

PART ONE

INTRODUCTION

CHAPTER ONE

INTERNATIONAL BUSINESS AND GLOBALIZATION

OBJECTIVES

- 1-1 Relate globalization and international business (IB) to each other and explain why their study is important
- 1-2 Grasp the forces driving globalization and IB
- 1-3 Discuss the major criticisms of globalization
- 1-4 Assess the major reasons companies seek to create value by engaging in IB
- 1-5 Define and illustrate the different operating modes for companies to accomplish their international objectives
- 1-6 Recognize why national differences in companies' external environments affect how they may best improve their IB performance

CHAPTER OVERVIEW

Globalization has become a major socioeconomic force and topic of debate in the twenty-first century. Chapter One examines the forces that are driving this phenomenon, as well as the often-passionate criticisms of the process. It reviews the objectives that firms pursue when they engage in international business activities and describes the various modes of entry that may be used. It also notes the terminology that has come into existence as new types of organizations have evolved. The chapter concludes with a discussion of the conditions in a company's external environment that may affect its international operations.

CHAPTER OUTLINE

OPENING CASE: THE GLOBALIZED BUSINESS OF SPORTS

[see Map 1.1]

Although not everyone agrees that the unbridled globalization of professional sports is all for the good, the process and possibilities are definitely far reaching. Today's satellite television broadcasts enable fans to watch top players and teams in nearly any sport from almost anywhere on earth. Professional teams scour the world to find and develop the most talented athletes, and players forsake home country allegiances in their pursuit of the world's highest salaries. Further, the more people that tournaments can attract through attendance and television, the more money that sponsors and advertisers are willing to pay—and the greater the likelihood that those

sponsors and advertisers will have business operations that span the globe. In addition, sports and nonsports companies alike pay famous athletes and teams generous sums to endorse their products. Successful teams have opened shops both domestically and internationally to sell souvenirs bearing their logos and may make more money on merchandise than from TV rights and sponsorships combined. Most recently, as teams and leagues have begun to seek income opportunities outside their home countries, foreign investors have acquired a U.S. baseball team; another group of foreign investors acquired controlling interest in a British soccer (football) team, and the National Football League (NFL) of the United States underwrites flag football games in Chinese schools and is playing some regular season NFL games in Europe. Map 1.1 outlines national sports in a variety of countries and can be used to discuss how culture impacts globalization.

Questions

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

"All questions marked with this blue star ★ in the textbook are also found as discussion board questions in the MyLab. These are meant to prompt discussion among your students and therefore, no correct answer is provided."

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.

"All questions marked with this blue star ★ in the textbook are also found as discussion board questions in the MyLab. These are meant to prompt discussion among your students and therefore, no correct answer is provided."

TEACHING TIPS: Carefully review the PowerPoint slides for Chapter One. A good Internet source of information on globalization can be found at www.globalization101.org. Finally, review the atlas provided in the text, where you will find maps of the world and its continents, as well as a country index.

I. INTRODUCTION

As people, firms, and other organizations have expanded their access to resources, goods, services, and markets across wider geographical areas, they have also become more deeply affected (positively and negatively) by conditions outside their home countries.

Globalization is the widening and deepening of interdependent relationships among people from different nations.

II. WHY STUDY ABOUT GLOBALIZATION, IB AND THEIR RELATIONSHIP

A. How Does IB Fit In?

International business consists of all commercial transactions between two or

more countries. Global events and competition affect almost all firms—large or small. However, the international environment is more complex and diverse than a firm's domestic environment. [see Fig. 1.1]

IB Relation to Globalization: The global connections between supplies and markets result from the activities of 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.

B. The Study of IB

Not only do companies sell output and secure supplies and resources abroad, they compete against products, services, and companies from foreign countries. Thus, most managers need to take into account IB when setting their operating strategies and practices.

1. Understanding the Environment/Operations Relationship

International companies have more diverse and complex operating environments than purely domestic ones.

2. Making Nonbusiness Decisions

A better understanding of IB will help you make more informed decisions, such as where to work and what governmental policies to support.

III. THE FORCES DRIVING GLOBALIZATION AND IB

Globalization is a difficult concept to measure. Currently, about a quarter of world production is sold outside of its country of origin, restrictions on imports continue to decline, the foreign ownership of assets as a percent of world production continues to increase, and world trade continues to grow more rapidly than world production. Recessionary contraction in recent years has at least temporarily reversed this trend. That said, on a value basis, only a few countries (mainly very small nations) either sell more than half of their production abroad or source more than half of their consumption from foreign countries. Further, the principal source of capital in almost all nations is domestic rather than international. Granted, these measurements address only economic aspects of globalization. Various studies have made more comprehensive comparisons by including, say, 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. The studies' results have several commonalities: (1) smaller countries tend to be more globalized than larger ones, mainly because their smaller land masses and populations permit a lower variety of production, (2) 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 and (3) 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. .

A. Factors in Increased Globalization

There are seven factors that are often cited as having contributed to the increased growth in globalization.

1. Rise in and Application of Technology

Advances in communications and transportation have significantly increased the effectiveness and efficiency of international business operations. Today, a much larger portion of the population is involved in the *development* of new products, than just the production of products.

2. Liberalization of Cross-Border Trade and Resource Movement

Over time most governments have lowered restrictions on trade and foreign investment in response to the expressed desires of their citizens and producers. The primary motives for this change include giving citizens greater consumer choice and lower prices, international competition making domestic producers more efficient, and the hope that liberalization will cause other countries to also lower trade barriers.

3. Development of Services That Support International Business

Services provided by government, banks, transportation companies, and other businesses greatly facilitate the conduct and reduce the risks of doing business internationally.

4. Growth of Consumer Pressures

Because of innovations in transportation and communications technology, consumers are well informed about and often able to access foreign products. Thus competitors the world over have been forced to respond to consumers' demand for increasingly higher quality and more cost-competitive offerings. Consumer pressure has also spurred companies to spend more on research and development (R&D) and to search worldwide for innovations and products they can sell to ever-more-demanding consumers.

5. Increased Global Competition

The pressures of increased foreign competition often persuade firms to expand internationally in order to gain access to foreign opportunities and to improve their overall operational flexibility and competitiveness. How companies become global players can be discussed using the terms **born-global companies** and **clustering**.

6. Changes in Political Situations and Government Policies

Today, only a few countries are heavily isolated economically or do business almost entirely within a political bloc. In fact, political changes sometimes open new frontiers, such as diplomatic relations between the United States and Cuba. In addition, the improvements in national infrastructure and the provision of trade-related services by governments the world over have further led to substantial increases in foreign trade and investment levels.

7. Expansion of Cross-National Cooperation

Governments have increasingly entered into cross-national treaties and agreements in order to gain reciprocal advantages for their own firms, to jointly attack problems that one country cannot solve alone, and to deal with areas of concern that lie outside the territory of all countries.

IV. THE CRITICISMS OF GLOBALIZATION

Antiglobalization forces have protested both peacefully and violently as they press for legislation and other means to stop or slow the globalization process. Issues of threats to national sovereignty, environmental stress, and growing income inequality and personal stress are addressed.

A. Threats to National Sovereignty

Many citizens fear that a country's participation in multilateral agreements will diminish its sovereignty and freedom from external control and curtail its ability to act in its own best interests. In particular, people in small countries worry that dependence on larger countries for sales and/or supplies, as well as the presence of large international firms, will make them vulnerable to the demands of parties against which they are essentially powerless. In addition, people the world over are concerned that globalization will bring the homogenization of products and traditional ways of life—including language and social structure.

B. 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. However, other factions assert that globalization is positive for conserving natural resources and maintaining an environmentally sound planet. The positive effects of pursuing global interests may, nevertheless, conflict with national interests.

C. Growing Income Inequality and Personal Stress

By various measurements, income inequality, with some notable exceptions, has been growing both among and within many countries. Although globalization has brought unprecedented opportunities for firms to profit by gaining more sales and cheaper or better supplies, critics argue that profits have gone disproportionately to the top executives rather than to the rank and file. Thus, even if the overall global gains from globalization are positive, there remains a continuing challenge to bring about the positive gains in ways that minimize costs to the losers. It is easy to think about the impacts of globalization at a macro level, but individuals are impacted very specifically, causing stress and insecurity.

POINT—COUNTERPOINT: Is Offshoring Good Strategy?

POINT: Offshoring is good because it reduces costs. Although a firm may temporarily need fewer workers in its home country, eventually domestic employment (particularly high-value jobs) will increase because of the firm's growth. In addition, offshoring not only contributes to the economic growth of less-developed countries, but it increases their need and ability to import products from developed countries and thus indirectly contributes to the growth of all nations. There is also a natural extension from outsourcing to offshoring. Some industries and companies have actually seen some reversal of the outsourcing trend.

COUNTERPOINT: Only a few people benefit from offshoring. Cheaper labor inputs have not resulted in cheaper prices for consumers. Further, firms that grow as a result of offshoring do so at the expense of their competitors; thus, there is no real economic growth. Displaced workers are forced to take jobs with fewer, if any, benefits and lower pay, while multinationals take advantage of their foreign workers, who are powerless. While a few countries are growing economically, world poverty levels have increased significantly in recent decades.

V. WHY COMPANIES ENGAGE IN INTERNATIONAL BUSINESS

When engaging in international business, a firm should consider its mission, its objectives, and its possible strategies. Primary objectives would include the following:

A. Expanding Sales

Companies may increase the potential market for their sales by pursuing international consumer and industrial markets.

B. Acquiring Resources

Foreign-sourced products, services, resources, and components can make a firm more competitive both at home and abroad.

C. Reducing Risk

Firms seek foreign markets in order to minimize cyclical effects on sales and profits. Defensively, they may also wish to counter the potential advantages that competitors might gain from participating in foreign market opportunities.

VI. INTERNATIONAL BUSINESS OPERATING MODES

A firm can engage in international business through various operating modes, [see Fig. 1.1] including *exporting* and *importing* merchandise and services (see Chapters 6 and 7 regarding international trade) and *licensing* and *foreign direct investment* (see Chapter 15 regarding direct investment and collaborative strategies), joint ventures, and management contracts. The firm or individual exporting merchandise or a service will receive international earnings while the firm or individual importing merchandise or a service will make an international payment.

A. Merchandise Exports and Imports

Merchandise exports consist of tangible (visible) products, i.e., goods that are sent to a foreign country for use or resale. **Merchandise imports** consist of tangible products, i.e., goods brought into a country for use or resale.

B. Service Exports and Imports

Service exports and imports represent intangible (invisible), i.e., non-merchandise products.

1. **Tourism and Transportation.** When an American flies to Paris on Air France and stays in a French-owned hotel, payments made to the airline and the hotel represent service export earnings (income) for France and service import payments (expenses) for the United States.
2. **Service Performance.** Some services, such as banking, insurance, rental, engineering, **turnkey operations** (construction, performed under contract, of facilities that are transferred to the owner when they are ready for operation), and **management contracts** (arrangements in which one firm provides personnel to perform management functions for another), net companies export earnings in the form of fees paid by a foreign client.
3. **Asset Use.** Firms may receive export earnings, i.e., **royalties**, by allowing foreign clients to use their assets (trademarks, patents, copyrights, and other expertise). **Licensing agreements** are contracts that represent a transaction in which a licensor sells the rights to the use of its intellectual property to a licensee in exchange for a fee or royalty. **Franchising** is a special form of licensing in which

the *franchisee* is granted additional control over the operation in exchange for the provision of additional support and services by the *franchisor*.

C. Investments

Foreign investment consists of the ownership of foreign property for the purpose of realizing a financial gain via profits, growth, dividends, and/or interest.

1. **Direct Investment. Foreign direct investment (FDI)** occurs when an investor gains a controlling interest in a foreign operation. A **joint venture** represents a direct investment in which two or more parties share ownership of an FDI.
2. **Portfolio Investment. Portfolio investment** is a noncontrolling interest in a venture made in the form of either debt or equity. Often, firms use portfolio investment as part of their short-term financial strategy.

D. Types of International Organizations

There are numerous forms of **collaborative arrangements** through which companies work together internationally, such as joint ventures, licensing agreements, management contracts, minority ownership, and long-term contractual arrangements. A **strategic alliance** is more narrowly defined to indicate that the agreement is of critical importance to the competitive viability of one or more of the partners. The **multinational enterprise (MNE)** is a firm that takes a global approach to foreign markets and production, i.e., it is willing to consider markets and production sites anywhere in the world. The terms **multinational corporation (MNC)** and **transnational company (TNC)** may also be used in this context.

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

Smart companies develop the means to implement international strategies by examining the following conditions abroad 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)

A. Physical Factors

1. **Geographic Influences.** The uneven distribution of resources results in different opportunities being located in different parts of the world. In addition, geographic barriers affect transportation, communications, and distribution channels within a country. Managers who are knowledgeable about geography are in a position to better determine the location, quantity, quality, and availability of the world's natural resources and conditions.
2. **Demographic Influences.** 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.

B. Institutional Factors

1. **Political Policies.** A nation's political policies influence how and if IB takes place because of the influence of government leaders over the process.
2. **Legal Policies.** While every nation has its own body of business law, agreements between/amongst nations determine international law. *Domestic business law* may

include regulations on home-country firms in both home and host countries regarding such matters as taxation, employment, and foreign exchange transactions. International law—in the form of legal agreements between countries—determines how earnings are taxed by all jurisdictions. Also, the ways in which laws are enforced also affect a firm's foreign operations

4. **Behavioral Factors.** By studying the disciplines of anthropology, psychology, and sociology, managers can better understand the interpersonal norms of people in foreign countries and the reasons why operating procedures may need to be adjusted in foreign locales.
5. **Economic Forces.** Among other things, economics explains why countries exchange goods and services, why capital and people travel among countries in the course of business, and why one country's currency has a certain value compared to another. It also provides the analytical tools to determine the impact of foreign operations on home and host countries, as well as the effect of a country's economic policies and conditions upon domestic and foreign firms.

C. The Competitive Environment

In addition to its physical and social environments, every globally active company operates within a competitive environment. Companies' competitive situations may differ by their relative size in different countries, the competitors they face by country, and the resources they can commit internationally. A firm's competitive strategy for products will usually involve competing on the basis of cost or differentiation. Other competitive factors are a company's size and resources compared to those of its competitors. Finally, market success, whether domestic or foreign, often depends on the strength of competition and whether it is international or local. [See Fig. 1.1]

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

By envisioning different ways in which the future may evolve, a company can be better prepared to develop the facilities and people needed to succeed in an uncertain environment. At this time, there is much discussion about the following three viewpoints.

The first view, that *further globalization is inevitable*, is based largely on the premise that technical advances in transportation and communications are pervasive, that consumers demand the best products for the best prices regardless of their country of origin, and that MNEs are so powerful they can pressure governments to further reduce restrictions on trade and investment. If this is true, then the challenge is to determine what to make of globalization with respect to the distribution of its costs and benefits.

The second view, that *international business will grow primarily along regional rather than global lines*, is premised on studies that show that almost all firms that consider themselves global conduct a dominant portion of the business in their home and neighboring countries. It may be possible, however, that regionalization is a transitional step on the route to globalization.

The third view, that *forces opposing globalization will greatly slow its growth*, is not to be dismissed. Historically, pressure groups have often been successful in obstructing policies and activities that threatened their own well being. In addition, recent *anti-globalization* interests have successfully promoted a variety of causes in numerous countries that span the globe. The

impact of other uncertainties also impacts the future of globalization. Some examples of these uncertainties include the impact of oil prices on global transportation, the general economic recession, and concerns about product safety. Whether institutions and people can work together to effectively manage the complexities of today's interconnected world remains to be seen.

CLOSING CASE: Transportation and Logistics: The Case for Dubai Ports World

The spike in the growth rates for the logistics and transportation industries have been owed to many reasons including the separation of raw materials, labor and production, decline in tariffs, import restrictions, and exchange rate controls. The World Bank and other prominent organizations have instituted policies and led initiatives spurring such growth. Ports serve as an important link in the global supply chain of logistics and transportation. The Dubai Ports World is a good example of a transportation and logistics company that operates in sixty-five terminals across six continents successfully. Government policies often influence the logistics operations and these include restrictive trade policies or agreements that distort competition, place embargoes, enforce business visa restrictions and list security requirements. The evolution of logistics clusters which are geographic concentrations of logistics related activities, are thus crucial to the proper health of the industry. Singapore, the Netherlands, Los Angeles, Dubai, Sao Paulo, and Aragon are some of the leading logistics clusters, their development being dependent on heavy investment in infrastructure. Dubai Ports World thus invests heavily in people and technology to deliver the highest quality of customer service and experience across its network of operations.

Questions

1-3 What factors have contributed to the growth of the transportation and logistics industry and how?

Various global factors have contributed to the growth of the transportation and logistics industry. These include: fragmentation of production, decline in tariffs, restrictions and controls, and the overall growth in global trade. (LO: 1, Learning Outcome: Define globalization and international business and show how they affect each other, AACSB: Analytical Skills)

1-4 What steps has DP World taken to benefit from global economic changes.

Dubai Ports World has purchased several ports in the U.S., although they were sold shortly after they were purchased. The company incorporates advanced technologies such as mobile technology for employees, and processes that speed up customer requests, ultimately resulting in highest levels of customer service. (LO: 2, Learning Outcome: To understand why companies engage in international business and why international business growth has accelerated, AACSB: Analytical Skills)

1-5 What economic factors influence the success of the international transportation and logistics industry?

Both international and local economic factors such as global or local policies, restrictive policies for importing raw material, bilateral agreements that distort competition, embargoes, business visa restrictions, and security requirements are factors that affect the success of the international transportation and logistics industry. (LO: 5, Learning Outcome: To apply social science disciplines to understanding the differences between international and domestic business, AACSB: Multicultural and Diversity Understanding)

ADDITIONAL EXERCISES: The Globalization Process

Exercise 1.1. Ask students to identify firms, both domestic and foreign that operate internationally. Take time to explore the extent and nature of their operations. Also, discuss a logical geographical pattern of expansion for each type of operation. Conclude the discussion by examining the list to determine if there are any particular types of firms that seem to lend themselves (or not) to global operations and strategies. Have the students explain why this might be so. (LO: 2, Learning Outcome: To understand why companies engage in international business and why international business growth has accelerated, AACSB: Dynamics of the Global Economy.)

Exercise 1.2. Ask students why they think the world's largest theme park operator, the Walt Disney Co., was motivated to establish parks in Tokyo, Paris, and Hong Kong. What particular market characteristics of each of those sites were especially attractive? Conclude the discussion by asking students if they believe that Disney should establish additional foreign parks, and if so, when, where, why, and how? (LO: 4, Learning Outcome: To become familiar with different ways in which a company can accomplish its global objectives, AACSB: Analytical Skills.)

Exercise 1.3. Divide students into small groups and ask them to explore the costs of the globalization process. What are the major issues? What companies seem to promote corporate responsibility in all aspects of their businesses? What can and/or should be done to encourage seemingly less-than-responsible businesses and governments to change their ways? (LO: 4, Learning Outcome: To become familiar with different ways in which a company can accomplish its global objectives, AACSB: Analytical Skills.)