1 Introduction to International Business

Overview

The chapter begins with an explanation of the philosophical distinction between 'international' and 'global' approaches to business. This is followed by a justification of the book's core belief that it is more useful for international managers to develop an ability to respond to varying international circumstances than to seek a 'one-best-way' solution applicable everywhere and always. Significant statistics are provided, demonstrating the growing importance of international business in the modern world. The final section reviews some of the many different reasons why companies engage in cross-border transactions, highlighting the specific difficulties that they will face in international as opposed to domestic dealings.

Learning Objectives

After reading this chapter, you will be able to:

- compare the concepts of international and global business;
- determine the value for international managers of developing a flexible mindset;
- understand the main terminology used in international business studies;
- perceive the link between politics, economics, and international business;
- analyse the internal and external drivers of international business.

Case Study 1.1

When American cars fall behind international standards

The first foreign producers to gain a significant share of the US automotive market were the Japanese in the 1970s, led by Toyota, Honda, and Nissan (or Datsun, as it was known). Offering fuel-efficient models that were better adapted to the high oil prices of the time, the Japanese helped to build a new market niche in a country where low fuel prices had always been taken for granted. The American carmakers, led by the 'Big 3' (General Motors, Ford, and Chrysler), reacted to this competition in their home market by lobbying Washington to place restrictions on Japanese imports. This seemed a cheaper option than redesigning their product ranges away from the big gas-guzzlers that American consumers had traditionally favoured.

The counter-oil shock of 1986, which led to a dramatic fall in fuel prices, appeared to justify the Big 3's strategy. Indeed, with energy inflation seemingly under control, the American carmakers decided to invest massively in the light truck segment, promoting household purchases of minivans, 4x4s, pick-ups, and sport utility vehicles. These vehicles were anything but efficient, and, despite a great deal of technological progress, fuel consumption averages actually rose in the USA between the 1980s and the 2000s. At the same time, strong light truck sales, which by 2008 accounted for 54 per cent of all new vehicle purchases in the USA versus 22 per cent in the 1980s, helped to restore the Big 3's profitability temporarily. This strategic decision came with a heavy cost, however, since it lulled US auto executives into believing that they still did not have to incorporate long-term global trends into their planning.

The credit crunch affected large American pick-up trucks more than it did fuel-efficient Japanese vehicles (© iStockphoto).

The energy crisis of 2006–7 shook up the global economic environment, with oil prices hitting new records and peaking US consumers' interest in fuel-efficient cars. This was a great opportunity for Toyota, which had concentrated more on global energy trends and used the years since the 1980s to develop a hybrid model (the Prius) that consumed less oil and emitted less carbon dioxide (a key contributor to global warming). This positioning gave the Japanese carmaker a tremendous edge and revealed serious flaws in the Big 3's strategic outlook. The 2008 credit crunch, which caused new model sales to crash worldwide, added to the pressure on the American carmakers. Not only were the Big 3 unable to count on export markets to offset falling demand at home; the recession meant that even in their domestic market it was also harder for them to sell the big expensive vehicles in which they had specialized. The American carmakers' product range is especially unfortunate given the likelihood that much future growth in the world automotive markets will occur in emerging economies, where households can afford only modest vehicles, like the small cars that companies such as Romania's Dacia or India's Tata are developing.

With hindsight, the decision taken by America's Big 3 carmakers during the 1980s and 1990s to remain focused on domestic conditions and consumer preferences undermined their chances of survival in what has become an increasingly globalized business. Things got so bad that by summer 2009 General Motors had declared bankruptcy and Italian carmaker Fiat had taken over Chrysler. This could be contrasted with the promising outlook for new producers like China's BYD, a battery specialist that was having great success in applying its technology to new kinds of passenger vehicles. One of the first rules of international business is that, with very few exceptions, global trends tend to have a greater impact than domestic ones.

Introduction

The simplest definition for international business is 'cross-border economic activity'. This has existed in various forms ever since human communities began interacting with one another. When human tribes first started trading beads or minerals like flint more than ten thousand years ago, they were engaging in prehistoric forms of international business (Watson 2005). Of course, trade has become slightly more complicated since then. Nowadays, international business refers to the exchange not only of physical goods but also of services, capital, technology, and human resources. The first point to make about this field is that it covers a very broad spectrum of activities.

Just as important is to recognize what makes international business distinct from other areas of study, and where it overlaps with them. Many aspects of domestic business are also found in international business, but they are treated differently because of the latter field's emphasis on cross-border aspects. Similarly, international business covers most if not all of the same topics as international management but goes much further. Where international management focuses mainly on decisions made by individuals operating within a corporate setting, international business also incorporates the broader political, economic, social, technological, philosophical, and environmental contexts within which firms operate. It is a very broad discipline with connections to many if not most of the issues affecting people in their daily lives. The best international business students and practitioners can analyse on many different levels and tend not to recognize artificial borders between business, economics, and politics (White 2001). Indeed, the ability and desire to embrace diversity give this discipline its distinct philosophy and enduring attraction.

Section I: Visions of international business

+ Globalization
Process whereby the world becomes increasingly interconnected at an economic, political and social level.

A good starting point for this book is to distinguish between the concept of international business and the neighbouring notion of **globalization**, with which it is often confused (Hirst and Thompson 1999). Every discipline has its own vocabulary, and it will be useful to introduce certain key terms early on. Subsequently there will be a brief look at the philosophies underlying international business. Lastly, analysis of current statistics will give readers a sense of its characteristics today.

Definitions and philosophy

+ Home/host country
People/companies originate from a 'home country'. When they operate abroad, they are working in a 'host country'.

Thinking point
Which has a bigger effect on the business environment, national differences or global similarities?

International business, if only because of its cross-border nature, raises several specific challenges that business practitioners and academics ignore at their peril. It can be a very difficult adjustment for companies or individuals leaving a **home country** with which they are familiar to operate in a **host country** where the environment and people are foreign to them. There is no doubt that the world has shrunk over human history and that globalization has been a key factor in this process (MacGillivray 2006). At the same time, it is unrealistic and even dangerous to assume that societies worldwide are converging to such an extent that there is no longer any need to study their economic, political, and cultural differences. This recognition that the world remains a complex and diverse place is best expressed through the distinction made between the terms 'global' and 'international'.

The word 'global' is associated with the idea of a single world and therefore stresses similarities between different communities. The word 'international', on the other hand, starts with an emphasis on the lack of similarity. There is a strong argument that this latter approach is more useful, since it acknowledges the specific obstacles that arise when people from different nations and cultures come together. It also prepares practitioners to develop the **insiderization** strategies that are necessary to overcome the many barriers that people face when they cross borders (Ohmae 1999). In an ideal world, no such barriers would exist. Unfortunately, humankind does not live in such a world, if only because of **xenophobia** and the feelings of 'animosity' that some populations have towards others (Amine 2008). This is not to deny growing similarities between many societies at certain levels, or that some sectors of activity operate along global instead of national lines (see Chapters 5 and 6). Indeed, there is little doubt that greater global interconnectedness has had a very deep effect on business and individuals, and some sociologists have identified what should be greeted as a positive trend towards greater cosmopolitanism and tolerance amongst many citizens of the world (Giddens 2002). By the same token, other observers doubt how long this new religion of 'globalism' will last, preferring to highlight the enduring and even resurgent nature of national awareness (Saul 2006). As shown by rising sentiments of **protectionism** in the wake of the 2008 credit crunch, when times are hard, many people's first concern is still for the welfare of their local community. Indeed, as the crisis worsened, fears arose that the world might 'retreat to narrow nationalism' (*Guardian* 2009). In our opinion, there is nothing inevitable about globalization or, indeed, any other socio-economic or cultural trend.

What is clear is that most people have an identity that reflects, at least in part, the specificities of their culture of origin and/or the **paradigm** they use to make sense of the world (see Chapters 2 and 10). An 'international' approach embodies this principle more completely than a 'global' one does, if only because it starts with an acknowledgement of individuality. Philosophically, it is not a neutral choice to stress diversity as opposed to oneness. It is an attitude that leads to the expectation that the international business strategies and behaviour that apply in one situation may not be appropriate in another—there is no 'one best way' of doing business. This may seem obvious to people whose culture of origin emphasizes the need to seek multiple solutions to any one problem, but it can be a difficult adjustment for people from a culture where the emphasis is on discovering a single optimal solution to a problem. A prime example from the early 1990s was when academics, impressed by Toyota's successful industrial methods, published an analysis that some observers took as proof that one particular way of working can be superior to all others at a given moment in time (Womack et al. 1991). This caused a storm in university circles. It is best to state openly that the present book is based on the idea that international business students are better served by an approach aimed at helping them to develop a flexible mindset instead of trying to help them find the 'right answer'.

+ **Insiderization**
When people or companies are so deeply integrated into a local society that their foreign origins are forgotten.

+ **Xenophobia**
Fear of things that are foreign.

+ **Protectionism**
General policy where a national government adopts policies restricting foreign producers' access to its domestic market.

+ **Paradigm**
A worldview—that is, a vision of how things are and/or should be organized.

Companies doing international business

Now that we have outlined how the term 'international' will be used here, the next task is to define what kind of business is actually involved. It could be argued that 'international business' is already occurring any time an individual engages in a cross-border transaction. Indeed, private parties play an important role in the world economy: investors purchasing currencies or shares in foreign companies (see Chapters 13 and 14); or local agents acting as representatives and providing firms with information on countries with which they are unfamiliar (see Chapter 8). Unsurprisingly, however, most international business is done by companies, ranging from huge firms to **small and medium-sized enterprises** (SMEs) to micro-firms that may or may not be 'born global' from the very outset. It is impossible to generalize why firms might want to seek their fortune abroad. In general, the main motivation used to be the acquisition of resources, whereas nowadays it tends to be the development of knowledge and markets (Aharoni and Ramamurti 2008). Paradigms vary strongly over time, however. As Chapters 4 and 5 demonstrate, history is another discipline that has much to offer the international business student.

The general terminology that this book uses to refer to companies that have regular dealings outside their home country is **multinational enterprise** (MNE). Other international business books will often use other terms, such as multinational corporation (MNC),

+ **Small and medium-sized enterprises**
'Enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million euros, and/or an annual balance sheet total not exceeding 43 million euros' (European Commission 2003).

+ **Multinational enterprises**
Firms whose regular activities cause them to engage with and/or operate in more than one country at a time.

+ Global firm
Company that is conceived of as serving a unified world market rather than differentiated national markets.

+ Configuration
How a company designs and locates different corporate functions such as research, production, marketing, and finance.

+ Subsidiary
(Foreign) unit belonging to a company's head office.

+ Foreign direct investment (FDI)
Where a firm funds a permanent or semi-permanent physical unit abroad. One definition is that this involves a company taking a minimum 10 per cent stake in a foreign entity.

+ Value chain
Succession of acts that successfully add value to an item as it is transformed from a raw material or input stage to a finished product or service.

+ Upstream
Early value chain activities undertaken when processing or transforming a product or service.

+ Downstream
Later value chain activities relating to the interface between a company and its customers.

+ Generic
Item that is not differentiated for a specific use but has a variety of applications.

transnational corporation (TNC), and **global firm**. The problem with these other expressions is that each designates a specific kind of company and is therefore not general enough. For instance, talking about MNCs neglects the fact that not all actors playing a role in international business are corporations or even privately owned enterprises. Similarly, terms such as TNCs and above all global firms do not sufficiently communicate the connections that continue to tie most companies with international interests to their country of origin. MNE is a more neutral term to describe the broad category of firms that, according to some statistics, account for more than 70 per cent of world trade (Steger 2003). Thus, for the rest of this book, the term MNE (which can include SMEs engaged in foreign transactions) will be the basic unit of analysis.

MNE configurations

A firm that owns facilities in a single country but carries out transactions regularly outside its borders may qualify as an MNE, but a far more typical and informative figure is the firm whose international **configuration** is comprised of a head office and **subsidiaries** located in different parts of the world. It has been estimated that MNEs' foreign subsidiaries are responsible for slightly more than 10 per cent of global economic activity (Serfati 2006). The significance of such units' activities can vary widely between countries like France or the UK, where they account for up to 30 per cent of national sales, and others like Japan, where they play almost no role at all in key areas like manufacturing employment. In general, however, there is a trend towards MNEs expanding their international presence through foreign subsidiaries. Alongside trade, companies' **foreign direct investment** (FDI) is the second main pillar of international business and constitutes a key focus in this field

The tendency has been for MNEs to try to integrate units' functional activities. This has often been in application of theories that different locations should specialize in activities where they have a competitive advantage (see Chapter 4). One consequence is that an increasing proportion of international business involves MNE subsidiaries trading with one another and/or with subcontractors (Coleman and Underhill 1998). This is one reason why it is so important to understand the different ways in which MNE head offices organize their relational networks (see Chapter 9).

International value chains

The most useful way of picturing MNEs' work organization is to imagine the production and sale of a good or service as a series of acts adding to the item's value as it is transformed from a raw material into a semi-processed stage before ending up as a finished good or service (see Figure 1.1). This series of acts is called the **value chain**. It is divided into production-related **upstream** activities (see Chapter 11) and marketing-related **downstream** activities (see Chapter 12). One of the main features of international business today is that many firms do not perform by themselves all of the activities comprising the value chain in which they are involved. Instead, they might ask external partners to take responsibility for certain phases. As such, it is more accurate to represent international value chains as the sum of several intermediary value chains. A good example is provided by blue jeans, which should be analysed not just as a finished product but as the sum of many lower-level **generic** products. One of these is the zip, which is the culmination of several intermediary businesses, starting with extraction of minerals, the processing of basic metals, and their subsequent transformation into zips. It is important to understand that the end product of one company's international value chain (for example, zip-makers) is just an intermediate phase in the value chain of another company (the jeans-maker).

This portrayal of international business as a series of cross-border value chains raises questions about the rate at which value accumulates while a service or good is being transformed into its final form. For presentation's sake, Figure 1.1 shows value accumulating at a linear rate. This is not entirely realistic, since, depending on the sector in question, value

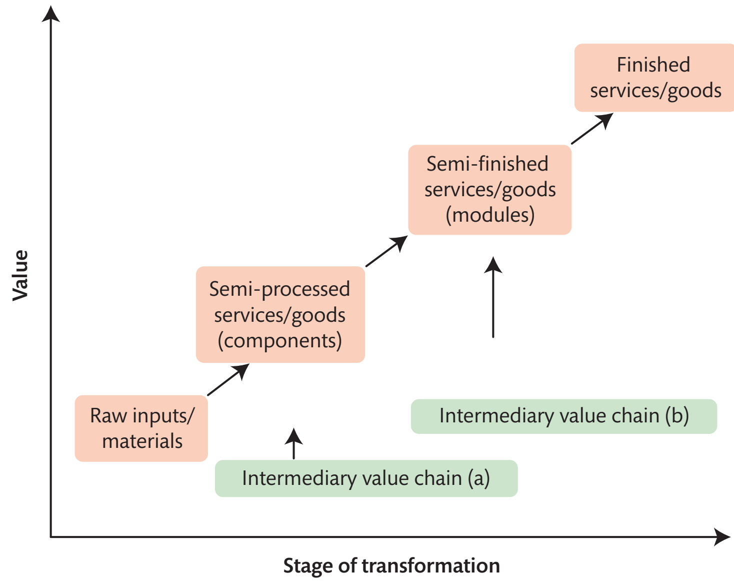

Figure 1.1 Visualizing the transformation of a good or service: each level adds value and also has its own intermediary value chains.

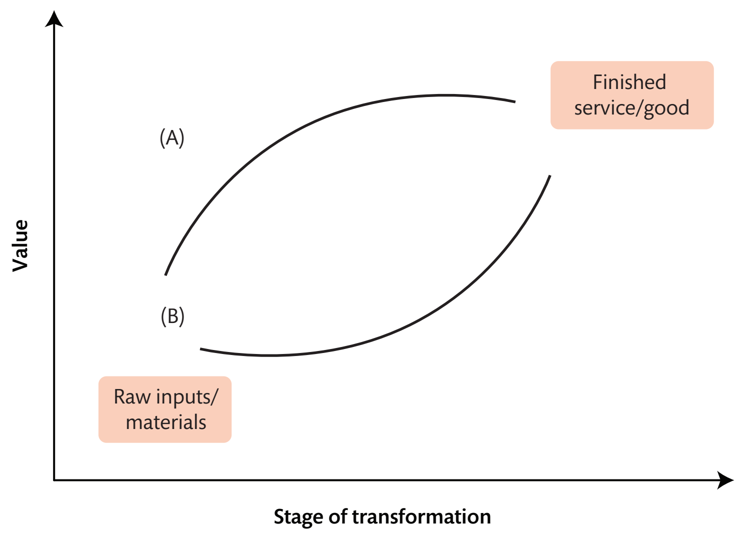

Figure 1.2 Value tends not to increase in a straight line. Curve (A) indicates a product or service where the upstream side accumulates a greater share of the value added than the downstream. Curve (B) indicates the opposite.

will tend to accumulate more or less quickly when the good or service is more towards the upstream or downstream side of the value chain. For instance, in the coffee business, a tiny percentage of what consumers pay for a cup at Starbucks goes to upstream bean-growers, possibly reflecting producers' lack of bargaining power when dealing with powerful MNEs whose main area of operations is further downstream, closer to consumers. Inversely, in a sellers' market (like oil) marked by less competition amongst producers, value will tend to accumulate in the hands of upstream producers. Figure 1.2 offers a more realistic picture of (international) value chain curves.

Clearly it is more efficient to operate at that part of the value chain where value accumulates most intensively (i.e. where the value-added curve is steepest). This is just as true for national economies as for companies. Those countries whose firms specialize in high value-added production are clearly at an advantage over those that specialize in low value-added goods—or, as economists would put it, they enjoy better **terms of trade**. For example, if US firms are global champions in computers and Sri Lankan companies lead the world in the tea business, the USA is clearly at an advantage, since the markets where it dominates create greater value than the markets where Sri Lanka dominates. National governments are

+ **Terms of trade** Relationship between the value added inherent to the goods/ services that a country imports, on one hand, and that it exports, on the other.

Photo 1.1 Jeans are the culmination of many lower-level value chains, including zips, buttons, and pockets (© iStockphoto).

+ Offshore Transactions or actors over which national regulators have no authority.

Thinking point
To what extent can international business be discussed without considering politics?

+ Shareholder value Idea that the purpose of a company is to maximize returns to shareholders.

+ Technology transfer Where technology belonging to one country or company is shared with another under a formal partnership arrangement.

+ Triad/OECD countries World's more affluent and industrialized nations. Triad refers to the three regions of Western Europe, North America, and Japan/Oceania. The Organization for Economic Cooperation and Development (OECD) is a Paris-based association whose membership is comprised of the world's leading economies.

very aware of this factor and will often take measures to improve their country's competitive position. Such efforts are part of the political environment within which MNEs operate—as are the measures enacted by global bodies (see Chapter 6) to control the actions that states might wish to take in the marketplace. When devising their value chain strategies, companies need to be aware of all relevant political and legislative frameworks, if only because they must obey the laws of the different countries where they will be operating. The problem is that many firms operate today on an **offshore** basis outside a single government's control. Further confusion is caused by the fact that many of the government regulations affecting international business (such as import taxes or export subsidies) vary significantly in time and place. In international business, political considerations are a key aspect of corporate strategizing.

Who benefits from globalization?

One source of political tension in international business is widespread disagreement about the distribution of the costs and benefits associated with this activity. This debate is crucial because of the way it impacts public policy and therefore the general environment. MNEs are affected by political tensions but will in turn also influence the political sphere. Ethical conflicts that arise within a domestic context, such as whether a company exists to maximize **shareholder value** or to serve the wider community, are aggravated when they extend across borders (see Chapter 3). As demonstrated in the statistics below, MNEs play a crucial role in most of the world's national economies, distributing wealth through their capital allocation and **technology transfer** decisions. At the same time, wealth distribution has become increasingly uneven (Milanovic 2005). MNEs representing the interests of the world's more affluent nations, alternatively called **Triad** or **OECD countries**, are blamed by some observers (Scholte 2005) for the problems faced by poorer nations, broadly described as **less developed countries** (LDCs). Inversely, others view globalization as the best hope of ending poverty (Samuelson 2008). Indeed, there is a growing sense that international business, alongside disciplines such as economics, sociology, or political sciences, is a key element of the development trajectories in which many poor countries are engaged (Lévy 2007). As such, it is logical that this book be divided between a 'macro' section describing national frameworks, and a 'micro' section focusing on how companies organize themselves to gain advantage.

Key statistics

International business is very much a living subject, rooted in the relationship between actions and outcomes. For this reason, it is crucial that practitioners and students develop the ability to analyse the basic concepts of this discipline in terms of what happens in the real world. Viewing international business in context means, among other talents, being able to link theory to front-page news.

International trade data

The 2008 credit crunch was devastating to world trade and investment. A complete set of statistics for early 2009 was not yet available by the time of this book's publication. (Go to the Online Resource Centre, extension material 1.1, to learn more about indicative post-crisis performance in a few leading trading nations.) However, the first indications are that trade and FDI had crashed much more quickly than the global economy had as a whole. One noteworthy figure is the 46 per cent fall that Japanese exports recorded between January 2008 and January 2009. A second is the estimation made two months later by the World Trade Organization (WTO), a leading body of global governance (see Chapter 6), that international trade was destined to suffer a 9 per cent fall over the course of 2009—much greater than the 1 or 2 per cent shrinkage that another major organization, the International Monetary Fund (IMF), was predicting for the global economy. This disproportionate fall in cross-border activity is unsurprising, since during a recession national governments tend to provide 'stabilizer' financial resources (paying welfare benefits or running budget deficits) that will be spent mainly on domestic activities like services. At the same time, it is very significant that many if not most economies react to crises by becoming more inwardly focused, at least temporarily. In a sense, the 'de-globalization' fears associated with the crisis of the late 2000s have revealed the limitations of international business.

+ **Less developed countries (LDCs)**
Countries where the industrial base and general level of human welfare do not enable most citizens to achieve a decent living standard. This is an umbrella term covering a vast range of economic, social, and demographic situations, ranging from 'emerging' or 'newly industrialized' countries that are on a clear industrialization trajectory to 'failed states' with very poor growth prospects.

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Nonetheless, longer-term statistics have clearly shown a trend towards increased cross-border activity, and there is every chance that this will resume once the effects of the credit crunch have faded. Arguably it is a poorly designed global financial system that is to blame for the crisis, not international business *per se*. Analytically, there is a clear need to distinguish between open product and service markets, on the one hand, and open capital markets, on the other (see Chapter 14). The two do not necessarily go hand-in-hand, and there is little reason to think that the likely future reregulation of the international banking and finance systems will seriously hamper trade and FDI in other sectors of activity. At the same time, it is also in international managers' interest to keep track of any decisions made regarding the global financial framework at meetings like the April 2000 G20 summit in London. The financial markets may be separate from the product or service markets, but the two spheres do interact.

Figure 1.3 shows how, in the decade preceding the credit crunch, world trade had risen by an annual average of around 5.5 per cent, or about 2 per cent faster than the global economy as a whole. The result of this trend is that international business had become a dominant aspect of many people's lives. Just one generation ago, trade accounted for around 10 per cent of the US **gross domestic product** (GDP); from 25 to 30 per cent of GDP in medium-sized industrial exporting nations such as Germany, France, and Japan; and around 50 per cent of GDP in some smaller open economies like the Netherlands. By 2008, the openness to trade in most of these countries, measured as the sum of imports and exports divided by GDP, had at least doubled (see Figure 5.5). Even more dramatically, in countries such as China, Russia, and India, which for political reasons had engaged in very little trade before the 1990s, the sum total of imports and exports amounted by the late 2000s to between 45 and 65 per cent of GDP. Of course, it could be argued that simply adding imports and exports overstates an economy's degree of openness. Admittedly, this is an inadequate way of accounting for certain situations, like temporary imports of components assembled in final goods destined for export markets. Similarly, in the wake of the 2008 credit crunch, some observers were predicting that, within a few short years, global trade would fall from an early 2008 peak of around two-thirds of global GDP to a more sustainable figure of 40–50 per cent (Munchau 2009). This is still very high, however. Even after the 2008 recession, there is no doubt that international trade will continue to account for a large proportion of all business today—justifying an in-depth study of this topic.

+ **Gross domestic product (GDP)**
Country's income, defined by national consumption ± investment ± government spending ± trade balance.

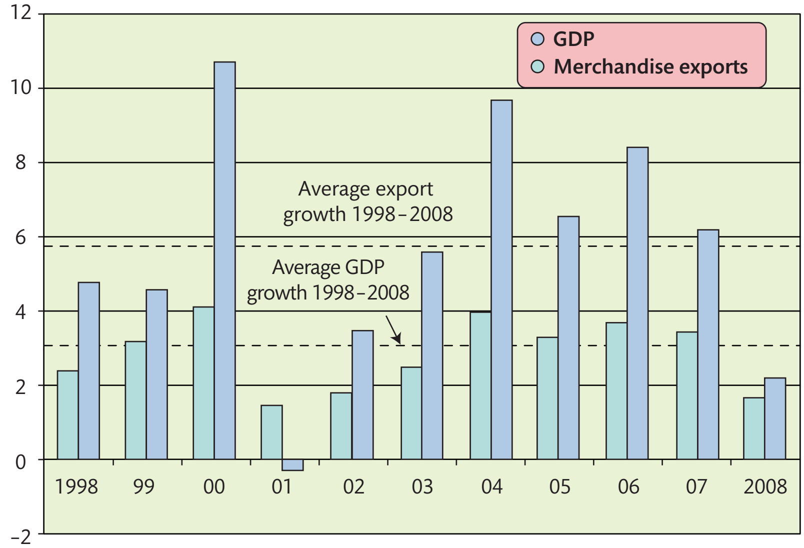

Figure 1.3
Average export growth has been much faster than average economic growth for at least a decade now (WTO 2009).

Within the overall trend towards increased world trade, Figure 1.4 shows variations among different regions of the world. The uneven breakdown of trade has clear implications for the politics of international business.

Figure 1.4 is interesting for both historical and current reasons. First, compared with the global breakdown in 1990, exports from North America and Western Europe have fallen in relative terms, compared to exports from the ex-Soviet Union, Africa, the Middle East, and above all Asia. For the first three regions, the change is largely explained by higher commodity prices. For Asia, it reflects the region's growing role as the world's manufacturing centre. (Go to the Online Resource Centre, extension material 1.2, for statistics concerning some aspects of the breakdown of trade between the primary sector (raw materials and agricultural products), the secondary sector (manufactured goods) and the tertiary sector (services).)

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All these trends are driven largely by MNEs' behaviour—before shaping, in turn, the contexts to which MNEs are forced to adapt.

Further study of Figure 1.4 reveals an enormous and rising gap between US imports and exports. As exemplified by the financial crisis of late 2008, there are serious questions about the sustainability of a global trading system in which the lead economy runs a huge deficit. Certainly this imbalance cannot help but affect different regions' growth prospects in the years to come. Despite the size of its economy, the USA is not even the world's leading exporter at present—Germany holds that title, a remarkable performance given Western Europe's generally lower share of world exports. Conversely, exports from China, the ex-Soviet Union, and India have risen at an impressive pace. For the first two countries, export growth has been accompanied by an equally rapid rise in imports, an unsurprising outcome given the huge development needs that these continent-sized nations face. The shifting geography of international business is one of the key features of the modern era (see Chapter 16). It has an enormous impact on MNEs' structure and the global distribution of capital and will affect managers' decisions at many different levels.

LDCs accounted for 37.6 per cent of total world exports in 2008 but only 33.5 per cent of imports. Some observers might analyse this as a sign that globalization offers poorer nations greater market opportunities, especially considering that, as recently as 1990, LDCs accounted for only around 25 per cent of world trade. This view is encapsulated in the body of theory supporting the idea that, one way or another, all countries stand to gain from international trade (see Chapter 4). Yet there is another side to this argument. First, countries that rely excessively on foreign demand to fuel their development trajectories are most at risk in case of a global slowdown—one example being the particularly devastating

	Value exports 2008	Total global exports 2008 %	Total global exports 1990 %	Value imports 2008	Total global imports 2008 %
World	**16,127**			**16,415**	
North America	**1,757**	**10.9**	**16.6**	**2,584**	**15.7**
USA	1,301			2,166	
South and Central America	**602**	**3.7**	**3.1**	**595**	**3.6**
Mercosur (*)	279			259	
Europe	**6,456**	**40.0**	**49.6**	**6,833**	**41.6**
European Union (27)	5,913			6,268	
Germany	1,465			1,206	
France	609			708	
UK	458			632	
CIS (ex-Soviet Union)	**703**	**4.4**	**1.7**	**493**	**3.0**
Africa	**561**	**3.5**	**3.1**	**466**	**2.8**
Middle East	**1,047**	**6.5**	**4.1**	**575**	**3.5**
Asia	**4,355**	**27.0**	**21.8**	**4,247**	**25.9**
China	1,428			1,133	
Japan	782			762	
India	179			24	
Asian NICs (†)	1,033			1,093	
ASEAN (‡)	990			936	
Developing economies	6,025	37.6		5,494	33.5
Least Developed Economies	176	1.1		157	0.9

(*) Argentina, Brazil, Paraguay, Uruguay
(†) Hong Kong; Republic of Korea; Singapore and Chinese Taipei
(‡) Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam

Figure 1.4
World merchandise trade, by region and selected country, in US$ billion and percentages; exports accounted for FOB (free on board), imports on CIF (cost insurance freight) basis (derived from WTO 2006, 2008).

effects that the 2008–9 crisis had on the exporter nations of South East Asia. Secondly, just as there are great disparities within the developing world between those countries that are emerging and those that are not, even within those countries where overall and average income has risen substantially, some segments of the population have benefited more than others. International business does not affect all parts of every society in the same way. Indeed, as shown by Figure 1.5, in recent years FDI has risen even more quickly than trade. Chapter 7 discusses the various ways in which FDI impacts home and host country populations. Long-term FDI trends, including the potential effects of the 2008 credit crunch (see Online Resource Centre, extension material 1.3), constitutes another key topic in international business.

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Introduction to foreign direct investment

+ Current account
Country's 'balance of trade' (exports minus imports) plus or minus its financial flows from abroad (interest or dividend payments, cash transfers).

+ Outsourcing
Where a company buys supplies that it needs for its products or services from an outside company instead of making them itself.

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Thinking point
What are the chances of de-globalization occurring in the wake of the credit crunch?

Recent FDI data should be handled with care due to statistical categorization problems and because the events of 2001 (the 9/11 attacks on New York's World Trade Center and the bursting of the 'dot.com' stockmarket bubble) made annual FDI flows plunge to levels from which it would take them years to recover. This explains the decision to analyse 2007 using a more distant benchmark like 1997. Excluding adjustments for inflation, the global stock of inward FDI increased more than fourfold over the decade in question, with only minor variations in the breakdown between developed countries (accounting for about two-thirds of all FDI stock) and LDCs. On the other hand, in terms of annual flows of inward investment, LDCs accounted for a mere 27 per cent of total FDI in 2007, down from 39 per cent a decade earlier. These statistics offer further proof of the Triad countries' ongoing domination of international business. They also raise questions about why LDCs have experienced faster growth in trade than in FDI. Chapter 8 will offer some insight into the reasons why MNEs' sense of comfort causes them to enter different foreign markets in different ways.

At the same time, trends explored in Chapter 7 indicate the possibility that FDI flows might even out in the future between the developed and developing worlds. Recent years have witnessed an increase in capital flows to poor countries, especially FDI, which amounted to more than 3 per cent of LDCs' gross domestic product in 2006, versus only 0.2 per cent in the early 1980s (Dorsey 2008). Whereas the developing world had an accumulated **current account** deficit equal to 3 per cent of GDP in the mid-1990s, by 2006 this measure was more or less in balance. The change is a positive one, all the more so because an increasing proportion of flows to LDCs now involve equity transfers (like FDI) as opposed to loans that must be reimbursed later. A major topic in international business discussions (see Online Resource Centre, extension material 1.4) is determining to what extent modern globalization has been helpful or harmful to the world's poorer nations. This is another of the many levels where 'micro' discussions of business strategies link to more political 'macro' analyses of national interest.

Chapter 16 explores several examples of how international managers might incorporate major macro-level trends (such as the growing ecological constraint or the emergence of new economic powers) into their strategic thinking. A notable case in point was the 2008 credit crunch and subsequent recession. Clearly this downturn will have significant effects on cross-border trade and FDI patterns for years to come. What is unknown, however, is exactly what shape these effects will take. Some observers predict that the credit crunch will go so far as to reverse the trends of the previous half-century and spark a return towards renewed protectionism by national governments—that is, 'de-globalization'. Others forecast

Figure 1.5
Major FDI indicators in US$ billion (UNCTAD 2007).

	1997	2007
Global stock of inward FDI	3,502	15,211
Global inward flows	486	1,833
Developed economies		
• Stock of inward FDI	2,351	10,459
• inward flows	285	1,248
• outward flows	400	1,692
(balance)	(–115)	(–444)
Developing economies		
• Stock of inward FDI	1,122	4,248
• inward flows	191	500
• outward flows	74	253
(balance)	(+117)	(+247)

that the recession will force companies to accelerate their cost-cutting efforts, renewing the decades-old trend towards international **outsourcing**. The only thing that is clear is that international business cannot be analysed in isolation from broader circumstances and must therefore always be studied in context.

Case Study 1.2

The *Fortune* Global 500

Fortune, an American business magazine that has been ranking the largest US corporations for more than fifty years, started a similar listing for multinational enterprises in 2005 (see Figure 1.6). In the years following the Second World War, the US economy dominated the rest of the world to such an extent that domestic performance was considered sufficient in and of itself. One sign of the rise of globalization is the central role that foreign markets now play in most large corporations' outlook. Fewer and fewer companies nowadays are isolated behind national borders.

Within a few short decades, Walmart grew from this small store in Bentonville (Arkansas) to become the biggest MNE in the world (reproduced with kind permission of Walmart).

Rank	Company (Headquarters)	Main sector	Revenues	Profits
1	Walmart (USA)	Retail	378.8	12.7
2	Exxon Mobil (USA)	Oil refining	372.8	40.6
3	Royal Dutch Shell (UK)	Oil refining	355.8	31.3
4	BP (UK)	Oil refining	291.4	20.8
5	Toyota Motor (Japan)	Automobile	230.2	15.0
6	Chevron (USA)	Automobile	210.8	18.7

Figure 1.6
World's twenty leading MNEs in 2008, by sector; data in US$ billion (*Fortune* 2008).

Figure 1.6
(continued)

Rank	Company (Headquarters)	Main sector	Revenues	Profits
7	ING Group (Netherlands)	Banking	201.5	12.6
8	Total (France)	Oil refining	187.3	18.0
9	General Motors (USA)	Automobile	182.3	–38.7
10	ConocoPhillips (USA)	Oil refining	178.6	11.9
11	Daimler (Germany)	Automobile	177.2	5.4
12	General Electric (USA)	Electronics	176.7	22.2
13	Ford Motor (USA)	Automobile	172.5	-2.7
14	Fortis (Belgium/ Netherlands)	Banking	164.9	5.5
15	Axa (France)	Insurance	162.8	7.8
16	Sinopec (China)	Oil refining	159.3	4.2
17	Citigroup (USA)	Banking	159.2	3.6
18	Volkswagen (Germany)	Automobile	149.1	5.6
19	Dexia Group (Belgium)	Banking	147.7	3.5
20	HSBC Holdings (UK)	Banking	145.5	19.1

+ **Economies of scale** When a company increases output using the same equipment, its per unit production costs fall.

The *Fortune* list of the world's 500 largest MNEs is notable in this respect because of the domination of just a few sectors. The sector with the largest number of representatives is banking, followed by the oil-refining and automotive sectors, followed at a distance by food/drug retailers, telecommunications, insurance, and electronics. Different factors explain the rise of global MNEs in these sectors. First and foremost has been firms' perceived need to consolidate their international operations—that is, to merge with rivals in order to achieve **economies of scale** and gain competitive advantage. There is also the fact that different paradigms dominate different sectors of activity, with more cultural fields like food or clothing tending to emphasize national differentiation, whereas hi-tech fields focus more on the efficiency of global operations (see the discussion of MNEs' 'push' or 'pull' orientations in Chapter 9). It is important to remember that international business is not a science but involves trying to understand managers' highly informed yet ultimately subjective appreciation of their circumstances. Lastly, there is the fact that the relative importance of different sectors will vary over time. For instance, the 2008 credit crunch was particularly damaging to companies in the banking sector, but also to airliners, because of the general fall in consumer spending on leisure pursuits. There is every chance that in years to come, the number of MNEs from sectors like these will diminish, replaced by firms from new growth areas like clean technology.

The *Fortune* rankings are also interesting for the information they offer on which countries host the most MNE headquarters. As Figure 1.7 shows, since the magazine started compiling figures worldwide in 2005, the share of US and Japanese companies in the Global 500 has fallen, whereas companies from the Far East have increased their representation.

	Number of *Fortune* 500 MNE headquarters in 2005	Number of *Fortune* 500 MNE headquarters in 2008
USA	176	153
Japan	81	64
France	39	39
Germany	37	37
UK	35	34
China	16	29
South Korea	11	15

Figure 1.7
Number of *Fortune* 500 companies with headquarters in world's seven leading home countries, 2005 and 2008 (*Fortune* 2008).

This is partially the result of currency movements—the US dollar declined over the period in question, reducing on paper the size of companies whose accounts are in dollars. Above all, it reflects a shift in global economic power. Without underestimating the ongoing strength of the US and indeed the Japanese and European economies, companies from newly industrialized Asian economies are now big players on the international business scene.

Thinking point
Can MNEs be criticized for becoming 'too big'?

Some observers would point to this trend as indicative of a world in which power is starting to spread. Others might emphasize the fact that the vast majority of the biggest MNEs hail from OECD countries. Indeed, with most high tech production activities also situated in the developed world, global economic power is still divided very unevenly (Mann 2004). MNEs' role in aggravating or reducing income inequalities, on a national but also a global scale, is another major topic of debate in international business.

Section II: The international business framework

A range of motivations, largely discussed in Chapters 8 and 9, explains why and where companies operate internationally. Some reasons for going abroad are timeless in so far as they involve strategic thinking unrelated to the circumstances that a company faces at a given moment in time. Others are more specific and involve corporate attempts to respond to a temporary context (see Chapter 5). This section offers an overview of both general and time-specific rationales for international business.

Activity drivers

Some of the motivations for international business are 'micro' in nature and mainly relate to firms' profit-seeking initiatives and strategic intent. Others involve companies' reactions to external 'macro' trends such as political, governmental, macro-economic, and socio-cultural factors over which they have little control (Yip 1989). Of course, 'micro' and 'macro' motivations are often interrelated. One example of this linkage can be found in the corporate philosophy of **internalization**. This is the idea that, when markets function poorly (for example, where market participants do not receive a fair reward for their efforts), companies may wish to run their international value chain operations themselves, if only because they wish to maintain in-house any knowledge that they may possess (Buckley and Casson 1976). In this view, firms will not need external partners to lead their internationalization drive as long as they have high-quality managers capable of assuming responsibilities abroad, and as long as the host countries are not too different from the ones to which the company and its managers are accustomed. This is a case where international business springs from the interface between a company's internal attributes (managers' qualities) and the characteristics (foreignness and/or market mechanisms) of the host

+ Internalization
When a company decides to run a particular function itself (using its own employees) instead of delegating it to an external partner.

Figure 1.8
Summary of main factors driving international business today.

Internal drivers

- Expand sales
- Leverage existing competencies
- Use extra capacities
- Spread risks
- Avoid saturation
- Internalize competencies
- Acquire resources
- Access more efficient inputs

External drivers

- Technology
- Liberalized regulatory framework
- Free trade friendly institutions
- Global competitive paradigm
- Deregulated finance

country where it is hoping to move. Another example of the interconnection between some micro- and macro-drivers of international business is when an MNE calculates that the costs of going abroad are lower than the potential gains it might achieve by operating in a regulatory, labour, or tax system where it is well placed to put pressure on the government (Ietto-Gillies 2003). This is because a company's cross-border success will depend not only on how suitable its behaviour is to the market(s) where it is operating (Porter 1986) but also on how effectively it deals with non-business actors such as politicians or regulators. In short, separating micro- and macro-drivers of international business may be a useful categorization (see Figure 1.8) but it is necessarily an artificial one.

Internal drivers of international business

Companies often operate outside their borders because they are in a sector shaped by international rather than domestic factors. At the same time, it is rare to find companies launched as multinationals from the very outset. The vast majority of MNEs throughout history—with the exception of 'born-globals' (see Chapter 9)—have started in their home markets and then moved abroad, expanding downstream to increase sales, upstream to acquire resources, or in both directions to diversify risk. Each of these actions is based on a different logic.

Expand sales

+ **Leverage**
Organizing operations in a way that maximizes output without increasing inputs.

Once a firm has built a system allowing it to produce and market a product or service efficiently, it will usually want to **leverage** this competency by selling the finished good, with or without modification, into a new market. Thus, on the downstream side, the expansion of sales is the main driver of international business. There are countless examples of this rationale being put to use. For instance, Dutch vegetable farmers have developed the greenhouse technology to grow tomatoes and peppers even during cold North European winters. Because consumer demand for these products from neighbouring countries such as Germany and the UK remains strong all year long, doing business across borders is a natural step for Dutch agribusiness companies like The Greenery, which sources fresh produce and sells it to foreign retailers. A related example is the trade between Japan, a dynamic but

Photo 1.2
Dutch greenhouses have the capacity to supply most of the tomatoes found in Northern Europe during wintertime (The Greenery; Photographer: Joop van Reeken Studio).

mineral poor industrial giant whose factories require enormous amounts of raw materials, and Australia, which has an abundance of minerals as well as an industrial sector capable of refining ore (like bauxite) into usable production inputs (like aluminium). For Australian mining or refining companies, exporting to Japan is a logical extension of what started out as a domestic activity. A third example from the service sector is the way that huge international banks such as Citigroup in New York or Barclays in London leverage their expensive trading infrastructure to sell financial products to customers located outside their national borders. Expanding sales worldwide is a quick way of paying for the enormous costs that they incurred building their trading rooms in the first place. Lastly, cross-border sales can also be a natural move for SMEs operating in sectors that are by their very nature international in scope. One example is IdeaCarbon, a UK-based consultancy that offers advice on carbon finance worldwide and which in 2008 signed a carbon instrument co-development agreement with India's MCX exchange. In all these instances, international business is as relevant to the company's mission as the work that it does in its home market. This is especially true when the company is looking to move into a foreign country that is similar in political, economic, and/or cultural terms, not to mention close geographically. Without minimizing the real differences that exist between the USA and Canada, when McDonald's first began expanding across America, setting up outlets across its northern border must have seemed a relatively easy step. The skills developed selling in one country can sometimes be transplanted seamlessly to another.

Thinking point
To what extent is international business an extension abroad of the competencies that a firm has developed at home?

There are also strategic reasons why companies organize their commercial functions to embrace international sales as a matter of course. As mentioned above, a basic principle of modern production is that selling large volumes is beneficial because it creates economies of scale. In a similar vein, the greater the experience that a company has acquired in producing something, the better it becomes at this activity. This is because it appropriates skills that will allow it to achieve productivity gains. As a result, many companies size their production operations to obtain **critical mass**. To justify these investments and avoid surplus capacities, they often need to sell more than they would if they were simply serving domestic customers. This is especially true if the firm comes from a small country. For example, discount airliner Ryanair would have been at a disadvantage using its Dublin home as its only hub. With so many more passengers travelling through the UK, it made sense for this Irish company to run its main

+ Critical mass
Minimum threshold beyond which positive, size-related benefits arise.

Photo 1.3
Ireland's sparse population meant that local carrier Ryanair needed to look overseas, to London Stansted Airport, for a hub large enough to justify its large-scale operations (© iStockphoto).

operations out of London Stansted Airport, which is, after all, a foreign location. Another way of looking at the size factor is in financial terms. In the mid-2000s, the cost of building a new automotive factory was roughly $1 billion. To have any hope of recovering such a large upfront investment, a car company would have to make sure that its new plant produced enough cars to justify the expense. This is not possible if the plant is located either in a small country (Luxembourg does not have a car plant serving its domestic market alone, for instance) or in one where demand is already saturated due to competition. In both cases, the production scale must be international or else the investment becomes impracticable.

Risk diversification

Another strategic driver of international business is the desire to spread risk by working in more than one country at a time. In and of itself, spreading risk is generally seen as a safe business principle, in part because it helps to avoid over-dependence on a single location or market. One way of looking at this is from an upstream, production perspective. If a firm had all its industrial assets in northern Turkey and another terrible earthquake were to hit the region, its chances of continuing manufacturing operations would be worse than if it also had plants in zones not affected by the earthquake. That is why so many firms have disaster plans allowing them to continue functioning in case a catastrophe affects one of their main locations. The same logic can be applied on the downstream, sales side. A company that is selling into only one market runs the risk that the market might collapse for whatever reason (natural disaster, bad policy, war) without there being any other customers to compensate for lost sales. Any firm whose entire business revolved around exports to Iraq at the time of the 2003 invasion would, for instance, have had difficulties surviving. The adversity that a company experiences in one location has less of an effect when it has interests in many others.

Spreading risk through international operations can be done in different ways. Commercially, there is something called the 'product life cycle' (PLC), which from an international marketing perspective is the idea that a product or service that is on an upward trend in some countries may be in decline elsewhere (see Chapter 12). Clearly, it is advantageous for firms to sell goods in markets where demand is on the rise, since they will be able to command higher prices. One example from the 1970s and 1980s is the way that jeans were so much more expensive in Western Europe, where they were new and fashionable, than in California, where they had long been a commodity product. The PLC variation enabled San Francisco firm Levi Strauss to offset lower revenues in its home market via exports to Europe. International business can be used to diversify other risks as well. Foreign sales can offset the foreign exchange risk of accumulating revenues (or liabilities) in just one currency (see Chapter 13). In a sense and despite the challenges of operating in a foreign environment, diversification means that international business can actually be a way for a company to reduce risk.

Thinking point

Is international risk automatically more dangerous than domestic risk?

Acquire inputs

The final internal driver of international business is the acquisition of resources (materials and labour but also capital and technology) used during a firm's production process. Sometimes this involves inputs that are unavailable at home. One example is the way that non-oil-producing countries such as Japan, Germany, and France must look abroad to source this commodity. At other times, the cost of an input might be so much lower overseas that a company would be at a competitive disadvantage if, unlike its rivals, it did not source the factor where it can be acquired most cheaply. As discussed in Chapter 8, this can be done via FDI or trade. UK vacuum cleaner manufacturer Dyson provides one example of a firm engaging in FDI to reduce input costs. Portrayed as the symbol of the rebirth of British manufacturing in the 1990s, by 2002 Dyson had decided that its new priority was to lower its cost base. Accordingly, it moved almost all its production activities to Malaysia, where workers' wages were a fraction of those paid to British production staff. As for reducing input costs through trade, the solar energy business is a good case in point. Builders worldwide seeking to enter this fast-growing sector need to source solar panels competitively. However, few countries can make these components as cheaply as Germany, where SMEs like Ritter Solar have already achieved critical mass. Thus, it is in the interest of energy system installers worldwide to import from Germany if they want to acquire resources cheaply. In short, international business is often driven by firms focusing more on the advantages inherent to a given production location and less on whether this site is in their country of origin or not.

External drivers of international business

Technology

It is not always easy to determine which drivers a company can control, and which it cannot. One case in point is technology, a key factor in today's global economy. This is an umbrella term that refers to companies' internal innovation efforts (see Chapter 11's section on knowledge management) but also to the technological advances that a particular society achieves as a whole. Thus, technology affects the international business environment at many different levels. On the upstream side, for instance, improved telecommunications enable companies to stretch their value chains to distant locations offering competitive advantages. One example is when hospitals in the West use remote diagnostics facilities to get advice from doctors located, for instance, in India. Out of a service that was once as localized as medical treatment is, modern technology has created an opportunity for an international work organization. The same applies to downstream activities, for instance, where company–customer relationships extend worldwide due to technological advances like the Internet. When consumers worldwide purchase their books through Amazon instead of at their local bookstore, they are cementing technology's role as a key organizing principle in international business. Indeed, given the positive impact that technology-related transportation improvements have traditionally had on trade, it can be argued that technology is one of the main causes of today's shrinking world. It is rare that a community chooses to remain completely isolated once the means exist for it to interact with other communities. Google's rapid rise in China, despite the obstacles raised by the Beijing government, is a good case in point. Before China had any exposure to Western consumption goods (or ideas), its population was much less focused on such items. People's outlooks and desires often change when they see how foreigners live. Cross-border comparison has always been a significant driver of international business.

Regulatory framework

+ Barriers to entry Regulatory, competitive, financial, and other obstacles that make it difficult for a firm to enter a particular market.

However, just because a technology exists enabling something to happen does not mean that it will necessarily occur—even if it were to create an advantage for someone. For international business to happen, there must be a general regulatory framework enabling it. After all, the leading responsibility of any national government is to ensure the well-being of its population in the face of danger from abroad. The main threat is clearly war, but, in so far as foreign economic competition can be damaging to certain parts of a local economy (even as it benefits others), states will also come to a judgement as to what kind of international business they find acceptable. Chapters 4 and 5 look at the issue of state intervention in greater depth. For the moment, it is worth stating that the general paradigm in many countries since the early 1980s has been to accept and indeed promote cross-border flows by allowing foreign actors to enter domestic marketplaces. The effect of this deregulation (also known as 'liberalization') trend has been to reduce **barriers to entry**, making it easier for companies to operate on an international scale.

Thinking point
What would international business be like in a protectionist world?

A liberalization philosophy has affected the trade and FDI regulations of most if not all of the world's nation-states, but, as Chapter 6 details, it has also led to the creation of a global framework that is conducive to international business. One aspect is the rise of regional trading arrangements like the European Union (EU). These are groups of neighbouring countries that have signed agreements enabling easier access to one another's markets. Their degree of integration can vary, but in general such arrangements promote free trade among members. The same philosophy has also led to the creation of trade-friendly international institutions like the WTO, whose laws create a framework in which countries are positively discouraged from adopting isolationist policies. The idea is to create a world where cross-border transactions are no longer considered unusual.

Global competition

In terms of corporate strategy, a whole new vision has arisen regarding what it means to compete. Before the arrival of a world of free trade, companies would position themselves in terms of local and/or national rivals, competing for a share of their domestic markets. Today, with increasingly penetrable national borders, economic rivals might come from anywhere, deriving competitive advantages derived from whatever experiences they have accumulated at home or abroad. This means that some companies that have worked very hard over the years to improve productivity or quality, and that would be very competitive in a purely domestic framework, might suddenly lose market share because of the arrival of hyper-competitive foreign companies. For example, where Bordeaux wineries used to compete successfully with domestic rivals from France's Burgundy region, they must now face challenges from New World winemakers from Australia, Chile, and South Africa. With rivals achieving economies of scale because they already operate globally, Bordeaux winemakers can no longer afford to think in domestic terms alone. Furthermore, the profits that global groups make in one market can be used to fund their activities in another, which is why it is sometimes just as important to go abroad specifically to limit rivals' profitability as it is to turn a profit oneself. This explains the outcry when companies, like US aircraft-maker Boeing and its European rival Airbus, suspect one another of receiving different kinds of preferential treatment at home, enabling them to subsidize lower prices to foreign customers, thereby gaining global market share to their rivals' detriment. The new competition involves fighting not just in rivals' home markets but also in markets all across the world—which is why business has become so much tougher in many sectors today.

Thinking point
How meaningful is purely domestic competition nowadays?

The main consequence of the new competitive paradigm is that producers are no longer able to rely on the comfortable positions they used to hold in their domestic markets. Consumers' greater awareness of possible foreign alternatives to domestic products, and their ability to access rival products at competitive prices, has given buyers greater power over sellers. For example, in the mid to late twentieth century, when German consumers could buy their television sets only from local companies AEG Telefunken and Grundig (or Dutch rival Philips), these proud old firms were in a position to sell their high-quality products at a good profit. Once the market began to be flooded with equally good but cheaper Japanese alternatives, the two Germans were forced to compete at a level to which they were unaccustomed. Today both survive only as brand names listed in other firms' product portfolios. Given the partial convergence of consumer behaviour and demand patterns worldwide (see Chapter 12), companies have come to realize that, regardless of how directly or indirectly they operate outside their national borders, international business will affect them at one level or the other. As Chapter 9 discusses, MNEs running worldwide operations increasingly look to integrate their units' management, in a bid for greater coherency (Held et al. 1999). Everyone's playing field has become bigger.

International finance

Corporate finance has also been affected by the trend towards a more globalized world. To source the capital needed to run vast multinational empires, MNEs often have to rely on different funding sources, many of which operate offshore, thus free from domestic controls. The deregulation of the finance industry since the 1980s (see Chapter 14), part of an overall 'liberalization' paradigm, has led to an explosion in cross-border capital flows. Much of this money is free floating—that is, not directly associated with the production of goods and services. This partial separation of finance from real business activity, one of the causes of the 2008 credit crunch, has added to pressures weighing on MNE managers today. On the one hand, financial asset prices are becoming increasingly volatile and difficult to predict, adding to the uncertainty of international business. On the other, whereas many MNEs used to be owned by 'passive shareholders' mainly interested in the safety of their investments, in the new 'shareholder value' paradigm international managers are under pressure to maximize short-term financial returns by running tighter operations and/or taking greater risks. In a similar vein, the deregulation of the world's financial markets means that problems first affecting just one country, like the 2007 subprime crisis in the USA, have become more contagious and are therefore more likely to affect other economies. A more globalized world has advantages but also creates particular challenges.

Challenges and choices

The demanding and constantly evolving nature of modern international business is the final point to be made in this introductory chapter. Some textbooks adopt what seems at times to be a checklist approach to international business, giving readers the impression that they will necessarily succeed in their foreign endeavours if they simply tick certain action boxes. In the opinion of the authors of this book and based on their personal experience and research, this is wrong, and books transmitting such an idea do a great disservice. If readers are led to believe that international business is a mere subcategory of domestic business, they will not develop the varied world view characterizing the vast majority of successful international practitioners. Thinking internationally is something new for many people.

It is true that international business is capable of creating the greatest opportunities for profit maximization—as proven by the fact that most if not all the wealthiest companies (and people) in the world operate on a cross-border basis. At the same time, operating internationally requires an ability to cope with challenges that do not arise at the domestic level. Politically, despite the trend towards more internationalist thinking, resistance to foreign competition for markets, resources, and jobs remains very widespread. Economically, many foreign operations (like technological transfers or global funding) are associated with distinct sets of problems. Socially, there is widespread condemnation of the unequal distribution of globalization's costs and benefits. Environmentally, there is the extra usage of resources and generation of waste caused by the organization of trade over long distances. Last but not least, psychologically there is the obstacle of xenophobia. Despite the authors' personal rejection of this attitude, the academic value of the present book would be undermined if its impact on international business relationships were underplayed. Now, some might argue that globalization stems from (and/or causes) lesser xenophobia. Conversely, others would argue that increased contact with foreigners sparks, at least in certain communities, greater dislike of the outside world (Huntingdon 2002; Barber 2003). If an international business book overestimates the cross-border obstacles that managers face, then at worst it is guilty of advocating excessive caution. If, on the other hand, it underestimates these obstacles, then it is guilty of leaving readers totally unprepared for the situations that they will face in the future. The consequences of the latter error would be much more severe than the former.

For this reason, the chapters in this book will include special sections highlighting different challenges inherent to international business, as well as choices that managers might make to overcome them. Each of these choices—how to allocate resources, target markets and customers, relate to foreign individuals or governments—should be grounded in managers' ability to provide an appropriate response to a specific set of circumstances. To repeat, the fundamental philosophy of this book is that it is more important to help readers learn how to make choices than to dictate to them what choices they should be making.

Chapter Summary

This brief introduction set the scene by identifying the differences between global and international approaches, and asking whether it is more effective to seek a 'one-best-way' approach that can be applied in all circumstances or to develop an ability to respond flexibly to different environments. In both cases, an argument was made in support of the second alternative. This is justified in part by the chapter's statistical analysis of the recent rise in world trade and FDI. Depending on their personal and national interests, people will react in different ways to the presence of foreign companies. Successful international managers will therefore be those whose thinking incorporates a range of views. Business is, after all, a social science.

The second section studied in greater depth the drivers of modern international business, categorizing them as macro-factors external to a firm's internal workings and micro-factors reflecting the policies it chooses to adopt. A distinction was made between factors that might be applicable irrespective of the circumstance and others that are directly linked to modern globalization. The chapter's final section stated the importance for future practitioners of respecting the challenges associated with international business.

Case Study 1.3

What powers Electricité de France?

Nationalized in 1946 by a post-war government seeking to exert state control over a strategic power sector, for a long time Electricité de France (EDF) enjoyed a monopoly status in France. This protection from market competition had several consequences, the main one being that EDF could always count on state support and therefore did not have to worry about funding and profitability constraints to the same extent as a private company would have done. As such, it was in a position to act quickly on any strategic opportunity it saw, whether or not the venture took a long time to turn a profit. In this atmosphere, EDF executives were quick to develop major ambitions, largely because they had a shareholder (the French state) with pockets that were deep enough to fund whatever expansion plans they concocted. By the 1980s, however, many observers were criticizing the company's structure as bloated and mismanaged, doubting whether support for EDF constituted a good use of French taxpayers' funds. Alongside this, as the European Union (EU) moved towards a Single Market in the 1990s and began promoting deregulation, France's politicians came under increasing pressure to privatize EDF and open up the domestic market to foreign competition. It is true that the French state dragged its feet in this respect, and at year end 2007 it still maintained a 84.8 per cent interest in EDF. There was also some reluctance to open up the French domestic utilities market as widely as the EU would have liked. Nevertheless, sensing changes in the competitive environment, EDF executives turned their attention to the expansion possibilities that international business offers. Their actions exemplify some of the approaches found in international business today.

Clearly, an imbalance exists when a company from a country like France, characterized by a particularly state-oriented business culture, engages with companies from countries like Britain, where the state has traditionally had much less of a presence in the economy. During 1999–2002, EDF embarked on acquisitions of £6.2 billion in the UK, merging companies such as London Electricity, the Southwest Electricity Board, and SEEBOARD to form EDF Energy, which became one of the UK's largest utilities. Under normal circumstances, a company with such enormous debts as EDF was carrying at the time would never have been able to fund this kind of programme. Clearly the investment was made possible only because EDF had political support for its projects back in France, and because it lacked any real opposition in the UK. The company's strategic interest was to establish a foothold in the UK, where there were plans to increase national capacities for producing nuclear power—an area where EDF benefited from a great deal of technological competence, largely because of the years of research assistance it had received from the French government. In September 2008 this strategy culminated in EDF's £12.4 billion acquisition of British Energy, whose power stations were responsible for more than 20 per cent of all electricity generated in the UK. Dominating a neighbour's domestic energy market in this way was quite an achievement for a state sector company.

Not all foreign markets were so welcoming to the French utilities giant, however. In early 2008, for instance, EDF expressed an interest in taking over the Spanish energy firm Iberdrola. The target company reacted by lodging several complaints against EDF with the European Union, specifically because the French predator's quasi-government status would have given it an unfair advantage in the event of a stockmarket battle. This was

The UK's need to replace existing nuclear plants has attracted the attention of foreign utilities like EDF (Photodisc).

not the first time that a company sought legal protection against a foreign competitor accused of not respecting the rules of capitalism, and it probably will not be the last. It is notable that EDF's main interest in Iberdrola related to the Spanish company's position as world leader in the growing wind power sector. Whereas growth in the UK had been aimed at leveraging EDF's existing technologies, growth in Spain was aimed at accessing new ones.

This also seemed to be EDF's motivation when it signed a photovoltaic solar panel supply master agreement in 2008 with a privately owned Californian 'start-up' called Nanosolar. The potential scope of the American deal was very different from the Spanish one, however, if only because of Nanosolar's ownership structure. Whereas publicly listed firms are increasingly being required by demanding shareholders to maximize short-term returns, unlisted firms are often given more time by their owners to develop a new technology. This explains the success of the venture capital model implemented by many computer companies that started in Silicon Valley—where Nanosolar, coincidentally enough, was also located. EDF may have wanted to purchase Nanosolar much like it acquired British Energy and tried to buy Iberdrola, but this option was never really possible. Instead, the French company had to resort to a more modest outsourcing and cooperation arrangement. These activities would be added to the portfolio that EDF lodged in a new subsidiary called 'EDF Energies Nouvelles'. By definition, the French utilities giant was committed to raising its profile in the global market for renewable energies. The diverse nature of the international business environment meant that it would need different methods to fulfil this commitment.

Case study questions

1. Electricité de France is virtually a state-owned company. What other examples exist of public sector organizations pursuing a direct interest in international business?
2. How does the French business culture vary from the British, Spanish, or American? What about your own country of origin?
3. What are some of the reasons motivating companies to engage in international business?

Discussion questions

1. Is globalization inevitable?
2. Is nationality an important factor in the way people do business?
3. To what extent is international business beneficial to wealthy and/or poor countries?
4. How would international business work if national regulatory environments were stricter?
5. To what extent is international business based on objective science versus human psychology?

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Further research

Mattoo, A., Stern, R. M., and Zanini, G. (2007). *A Handbook of International Trade in Services*. Oxford: Oxford University Press.

Propelled by ongoing improvements in information technologies, the service sector has become a crucial part of international business. Companies working out of central locations are increasingly in a position to offer foreign customers a variety of services, ranging from computer advice to insurance policies, banking, and tourism. Furthermore, many cross-border investments involve projects whose industrial element is associated with the local delivery of a service. This is particularly true in sectors like telecommunications, transportation, or energy, many of which used to be at least partially nationalized but are now subject to the rules of international competition. Given the expansion in other international service sectors such as education and medical diagnostics, it is no surprise that international trade and FDI in services have outpaced the total growth in goods since the mid-1990s.

At the same time, the investments and individuals that providing cross-border services still face many barriers to entry. Unlike the trade in goods, which really start to affect an economy only once products have crossed the national border, services usually materialize at the very heart of a society, if only because of the growing number of individuals employed in many economies in service-sector activities. This explains ongoing resistance in some corners to the liberalization of services. All in all, trade and investment in services have become a very specific and interesting subcategory of international business.

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