

PART 1 The World's Marketplaces

CHAPTER 1

An Overview of International Business



PCN Photography/Alamy

AFTER STUDYING THIS CHAPTER, YOU SHOULD BE ABLE TO:

1. Discuss the meaning of international business.
2. Explain the importance of understanding international business.
3. Identify and describe the basic forms of international business activities.
4. Discuss the causes of globalization.
5. Comprehend the growing role of emerging markets in the global economy.

MyManagementLab[®]

★ **Improve Your Grade!**

More than 10 million students improved their results using the Pearson MyLabs.
Visit mymanagementlab.com for simulations, tutorials, and end-of-chapter problems.

THE BUSINESS OF THE OLYMPICS

Every two years, the world's attention turns to the Olympic Games. Given that international business and the global economy play such a dominant role in the world today, it is not surprising that the Olympics have come to reflect international business at its most intense. The games are governed by the International Olympic Committee (IOC), which is based in Switzerland. The IOC decides where the games will be held and which sports will be represented, and it oversees the selection of judges and referees. Each country that wants to send athletes to compete in the games establishes a national committee to organize its Olympic effort. These committees are supervised by and report to the IOC.

Potential host cities must give elaborate presentations to the IOC and make substantial commitments in terms of facilities, a volunteer workforce, and related organizational support. For example, as part of their winning bids, Japan promised to build a new high-speed rail line between Tokyo and Nagano, the site of the 1998 winter games, while Greece's proposal featured a new ring road, subway system, and airport in Athens for the 2004 Summer Olympics. China invested more than \$38 billion on a variety of projects, including 37 new or refurbished sports facilities, transportation improvements, and communications upgrades, for the 2008 Beijing games. The British government spent £9.3 billion to build Olympic facilities and improve the transportation network serving the 2012 games, while the Russian government has budgeted \$50 billion for the 2014 Winter Olympics in Sochi.

The infighting among countries to be selected as the games' host is vicious. French President Jacques Chirac's pique over London's selection instead of Paris as the host for the 2012 Summer Olympics intensified the squabbles between France and the United Kingdom over European Union (EU) policies dealing with agriculture, taxation, and foreign affairs. China threatened a trade war with the United States after the U.S. Senate passed a resolution that hurt Beijing's chances to host the summer games in 2000, a prize eventually seized by Sydney, Australia. (Beijing was later awarded the 2008 games.) After Salt Lake City lost its bid for the 1998 games, the city's local organizing committee launched a massive campaign to procure the 2002 games. Unfortunately, its efforts included widespread gift-giving and the lavish entertaining of IOC delegates, which crossed ethical boundaries. As these facts became public, they triggered a worldwide cry for reform of the IOC.

Why would a city want to host the Olympic Games? Most compete for the privilege because the games would thrust them into the international spotlight and promote economic growth. Further, the tourism benefits are long lived; for example, skiers, skaters, and snowboarders continue to enjoy the facilities at previous Olympic sites such as Turin, Nagano, Lillehammer,

Calgary, Albertville, and Lake Placid, pouring money into the local economies long after the Olympic torch has been extinguished. The games also are frequently a catalyst for improving a city's infrastructure. For instance, the high-speed rail line between Tokyo and Nagano halves the travel time between the two cities—a benefit that continues for local residents and for future visitors, as does Athens's new ring road, airport, and subway system. London's Olympic Village was converted to 2,800 apartments after the completion of the 2012 games, providing much-needed housing in one of the world's most expensive real estate markets.

Because of the high cost of running the Olympics, both the IOC and national Olympic committees are always alert for ways to generate revenue. Television coverage provides one significant source of revenue. NBC paid \$1.27 billion for the U.S. broadcast rights for the 2000 Sydney summer games and the 2002 Salt Lake City winter games. It then shelled out an additional \$2.3 billion to lock up the U.S. broadcast rights for the 2004, 2006, and 2008 games and paid \$2.2 billion for the 2010 and 2012 games—even though their sites had not yet been determined. The broadcaster followed a similar strategy in 2011, successfully offering \$4.38 billion for rights to broadcast the 2014, 2016, 2018, and 2020 games in the United States. Broadcast rights for Europe, Australia, Asia, and the rest of the Americas sold for smaller but still breathtaking amounts to local broadcasters. NBC and these broadcasters, in turn, sold advertising time to companies eager to market their goods to Olympic fans throughout the world.

Not surprisingly, capturing viewers in emerging markets is an important part of the IOC's growth strategy. CCTV, the state-owned TV network, paid \$100 million for local broadcasting rights for the 2008 Beijing Olympics. Bidding for TV spots on Chinese television was intense. Yili, a Chinese milk producer, paid CCTV \$2.7 million for four 15-second advertisements for the Chinese market; in comparison, NBC charged \$800,000 for 30-second commercials in the U.S. market.

Another important source of revenue for the IOC and for national committees is corporate sponsors, who wish to capture the prestige and visibility of being associated with the games. The highest-profile level—and, at \$60 to \$80 million, the most expensive—is that of "worldwide partner," a designation valuable to firms that market their products to consumers throughout the world, such as Coca-Cola, McDonalds, Acer, Panasonic, and Samsung. The primary benefit of worldwide partnership is that the partners get priority advertising space during Olympic broadcasts, if they choose to buy it. The worldwide partnership program generated \$957 million during the 2009–2012 Olympic cycle.¹ ■

The millions of dollars spent on the Olympics by television networks and corporate advertisers reflect the internationalization of business—the result of the desire of firms such as Coca-Cola, Panasonic, and Samsung to market their products to consumers worldwide. The forces that have made the Olympics a growing international business are the same forces that affect firms worldwide as they compete in domestic and foreign markets. Changes in communications, transportation, and information technology not only facilitate domestic firms' foreign expansion but also aid foreign companies in their invasion of the domestic market. These trends have accelerated during the past decade as a result of the explosive growth of e-commerce, the reduction in trade and investment barriers sponsored by organizations such as the World Trade Organization and the EU, and the growing importance of emerging markets such as China and India.

The global economy profoundly affects your daily life, from the products you buy to the prices you pay to the interest rates you are charged to the kind of job you hold. By writing this book, we hope to help you become more comfortable and effective in this burgeoning international business environment. To operate comfortably in this environment, you need to learn the basic ideas and concepts—the common body of knowledge—of international business. Further, you must understand how these ideas and concepts affect managers as they make decisions, develop strategies, and direct the efforts of others. You also need to be conversant with the fundamental mechanics and ingredients of the global economy and how they affect people, businesses, and industries. You need to understand the evolution of the global economy and the complex commercial and political relationships among Asia, Europe, North America, and the rest of the world.

To help ensure your future effectiveness in the international business world, we plan to equip you with the knowledge, insights, and skills that are critical to your functioning in a global economy. To that end, we have included hundreds of examples to help demonstrate how international businesses succeed—and how they sometimes fail. You also will read tips and extended examples about global companies in special features called “Bringing the World into Focus,” “E-World,” “Emerging Opportunities,” “People, Planet, and Profits,” and “Venturing Abroad,” and you will have the chance to practice your growing skills in end-of-chapter exercises titled “Building Global Skills.”

What Is International Business?

International business consists of business transactions between parties from more than one country. Examples of international business transactions include buying materials in one country and shipping them to another for processing or assembly, shipping finished products from one country to another for retail sale, building a plant in a foreign country to capitalize on lower labor costs, or borrowing money from a bank in one country to finance operations in another. The parties involved in such transactions may include private individuals, individual companies, groups of companies, or governmental agencies.

How does international business differ from domestic business? Simply put, domestic business involves transactions occurring within the boundaries of a single country, whereas international business transactions cross national boundaries. International business can differ from domestic business for a number of other reasons, including the following:

- The countries involved may use different currencies, forcing at least one party to convert its currency into another.
- The legal systems of the countries may differ, forcing one or more parties to adjust their practices to comply with local law. Occasionally, the mandates of the legal systems may be incompatible, creating major headaches for international managers.
- The cultures of the countries may differ, forcing each party to adjust its behavior to meet the expectations of the other.
- The availability of resources differs by country. One country may be rich in natural resources but poor in skilled labor, whereas another may enjoy a productive, well-trained workforce but lack natural resources. Thus, the way products are produced and the types of products that are produced vary among countries. (“Bringing the World into Focus” provides additional insights into these issues.)

In most cases, the basic skills and knowledge needed to be successful are conceptually similar whether one is conducting business domestically or internationally. For example, the need for marketing managers to analyze the wants and desires of target audiences is the same regardless

BRINGING THE WORLD INTO FOCUS

BORDERS DO MATTER

A decade ago, many self-proclaimed business gurus announced the coming of the boundaryless global economy—one in which national borders were superfluous and irrelevant. It would be hard to find a concept more naïve or oblivious to the realities of doing business internationally. The simple truth is that boundaries and national borders do matter. Nations, defined by those boundaries, have different legal systems and different laws. They have different political systems and social structures. Cultural values differ among the citizens of different nations. Taxes, the price of labor, land, and other resources, and the requirements for establishing a business vary across nations. If we did not have borders, the need for a separate international business course would disappear. We could just study business.

The CAGE model developed by Pankaj Ghemawat, of IESE Business School in Barcelona, is a useful framework for understanding the operating challenges facing international businesses because of these national differences:

- *Cultural distance* (the “C” in CAGE) refers to differences in cultural, linguistic, religious, and social values that can affect the way firms do business within a country. Chapter 4 focuses on important elements of these cultural differences.
- *Administrative distance* refers to differences in the public administration of countries. It can be affected by past colonial ties, common legal heritages, use of a common currency, political alliances, or attitudes toward the proper balancing between the role of the private sector and the role of the public sector. Chapter 3 focuses on many of these differences.



- *Geographic distance* refers to the physical, communications, and transportation links between countries and how the geographic connectedness of countries affects their economic integration. Chapter 2 focuses on the economic geography of the world marketplace.
- *Economic distance* refers to the differences in the economic resource bases of countries. Although natural resources are a component of economic distance, human resources, infrastructure, creation of new knowledge, and promotion of technological innovation are in fact much more important causes of economic distance. Chapter 6 analyzes how these economic differences affect the nature and level of countries’ participation in the global marketplace.

One of the primary challenges facing international business practitioners is formulating and implementing strategies that recognize and then use these differences to create competitive advantages for their firms. This may be as simple as purchasing labor-intensive inputs from countries where wages are low to reduce the costs of necessary components. It may be as complex as restructuring how the firm is organized or how it does business to benefit from global efficiencies while respecting and responding to local culture, laws, and social norms.

Sources: Based on Pankaj Ghemawat, “Distance Still Matters,” *Harvard Business Review*, September 2001; Pankaj Ghemawat, “Managing Differences: The Central Challenge of Global Strategy,” *Harvard Business Review*, March 2007.

of whether the managers are engaged in international business or domestic business. However, although the concepts may be the same, there is little doubt that the complexity of skills and knowledge needed for success is far greater for international business than for domestic business. International businesspeople must be knowledgeable about cultural, legal, political, and social differences among countries. They must choose the countries in which to sell their goods and from which to buy inputs. International businesses also must coordinate the activities of their foreign subsidiaries, while dealing with the taxing and regulatory authorities of their home country and all the other countries in which they do business.

In Practice

- When doing business internationally, business persons must be aware of the differences between their home market and the host market.
- The CAGE model provides a useful framework for classifying these differences, or “distances,” as Ghemawat calls them.

For further consideration: Which element of “distance” is most important—cultural, administrative, geographic, or economic? Or does “importance” vary according to the issue at hand?

Why Study International Business?

There are many different reasons why today’s students need to learn more about international business. First, almost any large organization you work for will have international operations or be affected by the global economy. You need to understand this increasingly important area to better assess career opportunities and to interact effectively with other managers. For example, in your first job assignment, you could be part of a project team that includes members from

International Business Activities

Historically, international business activity first took the form of exporting and importing (see “Bringing the World into Focus”). However, in today’s complex world of international commerce, numerous other forms of international business activity are also common.

BRINGING THE WORLD INTO FOCUS

THE EARLY ERA OF INTERNATIONAL BUSINESS

International business originally consisted of international trade. Trade between nations can be traced back as far as 2000 B.C.E., when tribes in northern Africa took dates and clothing to Babylonia and Assyria in the Middle East and traded them for spices and olive oil. This trade continued to expand over the years, encompassing more regions and a growing list of resources and products. Even the Olympic Games have their roots in this early era, with the first games being held in Greece in 776 B.C.E. By 500 B.C.E. Chinese merchants were actively exporting silk and jade to India and Europe, and common trade routes were being established.

Success in international trade often led to political and military power. First Greece and then the Roman Empire prospered in part because of exploitation of international trade. Ancient wars were fought to maintain trade dominance. For example, the North African city of Carthage became an international business center that rivaled Rome in the third century B.C.E., as merchants from Europe brought precious metals and glass to trade for the grains, ivory, and textiles offered by African merchants. Over a period of 100 years, Rome fought three bloody wars with Carthage to maintain its trade supremacy, finally defeating the Carthaginians in 146 B.C.E. The victorious Romans burned the city and plowed salt into the soil so that crops could not grow, to ensure that Carthage would never again rise as a rival.

During the Middle Ages, Italy became a focal point for international business because of its central location in what was then



the world market. The political and military strength of Venice, Genoa, and Florence reflected their roles as major centers of international commerce and banking that linked trade routes between Europe and China. In 1453 these trade routes were severed when the Turks conquered Constantinople (now Istanbul) and gained control of the Middle East. Europe’s trade with China had been particularly profitable, so European governments became interested in finding new ocean routes to the Far East. Backed by the Spanish government, Christopher Columbus sailed west from Europe looking for such routes. His landing in the Caribbean islands served instead to identify an important new source of resources and, eventually, led to the colonization of the Americas by European countries.

As this colonization took place, new avenues of trade opened. Settlers throughout the Americas sold raw materials, precious metals, and grains to Europe in exchange for tea, manufactured goods, and other commodities. Most of the American territories eventually became independent countries and important contributors to the world economy.

Another phenomenon of great importance to international business developed during the colonial period and the subsequent Age of Imperialism: the growth of foreign direct investment (FDI) and multinational corporations (MNCs), both of which involve foreigners supplying and controlling investments in a host country. European capitalists from such imperialist powers as the United Kingdom, France, the Netherlands, Spain, Belgium, and Portugal nurtured new businesses in their colonial empires in the Americas, Asia, and Africa, establishing networks of banking, transportation, and trade that persist to this day. The earliest of these firms included the Dutch East India Company (established in 1600), the British East India Company (1602), and the Hudson’s Bay Company (1670). These and latter-day trading companies, such as Jardine Matheson Holdings, Ltd., owned copper mines, tea and coffee estates, jute and cotton mills, rubber plantations, and the like as part of their global trading empires.

During the nineteenth century, the invention and perfection of the steam engine, coupled with the spread of railroads, dramatically lowered the cost of transporting goods over land and thereby made larger factories more economical. This development in turn broadened the extent of FDI. The forerunners of such large contemporary MNCs as Unilever, Ericsson, and Royal Dutch Shell took their first steps on the path to becoming international giants by investing in facilities throughout Asia, Europe, and the Americas during this period. New inventions promoting technological change further stimulated FDI. For example, in 1852 Samuel Colt built a factory in Great Britain to produce his famous firearms, and later in the century Dunlop built factories in Belgium, France, and Japan to exploit its tire-making expertise.

Sources: Based on S. D. Chapman, “British-based investment groups before 1914,” *Economic History Review*, vol. 38 (1985), pp. 230–235; John H. Dunning, *Multinational Enterprises and the Global Economy* (Wokingham, England: Addison-Wesley Publishing Company, 1993), p. 3; Simcha Ronen, *Comparative and Multinational Management* (New York: John Wiley & Sons, 1986).



Michael Pustay

During the fifth century B.C., international commerce was dominated by Athens and its allies. The Peloponnesian War (431–404 B.C.) brought an end to Athens’s power and prosperity. Today’s visitors to the Acropolis are reminded of the poignant words of Edgar Allan Poe:

*On desperate seas long wont to roam . . . /Thy Naiad airs
have brought me home /To the glory that was Greece, /And
the grandeur that was Rome.*

Exporting and Importing

Exporting is the selling of products made in one's own country for use or resale in other countries. **Importing** is the buying of products made in other countries for use or resale in one's own country. Exporting and importing activities often are divided into two groups. One group of activities is trade in goods—tangible products such as clothing, computers, and raw materials. Official U.S. government publications call this type of trade **merchandise exports and imports**; the British often refer to it as *visible trade*. The other group of activities is trade in services—intangible products such as banking, travel, and accounting activities. In the United States this type of trade is called **service exports and imports**; in the United Kingdom it is often called *invisible trade*.

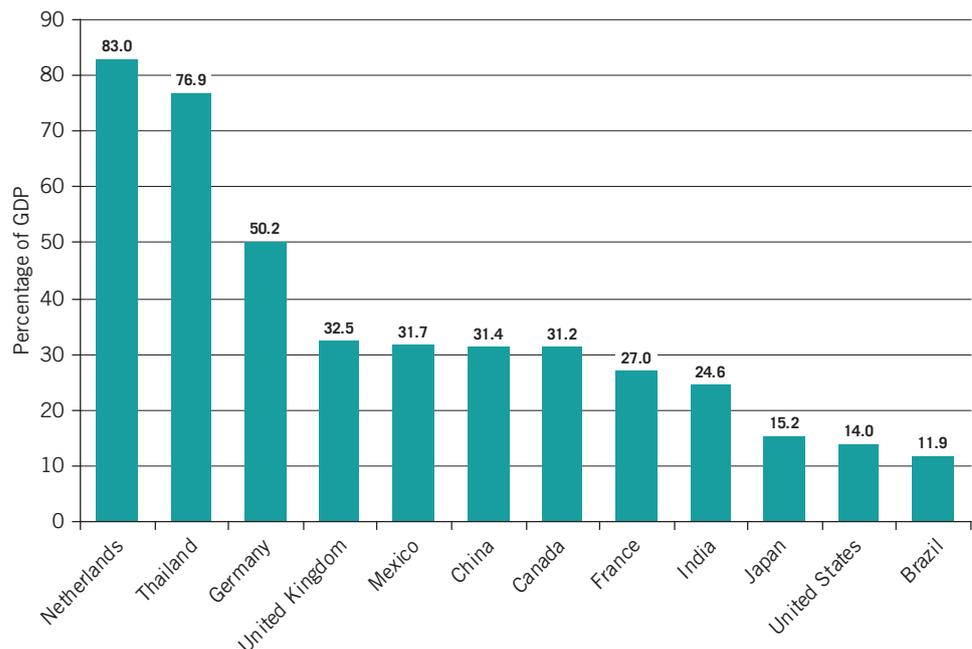
Exports are often critical to a firm's financial health. For example, in 2012, 54 percent of Boeing's \$81.7 billion in sales were to foreign customers, creating tens of thousands of jobs at the company and thousands more at the factories of its parts suppliers. International sales often are equally important to smaller firms, such as Task Force Tips, an Indiana manufacturer of fire hose nozzles, which exports one-third of its production.⁴ Trade is important to countries as well. As Figure 1.1 shows, exporting accounts for more than three-quarters of the gross domestic products (GDP) of the Netherlands and Thailand, and over 30 percent of the GDPs of Canada, China, Germany, Mexico, and the United Kingdom.

International Investments

The second major form of international business activity is **international investments**—capital supplied by residents of one country to residents of another. Such investments are divided into two categories: foreign direct investments and foreign portfolio investments. **Foreign direct investments (FDI)** are investments made for the purpose of actively controlling property, assets, or companies located in host countries. (The country in which the parent company's headquarters is located is called the **home country**; any other country in which the company operates is known as a **host country**.) An example of an FDI is the purchase of all the common stock of the UK's Cadbury PLC by Kraft. After the purchase Kraft installed its own executives to oversee Cadbury's operations and integrate them into Kraft's global procurement and marketing programs.

FIGURE 1.1

Exports of Goods and Services as a Percentage of GDP for Some Key Countries (2011 data)



Source: Based on World Bank data (www.worldbank.org).

Foreign portfolio investments (FPI) are purchases of foreign financial assets (stocks, bonds, and certificates of deposit) for a purpose other than control. An example of a portfolio investment is the purchase of 1,000 shares of Sony's common stock by a Danish pension fund. With this investment the pension fund is trying to raise the rate of return on its asset portfolio rather than control Sony's decision making. For the same reason many investors in recent years have bought shares of mutual funds that specialize in foreign stocks and bonds.

Other Forms of International Business Activity

International business activity can also take other forms. Licensing, franchising, and management contracts are among the most important. **International licensing** is a contractual arrangement in which a firm in one country licenses the use of its intellectual property (patents, trademarks, brand names, copyrights, or trade secrets) to a firm in a second country in return for a royalty payment. The Walt Disney Company may permit a German clothing retailer to market children's pajamas embroidered with Mickey Mouse's smiling face in return for a percentage of the company's sales. **International franchising**, a specialized form of international licensing, occurs when a firm in one country (the franchisor) authorizes a firm in a second country (the franchisee) to use its operating systems as well as its brand names, trademarks, and logos in return for a royalty payment. For example, McDonald's Corporation franchises its fast-food restaurants worldwide. Finally, an **international management contract** is an arrangement wherein a firm in one country agrees to operate facilities or provide other management services to a firm in another country for an agreed-upon fee. Management contracts are common, for instance, in the upper end of the international hotel industry. Hoteliers such as Marriott and Hilton often do not own the expensive hotels that bear their brand names throughout the world but rather operate them under management contracts.

A firm that engages in any of these types of transactions can be labeled an international business. More formally, we can define an **international business** as any organization that engages in cross-border commercial transactions with individuals, private firms, or public sector organizations. But note that we have also used the term *international business* to mean cross-border commercial transactions. Whenever you see this term, you need to determine, from the context in which it is being used, whether it is referring to a general process involving transactions across borders or to a single organization engaging in specific transactions across borders.

The term **multinational corporation (MNC)** is used to identify firms that have extensive involvement in international business. A more precise definition of an MNC is a firm "that engages in FDI and owns or controls value-adding activities in more than one country."⁵ In addition to owning and controlling foreign assets, MNCs typically buy resources in a variety of countries, create goods or services in a variety of countries, and then sell those goods and services in a variety of countries. MNCs generally coordinate their activities from a central headquarters but may also allow their affiliates or subsidiaries in foreign markets considerable latitude in adjusting their operations to local circumstances. Because some large MNCs, such as accounting partnerships and Lloyd's of London, are not true corporations, some writers distinguish between multinational corporations and **multinational enterprises (MNEs)**. Further, not-for-profit organizations, such as the IOC and the International Red Cross, are not true enterprises, so the term **multinational organization (MNO)** can be used when one wants to refer to both not-for-profit and profit-seeking organizations. Table 1.1 lists the world's largest corporations in 2012.

In Practice

- Trade between individuals, tribes, and then nations has occurred for thousands of years. Throughout the centuries, the desire to control trade and trade routes has often been the cause of conflict between countries.
- The most important modes of international commerce include international trade and international investing, as well as more specialized business activities like licensing, franchising, and management contracts.

For further consideration: Analyze the information in Table 1.1. How would you characterize the world's largest corporations? How would you characterize the relative changes in their sizes?

TABLE 1.1 The World's Largest Corporations

	Revenues (in millions of U.S. dollars)	
	2012	2002
Royal Dutch Shell	481,700	179,431
Walmart	469,162	246,525
Exxon Mobil	449,886	182,466
Sinopec Group	428,167	44,503
China National Petroleum	408,603	44,864
BP	388,285	178,721
State Grid	298,449	n.a.
Toyota Motor	265,701	131,754
Volkswagen	247,613	82,203
Total	234,277	96,944
Chevron	233,899	92,043
Glencore Xstrata	214,436	n.a.
Japan Post Holdings	190,859	n.a.
Samsung Electronics	187,800	47,606
E.ON	169,756	44,941
Phillips 66	169,551	58,384
ENI	167,905	46,328
Berkshire Hathaway	162,463	42,353
Apple	156,508	5,470
AXA	154,571	62,050

Sources: Based on *Fortune*, July 22, 2013, p. F1; *Fortune*, July 21, 2003, p. 106; various corporate websites.

The Contemporary Causes of Globalization

International business has grown so rapidly in the past decade that many experts believe we are living in the era of globalization. **Globalization** can be defined as “the inexorable integration of markets, nation-states, and technologies . . . in a way that is enabling individuals, corporations and nation-states to reach around the world farther, faster, deeper, and cheaper than ever before.”⁶

There is little doubt that international trade and international direct investment—the two primary vehicles for conducting international business—are becoming increasingly important in the world's economy. Globalization has led to an intensification of the role of international trade in the economies of the world. As Figure 1.2 indicates, the ratio of international trade to economic activity has risen dramatically. (You may note the impact of the global recession: In 2009, trade volumes decreased more than the world's GDP did, thus causing the ratio of trade to GDP to fall.) In 1950, merchandise trade accounted for about 1 percent of the total GDP of the world's nations; by 2011, it represented 26 percent. International trade in services added another 6 percent to this total. Some of the rapid growth in international trade in services is the result of the development of the Internet and associated technologies, which makes international trade in such diverse industries as banking, consulting, education, retailing, and gambling more feasible. For example, many Canadian and U.S. companies have shifted their customer service and data entry operations to areas with lower labor costs in and outside North America. As long as the transaction can be performed electronically, the physical location of the facility is of little importance. India, for example, has a growing call-center business, providing customer care and troubleshooting services for customers of numerous MNCs throughout the world.

The growth of international business in recent years has been clear and dramatic, as depicted in Figures 1.2 and 1.3. But why has this growth occurred? And why is international business activity likely to continue to skyrocket during the next decade? There are two broad reasons: strategic imperatives, which motivate globalization, and environmental changes, which facilitate it.

Strategic Imperatives

Several basic motives have compelled firms to become more global in both their orientation and actions. These strategic imperatives include leveraging a firm's core competencies, acquiring resources at low cost, expanding into new markets, and competing with industry rivals.

TO LEVERAGE CORE COMPETENCIES One major motive for globalization is the opportunity to leverage a core competency that a firm has developed in its home market. A **core competency** is a distinctive strength or advantage that is central to a firm's operations. By using its core competency in new markets, the firm is able to increase its revenues and profits. Samsung, for example, developed cutting-edge cellular phone technology that was eagerly adopted by domestic consumers in South Korea. Samsung's managers quickly recognized that the firm could increase its revenues and profits by expanding its operations and sales in other countries. Similarly, since its birth in 1972, Singapore Airlines has worked hard to develop award-winning standards of customer satisfaction and reliability that have drawn millions of Asian passengers to its flights. Believing that travelers in other markets would welcome the tender loving care for which the carrier is renowned, Singapore Airlines has deftly expanded its services to more than 60 cities in 30 countries throughout the world.

TO ACQUIRE RESOURCES AND SUPPLIES Another important reason for going international is to acquire resources such as materials, labor, capital, or technology. In some cases organizations must go to foreign sources because certain products or services are either scarce or unavailable locally. For example, North American grocery wholesalers buy coffee and bananas from South America; Japanese firms buy forest products from Canada; and firms worldwide buy oil from the Middle East and Africa. In other cases firms simply find it easier or more economical to buy from other countries. For instance, many U.S. advertising agencies shoot commercials overseas. Cape Town, South Africa, has become a popular site, for example, because production crews and equipment can be hired there for less than 40 percent of their cost in Los Angeles.⁷ As the chapter's closing case, "Demography Is Destiny," indicates, demographic changes will play a major role in the future resource acquisition strategies of MNCs.

TO SEEK NEW MARKETS Seeking new markets is also a common motive for international expansion. When a firm's domestic market matures, it becomes increasingly difficult to generate high revenue and profit growth. For example, the market for toothpaste in Canada, the United States, and the EU can be classified as mature—most people there have had the financial resources for decades to regularly purchase toothpaste. Thus, firms like Procter & Gamble, Unilever, and Colgate-Palmolive cannot expect to achieve significant growth in sales from their toothpaste products in these markets and have aggressively moved into emerging markets like China, India, and Indonesia to seek greener pastures. Expansion into new markets carries with it two other benefits. First, a firm may be able to achieve economies of scale, lowering its average costs as its production increases. Second, such expansion diversifies a firm's revenue stream. As it serves more countries, the firm becomes less dependent on its sales in any one country, thereby protecting itself should that country's economy turn sour.

TO BETTER COMPETE WITH RIVALS Finally, businesses sometimes enter foreign markets to better compete with industry rivals. For example, as Coca-Cola expands aggressively around the world, rival Pepsi-Cola has little choice but to follow and try to keep up. Should Pepsi allow Coca-Cola to dominate important markets, Coca-Cola could use profits from those markets to finance attacks on Pepsi in still other markets. Such thinking permeates industries such as earth-moving equipment, smartphones, and aircraft manufacturing, where the leading firms continually attack and counterattack each other in every region of the world to prevent their rivals from getting a stranglehold in any country.

The Environmental Causes of Globalization

These strategic imperatives provide firms with the motivation to internationalize their operations. However, firms would not have been able to expand their international activities to the extent we have observed during the post–World War II period without significant changes in two key areas: the political environment and the technological environment.

CHANGES IN THE POLITICAL ENVIRONMENT During the first half of the twentieth century, firms wishing to enter new markets were often frustrated by barriers against foreign trade and investment erected by national governments. After World War I, many countries, including the United States, France, the United Kingdom, and Germany, imposed tariffs and quotas on imported goods and favored local firms on government supply contracts. As a result, international trade and investment declined throughout the 1930s. However, after World War II these policies were reversed. The major trading powers negotiated reductions in tariffs and quotas and eliminated barriers to FDI within their borders. Many of the reductions were negotiated through the General Agreement on Tariffs and Trade (GATT) and its successor, the World Trade Organization (WTO). Regional accords, such as the EU, the Mercosur Accord, and the North American Free Trade Agreement (NAFTA), also have relaxed trade and investment barriers among their members.

TECHNOLOGICAL CHANGES Changes in governmental policies encouraged international business activity. Improvements in technology—particularly in communication, transportation, and information processing—made international business more feasible and more profitable. Think about the difficulties of conducting business internationally when the primary form of transportation was the sailing ship, the primary form of data processing was pencil and paper, and the primary form of communication was the letter delivered by a postman on horseback. Transportation improvements during the past 150 years—from sailing ship to steamship to seaplane to jet airliner—mean that a manager in London no longer needs to spend weeks traveling to confer with colleagues in New Delhi, Toronto, or New York. Advances in transportation also have stimulated growth in international tourism, which is the largest component of international trade in services. The increasing ability of computers to rapidly process vast quantities of information allows firms to manage offices and factories located in every corner of the globe. Exxon Mobil, for example, relies on its computers to continuously adjust the output of its refineries and the sailings of its tankers to meet changes in worldwide demand for its products. Changes in communications technology, such as the advent of electronic mail, smartphones, and

VENTURING ABROAD

MANCHESTER CITY IN DUBAI

It was the beginning of September 2008 and the usual excitement was mounting as the football transfer window was about to close. Suddenly, out of nowhere it seemed, came the Abu Dhabi United Group for Development and Investment. Headed by Dr. Sulaiman Al Fahim, a billionaire in his own right, the group bought the Premier League team, Manchester City, from the former Thailand Prime Minister, Thaksin Shinawatra. Negotiations had begun three weeks before and were completed late on Sunday August 31, at the Emirates Palace Hotel in Dubai. The group is believed to have \$221 billion at their disposal. In a stroke, the club's \$147 million plus debt was paid off and they began to throw their new financial muscle into the transfer market. They snatched the Real Madrid Brazilian-born striker, Robinho, from the cash-rich Chelsea, which is backed by Russian billionaire Roman Abramovitch.

Apparently, so cash-rich is the doctor and his group that the money required to purchase Manchester City (calculated at around \$295 million) was wired from reserves of the brother of the ruler



of Abu Dhabi, Sheikh Mansour Bin Zayed Al Nahyan. To put the purchase of Robinho at \$47.8 million into perspective, Abu Dhabi generates that amount in surplus revenue in five hours by pumping oil. The doctor intends to make \$385 million available to the football club for transfer spending over the next two years. The key aim of acquiring Manchester City is not only to win football glory in the world, but also raise the profile of Abu Dhabi itself.

Abu Dhabi has been trying to diversify their economy in recent years, specifically by making investments abroad in financial services and in tourism. Abu Dhabi's oil reserves are estimated to be worth around \$1 trillion.

Sources: Arab Business News, www.arabbusiness.com; Manchester City Football Club, www.mfc.co.uk; *Financial Times*, www.ft.com; Real Madrid, www.realmadrid.com; United Arab Emirates Government, www.government.ae; *Gulf News*, www.gulfnews.com.

tablet computers, enable a manager in Tokyo to receive reports from colleagues in Amsterdam, Abidjan, and Auckland in seconds rather than days. These technological advances make managing distant businesses far easier today than executives would have dreamed possible just a few decades ago and so have facilitated expansion into international markets.

Globalization and Emerging Markets

We noted that globalization has led to an intensification of international business activity. It is also marked by an expansion of such activity into new markets previously insulated from the international marketplace.

The political changes discussed previously have played a major role in this process. During the Cold War between the United States and the Soviet Union, many scholars divided the world into three regions: the First World, consisting of the rich, major trading nations from Western Europe, North America, Australia, and parts of Asia, most of which were allied diplomatically with the United States; the Second World, consisting of the Soviet Union and allied Communist states; and the Third World, consisting primarily of the low- to medium-income countries populating Latin America, Africa, and most of Asia. Most international business activity took place between members of the First World. The Second World walled itself off to commerce with the First World, while the Third World was primarily viewed as a supplier of raw materials and commodities to the First World countries.

This is no longer the case: The collapse of European Communism, the ideological and policy changes undertaken by China and India, and the reduction of trade barriers have transformed the global marketplace. Shakespeare once wrote, “All the world’s a stage.” Today savvy businesspersons recognize that business opportunities are no longer limited to the traditional markets of Western Europe, North America, or Japan. Indeed, today much of the attention of international businesses is focused on the so-called **emerging markets**, countries whose recent growth or prospects for future growth exceed that of traditional markets. Many companies are finding much of their sales and profit growth is attributable to emerging markets. For example, Burberry’s sales in China rose 20 percent in 2012. China now accounts for about 14 percent of this upscale retailer’s revenues.⁸

There is no universally accepted definition of the countries to be included in the emerging markets category. Some scholars limit the term to the **BRIC countries**—Brazil, Russia, India, and China. Other researchers have used the term to describe the so-called **Big Ten**—Argentina, Brazil, China, India, Indonesia, Mexico, Poland, South Africa, South Korea, and Turkey.⁹ Other experts have a more expansive definition, including most non-high-income countries in Africa, Asia, Eastern Europe, and Latin America. Regardless of the definition, it is clear that international businesses that ignore the emerging markets do so at their own risk. Consider that two of these emerging markets, China (see Map 1.1) and India, together account for more than one-third of the world’s population. Their economies are growing significantly faster than that of the world as a whole, as Table 1.2 indicates.

While China’s economy has enjoyed double-digit annual growth in the past 20 years, China’s leaders need to develop policies to ensure that its large rural population shares in the country’s prosperity.



Ricky W. Griffin

TABLE 1.2 Characteristics of Selected Emerging Markets, 2011

Country	Total Population (millions)	Total GDP (billions of U.S. dollars)	Per capita GDP (in U.S. dollars)	Average Annual Growth in GDP, 2003–2011, in percent
BRIC				
Brazil	197	2,477	12,594	3.9
Russia	142	1,858	13,089	4.8
India	1,241	1,848	1,488	8.1
China	1,334	7,318	5,444	10.8
Total	2,914	13,501		
Big Ten				
Argentina	41	446	10,942	7.8
Brazil	197	2,477	12,594	3.9
China	1,334	7,318	5,444	10.8
India	1,241	1,848	1,488	8.1
Indonesia	242	847	3,495	5.6
Mexico	115	1,153	10,047	2.4
Poland	38	514	13,462	4.5
South Africa	51	408	8,070	3.6
South Korea	50	1,116	22,424	3.8
Turkey	74	775	10,524	5.3
Total	3,383	16,902		
World total	6,966	69,981	10,035	2.7

Source: Based on World Bank, *World Development Indicators* data bank.

An Overview of the Contents of This Book

In writing this book, we have started with the assumption that most readers will eventually work for or own a firm that is affected by international business activity. Our goal is to help them become more confident and effective managers in the competitive global marketplace. To do so, we provide our readers with the knowledge and skills necessary to succeed in international business.

We have structured the contents of the book to move from relatively macro, or general, issues to increasingly micro, or specific, issues that managers deal with regularly. Our rationale is that managers must fully understand the context of international business to work effectively within it. This broad, general context provides the backdrop within which all international business occurs. At each increasingly specific level within that context, the international manager is faced with specific and operational issues, problems, challenges, and opportunities.

Part 1 comprises Chapters 1 through 5. It provides an overview of the world's marketplaces. Chapter 1 has supplied some background definitions and discussed the contemporary global business environment. Chapter 2 provides a wealth of economic and geographical information about the world's major economies and business centers. Chapters 3 and 4 describe the national environments of international business—the more specific, country-level environmental context that affects and impacts business activity and opportunities. Chapter 5 addresses the social responsibility challenges that international businesses must address in the era of globalization.

Parts 2 through 4 follow a logical progression of topics, moving from the broad, general issues confronting international business to increasingly more specific, focused issues that managers face daily (see Figure 1.4). Part 2 discusses the international environment in more detail, addressing the overall context of international business and introducing many of the global forces and conditions that affect organizations and managers. Part 3 adopts the perspective of a

CHAPTER REVIEW

Summary

International business encompasses any business transaction that involves parties from more than one country. These transactions can take various forms and can involve individual companies, groups of companies, or government agencies. International business can differ from domestic business because of differences in currencies, legal systems, cultures, and resource availability.

Studying international business is important for several reasons. First, any organization you work for, even if small, is likely to be affected by the global economy. Second, someday you may work for a foreign-owned firm. Further, you need to keep pace with other managers who are learning to function in international settings. Finally, you need to be culturally literate in today's world.

International business activity can take various forms. Exporting involves selling products made in one's own country for use or resale in another country. Importing involves buying products made in other countries for use or resale in one's own country. FDIs are investments made for the purpose of controlling property, assets, or companies located in foreign countries. Other common forms of international business activity include licensing, franchising, and management contracts.

An international business is one that engages in commercial transactions with individuals, private firms, or public sector organizations that cross national boundaries. Firms with extensive international involvement are called multinational corporations, or MNCs.

International business has grown dramatically in recent years because of strategic imperatives and environmental changes. Strategic imperatives include the need to leverage core competencies, acquire resources, seek new markets, and match the actions of rivals. Although strategic imperatives indicate why firms wish to internationalize their operations, significant changes in the political and technological environments have no doubt facilitated the explosive growth in international business activity that has occurred since World War II. The growth of the Internet and other information technologies is likely to redefine global competition and ways of doing international business once again.

Review Questions

- 1-1. How do country-specific reasons distinguish international business from domestic business?
- 1-2. Discuss the importance of the global economy in your life?
- 1-3. What are the differences between visible and invisible trade?
- 1-4. How do merchandise exports and imports differ from service exports and imports?
- 1-5. What is portfolio investment?
- 1-6. What are the basic reasons for the recent growth of international business activity?

Questions for Discussion

- 1-7. What is the impact of globalization on international business and its growth?
- 1-8. What are the driving forces behind global firms? How do emerging markets affect the ability of global firms in leveraging their core competencies? Explain your answer with examples.
-  1-9. Which markets are more important to international businesses—the traditional markets of North America, the EU, and Japan, or the emerging markets? Defend your answer.
- 1-10. What makes a firm truly 'global' in its outlook? Do you think technology, cultural and political changes affect the orientation of a firm?
-  1-11. What are some of the differences in skills that may exist between managers in a domestic firm and those in an international firm?
- 1-12. Would you want to work for a foreign-owned firm? Why or why not?

Building Global Skills

List different products you use on a regular basis, such as your alarm clock, camera, car, coffeemaker, computer, smartphone, television, tablet—perhaps even your favorite CD, shirt, fruit juice, ebook reader, or footwear. Determine which firms made these items. After you have developed your list, go to the library or surf the Internet to research the following for each item:

- 1-13. In which country is the firm headquartered?
- 1-14. What percentage of the firm's annual sales comes from its home market? What percentage comes from other countries?
- 1-15. Where was the item most likely manufactured?
- 1-16. Why do you think it was manufactured there?

Follow up by meeting with a small group of your classmates and completing these activities:

- 1-17. Discuss the relative impact of international business on your daily lives.
- 1-18. Compile a combined list of the 10 most common products the average college student might use.
- 1-19. Try to identify the brands of each product that are made by domestic firms.
- 1-20. Try to identify the brands of each product that are made by foreign firms.
- 1-21. Does your list of 10 products include items with components that are both domestically made and foreign made?

CLOSING CASE

Demography Is Destiny

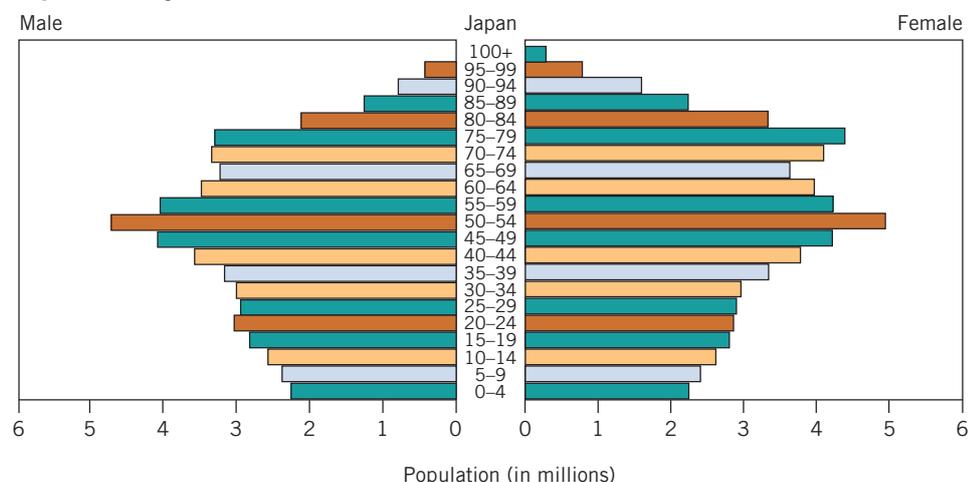
Recent newspaper headlines trumpeted stories of massive protests in Paris by students and workers denouncing pending labor market reforms; of teachers, policemen, and firefighters in Wisconsin protesting a bill that would truncate their collective bargaining rights; of marches by civil servants in Athens and London denouncing proposed cutbacks in their pensions and working conditions. Meanwhile, the Central Committee of the Communist Party announced new initiatives to promote economic development in China's rural areas. Underlying each of these actions are dramatic demographic changes occurring in these countries.

Demography is the study of the structure of human populations—their size, age composition, gender mix, growth, and so on. Demographers often assert that demography is destiny. By that they mean that a country's demography

constrains and shapes the opportunities available to it. If so, then changes in the population, age structure, and gender mix of the world's major economies suggest that significant changes are in store for the world economy.

A traditional way of examining a country's demography is through the use of population pyramids (see Figure 1.5). In olden days, the normal structure of a country's age distribution was a pyramid. Each layer of the pyramid consisted of the number of individuals in an age bracket. The pyramid shape resulted from the fact that the number of people aged 0–4 was slightly larger than the number aged 5–9; 5–9-year-olds slightly outnumbered 10–14-year-olds; and so forth. The declining size was the result of the cruel reality of death from disease, famine, and childbirth in a world without modern medicine. Fortunately, better health care, education, and

FIGURE 1.5
Population Pyramids for 2025



(Continued)

that one child enters the labor force and his or her parents subsequently retire, the child may need to provide financial support for both parents; and moreover, given the improvements in longevity in China, in some cases the child may also need to support four grandparents. Second, although saving rates in China are quite high, few companies provide pension benefits to their employees. Moreover, because of Chinese cultural values that favor male children, the one-child policy has created a conspicuous imbalance in the gender ratio between males and females, with unknown but likely significant impacts on the marriage market, family formation, and elder care. In a decade or two, consumption patterns in young, growing India are likely to diverge dramatically from those in a graying China. Suppliers of video games, big-screen TVs, and child car seats may flock to India, whereas purveyors of hypertension and anticholesterol medicines, bifocals, and retirement financial services will find China an attractive market.

Case Questions

- 1-22. What challenges do graying populations create for companies?
- 1-23. What opportunities do graying populations create for firms?
- 1-24. How will demographic changes affect the competitiveness of countries in the international marketplace?
- 1-25. What can countries do to counteract the impact of these demographic changes on their economic competitiveness?
- 1-26. What has been the impact of the one-child policy on China's economic fortunes?
- 1-27. Go to the U.S. Census Bureau's international data base at www.census.gov. Pick two countries and analyze their changing demographics. Which one faces the more favorable demographic future?

Sources: Based on "China's one-child plan faces new fire," *Financial Times*, April 29, 2011, p. 1; "India passes 1.2 billion mark," *Wall Street Journal*, April 1, 2011, p. A10; <http://www.census.gov/ipc/www/idb>; "No babies," *New York Times*, June 29, 2008 (online); "Cautiously, an aging Japan warms to foreign workers," *Wall Street Journal*, May 25, 2007, p. A1; "Bringing up baby," *The Economist*, June 14, 2007, (online); "Population shift is ignored threat," *Wall Street Journal*, June 6, 2006, p. A9; "Labor shortage in China may lead to trade shift," *New York Times*, April 3, 2006 (online); "Chinese president asks senior officials to promote rural development," People's Daily Online, February 15, 2006; "Turning boomers into boomerangs," *The Economist*, February 18, 2006, pp. 65–67; "Hey, big-spender," *The Economist*, December 3, 2005, p. 52; "Why China stands to grow old before it gets rich," *Financial Times*, November 10, 2005, p. 13; "China and India: The challenge and the opportunity," *Businessweek*, August 22/29, 2005, pp. 51–136; "The factory that has mastered the ageing challenge," *Financial Times*, July 5, 2005, p. 7; "China's golden oldies," *The Economist*, February 26, 2005, p. 65.

MyManagementLab[®]

Go to mymanagementlab.com for the following Assisted-graded writing questions:

- I-28. What are the primary causes of globalization?
- I-29. Is globalization good or bad for the world? Is its impact uniform, or are some groups and countries benefited/harmed more than other groups and countries?
- I-30. Mymanagementlab Only—comprehensive writing assignment for this chapter.

Endnotes

1. "NBC Says Olympic Ad Sales Strong," *Wall Street Journal*, May 16, 2013; "Olympic Bailouts for Russian Moguls," *Wall Street Journal*, April 29, 2013; "Russia Tempers Expectations for Sochi," *Wall Street Journal*, March 22, 2013; "NBC Realizes Olympic Dream," *Wall Street Journal*, June 8, 2011, p. B1; "Security is a 'massive challenge,'" *USA Today*, March 22, 2011, p. 2C; Olympic Marketing Fact File, www.olympic.org; "In NBC's shadow, Comcast ponders an Olympic plunge," *New York Times*, December 28, 2010; "When the circus leaves town," *The Economist*, July 24, 2010, p. 57; "Gold medal in the race for business," *Financial Times*, September 24, 2009, p. 12; "Olympic marketers seek to soar above politics," *Wall Street Journal*, March 20, 2008, p. B5; "Chinese Olympic ads draw high prices," *Wall Street Journal*, November 20, 2007, p. B3; "GM's pending Olympic exit reshapes marketing arena," *Wall Street Journal*, August 8, 2007, p. B2; "A year out, Beijing games test China's rising power," *Wall Street Journal*, August 7, 2007, p. A1; "Stepping up," *Houston Chronicle*, February 24, 2006, p. C2; "Obscurity takes a holiday," *Wall Street Journal*, February 11–12, 2006, p. A5; "Closing words opened door for London," *Financial Times*, July 7, 2005, p. 2; "A ringing endorsement: Business backing for the Olympics grows as scandals abate," *Financial Times*, July 1, 2005, p. 11; "NBC proud as a peacock of Olympics deal, high-tech focus," *Houston Chronicle*, June 7, 2003, p. 13B; "NBC plans 24-hour coverage of Summer Olympics in 2004," *Wall Street Journal*, February 5, 2003, p. B10; "Sydney already