provides inadequate compensation for the foreign-owned assets of an MNC; when no compensation is provided, it is confiscation. In countries that have a proven history of stability and consistency, the political risk to a multinational corporation is relatively low. The risk of expropriation is highest in countries that experience continuous political upheaval, violence, and change, as evidenced by actions such as those taken by Hugo Chavez in his continuing drive to place key industries under state control, as shown when he took control of Mexico's Cemex cement plants in Venezuela.

An event that affects all foreign firms doing business in a country or region is called a **macropolitical risk event**. In many regions, **terrorism** poses a severe and random political risk to company personnel and assets and can, obviously, interrupt the conduct of business. According to Micklous, terrorism is “the use, or threat of use, of anxiety-inducing . . . violence for ideological or political purposes.”¹⁰⁰ The increasing incidence of terrorism around the world concerns MNCs. In particular, the kidnapping of business executives has become quite common. In addition, the random acts of violence around the world have a downward effect on global expansion, not the least because of the difficulty in attracting and retaining good managers in high-risk areas, as well as the expense of maintaining security to protect people and assets and the cost of insurance to cover them. Companies that go ahead and invest in those high-risk areas do so with the expectation of a higher profit premium to offset risk.

An event that affects one industry or company or only a few companies is called a **micropolitical risk event**. Such events have become more common than macropolitical risk events. Such micro action is often called “creeping expropriation,” indicating a government's gradual and subtle action against foreign firms. This is a situation that occurs when you haven't been expropriated, but it takes ten times longer to do anything. Typically, such continuing problems with an investment present more difficulty for foreign firms than do major events that are insurable by political-risk insurers. The following list describes seven typical political risk events common today (and possible in the future):

1. Expropriation of corporate assets without prompt and adequate compensation
2. Forced sale of equity to host-country nationals, usually at or below depreciated book value
3. Discriminatory treatment against foreign firms in the application of regulations or laws
4. Barriers to **repatriation** of funds (profits or equity)

5. Loss of technology or other intellectual property (such as patents, trademarks, or trade names)
6. Interference in managerial decision making
7. Dishonesty by government officials, including canceling or altering contractual agreements, extortion demands, and so forth.¹⁰¹

Political Risk Assessment

International companies must conduct some form of political risk assessment to manage their exposure to risk and to minimize financial losses. Typically, local managers in each country assess potentially destabilizing issues and evaluate their future impact on their company, making suggestions for dealing with possible problems. Corporate advisers then establish guidelines for each local manager to follow in handling these problems. Dow Chemical has a program in which it uses line managers trained in political and economic analysis, as well as executives in foreign subsidiaries, to provide risk analyses of each country.

Risk assessment by multinational corporations usually takes two forms. One uses experts or consultants familiar with the country or region under consideration. Such consultants, advisers, and committees usually monitor important trends that may portend political change, such as the development of opposition or destabilizing political parties. They then assess the likelihood of political change and develop several plausible scenarios to describe possible future political conditions. A second and increasingly common means of political risk assessment used by MNCs is the development of internal staff and in-house capabilities. This type of assessment may be accomplished by having staff assigned to foreign subsidiaries, by having affiliates monitor local political activities, or by hiring people with expertise in the political and economic conditions in regions critical to the firm's operations. Frequently, all means are used. The focus must be on monitoring political issues before they become headlines; the ability to minimize the negative effects on the firm—or to be the first to take advantage of opportunities—is greatly reduced once the news spreads through social media or CNN. No matter how sophisticated the methods of political risk assessment become, nothing can replace timely information from people on the front line.

In addition to assessing the political risks facing a firm, alert managers also examine the specific types of impact that such risks may have on the company. For an autonomous international subsidiary, most of the impact from political risks (nationalization, terrorism) will be at the level of the ownership and control of the firm, because its acquisition by the host country would provide the state with a fully operational business. For global firms, the primary risks are likely to be from restrictions (on imports, exports, currency, and so forth), with the impact at the level of the firm's transfers (or exchanges) of money, products, or component parts.

Managing Political Risk

After assessing the potential political risk of investing or maintaining current operations in a specific country, managers face perplexing decisions on how to manage that risk. On one level, they can decide to suspend their firm's dealings with a certain country at a given point—either by the avoidance of investment or by the withdrawal of current investment (by selling or abandoning plants and assets). On another level, if they decide that the risk is relatively low in a particular country or that a high-risk environment is worth the potential returns, they may choose to start (or maintain) operations there and to accommodate that risk through adaptation to the political regulatory environment. That adaptation can take many forms, each designed to respond to the concerns of a particular local area. Some means of adaptation suggested by Taoka and Beeman are as follows:

1. Equity sharing includes the initiation of joint ventures with nationals (individuals or those in firms, labor unions, or government) to reduce political risks.
2. Participative management requires that the firm actively involve nationals, including those in labor organizations or government, in the management of the subsidiary.
3. Localization of the operation includes the modification of the subsidiary's name, management style, and so forth, to suit local tastes. Localization seeks to transform the subsidiary from a foreign firm to a national firm.
4. Development assistance includes the firm's active involvement in infrastructure development (foreign-exchange generation, local sourcing of materials or parts, management training, technology transfer, securing external debt, and so forth).¹⁰²

In addition to avoidance and adaptation, two other means of risk reduction available to managers are dependency and hedging. Some means that managers might use to maintain **dependency**—keeping both the subsidiary and the host nation dependent on the parent corporation—include, for example, maintaining control over key inputs or technology, or control over distribution; other means are through expatriate control in key positions.¹⁰³ Firms can also minimize loss through **hedging**, which includes, for example, political risk insurance and local debt financing.

Multinational corporations also manage political risk through their global strategic choices. Many large companies diversify their operations both by investing in many countries and by operating through joint ventures with a local firm or government or through local licensees. By involving local people, companies, and agencies, firms minimize the risk of negative outcomes due to political events. (See Chapters 6 and 7 for further discussion of these and other global strategies.)

Managing Terrorism Risk

No longer is the risk of terrorism for global businesses focused only on certain areas such as South America or the Middle East. That risk now has to be considered in countries such as the United States, which had previously been regarded as safe. Eighty countries lost citizens in the World Trade Center attack on September 11, 2001. Many companies from Asia and Europe had office branches in the towers of the World Trade Center; most of those offices, along with the employees from those countries, were destroyed in the attack. Thousands of lives and billions of dollars were lost, not only by those immediately affected by the attack but also by countless small and large businesses impacted by the ripple effect; global airlines and financial markets were devastated.

As incidents of terrorism accelerate around the world, many companies are increasingly aware of the need to manage the risk of terrorism. In high-risk countries, both IBM and Exxon Mobil try to develop a benevolent image through charitable contributions to the local community. They also try to maintain low profiles and minimize publicity in the host countries by using, for example, discreet corporate signs at company sites.¹⁰⁴

Some companies have put together teams to monitor the patterns of terrorism around the world. Kidnappings are common in Latin America (as a means of raising money for political activities). In the Middle East, car bombs, airplane hijackings, kidnapping of foreigners, and black-mail (for the release of political prisoners) are common. In Western Europe, terrorists typically aim bombs at U.S.-owned banks and computer companies. Almost all MNCs have stepped up their security measures abroad, hiring consultants in counterterrorism (to train employees to cope with the threat of terrorism) and advising their employees to avoid U.S. airlines when flying overseas. For many firms, however, the opportunities outweigh the threats, even in high-risk areas.

Economic Risk

Closely connected to a country's political stability is its economic environment—and the relative risk that it may pose to foreign companies. A country's level of economic development generally determines its economic stability and, therefore, its relative risk to a foreign firm. Historically, most industrialized nations have posed little risk of economic instability; less-developed nations pose more risk. However, as of 2012, the level of economic risk in Europe, for example, was a great concern around the world, in particular regarding concerns in the eurozone brought about by debt problems in Greece. As in 2008, the interdependence of financial institutions around the world was again threatening a global recession.

In 2011 the Heritage Foundation published its annual Index of Economic Freedom (excerpted in Table 1–2) which covers 183 countries and is based on ten specific freedoms such as trade freedom, business freedom, investment freedom, and property rights—all of which reduce economic risk. Interestingly, the much discussed emerging “BRICs”—Brazil, Russia, India and China—are way down on the list, indicating that there is quite a risk-return trade-off for investment in those markets. (Further details of each country on the index are available at www.heritage.org.)

*In economically free societies, governments allow labor, capital, and goods to move freely, and refrain from coercion or constraint of liberty beyond the extent necessary to protect and maintain liberty itself.*¹⁰⁵

TABLE 1-2 Index of Economic Freedom

Rank	Country	Score
1	Hong Kong	89.7
2	Singapore	87.2
3	Australia	82.5
4	New Zealand	82.3
5	Switzerland	81.9
6	Canada	80.8
7	Ireland	78.7
8	Denmark	78.6
9	United States	77.8
10	Bahrain	77.7
113	Brazil	56.3
124	India	54.6
135	China	52.0
143	Russia	50.5

Source: Based on selected data from the Heritage Foundation, 2011. <http://www.heritage.org>

A country's ability or intention to meet its financial obligations determines its economic risk. The economic risk incurred by a foreign corporation usually falls into one of two main categories. Its subsidiary (or other investment) in a specific country may become unprofitable if (1) the government abruptly changes its domestic monetary or fiscal policies, or (2) the government decides to modify its foreign-investment policies. The latter situation would threaten the company's ability to repatriate its earnings and would create a financial or interest-rate risk. Furthermore, the risk of exchange-rate volatility results in currency translation exposure to the firm when the balance sheet of the entire corporation is consolidated, and may cause a negative cash flow from the foreign subsidiary. Currency translation exposure occurs when the value of one country's currency changes relative to that of another. When exchange-rate changes are radical, repercussions are felt around the world.

Because every MNC operating overseas exposes itself to some level of economic risk, often affecting its everyday operational profitability, managers constantly reassess the level of risk that their companies may face in any specific country or region of the world. Methods of analyzing economic risk or a country's creditworthiness include the quantitative approach, the qualitative approach and the checklist approach.

The **quantitative approach**, says Mathis, "attempts to measure statistically a country's ability to honor its debt obligation"¹⁰⁶ by assigning different weights to economic variables. The **qualitative approach** evaluates a country's economic risk by assessing the competence of its leaders and analyzing the types of policies they are likely to implement. The **checklist approach** relies on a few easily measurable and timely criteria believed to reflect or indicate changes in the creditworthiness of the country. Most corporations recognize that no single approach can provide a comprehensive economic risk profile of a country. Therefore, they try to use a combination of approaches by selecting those variables to follow which they have found to be the most relevant indicators for the company.

THE LEGAL ENVIRONMENT

The prudent global manager consults with legal services, both locally and at headquarters, to comply with host-country regulations and to maintain cooperative long-term relationships in the local area. If the manager waits until a problem arises, little legal recourse may be available outside of local interpretation and enforcement. Indeed, this has been the experience of many foreign managers in China, where financial and legal systems remain limited in spite of attempts to show the world a capitalist face. Managers there often simply ignore their debts to foreign companies as they did under the old socialist system. The lesson for many foreign companies in

China is that they are losing millions because Beijing often does not stand behind the commitments of its state-owned enterprises.

Although no guarantee is possible, the risk of massive losses may be minimized, among other ways, by making sure you get approval from related government offices (national, provincial, and local), by seeing that you are not going to run amok of long-term government goals, and by getting loan guarantees from the headquarters of one of Beijing's main banks. Some of the contributing factors in cases that go against foreign companies are often the personal connections—*guanxi*—involved and the fact that some courts offer their services to the business community for profit. In addition, many judges get their jobs through nepotism rather than by virtue of a law degree.

Although the regulatory environment for international managers consists of the many local laws and the court systems in those countries in which they operate, certain other legal issues are covered by international law, which governs relationships between sovereign countries, the basic units in the world political system. One such agreement, which regulates international business by spelling out the rights and obligations of the seller and the buyer, is the United Nations Convention on Contracts for the International Sale of Goods (CISG). This applies to contracts for the sale of goods between countries that have adopted the convention.

Generally speaking, the manager of the foreign subsidiary or foreign operating division will comply with the host country's legal system. Such systems, derived from common law, civil law, or Islamic law (Sharia Law), are a reflection of the country's culture, religion, and traditions. Under **common law**, used in the United States and 26 other countries of English origin or influence, past court decisions act as precedents to the interpretation of the law and to common custom. **Civil law** is based on a comprehensive set of laws organized into a code. Interpretation of these laws is based on reference to codes and statutes. About 70 countries, predominantly in Europe (e.g., France and Germany), are ruled by civil law, as is Japan. In Islamic countries, such as Saudi Arabia, the dominant legal system is **Islamic law**; based on religious beliefs, it dominates all aspects of life. Islamic law is followed in approximately 27 countries and combines, in varying degrees, civil, common, and indigenous law.

Contract Law

A **contract** is an agreement by the parties concerned to establish a set of rules to govern a business transaction. Contract law plays a major role in international business transactions because of the complexities arising from the differences in the legal systems of participating countries and because the host government in many developing and state-controlled countries is often a third party in the contract. Both common law and civil law countries enforce contracts, although their means of resolving disputes differ. Under civil law, it is assumed that a contract reflects promises that will be enforced without specifying the details in the contract; under common law, the details of promises must be written into the contract to be enforced. Astute international managers recognize that they will have to draft contracts in legal contexts different from their own, and they prepare themselves accordingly by consulting with experts in international law before going overseas. While Western companies want to spell out every detail in a contract, in some countries the contract may be ignored or changed, and in Asia, "there is no shortcut for managing the relationship."¹⁰⁷ In other words, the contract is in the relationship, not on the paper, and the way to ensure the reliability of the agreement is to nurture the relationship.

Neglect regarding contract law may leave a firm burdened with an agent who does not perform the expected functions, or a firm may be faced with laws that prevent management from laying off employees (which, for example, is often the case in some countries in Europe).

Other Regulatory Issues

Differences in laws and regulations from country to country are numerous and complex. These and other issues in the regulatory environment that concern multinational firms are briefly discussed here.

Countries often impose protectionist policies, such as tariffs and non-tariff barriers, quotas, and other import and trade restrictions, to give preference to their own companies and industries. The Japanese have come under much criticism for protectionism, which they use to limit imports of foreign goods while they continue exporting consumer goods (e.g., cars and electronics) on a large scale.

A country's tax system influences the attractiveness of investing in that country and affects the relative level of profitability for an MNC. Foreign tax credits, holidays, exemptions, depreciation allowances, and taxation of corporate profits are additional considerations the foreign investor must examine before acting. Many countries have signed tax treaties (or conventions) that define such terms as "income," "source," and "residency" and spell out what constitutes taxable activities.

The level of government involvement in the economic and regulatory environment varies a great deal among countries and has a varying impact on management practices. In Canada, for example, the government has a significant involvement in the economy. It has a powerful role in many industries, including transportation, petrochemicals, fishing, steel, textiles, and building materials—forming partly owned or wholly owned enterprises. Wholly owned businesses are called Crown Corporations (Petro Canada, Ontario Hydro, Saskatchewan Telecommunications, and so forth), many of which are as large as major private companies. The government's role in the Canadian economy, then, is one of both control and competition. Government policies, subsidies, and regulations directly affect the manager's planning process, as do other major factors in the Canadian legal environment, such as the high proportion of unionized workers (30 percent). In Quebec, the law requiring official bilingualism imposes considerable operating constraints and expenses. For a foreign subsidiary, this regulation forces managers to speak both French and English and to incur the costs of language training for employees, translators, the administration of bilingual paperwork, and so on.

THE TECHNOLOGICAL ENVIRONMENT

The effects of technology around the world are pervasive—both in business and in private lives. In many parts of the world, whole generations of technological development are being skipped over. For example, many people will go straight to a digital phone without ever having had their houses wired under the analog system. In Entasopia, Kenya, its 4,000 inhabitants have no bank, no post office, and scant infrastructure of any kind. Yet it was there that three young engineers, with financial backing from Google, installed a small satellite dish powered by a solar panel, to hook up a handful of computers in the community center to the rest of the world. Google is paying the monthly fees for bandwidth connection. Locals can now send information instantly instead of having to physically travel to deliver it.¹⁰⁸

Advances in information technology are bringing about increased productivity—for employees, for companies, and for countries. As noted by Thomas Friedman, technology, as well as other factors that are opening up borders—"the opening of the Berlin Wall, Netscape, work flow, outsourcing, offshoring, open-sourcing, insourcing, supply-chaining, in-forming"—have converged to create a more level playing field. The result of this convergence was

The creation of a global, Web-enabled playing field that allows for multiple forms of collaboration—the sharing of knowledge and work—in real time, without regard to geography, distance, or, in the near future, even language.

Now that we are in a global information society, it is clear that corporations must incorporate into their strategic planning and their everyday operations the accelerating macro-environmental phenomenon of *technoglobalism*—in which the rapid developments in information and communication technologies (ICTs) are propelling globalization and vice versa. Investment-led globalization is leading to global production networks, which results in global diffusion of technology to link parts of the value-added chain in different countries. That chain may comprise parts of the same firm, or it may comprise suppliers and customers, or technology-partnering alliances among two or more firms. Either way, technological developments are facilitating, indeed necessitating, the firm network structure that allows flexibility and rapid response to local needs.

Clearly, the effects of technology on global trade and business transactions cannot be ignored; in addition, the Internet is propelling electronic commerce around the world. The ease of use and pervasiveness of the Internet raise difficult questions about ownership of intellectual property, consumer protection, residence location, taxation, and other issues.

New technology specific to a firm's products represents a key competitive advantage to firms and challenges international businesses to manage the transfer and diffusion of proprietary



UNDER THE LENS

Information Technology (IT)

The rapid advancement in IT and its applications around the world has had, and will continue to have, a transformative effect on global business for businesses of all sizes. The speed and accuracy of information transmission are changing the nature of the global manager's job by making geographic barriers less relevant. Indeed, the necessity of being able to access IT is being recognized by managers and families around the world, who are giving priority to that access over other lifestyle accoutrements.

Information can no longer be totally controlled by governments; political, economic, market, and competitive information is available almost instantaneously to anyone around the world, permitting informed and accurate decision making. Even cultural barriers are being lowered gradually by the role of information in educating societies about one another. Indeed, as consumers around the world become more aware, through various media, of how people in other countries live, their tastes and preferences begin to converge, as the "Arab Spring" illustrated.

The explosive growth of information technology is both a cause and an effect of globalism. The information revolution is boosting productivity around the world. Sweden is the most networked economy in the world, followed by Singapore, Finland, Switzerland, and the United States, according to the 2011 edition of the *Global Information Technology Report*. The report assessed 138 economies and ranked their Information Communications Technology (ICT) readiness levels to use and benefit from ICT for increased growth and development. (Table 1–3 shows the top ten as well as the ranks of selected other countries.) The report stresses the key role of ICT as an enabler of a more economically, environmentally, and socially sustainable world. Among the top ten, Finland, Taiwan, and the Republic of Korea posted the most notable improvements.¹⁰⁹

Indeed, the city of Seoul—where nine of every 10 residents subscribe to a high-speed wireless Internet connection—is already one gigantic hot spot. "By 2015, when 80 percent of the residents are expected to carry smartphones or tablet PCs, wireless connectivity will be almost as free as it is ubiquitous: the municipal authorities are installing free Wi-Fi wireless hot spots in all the city's public spaces, including 360 parks, 3,200 intersections and 2,200 streets around shopping centers."¹¹⁰ Every subway car, motel room, and street corner has high-speed Internet connectivity.

Making cities such as Seoul "smart" is intended to both improve productivity and attract businesses there. In addition, use of the Internet is propelling electronic commerce around the world (as discussed later in this chapter). Companies around the world are linked electronically to their employees, customers, distributors, suppliers, and alliance partners in many countries, resulting in increased communication and efficiency, as is described in the Procter and Gamble website: "P&G has more than 80 video collaboration studios globally. The immersive environment created by video studios allows employees to

TABLE 1–3 The Network Readiness Index 2011

Top Ten Rank by Country		Selected Other Ranks	
1	Sweden	Germany	13
2	Singapore	United Kingdom	15
3	Finland	Australia	17
4	Switzerland	Japan	19
5	United States	France	20
6	Taiwan, China	China	36
7	Denmark	India	48
8	Canada	Brazil	56
9	Norway	Russia	77
10	Korea, Republic of	Mexico	78

Source: Based on selected data from The Global Information Technology Report 2010–2011, World Economic Forum.

(Continued)

connect face to face from any part of the world—as if they were in the same room. These studios greatly reduce the need for travel—saving money, time, and reducing P&G's carbon footprint.”¹¹¹

Technology, in all its forms, gets dispersed around the world by **multinational enterprises (MNEs)** and their alliance partners in many countries. However, some of the information intended for electronic transmission is currently subject to export controls by an EU directive intended to protect private information about its citizens. In addition, some countries, such as China, monitor and limit electronic information flows. So, perhaps IT is not yet “borderless” but rather is subject to the same norms, preferences, and regulations as “human” cross-border interactions.

technology, with its attendant risks. Whether it is a product, a process, or a management technology, an MNC's major concern is the **appropriability of technology**—that is, the ability of the innovating firm to profit from its own technology by protecting it from competitors.

An MNC can enjoy many technological benefits from its global operations. Advances resulting from cooperative research and development (R&D) can be transferred among affiliates around the world, and specialized management knowledge can be integrated and shared. However, the risks of technology transfer and pirating are considerable and costly. Although firms face few restrictions on the creation and dissemination of technology in developed countries, less developed countries often impose restrictions on licensing agreements, royalties, and so forth, as well as on patent protection.

In most countries, governments use their laws to some extent to control the flow of technology. These controls may be in place for reasons of national security. Other countries in earlier stages of development use their investment laws to acquire needed technology (usually labor-intensive technology to create jobs), increase exports, use local technology, and train local people.

The most common methods of protecting proprietary technology are the use of patents, trademarks, trade names, copyrights, and trade secrets. Various international conventions afford some protection in participating countries; more than 80 countries adhere to the International Convention for the Protection of Industrial Property (often referred to as the Paris Union) for the protection of patents. However, restrictions and differences in the rules in some countries not signatory to the Paris Union, as well as industrial espionage, pose continuing problems for firms trying to protect their technology.

One risk to a firm's intellectual property is the inappropriate use of the technology by joint-venture partners, franchisees, licensees, and employees (especially those who move to other companies). Some countries rigorously enforce employee secrecy agreements.

Another major consideration for global managers is the need to evaluate the **appropriateness of technology** for the local environment—especially in less-developed countries. Studying the possible cultural consequences of the transfer of technology, managers must assess whether the local people are ready and willing to change their values, expectations, and behaviors on the job to use new technological methods, whether applied to production, research, marketing, finance, or some other aspect of the business. Often, a decision regarding the level of technology transfer is dominated by the host government's regulations or requirements. In some instances, the host country may require that foreign investors import only their most modern machinery and methods so that the local area may benefit from new technology. In other cases, the host country may insist that foreign companies use only labor-intensive processes, which can help to reduce high unemployment in an area.

When the choice is left to international managers, experts in economic development recommend that managers make informed choices about appropriate technology. The choice of technology may be capital intensive, labor intensive, or intermediate, but the key is that it should suit the level of development in the area and the needs and expectations of the people who will use it.

Global E-Business

Without doubt, the Internet has had a considerable impact on how companies buy and sell goods around the world—mostly raw materials and services going to manufacturers. Internet-based electronic trading and data exchange are changing the way companies do business while breaking down global barriers of time, space, logistics, and culture. However, the Internet is not totally open; governments still make sure that their laws are obeyed in cyberspace. This was evidenced

when France forced Yahoo! to stop displaying Nazi trinkets for sale where French people could view them.¹¹² The reality is that

Different nations, and different peoples, may want a different kind of Internet—one whose language, content, and norms conform more closely to their own.

There is no doubt, however, that the Internet has introduced a new level of global competition by providing efficiencies through reducing the number of suppliers and slashing administration costs throughout the value chain. **E-business** is “the integration of systems, processes, organizations, value chains, and entire markets using Internet-based and related technologies and concepts.”¹¹³ **E-commerce** refers directly to the marketing and sales process via the Internet. Firms use e-business to help build new relationships between businesses and customers.¹¹⁴ The Internet and e-business provide a number of uses and advantages in global business, including the following:

1. Convenience in conducting business worldwide; facilitating communication across borders contributes to the shift toward globalization and a global market.
2. An electronic meeting and trading place, which adds efficiency in conducting business sales.
3. A corporate Intranet service, merging internal and external information for enterprises worldwide.
4. Power to consumers as they gain access to limitless options and price differentials.
5. A link and efficiency in distribution.¹¹⁵

Although most early attention was on e-commerce, experts now believe the real opportunities are in business-to-business (**B2B**) transactions. Alibaba (China) for example, is the largest B2B site in the world, with over 60 million subscribers (see the Part 3 comprehensive case on Alibaba). In addition, while the scope, complexity, and sheer speed of the B2B phenomenon, including e-marketplaces, have global executives scrambling to assess the impact and their own competitive roles, estimates for growth in the e-business marketplace may have been overzealous because of the global economic slowdown and its resultant dampening of corporate IT spending. While we hear mostly about large companies embracing B2B, it is noteworthy that a large proportion of current and projected B2B use is by small and medium-sized firms, for three common purposes: supply chain, procurement, and distribution channel.

A successful Internet strategy—especially on a global scale—is, of course, not easy to create. Potential problems abound, as experienced by the European and U.S. companies surveyed by Forrester Research. Such problems include internal obstacles and politics, difficulties in regional coordination and in balancing global versus local e-commerce, languages and cultural differences, and local laws. Such a large-scale change in organizing business clearly calls for absolute commitment from the top, empowered employees with the willingness to experiment, and good internal communications.¹¹⁶ Barriers to the adoption and progression of e-business around the world include lack of readiness of partners in the value chain, such as suppliers. If companies want to have an effective marketplace, they usually must invest in increasing their trading partners’ readiness and their customers’ capabilities. Other barriers are cultural. In Europe, for example, “Europe’s e-commerce excursion has been hindered by a laundry list of cultural and regulatory obstacles, like widely varying tax systems, language hurdles, and currency issues.”¹¹⁷

In other areas of the world, barriers to creating global e-businesses include differences in physical, information, and payment infrastructure systems. In such countries, innovation is required to use local systems for implementing a Web strategy. In Japan, for example, very few transactions are conducted using credit cards. Typically, bank transfers and COD are used to pay for purchases. Also, many Japanese use convenience stores, such as 7-Eleven Japan, to pay for their online purchases by choosing that option online.¹¹⁸

For these reasons, B2B e-business is likely to expand globally faster than **B2C** (business-to-consumer) transactions, such as Amazon.com. In addition, consumer e-commerce depends on each country’s level of access to computers and the Internet, as well as the relative efficiency of home delivery. Clearly, companies who want to go global through e-commerce must localize to globalize, which means much more than just presenting online content in local languages.

*Localizing . . . also means recognizing and conforming to the nuances, subtleties, and tastes of multiple local cultures, as well as supporting transactions based on each country’s currency, local connection speeds, payment preferences, laws, taxes, and tariffs.*¹¹⁹

In spite of various problems, use of the Internet to facilitate and improve global competitiveness continues to be explored and discovered. In the public sector in Europe, for example, the European Commission advertises tender invitations online in order to transform the way public sector contracts are awarded, using the Internet to build a truly single market.

It is clear that e-business is not only a new Web site on the Internet but also a source of significant strategic advantage. Hoping to capture this strategic advantage, the European Airbus venture—a public and private sector combination—joined a global aerospace B2B exchange for aircraft parts. The exchange illustrates two major trends in global competition: (1) those of cooperative global alliances, even among competitors, to achieve synergies and (2) the use of technology to enable those connections and synergies. Indeed, “leading B2B firms, including Accenture, DuPont, GE, and IBM, spend significant amounts of money and effort building and managing their brands, and those brands account for a significant portion of their market capitalization.”¹²⁰ In addition, many small businesses exist almost completely online as B2Bs, purchasing, marketing, and selling their products and services in the ether without ever having to build a physical storefront. Their B2B services can even help small businesses look and feel like a large business. Examples of services for small businesses include smallbusiness@yahoo.com, and www.microsoftsmallbusiness.com.¹²¹

CONCLUSION

A skillful global manager cannot develop a suitable strategic plan or consider an investment abroad without first assessing the environment—political, economic, legal, and technological—in which the company will operate. This assessment should result not so much in a comparison of countries as in a comparison of (1) the relative risk and (2) the projected return on investments among these countries. Similarly, for ongoing operations, both the subsidiary manager and headquarters management must continually monitor the environment for potentially unsettling events or undesirable changes that may require the redirection of certain subsidiaries or the entire company. Some of the critical factors affecting the global manager's environment (and therefore requiring monitoring) are listed in Exhibit 1-4.

Risk in the global environment, as discussed in this chapter, has become the new frontier in global business. The skills of companies and the measures taken to manage their exposure to risk on a world scale will soon largely replace their ability to develop, produce, and market global brands as the key element in global competitive advantage.

EXHIBIT 1-4 The Environment of the Global Manager

Political Environment	Economic Environment
• Form of government • Political stability • Foreign policy • State companies • Role of military • Level of terrorism • Restrictions on imports/exports	• Economic system • State of development • Economic stability • GNP • International financial standing • Monetary/fiscal policies • Foreign investment
Regulatory Environment	Technological Environment
• Legal system • Prevailing international laws • Protectionist laws • Tax laws • Role of contracts • Protection for proprietary property • Environmental protection	• Level of technology • Availability of local technical skills • Technical requirements of country • Appropriability • Transfer of technology • Infrastructure
Cultural Environment (see Part 2)	

The pervasive role of culture in international management will be discussed fully in Part 2, with a focus on how the managerial functions and the daily operations of a firm are also affected by a subtle, but powerful, environmental factor in the host country—that of societal culture.

Chapter 2 presents some increasingly critical, and scrutinized, factors in the global environment—those of sustainability, corporate social responsibility (CSR), and ethical behavior. We will consider a variety of questions: What is the role of the firm in the future of other societies and their people? What stakeholders must managers consider in their strategic and operational decisions in other countries? How do the expectations of firm behavior vary around the world, and should those expectations influence the international manager's decisions? What role does long-term global economic interdependence and sustainability play in the firm's actions in other countries?

Summary of Key Points

1. Competing in the twenty-first century requires firms to invest in the increasingly refined managerial skills needed to perform effectively in a multicultural environment. Managers need a global orientation to meet the challenges of world markets and rapid, fundamental changes in a world of increasing economic interdependence.
2. International management is the process of developing strategies, designing and operating systems, and working with people around the world to ensure sustained competitive advantage.
3. One major direction in world trade is the rise of rapidly developing economies, such as China, India, Brazil, and Russia (often called the BRIC countries). Other emerging markets include Indonesia, Turkey, and South Africa.
4. Drastic worldwide changes present dynamic challenges to global managers. They include the political and economic trend toward the privatization of businesses, uprisings in some countries where people are demanding democracy, rapid advances in information technology, and the management of offshore human capital. Recently, global economic woes have been causing a resurgence of protectionism and nationalism around the world.
5. Global managers must be aware of political risks around the world that can adversely affect the long-run profitability or value of a firm. Managers must evaluate various means to either avoid or minimize the effects of political risk.
6. The risk of terrorist activity represents an increasing risk around the world. Managers have to decide how to incorporate that risk factor in their strategic and operational plans.
7. Economic risk refers to a country's ability to meet its financial obligations. The risk is that the government may change its economic policies, thereby making a foreign company unprofitable or unable to repatriate its foreign earnings.
8. The regulatory environment comprises the many different laws and courts of those nations in which a company operates. Most legal systems derive from the common law, civil law, or Islamic law.
9. Use of the Internet in e-commerce—in particular, in business-to-business (B2B) transactions—and for intracompany efficiencies, has become a critical factor in global competitiveness.
10. The appropriability of technology is the ability of the innovating firm to protect its technology from competitors and to obtain economic benefits from that technology. Risks to the appropriability of technology include technology transfer, pirating, and legal restrictions on the protection of proprietary technology. Intellectual property can be protected through patents, trademarks, trade names, copyrights, and trade secrets.

Discussion Questions

1. Poll your classmates about their attitudes towards “globalization.” What are the trends and opinions around the world that underlie those attitudes?
2. Describe the recent effects of financial globalization on the world economy. What actions have governments taken to offset negative effects? Are they working?
3. How has the economic downturn impacted trends in protectionism and nationalization?
4. Discuss examples of recent macropolitical risk events and the effect they have or might have on a foreign subsidiary. What are micropolitical risk events? Give some examples and explain how they affect international business.
5. What means can managers use to assess political risk? What do you think is the relative effectiveness of these different methods? At the time you are reading this, what countries or areas do you feel have political risk sufficient to discourage you from doing business there?
6. Can political risk be “managed”? If so, what methods can be used to manage such risk, and how effective are they? Discuss the lengths to which you would go to manage political risk relative to the kinds of returns you would expect to gain.
7. Explain what is meant by the economic risk of a nation. Use a specific country as an example. Can economic risk in this country be anticipated? How? How does economic instability affect other nations?

8. Discuss the importance of contracts in international management and how contracts are viewed in other countries. What steps must a manager take to ensure a valid and enforceable contract?
9. Discuss the effects of various forms of technology on international business. What role does the Internet play? Where is all this leading? Explain the meaning of the “appropriability of technology.”

What role does this play in international competitiveness? How can managers protect the proprietary technology of their firms?

10. Discuss the risk of terrorism. What means can managers use to reduce the risk or the effects of terrorism? Where in the world, and from what likely sources, would you anticipate terrorism?

Application Exercises

1. Do some further research on the technological environment. What are the recent developments affecting businesses and propelling globalization? What problems have arisen regarding use of the Internet for global business transactions, and how are they being resolved?
2. Consider recent events and the prevailing political and economic conditions in the Russian Federation. As a manager who has been considering investment there, how do you assess the political and economic risks at this time? What should be your company's response to this environment?

Experiential Exercise

In groups of three, represent a consulting firm. You have been hired by a diversified multinational corporation to advise on the political and economic environment in different countries. The company wants to open one or two manufacturing facilities in

Asia. Choose a specific type of company and two specific countries in Asia and present them to the class, including the types of risks that would be involved and what steps the firm could take to manage those risks.

Internet Resources

Visit the Deresky Companion Website at www.pearsonhighered.com/deresky for this chapter's Internet resources.

CASE STUDY

Apple's iPhones—Not “Made in America”¹

*Apple has become one of the best-known, most admired and most imitated companies on earth, in part through an unrelenting mastery of global operations.*²

There are risks and rewards for all in a global economy. The globalization of human capital results in a range of winners and losers around the world: companies and their stockholders, consumers, contractors, firms up and down the supply chain, employed people, and unemployed people, as well as their economies. In February 2011, President Obama asked Apple's Steve Jobs why Apple could not bring back all the jobs it used to provide in the United States. The jobs related to most high-tech products made by companies such as Dell, HP, and Apple have now migrated overseas, including those for Apple's 70 million iPhones, 30 million iPads, and 59 million other products sold in 2011. Breaking down the retail price of \$500 for Apple's iPhone, for example, *Time* magazine estimates that \$61 worth of value comes from Japan, with its high-end technology manufacturing; \$30 of value is added from Germany; \$23 from South Korea; \$7 from Chinese assembly lines; \$48 from “unspecified”; and \$11 from the U.S. Those inputs total \$179 for parts and assembly abroad, leaving Apple, the inventor in the U.S., a profit of \$321.³ For the first quarter of 2012, Apple made \$13 billion in profit.

Although Apple directly employs 43,000 in the U.S. and 20,000 overseas, an additional 700,000 people engineer, build, and assemble iPads, iPhones, and Apple's other products in Asia and Europe. Sophisticated component parts outsourced in various countries are assembled in China. Some of those are contracted to the Taiwanese-headquartered company Foxconn's Longhua factory campus in Shenzhen, for example, where over 300,000 employees live in dorms, eat on site, and churn out iPhones, Sony PlayStations, and Dell computers. Foxconn Technology, with 1.2 million employees in plants throughout the country, is China's largest exporter and assembles an estimated 40 percent of the



Source: Alex Segre/Alamy

world's consumer electronics, including for customers such as Amazon, Dell, Hewlett-Packard, Nintendo, Nokia, and Samsung. No other factories in the world have the manufacturing scale of Foxconn.

The answer to the President's question is not as simple as the ability to acquire cheaper labor overseas; Apple's executives and those at other high-tech firms claim that "Made in the U.S.A." is not a competitive strategy for them because America does not compare favorably with the industrial skills, hard work, and flexibility that can be found in companies such as Foxconn. Questions as to what corporate America owes to Americans are met with the example of thousands of Chinese workers being roused in the night to accommodate a redesigned iPhone screen, and within a few days being able to produce 10,000 iPhones a day—a feat not possible in U.S. factories. While the cost of labor is a small percentage of an iPhone's cost, the major advantage and cost saving in China is in the management of supply chains and rapid access to component parts and manufacturing supplies from various factories in close proximity. In addition, Apple maintains that the large number of engineers and other skilled workers who could be accessed on short notice in China simply are not readily available in the United States; nor are the factories with the scale, speed, and flexibility that such a high-tech company needs. Apple executives give the example of visiting a factory to consider whether it could do the necessary work to cut the glass for the iPhone's touchscreen. Upon their arrival, a new wing of the plant was already being built "in case you give us the contract."⁴ Fareed Zakaria, in *Time*, maintains that this competitive edge is gained largely through Chinese government subsidies and streamlined regulations in order to boost domestic manufacturing. In the end, however, Apple maintains that:

*We don't have an obligation to solve America's problems. Our only obligation is making the best product possible.*⁵

However, after a number of suicides at Foxconn in 2010, reportedly attributable to the poor working conditions and excessive hours for very low pay, Apple was under some pressure from negative publicity; subsequently Foxconn raised wages, retained counselors, and literally strung nets from its highest buildings (to catch people). Apple does have a supplier code of conduct. In January 2012, Apple joined the Fair Labor Association (FLA), the first technology company to do so, and asked the group to do an independent assessment of conditions at its major factories. This move followed the company's own report that documented numerous labor violations, including employees doing 60 hour workweeks and not getting paid proper overtime. A few days after the FLA started its investigation, Foxconn said that they would increase salaries for some workers by 16% to 20%—to about \$400 a month before overtime—and that they would reduce overtime. While this is encouraging news for workers' rights, it should be noted that Apple and other contractors are known to only allow the slimmest of profits to its suppliers, which results in the suppliers trying anything to reduce their costs, such as using cheaper and more toxic chemicals or making their employees work faster and longer.

*"The only way you make money working for Apple is figuring out how to do things more efficiently or cheaper," said an executive at one company that helped bring the iPad to market. "And then they'll come back the next year, and force a 10 percent price cut."*⁶

China is being forced to take notice of such problems and labor is gaining some ground; the issue then is that firms have already started to move jobs to other countries with lower wages.

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2. Duhigg and Bradsher, 2012.
 3. M. Schuman, "Adding Up the iPhone: How an American Invention Makes Money for the World," *Time*, May 16, 2011.
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 5. Duhigg and Bradsher, 2012.
 6. Duhigg and Barboza, January 25, 2012.

Case Questions

1. What is meant by the globalization of human capital? Is this inevitable as firms increase their global operations?
 2. How does this case illustrate the threats and opportunities facing global companies in developing their strategies?
 3. Comment on the Apple executive's assertion that the company's only obligation is making the best product possible. "We don't have an obligation to solve America's problems."
 4. Who are the stakeholders in this situation and what, if any, obligations do they have?
 5. How much extra are you prepared to pay for an iPhone if assembled in the United States?
 6. How much extra are you prepared to pay for an iPhone assembled in China but under better labor conditions or pay? What kind of trade-off would you make?
 7. To what extent do you think the negative media coverage has affected Apple's recent decision to ask the FLA to do an independent assessment and the subsequent decision by Foxconn to raise some salaries? What do you think will happen now?
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