GLOBALISATION AND THE INTERNATIONAL MARKET (3.5)

(Chapter 21 - A level 3.5)

Globalisation refers to companies operating internationally or on a global scale. This involves most of the world's economies working together to produce goods and services.

Reasons why globalisation has increased dramatically over recent years :

- **Increasing number of free trade agreements** – these are agreements between countries that allow them to import and export goods and services with no tariffs or quotas.
- **Improved and cheaper transport** (water, land, air) and communications (internet) infrastructure
- **The internet** and other **technological developments**
- Expansion of **multinational corporations**

Potential benefits of globalisation :

✔ **Allows businesses to sell in new foreign markets**, spreading risk + increasing sales/profits
✔ Can open factories and production units in other countries, possibly at a **cheaper** rate
✔ **Import products from other countries and sell it to customers** in the domestic market- this could be more profitable and producing and selling the good themselves
✔ **Improve the relationships** and political links **between countries**
✔ Globalisation brings **consumers more choice and lower prices**
✔ International businesses **force domestic firms to be more efficient** (to remain competitive)

Potential limitations of globalisation :

✖ **Increased competition** can lead to domestic firms shutting down, this will lose local jobs
✖ Can lead to the **exploitation** of workers when a business relocates to a country to employ cheap labour
✖ **Governments will have much less influence on business decisions**, e.g. preventing closure of factories to relocate in low-cost countries (MNCs can have power over governments.)

Multinational corporations (MNCs)

MNCs are businesses which have their operations, factories and assembly plants in more than one country. The number and size of MNCs have increased greatly in recent years due to globalisation.

The country they are based in is called the *home country* (where the head shareholders and directors work), and the countries they operate in are called *host countries* (where, say, the factory is located.) Examples of MNCs include Starbucks, IKEA, Toyota, Adidas etc.

Why do firms become multinationals?

- To produce goods with lower costs – cheaper material and labour may be available in other countries (lower minimum wages etc.)
- To extract raw materials for production, available in a few other countries. For example: crude oil in the Middle East
- To produce goods nearer to the markets to avoid transport costs
- To avoid trade barriers on imports. If they produce the goods in foreign countries, the firms will not have to pay import tariffs or be faced with a quota restriction
- To expand into different markets and spread their risks
- To remain competitive with rival firms which may also be expanding abroad

*Advantages of a multinational corporation to the **host** country :*

✔ **More jobs** created by multinationals for local workers

✔ **Increases GDP** of the country (**gross domestic product** - the total goods produced by a country in a specific period of time. GDP measures the health of a country.)

✔ The technology that the multinational brings in can bring in **new ideas and methods** into the country

✔ **Multinationals will also pay taxes**, thereby increasing the government's tax revenue

✔ **More product choice** for local consumers

*Disadvantages of multinational to the **host** country :*

✖ The jobs created are often for unskilled tasks. The more skilled jobs will be done by workers that come from the firm's home country. The unskilled workers may also be **exploited** with low wages + bad working conditions.

✖ **Local firms may be forced out of business**, unable to survive the competition. This will result in loss of jobs

✖ Multinationals can **use up the resources** in the country

✖ As multinationals are large, they can **influence the government and economy**. They could threaten the government that they will close down and make workers unemployed if they are not given financial grants etc.

✖ The profits earned by the multinational could be sent back to their home country and the **government will not be able to tax it**

Free trade and protectionism

Free trade is when there are no restrictions for trade between economies**.** This reduces costs of transporting goods, encouraging globalisation and increasing competition among businesses.

Protectionism refers to when governments protect domestic firms from foreign competition using trade barriers such as tariffs and quotas (protectionism is the opposite of free trade.)

Trade barriers include :

- **Tariffs**: these are indirect taxes on imported (or exported) goods that make them more expensive, imposed in order to help discourage domestic consumers from purchasing them
- **Subsidies**: government allows subsidies to domestic producers so that they can increase their output and reduce costs and in turn reduce prices, in the hope that consumers will be encouraged to buy inexpensive domestic goods rather than the imported goods
- **Quotas**: this is a limit on the number of imports allowed into a country in a given period. Restricting supply will push up their market prices and discourage consumption of those imports.
- **Excessive quality standards**: imports may only enter a country after extensive quality checks which will be costly and so foreign producers will be discouraged to sell their products in the country
- **Embargo**: this is a complete ban on imports of a good to a country

Protectionism and trade barriers act to reduce the number of foreign goods in the domestic market and make them expensive to buy. This will reduce the competitiveness of the foreign goods and make it easy for domestic firms to produce and sell their goods. However, it also reduces free trade and globalisation.

It helps to remember that **the advantages of free trade are the disadvantages of protectionism** and the **disadvantages of free trade are the advantages of protectionism.** Protectionism and free trade are mortal enemies!

Impact of globalisation on marketing

The growth of world trade has created more opportunities for businesses to sell in global markets - **international marketing**.

BRICS is the acronym for five rapidly developing economies with great market opportunities – **Brazil**, **Russia**, **India**, **China** and **South Africa**. Many businesses have started selling to BRICS countries, or plan to do so.

Growing business in other countries can increase sales, revenue and profits. This is because the business is now available to a wider group of people, which increases potential customers. If the home markets have saturated (product is in maturity stage), firms take their products to international markets. There may be, of course, some obstacles to overcome.

Potential problems of entering foreign markets

- **Difference in language and culture**: It may be difficult to communicate with people in other countries because of language barriers and as for culture, different images, colours and symbols have different meanings and importance in different places
- **Lack of market knowledge**: The business won't know much about the market it is entering and the customers won't be familiar with the new business brand, and so getting established in the market will be difficult and expensive
- **Economic differences**: The cost and prices may be lower or higher in different countries so businesses may not be able to sell the product at the price which will give them a profit
- **Political differences** : some countries are more conservative than others etc.
- **Social differences**: Different people will have different needs and wants from people in other countries, and so the product may not be successful in all countries
- **Legal differences :** like laws controlling advertising to children or unethical business practices (minimum wage, health and safety laws etc.)

Different methods for entering foreign markets

A decision to market products internationally is just one step in a long and detailed planning process. The next major decision must be the method of entering the markets. Methods including :

1. Exporting
2. Franchising
3. Licensing
4. Joint ventures
5. Investing in subsidiaries

1. **Exporting**

Exporting can be **direct**, where the product is sold directly to a foreign customer (perhaps the order has been placed via the company website) – or it can be **indirect**, where it's sold through an export intermediary, such as an agent or trading company based in the country.

Exporting directly means the company has complete control over the international marketing, and no profit is needed to be paid to any intermediaries like an agent. However, the business may lack important local knowledge that an agent would know.

Exporting indirectly means the company has someone with local knowledge handling transport and administrative procedures, as well as possibly having local contacts. However, said agent will require a commission (reducing profit slightly.)

2. International franchising

Franchising is when the owner of a business (the franchisor) grants a licence to another person or business (the franchisee) to use their business idea – often in a specific geographical area. Fast food companies such as McDonald's and Subway operate around the globe through lots of franchises in different countries.

Advantages to the franchisor :

✔ Rapid, low cost method of business expansion
✔ Gets an income from franchisee in the form of franchise fees and royalties
✔ Franchisee will better understand the local tastes and so can advertise and sell appropriately
✔ Franchisee will run the operations

Disadvantages to the franchisor :

✖ Profits from the franchise needs to be shared with the franchisee
✖ Loss of control over running of business
✖ If one franchise fails, affects reputation
✖ Need to supply raw materials + training
✖ Franchisee may not be as skilled

Advantages to the franchisee :

✔ Working with an established brand means chance of business failing is low
✔ Franchisor gives technical/managerial support
✔ Franchisor will supply the raw materials/products
✔ Banks/investors are more likely to give loans as working with established brand means less risk

Disadvantages to the franchisee :

✖ Cost of setting up business
✖ No full control over business - must strictly follow franchisor's rules
✖ Profits have to be shared with franchisor (+ royalty fees.)
✖ Need to advertise themselves

3.Licensing

Licensing involves the business allowing another firm in the country being entered to produce its branded goods or patented products 'under licence', which will involve strictly controlled terms over quality.
Example: Walt Disney granting McDonalds a licence for McDonalds to co-brand McDonald's Happy Meals with a Disney trademarked character.

This means that goods do not have to be physically exported, **saving on time** and **transport cost** – and making food **products fresher** too. However, allowing another firm to produce their products may lead to **reduced quality** or the licensee may use unethical production methods to cut costs – both instances will **reflect badly** on the main business.

Difference between franchise and licensing :

Franchises and licences are both business agreements in which certain brand aspects are shared in exchange for a fee. However, a franchising agreement pertains to a business's entire brand and operations, while a licensing agreement only applies to registered trademarks (certain projects.)

4. **Joint ventures**

Joint venture is an agreement between two or more businesses to work together on a project. The foreign business will work with a domestic business in the same industry. Eg: Japan's Suzuki Motor Corporation created a joint venture with India's Maruti Udyog Limited to form Maruti Suzuki, a highly successful car manufacturing project in India.

Advantages of joint ventures :
✔ Reduces risks and cuts costs - businesses share expenses and split costs
✔ Each business brings different expertise to the joint venture
✔ The market potential for all the businesses in the joint venture is increased
✔ Market and product knowledge can be shared to the benefit of the businesses

Disadvantages of joint ventures :
✖ Any mistakes made will reflect on all parties of the joint venture, which may damage their reputations
✖ The decision-making process may be ineffective due to clashing business culture or different styles of leadership

5. **Investing in subsidiaries**

A subsidiary is a company that belongs to another company, which is usually referred to as the parent company or the holding company. The parent holds a controlling interest in the subsidiary company, meaning it has bought more than half its stock and is therefore in control.

Advantages of investing in subsidiaries :
✔ Head office has full control of operations
✔ All profits after tax belong to the company – no commission is paid and no sharing of profits with partner business
✔ Foreign governments may be willing to offer financial support to encourage investments

Disadvantages of investing in subsidiaries :
✖ It is expensive to set up operations in foreign countries – Much higher capital cost required than exporting directly or indirectly
✖ Senior staff will need to visit and may need to be based in the country

Factors that influence choosing the method of entering foreign markets :

- **The costs of the different methods of entry** - intermediaries are costly
- **The risk involved** - less risky to work through intermediaries who know the market
- **Likely returns/profits to be made**
- **The experience of the business in entering foreign markets** - an experienced business won't need the help of someone who's familiar with the domestic market

International marketing strategies

There are two broad approaches to selling goods and services internationally. These are known as '**pan-global marketing**' and '**global localisation**'.

Pan-global marketing refers to selling the same products the same way in all international markets. It attempts to reduce marketing costs and new product development costs, by having their processes to promote, create and sell their product remain the same.

Advantages :
✔ A common identity for the product can be established - same marketing, price etc.
✔ Reduces costs of changing the product to suit foreign markets

Disadvantages :
✖ May be necessary to change product to suit the different culture, taste or religion of the country in order to be profitable
✖ May be legal restrictions that the product doesn't meet (restrictions on quality etc.)
✖ Setting the price the same in all countries - what about the different average incomes? What if consumers can't afford it?
✖ Brand name might not translate well in a different language - may be seen as offensive

Global localisation refers to the process of adapting the marketing mix (price, product, promotion and place) to suit the foreign country's tastes and culture.

Advantages :
✔ Local tastes, needs and cultures are reflected in the product, making it more desirable to local consumers
✔ Products more likely to meet legal requirements (health and safety, advertising laws etc.)
✔ Locals won't feel as if they are having foreign brands shoved down their throats

Disadvantages :
✖ There will be additional costs of adapting products, adverts, store layouts, etc. to local needs
✖ These additional costs may force the business to charge a higher price that consumers aren't willing to pay
✖ Inconsistent product image