CHAPTER 8

IMPORTING, EXPORTING, AND SOURCING

SUMMARY

A. A company's first business dealings outside the home country often take the form of exporting or importing. Companies should recognize the difference between **export marketing** and **export selling**. By attending **trade shows** and participating in **trade missions**, company personnel can learn a great deal about new markets.

B. Governments use a variety of programs to support exports, including tax incentives, subsidies, and export assistance. Governments also discourage imports with a combination of **tariffs** and **nontariff barriers**.

C. A **quota** is one example of a nontariff barrier. Export-related policy issues include the status of **foreign sales corporations** (FSCs) in the United States, Europe's **Common Agricultural Policy** (CAP), and **subsidies**. Governments establish **free trade zones** and **special economic zones** to encourage investment.

D. The **Harmonized Tariff System** (HTS) has been adopted by most countries that are actively involved in export-import trade. **Single-column tariffs** are the simplest type of tariffs; **two-column tariffs** include special rates such as those available to countries with **normal trade relations** (NTR) status. Governments can also impose special types of duties including **antidumping duties,** which are imposed on products whose prices government officials deem too low and **countervailing duties,** which are designed to offset government subsidies.

E. Key participants in the export-import process include **foreign purchasing agents**, **export brokers**, **export merchants**, **export management companies**, **manufacturers' export agents**, **export distributors**, **export commission representatives**, **cooperative exporters**, and **freight forwarders**.

F. A number of export-import payment methods are available. A transaction begins with the issue of a **pro forma invoice** or some other formal document. A basic payment instrument is the **letter of credit** (**L/C**) that assures payment from the buyer's bank. **Documentary collection** is an option that involves either using a **sight draft** or a **time draft**. Sales may also be made using cash with order (CWO), and sales on open account or a consignment agreement.

G. Exporting and importing are directly related to management's **sourcing decisions**. Concern is mounting in developed countries about job losses linked to **outsourcing** jobs, both skilled and unskilled, to low-wage countries. A number of factors determine whether

a company makes or buys the products it markets as well as *where* it makes or buys those products.

LEARNING OBJECTIVES

8-1 Compare and contrast export selling and export marketing.

8-2 Identify the stages a company goes through, and the problems it is likely to encounter, as it gains experience as an exporter.

8-3 Describe the various national policies that pertain to exports and imports.

8-4 Explain the structure of the Harmonized Tariff System.

8-5 Describe the various organizations that participate in the export process.

8-6 Identify home-country export organization considerations.

8-7 Identify market-country export organization considerations.

8-8 Discuss the various payment methods that are typically used in trade financing.

8-9 Identify the factors that global marketers consider when making sourcing decisions.

DISCUSSION QUESTIONS

8-1. What is the difference between export marketing and export selling?

Export selling basically presents an extension strategy whereby products are offered for sale outside the home country without adaptation. The mindset of export selling is, "Here's the product, take it or leave it." One symptom of export selling would be providing sales literature in the home country language only. Export marketing, by contrast represents willingness to adapt one or more of the marketing mix elements as required by the characteristics of the target market.

8-2. Describe the stages a company typically goes through as it learns about exporting.

The chapter outlines seven stages:

1. The firm is unwilling to export.
2. The firm fills unsolicited export orders but does not pursue unsolicited orders.
3. The firm explores the feasibility of exporting.
4. The firm exports to one or more markets on a trial basis.
5. The firm is an experienced exporter to one or more markets.
6. The firm pursues country- or region-focused marketing based on certain criteria (e.g., all countries where English).

7. The firm evaluates global market potential before screening for the "best" target markets to include in its marketing strategy and plan.

8-3. Governments often pursue policies that promote exports while limiting imports. What are some of those policies?

First and foremost, governments can impose duties on imports. In addition, most governments utilize nontariff trade barriers that serve as deterrents or obstacles to imports from other countries. NTBS include quotas, discriminatory procurement policies, restrictive customs procedures, arbitrary monetary policies, and restrictive regulations.

8-4. What are the various types of duties that export marketers should be aware of?

Ad valorem duties are expressed as a percentage of the customs value of particular goods. For example, China has imposed a 60 percent duty pm 35mm imports; the U.S. imposes a 25 percent duty on light trucks imported from Japan.

Specific duties are expressed as a specific amount (in the importing country's currency) per some unit of measurement. For example, prior to NAFTA, the specific duty on Mexican tomato imports into the United States was 1.4 cents per pound; after NAFTA passed, the duty was lowered to 1 cent per pound.

Antidumping duties are imposed on products from producers that have set export prices at unfairly low prices. Pasta makers in Italy and Turkey were assessed antidumping duties after the International Trade Administration ruled the companies were selling pasta below fair value and injuring American producers.

Countervailing duties are designed to offset government subsidies in the exporting country.

8-5. How did the recent economic crisis affect financing for global trade?

The global financial crisis undermined the ability of firms of all sizes to get the financing they depend on for trade. Compounding the problem was the fact that trade finance is drying up in key emerging markets.

8-6. What is the difference between an L/C and other forms of export-import financing? Why do sellers often require letters of credit in international transactions?

A letter of credit constitutes an agreement whereby an importer's bank assumes the obligation of payment on behalf of the importer. The seller is assured of payment because the bank guarantees payment as long as the seller complies with the terms in the L/C. A documentary collection is a negotiable bill of exchange that can be transferred from one party to another. When a bill of exchange is used, banks are involved but do not bear financial risk. Other forms of payment include cash in advance (usually via wire transfer), sales on open account, and sales on a consignment basis.

OVERVIEW

This chapter provides an overview of import–export basics. We begin by explaining the difference between export selling and export marketing. Next up is a survey of organizational export activities. An examination of national policies that support exports and/or discourage imports follows. After a discussion of tariff systems, we introduce key export participants. The next section provides an overview of organizational design issues as they pertain to exporting.

The chapter ends with a discussion of outsourcing, a topic that is becoming increasingly important as companies in many parts of the world cut costs by shifting both blue-collar and white-collar work to nations with low-wage workforces.

ANNOTATED LECTURE/OUTLINE

EXPORT SELLING AND EXPORT MARKETING: A COMPARISON

- ✓ **(Learning Objective #1)**

To better understand importing and exporting, it is important to distinguish between **export selling** and **export marketing**.

Export selling does <u>not</u> involve tailoring the product, the price, or the promotional material to suit the requirements of global markets. The only marketing mix element that differs is the "place"; that is, the country where the product is sold.

Export marketing targets the customer in the context of the total market environment. The export marketer does not simply take the domestic product "as is" and sell it to international customers. To the export marketer, the product offered in the home market represents a starting point. It is modified as needed to meet the preferences of international target markets.

Export marketing is the integrated marketing of goods and services that are destined for customers in international markets. Export marketing requires:

1. An understanding of the target market environment
2. The use of marketing research and identification of market potential
3. Decisions concerning product design, pricing, distribution and channels, advertising, and communications - the marketing mix.

After the research effort has zeroed in on potential markets, there is no substitute for a personal visit to size up the market firsthand and begin the development of an actual export-marketing program.

A market visit should accomplish several things. First, it should confirm (or contradict) assumptions and research regarding market potential. Second, the company representative should gather the additional data necessary to reach the final go or no-go decision regarding an export-marketing program

For example, an export manager or international marketing manager may have a list of potential distributors provided by the U.S. Department of Commerce. He or she may have corresponded with distributors on the list and formed some tentative idea of whether they meet the company's international criteria. It is difficult to negotiate a suitable arrangement with international distributors without actually meeting face-to-face to allow each side to appraise the capabilities and character of the other party. Third, a visit to the export market should enable the company representative to develop a marketing plan in cooperation with the local agent or distributor. This plan should cover the necessary product modifications, pricing, advertising and promotion expenditures, and a distribution plan. If the plan calls for investment, agreement on the allocation of costs must also be reached.

One way to visit a potential market is through a **trade show** or a state- or federally sponsored **trade mission**. Each year hundreds of trade fairs, usually organized around a product category or industry, are held in major markets. (Exhibit 8-2)

Perhaps most important, attending a trade show enables company representatives to learn a great deal about competitors' technology, pricing, and depth of market penetration.

ORGANIZATIONAL EXPORT ACTIVITIES
✓ **(Learning Objective #2)**

Exporting is becoming increasingly important as companies in all parts of the world step up their efforts to supply and service markets outside their national boundaries. Research has shown that exporting is essentially a developmental process that can be divided into the following distinct stages:

1. The firm is unwilling to export; it will not even fill an unsolicited export order. This may be due to perceived lack of time ("too busy to fill the order") or to apathy or ignorance.
2. The firm fills unsolicited export orders but does not pursue unsolicited orders. Such a firm is an export seller.
3. The firm explores the feasibility of exporting (this stage may bypass Stage 2).
4. The firm exports to one or more markets on a trial basis.
5. The firm is an experienced exporter to one or more markets.
6. After this success, the firm pursues country- or region-focused marketing based on certain criteria (e.g., all countries where English is spoken or all countries where it is not necessary to transport by water).
7. The firm evaluates global market potential before screening for the "best" target markets to include in its marketing strategy and plan. *All* markets—domestic and international—are regarded as equally worthy of consideration.

However, *commitment* is the most important aspect of a company's international orientation. Before a firm can reach Stage 4, it must receive and respond to unsolicited export orders. The quality and dynamism of management are important factors that can lead to such orders.

One study noted that export procedural expertise and sufficient corporate resources are required for successful exporting. An interesting finding was that even the most experienced exporters express lack of confidence in their knowledge about shipping arrangements, payment procedures, and regulations. The same study also showed that, although profitability is an important expected benefit of exporting, other advantages include increased flexibility and resiliency and improved ability to deal with sales fluctuations in the home market.

Although research generally supports the proposition that the probability of being an exporter increases with firm size, it is less clear that export intensity—that is, the ratio of export sales to total sales—is positively correlated with firm size. Table 8-1 lists some of the export-related problems that a company typically faces.

NATIONAL POLICIES GOVERNING EXPORTS AND IMPORTS

- ✓ **(Learning Objective #3)**

It is hard to overstate the impact of exporting and importing on the world's national economies.

In 1997, for example, total imports of goods and services by the United States passed the $1 trillion mark for the first time; in 2017, the combined total was $2.9 trillion. European Union imports, counting both intra-EU trade and trade with non-EU partners, totaled more than $3 trillion.

Trends in both exports and imports reflect China's pace-setting economic growth in the Asia-Pacific region. Exports from China have grown significantly; they are growing even faster now that China has joined the WTO. As shown in Table 8-2, Chinese apparel exports surpass those of other countries by a wide margin.

One word can summarize national policies toward exports and imports: contradictory.

For centuries, nations have combined two opposing policy attitudes toward the movement of goods across national boundaries. On the one hand, nations directly encourage exports; on the other hand, they generally restrict the flow of imports.

Government Programs that Support Exports

To see the economic boost that can come from a government-encouraged export strategy, consider Japan, Singapore, South Korea, and the so-called Greater-China or "China triangle" market, which includes Taiwan, Hong Kong, and the People's Republic of China. After recovering from the destruction of its economy during World War II, Japan became an economic superpower as a direct result of export strategies devised by the Ministry for International Trade and Industry (MITI).

The four tigers – Singapore, South Korea, Taiwan, and Hong Kong—learned from the Japanese experience and built strong export-based economies of their own.

Although Asia's "economic bubble" burst in 1997 as a result of uncontrolled growth, Japan and the tigers are moving forward in the twenty-first century at a more moderate rate.

Any government concerned with trade deficits or economic development should focus on educating firms about the potential gains from exporting.

Governments commonly use four activities to support and encourage firms that engage in exporting: tax incentives, subsidies, export assistance, and free trade zones.

Tax incentives treat earnings from export activities preferentially either by applying a lower tax rate to earnings from these activities or by refunding taxes already paid on income associated with exporting.

From 1985 until 2000, the major tax incentive for exporters under U.S. law was the **foreign sales corporation** (FSC), through which American exporters could obtain a 15 percent exclusion on earnings from international sales.

However, in 2000, the World Trade Organization ruled that any tax break that was contingent on exports amounted to an illegal subsidy.

Accordingly, the U.S. Congress has set about the task of overhauling the FSC system; failure to do so would entitle the EU to impose up to $4 billion in retaliatory tariffs.

Governments also support export performance by providing outright **subsidies**, which are direct or indirect financial contributions or incentives that benefit producers. Subsidies can severely distort trade patterns when less competitive but subsidized producers displace competitive producers in world markets.

Agricultural subsidies are particularly controversial because, although they protect the interests of farmers in developed countries, they work to the detriment of farmers in developing areas such as Africa and India. The EU has undertaken an overhaul of its **Common Agricultural Policy** (CAP).

Another means of supporting exporters is by extending *governmental assistance* to exporters. Companies can avail themselves of a great deal of government information concerning the location of markets and credit risks. Assistance may also be oriented toward export promotion. Government agencies at various levels often take the lead in setting up trade fairs and trade missions designed to promote sales to foreign customers.

The export/import process often entails red tape and bureaucratic delay, especially in emerging markets such as China and India. In an effort to facilitate exports, countries are designating certain areas as **free trade zones** (FTZ) or **special economic zones** (SEZ). In geographic entities, manufacturers benefit from simplified customs procedures, operational flexibility, and a general environment of relaxed regulations.

Governmental Actions to Discourage Imports and Block Market Access

Measures such as tariffs, import controls, and nontariff barriers are designed to limit the inward flow of goods.

Tariffs can be thought of as the “three Rs” of global business: rules, rate schedules (duties), and regulations of individual countries.

Duties on individual products or services are listed in the schedule of rates (Table 8-3).

One global trade expert defines duties are “taxes that punish individuals for making choices of which their governments disapprove.”

Developed under the auspices of the Customs Cooperation Council (now the World Customs Organization), the **Harmonized Tariff System** (HTS) went into effect in January 1989 and has since been adopted by the majority of trading nations. Under this system, importers and exporters have to determine the correct classification number for a given product or service that will cross borders.

INNOVATION, ENTREPRENEURSHIP, CREATIVE THINKING, AND THE GLOBAL STARTUP
Oscar Farinetti, Eataly

Oscar Farinetti is an entrepreneur. He developed an innovative retail concept, Eataly, and started a company to market it. By applying the basic tools and principles of modern global marketing, Farinetti has achieved remarkable success.

Starting in 2007 with a single location in Turin, Italy, Farinetti now presides over a far-flung global empire of Eataly megastores that celebrate all things Italian. Farinetti has opened more than 25 stores in major cities such as Chicago, Dubai, and New York City.

Eataly gourmet supermarkets, and the restaurants tucked inside them, are helping Italian food producers during Italy’s ongoing recession.

Many observers note that the “Made in Italy” movement got an additional boost from the 2015 World Expo in Milan. The theme of the Expo was “Feeding the Planet. Energy for Life.” Eataly Milan Smeraldo opened months before the Expo itself. Farinetti is optimistic about Italy’s future. “We need to double tourism in Italy, we can double our export of food and agriculture products, we need to open up other industries of fashion, design, industrial manufacturing. And if we manage this we will bring the country to another renaissance.” he says.

In spite of the progress made in simplifying tariff procedures, administering a tariff is an enormous burden. People who work with imports and exports must familiarize themselves with the different classifications and use them accurately. Even a tariff schedule of several thousand items cannot clearly describe every product traded globally.

The introduction of new products and new materials used in manufacturing processes creates new problems. Often, determining the duty rate on a particular article requires assessing how the item is used or determining its main component material. Two or more alternative classifications may have to be considered. A product's classification can make a substantial difference in the duty applied.

One of the most controversial aspects of U.S. Donald Trump's "America First" policy was his decision to impose tariffs on imports of steel and aluminum (See Exhibit 8-4). Opponents of this policy – including trade partners and some U.S. industry leaders – argue that the tariffs will negatively the U.S. economy and invite retaliation from abroad.

A **nontariff barrier** (NTB) is any measure other than a tariff that is a deterrent or obstacle to the sale of products in a foreign market. Also known as **hidden trade barriers**, NTBs include quotas, discriminatory procurement policies, restrictive customs procedures, arbitrary monetary policies, and restrictive regulations.

A **quota** is a government-imposed limit or restriction on the number of units or the total value of a particular product or product category that can be imported. Generally, the quotas are designed to protect domestic producers.

Discriminatory procurement policies can take the form of government rules, laws or administrative regulations requiring that goods or services be purchased from domestic companies.

Customs procedures are considered restrictive if they are administered in a way that makes compliance difficult and expensive.

Discriminatory exchange rate policies distort trade in much the same way as selective import duties and export subsidies.

Restrictive administrative and technical regulations can create barriers to trade. They may take the form of antidumping regulations, product size regulations, and safety and health regulations.

TARIFF SYSTEMS

- ✓ **(Learning Objective #4)**

Tariff systems provide either a single rate of duty for each item, applicable to all countries, or two or more rates, applicable to different countries or groups of countries. Tariffs are usually grouped into two classifications.

The **single-column tariff** is the simplest type of tariff. It is a schedule of duties in which the rate applies to imports from all countries on the same basis.

Under the **two-column tariff** (Table 8-4), column 1 includes “general” duties plus “special” duties indicating reduced rates determined by tariff negotiations with other countries.

Rates agreed upon by “convention” are extended to all countries that qualify for **normal trade relations** (NTR; formerly most-favored nation or MFN) status within the framework of the WTO. Column 2 shows rates for countries that do not enjoy NTR status.

A **preferential tariff** is a reduced tariff rate applied to imports from certain countries.

The United States is now a signatory to the GATT customs valuation code. GATT prohibits the use of preferential tariffs, with three major exceptions:

1. Historical preference arrangements such as the British Commonwealth
2. Preference schemes that are part of a formal economic integration treaty, such as free trade areas or common markets.
3. Industrial countries are permitted to grant preferential market access to companies based in less-developed countries.

Under the code, the primary basis of customs valuation is "transaction value". **Transaction value** is defined as the actual individual transaction price paid by the buyer to the seller of the goods being valued.

Customs Duties

Customs duties are divided into categories based on how they are calculated; either as a percentage of the value of the goods (ad valorem duty), as a specific amount per unit (specific duty), or as a combination of both of these methods.

As noted, an *ad valorem duty* is expressed as a percentage of the value of the goods. In countries adhering to GATT conventions on customs valuation, the customs value is the value of cost, insurance, and freight (CIF) at the port of importation.

A *specific duty* is expressed as a specific amount of currency per unit of weight, volume, length, or other unit of measurement. Specific duties are usually expressed in the currency of the importing country.

Other Duties and Import Charges

Dumping is the sale of merchandise in export markets at unfair prices. To offset the impact of dumping and to penalize guilty companies, most countries have introduced legislation providing for the imposition of **antidumping duties.**

Countervailing duties (CVDs) are additional duties levied to offset subsidies granted in the exporting country.

Several countries apply a system of **variable import levies** to certain categories of imported agricultural products. If prices of imported products would undercut the prices of domestic products, these levies raise the price of imported products to the domestic price level.

Temporary surcharges have also been introduced from time to time by certain countries, to provide additional protection for local industries and, in particular, in response to balance of payments deficits.

KEY EXPORT PARTICIPANTS

- ✓ **(Learning Objective #5)**

Export participants include: foreign purchasing agents, export brokers, and export merchants, who have no assignment of responsibility from the client. Others, including export management companies, manufacturers' export representatives, export distributors, and freight forwarders, are assigned responsibilities by the exporter.

Foreign purchasing agents are variously referred to as the *buyer for export*, *export commission house*, or *export confirming house*. These agents operate on behalf of, and are compensated by, an overseas customer known as a "principal".

The **export broker** receives a fee for bringing together the seller and the overseas buyer. Although this fee is usually paid by the seller, sometimes the buyer pays it. The broker takes no title to the goods and assumes no financial responsibility.

Export merchants are sometimes referred to as *jobbers*. These marketing intermediaries identify market opportunities in one country or region and make purchases in other countries to fill these needs.

Export management company (EMC) is an independent marketing intermediary that acts as the export department for two or more manufacturers ("principals") whose product lines do not compete with each other.

Manufacturer's export agents (MEA) can act as an export distributor or as export commission representative. However, the MEA does <u>not</u> perform the functions of an export department, and the scope of its market activities is usually limited to a few countries.

An **export distributor** does assume financial risk as part of the export process. The export distributor usually represents several manufacturers and is therefore sometimes known as a *combination export manager.*

The **export commission representative** assumes no financial risk. The commission representative is assigned all or some foreign markets by the manufacturer.

The **cooperative exporter**, sometimes called a *mother hen*, *piggyback exporter*, or *export vendor*, is an export organization of a manufacturing company retained by other independent manufacturers to sell their products in foreign markets.

Freight forwarders are licensed specialists in traffic operations, customs clearance, and shipping tariffs and schedules; simply put, they can be thought of as travel agents for freight.

ORGANIZING FOR EXPORTING IN THE MANUFACTURER'S COUNTRY

- ✓ **(Learning Objective #6)**

Home-country issues include deciding whether to assign export responsibility inside the company or to work with external organizations specializing in a product or geographic area. Most companies handle export operations within their own in-house export organization.

The possible arrangements for handling exports include the following:

- A part-time activity performed by domestic employees
- Through an export partner that takes possession of the goods before they leave the country
- Through an export department that is independent of the domestic marketing structure
- Through an export department within an international division
- For multidivisional companies, each of the preceding options is available.

A company that assigns a sufficiently high priority to its export business will establish an in-house organization.

The company that chooses not to perform its own marketing and promotion in-house has numerous external export service providers from which to choose. These options include export management companies (EMCs), export merchants, export brokers, combination export managers, manufacturers' export representatives or commission agents, and export distributors. (All discussed earlier.)

ORGANIZING FOR EXPORTING IN THE MARKET COUNTRY

- ✓ **(Learning Objective #7)**

In addition to deciding whether to rely on in-house or external export specialists in the home country, a company must make arrangements to distribute its products in the target market country.

Every exporting organization faces one basic decision: To what extent do we rely on direct market representation as opposed to representation by independent intermediaries?

Two major advantages to direct representation in a market are control and communications.

Direct market representation enables decisions concerning program development, resource allocation, or price changes to be implemented unilaterally.

Direct representation's great advantage is that the possibilities for feedback and information from the market are much greater.

Direct representation does not mean that the exporter is selling directly to the consumer or customer; in most cases, direct representation involves selling to wholesalers or retailers.
In smaller markets, it is usually not feasible to establish direct representation because the low sales volume does not justify the cost. Finding "good" distributors can be the key to export success.

TRADE FINANCING and METHODS OF PAYMENT

- ✓ **(Learning Objective #8)**

The need for a company to be paid for its export sales should be obvious.

Selling across borders is inherently riskier than selling within one's home country. Managers may have only limited understanding of several factors including: language and culture differences, competing cultural norms, and foreign political environments.

Fortunately, the international banking system plays a critical role in enabling successful international commerce by reducing transactions risks such as "nonpayment" and "nonperformance" by their business problems.

Before taking up a discussion of banking's role, we need to highlight two other methods of payment: cash with order and open account.

Cash With Order (CWO)

Cash with order presents the least transaction risk to the exporter. In this payment arrangement, the exporter sends the importer a **pro-forma invoice** with the details and costs of a future shipment. After receiving this invoice, the importer then sends its purchase order with prepayment (CWO) to the exporter.

Open Account

Open Account payment presents the greatest transaction risk to the exporter. In this arrangement, the importer sends a purchase order to the exporter, which then produces, ships, and subsequently invoices the importer for this shipment. The importer than remits payment to the exporter via wire transfer.

While the CWO and open account payment methods both carry risks, they may be used when two companies have a longstanding, mutually beneficial relationship with each other.

However, for most firms entering cross-border business with a new commercial partner, the risks of nonpayment or nonperformance are simply too great, and failure could put companies at risk.

This is where the banking system helps manage risk via a key document call the letter of credit (also known as a *documentary credit*).

Letter of Credit

Letters of Credit (also known as documentary credits) are widely used as a payment method in international trade. A **letter of credit** (L/C) is essentially a document stating that a bank as substituted its creditworthiness for that of the import-buyer.

The importer-buyer's bank is the "issuing" bank; the importer-buyer is, in essence, asking the issuing bank to extend credit.

The actual payment process is set in motion when the exporter-seller physically ships the product.

Once the documents are negotiated, the confirming bank, requests payment from the issuing bank. Comparing shipping documents, comparing it to the L/C, and if there are no discrepancies, the money is transferred to the exporter-seller's account.

Documentary Collections (Sight or Time Drafts)

After an exporter and importer have established a good working relationship, it may be possible to move to a documentary collection or open-account method of payment. A documentary collection is a method of payment that uses a bill of exchange, also known as a *draft*. A **bill of exchange** is a negotiable instrument that is easily transferable from one party to another.

Drafts are different from L/Cs; a **draft** is a payment instrument that transfers all the risk of nonpayment onto the exporter/seller. Banks are involved as intermediaries but they do not bear financial risk. Because a draft is negotiable, a bank may be willing to buy the draft from the seller at a discount and thus assume the risk.

Also, because bank fees for drafts are lower than those for L/Cs, drafts are frequently used when the monetary value of an export transaction is relatively low.

The draft is presented to the importer; payment takes place in accordance with the terms specified in the draft. In the case of a *sight draft* (also known as a D/P or *documents against payment*), the importer-buyer is required to make payment when presented with both the draft and the shipping documents.

Time drafts can take two forms. An *arrival draft* specifies that payment is due when the importer/buyer receives the goods; a *date draft* requires payment on a particular date.

ADDITIONAL EXPORT/IMPORT ISSUES

In the post-September 11 business environment in the United States, national security concerns have resulted in increased security of imports into the country. A number of initiatives have been launched to ensure that international cargo cannot be used for terrorism.

The **Customs Trade Partnership Against Terrorism** (C-TPAT) has as its goal to secure voluntary cooperation of supply chain participants in an effort to reduce inspection delays. Organizations that have achieved certified C-TPAT status are entitled to priority status for CBP inspections.

Another issue is d*uty drawback*. This refers to refunds of duties paid on imports that are incorporated into other goods and then re-exported.

SOURCING

- ✓ **(Learning Objective #9)**

In global marketing, the issue of customer value is inextricably tied to the **sourcing decision:** whether a company makes or buys its products as well as ***where*** it makes or buys its products.

Outsourcing is shifting production jobs or work assignments to another company to cut costs.

When the outsourced work moves to another country, the *terms global outsourcing* or *offshoring* are sometimes used**.**

In today's competitive marketplace, companies are under intense pressure to lower costs; one way to do this is to locate manufacturing and other activities in low-wage countries.
In theory, this situation bestows great flexibility on companies.

The first wave of non-manufacturing outsourcing primarily affected *call centers.* These are sophisticated telephone operations that provide customer support and other services to in-bound callers from around the world.

The decision of where to locate key business activities depends on other factors besides cost. There are no simple rules to guide sourcing decisions.

Several factors may figure into the sourcing decision: management vision, factor costs and conditions, customer needs, public opinion, logistics, country infrastructure, the political environment, and exchange rates.

Management Vision

Some chief executives are determined to retain some or all manufacturing in their home country. (E.g., Swatch manufactures mass-market products in high-wage countries).

Top managers at Canon chose to maintain a strategic focus on high value-added products rather than the manufacturing location, keeping 60 percent in Japan.

Factor Costs and Conditions

Factor costs are land, labor, materials, and capital costs.

German hourly compensation costs for production workers in manufacturing are 160 percent of those in the United States. Those in Mexico are only a fraction of those in the United States.

Labor costs in non-manufacturing jobs are also dramatically lower in some parts of the world. For example, a software engineer in India may receive an annual salary of $12,000 as compared to $80,000 in the U.S.

The other factors of production are land, materials, and capital. The cost of these factors depends upon their availability and relative abundance. Often, the differences in factor costs will offset each other so that, on balance, companies have a level field in the competitive arena.

The application of advanced computer controls and other new manufacturing technologies has reduced the proportion of labor relative to capital for many businesses.

Company managers and executives should also recognize the declining importance of direct manufacturing labor as a percentage of total product cost.

Customer Needs

Although, outsourcing can help reduce costs, sometimes customers are seeking something besides the lowest possible price.

Dell Computer recently rerouted some of its call center jobs back to the United States from India after complaints from key business customers.

Logistics

In general, the greater the distance between the product source and the target market, the greater the time delay for delivery and the higher the transportation cost.

Manufacturers can take advantage of intermodal services that allow containers to be transferred between rail, boat, air, and truck carriers.

Country Infrastructure

To present an attractive setting for a manufacturing operation, it is important that a country's infrastructure be sufficiently developed to support a manufacturing and distribution. Infrastructure requirements will vary by company and by industry, but at a minimum, they will include power, transportation and roads, communications, service and component suppliers, a labor pool, civil order, and effective governance.

A country needs support services or infrastructure to support a high volume of business activities (e.g., Hong Kong, Taiwan, and Singapore do).

One of the challenges of doing business in the new Russian market is an inadequate infrastructure.

Political Factors

Political risk is a deterrent to investment in local sourcing. The difficulty of assessing political risk is inversely proportional to a country's stage of economic development.

All other things being equal, the less developed a country the more difficult it is to predict political risk.

The political risk of the Triad countries, for example, is quite limited as compared to that of a less-developed country in Africa, Latin America, or Asia.

Market access is another type of political factor. If a country or a region limits market access because of local content laws, balance-of-payments problems, or any other reason, it may be necessary to establish a production facility within the country itself.

Foreign Exchange Rates

In deciding where to source a product or locate a manufacturing activity, a manager must take into account foreign exchange rate trends in various parts of the world. Exchange rates are so volatile today that many companies pursue global sourcing strategies as a way of limiting exchange-related risk.

The dramatic shifts in price levels of commodities and currencies are a major characteristic of the world economy today. Such volatility argues for a sourcing strategy that provides alternative country options for supplying markets.

CASES

Case 8-1: The Game's Afoot: Exports Revive Britain's Shoe Industry

Overview: Cheaney & Sons is based in Northhamptonshire, the heart of England's traditional shoemaking industry since the Middle Ages. Having begun as a cottage industry, shoemaking in Northhamptonshire became more industrialized in the mid-nineteenth century. Productivity increased, and by the mid-twentieth century there were some 200 shoe manufacturers in Northhamptonshire. Production totaled about 160 million pairs per year.

Then, as production moved to China and other low-waged countries, the English shoe industry went into decline. Church's bought Cheaney & Sons in the 1960s, which was then acquired by Prada. In 2009, cousins William and Jonathan Church bought Cheaney & Sons from Prada and began rebuilding the brand. Online sales for the revamped Cheaney and Sons has been roughly $3.6 million.

Grenson is another British heritage shoe brand whose owner has discovered collaboration is a good route to winning in the marketplace. Great Britain is not the only EU nation where traditional shoemaking is on the rebound.

Discussion Questions

8-7. What explains the appeal of expensive shoes that are "Made in England" or "Made in "Italy?

This is known as the Country of Origin effect. Many consumers perceive value based on where the product is manufactured. Some countries products are considered luxury items based on where they are made.

8-8. In 2006, the European Union imposed tariffs on imports of inexpensive shoes from China and Vietnam. Who are the winners, and who are the losers, when such tariffs are imposed?

The winners would be the manufacturers' that produce quality products regardless of the cost of the item. The losers would be the low-cost producers who are manufacturing low-quality products.

8-9. What is the key to the popularity of the Dr. Martens brand?

Having the right product at the right time.

8-10. Compare the M. Gemi business model with that of Cheaney & Sons.

Student's answer will vary. M. Gemi is bringing a "post-luxury" business model to Italy's shoemaking industry. The company's direct-to-consumer channel offers luxury shoe styles at fast-fashion prices. Cheaney & Sons employ a network of sales agents to handle accounts in key European countries as well as in North America.

Case 8-2: A Day in the Life of an Export Coordinator

Overview: Mikkel Jakobsen works as an export coordinator with Shipco Transport, a subsidiary of ScanGroup, a major European transportation company. As a non-vessel operating common carrier (NVOCC), Shipco Transport operates similarly to shipping companies such as Maersk Sealand, Mediterranean Shipping Company, and others, with one key difference: Shipco has no vessels of their own. Instead, Shipco relies on favorable contracts with more than 40 carriers, enabling the company to offer competitive rates on routings to destinations around the world.

In 2006, Jakobsen earned a BA degree in international management and economics from a small liberal arts college in the Midwest. Jakobsen's day begins at 8:30 AM, and usually ends at 5:30 PM, depending on the workload. Although quoting and setting up bookings takes up a lot of my workday, the majority is spent addressing various problems and issues that arise.

When doing business internationally it is essential to recognize differences in how business is conducted around the world.

8-11. What knowledge and skills are required to be successful as an export coordinator?

In general, this job consists of quoting out shipping costs to customers, placing bookings with steamship lines, preparing export documentation, and dealing with problems that arise during the container's journey from shipper to consignee. The knowledge and skills required would be an analytical mind, organizational skills, and customer service skills. Students answers will vary.

8-12. What do you think is the best part of Jakobsen's job? The most challenging part?

Student answers will vary. Personally, I think the best part of the job is dealing with the various international laws and customs. I also believe this would be the most challenging.

8-13. If you were in Jakobsen's position, what would your next career move be?

Students answers will vary. However, my next career move would be running/owning a freight forwarding business.

TEACHING TOOLS AND EXERCISES

Additional Cases:

"ECCO A/S – Global Value Chain Management". Bo Nielsen; Torban Pedersen; Jacob Pyndt. *HBS* 908M14.

"Sony Ericsson: Marketing the Next Music Phone". Qui Cheng; Zane Moi. *HBS* HKU801.

Activity: Students should be preparing or presenting their Cultural-Economic Analysis and Marketing Plan for their country and product as outlined in Chapter 1.

Out-Of-Class Reading: Wolff, James A., and Timothy L. Pett. "Internationalization of Small Firms: An Examination of Export Competitive Patterns, Firm Size, and Export Performance." *Journal of Small Business Management* 38, no. 2 (April 2000) pp. 34-47.

Internet Exercise: Find out about the activities of Global Exchange, a human rights group, that offers information on efforts to combat sweatshops: *www.globalexchange.org*

Prepare a short 1-2 page paper outlining the activities of this group.

SUGGESTED READINGS

Books

Branch, Alan E. *Elements of Export Marketing Management*. London: Chapman and Hall, 1990.

Czinkota, Michael P. and Jon Woronoff. *Unlocking Japan's Markets.* Chicago: Probus, 1991.

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Porter, Michael. *The Competitive Advantage of Nations.* New York: Free Press, 1990.

Raynauld, Andre. *Financing Exports to Developing Countries*. Paris, France: Development Centre of the Organization for Economic Cooperation and Development, 1992.

Rommel, Gunter, Jurgen Kluge, Rolf-Dieter Kempis, Raimund Diederichs and Felix Bruck, *Simplicity Wins: How Germany's Mid-sized Industrial Companies Succeed.* Boston: Harvard Business Review Press, 1995.

Rossen, Philip J., and Stan D. Reid, eds. *Managing Export Entry and Expansion*. New York: Praeger, 1987.

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Alden, Vernon R. "Who Says You Can't Crack the Japanese Market?" *Harvard Business Review* (January-February 1987), pp. 52-56.

Bonaccorsi, Andrea. "On the Relationship Between Firm Size and Export Intensity." *Journal of International Business Studies* 23, no. 4 (Fourth Quarter 1992), pp. 605-636.

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Cavusgil, S. Tamer, and V.H. Kirpalani, “Introducing Products into Export Markets: Success Factors.” *Journal of Business Research* 27, no. 1 (May 1993), 1-15.

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Howard, Donald G. “The Role of Export Management Companies in Global Marketing.” *Journal of Global Marketing* 8, no. 1 (1994), pp. 95-110.

Katsikeas, Constantine S. “Perceived Export Problems and Export Involvement: The Case of Greek Exporting Manufacturers.” *Journal of Global Marketing* 7, no. 4 (1994), pp. 29-57.

Korth, Christopher M. “Managerial Barriers to U.S. Exports.” *Business Horizons* 34, no. 2 (March/April 1991), pp. 18-26.

Kotabe, Masaaki. “Patterns and Technological Implications of Global Sourcing Strategies: A Study of European and Japanese Multinational Firms.” *Journal of International Marketing* 1, no. 1 (1993), pp. 26-43.

Leonidou, Leonidas C. “Empirical Research on Export Barriers: Review, Assessment, and Synthesis.” *Journal of International Marketing* (3), no. 1 (1995), 29-44.

MacCormack, Alan David, Lawrence James Newman III, and Donald B. Rosenfield. “The New Dynamics of Global Manufacturing Site Locations.” *Sloan Management Review* 35, no. 4 (Summer 1994), pp. 69-80.

Mahone, Charlie E. Jr. “Penetrating Export Markets: The Role of Firm Size.” *Journal of Global Marketing* 7, no. 3 (1994), pp. 133-148.

Murphy, Paul R., James M. Daley, and Douglas R. Dalenberg. “Doing Business In Global Markets: Perspectives of International Freight Forwarders.” *Journal of Global Marketing* 6, no. 4 (1993), pp. 53-68.

Namiki, Nobuaki. “A Taxonomic Analysis of Export Marketing Strategy: An Exploratory Study of U.S. Exporters of Electronics Products.” *Journal of Global Marketing* 8, no. 1 (1994), pp. 27-50.

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