CHAPTER 1

Globalization and International Business

Daniels, J., Radebaugh, L., & Sullivan, D. (2021). International business, global edition. Pearson Education, Limited.

OBJECTIVES

After studying this chapter, you should be able to

1-1 Explain why and how the study of international business (**IB**) is important

1-2 Understand the relationship between globalization and IB

1-3 Grasp the forces driving globalization and IB

1-4 Discuss the major criticisms of globalization

1-5 Assess the major reasons companies seek to create value by engaging in IB

1-6 Define and illustrate the different operating modes for companies to accomplish their international objectives

1-7 Recognize why national differences in companies' external environments affect how they may best improve their IB performance

Source: aarows/Shutterstock

▲ International tourists visiting for the 2018 World Cup in Russia.

The world's a stage; all play their parts and take their share.

—Dutch proverb

CASE

The Globalized Business of Sports[1]

Sports may be the world's most globalized business. Fans demand to see the best, and "best" has become a global competitive standard. (The opening photo shows tourists from several countries in Moscow for the 2018 World Cup.) Satellite TV brings live events from just about anywhere in the world to fans just about anywhere else. This gives the key sports-business participants—athletes, team owners, league representatives, and sports associations—broadened audience exposure, expanded fan bases, and augmented revenues.

National sports federations' sponsorship of international competitions is common, most notably the long-standing World Cup in football (soccer) and the Olympics. More national organizations participate in these events than there are United Nations (UN) members, and probably more people follow them than follow most of the UN's activities. How do these international competitions relate to business? Cities and countries compete to host events to attract tourists and publicize their business opportunities. In turn, companies pay for marketing rights as sponsors. Finally, individual athletes compete not only for medals, but also for lucrative contracts to endorse products.

While the Olympics and the World Cup participations have long been global, the competitive location is increasingly so. The World Cup has recently moved about to such locales as South Africa, Brazil, Russia, and on to Qatar in 2022. Likewise, the Olympics have bounced among Canada, China, Russia, and Brazil over the past few years and are likely headed to Japan, China, France, and the United States.

THE INTERNATIONAL JOB MARKET

The search for talent has become worldwide. Professional basketball scouts search remote Nigerian areas for tall high-potential youngsters. Baseball agents provide live-in training camps for Dominican Republic teenagers in exchange for a percentage of their future professional signing bonuses. (However, overzealous agents are criticized for promising teenagers more than they can deliver in terms of education, training, and living standards.) But just assembling talent, although necessary, is insufficient for making a sports business successful. Shrewd marketing and financial management are crucial too. For instance, Fútbol Barcelona, one of recent years' best professional soccer teams, turned to young business graduates to help improve its finances.

Most of today's top-notch athletes are willing to follow the money anywhere. Most of the top professional sports leagues in North America and Europe share an important trait: Their composition is more international than ever before. England's professional soccer league (Premier) and Spain's La Liga have players from 66 and 50 countries respectively. Besides improving the caliber of play, foreign players expand the international fan base.

How the ATP Courts Worldwide Support

You've probably noticed that individual sports professionals are globe hoppers. Take tennis. No country boasts enough fans to keep players at home for year-round competition, yet today's top-flight tennis pros come from every inhabited continent. For 2019 the Association of Tennis Professionals (ATP) sanctioned 64 tournaments in 31 countries—and thus players travel to many countries. Logistics, compounded by fatigue, means that no tennis pro can compete in every ATP event.

Tournaments earn money through ticket sales, corporate sponsorship agreements, television contracts, and leasing of advertising space. The larger the stadium and TV audiences, the more backers and advertisers will pay to get their attention. Moreover, international broadcasts attract sponsorship from companies in various industries and countries. Consequently, organizers compete for top draws to fill stadium seats and land lucrative media contracts. Prizes are extremely generous—about US 50 million for competitors at the 2020 Australian Open.

From National to International Sports Pastimes

Some countries have legally designated a national sport to help preserve traditions; others effectively have one. Map 1.1 shows a sample of these. However, other sports have sometimes replaced national sports in popularity, such as cricket replacing field hockey as India's most popular sport.

Historically, baseball was popular only in its North American birthplace. Today the International Baseball Federation lists more than 100-member countries. As media revenues flattened in North America, Major League Baseball (MLB) broadened its fan base by broadcasting games to international audiences, which also showed youngsters all over the world how the game was played. The average MLB clubhouse is now a bastion of multilingual camaraderie, with players and coaches talking baseball in Spanish, Japanese, Mandarin, and Korean as well as English.

THE WIDE WORLD OF TELEVISED SPORTS

Not surprisingly, other professional sports have expanded their global TV coverage (and marketing programs). Most viewers of Stanley Cup hockey watch from outside North America. Fans can watch NASCAR races (National Association for Stock Car Auto Racing) and National Basketball Association (NBA) games in most countries.

TV isn't the only means by which sports organizations are seeking foreign fan bases and players. The U.S.'s National Football League (NFL) underwrites football programs in Chinese schools and plays some regular games in Europe. The NBA is helping to build youth leagues in India.

The Top-Notch Pro as Upscale Brand

Many top players are effectively global brands, such as U.S. tennis pro Serena Williams and Portuguese soccer forward Cristiano Ronaldo. Because of their sports success and charisma, companies within and outside the sports industry pay them handsomely for endorsing clothing, equipment, and other products. Swiss tennis star Roger Federer, long affiliated with Nike, parted ways with the swoosh to join Japanese casual clothing brand Uniqlo—for a guaranteed US $300 million over 10 years.

Promotion as Teamwork

A few teams, such as the New York Yankees in baseball, the New Zealand All Blacks in rugby, and Manchester United (Man U) in soccer, also have enough brand-name cachet to be global brands for selling clothing and other items. Just about every team can get something for the rights to use its logo, while some have enough name recognition to support global chains of retail outlets. Similarly, companies both sponsor and seek endorsements from well-known teams, such as the placement of "Fly Emirates" on Real Madrid's soccer jerseys.

Still others pay for naming rights to arenas and other venues. Of course, teams themselves can be attractive international investments. For instance, U.S. investors bought the Liverpool Football Club of the United Kingdom.

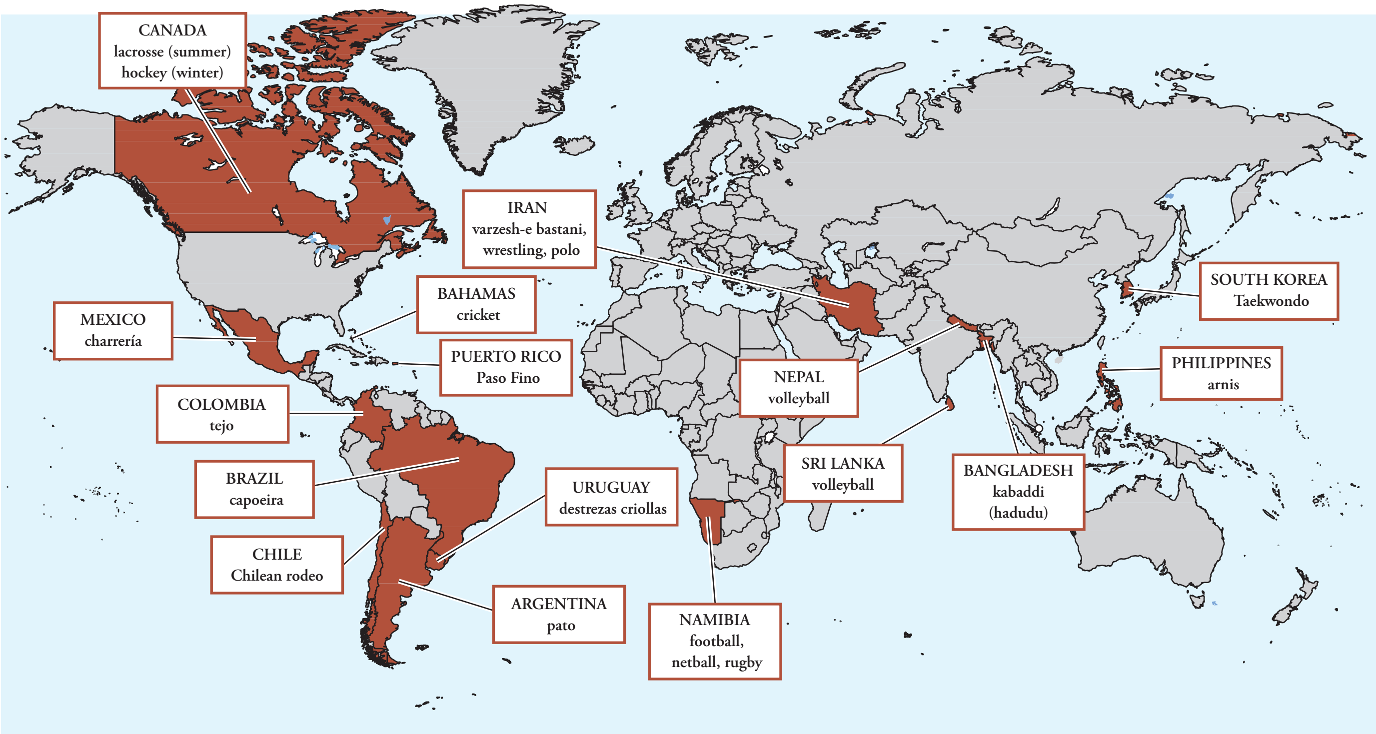
The Upsides and Downsides of Globalized Sports

What does all this mean to a sports fan? Now that pro sports have become a global phenomenon, fans can enjoy a greater variety of sports—and a higher level of competition—than any former

MAP 1.1 Examples of National Sports

Some 62 countries have a national sport; 16 have declared it by law, the rest by de facto. Some national sports are shared by more than one country, such as cricket by England and seven of its former colonies. Others protect the historical heritage, such as tejo in Colombia, kabaddi in Bangladesh, or pato in Argentina. Several countries have more than one national sport, such as Canada with hockey in the winter and lacrosse in the summer.

Source: The information on sports was taken from Wikipedia, http://en.wikipedia.org/wiki/National_sport (accessed March 18, 2016).



generation. That's the upside, but people don't always take easily to another country's sport. Despite many efforts, cricket, although popular in countries that once were British colonies, is popular elsewhere only where there are many immigrants from cricket-popular countries, such as in Germany where the Pakistani population is large. Nor has American football gained much popularity outside the United States. One possible reason is that rules for cricket and American football are so complicated. However, basketball and soccer have traveled to new markets more readily because they are easier to understand and require little specialized equipment.

Further, there is disagreement about the economic effect of successfully winning a bid to host big international competitions such as the World Cup and Olympics. On the one hand, they help spur tourism, foreign investment, infrastructure construction, and improvement of blighted areas. On the other hand, threats from terrorism boost the cost of security, while hosts may have to spend on stadiums and facilities that have no use afterward. Further, political disturbances, natural disasters, and contagious health conditions may play havoc with competitions. At this writing, the 2020 Summer Olympics in Japan has already been delayed until 2021 because of the global COVID-19 pandemic. Further, other sports have had to adjust to attendance limits at games and restrictions on the international movements of players and fans. Finally, many competitions have ended with substantially increased debt. Critics, therefore, often believe the funds would have been better spent on social services.

Nor is everyone happy with the unbridled globalization of sports—or at least with some of the effects. Brazilian soccer fans lament the loss of their best players, Cuban baseball fans fret about the movements of its players to U.S. and Japanese teams, and French fans protested the Qatar Investment Authorities' purchase of the Paris Saint-Germain (PSG) football club. Some factions within England have contended that the large influx of foreign players has disadvantaged the development of native players. Further, the income and publicity from winning and hosting in international competition have influenced cheating, such as by using illegal performance-enhancing drugs and bribing officials who decide the location of competitions. Finally, the high stakes of professional sports have led to vast gambling, which tempts corruption. It has shown up in sports both obscure, such as handball and sumo wrestling, and prominent, like soccer, baseball, and tennis.

QUESTIONS

1-1 Professional athlete A is a star, and athlete B is an average professional player. How has the globalization of professional sports affected each of these both positively and negatively?

1-2 As you read the chapter, identify and show an example of each international mode of operations that is illustrated in the globalization of professional sports.

THE WHY, WHAT, AND HOW OF STUDYING INTERNATIONAL BUSINESS (IB)

1-1 Explain why and how the study of international business (IB) is important

Welcome to the exciting world of IB! The title character and global traveler in one of the mid-20th century's most popular novels, movies, and plays (Auntie Mame) said, "Life is a banquet, and most poor suckers are starving to death." Although meant figuratively, this declaration rings of reality. In essence, the figurative message is that the world offers more variety and attraction than any single country. Sadly, the reality of the message is that much of the world's population faces profound challenges, such as hunger, sickness, inequality, and insecurity. Still, every global problem is also an opportunity for IB to help solve, and you'll play a part in finding solutions.

WHY STUDY IB?

Individual and Organizational Performance This text's material is critical for a student aspiring to work for an organization operating in the global environment. Today, that means virtually every organization. Nearly all organizations compete abroad, compete domestically against foreign or domestic companies with international operations, and/or use inputs from foreign suppliers. The opening case illustrates reasons for the multifaceted international participation of individuals, teams, companies and associations in sports—a process that is similar to that in many other industries as well. Regardless of your professional ambitions, you'll need to evaluate (1) where in the world you obtain the best resources at the best possible price for your organizational and personal development and (2) where you can best sell the product or service you've put together. Thus, the more you understand organizations' operating environments and experiences in different situations, the more likely you'll stand out and either attract the attention of recruiters as you prepare to enter the job market or, if already working, position yourself for promotion.

Making Nonbusiness Decisions Even if you don't anticipate direct IB activities, understanding the subject matter will likely prove useful. The international operations of companies, both big and small, along with the policies of their governments affect overall national conditions—economic growth, employment, consumer prices, national security—as well as the success of individual industries and firms. Currently, for example, nations grapple with questions on the degree to depend on foreign production and markets, ally with other countries for defense, and cooperate to solve problems that transcend national borders. A better understanding of IB will help you make more informed decisions, such as where to work and what governmental policies to support.

Let's also not overlook what Auntie Mame called a banquet. Growing knowledge about the variety of world attractions has powered a tremendous expansion in international travel. As you study the content in this text, you'll improve your understanding not only of the business opportunities that exist worldwide, but also the tools to better interpret national behavioral and opinion differences in your future travel. So, enjoy your global banquet!

Studying IB is important because

- most organizations are either international or compete with international companies,
- modes of operations may differ from those used domestically,
- it helps managers to decide where to find resources and to sell,
- the best way of conducting business may differ by country,
- an understanding helps you make better career decisions,
- an understanding helps you decide what governmental policies to support.

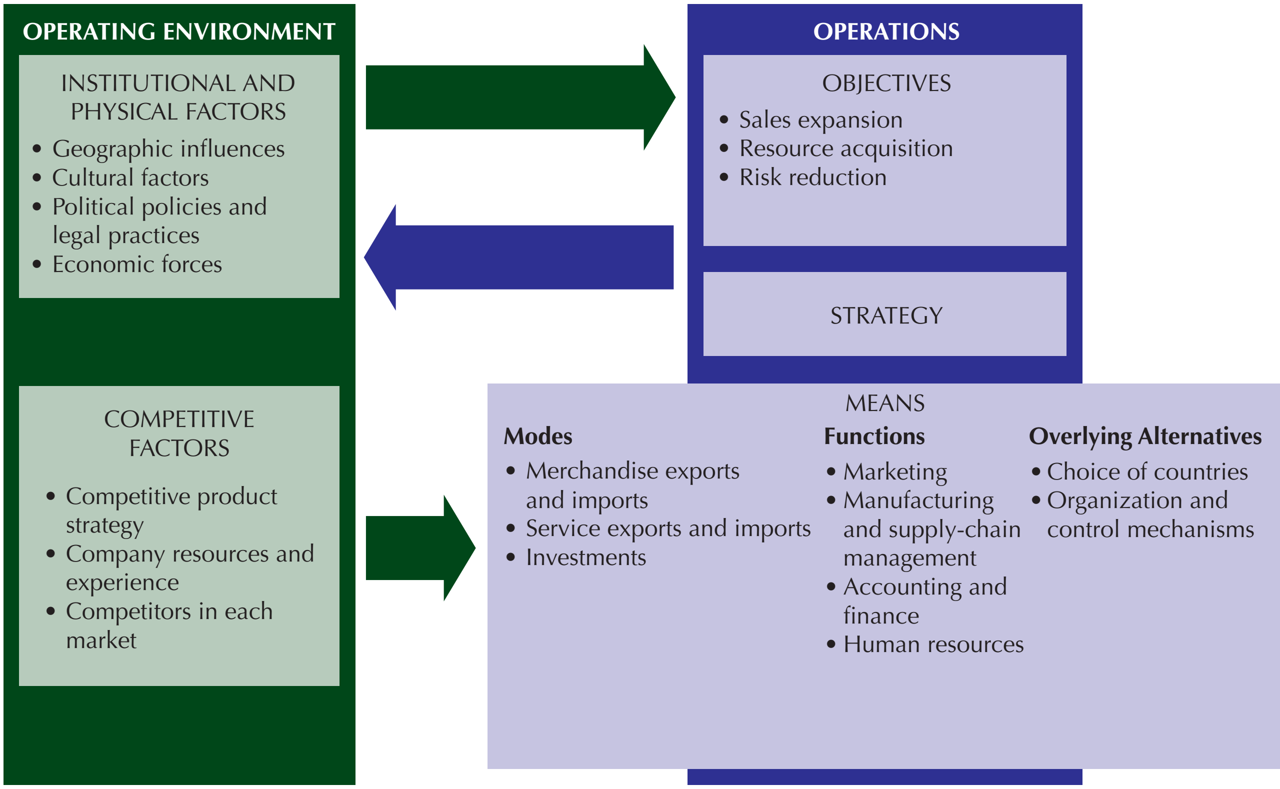
WHAT TO STUDY IN IB

Some of you may aspire to work directly in IB in your home or a foreign country. Some of you may work within your home country for companies dealing with foreign clients, suppliers, and competitors. In either case, your organization's performance depends on making sense of operating environments, identifying your objectives, and developing the means to achieve them. Thus, we have divided this text into two main sections—the environments and operations of IB—as you see illustrated in the text's title as well as Figure 1.1.

In your professional future, you'll discover that the way you do business in your home market is often not the best way to do business internationally. Why? First, companies operating internationally engage different modes of business, such as exporting

FIGURE 1.1 Factors in IB Operations

The conduct of an organization's international operations depends on two factors: its objectives and its means to achieve them. Likewise, its operations affect, and are affected by two sets of factors: physical/social and competitive.



and importing. Second, physical, institutional, and competitive conditions differ among countries; these differences inevitably affect the optimum ways to do business. Thus, international companies have more diverse and complex operating environments than purely domestic ones.

HOW TO STUDY IB TO DEVELOP A CRITICAL SET OF SKILLS

The text broadly profiles the environments and operations of IB. We cover a lot of ideas and issues in order to help you develop skills that support your employability and professional success. Although we cover a lot about a lot, you'll find many features that help you study, understand, and use the materials. We summarize key points in the margin and highlight fundamental connections to ideas in other chapters. Similarly, we highlight, in bold type, the introduction of foundation terms that anchor an understanding of IB; too, we compile these in the Glossary. We link your learning experience to your development of important employability skills. Specifically, in the Preface, on pp. 28–29, you'll find seven skills that institutions, such as the Graduate Management Admissions Council (GMAC) and World Economic Forum, identify as critical to getting and being successful in a job. A quick look at this section shows you how we incorporate each into the main features of your text. For example, the Opening and Closing Chapter Cases, "Point-Counterpoint," and "Looking to the Future" features, included in all chapters, help you develop your skills on complex problem-solving, comprehension and logic, critical thinking, cultural awareness, ethics, global mindset, and integrated reasoning. Each and all help you improve your talents for evaluating ideas, interpreting complex information, reconciling contradictions, synthesizing diverse recommendations, and making insightful decisions. Undoubtedly, you have already begun developing these skills in previous coursework. Our text helps you improve them within the fascinating context of the environments and operations of IB. Eventually, you'll showcase these skills in job interviews, and then use them to build a rewarding and successful career. Along the way, you'll probably even enjoy your global banquet!

THE RELATIONSHIP BETWEEN GLOBALIZATION AND IB

1-2 Understand the relationship between globalization and IB

Globalization is the widening and deepening of interdependent relationships among people from different nations. The term sometimes refers to the elimination of barriers to international movements of goods, services, capital, technology, and people that influence the integration of world economies.[2] Throughout history, expanded human connections have extended people's access to more varied resources, products, services, and markets. We've altered the way we want and expect to live, and we've become more deeply affected (positively and negatively) by conditions outside our immediate domains.

Industries and organizations, like those described in the opening case, have expanded to distant places to gain supplies and markets. As consumers we know from "Made in" labels that we commonly buy products from all over the world, but these labels do not tell us everything. For instance, a Belgian Neuhaus bonbon and an American Ford automobile contain so many different components, ingredients, and specialized business activities from diverse countries that pinpointing where they were made is challenging.[3] Although Apple ships its iPhones from China and they appear to be Chinese products, very little value is created in China. For example, the iPhone 7 had a factory-cost estimate of $237.45; all that's earned in China is $8.46.[4]

Globalization enables us to get more variety, better quality, or lower prices. Our meals contain spices that aren't grown domestically and fresh produce that may be out of season locally. Our cars cost less than they would if all the parts were made and the labor performed in one place.

HOW DOES *IB* FIT IN?

IB consists of all commercial transactions between two or more countries.

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

The Relation to Globalization The global connections between supplies and markets result from the activities of **international business** (IB), which are all commercial transactions (including sales, investments, and transportation) that take place among countries. Private companies undertake such transactions for profit; governments may undertake them either for profit or for other reasons.

THE FORCES DRIVING GLOBALIZATION AND IB

1-3 Grasp the forces driving globalization and IB

Although hard to measure, globalization

- has been growing, although sporadically,
- is less pervasive than generally thought,
- has economic and noneconomic dimensions,
- is stimulated by several factors.

Measuring globalization is a problem, especially for historical comparisons. First, a country's interdependence must be measured indirectly.[5] Second, when national boundaries shift, such as Ukraine's territorial loss to Russia, domestic business transactions can become international ones and vice versa. Nevertheless, various reliable indicators assure us that economic interdependence has been increasing, although sporadically, at least since the mid-twentieth century. Currently, about a quarter of world production is sold outside its country of origin, compared to about 7 percent in 1950. Restrictions on imports have generally been decreasing (once again sporadically), and output from foreign-owned investments as a percentage of world production has increased. In periods of rapid economic growth, such as most years since World War II, world trade grows more rapidly than world production. However, in economic downturns, such as the one caused by the COVID-19 pandemic, global trade and investment shrink even more than the global economy.

At the same time, however, globalization is less pervasive than you might suppose. In fact, many people in the United States are surprised to learn that only about 15 percent of the value of U.S. consumption comes from other countries. In much of the world (especially in poor rural areas), people lack the resources to connect much beyond their isolated domains. Such isolation is changing quickly, though, especially since the advent of mobile phones.[6] Only a few countries—mainly very small ones—either sell over half their production abroad or depend on foreign output for more than half their consumption. This means that most of the world's goods and services are still sold in the countries where they're produced.

Haier Electronics Group generates most of its revenue from customers in China.

Source: Lou-Foto/Alamy Stock Photo

(The adjacent photo shows washing machines of Qingdao Haier Co. Ltd. at a store in Beijing, China.) Moreover, the principal source of capital in most countries is domestic rather than international.

Granted, these measurements address only *economic* aspects of globalization. More comprehensive comparisons include people-to-people contacts through travel and communications, technological interchanges, government-to-government relationships, and acceptance and adaptation of attributes from foreign cultures such as words from other languages.[7] These comparisons have several commonalities:

- Size of countries—Smaller countries tend to be more globalized than larger ones, mainly because their smaller land masses and populations permit a lower variety of production.
- Per capita incomes—Countries with higher per capita incomes tend to be more globalized than those with lower ones because their citizens can better afford foreign products, travel, and communications.
- Variance among globalization aspects—Although a country may rank as highly globalized on one dimension, it may be low on another, such as the United States being high on technological scales but low on economic ones.

FACTORS IN INCREASED GLOBALIZATION

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

1. Rise in and application of technology
2. Liberalization of cross-border trade and resource movements
3. Development of services that support IB
4. Growth of consumer pressures
5. Increase in global competition
6. Changes in political situations and government policies
7. Expansion of cross-national cooperation

Rise in and Application of Technology Many of the proverbial "modern marvels" and efficient means of production have come about recently. These include new products, such as handheld mobile communications devices, as well as new applications of old products, such as biodegradable plastic made from mushrooms, tin in circuit boards, or Indian guar beans in oil and natural gas mining.[8] The shift in demand for older products has also altered production locations, such as the demand for air conditioners that has turned southern China into the workshop of the world.[9] Thus, much of what we trade today either did not exist or was unimportant in trade a decade or two ago. Why have technical developments increased so much? More than half the scientists who have ever lived are alive today. One reason, of course, is population growth. But another is rising productivity—taking less time to produce the same thing—which frees up more people to *develop* new products because fewer people are necessary to *produce* them. This rising productivity also means that on average people can buy more, including the new products, by working the same number of hours. The entry of new products into the market creates a need for other complementary products (such as apps for smartphones), thus accelerating the need for scientists and engineers.

Production of many new products cannot successfully take place in a single country. Much new technical innovation takes so many financial and intellectual resources that companies from different countries must cooperate to take on portions of development. Further, when new products are developed, the optimum scale size of production seldom corresponds with the market demand in a single country. Consequently, companies may need to sell both domestically and internationally to spread the fixed developmental and production costs over more units of production.

Advances in Communications and Transportation Strides in communications and transportation now allow us to discover, desire, and demand goods and services from abroad. Meanwhile, the costs of these strides have risen more slowly in most years than costs in general, thus increasing affordability. A three-minute phone call from New York to London that cost $10.80 in 1970 costs less than $0.20 today, while a call using Voice over Internet Protocol (VoIP) is virtually free. Similarly, passenger airfares have been falling for years. Between 1995 and 2014, they fell by half in real terms.[10]

Innovations in transportation mean that more countries can compete for sales to a given market. U.S. purchases of foreign-grown flowers used to be largely impractical and aimed only at high-income consumers; today, however, flower producers from as far away and dispersed as Ecuador, Israel, the Netherlands, and New Zealand compete for the U.S. market because growers can ship flowers quickly and economically.

Improved communications and transportation also enhance a manager's ability to oversee foreign operations, such as more easily visiting foreign facilities and communicating with managers therein. Thanks to the Internet, companies can instantly exchange pictures of samples. Even small companies can reach global customers and suppliers. However, you may ponder the following question: Has the Internet been a bigger force in globalization than the laying of the first transoceanic cable across the Atlantic in 1858 that reduced communication time from 10 days to a matter of a few minutes?

Liberalization of Cross-Border Trade and Resource Movements To protect its own industries, every country restricts the entry and exit of not only goods and services but also the resources—workers, capital, tools, and so on—needed to produce them. Such restrictions, of course, set limits on IB activities and, because regulations can change at any time, contribute to uncertainty. For example, the United States and China escalated restrictions on each other's products in the late twenty-teens. Over time, however, most governments have reduced such restrictions, primarily for three reasons:

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

Services That Support IB Companies and governments have developed services that facilitate global commerce. For example, because of bank credit agreements—clearing arrangements that convert one currency into another and insurance that covers such risks as nonpayment and damage en route—most producers can be paid relatively easily for their sales abroad. When Nike sells sportswear to a French soccer team, a bank in France collects payment in euros from the soccer team when the shipment arrives at French customs and pays Nike in U.S. dollars through a U.S. bank.

Growth in Consumer Pressures More consumers know more today about products and services available in other countries, can afford to buy them, and want the greater variety, better quality, and lower prices offered by access to them. However, this demand is spread unevenly because of uneven affluence, both among and within countries as well as from year to year.

Consumer pressure has also spurred companies to spend on research and development (R&D) and to search worldwide for innovations and products they can sell to ever-more-demanding consumers. By the same token, consumers are more proficient today at scouring the globe for better deals, such as searching the Internet for lower-priced prescription drugs abroad.

Increase in Global Competition Increased competitive pressures can persuade companies to buy or sell abroad. For example, a firm might introduce products into markets where competitors are already gaining sales, or seek supplies where competitors are getting cheaper or more attractive products. Once a few companies respond to foreign opportunities, others inevitably follow suit. And they learn from each other's foreign experiences. As the opening case suggests, the early success of foreign-born baseball players in U.S. leagues spurred U.S. basketball and football organizations to look for and develop talent abroad.[11]

So-called **born-global companies** start out with a global focus because of their founders' international experience[12] and because advances in communications give them a good idea of the location for global markets and supplies. Take SoundCloud, a Swedish audio-sharing web service. Its cofounders—one born in England and one in Sweden—were previously knowledgeable enough about the German and U.S. markets to move into both within months of starting up.[13] Meanwhile, some startups, like Airobotics of Israel, maker of drones, develop compelling technical solutions.[14] Akin to the idea "build a better mousetrap, and the world will beat a path to your door," they developed customers worldwide from their beginning. Regardless of industry, most firms and individuals must become more global; in today's competitive business environment, failure to do so is costly.

Changes in Political Situations and Government Policies For nearly half a century after World War II, business between Communist countries and the rest of the world was minimal. Today, only a few countries are heavily isolated economically or do business almost entirely within a political bloc. Nevertheless, governments still deny business with others for political reasons, such as many countries' sanctions against doing business with North Korea and Iran. However, government policies may open markets as well as close them.

Governments support programs, such as improving airport and seaport facilities, to foster efficiencies for delivering goods internationally. They also now provide an array of services to help domestic companies sell more abroad, such as collecting information about foreign markets, furnishing contacts with potential buyers, and offering insurance against nonpayment in the home-country currency.

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

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

Gain Reciprocal Advantages Essentially, companies don't want to be disadvantaged when operating internationally, so they lobby their governments to act on their behalf. Thus, governments join international organizations and sign treaties and agreements for a variety of commercial activities. For instance, some treaties and agreements allow countries' commercial ships and planes to use each other's seaports and airports; some cover commercial-aircraft safety standards and flyover rights; and some protect property, such as foreign-owned investments, patents, trademarks, and copyrights. Countries also enact treaties for reciprocal reductions of import restrictions.

Multinational Problem Solving Governments often act to coordinate activities along their mutual borders by building highways, railroads, and hydroelectric dams that serve the interests of all parties. However, there are still legacy border problems. For instance, fears of invasions from a rail-borne foreign army spurred nations to install wider or narrower rail tracks. Russia uses wider tracks than the standard Chinese gauge while in Europe trains between Italy and Sweden must change locomotives three or four times because of different national systems.[15]

Governments cooperate to resolve problems that they either can't or won't solve alone. First, the needed resources may be too great for one country to manage. Further, sometimes no single country is willing to pay all the cost for a project that will also benefit another country. In any case, many problems are inherently global—think of countering global climate change, terrorism, and diseases.

Second, one country's policies may affect those of others. Higher real-interest rates in one country, for example, can attract funds very quickly from individuals and firms in countries with lower rates, thus creating a shortage of investment funds in the latter. This movement is particularly disruptive to small developing economies.[16] Similarly, a country may weaken the value of its currency so that its products are cheaper in foreign markets. Thus, buyers may divert purchases to the newly cheaper country, hence contributing to unemployment in the country they forsook. To coordinate economic policies in these and other areas, the most economically important countries meet regularly to share information and pool ideas. The most notable coordination, known as the G20 countries, consists of 19 of the world's most economically important countries plus representation from the European Union of its members not included in the 19. These countries account for about 90% of world production, 80% of world trade, two-thirds of the world population, and approximately half of the world land area.[17]

Areas Outside National Territories Three global areas belong to no single country: the noncoastal areas of the oceans, outer space, and Antarctica. Until their commercial viability was demonstrated, they excited little interest for either exploitation or multinational cooperation. The oceans, however, contain food and mineral resources and constitute the surface over which much international commerce passes. Today, we have agreements to specify the amounts and methods of fishing, to address questions of oceanic mineral rights (such as on oil resources below the Arctic Ocean), and to deal with the piracy of ships.[18]

Likewise, there is disagreement on the commercial benefits to be reaped from outer space. Commercial satellites, for example, pass over countries that receive no direct benefit from them but argue that they should. If that sounds a little far-fetched, remember that countries do charge foreign airlines for flying over their territories.[19]

Antarctica, with minerals and abundant sea life along its coast, attracts thousands of tourists each year and has a highway leading to the South Pole and a Russian Orthodox church. Thus, it has been the subject of agreements to limit commercial exploitation, such as the Antarctic Treaty of 1959 that dedicated the continent to research. Since then, several countries have constructed research facilities there that use state-of-the-art architecture.[20] However, there is still disagreement about the continent's development—how much there should be and who does it.

THE CRITICISMS OF GLOBALIZATION

1-4 Discuss the major criticisms of globalization

Critics of globalization claim

- countries' sovereignty is diminished,
- the resultant growth hurts the environment,
- some people lose both relatively and absolutely,
- greater insecurity increases personal stress.

Although we've discussed interrelated reasons for and the benefits from the rise in IB and globalization, the consequences of the rise are controversial. *Antiglobalization* forces regularly protest at home and at international conferences about governmental policies—sometimes violently. We focus here on three issues: *threats to national sovereignty, environmental stress,* and *growing income inequality and personal stress*.

THREATS TO NATIONAL SOVEREIGNTY

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

The Question of Local Objectives and Policies Countries seek to fulfill their citizens' objectives by setting policies reflecting national priorities, such as those governing worker protection and environmental practices. However, critics argue that these priorities are undermined by opening borders to trade. For example, if a country has stringent regulations to improve labor conditions and promotes clean production methods such as by taxing companies' carbon emissions, it may not be able to compete with countries that have less rigorous rules. [21] By opening its borders to trade, it must either forgo its labor and environmental priorities to be competitive or face the downside of fewer jobs and less economic output.

The Question of Small Economies' Overdependence Critics complain that economically small countries depend too much on larger ones for supplies and sales. Thus, they are vulnerable to foreign mandates, including everything from defending certain UN positions to supporting a large economy's foreign military or economic actions. Nobel economist George Akerlof has noted that this dependence is intensified by poor countries' inadequate administrative capacity to deal with globalization.[22] Similarly, critics complain that large international corporations are powerful enough to dictate their operating terms (say, by threatening to relocate), exploit legal loopholes to avoid political oversight and taxes, and counter the small economies' best interests by favoring their home countries' political and economic interests.

The Question of Cultural Homogeneity Finally, critics charge that globalization homogenizes products and how they are made, social structures, and even language, thus undermining the cultural foundation of sovereignty. In essence, they argue that countries have difficulty maintaining the traditional ways of life that unify and differentiate them. Fundamentally, they claim helplessness in stopping the incursion of foreign influences by such means as satellite television, print media, and Internet sites.[23]

ENVIRONMENTAL STRESS

Much critique of globalization revolves around the economic growth it brings. One argument is that growth in both production and international travel consumes more nonrenewable natural resources and increases environmental damage—despoliation through toxic runoff into rivers and oceans, air pollution from factory and vehicle emissions, and deforestation that can affect weather and climate. In addition, critics contend that buying from more distant locations increases transportation, hence increasing the *carbon footprint*, which refers to the total set of greenhouse gases emitted.[24] They point further to the more than 1,000 container ships plying the seas and relying on heavy oil as a fuel; each pollutes as much as 50 million cars do. Indeed, the emissions from 15 mega-ships match those from all the cars in the world.[25]

The Argument for Global Growth and Global Cooperation However, other factions assert that globalization is positive for conserving natural resources and maintaining an environmentally sound planet—the former by fostering superior and uniform environmental standards and the latter by promoting global competition that encourages companies to seek resource-saving and eco-friendly technologies. A case in point is the automobile industry that has progressively produced cars that use less gas and emit fewer pollutants.

The positive effects of pursuing *global* interests may, nevertheless, conflict with *national* interests. Consider the effect of global pressure on Brazil to help protect the world's climate by curtailing logging and agricultural activity in the Amazon region. Unemployed Brazilian workers have felt that national job creation is more important than climate protection outside Brazil.

GROWING INCOME INEQUALITY AND PERSONAL STRESS

In terms of economic well-being, we look not only at our absolute situations but also compare ourselves to others (our relative situations). We generally don't find our economic status satisfactory unless we're doing better *and* keeping up with others.[26]

Income Inequality By various measurements, income inequality, with some notable exceptions, has been growing both among and within many countries.[27] Critics claim that globalization has affected this disparity by helping to develop a global superstar system, creating access to a greater supply of low-cost labor, and developing competition that leads to winners and losers.

The superstar system is especially apparent in sports, where today's global stars (as compared to past years) earn far more than the average professional player or professionals in less popular sports. The system carries over to other professions, such as in business, where charismatic leaders can command many times what others can.

Although globalization has brought unprecedented opportunities for firms to profit by gaining more sales and cheaper or better supplies, critics argue that profits have gone disproportionately to the top executives and shareholders rather than to the rank and file. Nobel economist Robert Solow has supported this criticism by arguing that greater access to low-cost labor in poor countries has reduced the real wage growth of labor in rich countries.[28] And even if overall worldwide gains from globalization are positive, there are bound to be some absolute or relative losers (who will probably oppose globalization). The speed of global technological and competitive expansion creates more winners and losers along with changing the relative positions of individuals, companies, and countries. As an example, recent manufacturing and foreign sales growth in China and India have helped them to grow more rapidly than the United States, thus lessening the *relative* economic leadership of the United States over those countries.[29] Likewise, some workers have lost economic and social standing as manufacturing jobs have shifted to other countries. The challenge, therefore, is to maximize the gains from globalization while simultaneously to minimize the costs borne by the losers.

Personal Stress Some repercussions of globalization can't be measured in strictly economic terms, such as people's stress from real and potential loss of relative economic and social positions.[30] Many worry also that immigration will lead them to become minorities rather than members of their countries' dominant group.[31] Further, stress, if widespread, goes hand in hand with costly social unrest.[32] The adjacent photo shows part of a violent protest influenced by such stress that rocked French politics in 2018–19. Although few of the world's problems are brand new, we may worry about them more now because globalized communications bring exotic sagas of misery into living rooms everywhere.[33]

The Paris protests in the photo ▶ were largely in response to an increase in gasoline taxes to help reduce global carbon emissions at the sacrifice assumed by French consumers.

Source: Alexandros Michailidis/Shutterstock

POINT

Is Offshoring of Production a Good Strategy?

YES Offshoring is the dependence on production in a foreign country, usually by shifting from a domestic source. If offshoring succeeds in reducing costs, it's good. This is happening with many companies. Most branded clothing companies depend on production offshore to have work done by cheaper sewing machine operators. Many investment companies, such as Fidelity in India, are hiring back-office workers in lower-wage countries to cut the cost of industry research. What good are cost savings? It's basic. If you can cut your costs, you can cut your prices or improve your product. Thus, by offshoring work to India, Claimpower, a small U.S. medical-insurance billing company, cut costs, lowered its prices to doctors, quadrupled its business in two years, and hired more U.S. employees because of the growth.[34]

What's the main complaint about offshoring? Too many domestic jobs end up abroad. As we discuss this, keep in mind that employment results from offshoring are difficult to isolate from other reasons for employment changes. Sure, many workers in high-income countries have lost jobs, but this has probably been due mainly to improvements in production technology. Let's try to pinpoint direct results of offshoring.

Samsung is a good example. By offshoring mobile phone assembly from Korea to Brazil, China, India, and Vietnam, the company was able to lower costs and sell more units, thereby maintaining the same number of low-paying domestic jobs while increasing high-paying jobs at home in R&D, engineering, design, and marketing.[35] If Samsung failed to enact such cost savings, its competitors in low-wage countries could underprice it with competitive products and services. In summary, cost savings generate growth, and growth creates more jobs.

Not just any jobs, either: This process lets companies create more high-value jobs at home—the ones performed by people like managers and researchers, who draw high salaries. When that happens, demand for qualified people goes up. In the United States, that process has already resulted in a higher percentage of white-collar and professional employees in the workforce. These are high-income people, and more of them are employed as a result of sending low-income jobs to countries with lower labor costs.[36]

Further, offshoring is a natural extension of outsourcing, the process of companies' contracting work to other companies so that they can concentrate on what they do best.[37] This contributes to making a company more efficient. What is the difference, then, of outsourcing to a domestic versus a foreign location?

Admittedly, workers do get displaced from offshoring, but aggregate employment figures show that these

COUNTERPOINT

Is Offshoring of Production a Good Strategy?

NO Some things are good for some of the people some of the time, and that's almost the case with offshoring. Unfortunately, it is good for only a few people but not for most. I keep hearing about the cost savings, but when I buy goods or services I rarely find anything that's cheaper than it used to be. Whether buying a Ralph Lauren shirt, getting medical services from a doctor who is saving money through Claimpower, or having Fidelity manage my assets, I have seen no lower prices for me. Instead, the lower production costs have resulted in higher compensation for already high-paid managers and for shareholders. Further, Claimpower's growth had to be at the expense of other companies in the business, not because of growth in the number of people getting medical services. In fact, studies show that the share of the economy going to employee wages steadily decreases while the share of national income going to profits steadily increases.[43] Meanwhile, the extreme pay gap between CEOs and workers expands.[44]

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

Now many of these employees have worked long and loyally for their employers and have little to show for it in the offshoring era. Yes, governments give them unemployment benefits, but these never equal what the employees had before, and they run out.[45] On top of everything else, they may have no other usable skills, and at their age, who's going to foot the bill for retraining them? The increase in what is called "high-value jobs" doesn't do them any good. Further, when reshoring occurs (usually because managers didn't think through the offshoring decision adequately in the first place), you can bet they rehire domestic workers at less cost than before they offshored those jobs. Offshoring may lead to short-term cost savings, but it merely diverts companies' attention from taking steps to find innovative means of more efficient production, such as productivity-enhancing technologies.[46] Concentrating on these innovative means may cut costs, increase production, maintain the jobs that are going abroad, and permit incomes of workers to rise. In addition, offshoring brings additional risks to companies, primarily because their governments may impose import workers find other jobs, just like workers who get displaced for other reasons. In a dynamic economy, people are constantly shifting jobs, partly due to technology. The prevailing employment for U.S. women was once as telephone operators; direct dialing technology changed that. Attendants used to pump all the gas, but most is now self-service. Passenger aircraft used to carry five cockpit crew members; technology eliminated the need for the navigator, flight engineer, and radio operator. On the near-future horizon, pilotless passenger aircraft and package-carrying drone helicopters will reduce the cockpit crew to one or even zero,[38] while driverless cars will reduce demand for traffic policemen, auto insurers, emergency room personnel, auto-accident lawyers, and makers of such products as road signals and guard rails.[39] In fact, reports predict that in the United States, computerization threatens 47 percent of jobs, while in the European Union, estimates range up to 55 percent.[40] Furthermore, some predictions are that by 2030, as many as 800 million jobs could be lost worldwide to automation and artificial intelligence.[41]

What all this means is that the shifting of jobs because of offshoring is no different from shifting for any other reason. In any case, because there are bound to be upper limits on the amount of outsourcing work a country can do, the direst predictions about job loss are exaggerated: There simply aren't enough unemployed people abroad who have the needed skills and who will work at a sufficiently low cost. Further, as production increases in outsourced facilities abroad, wage rates go up there.

Offshoring isn't for all companies or all types of operations. Some firms are bringing many operations back from abroad, a situation known as **reshoring** or **rightshoring**, because of miscalculating offshoring advantages to begin with as well as poor quality, consumer pressure, concerns about competitive security, fear of transportation risks, and advantages of locating production near technical development.[42] That brings us back to what we said explicitly at the outset: Offshoring works when you cut operating costs *effectively*.

restrictions on what they are buying abroad, such as occurred for the U.S. auto producers in the late 2010s. Finally, the dependence on foreign production makes them vulnerable to shortages created by natural disasters or export restrictions elsewhere. For example, U.S. companies offshored almost all the production of face masks to China, but with the global spread of the COVID-19 pandemic in 2020, China limited the export of those masks.

While we're on the subject of job "value," what kinds of jobs are we creating in poor countries? Because countries are competing with lower wages, they are encouraged to keep wages from rising, a sort of race to the bottom. However, multinational enterprises (MNEs) no doubt pay workers in low-wage countries more than they could get otherwise, and admittedly some of these jobs—the white-collar and technical jobs—are pretty good. But for most people, the hours are long, the working conditions are brutal, and the pay is barely enough to survive. Take Bangladesh. Workers were killed when locked doors prevented their escape from a fire, and others were killed when their ramshackle workplace building collapsed, which caused a backlash against and loss of reputation for companies that had used those suppliers. There is also little job security. If salaries creep up where companies are offshoring, the companies merely move to even cheaper places to get the job done.

Admittedly, in a dynamic economy, people must change jobs more often than they would in a stagnant economy—but not to the extent caused by offshoring. There's still some disagreement about the effects of offshoring on a country's employment rate. Researchers are looking into the issue, but what they're finding is that more of the so-called better jobs are also being outsourced, such as in finance and IT. So, are we really creating higher-level jobs at home? Here's the bottom line: In countries like the United States, workers simply aren't equipped to handle the pace of change when jobs can be exported faster than the average worker can retrain for different skills.

WHY COMPANIES ENGAGE IN IB

1-5 Assess the major reasons companies seek to create value by engaging in IB

Let's now focus on some of the specific ways firms can create value through IB. Take another look at Figure 1.1, where you'll see three major IB operating objectives:

- Sales expansion
- Resource acquisition
- Risk reduction

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

SALES EXPANSION

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

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

So increased sales are a major motive for expanding into international markets, and many of the world's largest companies derive more than half their sales outside their home countries. It is also true that IB is not the purview only of large companies. Some 280,000 small and medium-size enterprises (SMEs)—specifically, companies with fewer than 500 workers—account for 98 percent of U.S. exporters.[47] Nevertheless, some 7,000 large companies in the United States—such as Caterpillar, Boeing, General Electric, and Intel—generate just over two-thirds of export value.

RESOURCE ACQUISITION

Foreign locations may give companies

- lower costs,
- new or better products and components,
- additional operating knowledge.

Producers and distributors seek out products, services, resources, and components from foreign countries—sometimes because domestic supplies are inadequate (such as industrial diamonds in the United States). They're also looking for anything that will create a competitive advantage. This may mean acquiring any resource that cuts costs. For instance, think again of Apple's call to make the iPhone in China and its aims to access inexpensive, productive local expertise in tooling engineering, materials management, and assembly. Those resources are available elsewhere but, as Apple's CEO explained, the "Chinese have developed and scaled these skills over the last three decades while the U.S. and other countries have gone the other direction."[48]

Sometimes firms gain competitive advantage by improving product quality or differentiating their products from those of competitors; in both cases, they're potentially increasing market share and profits. This process often takes them abroad. Most automobile manufacturers, for example, hire design companies in northern Italy to help with styling. Many companies establish foreign R&D facilities to tap additional scientific resources.[49] Indian firms have followed foreign acquisition strategies to gain knowledge needed to compete globally.[50] Further, by operating abroad, companies gain diversity among their employees that can bring them new perspectives.

RISK REDUCTION

International operations may reduce operating risk by

- smoothing sales, profits, and supplies,
- preventing competitors from gaining advantages.

Selling in countries with different timing of business cycles can decrease swings in sales and profits (e.g., increasing sales stability through operations in countries that enter and recover from recessions at even slightly different times). Moreover, by obtaining supplies of products or components both domestically and internationally, companies may be able to soften the impact of price swings or shortages in any one country.

Finally, companies often go international for defensive reasons. Perhaps they want to counter competitors' advantages in foreign markets that might hurt them elsewhere. By operating in Japan, for instance, Procter & Gamble (P&G) delayed potential Japanese rivals' foreign expansion by slowing their amassment of the resources needed to enter into other international markets where P&G was active. Similarly, Tredegar Industries followed its main U.S. customer into the Chinese market to prevent that customer from finding an alternative supplier who might then threaten Tredegar's U.S. position.

IB OPERATING MODES

1-6 Define and illustrate the different operating modes for companies to accomplish their international objectives

When pursuing IB, an organization must decide on suitable *modes of operations* included in Figure 1.1. In the following sections, we define and introduce each of these modes.

MERCHANDISE EXPORTS AND IMPORTS

Merchandise exports and imports are the most popular IB modes.

Exporting and importing are the most popular IB modes, especially among smaller companies. **Merchandise exports and imports** are tangible products—goods—that are respectively sent *out* of and brought *into* a country. Because we can actually *see* these goods, they are sometimes called *visible exports* and *imports*. For most countries, the export and import of goods are the major sources of international revenues and expenditures.

SERVICE EXPORTS AND IMPORTS

Service exports and imports are international nonproduct sales and purchases.

- They include travel, transportation, banking, insurance, and the use of assets such as trademarks, patents, and copyrights.
- They are very important for some countries.
- They include many specialized IB operating modes.

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

- Tourism and transportation
- Service performance
- Asset use

Tourism and Transportation Let's say that some Australian fans take Air France to watch the Tour de France bicycle competition. Their tickets on Air France and travel expenses in France are service exports for France and service imports for Australia. Obviously, then, tourism and transportation are important sources of revenue for airlines, shipping companies, travel agencies, and hotels. The economies of some countries depend heavily on revenue from these sectors, such as Greece from foreign cargo carried on their shipping lines and the Bahamas from foreign tourists.

Service Performance Some services, including banking, insurance, rental, engineering, and management services, net companies' earnings in the form of *fees*: payments for the performance of those services. On an international level, for example, companies receive fees for engineering services rendered in **turnkey operations**, which are contracted construction projects transferred to owners when they're operational. For instance, the Spanish turnkey operator Sacyr Vallehermoso constructed the Panama Canal expansion. Companies also receive fees from **management contracts**—arrangements in which they provide personnel to perform management functions for another, such as Disney's management of theme parks in France and Japan.

Asset Use Companies receive **royalties** from **licensing agreements**, whereby they allow others to use some assets—such as trademarks, patents, copyrights, or expertise. For example, the Real Madrid football team receives a royalty from Adidas' use of its logo on merchandise. Companies also receive royalties from **franchising**, a contract in which a company assists another on a continuous basis and allows use of its trademark. For instance, McDonald's assists individually owned McDonald's' trademarked restaurants by providing supplies, management services, technology, and joint advertising programs.

INVESTMENTS

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

Direct Investment In **foreign direct investment (FDI)**, sometimes referred to simply as *direct investment*, the investor takes a controlling interest in a foreign company. When, for example, the owner of the Boston Globe and Boston Red Sox bought the Liverpool Football Club, it became a U.S. FDI in the United Kingdom. Control need not be a 100 percent or even a 51 percent interest; if a foreign investor holds a minority stake and the remaining ownership is widely dispersed, no other owner may effectively counter the investor's decisions.

When two or more companies share ownership of an FDI, the operation is a **joint venture**. (There are also non-equity joint ventures.)

Key components of portfolio investment are

- noncontrolling interest of a foreign operation,
- extension of loans.

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

TYPES OF INTERNATIONAL BUSINESS ORGANIZATIONS

Basically, an "international company" is any company operating in more than one country, but a variety of terms designate different ways of operating. The term **collaborative arrangements** denotes companies' working together—in *joint ventures, licensing agreements, management contracts, minority ownership*, and *long-term contractual arrangements*. The term **strategic alliance** is sometimes used to mean the same, but it usually refers to either an agreement that is of critical importance to a partner or one that does not involve joint ownership.

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

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

Does Size Matter? Some definitions require a certain size—usually giant. However, a small company can have foreign direct investments and adopt any of the operating modes we've discussed. Note, though, that if successful, small companies become medium or large ones.[51] Vistaprint (now Cimpress) is a good example. Founded in 1995, its sales grew to $6.1 million in 2000 and to over $1 billion by 2012 with operations mainly in North America and Europe.

WHY DO COMPANIES' EXTERNAL ENVIRONMENTS AFFECT HOW THEY MAY BEST OPERATE ABROAD?

1-7 Recognize why national differences in companies' external environments affect how they may best improve their IB performance

Although foreign external environmental differences are problematic

- some anecdotes of IB failures are merely myths,
- they must be weighed against domestic opportunities and risks,
- understanding institutional factors and how they affect all business functions helps assure success abroad.

Let's now turn to the conditions in a company's *external environment* that may affect its international operations. Although there are many anecdotes illustrating operational problems when companies have failed to consider foreign environmental differences, these differences are not so daunting that they prevent success. First, some of the anecdotes are merely myths that have been repeated so often their validity is seldom challenged. Second, gaining start-up success domestically is also problematic; thus, when companies look objectively at their domestic versus foreign opportunities and risks, foreign entries may seem comparatively less formidable. Third, a good understanding of what one will encounter helps reduce operating risks, and smart companies develop the means to implement international strategies by examining the following conditions that can affect their success:

- *Physical factors* (such as geography or demography)
- *Institutional factors* (such as culture, politics, law, and economy)
- *Competitive factors* (such as the number and strength of suppliers, customers, and rival firms)

In examining these categories, we delve into external conditions that affect patterns of companies' behavior in different parts of the world and that influence companies to alter what they do domestically to fit foreign needs.

PHYSICAL FACTORS

Physical factors affect

- where different goods and services can be best produced,
- operating risks.

Physical factors, such as geography and demography, can affect how companies produce and market products, employ personnel, and even maintain accounts. Remember that any of these factors may require a company to alter its operation abroad (compared to domestically) for the sake of performance.

Geographic Influences Managers who are knowledgeable about geography can better determine the location, quantity, quality, and availability of the world's natural resources and conditions. Their uneven global distribution helps explain why different products and services are produced in different places.

Again, take sports. Norway fares better in the Winter Olympics than in the Summer Olympics because of its climate, and except for the well-publicized Jamaican bobsled team (whose members actually lived in Canada), you seldom hear of tropical countries competing in the Winter Olympics. East Africans' domination in distance races is due in part to their ability to train at higher altitudes than most other runners.

Geographic barriers—mountains, deserts, jungles, and land-locked areas—often affect communications and distribution channels. And the chance of natural disasters and adverse climatic conditions can make business riskier in some areas than in others by affecting supplies, prices, and operating conditions. Keep in mind also that climatic conditions may have short- or long-term cycles and changes. For instance, recent melting of Arctic ice floes along with new ship technologies have allowed more ships to use a Northwest Passage between the Atlantic and Pacific Oceans to cut transport costs by saving as many as 15 days at sea.[52]

Demographic Influences Finally, countries' populations differ in many ways, such as density, education, age distribution, and life expectancy. These differences impact IB operations, such as market demand and workforce availability.

INSTITUTIONAL FACTORS

Institutions refer to "systems of established and prevalent social rules that structure social interactions. Language, money, law, systems of weights and measures, table manners and firms (and other organizations) are thus all institutions."[53] We will now examine a sample of these.

Politics often determines where and how IB can take place.

Political Policies Not surprisingly, a nation's political policies influence how and if IB takes place. For instance, before Cuba and the United States severed diplomatic relations in the 1960s, Havana had a minor league baseball franchise. Not only did that disappear, but also the facility by which Cuban baseball players could join U.S. professional teams. Many of them did so, although most had to defect from Cuba to play abroad. That changed sporadically with some political normalizations since 2013.[54]

Obviously, political disputes—particularly military confrontations—can disrupt trade and investment. Even conflicts that directly affect only small areas can have far-reaching effects since these areas may produce important components needed for production elsewhere and because tourists' and companies' fear prevents their interactions abroad.

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

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

International law—in the form of legal agreements between countries—determines how earnings are taxed by *all* jurisdictions. International agreements permit ships' crews to move about almost anywhere. Sometimes, transactions between countries devolve into disputes, such as whether a French football team, questioning the quality of uniforms provided by U.S. incorporated Nike, withholds payment. Sales contracts usually include a choice-of-law clause that stipulates which nation's laws, when necessary, govern dispute resolution. Similarly, companies can include an arbitration provision in the contract, agreeing in advance to resolve potential disputes outside of court. Finally, the ways in which laws are *enforced* also affect a firm's foreign operations. In the realm of trademarks, patented knowledge, and copyrights, most countries have joined in international treaties and enacted domestic laws dealing with violations. Many, however, do very little to enforce either the agreements or their own laws. Therefore, companies must determine how fastidiously different countries implement their laws.

Behavioral Factors The related disciplines of anthropology, psychology, and sociology can help managers better understand different values, attitudes, and beliefs to enable

Countries' behavioral norms influence how companies should operate there.

them to make operational decisions abroad. Let's return once again to the opening case. Although professional sports are spreading internationally, the popularity of specific sports differs among countries, while rules and the customary way of play for the same sport sometimes differ as well. Because of tradition, tennis's grand slam tournaments are played on hard courts in Australia and the United States, on clay in France, and on grass in England. A baseball game in the United States continues until there is a winner, while Japanese games end with a tie if neither team is ahead after 12 innings. Presumably the reason for the baseball difference is that the Japanese value harmony more than Americans do, whereas Americans value competitiveness more than the Japanese do.

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

Economic Forces Economics helps explain why countries exchange goods and services, why capital and people travel among countries in the course of business, and why one country's currency has a certain value compared to another's. Recall the internationalization of sports. Non-U.S.-born players make up an increasing portion of major league baseball rosters, and players from the Dominican Republic form the largest share. Obviously, higher incomes in the United States and Canada enable major league teams to offer salaries that attract Dominican players. Further, putting a major league baseball team in the Dominican Republic isn't practical because too few Dominicans can afford the ticket prices necessary to support a team.

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

THE COMPETITIVE ENVIRONMENT

Companies' competitive situations may differ by

- their relative size in different countries,
- the competitors they face by country,
- the resources they can commit internationally.

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

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

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

Using either approach, a firm may mass-market a product or sell to a niche market (the latter approach is called a *focus strategy*). Different strategies can be used for different products or for different countries, but a firm's choice of strategy plays a big part in determining how and where it will operate. Take Fiat Chrysler Automobiles (FCA), an Italian and U.S. MNE that is one of the world's largest auto makers. FCA competes with its best-selling models, like the Fiat UNO, primarily through a cost strategy targeting mass-market sales. This strategy led FCA to shift some engine plants to China, where production costs are low, and to target price-sensitive markets like Brazil, India, and Mexico. At the same time, FCA concentrates production of its premium Alfa Romeo and Maserati brands in Italy, using a high-priced focus strategy that requires access to the innovative design expertise as well as playing to customers' sense of sophistication. FCA then targets affluent, status-sensitive customers in higher-income countries such as Germany and the United States.

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

In large markets (such as the United States), companies must invest much more to secure national distribution than in small markets (such as Singapore). Further, they'll probably face more competitors in large markets than in small ones. Conversely, national market share and brand recognition have a bearing on operating in a given country. A company with a long-standing dominant national market position uses operating tactics that are quite different from those employed by a newcomer. Such a company, for example, has much more clout with suppliers and distributors. Remember, too, that being a leader in one country doesn't guarantee being a leader anywhere else. For example, in terms of global market share, Volkswagen, Toyota and General Motors vie to be the biggest carmaker. In many countries, however, none of them hold any of the top three positions. Maruti Suzuki, Hyundai, and Mahindra & Mahindra, for instance, claim the top three rankings in India.[55]

Competitors Faced in Each Market Finally, market success, whether domestic or foreign, often depends on the strength of competition and whether it is international or local. Large commercial aircraft makers Boeing and Airbus, for example, compete almost only with each other in every market they serve. What they learn about each other in one country is useful in predicting the other's strategies elsewhere. In contrast, Walmart faces different local competition with customized local strategies in almost every foreign market it enters.

LOOKING TO THE FUTURE Three Major Scenarios on Globalization's Future

At this juncture, opinions differ on the future of IB and globalization. Basically, there are three major scenarios:

- Further globalization is inevitable.
- IB will grow, but more regionally than globally.
- Forces working against further globalization and IB will slow down the growth of both.

Globalization of Business Is Inevitable

The view that globalization is inevitable reflects the premise that advances in human connectivity are so pervasive that consumers everywhere will know about and demand the best products for the best prices regardless of their origins. This view, known as *connectography*, premises that internationally connecting infrastructure will accelerate.[56] Those who hold this view also argue that because MNEs have built so many interconnecting international production and distribution networks, they'll pressure their governments to place fewer restrictions on international movements of goods and means to produce them.

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

The *Wall Street Journal* posed a question to Nobel Prize winners in economics: "What is the greatest economic challenge for the future?" Several responses addressed globalization and IB. Robert Fogel said it's the problem of getting available technology and food to people who are needlessly dying. Both Vernon Smith and Harry Markowitz specified the need to bring down global trade barriers. Lawrence Klein called for "the reduction of poverty and disease in a peaceful political environment." John Nash felt we must address the problem of increasing the worldwide standard of living while the amount of the earth's surface per person is shrinking.[57] Clearly, each of these responses projects both managerial challenges and opportunities.

IB Growth That Is Less Global

The second view—that IB growth will be less global—is based on studies showing that almost all the companies we think of as "global" conduct most of their business in home and neighboring countries.[58] Most world trade is regional, and many treaties to remove trade barriers are regional. Additionally, recent years have witnessed a greater growth in bilateral agreements between two countries rather than multilateral ones that encompass huge swaths of nations. Transport costs favor regional over global business. And regional sales may be sufficient for companies to gain scale economies to cover their fixed costs adequately. Nevertheless, regionalization of business may be merely a transition stage. In other words, companies may first promote international business in nearby countries and then expand their activities once they've reached certain regional goals.

Globalization and IB Will Slow

The third view argues that the pace of globalization will slow or may already have begun collapsing.[59] This is often referred to as *deglobalization*. In light of the antiglobalization sentiments mentioned earlier, it's easy to see that some people are adamant and earnest in voicing their reservations. The crux of the antiglobalization movement is the perceived schism between parties (including MNEs) who are thriving in a globalized environment and those that aren't. For example, in 2019, about 10 percent of the world's population—over 700 million people—lived in extreme poverty, surviving on no more than $1.90 per day. However, it was 47 percent in 1990. Most of the improvement results from the economic transformation in China. In 1981, 500 million people, about 90 percent of China, lived in extreme poverty; today, 6.5 percent do.[60]

Antiglobalists pressure governments to promote nationalism by raising trade barriers and rejecting international organizations and treaties. Historically, they have often succeeded (at least temporarily) in obstructing either technological or commercial advances that threatened their well-being. Recently, antiglobalization sentiments have grown in many countries, such as law changes in some U.S. states that hinder activities of undocumented aliens, the deportation by France of ethnic Roma (gypsies), the backlash against accepting refugees in several countries, and new import restrictions in China and the United States on each other's products. In Brazil and South Africa, the governments have authorized domestic companies to copy pharmaceuticals under global patent protection. Bolivia and Venezuela have nationalized some foreign investments, and Canada prevented the Malaysian state energy firm, Petronas, from buying Progress Energy, a natural gas producer. The sparring between pro- and anti-globalists is one reason why the globalization process has progressed in fits and starts.

Other uncertainties may hamper globalization. First is the question of oil prices, which affect international transportation because they can constitute more than 75 percent of operating costs on large ships.[61] Not only have global oil prices fluctuated widely, but technology for fracking and shale oil conversion has altered production locations when prices are high. Further, continuing political disturbances in the Middle East disrupt the global energy market. Many U.S. companies, such as furniture manufacturers, have responded by reshoring rather than facing transport cost and trade restriction uncertainty. Second, safety concerns—property confiscation, terrorism, piracy of ships, and outright lawlessness—may inhibit companies from venturing abroad as much.

Finally, one view holds that for globalization to succeed, efficient organizations with clear-cut mandates are necessary; however, there is concern that neither the organizations nor the people working in them can adequately handle the complexities of an interconnected world.[62]

Going Forward

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

CASE

Transportation and Logistics: Dubai Ports World[63]

—Hamed Shamma

The world economy and global trade has grown gradually since the recession of 2008–2009. This growth has occurred in Europe and Japan, where trade has been stronger than expected; in China and India, which have continually recorded high growth rates, as well as in the less-developed countries where trade is primarily based on petroleum and basic commodities. However, the COVID-19 pandemic dealt a strong blow to this steady growth, with the WTO forecasting a 9.2 percent decline in the volume of world trade for 2020, improving to 7.2 percent in 2021.

One of the most important contributors to the expansion of trade, an awareness of the global transportation and logistics industry is essential to understanding how this industry operates and what its trends are. Several factors have led to growth in the transportation and logistics industry: the separation of raw materials, labor, and production, decline in tariffs, import restrictions, and exchange rate controls. These factors have resulted in an increased demand for the transport of raw materials, unfinished goods, and finished goods in the global economy. According to Statista, containers handled by ports around the world in 2020 have been estimated at more than 829 million TEUs (twenty-foot equivalent units).

Trends in the Transportation and Logistics Industry

The geographic fragmentation of production has been an important driver of global trade. Tariffs, import restrictions, and exchange rate controls have also undergone a gradual decline. Many countries had instituted trade restrictions to help companies in the domestic market, but this in fact hindered their growth in global markets. The rise in global logistics and supply chains also means that governments today have less reason to impose trade barriers than in the past.

Competition and rivalry entail a constant need for change and improvement. In response to the growing volume of world trade, the number of high-capacity container ships has increased over the past few years, and so has the vessel size. Both require new port infrastructure.

Ports clearly play an important role in the international logistics chain, but to stay competitive, they need to use advanced technologies and skilled labor. The World Bank has developed a Logistics Performance Indicator (LPI) that allows comparisons to be made across 160 countries. The LPI measures dimensions of supply chain performance such as customs clearance procedures, quality of trade-related infrastructure, quality of transport services, timeliness of delivery, and the ability to track and trace consignments. The World Bank has also highlighted the importance that government policies have on logistics performance; countries that attempt to develop policies to improve supply chain activities score higher on the LPI than those that do not.

Transportation and Logistics Industry

In the past, logistics focused on reducing barriers to trade and the procedures to be followed by governments to get clearance for goods at customs. While these are important, so too are policies that integrate all the elements of the supply chain so that the various players can easily manage their business. The transportation and logistics industry has been lacking in this aspect. An approach that brings together all the components of the logistics chain, such as cargo handling, storage, warehousing, freight services, and courier services, will have a major impact on the productivity and efficiency of logistics businesses.

Developing Logistics Clusters

Governments around the world are investing significant resources in developing logistics clusters, which are also often referred to as logistics parks, transport centers, logistics platforms, or logistics centers. This involves investment in seaports, airports, railroads, and highways. Examples of leading logistics clusters include Singapore, the Netherlands, Los Angeles, Dubai, and Sao Paulo.

The advantages of logistics clusters include economies of scope, economies of scale, economies of density, superior service, and price stability. These benefits create a positive feedback loop that attract more companies to the cluster, resulting in further cost reduction and improved efficiency.

Doing Business in Different Countries

Local or domestic policies may affect the logistics operations in various markets. Some of these policies may increase costs, reduce efficiency, provide preferential treatment for local or public-owned corporations, result in domination by a single supplier, or impose limitations on investment in certain activities. These policies can significantly impact the supply chain, which may increase a firm's costs and affect business activity.

Countries where processing of goods is more efficient and economic may introduce restrictive policies such as lower tariff rates for import of raw material and higher tariffs for labor-intensive processed products. Other restrictions include bilateral agreements that distort competition, embargoes, business visa restrictions, and security requirements.

Dubai Ports (DP) World

Headquartered in Dubai, in the United Arab Emirates, Dubai Ports (DP) World is among the top three global terminal operators. It is considered a relatively new player in the global market, but it has an aggressive growth and acquisition strategy. Founded in 2005 as a result of the merger between the Dubai Ports Authority and Dubai Ports International, DP World's first project was in Jeddah, Saudi Arabia, and it has expanded its operations to many other countries including Djibouti, India, and Romania. A large portion of its business comes from the emerging markets in South America and Africa. With a team of over 50,000 employees from 103 countries, DP World operates in 78 marine and inland terminals across 40 countries.

In 2017, DP World handled around 70 million TEUs across their portfolio. In 2019, Dubai Ports ranked among the top 10 global ports in container traffic (Shanghai led the list). As DP World's capacity is estimated to have risen to more than 100 million TEUs by 2020, it continues to invest in its people and technology to provide better customer service quality to its customers across the world. This customer-oriented approach has resulted in strong relationships with customers and superior customer service levels. DP World's Jebel Ali facility was voted as the "Best Seaport in the Middle East" for 24 years up to 2018.

In 2006, DP World acquired the Peninsular & Oriental (P&O) Steam Navigation company and expanded its global network and market position in Asia, Africa, Australia, Europe, and the Americas. However, in the same year, it faced some controversy after its purchase of several ports in the United States fueled a debate on national security. To defuse the situation, DP World later agreed to drop the deal.

The Overseas Environment

Operating in various markets offers opportunities as well as challenges. The opportunities include access to new markets, resources, and technology, leading to innovation and an expansion of business. The industry remains dynamic and profitable, and emerging markets are experiencing significant growth in business.

Governments are usually eager to open their ports to logistics companies. Logistics brings economic growth and jobs. The companies create opportunities for blue-collar and white-collar jobs as well as for new businesses. Logistics companies also offer value-added services on products, and many manufacturers prefer to be located close to logistics companies because of the support offered to a variety of industries.

The challenges include the complexity of operating in certain territories such as Africa, where the supply chain is expensive and time-consuming. Transportation costs comprise up to 75 percent of the retail price in markets such as Malawi, Rwanda, and Uganda. For example,

MAP 1.2 Dubai Ports World

Dubai Ports World operates in more than 70 terminals across 40 countries, some of which have been indicated in the map.

Source: Data from "Our Locations," https://www.dpworld.com/about-us/our-locations, accessed April 15, 2021.

transporting a car in a 20-foot container from Japan to Uganda can cost $3,000.

Finding the Right Skills

The logistics industry is primarily a people-intensive business. Around 25 percent of the costs of logistics are labor-based. Thus, it is essential to attract, train, and motivate qualified people at all levels. Most companies find it difficult to recruit people with the right set of skills, especially when they operate in foreign countries. In addition to a usually limited supply of qualified candidates, the low wages, a low profile of the industry among many people, and poor working conditions have also hindered the industry in recruiting the right people.

Risks

In May 2020, during the COVID-19 pandemic, the Trump administration in the United States began the process of shifting global supply chain reliance from China to other countries. Addressing risks in supply chains is becoming a priority for businesses. Such risks can be caused by various disruptions—disease outbreaks or natural disasters; geopolitical tensions such as terrorism and threats of attack; economic turmoil such as currency fluctuations, demand shocks, and supplier failings; and technological failures such outages in IT and telecommunication systems. Risks may be mitigated by conducting scenario analyses, collaborating with the different players by sharing information, identifying vulnerabilities, and synchronizing backup plans.

Technology in Business

DP World has been keen to use advanced information technology tools to facilitate its business. It has been using mobile technology to make life easier for customers, saving them time and money. They also use mobile technology for their employees. Labor deployment, vessel arrival, and gate appointments can all be accessed on mobile devices. These are linked to the human resources department, which assigns labor to points of work, resulting in increased efficiency. This technology has enabled container shipping lines to access bay and stowage and has reduced port call time.

In keeping with the ongoing trend of digital transformation, DP World is increasingly utilizing blockchain and IoT capabilities in its operations. In 2020, DP World founded the Digital Freight Alliance, an online network where leading logistics providers from more than 150 countries gain access to new tools, services, and routes to expand their business. BOXBAY is a joint venture between DP World and the SMS Group that offers High Bay Storage (HBS) systems to improve storing and handling at container terminals.