

Chapter 4

Ethics, Corporate Social Responsibility, Sustainability, and Governance in International Business

Learning Objectives *After studying this chapter, you should be able to:*

- 4.1 Learn the components of ethical behavior and their importance in international business.
- 4.2 Recognize ethical challenges in international business.
- 4.3 Understand corporate social responsibility.
- 4.4 Understand sustainability.
- 4.5 Know the role of corporate governance.
- 4.6 Learn how to apply the framework for making ethical decisions.

Improving the Lives of Bangladeshi Garments Factory Workers

Bangladesh is one of the top exporters of garments, with a 4.8 percent export market share. It is the most significant industry for the country, accounting for around 75 percent of the total export revenue and employing nearly 4 million people. The biggest export destinations are the European Union and the United States. New export markets are opening up in the emerging economies of Russia, Brazil, and China. Beside trade revenue and employment creation, this industry is very important for Bangladesh due to its contribution to social mobility, urbanization, and above all to empowerment of women. Most of the workers are female and from rural areas where agriculture is the only

source of employment. The remarkable improvement Bangladesh has achieved over the last 25 years in public health, primary education, and poverty alleviation are the fruits of the success of its garment industry. However, working conditions and pay in this industry have not met expectations.

The garment industry value chain is very buyer-driven, and suppliers have very limited bargaining power. Buyer-driven value chains usually occur in industries where production is labor-intensive, non-specialized, and requires low fixed cost. Entry barriers are high in designing, distribution, branding, advertising, and market intelligence but low in the production stage. Hence,



Source: Shafiqul Alam/Alamy Stock Photo

maximum bargaining power rests in the hands of large brand owners, distributors, and retailers, endowing them with price-determining powers. Suppliers are simply required to match the offered prices. This price elasticity also offers limited switching costs for buyers. Therefore, major buyers are able to significantly control their value chain without much involvement in the manufacturing process. Manufacturers are under constant pressure to gain production efficiency and achieve low-cost advantages. In many cases, health and safety issues are being overlooked to save cost. As a result, several accidents have taken place, resulting in high casualties and subsequent labor unrest. Many large importers also have cancelled purchase orders.

Responding to the working conditions and compliance issues, the International Labor Organization, consumers, stakeholders, and fair-trade agencies are working together with the Bangladeshi government, garments manufacturers, industrial associations, and trade unions to raise working conditions and pay. The minimum wage has seen a 77 percent increase and rigorous inspections are in place for safety and environmental regulation compliances. Work is also in progress in job security, value added, increased productivity through better training and distribution of control power across the value chain, etc. But consumers also need to consider the effect of fast fashion on sustainability and well-being.

AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Ethical Understanding and Reasoning, Analytical Thinking, Reflective Thinking, and Application of Knowledge.

Questions

- 4-1.** How do industries value chains effect working conditions and determine wages in certain industries?
- 4-2.** What could Bangladesh do better in moving up the garment value chain?
- 4-3.** What might be the relationship of ethical consumption and sustainability?

SOURCES: R.-D. Mariani and F. Valenti, "Working Conditions in the Bangladeshi Garment Sector: Social Dialogue and Compliance," Fair Wear Foundation, www.fairwear.org, last accessed September 10, 2015; "Bangladesh Garment Workers Suffer Poor Conditions Two Years After Reform Vows," *The Guardian*, April 22, 2015, www.theguardian.com; E. Naumann, "The Multifibre Agreement—WTO Agreement on Textiles and Clothing," Trade Law Centre for Southern Africa (Tralac) Working Paper No. 4/2006, International Centre for Trade and Sustainable Development; H. Naomi, "Exports, Equity, and Empowerment: The Effects of Readymade Garments Manufacturing Employment on Gender Equality in Bangladesh," World Development Report 2012, Gender Equality and Development, Background Paper.

This case was written by Krish Saha, Birmingham City University.

The opening case describes the ethical issues surrounding the working conditions of Bangladesh's garments factory workers. It describes the reasons they have little to no ability to negotiate but notes that gradual improvements are being introduced, driven by calls for sustainability. In this chapter, we examine ethics, corporate social responsibility, and sustainability in an international business context.

4.1 Learn the components of ethical behavior and their importance in international business.

Ethics

Moral principles and values that govern the behavior of people, firms, and governments regarding right and wrong.

Corporate social responsibility (CSR)

A manner of operating a business that meets or exceeds the ethical, legal, commercial, and public expectations of customers, shareholders, employees, and communities.

Sustainability

Meeting humanity's needs without harming future generations.

Corporate governance

The system of procedures and processes by which corporations are managed, directed, and controlled.

Ethical Behavior and Its Importance in International Business

Ethical behavior is essential for successful business in today's global marketplace.¹ Ethical behavior is about doing the right things for the company, the employees, the community, the government, and the natural environment. It requires companies to act in ways that stakeholders consider honest and fair.

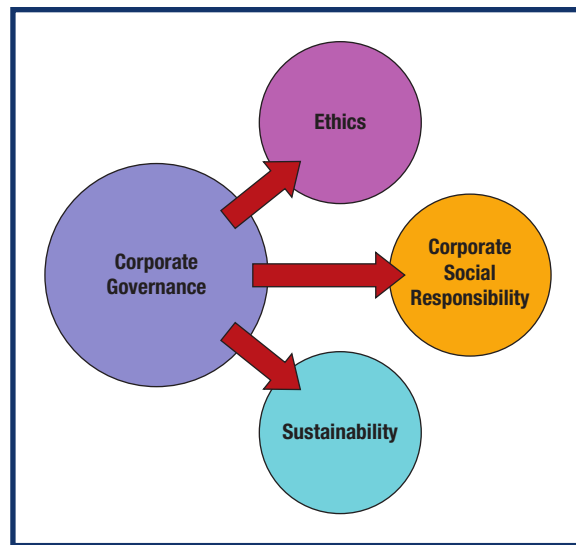
Components of Ethical Behavior

Global business leaders define ethical behavior in terms of four key components:

- Ethics
- Corporate social responsibility
- Sustainability
- Corporate governance

Ethics are moral principles and values that govern the behavior of people, firms, and governments regarding right and wrong.² **Corporate social responsibility (CSR)** refers to operating a business in a manner that meets or exceeds the ethical, legal, and commercial expectations of customers, shareholders, employees, and the communities where the firm does business. **Sustainability** means meeting humanity's needs today without harming the ability of future generations to meet their needs. **Corporate governance** is the system of procedures and processes by which corporations are managed, directed, and controlled. Corporate governance provides the means through which the organization's directors and managers undertake ethical behavior, corporate social responsibility, and sustainability.

Leading corporations ensure that ethical behavior transcends all international business activities and figures prominently in management decisions about financial performance and competitive advantage. An integrated, strategic approach to ethical, sustainable, and socially responsible behavior provides the firm with competitive advantages, including stronger relationships with customers, employees, shareholders, customers, suppliers, local governments, and the

**EXHIBIT 4.1****Organizing Framework
for Ethical Behavior in
International Business**

communities where they do business. Exhibit 4.1 provides a framework for the key managerial approaches to ethical behavior addressed in this chapter.

Experienced executives understand that incorporating a culture of ethical behavior is essential to achieving their profit objectives. Just as reputation affects the success of individuals, it is critical for companies as well. Failure to protect and nurture the corporate image translates into poor performance and potential ruin. This is even more critical in cross-border business where the firm is constantly under the scrutiny of stakeholders in multiple countries. Let's examine ethics in terms of its value to firms.

Value of Ethical Behavior

Why is it imperative for firms that conduct international business to behave ethically? Here are key reasons.

- Acting in a fair and respectful way that does not harm human rights is the right thing to do.
- Ethical behavior is often prescribed within laws and regulations. Violating laws and regulations has obvious legal consequences.
- Customers, governments, and the news media demand ethical behavior. Firms that commit ethical blunders attract unwanted attention from opinion leaders.
- Ethical behavior is good business, leading to enhanced corporate image and selling prospects.³

The firm with a reputation for high ethical standards gains advantages in hiring, motivating employees, partnering, and dealing with foreign governments. Firms that behave unethically run the risk of criminal or civil prosecution, damage to their own reputations, harm to employee morale and recruitment efforts, and exposure to blackmailers or other unscrupulous parties.⁴ For all these reasons, companies need to incorporate ethical considerations into their international activities.

In host countries, firms with iconic global brands, such as Coca-Cola and BMW, are especially conspicuous to consumers and can become targets of public protest. Increasingly, governments insist that firms behave in ways that serve the public interest. The European Union restricts the use of lead, mercury, and other harmful substances in manufacturing and requires firms to collect and recycle unwanted electronic products. Canada has well-developed complaint procedures for dealing with bribery, including liaison officers in 25 countries and a website (www.recol.ca) for posting concerns about possible corruption.⁵

Unethical Behavior

Before entering a country and throughout the life of the firm's operations there, management must be alert to the various ethical challenges that may confront the firm. Management should scan the country and potential partners for the possibility of ethical abuses and regard such scanning as an ongoing process. Managers must be constantly vigilant about their current and

potential activities. With enough practice, management can develop a systematic approach to scanning and create a culture within the firm that supports alertness and ongoing analysis of potential ethical concerns.

Management should focus not only on specific national environments but also on proposed and existing value-chain activities, which often take place in multiple countries. In each country and venture, areas that merit particular attention encompass commercial environments, labor conditions, partners, customers, accounting practices, and conditions regarding the natural environment as well as the range of the firm's potential or existing value-chain activities, including sourcing, production, marketing, and distribution.

If ethical behavior is imperative, why do we still encounter abundant examples of questionable ethical practices or even breaches of responsible conduct? A study in the *Harvard Business Review* found that bad behavior results when:

- Top management sets goals and incentives aimed at promoting good outcomes (e.g., profits) that instead encourage bad behaviors. Law firms and accounting firms often encourage employees to maximize the hours they bill for their services. Under pressure, some employees pad their hours or charge clients for work they did not do.
- Employees overlook unethical behavior because of peer pressure or self-interest. A manager may fail to complain about toxic waste discharged by a subsidiary because he doesn't want to rock the boat.
- Managers tolerate lower ethical standards in value-chain activities suppliers or third-party firms perform. Coffee producers sometimes ignore the poor working conditions of supplier farmers in Africa, Latin America, and other areas.
- Unethical practices are allowed to accumulate in the firm slowly over time. When a firm is awash in bad behavior, smaller infractions seem less noticeable. A permissive environment tends to foster further unethical behavior.
- Questionable means are justified by good ends. Pharmaceutical firms sometimes use unethical testing procedures to validate the effectiveness of new medications for disorders such as cancer and AIDS. The drugs help people but were developed through bad practice.⁶

Examples of Unethical Behavior

Firms may:

- *Tolerate sweatshop conditions* or otherwise abuse employees.
- *Pay or accept bribes, kickbacks, or inappropriate gifts.*
- *Falsify or misrepresent contracts* or financial statements.
- *Undertake false advertising* and other deceptive marketing practices.
- *Engage in pricing that is deceptive, discriminatory, or predatory.*
- *Deceive or abuse intermediaries* in international channels.
- *Engage in activities that harm the natural environment.*

After management possesses ongoing awareness of questionable ethical behavior, the next step is systematically to explore the ethical aspects of each decision the firm may make regarding its current and potential activities.⁷

Ethical Standards and Dilemmas Around the World

Are ethical standards uniform around the world? Not really. Each society develops its own traditions, values, attitudes, norms, customs, and laws. Each culture develops its own ethical values and understanding of ethical principles. There is no global standard of ethical behavior. Appropriate behavior in one culture may be viewed as inappropriate or unethical elsewhere.⁸ Let's review some examples.

- In China, counterfeiters frequently publish translated versions of imported books without compensating the original publisher or authors, an illegal practice in most of the world.
- In parts of Africa, accepting expensive gifts from suppliers is acceptable, even if inappropriate elsewhere.

- In the United States, CEOs receive compensation often a hundred times greater than that of low-ranking subordinates, a practice widely considered unacceptable in other parts of the world.
- Finland and Sweden ban advertising directed at children, whereas the practice is well accepted in other parts of Europe.

Ethical standards often vary by levels of economic development. For example, Africa is beset by widespread hunger. Some restaurant workers steal food on the job to take home to their families. Is this equivalent to restaurant workers stealing food in rich countries? Standards also change over time. Although slavery is no longer tolerated, some multinational firms today tolerate working conditions that are akin to it. In China, some MNEs operate factories that pollute local water supplies, a practice once also commonplace in the United States and other advanced economies.

Deciding what is right and wrong is not always clear. Ethical problems arise when requirements are ambiguous, inconsistent, or based on multiple legal or cultural norms. The firm may be faced with multiple and sometimes conflicting laws and regulations. In the United States, for example, the Occupational Safety and Health Administration (OSHA) specifies numerous regulations regarding labor and employment conditions, but U.S. companies often do not need to follow OSHA regulations in their foreign operations.⁹

In many countries, legal systems are weak or laws are poorly enforced. What should the firm do? Should it follow weak local laws, or should it follow the laws of the home country? Even when a country has a sound legal system or the firm has a strong code of ethics, managers regularly face the challenge of determining appropriate behavior.

An **ethical dilemma** is a problem that involves two or more possible solutions, none of which resolves the situation in a morally satisfactory manner. Available solutions may be equally justifiable but equally imperfect. The dilemma may result in conflicts among different interests when determining the most appropriate course of action. Possible actions may be mutually exclusive; the choice of one automatically negates the other(s).¹⁰ An example of such a dilemma is presented in the *Ethical Connections* box. It is typical of the type of ethical dilemmas that employees often encounter in international business. Managers working abroad may be most exposed because they are caught between home country ethical norms and those encountered in the foreign country.

In a world of seemingly endless ethical challenges, how should managers and companies respond? Consider the framework in Exhibit 4.2. After complying with local law (the bottom of the pyramid), management should ensure that company activities follow high ethical standards (the middle). Finally, once the firm has fulfilled both its legal and ethical obligations, it should emphasize socially responsible behavior (the top of the pyramid).

Ethical dilemma

A problem that involves two or more possible solutions, all of which entail violating moral principles and values.

Ethical Connections

Imagine you are a manager and visit a factory an affiliate owns in Colombia, only to discover the use of child labor in the plant. Upon studying the problem, you learn that child labor is accepted in many developing economies, even though girls are vulnerable and may be abused or exploited and work prevents children from attending school, which would improve their prospects for a better life. There are more than 50 million children working in India alone. However, you also learn that without their children's income, families often go hungry. If the kids are dismissed from the plant, many will turn to other income sources, including prostitution and street crime. The age at which children are deemed adults varies worldwide and is sometimes as young as 15 years. What should you do? Do you make a fuss about the immorality of child labor, or do you look the other way?

Relativism and Normativism

Relativism is the belief that ethical truths are not absolute but differ from group to group. According to this perspective, a good rule is "When in Rome, do as the Romans do." Thus, a Japanese multinational firm adhering to the position that bribery is wrong might nevertheless pay bribes in countries where the practice is customary and culturally acceptable. Relativists opt for passive acceptance of the values, behaviors, and practices that prevail in each of the countries where they do business.

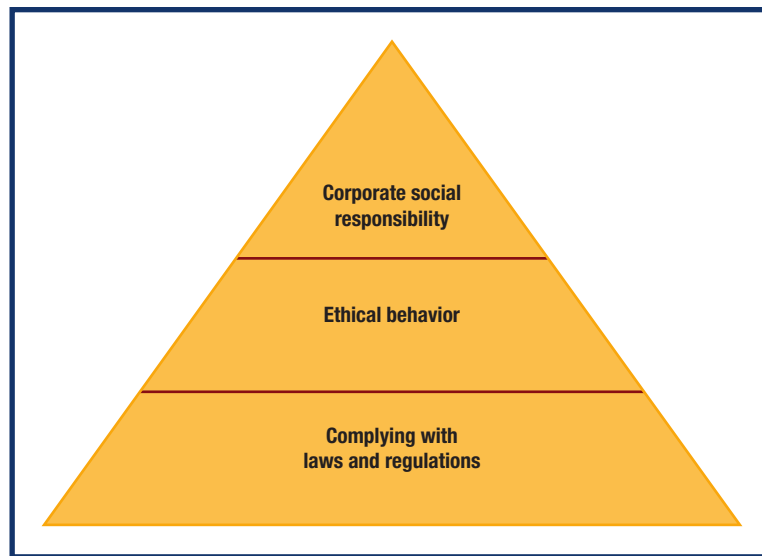
Normativism is the belief that ethical behavioral standards are universal and that firms and individuals should seek to uphold them consistently around the world. According to this view, managers of the Japanese multinational firm who believe bribery is wrong will enforce this standard everywhere in the world. The United Nations and other ethics proponents encourage companies

Relativism

The belief that ethical truths are not absolute but differ from group to group.

Normativism

The belief that ethical behavioral standards are universal and that firms and individuals should seek to uphold them around the world.

EXHIBIT 4.2**The Pyramid of Ethical Behavior**

to follow a normative approach in their international dealings. Responsible firms attempt to correct unethical practices that arise in their ongoing business dealings around the world.¹¹

In reality, most firms apply a combination of relativism and normativism abroad. Most corporations strike a balance between corporate values developed in the home country and local ethical values. In countries with questionable ethical norms, it is usually best to maintain ethical standards *superior to* what is required by local laws and values. This strategy helps win goodwill in the local market and prevents potentially damaging publicity in the firm's other markets.

To make ethical practices, CSR, and sustainability succeed in the firm, it is important for corporate directors and executives to undertake systematic and ongoing education of employees, suppliers, and intermediaries. As the firm builds a track record of positive ethical behavioral changes and successes, it will begin to build a culture of appropriate behavior in its operations worldwide. As they ply the waters of international business, addressing the moral integrity of strategic and daily operational decisions is a prime consideration for companies today.¹²

4.2 Recognize ethical challenges in international business.

Ethical Challenges in International Business

Companies encounter ethical challenges in a range of international activities. Ethical challenges include corruption, bribery, unethical management practices, harmful global sourcing, illicit products and marketing, and intellectual property infringement. Let's examine these challenges in more detail.

Corruption

Corruption is an extreme form of unethical behavior.¹³ **Corruption** is the practice of obtaining power, personal gain, or influence through illegitimate means and usually occurs at others' expense. Why is corruption bad? Corruption influences our political, social, and economic environments. It diminishes trust in public institutions, undermines the rule of law, and challenges democratic principles. It stunts economic development by discouraging foreign direct investment and hurts small businesses that lack the means to pay up.

More than 30 percent of MNEs believe corruption is a major concern in their activities worldwide. Recent data suggest that the cost of corruption amounts to more than 5 percent of global GDP annually (more than \$2.6 trillion) and increases global business costs by up to 10 percent.¹⁴

How is corruption encountered in international business? Mainly in the following ways:

- **Bribery** occurs when a person offers or gives another person a gift, cash, or a favor to act dishonestly in exchange for personal gain.
- **Embezzlement** is the theft or misuse of funds typically placed in one's care or belonging to one's employer.
- **Fraud** involves wrongfully deceiving a person or other party to give up assets or cash.
- **Extortion and blackmail** involve threats of harm against another person or party unless payment is received or some other demand is met. Threats can include physical harm, false imprisonment, exposure of an individual's secrets or past, or other harmful outcomes.

Corruption

The practice of obtaining power, personal gain, or influence through illegitimate means, usually at others' expense.

- *Money laundering* is the concealment of the origins of funds obtained through illegal means, typically by transferring the funds illicitly through banks or other legitimate businesses.

Corruption may appear as political corruption, in which officials abuse public power or profit improperly from government resources. It may arise as police corruption, in which law enforcement officials obtain financial or other benefits in exchange for granting favors such as not pursuing crimes. In firms, corruption occurs across the range of value-chain activities.

To assess corruption worldwide, Transparency International (www.transparency.org) surveys business executives every year regarding their perceptions of bribery, embezzlement, and other illicit behavior in the public sector in 180 countries. The result is the Corruption Perceptions Index, presented in Exhibit 4.3, which ranks countries on a scale from 1 to 100.¹⁵

Singapore, the Netherlands, and other nations that score well on the Corruption Perceptions Index attract much direct investment partly because managers know business in such countries is conducted fairly. Commercial laws are fair and adequately enforced, and financial and accounting information is transparent, reliable, and easily accessed. By contrast, foreign firms are reluctant to invest in countries such as Somalia and Russia due to rampant corruption. In Russia, for example, entrepreneurs typically are required to pay thousands of dollars in bribes to officials to gain the right to launch their businesses and run them smoothly.

Widespread corruption hinders economic development. This relationship points to an important dilemma—trade and investment help reduce poverty, but MNEs avoid doing business with corrupt countries. Corruption harms the poorest in societies, those forced to pay bribes to gain access to needed products and services, such as water, electricity, and phone service. Various bodies have issued international conventions against corruption. The United Nations issued a declaration against corruption in international transactions.

Bribery

Bribery, widely practiced around the world, is the most notable form of corruption in international business. It is estimated that more than \$1 trillion in bribes are paid worldwide every year to gain access to important markets and achieve other business goals. One study found that 40 percent of business executives have been asked to pay a bribe when dealing with public institutions. Twenty percent claimed to have lost business because of bribes paid by a competitor. In 2018, senior management at Brazil's state-controlled oil company, Petrobras, acknowledged the firm had been part of a scheme to pay nearly \$3 billion in bribes. The ensuing scandal implicated officials at Petrobras and in the Brazilian government, including two former presidents.¹⁶ In South Korea, the vice chairman of Samsung was convicted of bribery and sentenced to five years in prison.¹⁷ In the United States, a private consultant was sentenced to five years in prison for bribing an official at the European Bank for Reconstruction and Development with \$3.5 million.¹⁸

Numerous countries have signed the anti-bribery convention developed by the Organisation for Economic Co-operation and Development (OECD). In the United States, the Foreign Corrupt Practices Act (FCPA) makes it illegal for U.S. firms to offer bribes to foreign parties to secure or retain business. Firms can be fined \$2 million and managers can be imprisoned for up to five years. The FCPA excludes *grease payments*, small payments made to low-level government officials to perform routine duties more efficiently.

Bribery is especially common in developing economies such as Egypt, Indonesia, Nigeria, and Pakistan, where it can be nearly impossible to achieve important business objectives without paying bribes to public officials and other individuals. The problem is especially common in the global energy, mining, and telecommunications industries. This helps explain why firms from these industries, such as Halliburton and Siemens, have been implicated in major bribery scandals.



Source: Atstock Productions/Shutterstock

Bribery occurs around the world and is the most blatant form of corruption in international business.

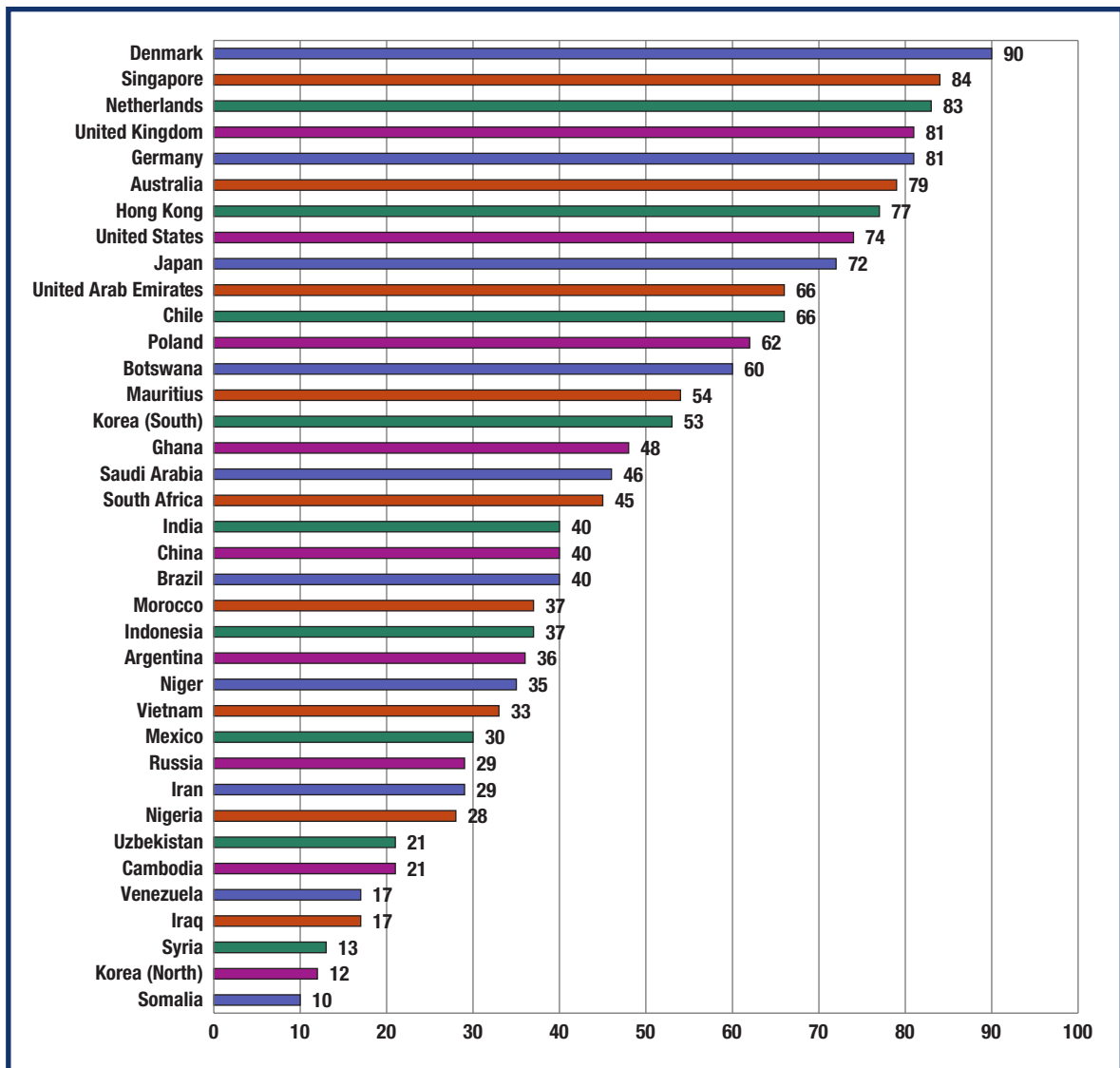


EXHIBIT 4.3

Corruption Perceptions Index 2017

Note: Countries with the highest scores have the lowest levels of corruption.

Sources: Based on *Corruption Perceptions Index*. Copyright © 2017 Transparency International: The Global Coalition Against Corruption, www.transparency.org.

Bribery has led to countless negative consequences, such as illegal logging in Indonesia, terrible work conditions in China, and poorly constructed buildings that collapsed in Turkey. Paying bribes increases the risks and costs of doing business. It promotes a culture and practice of dishonesty and immorality that opens the door to other types of wrongdoing. Bribery threatens fundamental business principles of fair competition and merit-based selection and even the essential functioning of market economies.

Executives of Walmart's Mexico subsidiary allegedly paid millions of dollars in bribes to Mexican officials in the late 1990s and early 2000s. The bribes were paid to expedite permits for construction and operation of hundreds of its retail stores in Mexico. Walmart headquarters' own investigation revealed that its subsidiary indeed had paid millions of dollars in bribes to local politicians and their organizations, actions that appeared to violate both Mexican and U.S. law. Ultimately, no executives in the firm's Mexican operations were disciplined, but in the wake of the scandal, Walmart exposed itself to substantial class-action lawsuits.¹⁹

MyLab Management Watch It! 1

If your professor has assigned this, go to the Assignments section of www.pearson.com/mylab/management to complete the video exercise titled Global Ethics and Siemens.

Harmful Work Environment

A *sweatshop* is a factory or workshop characterized by harmful or morally objectionable working conditions. In such settings, employees may work long hours for very low wages under poor conditions that entail health risks. In some cases, children under age 18 may be employed full time. Sweatshops arise mainly in developing economies, especially in the garment and footwear industries. Occasionally factories associated with popular fashion brands – for example, Adidas, Gap, H&M, Nike, and UNIQLO – have been found to operate under sweatshop conditions. Work environments similar to sweatshops are also a feature among agricultural workers in many countries. Numerous nonprofit organizations have emerged that seek to expose and eradicate such poor work conditions.²⁰

Another problem common in work environments worldwide is *workplace harassment*, which refers to threatening or demeaning behavior directed at an individual employee or a group of employees. It may involve *sexual harassment*—unwelcome sexual advances or the inappropriate promise of rewards in exchange for sexual favors. Workplace harassment may originate as discrimination against specific groups, including women, homosexuals, immigrants, racial or ethnic minorities, or people with disabilities. Such harassment takes the form of physical or emotional abuse or both. Systematic harassment can damage employees' emotional or physical health, which helps explain why such abuse is prohibited in many countries under occupational health and safety laws. However, workplace attitudes and standards vary substantially around the world, and thus such harassment is relatively widespread.²¹

Unethical Business Practices

Unethical management practices are a significant factor at the level of individual firms, especially in countries that lack adequate regulation and professional standards. A corporate culture that advocates profit over sustainability and human welfare can lead to employee abuse, harmful procedures, and other unsustainable practices. The recent global financial crisis resulted in part because top management in banks and financial firms neglected to devise safeguards against making bad loans or offering high-risk securities. Lax management standards also give rise to dishonest accounting practices, in which companies provide deceptive information to investors, customers, and government authorities. In much of the world, managers may unduly favor certain suppliers or colleagues over others, leading to lost productivity and demoralized employees.

Harmful Global Sourcing

Global sourcing is the procurement of products or services from suppliers located abroad. In a typical scenario, the focal firm buys parts and components from foreign companies that manufacture such goods, or the firm may establish its own factories abroad. However, global sourcing raises concerns about ensuring human rights and protecting the environment. Some companies operate illicit sweatshop factories in which employees are children or work long hours for very low wages, often in harsh conditions.²² Suppliers might operate factories that generate much pollution. The use of third-party suppliers is challenging for firms such as Nike and Philips with thousands of partners that operate in a range of cultures and belief systems worldwide.



Source: Dmitry Kalinovsky/123RF

Workers at an electronics factory in China. Foxconn is a leading supplier to Apple. Following charges about poor working conditions at Foxconn plants, Apple and Foxconn took steps to improve the work environment.

Illicit Products and Marketing

Firms might market defective or harmful products or engage in unethical marketing practices. Flawed products or packaging can lead to disastrous outcomes for public health and safety or for natural environments. For example, millions of electronic products from cell phones to computers are discarded every year. Products that could be recycled instead end up in landfills. Excessive product packaging generates pollution and consumes energy and natural resources. Excessive use of plastic packaging is wasteful, and because plastic does not easily decompose, the amount of plastic waste is steadily increasing on land and in the oceans.

Some companies use deceptive means to induce consumers to buy their products. Marketers may make false claims about the qualities or effectiveness of a product. Advances in communications technologies allow fraudulent marketers to easily target victims in foreign countries. The transnational nature of such scams makes it difficult for law enforcers to catch and prosecute perpetrators. International marketing provides many benefits but also presents challenges for protecting consumers worldwide.

Intellectual Property Infringement

Intellectual property refers to ideas or works that individuals or firms create and includes a variety of proprietary, intangible assets: discoveries and inventions; artistic, musical, and literary works; and words, phrases, symbols, and designs. Illicit use of intellectual property is common worldwide, typically through outright theft or illegal copying.

Trademarks, *copyrights*, and *patents* are examples of **intellectual property rights**, the legal claim through which proprietary assets are protected from unauthorized use by other parties. *Trademarks* are distinctive signs and indicators that firms use to identify their products and services. *Copyrights* grant protections to the creators of art, music, books, software, movies, and TV shows. *Patents* confer the exclusive right to manufacture, use, and sell products or processes. Intellectual property rights are not guaranteed in much of the world. Laws enacted in one country are enforceable only in that country and offer no protection abroad.²³

Intellectual property infringement arises in the form of *piracy* and *counterfeiting*, the unauthorized reproduction or use of copyrighted or patented work for financial gain. Pirated goods typically are sold at low prices in illicit markets, in person, or through the Internet. The total value of counterfeit and pirated products is expected to reach approximately \$2 trillion annually by 2022.²⁴ In Russia, software and movies produced by such firms as Microsoft and Disney often fall prey to counterfeiting. Global brands—Rolex, Louis Vuitton, and Tommy Hilfiger, among others—are frequently pirated, eroding firms' competitive advantages and brand equity.

Intellectual property

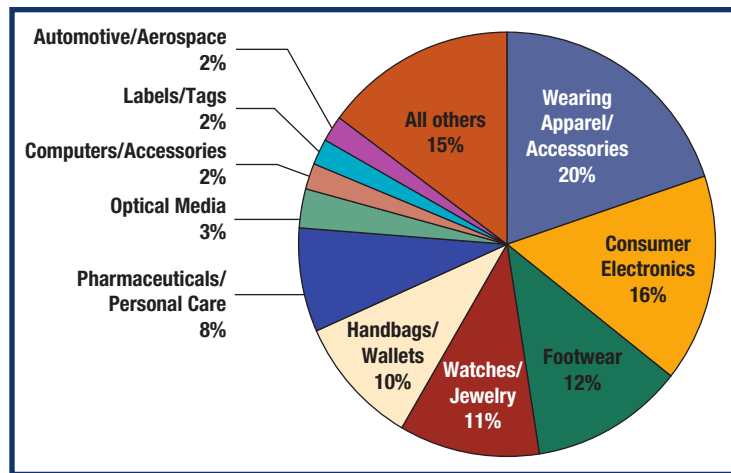
Ideas or works that individuals or firms create, including discoveries and inventions; artistic, musical, and literary works; and words, phrases, symbols, and designs.

Intellectual property rights

The legal claim through which the proprietary assets of firms and individuals are protected from unauthorized use by other parties.

Piracy and counterfeiting hurt the world economy in various ways, especially regarding:

- **International trade.** Exports of legitimate products must compete with trade in counterfeit goods.
- **Direct investment.** Firms avoid investing in countries known for widespread intellectual property violations.
- **Company performance.** Piracy and counterfeiting undermine the sales, profits, and strategies of firms that produce legitimate products. Business costs rise because the brand value of pirated goods can fall over time and companies must invest more to market their products and combat illicit competitors.
- **Innovation.** Companies avoid doing research and development in countries beset by illegal copying of intellectual property.
- **Tax revenues.** Pirates usually don't pay taxes, which, together with reduced legitimate business activity, hurts government tax revenues.
- **Criminal activity.** Piracy and counterfeiting often encourage or are supported by organized crime.
- **The natural environment.** Intellectual property violators disregard environmental standards when producing illicit goods.
- **National prosperity and well-being.** In the long run, widespread piracy and counterfeiting harm job prospects, prosperity, and moral standards in affected nations.

**EXHIBIT 4.4****Top Counterfeit Commodities Seized, United States, 2016**

Source: CBP Office of International Trade, *Intellectual Property Rights Seizure Statistics Fiscal Year 2016* (Washington, DC: U.S. Immigration and Customs Enforcement, 2017).

Pirated and counterfeit products are usually of inferior quality. They can be used unknowingly in the manufacture of military hardware, infrastructure, and consumer products. In Kenya, counterfeit batches of the medicine Zidolam were distributed to patients receiving treatment for HIV/AIDS. Nearly 3,000 people failed to receive appropriate therapy, resulting in increased illness in life-threatening conditions. In the United States, dozens of patients were affected when they received fake doses of Avastin, a drug used to treat cancer. Many people have died due to consumption of counterfeit goods.

In 2016, U.S. Department of Homeland Security agents seized pirated and counterfeit products at U.S. borders with an estimated retail value of more than \$1.4 billion. Exhibit 4.4 highlights the categories of seized illicit commodities.²⁵ Among the most counterfeited goods are jewelry, consumer electronics, and pharmaceuticals. The largest single source of counterfeit products was China, which accounted for 63 percent of Homeland Security seizures, followed by Hong Kong, an administrative region of China, amounting to 25 percent of seizures. All other countries accounted for the remaining 12 percent.²⁶ MNEs seeking to do business within China may become victims of domestic counterfeiting activities. For example, Disney has struggled to launch its DVD movie business in China due to rampant local piracy. Genuine Disney DVDs of films such as *Frozen* and *The Lion King* cost up to ten times as much as fake versions, which reduces legitimate sales to a trickle.²⁷ Numerous websites and apps facilitate illegal downloading of copyrighted music. Such sites allow users to convert Spotify songs, YouTube videos, and other streaming content into permanent files to store on phones and computers. As many as 20 percent of Internet users worldwide regularly access unlicensed music vendors online. Counterfeiting laws in many countries are insufficient to thwart such crimes, and enforcement is often weak.²⁸

Suppose you work for a small online retailer that decides to offer pirated music through the company website to potential buyers in Russia and other emerging markets with weak intellectual property laws. How should you respond to this dilemma? Later in this chapter, we present a framework for ethical conduct that you can use to analyze this problem and identify an appropriate way forward.

Corporate Social Responsibility

Corporate social responsibility (CSR) refers to operating a business in a manner that meets or exceeds the ethical, legal, and commercial expectations of customers, shareholders, employees, and the communities where the firm does business. Companies that practice CSR aim to do more for the betterment of others than is required by laws, regulations, or special interest groups. Sometimes called corporate citizenship, CSR emphasizes the development of *shared value* for both shareholders and stakeholders, creating a double-win scenario.

Firms that practice CSR behave ethically and support a voluntary, self-regulated business model. Managers develop strategies that thoughtfully considers the social, economic, and environmental impact of company actions and aims to improve the life quality of employees, the community, and society.

4.3 Understand corporate social responsibility.



Source: OlegD/Shutterstock

Policies that protect the natural environment are an important part of corporate social responsibility. Such efforts can go far in reducing environmental decay and raising living standards in poor areas.

Settings of Corporate Social Responsibility

CSR is a broad concept and applicable to various settings, as illustrated in Exhibit 4.5. Workplace CSR focuses on the firm's employees and implies a thoughtful approach to diversity, recruitment, salary, safety, health, and working conditions. Marketplace CSR emphasizes company interactions with customers, competitors, suppliers, and distributors. It implies appropriate behavior regarding product development, marketing, and advertising as well as approaches that suppliers and distributors follow. Environmental CSR refers to the firm's activities to minimize or eliminate the creation of pollutants as well as efforts to improve the natural environment. Community CSR accounts for the firm's activities aimed at benefiting the community and society. It includes employee volunteering programs and philanthropy.²⁹ Indeed, research reveals that companies which support employee volunteer programs, such as charity work and community service, tend to increase employee engagement, loyalty, skills, and personal growth.³⁰

Adhering to CSR principles implies a *proactive* approach to ethical behavior in which firms seek not only to maximize profits but also to benefit society and the environment. Examples of CSR values include:

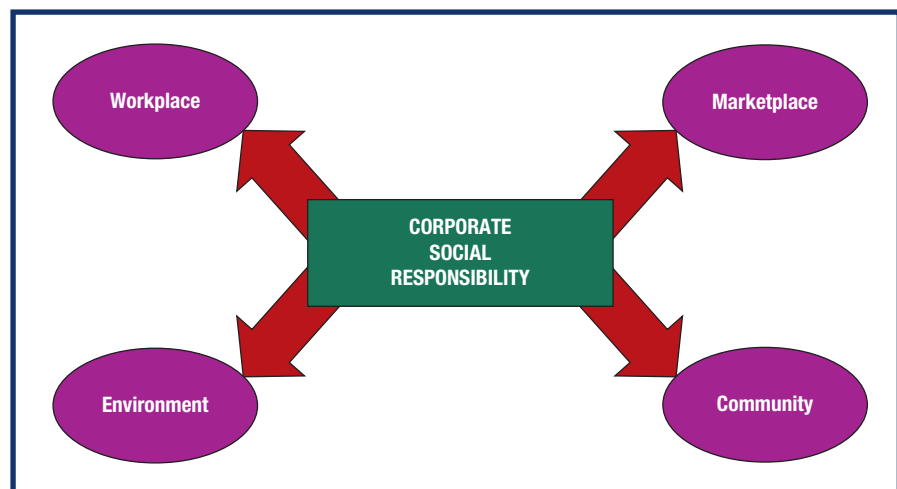
- Avoiding human rights abuses.
- Upholding the right to join or form labor unions.
- Eliminating child labor.
- Avoiding workplace discrimination.
- Protecting the natural environment.
- Guarding against corruption.
- Undertaking philanthropic efforts.³¹

Successes and Failures of CSR

Failure to adopt CSR behaviors can have adverse, even ruinous, consequences. Efforts by the China National Petroleum Company (CNPC) to raise money on the New York Stock Exchange in 2000 were partly depressed by the firm's activities in Sudan, which human rights groups had criticized. The Shell Oil Company has faced protests and lost revenues due to its oil-drilling

EXHIBIT 4.5

Settings for Corporate Social Responsibility



activities in Nigeria, which were seen as harming community interests and generating excessive pollution. Walmart executives were accused of engaging in bribery in Mexico, India, and China. Walmart was required to pay a penalty of nearly \$300 million, and spent more than \$800 million on legal fees, internal investigations, and enhanced ethical compliance. Following the massive BP oil spill in the Gulf of Mexico, BP gas stations in the United States reported that sales fell between 10 and 40 percent due to backlash against the firm. BP lost billions of dollars due to federal penalties, state-mandated grants, and enormous claims. Damage to BP's reputation and sales were considerable.³²

In contrast, countless firms have improved their performance by adopting CSR. The most successful companies focus on maximizing the value of key intangible assets such as reputation and a trustworthy brand name. The African MNE Celtel is a leading exemplar. Africa is one of the world's most underserved telecommunications markets. To address pent-up demand, African native Mo Ibrahim launched Celtel, a mobile communications company. To do so, he had to design, build, and operate phone systems in countries with antiquated or nonexistent infrastructure, including poor roads as well as scarce electricity, water, and other utilities. Celtel developed a plan to deal with corruption. It built schools and clinics, trained local staff, and provided health insurance to employees. Because customers lacked access to modern payment methods, Celtel developed a system of inexpensive, prepaid phone cards. Ibrahim's firm enjoyed huge success and improved conditions for millions of people and businesses around Africa.³³

Exhibit 4.6 summarizes additional CSR initiatives firms have undertaken worldwide. For example, Africa accounts for the most deaths from AIDS, but few Africans can afford to pay the high cost of medications to treat the terrible disease. GlaxoSmithKline (GSK) offers its AIDS medications to Africans at or below its production costs. Indeed, GSK sells 90 percent of its vaccines, in volume terms, at not-for-profit prices to customers in the developing economies.³⁴ In Scotland, the large utility firm Scottish and Southern Energy (SSE) emphasizes sustainability in providing energy to its customers. In Ireland, the firm provides electricity through numerous wind farms. Only two of SSE's power plants are fueled by coal, which is more polluting than other energy sources.³⁵

Company	Industry	Sample Accomplishments
ABN AMRO (Netherlands)	Financial services	Finances various socially responsible projects, including biomass fuels and micro enterprises
SC Johnson (United States)	Consumer products	Shifted packaging to lightweight bottles, saving millions of kilograms of consumer waste annually
GlaxoSmithKline (United Kingdom)	Pharmaceuticals	Devotes substantial R&D to poor-country ailments, such as malaria and tuberculosis; was first to offer AIDS medication at cost
Hindustan Unilever (India)	Consumer products	Provided microfinance and training to 65,000 poor women to start their own wholesale firms, doubling their incomes
Nokia (Finland)	Telecommunications	Makes telephones for low-income consumers; has been a leader in environmental practices such as phasing out toxic materials
Norsk Hydro (Norway)	Oil and gas	Cut greenhouse gas emissions by 32 percent; consistently measures the social and environmental impact of its projects
Philips Electronics (Netherlands)	Consumer electronics	Top innovator of energy-saving appliances and lighting products as well as medical devices for developing economies
Tesla (United States)	Automobiles	A world leader in developing electric vehicles

EXHIBIT 4.6

Corporate Social Responsibility: A Sampling of MNE Accomplishments

Sources: Pete Engardio, "Beyond the Green Corporation," *Business Week*, January 29, 2007, pp. 50–64; Fisk Johnson, "How I Did It: SC Johnson's CEO on Doing the Right Thing, Even When It Hurts Business," *Harvard Business Review*, April, 2015, pp. 33–36; Kasturi Rangan, Lisa Chase, and Sohel Karim, "The Truth About CSR," *Harvard Business Review*, January/February, 2015, pp. 40–49.

Denmark enacted laws that require firms to incorporate CSR activities and report on them in their financial reports. In the United Kingdom, large companies are required to consider community and environmental issues in managing the firm. Legislation in India encourages companies to spend a proportion of their profit on CSR activities.³⁶ Increasingly, many consumers favor products made by firms with strong CSR.

In addition to profit-seeking focal firms, more nongovernmental organizations (NGOs) are undertaking international CSR initiatives, often in conjunction with multinational firms. For example, such NGOs as CARE, Médecins Sans Frontières, and the Bangladesh Rural Advancement Committee work to reduce global poverty and frequently partner with private companies to provide vital products and services.³⁷

4.4 Understand sustainability.

Sustainability

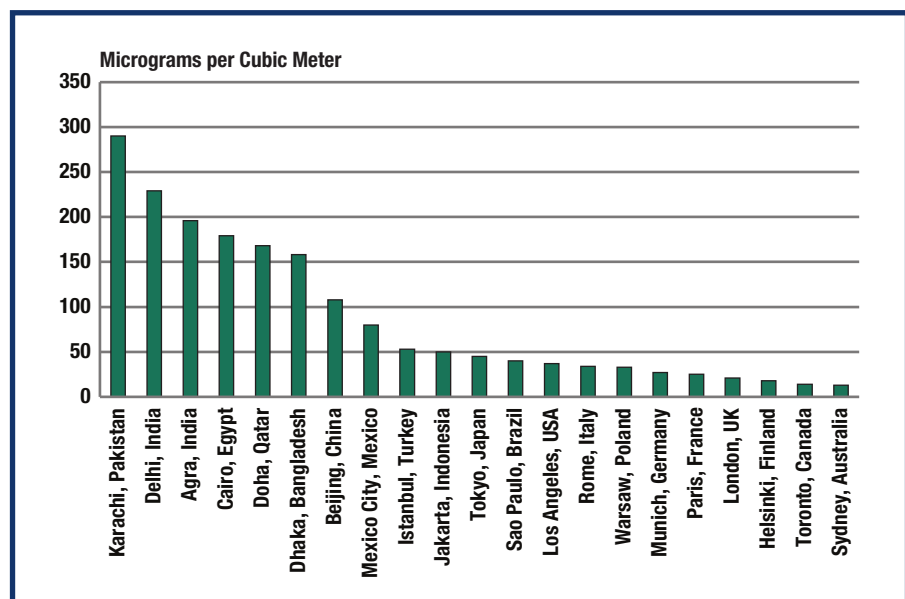
Sustainability implies the development and execution of company practices that avoid harming the ability of future generations to meet their needs. It is endorsed by economic development experts, environmentalists, and human rights activists. The sustainable firm carries out value-chain activities in ways that protect and preserve economic, social, and natural environments. For example, sustainable firms pay fair wages, ensure worker safety, and avoid emitting toxic waste. Examples of sustainable practices include:

- **Beneficial agricultural practices.** The appropriate use of crop rotation and natural pesticides improves the quality of crops grown and preserves land for use by future farmers.
- **Water conservation.** Clean water is an increasingly scarce resource worldwide. Companies that depend heavily on water, such as Coca-Cola, seek ways to recycle used water and minimize waste.
- **Air quality protection.** As shown in Exhibit 4.7, industrialization generates much air pollution. Industrial practices to reduce air pollution improve life quality and enhance competitive advantages.
- **Reduced energy and fuel consumption.** Efforts to support the natural environment include regulation of fossil fuel usage and government incentives to use renewable energy sources.
- **Increased use of solar and wind energy.** Cost-effective solar and wind energy can contribute enormously to reducing dependence on nonrenewable and polluting power sources.
- **Improved work processes.** Modifying work processes to improve sustainability reduces corporate costs and supports the natural environment.

EXHIBIT 4.7

Air Pollution in Selected Cities (particulate matter concentration in micrograms per cubic meter)

Sources: CBS News, “The Most Polluted Cities in the World,” 2018, www.cbsnews.com; World Bank, *World Bank Development Indicators* (Washington, DC: World Bank, 2017); World Health Organization, “Ambient (Outdoor) Air Pollution Database, by Country and City,” April 4, 2017, www.who.int.



A Sustainable Business Simultaneously Pursues Three Types of Interests

- *Economic interests* refer to the firm's economic impact on the localities where it does business. Management considers the effect of the firm's activities on such local concerns as job creation, wages, tax flows, disadvantaged communities, public works, and other areas where the firm can contribute positively to local economic interests.
- *Social interests* refer to how the firm performs relative to societies and social justice, often termed *social impact*. The firm with a strong social interest optimizes work conditions and diversity in hiring. It avoids using sweatshops, child labor, and other practices that harm workers. Instead, the sustainable firm provides safe work environments, health insurance, retirement benefits, and educational opportunities for employees.
- *Environmental interests* refer to the extent of the firm's contribution to preserving environmental quality, commonly known as *environmental impact*. This concept refers to reducing the effect of the firm's value-chain activities on the natural environment. The sustainable firm maximizes its use of recycled or renewable raw materials and environmentally friendly energy. It minimizes pollutants, designs production lines to use water and energy efficiently, and constantly seeks ways to reduce waste. Sustainable business practices tend to reduce the firm's reliance on polluting fossil fuels. Many firms establish a green purchasing policy, through which they procure inputs that support environmental interests.

Sources: John Blewitt, *Understanding Sustainable Development* (London: Earthscan, 2008); F. Reimann Kaumann, M. Ehrigott, and J. Rauer, "Sustainable Success," *Wall Street Journal*, June 22, 2009, retrieved from www.wsj.com; Nancy Landrum and Sandra Edwards, *Sustainable Business: An Executive's Primer* (New York: Business Expert Press, 2009).

Company Role in Sustainability

Sophisticated companies, large or small, view sustainability as an opportunity to reduce waste, increase efficiency and effectiveness, and generally create competitive advantage.³⁸ Businesses function by employing resources and raw materials derived from the natural environment. Industrial activities can produce smog, acid rain, and other toxins that harm the atmosphere. Many industrial firms use or produce synthetic chemicals and materials that contain hazardous substances. Consumer and industrial products are themselves a major source of toxic waste.³⁹

Firms consume vast quantities of water resources, contributing to the creation or expansion of deserts (desertification) and loss of important ecosystems around the world. For example, Brazil recently has endured a drought of historic proportions, and some experts believe loss of Amazon rain forest is an important cause.⁴⁰ Many countries endure chronic water shortages, and industrial activity pollutes clean water supplies. Residential and industrial activity results in land loss and the destruction of ecosystems needed for healthy natural environments. Long-term, successful business performance necessitates healthy ecosystems.

Businesses are major consumers of all the natural environment offers and, hence, must take pains to ensure ecological sustainability. Reversing environmental damage requires industrialized countries to reduce their emissions of pollutants substantially. The pace with which resources and raw materials are depleted should not exceed their rate of regeneration. The rate of waste production should not exceed the environment's ability to absorb it. Thus, firms increasingly seek ways to employ renewable resources and minimize pollutants in their operations. Because of their size, MNEs are among the most



Source: Riccardo Lennart Niels Mayer/123rf.com

Firms in the paper, textiles, and steel industries are major water consumers. As water becomes scarce, numerous multinational firms are undertaking efforts to conserve this critical resource.

important stewards of the environment through skillful use of innovative technologies, improved water productivity, management of shortages in vulnerable areas, and planning that incorporates sustainability practices.

The most advanced companies monitor suppliers to ensure that they use sustainable practices. For example, following charges that some of its Indian subcontractors were using forced child labor, GAP withdrew a line of children's wear from its clothing stores worldwide. H&M was accused of employing children as young as 14 in clothing factories in Myanmar. Sustainable firms usually opt for local suppliers to reduce the pollution that transporting goods long distances causes.⁴¹

At the consumer products company Unilever, management has committed to tackling big social and environmental problems such as pollution, disease, and poverty. The firm aims to halve its environmental footprint and ensure that sourced foods are grown using sustainable farming practices. Unilever's global hand-washing campaign aims to reduce diarrhea and other noxious diseases in Africa and Asia. The firm is also developing a laundry detergent that can clean clothes in a few minutes at any water temperature, thereby saving energy and water. Unilever's plan includes 60 targets, such as sourcing "75% of the paper and board for our packaging from certified sustainably managed forests or recycled material." CEO Paul Polman ensures that CSR and sustainability are incorporated into all of the firm's strategy making.⁴²

BMW introduced a series of electric cars to support the firm's sustainability goals. The cars have carbon-fiber bodies to reduce weight and save fuel. Recycled aluminum is used in the chassis, and interior panels and seats are made of hemp fibers and recycled water bottles. Lithium-ion batteries allow users to drive for up to 100 miles before charging. Smartphone apps show the way to charging stations and smart parking spots. BMW is making such features standard on a wide range of vehicles for sale worldwide.⁴³

Consumers increasingly shop online from suppliers like Amazon and Alibaba and have goods delivered to their homes in cardboard boxes. Germany, South Korea, the United Kingdom, and the United States are among nations with the most online retail consumers. Amazon Prime members alone number more than 75 million shoppers worldwide. Online shopping generates an enormous number of cardboard boxes that end up in landfills. Personalized freight services increase carbon dioxide and other exhaust gases from delivery trucks. Amazon and other retailers are trying to address the problem by reducing packaging and using less polluting delivery services such as drones and electric trucks.⁴⁴

Like CSR, sustainable practices pay off in various ways such as promoting a strong corporate reputation, the ability to hire and retain superior employees, cost savings from more efficient production, better linkages with suppliers, and smoother relations with foreign governments.

Achieving sustainability often requires the firm to be flexible and creative. A good example is Coca-Cola, which had to deal with water sustainability challenges. As water resources dwindled in some countries, Coke began to experience conflicts with communities and other water users, especially in India. To address such challenges, Coke developed a water sustainability program that goes well beyond efficiency and legal compliance needs alone. Management devised global projects that protect water resources and ensure access to clean drinking water. Coke mobilized the international community to anticipate and deal with ever more severe water crises worldwide.⁴⁵

MyLab Management Watch It! 2

If your professor has assigned this, go to the Assignments section of www.pearson.com/mylab/management to complete the video exercise titled Root Capital International Strategy.

4.5 Know the role of corporate governance.

The Role of Corporate Governance

Implementing ethical conduct, CSR, and sustainability is challenging for most firms, especially those with extensive operations across many countries. Corporate governance provides the means through which the firm's directors and managers undertake such behaviors. Leading companies implement corporate governance by creating (a) a *set of values* that serve as a guide for employees and (b) a *set of ground rules* for guiding behavior, which include criteria for acceptable decision-making, used by all employees. The values and ground rules should be established in the firm's code of ethics and code of conduct documents.

A **code of ethics** is a document that describes the *values and expectations* that guide decision making by all employees in the firm. The code aims to function like a moral compass for the firm's operations worldwide. It should be designed to ensure that any employee can identify ethical problems and distinguish between right and wrong actions. The code should be general enough to apply to any ethical challenge that confronts the firm. It should list the general principles that guide daily decisions and interactions with customers, employees, and partners. The code should be created by senior management and disseminated throughout the firm. It should be translated into all languages the firm uses in its international operations.⁴⁶

The **code of conduct** translates the code of ethics into specific rules regarding behaviors and practices that are prohibited or required. It identifies the consequences for specific violations and the conditions for continued employment. Inappropriate behaviors the code of conduct addresses might include sexual harassment, conflicts of interest, racial discrimination, and acceptance of gifts. Due to differing cross-national laws and practices, developing a single code to cover the firm's operations worldwide is often impractical. Many companies develop codes of conduct for individual countries or regions to address local conditions. In numerous Asian countries, for example, gift giving is relatively acceptable and even expected. In some Muslim countries, interaction between male and female employees is discouraged.

Integrating local codes with the firm's global standards is challenging. One approach is to have such codes developed broadly by cross-functional and cross-national teams that represent the interests of headquarters and subsidiaries as well as specific functional areas. Managers native to specific countries are positioned best to identify and clarify approaches in those countries. Senior management commitment to appropriate behavior is critical to fostering ethics and CSR in international operations and should regularly communicate the importance of ethical and conduct codes. The firm should devise continuing education programs to ensure that employees understand and practice ethical and conduct codes. In addition to helping ensure ethical conduct, CSR, and sustainable practices, implementing a code of ethics and a code of conduct also foster trust with customers, employees, and partners.⁴⁷

Embracing Ethical Behavior

In a world ever sensitive to social and environmental issues, managers increasingly undertake the following types of practices.

- Build internal and external capabilities to enhance the firm's contribution to the local community and global environment.
- Ensure that diverse voices are heard by creating organizational structures that employ managers and workers from around the world.
- Develop global ethical standards and objectives that are communicated and implemented across the firm worldwide.
- Train managers in global ethical principles and integrate these into managerial responsibilities.
- Develop closer relations with foreign stakeholders to understand their needs better and jointly work toward solutions.

Ethical Standard Approaches for Corporate Governance

Scholars have devised five ethical standards approaches that managers can use to examine ethical dilemmas. These are summarized in the following box.⁴⁸

Utilitarian Approach	Rights Approach	Fairness Approach	Common Good Approach	Virtue Approach
The best ethical action is the one that provides the most good or the least harm. It produces the greatest balance of good over harm to customers, employees, shareholders, the community, and the natural environment.	The best action protects and respects the moral rights of everyone involved. It is based on the belief that, regardless of how you deal with an ethical dilemma, human dignity must be preserved.	The best action treats everyone equally and fairly. Workers should be paid a fair wage that provides a decent standard of living, and colleagues and customers should be treated as we would like to be treated.	The best action emphasizes the welfare of the entire community or nation. It asks what action contributes most to the quality of life of all affected people. Respect and compassion for all, especially the vulnerable, are the basis for decision making.	The best action emphasizes virtues that provide for the full development of our humanity. The most important virtues are truth, courage, compassion, generosity, tolerance, love, integrity, and prudence.

Code of ethics

A document that describes the values and expectations that guide decision making by all employees in the firm.

Code of conduct

A document that translates the code of ethics into specific rules regarding behaviors and practices that are prohibited or required.

Using these approaches to analyze ethical dilemmas can be challenging because they occasionally conflict with each other. Not everyone agrees on which standard to use in all situations. Different cultures adhere to differing norms of morality and human rights and basic standards or norms of right and wrong. Many ethical dilemmas are complex, and proposed approaches may not provide adequate guidance in determining the best course of action. Nevertheless, each standard is useful because it helps guide ethical behavior in almost any predicament. In most cases, they lead to similar solutions.

A Global Consensus

Incorporating ethics, CSR, and sustainability into global operations is a path to long-term superior performance. Various resources are available to assist managers. International organizations such as the United Nations, the World Bank, and the International Monetary Fund have launched programs to combat international corruption.

The International Chamber of Commerce has adopted Rules of Conduct to Combat Extortion and Bribery, and the United Nations issued a Declaration against Corruption and Bribery in International Commercial Transactions.

The Organisation for Economic Co-operation and Development (OECD) has developed an anti-bribery agreement, which was signed by its 30 member nations (essentially, all the advanced economies) plus several Latin American countries.⁴⁹

The United Nations Global Compact (see www.unglobalcompact.org) is a policy platform and practical framework for companies committed to sustainability and responsible business practices. It seeks to align business operations and strategies with universally accepted principles in the areas of human rights, labor, corruption, and the natural environment. It is the world's largest voluntary corporate citizenship initiative, representing thousands of businesses in more than 135 countries.

The Global Reporting Initiative (www.globalreporting.org) pioneered the development of the most widely used sustainability reporting framework. It sets out the principles and indicators that organizations can use to measure and report their economic, environmental, and social performance. Today, most large MNEs produce sustainability reports, many following the GRI guidelines.

Going Deep, Wide, and Local

Ultimately, pursuing a culture of ethical behavior requires the firm to go deep, wide, and local. *Going deep* means institutionalizing appropriate behavior in the organization's culture so it becomes part and parcel of strategy. *Going wide* implies a continuous effort to understand how CSR and sustainability affect every aspect of the firm's operations worldwide. *Going local* goes hand in hand with globalization. It requires the firm to examine its global operations to identify and improve specific local issues that affect customers, competitive position, reputation, and any other dimension that affects the firm's operations worldwide.⁵⁰

Benefits of Corporate Governance

Corporate governance that ensures ethical practices, CSR, and sustainability provides numerous benefits to the firm.⁵¹ These benefits include:

- *Increased employee commitment.* Firms that practice ethics, CSR, and sustainability find it easier to attract and retain employees. When workers are proud of their employer, they tend to work more diligently and increase productivity.
- *Increased customer loyalty and sales.* Many customers prefer to patronize businesses that emphasize ethical practices. Best practices that benefit society enhance sales prospects.
- *Improved reputation and brand image.* Operating ethically and responsibly enhances the firm's public image, customer preference, and the ability to attract capital. Firms with a strong image are less likely to conflict with value-chain members and government authorities.
- *Reduced likelihood of government intervention.* The increased trust, transparency, and accountability that follow from applying superior corporate governance can reduce the likelihood of governments imposing burdensome regulations and other forms of government intervention.

- *Reduced business costs.* Various efficiencies arise from CSR and sustainable practices, including the ability to hire quality employees, reduced employee turnover, and decreased regulatory scrutiny. Sustainability efforts such as recycling and using alternative energy help reduce waste and the cost of inputs.
- *Improved financial performance.* Several recent studies have shown that companies with sound values, strong ethical behavior, and strong social and environmental practices have significantly greater rates of growth than those firms focused only on company profits.

Read the *You Can Do It: Recent Grad in IB* feature, which profiles Javier Estrada, who has gained much experience working on poverty and sustainability issues in various emerging markets and developing economies.

You Can Do It

RECENT GRAD IN IB



JAVIER ESTRADA

Javier's major: Business

Objectives: Integrating business skills with social planning in a public agency and pursuing a career in politics

Jobs held since graduating:

- United Nations World Food Programme in Guatemala and Honduras
- Director of Research, Bates Advertising, Dominican Republic
- Manager in a major charity in Mexico

Source: Javier Estrada

Javier Estrada graduated from a state university several years ago with a bachelor's degree in business. He moved to the Dominican Republic, where he took a research position in the local office of Bates Advertising, a global ad agency that handled accounts such as Wendy's, Purina, and Bell South. Along the way, Javier also worked in the social sector. He served as a coordinator in the United Nations World Food Programme in Guatemala and Honduras. He also became the manager of a charity in Mexico.

Success Factors

"My parents felt strongly that our lives should be influenced not only by the quality of our education, but also by our travels In school we were among the most

traveled kids." Javier was lucky enough to visit several countries during his teens and twenties. He comments: "You get to know yourself when you're completely alone in a new culture and establishing a network of friends and work contacts." International experience contributed to Javier's independent spirit and his ability to function successfully around the world.

Javier enjoyed going to other countries and meeting different people. "My job provided the chance to help companies and customers. I would not have gotten the job if I had not worked hard in school. Management training provided me with the skills to perform effectively. Sensitivity is important, since you need to be able to communicate with people who are culturally different from you. You need a strong

empathy for your customers. You need to identify which research questions are best."

What's Ahead?

Javier has ever-higher goals for his career. He has been long concerned about poverty issues in Latin America, and his experiences with the United Nations affected him profoundly. Javier earned a master's degree in social policy and planning from the London School of Economics. Having worked in both business and development, Javier found his passion in integrating his business skills with social planning at the governmental level. Recently, Javier worked for a major charity organization in Mexico. He says, "I need to dream big."

Source: Photo courtesy of Javier Estrada.

4.6 Learn how to apply the framework for making ethical decisions.

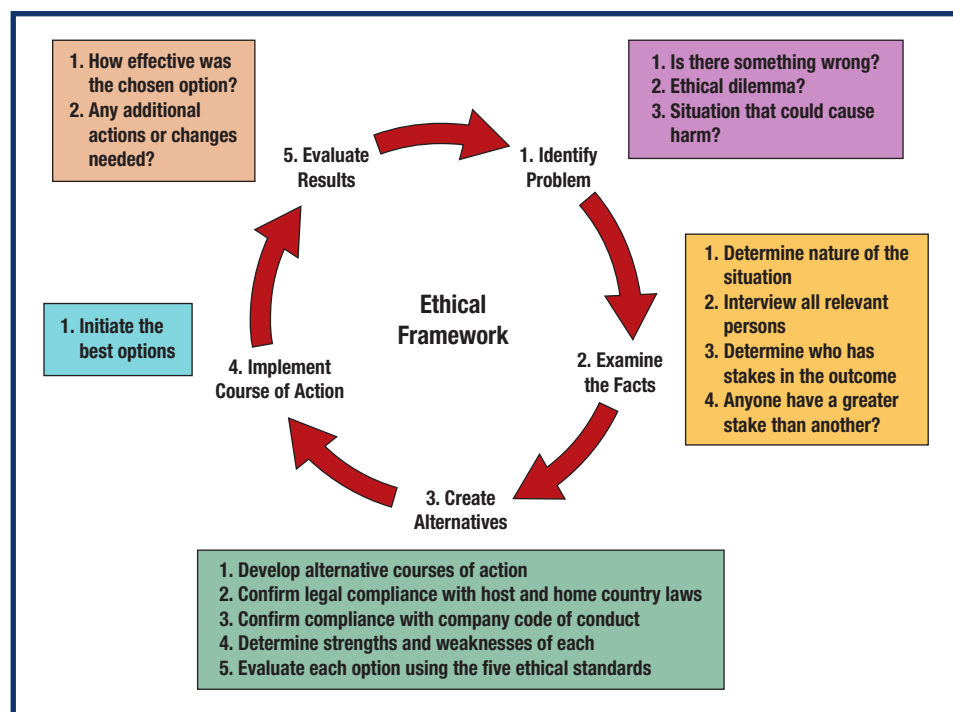
A Framework Tool for Making Ethical Decisions

Scholars suggest that managers follow a systematic approach to resolving ethical dilemmas. Exhibit 4.8 presents a five-step framework for arriving at ethical decisions that will help you arrive at appropriate solutions to ethical dilemmas.⁵² With practice, it can become second nature. The steps in the framework follow.

1. *Identify the problem.* The first step is to acknowledge the presence of an ethical problem. Ask questions such as: Is something wrong? Is an ethical dilemma present? Is there a situation that might harm personnel, customers, the community, or the nation? In international business, recognizing the issue can be tricky because subtleties of the situation may be outside your knowledge or experience. Often, it is best to rely on your instincts. If some action feels wrong, it probably is.
2. *Examine the facts.* Determine the nature and dimensions of the situation. Have all the relevant persons and groups been consulted? What individuals or groups have a stake in the outcome? How much weight should be given to the interests of each? Do some parties have a greater stake because they are disadvantaged or have a special need? This stage is often challenging because determining specific details and distinguishing facts from irrelevant information is challenging. The process often involves interviewing personnel and stakeholders who may offer differing versions or opinions about the issue at hand. The manager's task is to identify and validate the most useful, valid information that makes the true nature of the problem clear.
3. *Create alternatives.* Identify potential courses of action and evaluate each. Initially, consistent with the pyramid of ethical behavior, review any proposed action to ensure that it is legal. If it violates host or home country laws or international treaties, it should be rejected. Next, review any proposed action to ensure that it is acceptable according to company policy, the firm's code of conduct, and its code of ethics. If discrepancies are found, the action should be rejected. Finally, evaluate each proposed action to assess its consistency with accepted ethical standards, using the approaches described earlier:
 - Utilitarian: Which action results in the most good and least harm?
 - Rights: Which action respects the rights of everyone involved?
 - Fairness: Which action treats people most fairly?
 - Common good: Which action contributes most to the overall quality of life of the people affected?
 - Virtue: Which action embodies the character strengths you value?

EXHIBIT 4.8

Framework for Arriving at Ethical Decisions



The goal is to arrive at the best decision or most appropriate course of action. It might be useful to enlist the aid of local colleagues familiar with the situation to provide insights and help generate options. Assess the consequences of each action from the perspective of all parties who will be affected by it. Any decision should be tested by asking whether you would feel comfortable explaining it to your mother, a colleague you respect, or a valued mentor. If you had to defend the decision on television, would you be comfortable doing so?

- *Implement the course of action.* Put the chosen plan into action. This implies making new rules, processes, or procedures and putting these into effect. Implementation is critical because it determines the success or failure of the chosen action. Managers need to be particularly diligent at this stage to ensure that the action is carried out according to plan.
- *Evaluate results.* After the decision is implemented, management will need to evaluate it to see how effective it was. How did it turn out? If you had it to do again, would you do anything differently? Results evaluation may require collecting, analyzing, and using information to answer questions about the chosen course of action. The goal is to ensure that the action achieves its intended effect and discover whether the firm should modify the approach or pursue a different one.

To illustrate briefly, let's revisit the example of you as a manager visiting a company factory in Colombia, where you discover child labor. Without the children's income, their families might go hungry, or the children could turn to illicit activity such as street crime. Having identified the problem, you examine facts by consulting colleagues at both the plant and the headquarters. You seek information about the status of the employed children as well as local law and customs on child labor. You then create alternative possible solutions, ensuring that they are legal and consistent with company policy. Keeping the five ethical standards in mind, you evaluate each proposed action. Finally, you choose and implement the best course of action and evaluate its effectiveness.

Managers must make ethical behavior, CSR, and sustainability part of company activities and operations. MNE pursuits generate environmental harm and bring firms into contact with various activities—from R&D to manufacturing to marketing—that can pose various ethical dilemmas. Business executives should balance their obligation to shareholders with explicit contributions to the broader public good. Most executives agree that generating high returns for investors should be accompanied by a focus on providing good jobs, supporting social causes in local communities, and going beyond legal requirements to minimize pollution and other negative effects of business.

CLOSING CASE

Scandal at Volkswagen

The U.S. Environmental Protection Agency and the California Air Resources Board discovered that diesel vehicles produced and sold by Volkswagen (VW) from 2009 to 2015 had been equipped with software that enabled them to “cheat” on air pollution emissions tests. Authorities found the software was able to detect emissions tests by monitoring speed, engine operation, and other factors. When such testing was detected, the software immediately switched vehicles to a “test mode,” and the engine would run below normal power and performance levels. In this way, tested vehicles gave false readings of emitted air pollutants. Once back on the road, the software switched the vehicle out of test mode. In this way, VW was able to systematically evade environmental protection laws in the United States.

The evasive software gave VW a competitive advantage over its rivals in the large U.S. car market. Engineering experts initially discovered the emissions test inconsistencies. The experts were surprised to find that the diesel vehicles were emitting pollutants several times above the limit prescribed by U.S. law. Subsequent investigation revealed that some 11 million diesel cars had been equipped with the software, apparently for the purpose of providing deceptively positive results on emission tests.

Once the magnitude of the scandal was revealed, the value of VW stock crashed, and billions of dollars had to be set aside to cover resulting costs. Countless vehicles were recalled, and company executives became subject to possible criminal charges.

The Volkswagen Group was founded in 1937 and is headquartered in Wolfsburg, Germany. VW makes and sells more than 10 million cars, trucks, and vans annually. VW operates in more than 150 countries, with recent annual revenues in excess of \$250 billion. The automotive industry dominates Germany's economy. The combined revenues of VW, Daimler and BMW amount to about 15 percent of Germany's gross domestic product. The nation's economic strength is rooted in the belief that German production is reliable and trustworthy, with superior engineering prowess.

Background on the Scandal

Investigators attempted to find out why VW might have knowingly sought to cheat on emissions tests. Some suggested the firm was seeking to increase its presence in the competitive U.S. market, and the ability to perform well on emissions tests may have helped control costs as sales of VW sport utility vehicles increased. Others

noted that cheating had become prevalent in the auto industry and that other top automakers such as Ford, Toyota, and General Motors had been implicated.

Automakers face a tension between profit-making goals and social responsibility. Rather than emphasizing the “triple bottom line” of people, planet, and profit, VW may have put too much emphasis on financial profits. Some suggested that VW was betting on the trade-off between potential punishment for cheating versus prospects for big profits in the U.S. market. For large-scale sales of defective and dangerous vehicles, General Motors and Toyota each were fined only about \$1 billion, a small sum compared to these firms’ annual sales. VW management might have calculated that the potential loss of a scandal would be less than potential market gains from selling vehicles equipped with “defeat devices” in the large U.S. market.

Impact of the Scandal

VW experienced various losses from the scandal. Initially, the firm’s stock price tumbled by more than 30 percent, from about \$160 to \$110 per share. Many months passed before VW’s stock price returned to earlier levels. In addition, VW had to pay a \$4.3 billion settlement to the U.S. government. VW made plans to spend up to \$25 billion to address claims from owners, dealers, regulators, and states and to buy back about 500,000 polluting vehicles. Costs of the scandal were unexpectedly high, and complying with the settlements proved complex and time-consuming. The governments of Canada, France, Germany, Italy, South Korea, and the United Kingdom opened investigations to check if VW was cheating on emissions tests in their countries too. The firm had to reduce its workforce by thousands of employees to cover the costs of the scandal, an outcome that affected the lives of countless people.

VW had positioned its vehicles as “attractive, safe, and environmentally sound,” but such marketing campaigns seemed

misleading once the emissions scandal broke. On social media, consumers claimed the scandal affected the trust they once felt toward VW and expressed concerns about the health consequences of many pollution-emitting vehicles on the road.

Despite the negative publicity, however, many consumers were unaware of the scandal, and market surveys in Germany, the United States, and elsewhere suggested that most consumers continued to trust the brand. Profits have remained strong, and the firm recently became the global leader in automotive volume sales.

Other Consequences

In the days following revelation of the scandal, CEO Martin Winterkorn stepped down and VW suspended five high-ranking executives. Some top engineers were arrested. In the meantime, the firm announced plans to launch a line of all-electric vehicles, aiming to position itself as a leader in green transportation. Before the scandal, VW’s corporate culture had been described as “aggressive.” The firm set ambitious goals and pushed managers to achieve success. After the scandal, newly appointed CEO Matthias Mueller stated that changes would “require us—following the serious setback as a result of the diesel issue—to learn from mistakes made, rectify shortcomings and establish a corporate culture that is open, value-driven and rooted in integrity.”

VW plans to streamline operations to reduce costs incurred by the scandal. Management will downsize the firm’s components business and reduce its workforce by 30,000 people. However, VW expects to create 9,000 new jobs by producing more electric cars.

The scandal has intensified regulatory scrutiny of the auto industry, especially environmental standards. Automakers worldwide continue to confront the tension between strict environmental controls, intense global competition, and the relentless drive for profitability.

AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Ethical Understanding and Reasoning, Analytical Thinking, Diverse and Multicultural Work Environments, Reflective Thinking.

Case Questions

- 4-4. What does the case suggest about the value of ethical behavior? Do you think VW was penalized enough for its wrongdoing? Why or why not? What does VW gain through its efforts to introduce a culture that is rooted in integrity and responsible behavior?
- 4-5. Most countries lack sufficient laws or enforcement to adequately protect the natural environment. What are the consequences of this? What can nations do to better protect the environment?
- 4-6. Who should be held responsible for the VW emission scandal: VW senior management, engineers, or government regulators? Justify your answer.
- 4-7. What steps can VW take to prevent similar incidents from occurring in the future?


Sources: BBC News, “VW Plans Huge Investment to Become Electric Cars Leader,” June 16, 2016, www.bbc.com; Nick Carey and David Shepardson,

“VW Pleads Guilty in Diesel Emissions Case as Part of \$4.3 Billion Settlement,” *Washington Post*, March 10, 2017, www.washingtonpost.com; Jack Ewing, “Engineering a Deception: What Led to Volkswagen’s Diesel Scandal,” *The New York Times*, March 16, 2017, www.nytimes.com; Michael Le Page, “How Did Volkswagen Cheat in Tests and Can It Fix Affected Cars?,” *New Scientist*, September 30, 2015, www.newscientist.com; Los Angeles Times, “Volkswagen to Shed 30,000 Jobs to Cut Costs After Emissions-Cheating Scandal,” November 18, 2016, www.latimes.com; Nazanin Mansouri, “A Case Study of Volkswagen Unethical Practice in Diesel Emission Test,” *International Journal of Science and Engineering Applications* 5, No. 4 (2016), pp. 211–216; Kartikay Mehrotra and David Welch, “Why Much of the Car Industry Is Under Scrutiny for Cheating,” *Bloomberg*, January 10, 2018, www.bloomberg.com; Kevin O’Marah, “VW Scandal: Awareness and Accountability,” *Forbes*, September 24, 2015, p. 97; Natasha Terry-Armstrong, “The VW Scandal—The High Cost of Corporate Deceit,” *Busidate* 24, No. 1 (2016), pp. 9–13; *Economist*, “A Long Road to Recovery; VW,” November 12, 2016, p. 59; Trefis Team, “Volkswagen Is the New Global Sales Leader: What It Means,” *Forbes*, February 1, 2017, www.forbes.com.

This case was written by Bohua Fu under the supervision of Professor Gary Knight.

END-OF-CHAPTER REVIEW

MyLab Management

Go to www.pearson.com/mylab/management to complete the problems marked with this icon .

Key Terms

code of conduct 141	corruption 130	normativism 129
code of ethics 141	ethical dilemma 129	relativism 129
corporate governance 126	ethics 126	sustainability 126
corporate social responsibility (CSR) 126	intellectual property 134	
	intellectual property rights 134	

Summary

In this chapter, you learned about:

- **Components of ethical behavior and their importance in international business**

Ethics are the moral principles and values that govern the behavior of people, firms, and governments. Ethical standards vary around the world. Relativism is the belief that ethical truths are not absolute but differ from group to group. Normativism holds that ethical standards are universal, and firms and individuals should uphold them consistently around the world. An ethical dilemma is a predicament involving major conflicts among different interests. Determining the best course of action is confounded by several possible solutions that may be equally justifiable.

- **Ethical challenges in international business**

Companies encounter various ethical challenges, including violations of intellectual property, corruption, bribery, and unethical management practices. Corruption implies obtaining power, personal gain, or influence through illegitimate means. Intellectual property refers to ideas or works created by individuals or firms. Governments aim to protect intellectual property, but protection is not guaranteed in much of the world.

- **Corporate social responsibility**

Maintaining corporate social responsibility (CSR) means operating a business in a manner that meets or exceeds the ethical, legal, commercial, and public expectations of stakeholders. Sustainability refers to meeting humanity's needs without harming future generations. In addition to complying with laws, regulations, and basic ethical standards, prudent MNEs emphasize corporate social responsibility in their activities. A strong business rationale for CSR includes the firm's ability to motivate employees and develop

superior strategy. Failure to develop a CSR has important negative consequences for the firm.

- **Sustainability**

Sustainable businesses simultaneously pursue three types of interests: economic, social, and environmental. They maximize the use of recycled or renewable materials and environmentally friendly energy; reduce waste in manufacturing and minimize harmful air and water pollution; provide health insurance, training, and care for employees in various other ways. They are active in the local community with initiatives in education, health care, and environmental protection. Sustainable firms choose and work with suppliers that adhere to high social and environmental standards.

- **Corporate governance**

Corporate governance is the system of procedures and processes by which corporations are managed, directed, and controlled. Management utilizes corporate governance to implement ethics, CSR, and sustainability, which support the firm's best interests. Scholars have devised five standards managers can use to examine ethical dilemmas, based on utilitarianism, rights, fairness, common good, and virtue. Senior managers should develop a code of ethics that describes what the firm expects of its employees when facing ethical dilemmas.

- **A framework tool for making ethical decisions**

Scholars have devised a five-step framework for making ethical decisions. Initially, the manager should recognize the existence of an ethical problem. The next steps are to get the facts, evaluate alternative courses of action, implement the decisions, and evaluate the results. Ethical behavior and CSR must be part of managers' day-to-day pursuits. Various resources from organizations such as the United Nations and the World Bank are available to assist managers.

Test Your Comprehension

AACSB: Ethical Understanding and Reasoning, Analytical Thinking, Diverse and Multicultural Work Environments, Application of Knowledge

- 4-8. Distinguish between ethics and corruption in international business.
- 4-9. Describe typical ethical problems that firms encounter in international business.
- 4-10. What is the Corruption Perceptions Index, and how can a manager use it to assess international risk?
- 4-11. What is intellectual property? What industries are most affected by threats to intellectual property?
- 4-12. How can the most justifiable solution to a dilemma be identified?
- 4-13. What is an ethical dilemma? Give an example of an ethical dilemma that MNEs encounter abroad.
- 4-14. Distinguish relativism and normativism. Which one should the firm apply in its activities?
- 4-15. Distinguish between workplace, marketplace, environmental, and community CSR. Why is it important to establish all four approaches?
- 4-16. What is a sweatshop, and what are the main characteristics used to identify one?
- 4-17. What are the three key areas that a sustainable business tries to address?
- 4-18. How does an organization's management use corporate governance to implement ethics and CRS?
- 4-19. Why should ethical behavior be a part of a manager's everyday activities?
- 4-20. Describe the steps in the framework for ethical conduct.

Apply Your Understanding

AACSB: Written and Oral Communication, Ethical Understanding and Reasoning, Analytical Thinking, Application of Knowledge

- 4-21. *Ethical Dilemma:* You were recently hired by ThunderCat Corporation, a major aircraft producer with a manufacturing presence in numerous countries. ThunderCat's sales personnel constantly travel the world, selling fighter jets and commercial aircraft to airlines and foreign governments. You are keenly aware that countries vary enormously in terms of culture, laws, and political systems. Top management has asked you to develop a code of ethics to guide ThunderCat employees in their interactions anywhere in the world. Given the diversity of countries where ThunderCat operates, what sort of code will you develop? What issues should you consider? Given the diversity of countries around the world, is it possible to develop a code that guides ethical behavior everywhere?
- 4-22. *Ethical Dilemma:* Royal Dutch Shell has been doing business in Nigeria since the 1920s and has announced new plans to develop oil and gas projects there. However, over the years, Shell has experienced a series of complex issues. Its operations are centered in Nigeria's Ogoni region, where the local citizens have protested Shell's drilling and refining activities, which harm the natural environment and reduce the amount of available farmland. Protestors also accuse Shell of extracting wealth from the region without adequately compensating local residents. Following sabotage of its facilities, the firm suspended some of its Nigerian operations and then came under pressure to divest its operations and pay reparations to the local people. Despite these problems, Shell has persisted in Nigeria. Management instituted various community development programs in the region, budgeted at \$50 million per year. Using the ethical framework in this chapter, identify steps Shell can take to be a better corporate citizen in Nigeria.
- 4-23. *Ethical Dilemma:* American International Group (AIG) is the largest insurance company in the United States. When AIG faced financial ruin, the U.S. government used taxpayer money to loan AIG more than \$170 billion in exchange for an 80 percent stake in the firm. A few months later, it was revealed that AIG had used part of the money (at least \$30 billion) to pay off banks in Europe, largely for debt obligations it incurred in foreign transactions. U.S. government officials were furious. The furor intensified when AIG tried to renegotiate loans with some of its U.S. creditors, implying they were less important than the European banks. Suppose you were the chief financial officer at AIG. What would you have done? How would you handle this predicament? Use the ethical framework in this chapter to analyze how AIG might have handled the situation better.



INTERNET EXERCISES

Access globalEDGE™ at www.globalEDGE.msu.edu

AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Written and Oral Communication, Ethical Understanding and Reasoning, Information Technology, Analytical Thinking, and Application of Knowledge.

- 4-24. Various organizations have devised international standards for ethical corporate behavior. These include the United Nations' Universal Declaration for Human Rights (available at www.un.org), the OECD's Guidelines for Multinational Enterprises (www.oecd.org), and the International Labour Organization's International Labour Standards (www.ilo.org). Visit these online portals, and prepare a set of guidelines that firms can follow to pursue acceptable ethical standards in international business.
- 4-25. Transparency International (www.transparency.org) publishes information about the nature of corruption around the world. Suppose you worked at a firm that makes computer software and wanted to begin doing business in Brazil and Russia. Your task is to examine reports and indices about these countries at the Transparency International site and write a brief report explaining how your firm should

conduct business in these countries with a view to avoiding problems associated with corruption. Key issues to consider include bribery and threats to intellectual property.

- 4-26. The websites for Lenovo (China, www.lenovo.com), Nokia (Finland, www.nokia.com), and Allergan (United States, www.allergan.com) contain substantial information about how these firms undertake corporate social responsibility (CSR). Visit each website, and write a report in which you compare and contrast each firm's CSR. Which firm appears most effective in CSR? How does the CSR of a pharmaceutical firm (Allergan) differ from that of electronics manufacturing firms such as Lenovo and Nokia? Lenovo is based in an emerging market, whereas Allergan and Nokia are in advanced economies. What differences in the firms' CSR orientations can you detect based on this distinction? Justify your answer.

Endnotes

1. We are grateful to Professor Larry Beer, Arizona State University Emeritus, and to Elizabeth Amanda Napier, Georgia State University, for their helpful comments in the development of this chapter.
2. Andrew Crane and Dirk Matten, *Business Ethics: Managing Corporate Citizenship and Sustainability in the Age of Globalization* (Oxford: Oxford University Press, 2016); Naresh Malhotra and G. Miller, "An Integrated Model for Ethical Decisions," *Journal of Business Ethics* 17, No. 3 (1998), pp. 263–280; D. McAlister, O. C. Ferrell, and L. Ferrell, *Business and Society* (Boston: Houghton Mifflin, 2003); Gaston de los Reyes, Tae Wan Kim, and Gary R. Weaver, "Teaching Ethics in Business schools: A Conversation on Disciplinary Differences, Academic Provincialism, and the Case for Integrated Pedagogy," *Academy of Management Learning & Education* 16, No. 2 (2017), pp. 314–336.
3. Marco Celentani, Juan-Jose Ganuza, and Jose-Luis Peydros, "Combating Corruption in International Business Transactions," *Economica* 71, No. 283 (2004), pp. 417–449; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; McAlister, Ferrell, and Ferrell, 2003; David Zussman, "Fighting Corruption Is a Global Concern," *Ottawa Citizen*, October 11, 2005, p. A15.
4. Larry Beer, *Business Ethics for the Global Business and the Global Manager: A Strategic Approach* (New York: Business Expert Press, 2010); United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2015* (New York: UNCTAD, 2009); Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017.
5. Larry Beer, 2010; Lutz Kaufmann, Felix Reimann, Matthias Ehrgott, and Johan Rauer, "Sustainable Success," *Wall Street Journal*, June 22, 2009, www.wsj.com; Malhotra and Miller, 1998; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Alan Muller and Ans Kolk, "Extrinsic and Intrinsic Drivers of Corporate Social Performance: Evidence from Foreign and Domestic Firms in Mexico," *Journal of Management Studies* 47, No. 1 (2010), pp. 1–26.

6. Max Bazerman and Ann Tenbrunsel, "Ethical Breakdowns," *Harvard Business Review*, April 2011, pp. 58–65.
7. Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; John Sullivan, *The Moral Compass of Companies: Business Ethics and Corporate Governance as Anti-Corruption Tools* (Washington, DC: International Finance Corporation, World Bank, 2009).
8. Sullivan, 2009; Muller and Kolk, 2010; Transparency International, *Progress Report: OECD Anti-Bribery Convention 2009*, www.transparency.org.
9. Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; McAlister, Ferrell, and Ferrell, 2003.
10. Beer, 2010; Kaufmann, Reimann, Ehrhott, and Rauer, 2009; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Muller and Kolk, 2010.
11. OECD, *The Detection of Foreign Bribery*, 2017, www.oecd.org/corruption/the-detection-of-foreign-bribery.htm; Transparency International, *Progress Report: OECD Anti-Bribery Convention 2009*, www.transparency.org.
12. Beer, 2010; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017.
13. Beer, 2010; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; OECD, 2017.
14. Celentani, Ganuza, and Peydros, 2004; International Chamber of Commerce, Transparency International, the United Nations Global Compact, and World Economic Forum, *Clean Business Is Good Business: The Business Case Against Corruption*, retrieved from www.weforum.org/pdf/paci/BusinessCaseAgainstCorruption.pdf on April 5, 2015; Zussman, 2005; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017.
15. Transparency International, *Corruption Perceptions Index 2017* (Berlin: Transparency International, 2017), accessed at www.transparency.org.
16. Chad Bray and Stanley Reed, "Petrobras of Brazil to Pay \$2.95 Billion over Corruption Scandal," *New York Times*, January 3, 2018, www.nytimes.com; Petrobras, "Petrobras Signs Agreement in Principle to Settle Class Action in the U.S.," news release, January 3, 2018, www.petrobras.com.br/en/news/.
17. Sam Kim, "Playing Dumb Didn't Help Samsung's Heir Apparent," *Bloomberg BusinessWeek*, September 4, 2017, pp. 22–23; Choe Sang-Hun, "Samsung's Leader Is Indicted on Bribery Charges," *New York Times*, February 28, 2017, www.nytimes.com/2017/02/28/.
18. United States Department of Justice, "Former Owner of Bucks County Financial Consulting Firm Sentenced to Five Years in Prison for Bribing Foreign Official," July 18, 2017, www.justice.gov; *U.S. News and World Report*, "Consultant Gets 5 Years in Prison for International Bribery," July 20, 2017, www.usnews.com.
19. David Barstow, "The Bribery Aisle: How Wal-Mart Used Payoffs to Get Its Way in Mexico," *New York Times*, December 18, 2012, pp. A1, A3; Beer, 2010; James Detar, "Wal-Mart Loses Round In Alleged Mexico Bribery Action," *Investor's Business Daily*, May 9, 2014, p. 1; Russell Gold, "Halliburton to Pay \$559 Million to Settle Bribery Investigation," *Wall Street Journal*, January 27, 2009, p. B3; Sullivan, 2009; OECD, 2017; Transparency International, *Progress Report: OECD Anti-Bribery Convention 2009*, www.transparency.org; Transparency International, "Promoting Good Governance in Africa," March 5, 2009, www.transparency.org; N. Watson, "Bribery Charge Hits Halliburton Profits," *Petroleum Economist*, May 2009, p. 2; John Zhao, Seung Kim, and Jianjun Du, "The Impact of Corruption and Transparency on Foreign Direct Investment: An Empirical Analysis," *Management International Review* 43, No. 1 (2003), pp. 41–62; Zussman, 2005.
20. Alessandra Mezzadri, "Class, Gender and the Sweatshop: On the Nexus Between Labour Commodification and Exploitation," *Third World Quarterly* 37, No. 10 (2016), pp. 1877–1900; Brian Stauffer, "Follow the Thread: The Need for Supply Chain Transparency in the Garment and Footwear Industry," *Human Rights Watch*, April 20, 2017, www.hrw.org.
21. *Ending Violence and Harassment Against Women and Men in the World of Work* (Geneva: International Labour Office, 2018, www.ilo.org; Maryam Omari and Megan Paull (Eds.), *Workplace Abuse, Incivility and Bullying: Methodological and Cultural Perspectives* (New York: Routledge, 2016).
22. Fair Labor Association, *2017 Annual Report*, www.fairlabor.org; Tara Radin and Martin Calkins, "The Struggle Against Sweatshops: Moving Toward Responsible Global Business," *Journal of Business Ethics* 66 (2006), pp. 261–268.
23. OECD, 2017; OECD, *OECD Foreign Bribery Report: An Analysis of the Crime of Bribery of Foreign Public Officials* (Paris: OECD Publishing, 2014); Transparency International, *Progress Report: OECD Anti-Bribery Convention 2009*, www.transparency.org.
24. International Chamber of Commerce, "Global Impacts of Counterfeiting and Piracy to Reach US\$4.2 Trillion by 2022," June 2, 2017, www.iccwbo.org.
25. CBP Office of International Trade, *Intellectual Property Rights: Fiscal Year 2016 Seizure Statistics* (Washington, DC: U.S. Immigration and Customs Enforcement, 2017), www.cbp.gov; Frontier Economics, *The Economic Impacts of Counterfeiting and Piracy*, 2017, <https://cdn.iccwbo.org>.
26. CBP Office of International Trade, 2017.
27. Angela Doland, "In China, There's Not Just Disney, There's 'Disnay' and 'Disnesy' Too," *AdAge*, June 2, 2016, www.adage.com; Sarah McBride and Loretta Chao, "Disney Fights Pirates at China Affiliate," *Wall Street Journal*, November 21, 2008, p. B1.
28. Carter Dougherty, "One Hot List You Don't Want to Be On," *BloombergBusiness*, March 5, 2015, www.bloomberg.com; Murray Stassen, "Music Piracy Should Be a Thing of the Past," *MusicWeek*, April 25, 2016, pp. 14–18; Mark Savage, "Stream-Ripping Is 'Fastest Growing' Music Piracy," *BBC News*, July 7, 2017, www.bbc.com.
29. OECD, *Annual Report on the OECD Guidelines for Multinational Enterprises 2016* (Paris: Organisation for Economic Co-operation and Development); Andreas Rasche, Mette Morsing, and Jeremy Moon, *Corporate Social Responsibility: Strategy, Communication, Governance* (New York: Cambridge University Press, 2017).
30. Jessica Rodell, Heiko Breitsohl, Melanie Schröder, and David Keating, "Employee Volunteering: A Review and Framework for Future Research," *Journal of Management* 42, No. 1 (2016), pp. 55–84.
31. David Chandler, *Strategic Corporate Social Responsibility: Sustainable Value Creation*, 4th ed. (Thousand Oaks, CA: Sage, 2017); Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Ethics & Compliance Initiative, *Global Business Ethics Survey 2016*, www.ethics.org.

32. Chip Cummins, "Shell, Chevron to Cut Deliveries of Oil amid Protests in Nigeria," *Wall Street Journal*, December 23, 2004, p. A2; *Fortune*, "Walmart Is Reportedly Getting Ready to Settle a Bribery Probe for \$300 Million," May 10, 2017, www.fortune.com; U. Idemudia, "Oil Extraction and Poverty Reduction in the Niger Delta: A Critical Examination of Partnership Initiatives," *Journal of Business Ethics* 90 (May 2009), pp. 91–116; Kris Maher, "Wal-Mart Tops Global Agenda for Labor Leaders," *Wall Street Journal*, August 18, 2005, p. A2; Tom Schoenberg, "Wal-Mart Close to Resolving Bribery Probe for \$300 Million," *Bloomberg*, May 9, 2017, www.bloomberg.com; Harry Weber, "Time to Scrap BP Brand? Gas-Station Owners Divided," *USA Today*, July 31, 2010, retrieved April 4, 2015, from http://usatoday30.usatoday.com/money/industries/energy/2010-07-31-bp-amoco-rebrand_N.htm.
33. *Foreign Affairs*, "Africa Calling," 94, No. 1 (January/February 2015), pp. 24–30; Mo Ibrahim, "Celtel's Founder on Building a Business on the World's Poorest Continent," *Harvard Business Review*, October 2012, pp. 41–44; Ricardo Geromel, "Can We Use Corporate Social Responsibility to Evaluate Companies?" *Forbes*, May 21, 2012, www.forbes.com.
34. *The Guardian*, "GSK Partners with Stakeholders on Healthcare Development in Africa," May 4, 2017, www.guardian.ng; Andrew Witty, "New Strategies for Innovation in Global Health: A Pharmaceutical Industry Perspective," *Health Affairs* 30, No. 1 (2011), pp. 118–126.
35. James Henderson, "SSE Issues Biggest Ever UK Green Bond, Worth €600mn," *Energy Digital*, September 1, 2017, www.energydigital.com; SSE Plc., *Providing More Than Energy: SSE plc Sustainability Report 2017*, www.sse.com.
36. Esha Chhabra, "Corporate Social Responsibility: Should It Be a Law?," *Forbes*, April 18, 2014, www.forbes.com; Noreen Ohlrich, "Mandatory Corporate Social Responsibility in India: How Is It Working?," *Nonprofit Quarterly*, February 17, 2017, www.nonprofitquarterly.org; Andreas Rühmkorf, *Corporate Social Responsibility, Private Law and Global Supply Chains* (Cheltenham, UK: Edward Elgar, 2015); Wayne Visser and Nick Tolhurst, *The World Guide to CSR: A Country-by-Country Analysis of Corporate Sustainability and Responsibility* (New York: Routledge, 2017).
37. Beer, 2010; Philip Kotler and Nancy Lee, *Up and Out of Poverty: The Social Marketing Solution* (Upper Saddle River, NJ: Wharton School Publishing, 2009); Timothy Besley and Maitreesh Ghatak, "Public-Private Partnerships for the Provision of Public Goods: Theory and an Application to NGOs," *Research in Economics* 71, No. 2 (2017), pp. 356–371; Hildy Teegen, Jonathan Doh, and Sushil Vachani, "The Importance of Nongovernmental Organizations (NGOs) in Global Governance and Value Creation: An International Business Research Agenda," *Journal of International Business Studies* 35, No. 4 (2004), pp. 463–483.
38. Beer, 2010; Erin Cavusgil, "Merck and Vioxx: An Examination of an Ethical Decision-Making Model," *Journal of Business Ethics* 76, No. 4 (2007), pp. 451–461; Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; MIT Sloan Management Review and Boston Consulting Group, *Sustainability: The "Embracers" Seize Advantage*, research report (Cambridge, MA: Massachusetts Institute of Technology, 2011).
39. Robert H. Friis, *Essentials of Environmental Health*, 3rd ed. (Sudbury, MA: Jones and Bartlett, 2018); Secretariat of the Basel Convention, *Vital Waste Graphics 3* (Geneva: Secretariat of the Basel Convention, 2012).
40. BBC, "Brazil's Most Populous Region Faces Worst Drought in 80 Years," January 24, 2015, www.bbc.com; Jose Marengo, Roger Torres, and Lincoln Alves, "Drought in Northeast Brazil—Past, Present, and Future," *Theoretical and Applied Climatology* 129, No. 3–4 (2017), pp. 1189–1200.
41. Sarah Butler, "H&M Factories in Myanmar Employed 14-Year-Old Workers," *The Guardian*, August 21, 2016, www.theguardian.com; Jo Johnson and Aline van Duyn, "Forced Child Labour Claims Hit Clothes Retailers," *Financial Times*, October 29, 2007, p. 3; Landrum and Edwards, 2009; Masha Zager, "Doing Well by Doing Good: Gap Inc.'s Social Responsibility Program," *Apparel*, August 2009, p. 10.
42. Marc Gunther, "Unilever's CEO Has a Green Thumb," *Fortune*, June 10, 2013, pp. 124–128; Vivienne Walt, "Unilever CEO Paul Polman's Plan to Save the World," *Fortune*, February 17, 2017, www.fortune.com.
43. *Fortune*, "BMW Wants to Sell Half a Million Hybrids and Electric Cars by 2019," December 21, 2017, www.fortune.com; Alex Taylor, "BMW Gets Plugged In," *Fortune*, March 18, 2013, pp. 150–155.
44. Krystina Gustafson, "Amazon Hints at One of Its Best-Kept Secrets: How Many Prime Members It Has," *CNBC*, February 17, 2017, www.cnn.com; Jennifer Langston, "Drone vs. Truck Deliveries: Which Create Less Carbon Pollution?," *UWNEWS*, May 30, 2017, www.washington.edu/news; Leena Rao, "Out of the Box," *Fortune*, December 1, 2016, p. 23; Matt Richtel, "E-Commerce: Convenience Built on a Mountain of Cardboard," *The New York Times*, February 16, 2016, www.nytimes.com; *Worldatlas*, "Countries Who Spend the Most Money Shopping Online," August 1, 2017, www.worldatlas.com.
45. Andrew Batson, "Coke Aims to Improve Water Recycling," *Wall Street Journal*, June 6, 2007, p. A10; Jenny Wiggins, "Coke Develops Thirst for Sustainability," *Financial Times*, July 2, 2007, p. 26; Daniel Vermeer and Robert Clemen, "Why Sustainability Is Still Going Strong," *Financial Times*, February 19, 2015, www.ft.com.
46. Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Sullivan, 2009.
47. de los Reyes, Kim, and Weaver, 2017; Muller and Kolk, 2010.
48. Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Ferrell and Gresham, 1985; T. Low, L. Ferrell, and P. Mansfield, "A Review of Empirical Studies Assessing Ethical Decision Making in Business," *Journal of Business Ethics* 25, No. 3 (2000), pp. 185–204; Malhotra and Miller, 1998; McAlister, Ferrell, and Ferrell, 2003.
49. OECD, 2017; Transparency International, *Progress Report: OECD Anti-Bribery Convention 2009*, www.transparency.org.
50. de los Reyes, Kim, and Weaver, 2017; Vermeer and Clemen, 2009.
51. Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Cavusgil, 2007; Malhotra and Miller, 1998; McAlister, Ferrell, and Ferrell, 2003; MIT Sloan Management Review and Boston Consulting Group, 2011.
52. A version of this framework appeared originally in *Issues in Ethics* 1, No. 2 (1988). It was developed at the Markkula Center for Applied Ethics at Santa Clara University, California. See also Crane and Matten, 2016; de los Reyes, Kim, and Weaver, 2017; Cavusgil, 2007; Ferrell and Gresham, 1985; Low, Ferrell, and Mansfield, 2000; Malhotra and Miller, 1998; McAlister, Ferrell, and Ferrell, 2003; UNCTAD, *World Investment Report 2006* (New York: UNCTAD, 2006); Sullivan, 2009.

Chapter 5

Theories of International Trade and Investment

Learning Objectives After studying this chapter, you should be able to:

- 5.1 Explain why nations trade.
- 5.2 Learn about how nations can enhance their competitive advantage.
- 5.3 Understand why and how firms internationalize.
- 5.4 Explain the strategies internationalizing firms use to gain and sustain competitive advantage.

Apple's Advantages in Global Competition

Since inception, Apple has sold more than 1.2 billion iPhones in 120 countries. Apple achieved worldwide sales of \$230 billion dollars in 2017 with net income of more than \$48 billion dollars. North and South America account for about 40 percent of total sales, followed by Asia with 30 percent and Europe with 25 percent. After the United States, China is Apple's best market, providing about 20 percent of total sales.

Apple products were once made entirely in the United States. Now, almost all of them are manufactured outside the United States.

Through *global sourcing*, Apple contracts with suppliers around the world, where more than 700,000 engineers build and assemble its products. One of Apple's key goals is to use comparative advantages from different countries. *Comparative advantage* is the ability of a specific country to produce a given product or service better or for a lower cost than other countries. For

example, Apple bases most of its iPhone manufacturing in China because of the country's high-quality, low-cost labor.

Consumers are one of the primary drivers of global trade, and they demand the best quality at the lowest prices. *Global sourcing* occurs when firms, striving for competitive advantage, capitalize on the comparative advantages of select countries to meet that demand. This results in increased imports through global trade.

Apple exemplifies superior *innovation*, including new product designs and more efficient production methods. It conducts most of its own research and product development in company-owned facilities in California. Innovation increases Apple's *productivity*, a gauge of how efficiently products are manufactured. Higher productivity allows firms like Apple to lower their production costs, which in turn increases profits and builds competitive advantage. An iPhone contains hundreds of parts, 90 percent of which