

Chapter 2

Globalization of Markets and the Internationalization of the Firm

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

- 2.1** Understand market globalization as an organizing framework.
- 2.2** Learn the driving forces of globalization.
- 2.3** Understand the impact of technological advances on globalization.
- 2.4** Learn the dimensions of globalization.
- 2.5** Understand firm-level consequences of market globalization.
- 2.6** Understand the societal consequences of globalization.

Skype: A “Born Global” Business

Skype is a telecommunications application available on most major platforms and devices that provides video, audio, and text chat over the Internet between devices. It was founded in August 2003 by Niklas Zennstrom from Sweden and Janus Friis from Denmark, and it was developed in Estonia. Skype is now headquartered in Luxembourg, with offices across Europe, the United States, and Asia.

Its Swedish, Danish, and Estonian roots alone cast Skype as a business that was born to be global from the moment of its launch, but the very nature of the software and the ease of communication that it has enabled between businesses and individuals around the world speak to its position as a truly international brand.

A little over a year after its launch in October 2004, it had already been downloaded 1.5 million times. By June

2005, 10 million Skype-to-Skype calls had been made. In March 2007, its download count had reached 500 million, and by February 2008, 100 billion minutes of Skype-to-Skype calls had been made.

To the present day, Skype has grown its business strongly across the Windows, Android, and Apple platforms. This growth has been accelerated by a number of factors but predominately to its first-mover advantage, the availability of Skype across numerous platforms, and the freemium business model upon which it is built upon. This business model means that the software or application and its core features are free for users to download, but money is charged for additional features. Thanks to the size of its userbase, Skype needs only a small proportion of users to purchase premium features to generate its revenue.



Source: Ian Shaw/Alamy Stock Photo

Skype's astonishing global growth should perhaps not be so surprising given that the application is freely available to anyone with a compatible device—most are—and an Internet connection anywhere in the world. Skype launched at a time when it had no established competitors and was therefore unique in its offering. These factors, combined with the rise of the Internet, endless innovation in technology, and growth in service offerings has made globalization far more practicable, less expensive, and for many businesses a must. Globalization has turned Skype into the giant it is today.

As a “born global” business, Skype has succeeded in entering a number of international markets within a short space of time of its initial launch. It was able to grow exponentially thanks to its international outlook, the agility of its business and software, and the its distribution

channel—the Internet. This growth and service ultimately culminated in Microsoft swooping in and acquiring the business for \$8.5 billion, but the value that Microsoft has placed is well beyond that sum. Microsoft's faith in the business and underlying technology is so great that it has discontinued many of the messaging services it had developed in-house in favor of Skype.

Other born global companies include Airbnb (accommodation), HTC (smartphones), Uber (transportation), Spotify (music streaming). Skype and the “born global” businesses demonstrate that even new ventures with very limited experience but high innovation and can quickly grow internationally without having vast resources at their disposal. Our connected world makes it much easier to communicate and operate on a global basis; indeed, more companies are operating internationally today than ever before.

AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Analytical Thinking, Reflective Thinking**Questions**

- 2-1.** What environmental factors create favorable conditions for businesses such as Skype to rapidly grow internationally?
- 2-2.** Beyond simply increasing revenue, what advantages might a new business benefit from thanks to early international exposure and growth?
- 2-3.** What are the risks associated with such rapid and dispersed growth for a new company?

SOURCES: "The History of Skype," Skype Blogs, August 2012, <https://blogs.skype.com/wp-content/uploads/2012/08/skype-timeline-v5-2.pdf>; "Microsoft Confirms Takeover of Skype," BBC News, May 10, 2011, <https://www.bbc.com/news/business-13343600>.

This case was written by John Bancroft, Oxford Brookes University.

The opening case highlights important driving forces and causes of market globalization. These include worldwide reduction of barriers to trade and investment, market liberalization and adoption of free markets, and advances in technology.

Globalization of markets refers to the gradual integration and growing interdependence of national economies. Declining trade barriers and rapid changes in communications, manufacturing, and transportation technologies are enabling firms to internationalize much more rapidly and easily than ever before.

Globalization allows companies to outsource value-chain activities to the most favorable locations worldwide. A **value chain** is the sequence of value-adding activities the firm performs in the course of developing, producing, marketing, and servicing a product. Firms source raw materials, parts, components, and service inputs from suppliers around the globe. Globalization has also made it easier for companies to sell their offerings worldwide. These trends are transforming national economies. Growing world trade and foreign direct investment (FDI) provide buyers with a wider choice of products than ever before. Global competition and innovation frequently help to lower consumer prices. Firms with cross-border business create millions of jobs that raise living standards around the world.

Globalization is not new. In early history, civilizations in the Mediterranean, Middle East, Asia, Africa, and Europe all contributed to the growth of cross-border trade. Globalization evolved out of a common desire of civilizations to reach out and touch one another.¹ It is a culmination of people's recognition, thousands of years ago, of the wonders of difference and discovery. Cross-border trading opened the world to innovations and progress by giving societies the opportunity to expand and grow. Trade through the ages fostered civilization; without it, the world would consist of warring tribes bent on getting what they need through combat.²

Phases of Globalization

We can identify five distinct phases in the evolution of globalization since the 1800s. As illustrated in Exhibit 2.1, each phase was accompanied by radical technological advances and internationalization trends.

- *The first phase of globalization* began in about 1830 and peaked around 1880.³ It was associated with the use of water and steam power to mechanize production and power ships and trains. International business became widespread due to the growth of railroads, efficient ocean transport, and the rise of large manufacturing and trading firms. Invention of the telegraph and telephone in the late 1800s enabled information flows between and within nations and aided early efforts to manage companies' supply chains.
- *The second phase of globalization* began around 1900 and was associated with the rise of electricity and steel production. Electric power was widely used to drive mass production. This phase reached its height just before the Great Depression, a worldwide economic downturn that began in 1929. In 1900, Western Europe was the most industrialized world region. Europe's colonization of countries in Asia, Africa, and the Middle East led to the establishment of some of the earliest subsidiaries of multinational enterprises (MNEs). European companies such as BASF, Nestlé, Shell, Siemens, and British Petroleum established foreign manufacturing plants by 1900.⁴ In the years before World War I (pre-1914), many firms operated globally. The Italian manufacturer Fiat supplied vehicles to nations on both sides of the war.

Phase of Globalization	Approximate Period	Triggers	Key Characteristics
First phase	1830 to late 1800s, peaking in 1880	Introduction of railroads and ocean transport	Rise of manufacturing; cross-border trade of commodities, largely by trading companies
Second phase	1900 to 1930	Rise of electricity and steel production	Emergence and dominance of early MNEs (mainly from Europe and North America) in manufacturing, extractive, and agricultural industries
Third phase	1948 to 1970s	Formation of General Agreement on Tariffs and Trade (GATT); conclusion of World War II; Marshall Plan to reconstruct Europe	Focus by industrializing Western countries to reduce trade barriers; rise of MNEs from Japan; development of global capital markets; rise of global trade names
Fourth phase	1980s to about 2006	Privatization of state enterprises in transition economies; revolution in information, communication, and transportation technologies; remarkable growth of emerging markets	Rapid growth in cross-border trade of products, services, and capital; rise of internationally active SMEs and services firms; rising prosperity of emerging markets
Fifth phase	2007 to present	Rise of digital technologies, and other new technologies, which are boosting manufacturing productivity and the efficiency of international trade in services	Leveraging technology to facilitate trade and local production; rising trade in digitally enabled services but slowing growth of trade in merchandise goods

EXHIBIT 2.1
Phases of Globalization Since the Early 1800s

- The third phase of globalization began after World War II. This phase was associated with reconstruction efforts after the war and the dismantling of trade barriers. By the war's end in 1945, substantial pent-up demand fueled markets for consumer and industrial products to rebuild Europe and Japan. Leading industrialized countries, including Australia, the United Kingdom, and the United States, sought to reduce international trade barriers to supply goods to meet this demand.

In 1947, the Bretton Woods Conference of 23 nations created the *General Agreement on Tariffs and Trade (GATT)*, which reduced barriers to international trade and investment. Participating governments recognized that liberalized trade would stimulate industrialization, modernization, and better living standards. In turn, the GATT led to the formation of the **World Trade Organization (WTO; www.wto.org)**, which grew to include about 164 member nations. The WTO aims to regulate and ensure fairness and efficiency in global trade and investment. Global cooperation in the postwar era also gave birth to the International Monetary Fund and the World Bank.

Early multinationals from the third phase of globalization originated in the United States, Western Europe, and Japan. European firms such as Unilever, Philips, Royal Dutch-Shell, and Bayer organized their businesses by establishing subsidiaries around

World Trade Organization (WTO)
A multilateral governing body empowered to regulate international trade and investment.

the world. Many companies developed internationally recognized trade names, including Nestlé, Kraft, Lockheed, Caterpillar, Coca-Cola, and Levi's. Foreign subsidiaries of such companies operated as small versions of the parent firm, marketing their products around the world. MNEs began to seek cost advantages by locating factories in developing countries with low labor costs. International trade and investment expanded significantly in the 1960s. Recovered from World War II, MNEs in Europe and Japan began to challenge the dominance of U.S. multinationals. Growing international trade coincided with increased cross-national flows of capital, leading to integration of global financial markets.⁵

- *The fourth phase of globalization* began in the early 1980s and featured the use of electronics and information technology to automate production. The phase was characterized by enormous growth in cross-border trade and investment. It was triggered by the development of personal computers, the Internet, and web browsers. It was also characterized by the collapse of the Soviet Union and the market liberalization of Central and Eastern Europe. Impressive industrialization and modernization in East Asian economies followed. International prosperity began to develop in the emerging markets, including Brazil, India, and Mexico. The 1980s witnessed huge increases in FDI, especially in capital- and technology-intensive sectors. Technological advances in information, communications, and transportation supported the rise of internationally active small and medium-sized enterprises. These advances increased the ability to organize and manage exports more efficiently and at lower cost. Modern technologies also enabled the globalization of the service sector in such areas as banking, entertainment, tourism, insurance, and retailing.
- *The fifth phase of globalization* began around 2007 with the rise of digital technologies. Technological breakthroughs in fields such as quantum computing, the Internet of Things, artificial intelligence, robotics, autonomous vehicles, 3D printing, nanotechnology, and biotechnology are blurring the lines between the physical, digital, and biological spheres. Digital and other new technologies are boosting the efficiency of international trade, especially in services. For example, much retailing is now done through giant firms such as Amazon and Alibaba, which sell their offerings around the world via online platforms. From Africa to South Asia to Latin America, as more people become digitally connected, they consume more international services. The value of world exports of services rose from about \$3 trillion in 2007 to more than \$5 trillion in 2017. Thanks to technological advances, national borders and traditional country-based business models are losing much of their relevance.

Meanwhile, growth in international trade of goods has slowed during this phase. Just as new technologies support international services trade, they also increase the productivity of local manufacturing. This tendency reduces firms' cost of domestic operations and increases the attractiveness of homegrown, local manufacturing. FDI as a share of total investment has declined. Emerging market countries increasingly focus on developing local markets for locally manufactured products.⁶

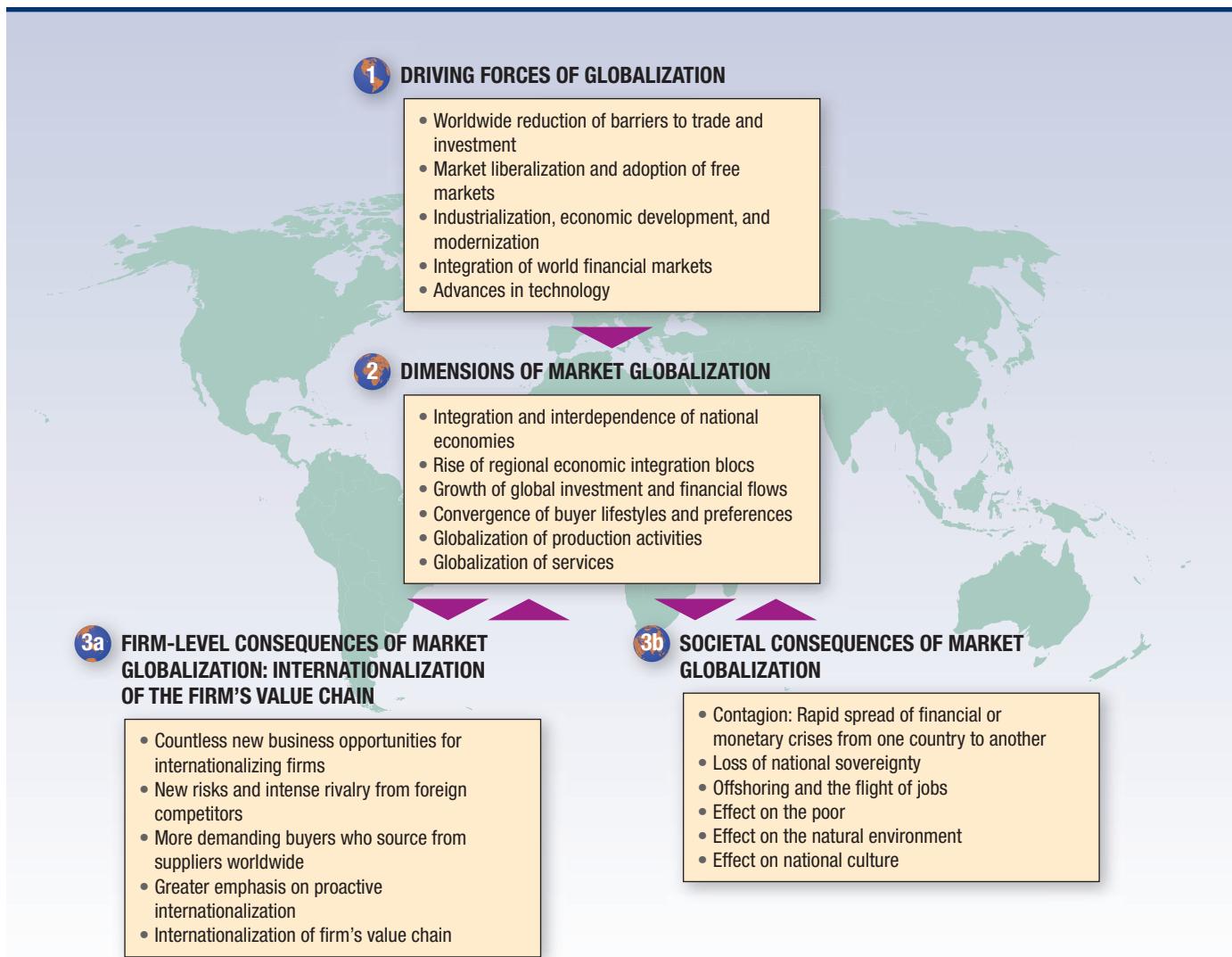
2.1 Understand market globalization as an organizing framework.

Market Globalization: Organizing Framework

Firms expand abroad proactively to increase sales and profit through new markets, find lower-cost inputs, or obtain other advantages. Firms may also internationalize reactively because of unfavorable conditions in the home market such as regulation or declining local industry sales. Exhibit 2.2 presents an organizing framework for examining market globalization. The exhibit makes a distinction among:

- **driving forces** or causes of globalization.
- **dimensions** or manifestations of globalization.
- **firm-level consequences** of globalization.
- **societal consequences** of globalization.

In the exhibit, the double arrows illustrate the interactive nature of the relationship between globalization and its consequences. As globalization intensifies, individual firms respond to the challenges and new advantages that it brings.



America Movil (www.americamovil.com) is a leading wireless phone service provider, with more than 225 million subscribers in 18 countries, that has pursued internationalization as a growth strategy. Based in Mexico, America Movil internationalized mainly through foreign direct investment (FDI) with initial operations in Brazil and Colombia. It then expanded to Ecuador, Chile, the Netherlands, and numerous other foreign markets. The firm entered into a joint venture with Citigroup to fund expansion in South America. It acquired Verizon's telephone operations in Puerto Rico. In each case, America Movil took advantage of such globalization trends as harmonizing communications technologies, converging buyer characteristics, and reduced trade and investment barriers. As emerging markets transform into sophisticated economies, they leapfrog older telecom technologies and embrace contemporary mobile phone technology—a boon to America Movil.

To minimize costs, many of the firm's cell phones are essentially identical worldwide. They are adapted only to accommodate for local languages, regulations, and telephone standards. America Movil's positioning emphasizes a global brand that is recognized everywhere. Worldwide convergence of buyer lifestyles and incomes help facilitate this transnational approach. Management coordinates operations on a global scale and applies common business processes in procurement and quality control. The strategies of product standardization, global branding, and selling to customers worldwide owe much of their success to the globalization of markets.⁷

EXHIBIT 2.2

The Driving Forces, Dimensions, and Consequences of Globalization

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 Born Global.

2.2 Learn the driving forces of globalization.

Driving Forces of Globalization

Various trends have converged in recent years as causes of globalization. The following are particularly notable:

- *Worldwide reduction in barriers to trade and investment.* The tendency of national governments to reduce trade and investment barriers has accelerated global economic integration. For example, tariffs on the import of industrial and medical equipment and countless other products have declined nearly to zero in many countries, encouraging freer international exchange of goods and services. Falling trade barriers are facilitated by the WTO. After joining the WTO in 2001, China has made its market increasingly more accessible to foreign firms. The decrease in trade barriers is also associated with the emergence of regional economic integration blocs. The recent rise of nationalistic politicians in some countries has tended to hinder ongoing reduction of trade and investment barriers. However, the overall trend of increasing free trade continues.⁸
- *Market liberalization and adoption of free markets.* In the past three decades, free-market reforms have smoothed the integration of China, India, Russia and other formerly protectionist countries into the global economy. Numerous Asian economies—for example, India, Indonesia, Malaysia, and South Korea—embraced free market norms. These events opened much of the world to freer international trade and investment. China, India, and Eastern Europe have become some of the most cost-effective locations for producing goods and services worldwide. Privatization of previously state-owned industries in these countries has encouraged economic efficiency and attracted massive foreign capital to their national economies.
- *Industrialization, economic development, and modernization.* Many emerging markets—rapidly developing economies in Asia, Latin America, and Eastern Europe—have now moved from being low value-adding commodity producers to sophisticated, competitive producers and exporters of premium products such as electronics, computers, and aircraft.⁹ For example, Brazil is now a leading manufacturer of Embraer commercial aircraft. The Czech Republic excels in producing automobiles. India is a leading supplier of software.

Economic development results in increased incomes and living standards, an important measurement of which is *gross national income (GNI)* per person.¹⁰ Exhibit 2.3 maps the levels of GNI worldwide. It reveals that Africa and several countries in Asia and Latin America are the lowest-income countries. These areas are also characterized by lower levels of globalization. A critical driver of rising income levels is the nation's volume of international trade. Exhibit 2.4 highlights the relationship between trade and gross domestic product (GDP). In this exhibit, trade is expressed as the volume of merchandise exports, and GDP measures the volume of goods and services production. The exhibit suggests that countries that undertake the most international trade, and whose trade levels have sharply increased in the past decade, also enjoy high and rapidly rising GDP.

- *Integration of world financial markets.* Financial market integration makes it possible for internationally active firms to raise capital, borrow funds, and engage in foreign currency transactions. Financial services firms follow their customers to foreign markets. Cross-border transactions are made easier because of the ease with which funds can be transferred between buyers and sellers. This takes place through networks of international commercial banks. For instance, the SWIFT network connects more than 11,000 financial institutions in some 200 countries. This global financial connectivity assists firms in developing and operating world-scale production and marketing operations. It enables companies to pay suppliers and collect payments from customers worldwide.
- *Advances in technology.* Technological advances are a remarkable facilitator of cross-border trade and investment. This is an important megatrend that requires greater elaboration.

Technological Advances and Globalization

Perhaps the most important driving force of market globalization has been technological advances in information, communications, manufacturing, and transportation. Technological advances provide the *means* for market globalization to happen.

2.3 Understand the impact of technological advances on globalization.

Information Technology

Information technology (IT) is the science and process of creating and using information resources. Its effect on business has been revolutionary. The cost of computer processing fell by more than 30 percent per year during the past three decades and continues to fall. IT creates competitive advantages by giving companies new ways to outperform rivals.¹¹ Geographically distant subsidiaries of a multinational firm are now interconnected by intranets that facilitate instant sharing of data, information, and experience across company operations worldwide. MNEs use collaboration software to connect widely dispersed product development teams.

IT benefits smaller firms, too, allowing them to design and produce customized products they can target to narrow, cross-national market niches. Online search engines provide easy access to unlimited data for researching markets, competitors, and other key information. At a higher level, IT supports managerial decision making, such as the selection of qualified foreign business partners, by allowing firms to access key information and intelligence quickly.

Technology enables firms to interact with foreign partners and value-chain members in a more timely and cost-effective way. Such productivity advances provide substantial competitive advantages for the firm.¹² One result is the increased early internationalization by SMEs. Emerging markets and developing economies benefit from technological leapfrogging. For example, numerous African countries are adopting cell phone technology directly, bypassing the landline technology common to some advanced economies.

Panel (a) of Exhibit 2.5 reveals how the cost of international communications has fallen since 2000, expressed as the dramatic rise in the volume of international traffic in Voice over Internet Protocol (VoIP) calls. VoIP is the mother technology of Skype, FaceTime, and numerous other platforms that facilitate very low-cost international voice and video communications. Panel (b) of Exhibit 2.5 reveals the growth in Internet users in various regions since 2000. Africa has the fewest Internet users, whereas Europe and North America have the most, reflecting the level of economic and infrastructural development in each region.

Digitalization

Digitalization refers to enabling or transforming business functions, operations, and activities by leveraging digital technologies and digitized data. Digital connectivity has become possible because of advanced IT and telecommunications technologies. Digital networks provide a global platform through which people and organizations interact, collaborate, obtain information, and develop strategies. Digital flows of information and commerce are connecting the world more than ever before. E-commerce now encompasses a vast range of platforms and applications that facilitate international buying and selling of goods and services online. For example, sharing-economy firms such as Uber and Airbnb use specialized software and the Internet to facilitate the joint creation of value and services between asset users and asset owners. Around the world, Uber allows people who need temporary transportation to hire drivers and vehicles owned by others. Airbnb allows travelers to rent other people's homes.

Digitalization is transforming interactions among customers, employees, business partners and investors by connecting locations, products, services, and data.¹³ Large-scale data analysis helps uncover breakthrough business insights and develop products, services, and experiences tailored to specific customer needs. For example, automakers continuously collect data on how customers use their cars and then utilize the data to improve product quality and the driving experience. Leveraging emergent technologies such as virtual reality and artificial intelligence helps to create innovative products and services that provide competitive advantages. Robots, artificial intelligence, and IT-based automation improve operational efficiency and deliver more engaging customer experiences. For example, MNEs are introducing sensors into manufacturing operations to improve production efficiency, predict maintenance problems, and perform repairs from remote locations.



EXHIBIT 2.3

Gross National Income, in U.S. Dollars

Source: Based on World Bank (2018); World Bank Development Indicator database, GNI per capita, Atlas method (current US\$), www.data.worldbank.org.



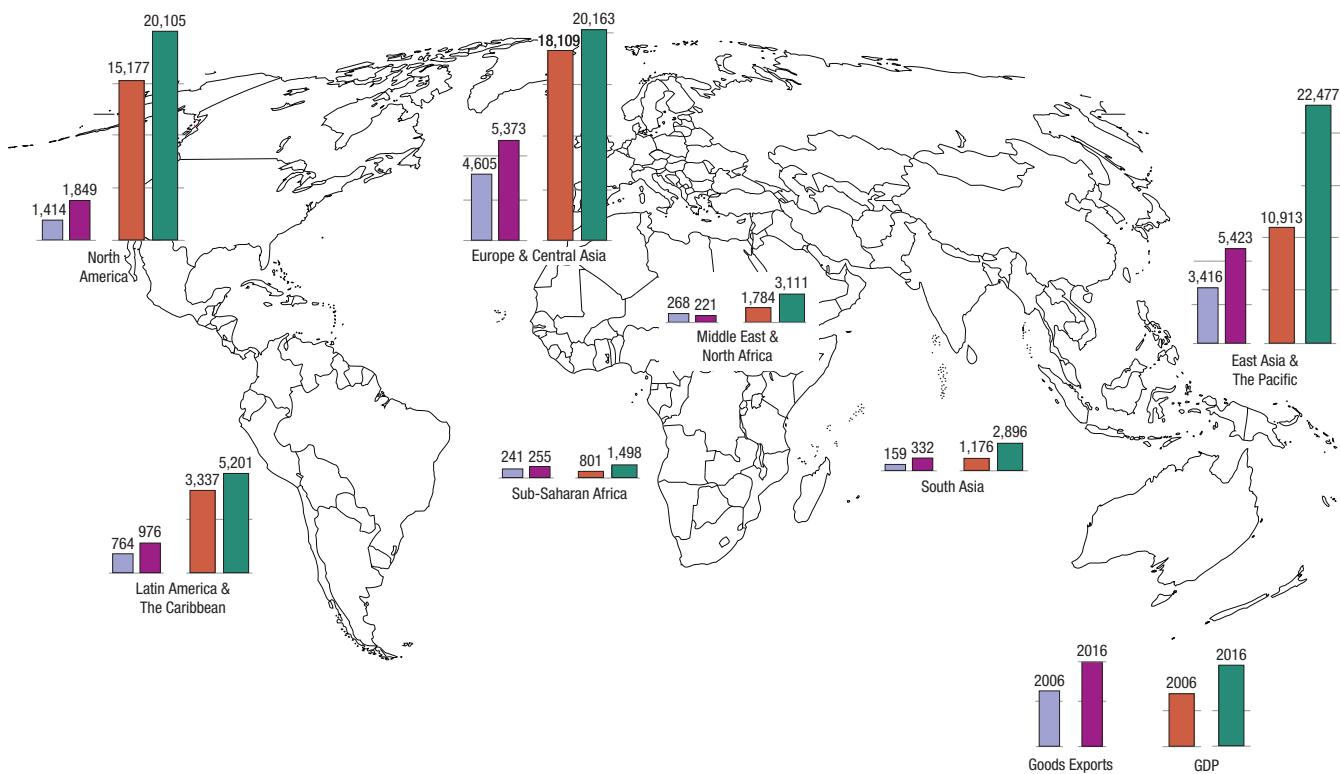


EXHIBIT 2.4

Relationship Between Trade and GDP Growth, in Billions of U.S. Dollars

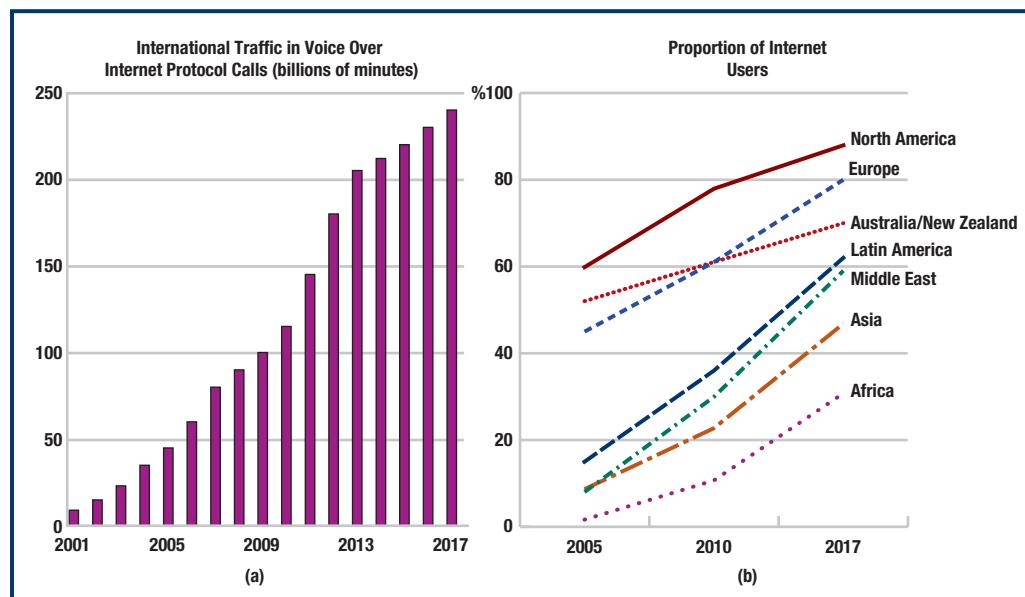
Source: Based on World Bank, Data, 2018, www.worldbank.org.

Digitalization has numerous consequences. The marginal cost of transmitting data and information worldwide is now essentially zero. Digitalization has reduced both the importance of geographic boundaries and the costs of international interactions and transactions. Companies extensively use digital tools to support innovation and improve productivity and the effectiveness of value chains worldwide. All kinds of firms use digital platforms to connect with customers and suppliers around the world. Competition is becoming more sophisticated and global. For example, Alibaba and Amazon are connecting global suppliers and imposing competitive pressures on traditional retailers worldwide.¹⁴

EXHIBIT 2.5

Growth of Global Communication and the Internet

Sources: BridgeVoicePluto, "Disrupting Wholesale Telecom: VoIP Market Trends and Predictions," 2017, www.bridgevoice.com; IMF, *World Economic Outlook* (Washington, DC: International Monetary Fund, 2017); United Nations International Telecommunications Union, *ICT Statistics*, 2017, [www.itu.int](http://itu.int); Internet World Stats, *Internet Usage Statistics*, 2018, www.internetworldstats.com.



Communications

The Internet and Internet-dependent systems such as intranets, extranets, social media, and email connect billions of people and companies. Marketers use the Internet to promote the widest range of products and services to customers worldwide. Transmitting voice, data, and images is essentially costless, making Seoul, Stockholm, and San Jose next-door neighbors. South Korea has nearly 100 percent Internet access, with one of the fastest broadband networks worldwide. Koreans use their phones to pay bills, do banking, and watch news programs.

The Internet opens the global marketplace to SMEs and other firms that would normally lack the resources to do international business. By establishing a presence on the web, even tiny enterprises can take the first step to become multinational firms. Services as diverse as designing an engine, monitoring a security camera, selling insurance, and doing secretarial work are easier to export than car parts or refrigerators. In China, thousands of rural farmers use Internet sites such as www.taobao.com to market their produce to urban consumers.¹⁵

Ethical Connections

In six years, Nigeria increased its telecom infrastructure from just 500,000 phone lines to more than 30 million cellular subscribers. The result has been a dramatic rise in productivity and commerce, which has helped improve living standards. Greater access to cell phones saves wasted trips, provides access to education and health care services, and facilitates communication between suppliers and customers. MNE telecom investment in Africa allows firms to fulfill social responsibilities and improve the lives of millions of poor people.

Countries need modern infrastructure in communications, such as reliable telephone systems, to support economic development. Mobile phones are the most transformative technology in developing economies. Fortunately, cell phone infrastructure is inexpensive and relatively easy to install.

The *Internet of Things* refers to machine-to-machine connectivity online. Worldwide, mobile telephony and app development have grown enormously, creating millions of jobs, increasing productivity, and producing big GDP gains. The number of smartphone users reached 3 billion in 2017, double the figure in 2013. People everywhere are now online.¹⁶

Social media such as Snapchat, Instagram, and WeChat facilitate the free flow of information, deepening the pace and impact of globalization. Global communities created by platforms such as YouTube and Twitter help mobilize audiences that transcend borders and geographic distance. The “Arab Spring” in the Middle East was facilitated in large part by social media. In view of this, in some authoritarian countries, national governments restrict access to social media, fearing the role it can play in accelerating social movements. Many companies and other organizations leverage social media to communicate with their publics through direct sales, advertising, and public relations. Social media provide the means to communicate directly with millions of connected individuals in new markets. Puma uses Twitter and other platforms to market sportswear to customers in Europe and Latin America ahead of the World Cup games. McDonald’s used the social media site Renren.com to market burgers and sundaes to customers in China. Social media provide various means to reach important audiences in markets around the world.¹⁷

Manufacturing

Digitalization and computer-aided design (CAD) of products, robotics, and production lines have transformed manufacturing, mainly by reducing production costs. Revolutionary developments facilitate low-scale and low-cost manufacturing; firms can make products cost-effectively even in short production runs. Online platforms are increasing the productivity of business and industrial activity. Such developments benefit international business by allowing firms to adapt products more efficiently to individual



Source: © Gilles Paire/Fotolia

Increasing availability of cell phones in Africa has helped spur economic growth there.



Source: federico rostagno/123rf

Advances in transportation and low freight costs have helped spur market globalization. Triple E class ships can carry thousands of shipping containers.

rail cars that carry the world's cargo. Today's ocean-going container ships hold more than 2,500 containers.¹⁹

Transportation of products has been revolutionized over time. However, growing transportation poses an increasing threat to the natural environment in terms of the usage of energy and other resources.

Shipbuilders, such as Maersk, have recently introduced container ships that can carry upward of 9,000 40-foot shipping containers. The vessels are so massive that only a handful of international ports can handle them, including Shanghai in China and Rotterdam in the Netherlands. These ships are used mainly to transport goods between Europe and Asia because they are too wide to pass through the Panama Canal. Technological advances in these Triple E vessels provide economies of scale that reduce the cost of transportation dramatically. They are energy efficient and environmentally friendly.²⁰

2.4 Learn the dimensions of globalization.

Dimensions of Market Globalization

The globalization of markets can be characterized by several major dimensions.

- *Integration and interdependence of national economies.* Internationally active firms develop multi-country operations through trade, investment, geographic dispersal of company resources, and integration and coordination of value-chain activities. The collective activities of such firms give rise to *economic integration*, that is, increased trade and other commercial activities among the nations of the world. Governments assist this integration by lowering barriers to international trade and investment, harmonizing their monetary and fiscal policies within *regional economic integration* blocs, and creating *supranational* institutions. These include such organizations as the World Bank, International Monetary Fund, and World Trade Organization.
- *Rise of regional economic integration blocs.* Regional economic integration blocks consist of groups of countries that facilitate reduced trade and investment barriers among themselves. Examples include the North American Free Trade Agreement area (NAFTA), the Asia Pacific Economic Cooperation zone (APEC), and Mercosur in Latin America. In more advanced arrangements, such as a common market, the barriers to the cross-border flow of labor and capital are completely removed. A notable example is the European Union (www.europa.eu). The European Union has adopted free trade among its member countries and harmonized fiscal and monetary policies and business regulations.
- *Growth of global investment and financial flows.* In the process of conducting international transactions, firms and governments buy and sell large volumes of national currencies (such as dollars, euros, and yen). The free movement of capital around the world—the globalization of capital—extends economic activities across the globe. It further increases interconnectedness among world economies. The bond market has gained worldwide scope, with foreign bonds representing a major source of debt financing for governments and firms.

foreign markets, profitably target small national markets, and compete more effectively with foreign competitors that enjoy cost advantages.¹⁸

Transportation

Firms consider the cost of transporting raw materials, components, and finished products when deciding to either export or manufacture abroad. If transport costs to an important market are high, management may decide to manufacture merchandise in that market. The development of fuel-efficient jumbo jets, giant ocean-going freighters, and new transportation technology has greatly reduced shipping times and costs. In recent decades, the volume of international shipping has increased dramatically. For example, world traffic in shipping containers increased from 225 million 20-foot equivalent containers in 2000 to more than 700 million such containers in 2017, a rise of 210 percent. Containers are the big boxes, usually 40 feet long (about 12 meters), loaded on top of ships, trucks, and

- *Convergence of consumer lifestyles and preferences.* Consumers around the world increasingly spend their money and time in similar ways. Many aspects of lifestyles and preferences are converging. Shoppers in New York, Paris, and Shanghai increasingly demand similar household goods, clothing, automobiles, and electronics. Teenagers everywhere are attracted to iPhones, Levi's jeans, and Hollywood movies. Major brands enjoy a global following encouraged by movies, global media, and the Internet. Movies such as *Transformers* and *The Hunger Games* have developed global audiences of fans. Convergence of preferences is also occurring in industrial markets, where professional buyers source raw materials, parts, and components that are increasingly *standardized*—that is, similar or identical in design and structure.
- *Globalization of production.* Intense global competition is forcing firms to reduce their costs of production. Companies cut their costs and selling prices through economies of scale, standardization of finished products, and shifting manufacturing and procurement to foreign locations with less expensive labor. For example, firms in the auto and textile industries have relocated their manufacturing to low labor-cost locations such as China, Mexico, and Poland.
- *Globalization of services.* The services sector—banking, hospitality, retailing, and other service industries—is undergoing widespread internationalization. The real estate firm REMAX has established more than 6,500 offices in some 100 countries. Firms increasingly outsource business processes and other services in the value chain to vendors located abroad. In a relatively new trend, many people go abroad to undergo medical procedures, such as cataract and knee surgeries, to save money.²¹



Source: Robert Harding Picture Library Ltd/Alamy

Google is one of many multinational enterprises that contribute to convergence of consumer lifestyles and preferences.

Firm-Level Consequences of Market Globalization: Internationalization of the Firm's Value Chain

The most direct consequence of market globalization is on the firm's value chain. Globalization compels firms to organize their sourcing, manufacturing, marketing, and other value-adding activities on a global scale to achieve cost advantages and time efficiencies. In a typical value chain, the firm conducts research and product development (R&D), purchases production inputs, and assembles or manufactures a product or service. Next, the firm performs marketing activities such as pricing, promotion, and selling, followed by distribution of the product in targeted markets and after-sales service. The value-chain concept is useful in international business because it helps clarify *what* activities are performed *where* in the world. For example, exporting firms perform many upstream value-chain activities (e.g., R&D and production) in the home market and many downstream activities (e.g., marketing and after-sales service) abroad.

Each value-adding activity in the firm's value chain is subject to internationalization; that is, it can be performed in locations outside the home country. Exhibit 2.6 illustrates a value chain in a typical international firm. As examples in the exhibit suggest, companies have considerable latitude regarding where in the world they can locate or configure key value-adding activities. The most typical reasons for locating value-chain activities in particular countries are to reduce the costs of R&D and production or to gain closer access to customers. Through offshoring, the firm relocates a major value-chain activity by establishing a factory or other subsidiary abroad. A related trend is global outsourcing, in which the firm delegates performance of a value-adding activity to an external supplier or contractor located abroad.

In the same month that German carmaker BMW launched a new factory in South Carolina, an aging textile plant a few miles away, Jackson Mills, closed its doors and shed thousands of workers. Globalization created a new reality for both these firms. By establishing operations in the United States, BMW found it could manufacture cars cost-effectively while more readily accessing

2.5 Understand the firm-level consequences of market globalization.

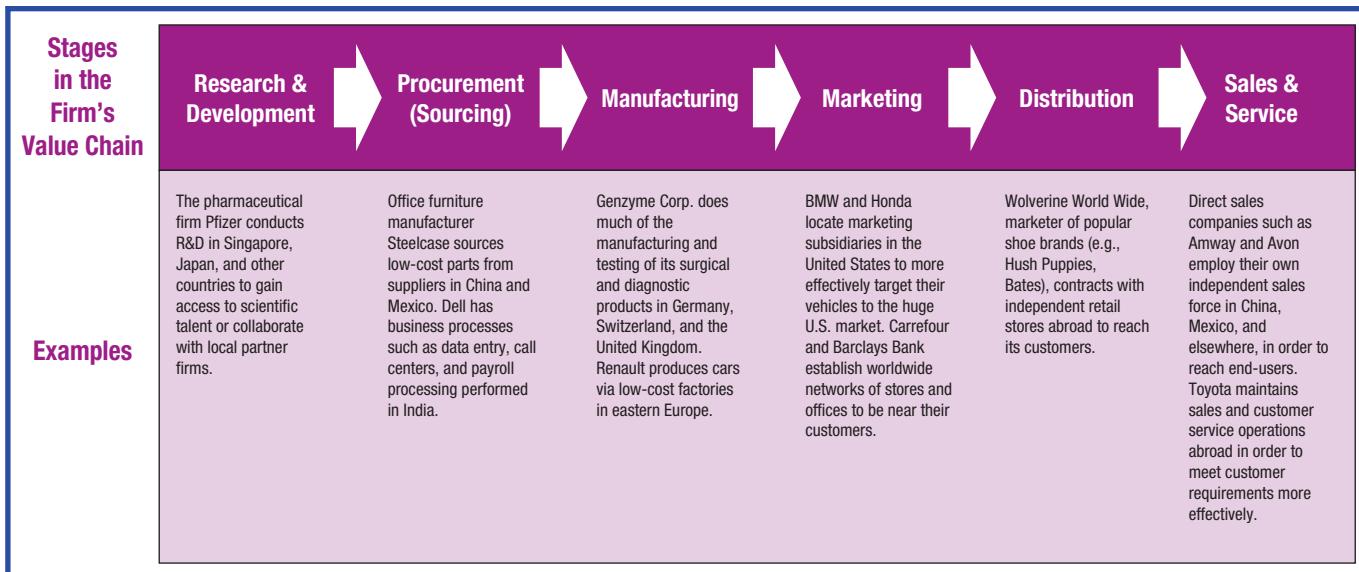


EXHIBIT 2.6

Examples of How Firms' Value-Chain Activities Can Be Internationalized

the huge U.S. market. In the process, BMW created thousands of high-paying, better-quality jobs for U.S. workers. Simultaneously, Jackson Mills had discovered it could source textiles of comparable quality more cost-effectively from suppliers in Asia. Globalization drove these firms to relocate key value-adding activities to the most advantageous locations around the world.

Without a doubt, globalization has created a crowded and intensely competitive global marketplace. As illustrated in Exhibit 2.7, globalization has meant that firms face intense rivalry from foreign competitors. This exhibit shows that in 1989 General Motors, Ford, and Chrysler together held nearly three-quarters of the market share in passenger car sales in the United States. By 2017, the percentage had fallen to 44 percent, and Chrysler had been acquired by the Italian automaker Fiat. The market shares of competitors such as Toyota, Hyundai, and others rose dramatically. Over time, the services sector also has been internationalizing at a fast pace. See the *You Can Do It: Recent Grad in IB* below featuring Terrance Rogers, who is working in the global banking industry.

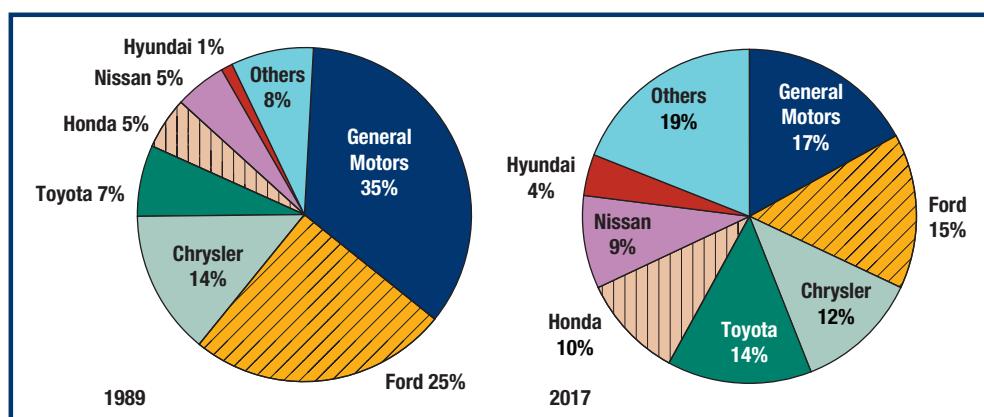
EXHIBIT 2.7

Market Shares of Automakers in Passenger Car Sales in the United States, 1989 and 2017

Sources: Based on Craig Trudell, "U.S. Automakers Seen Losing Market Share amid 2012 Growth: Cars," *Bloomberg BusinessWeek*, February 8, 2012, www.businessweek.com; J. Muller, "Automakers Gold Rush," *Forbes*, June 8, 2009, pp. 70–77; *Wall Street Journal*, "Sales and Total Share of Market by Manufacturer," February 1, 2018, www.wsj.com/mdc/public/page/2_3022-autosales.html.

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 Rudi's Bakery Management in the Global Environment.



You Can Do It

RECENT GRAD IN IB



TERRANCE ROGERS

Terrance's Majors: Finance and international business

Objectives: Exploration, international perspective, self-awareness, career growth, and learning about foreign markets

Internships during college: Deutsche Bank

Jobs held since graduating:

- Business analyst at Deutsche Bank, New York
- Management associate at Deutsche Bank, New York
- Executive management rotation at Deutsche Bank, New York
- Executive management associate at Deutsche Bank, London and New York

After taking his first international business course, Terrance became fascinated with the idea of working abroad. As a university student, he enrolled in his college's International Business Certificate program. The program allowed Terrance to combine his passion for finance with his appetite for learning about culture and doing business abroad. Terrance took his first international trip through a short study abroad course. The course, "Financial and Managerial Issues in the EU," brought him to Paris and Brussels. Terrance and his classmates visited prominent businesses and the European Union offices to hear from leaders across multiple sectors. The experience allowed Terrance to believe that working abroad could be a real possibility for him.

After graduation, Terrance started his career as a business analyst with Deutsche Bank in New York. The position gave him experience in regulatory change, process improvement, and crisis management. Terrance got the opportunity to work on several global projects. After being promoted to management associate, Terrance worked directly with the chief operations officer of the Americas for his division.

After spending four years gaining experience in various areas of the bank,

Terrance took a position with numerous international responsibilities. Today, Terrance is an executive management associate, leading business strategy, finance analysis, and communications for the United Kingdom Executive Team. In this role, he splits his time between London and New York. He is responsible for interpreting financial drivers, product strategy, and operational issues that shape each business line in the region. He works directly with the head of Marketing and Communications to craft and execute communication strategy for the chief executive officer.

Terrance's Advice for an International Career

Terrance owes his success to early exposure at his university to international business and study abroad. Terrance says that "international careers are a requirement for today's business leaders. Major clients don't just reside in the U.S. anymore, so if you want to have a long impactful career, you must find a way to gain some international exposure. Your boss will rely on you to be able to work with business associates from different cultures. Your clients will expect you to understand issues with a global perspective, and if you don't have

any global experience, your competitors (for jobs and clients) will be one step ahead of you."

Success Factors

"If you want to work abroad, do the following things to increase your chances at securing an international role: (a) Work on projects that expose you to people in different regions across the globe; (b) mention your interest in working abroad early and bring it up in your annual review; and (c) find a way to impress the people who can make the decision. It becomes easier to make the move when the 'right people' know that you can deliver."

Challenges

"Challenges like language barriers and cultural differences are things that should be faced as soon as you can in your career. Don't be afraid to make a mistake. It's much better to learn from cultural missteps now so that you can be a better business leader tomorrow." Globalization is a major dimension of business today.

Source: Courtesy of Terrance Rogers.

2.6 Understand the societal consequences of globalization.

Societal Consequences of Globalization

Our discussion so far has highlighted the far-reaching, positive outcomes of globalization. Major advances in living standards have been achieved in virtually all countries that have opened their borders to increased trade and investment.²² Yet the transition to a global marketplace also poses challenges to individuals, organizations, and governments. Low-income countries have not been able to integrate with the global economy as rapidly as others have. Poverty remains a major problem in Africa and in populous nations such as Brazil, China, and India.²³ Let's consider some of the unintended consequences of globalization.

Contagion: Rapid Spread of Monetary and Financial Crises

The world economy has experienced numerous financial and monetary crises. In 2008, for example, a major financial crisis was triggered by unsustainably high prices in housing and commodities. As real estate prices tumbled, many owners were left with mortgage debts greater than the value of their homes. Tens of thousands of those mortgages had been bundled and sold as investments on stock markets worldwide. As the value of these homes and securities plunged or became uncertain, stock markets also plunged.²⁴ The crisis began in the United States and spread around the world, like a contagious disease.

Contagion

The tendency of a financial or monetary crisis in one country to spread rapidly to other countries due to the ongoing integration of national economies.

In international economics, **contagion** refers to the tendency for a financial or monetary crisis in one country to spread rapidly to other countries due to integrated national economies.²⁵ For example, excessive consumer borrowing can give rise to instability or overheating of national economies. Resultant crises can be aggravated by insufficient or ill-conceived regulation of the financial and banking sector or of the economy at large. As we will see later in this text, having a strong legal and regulatory framework is critical to national economic well-being.²⁶

Financial or economic crises may weaken consumer confidence and reduce spending on consumer goods, services, and other consumables. Decreased spending, in turn, affects global commerce and international trade.²⁷ Following the crisis that began in 2008, global growth declined to levels not seen since World War II. Many national economies did not begin to recover until 2010. Economies in Japan and several countries in Europe have remained sluggish.²⁸

Exhibit 2.8 shows how GDP growth in advanced, developing, and emerging economies varies over time. GDP in all three of these economies declined substantially during the recent global recession and financial crisis. One lesson of the exhibit is that, even following deep recessions, the global economy has always rebounded, and countries' GDPs have returned to growth.

Loss of National Sovereignty

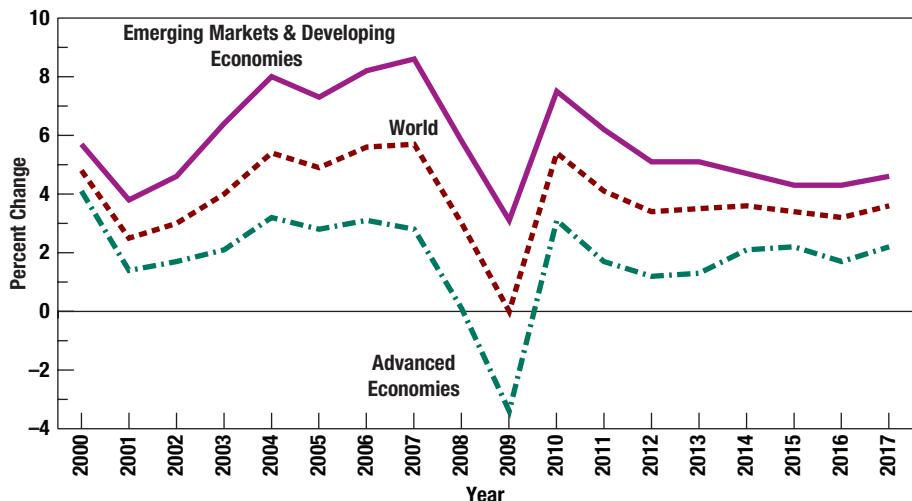
Sovereignty is defined as the ability of a nation to govern its own affairs; normally one country's laws cannot be applied or enforced in another country. Globalization, however, can threaten national sovereignty in various ways. MNE activities can interfere with a government's ability to control its own economy, social structure, and political system. Some corporations are bigger than the economies of small nations; Walmart's internal economy—its total revenues—is larger than the GDP of many of the world's nations, including Israel, Greece, and Poland. Large multinational firms can apply much pressure on governments through lobbying or campaign contributions and can frequently influence the legislative process.

The largest firms are constrained by market forces. In countries with many competing firms, one company cannot force customers to buy its products or force suppliers to supply it with raw materials and inputs. Resources that customers and suppliers use are made through free choice.

EXHIBIT 2.8

Percentage of Change in Annual GDP Growth

Sources: World Bank, Data, GDP Growth (Annual %), <http://data.worldbank.org>, 2017; IMF, *World Economic Outlook* (Washington, DC: International Monetary Fund, September 2017); IMF, *World Economic Outlook Database*, 2017, www.imf.org; United Nations, UNData, "GDP Growth (annual %)," 2017, <http://data.un.org>.



Company performance depends on the firm's skill at winning customers, working with suppliers, and dealing with competitors. Corporate dominance of individual markets is rare. In reality, market forces generally dominate companies. For example, Ford, Chrysler, and General Motors once dominated the U.S. auto market. Today, many more automotive firms—Toyota, Honda, Hyundai, Nissan, and Volkswagen—compete in the United States, along with newcomers such as Tesla. Volkswagen now leads the global market in annual unit sales. Home-country market shares of domestic U.S. automakers have tumbled.²⁹

To minimize globalization's harm and reap its benefits, governments should ensure the freedom to enter and compete in markets, protect private property, enforce the law, and support voluntary exchange through markets rather than through political processes. Banks and financial institutions should be regulated appropriately. Transparency in the affairs of business and regulatory agencies is critical.

Offshoring

Globalization has created countless new jobs and opportunities worldwide, but it also has cost many people their jobs. Ford and General Motors have laid off thousands of workers in the United States, partly the result of competitive pressures posed by carmakers from Europe, Japan, and South Korea. Ford, GM, and Volkswagen all have transferred thousands of jobs from their factories in Germany to countries in Eastern Europe.³⁰ *Offshoring* is the relocation of manufacturing and other value-chain activities to cost-effective locations abroad. For example, the global accounting firm Ernst & Young relocated much of its accounting support work to the Philippines. Massachusetts General Hospital has its CT scans and X-rays interpreted by radiologists in India. Many IT support services for customers in Germany are based in the Czech Republic and Romania.³¹

High-profile plant closures and manufacturing relocation have received much media attention. For example, Polaris, the U.S. manufacturer of all-terrain vehicles, moved its Wisconsin factory to Mexico to reduce production costs. In Australia, Toyota closed a Camry factory, resulting in the loss of thousands of jobs. Such closures disrupt local communities in various ways.³²

Simultaneously, however, MNEs create millions of jobs abroad, which help raise living standards. For example, U.S. MNEs now employ about a million workers in each of Canada, China, Mexico, and the United Kingdom.³³ In developing economies and emerging markets, such positions help raise living standards.

Reshoring

MNEs sometimes engage in *reshoring*—the return of manufacturing and services back to the home country. It is the opposite of *offshoring* which refers to the relocation of manufacturing to a foreign country, usually to take advantage of low-cost labor. For example, Ford and Boeing have reshored thousands of jobs back to the United States. Reshoring is done for various reasons, including the rise of wages and other business costs in emerging market countries as well as the desire to manage operations more effectively and locate value-chain activities closer to customers. General Electric reshored the production of energy-efficient water heaters from China back to the United States in order to manage inventory and transportation costs better. Symington's, a British food company, moved noodle production from China back to England in order to improve product quality, increase delivery speed, and manage the supply chain more effectively.³⁴

Effect on the Poor

Globalization has affected the poor in areas related to income distribution and worker exploitation by MNEs. *Income distribution* refers to the allocation of GDP and national income among the members of a society. In some countries, a relatively small minority, often less than 10 percent, holds most of the country's wealth, and the great majority of citizens live in poverty. This income inequality is substantial in several nations in Southern Africa and in Latin America, for example. Among the advanced economies, income inequality is less of a factor in Japan and most countries in Northern Europe due mainly to cultural factors and public policies. Income inequality is relatively more common in the United States, which is home to many highly paid executives and other wealthy individuals.

As nations' economies develop and per-capita incomes rise, globalization can worsen income inequality because many good-paying jobs in the manufacturing sector are lost as companies shift



Source: Peter Cook/Dorling Kindersley

Media attention and consumer concern are helping to improve wages and sweatshop conditions slowly in developing economies, such as those in South Asia.

children educational opportunities. It is estimated there are more than 215 million children aged 5 to 17 at work around the world. About 73 million children are believed to work in hazardous conditions.³⁶

Bangladesh, China, Colombia, Egypt, and the Philippines are examples of countries often characterized by poor working conditions. In Egypt, employees who strike or protest poor working conditions can be jailed. In China, many factory workers earn less than \$3 per day and may have to work long hours. Companies ranging from Nike to H&M to the Gap have been accused of tolerating sweatshop conditions in their factories overseas.³⁷

MyLab Management Watch It! 3

If your professor has assigned this, go to the Assignments section of www.pearson.com/mylab/management to complete the video exercise titled Save the Children Social Networking.

Labor exploitation and sweatshop conditions are major concerns in many developing economies.³⁸ But some ask, “What other employment choices are available to poorly educated people?” A low-paying job is usually better than no job at all. Studies suggest that banning products made using child labor may produce unintended negative consequences such as reduced living standards for families.³⁹ Legislation passed to reduce child labor in the formal economic sector (the sector regulated and monitored by public authorities) may have little effect on jobs in the informal economic sector, sometimes called the *underground economy*. In the face of persistent poverty, abolishing formal sector jobs does not ensure that children leave the workforce and go to school.

Work conditions and salaries tend to improve, over time, in many developing countries. The growth of the footwear industry in Vietnam translated into a fivefold increase in wages. While still low by advanced economy standards, those growing wages are improving the lives of millions of workers and their families. Globalization tends to support a growing economy. Countries that liberalize international trade and investment enjoy faster per-capita economic growth. Developing economies that seek to integrate with the rest of the world tend to have faster per-capita GDP growth than those that fail to participate in the world economy.⁴⁰

Exhibit 2.9 shows the global GDP growth rate from 2009 to 2018. Most nations are experiencing positive growth. The fastest-growing large economies are China and India. Exhibit 2.10 reveals that, on average, global poverty is declining over time.⁴¹ This exhibit

production to low-wage countries. In the advanced economies, growing international trade coincided with falling wages in many industries as firms transferred manufacturing jobs to lower-cost countries, such as China and Mexico. However, income inequality is a complex and dynamic phenomenon. While the creation of new manufacturing jobs has increased wages for many individuals in China, Mexico, and other emerging markets, income levels among other, often larger groups in such countries have remained relatively stagnant.

In addition, automation and technology, to a large extent, have resulted in lower incomes for many people. Just as demand for high-skill workers has increased, demand for lower-skill or less-educated workers has decreased. This arises because many jobs that historically were done by low-skill workers are now performed by machines and digital platforms.³⁵

Many MNEs have been criticized for paying low wages, exploiting workers, and employing child labor. Child labor is particularly troubling because it denies

illustrates the income status of people in developing economies. Poverty remains a major factor in South Asia and sub-Saharan Africa (that part of Africa below the Saharan Desert), but even those areas have made much progress in the past decade. The Middle East and North Africa, Latin America, and East Asia are home to billions of people whose daily incomes have risen substantially. Much of these improvements are due to international trade and investment activities.⁴²

Effect on Sustainability and the Natural Environment

Globalization promotes manufacturing and economic activity that result in increased pollution, habitat destruction, and deterioration of the ozone layer. In China, for example, economic development is attracting much inward FDI and stimulating the growth of numerous industries. The construction of factories, infrastructure, and modern housing can spoil previously pristine environments. In eastern China, growing industrial demand for electricity led to construction of the Three Gorges Dam, which flooded agricultural lands and permanently altered the natural landscape. See the *Apply Your Understanding* exercise at the end of this chapter, which presents an Ethical Dilemma problem on the environmental damage done by a large oil company in Nigeria.

As globalization stimulates rising living standards, concerned citizens focus on improving their environment. Over time, governments pass legislation that promotes improved environmental conditions. For example, Japan endured polluted rivers and smoggy cities in the early decades of its economic development following World War II. As its economy grew, the Japanese passed tougher environmental standards to restore their natural environment.

Evolving company values and concern for corporate reputations have led many firms to reduce or eliminate practices that harm the environment.⁴³ In Mexico, for example, big automakers such as Ford and General Motors have gradually improved their environmental standards. Alcan in Canada (aluminum), Kirin in Japan (beverages), and Google in the United States (Internet services) are examples of firms that embrace practices that protect the environment, often at the expense of profits.⁴⁴ The Conservation Coffee Alliance has committed approximately \$2 million to environmentally friendly coffee cultivation in Central America, Peru, and Colombia.

Effect on National Culture

Globalization exerts strong pressures on national culture because market liberalization exposes local consumers to global brands, unfamiliar products, and different values. People worldwide are exposed to movies, television, the Internet, and other information sources that promote lifestyles of people in the United States and other advanced economies. Appetites grow for Western products and services, which are seen to signal higher living standards. For example, despite low per-capita income, many Chinese buy consumer electronics such as smartphones and TV sets. Advertising disseminates societal values modeled on Western countries. Hollywood dominates the global entertainment industry.

The flow of cultural influence often goes both ways, too. Cafe Spice is an Indian food company whose founder hails from Mumbai. The firm is transforming American tastes by selling curry dishes and other Indian favorites in cafeterias and supermarkets. Cafe Spice is helping to make Indian cuisine mainstream in the United States.⁴⁵ As the influence of the Chinese economy grows over time, Western countries will likely adopt some of China's cultural attitudes and behaviors. Chinese restaurants and some Chinese traditions are already a way of life in much of the world. Similar influences are evident from Latin America and other areas in the developing world.



Source: Sergey Zhukov/Shutterstock

Western companies can influence food preferences, but cultural values tend to remain stable over time. This Burger King is in Bangkok, Thailand.



EXHIBIT 2.9

The Growth of World GDP, Average Annual GDP Growth Rate, 2009–2018 (%)

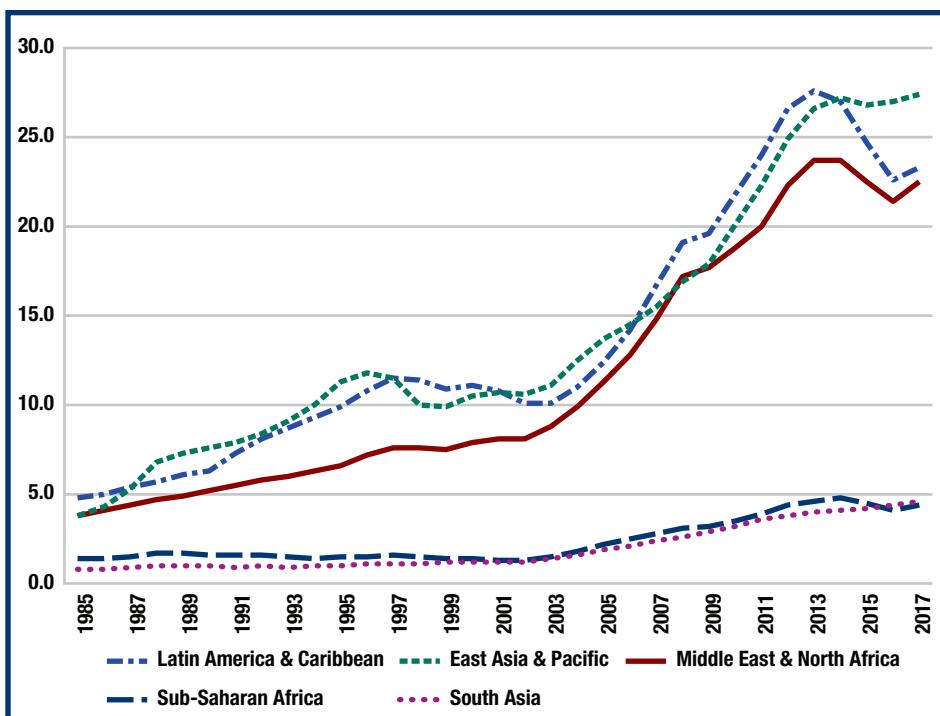
Source: International Monetary Fund, World Economic Outlook database, 2018, www.imf.org.



EXHIBIT 2.10**The Rise of Daily Income Levels, by Region, in U.S. Dollars**

Sources: L. Chandy, N. Ledlie, and V. Penciakova, *The Final Countdown: Prospects for Ending Extreme Poverty by 2030*, Policy Paper 2013–14 (Washington, DC: Brookings Institution); *Economisthttp://data.worldbank.org.*

Note: The figures show average daily income per capita, in U.S. dollars, adjusted for inflation.



Cultural imperialism is offset by the countertrend of local nationalism. Although many products and services have become largely universal, people's behaviors and attitudes remain relatively stable over time. Religious differences are as strong as ever. Language differences are steadfast across national borders. As globalization standardizes superficial aspects of life across national cultures, people resist these forces by insisting on their national identity and taking steps to protect it. For example, laws exist to protect national language and culture in Belgium, Canada, and France.

Globalization and Africa

Africa is home to the poorest countries. The majority of its 1 billion people live on less than \$5 a day. It is the area least integrated into the world economy and accounts for less than 5 percent of world trade. Although it has abundant natural resources, Africa remains underdeveloped due to many factors, including an inadequate commercial infrastructure, lack of access to foreign capital, high illiteracy, government corruption, wars, and the spread of AIDS.

Experience of the past half century suggests that traditional methods of trying to help Africa—mainly foreign aid provided by advanced economies—have achieved little success. Despite billions of dollars of aid to Africa, per-capita income is increasing relatively slowly.⁴⁶

One of the most effective ways to alleviate African poverty is to develop more business-based models of development.⁴⁷ Several sub-Saharan African countries have recently experienced significant economic growth by increasing international trade in commodities. Africa is a major supplier of petroleum to Europe and the United States. Angola is among the top oil suppliers to China. This activity has developed a ripple effect of economic development. Because of the boom of certain sectors in Africa, there has been an increase in foreign banks, retailers, and MNE operations in the continent.⁴⁸

Rwanda had developed business opportunities in sectors as diverse as mining, tourism, telecommunications, and real estate. China and India are beating out U.S. firms and quickly increasing their business dealings in Africa. Chinese companies are investing billions of dollars in the continent. All this international trade and investment is helping to address many of Africa's most pressing development needs.⁴⁹ Samsung has set a goal of \$10 billion in African sales and is committed to training 10,000 African engineers and technicians to develop the capabilities

needed for success. Even so, it will take many more years for Africa to achieve a critical mass of infrastructure and business culture sufficient to raise average incomes substantially across the continent.

Technology plays an increasing role in reducing poverty. Increasing use of mobile phones, satellite technology, and IT is helping farmers in Africa to increase crop yields and agricultural productivity. IT is being used to develop databases of information that support farmers in minimizing crop damage and improve farming methods. Data obtained from satellite technology helps farmers assess the likelihood of draught and prepare accordingly.⁵⁰

CLOSING CASE

A Debate on the Good and Harm of Globalization

People around the world are concerned about the impact of globalization, which they associate with job losses, declining national sovereignty, mass migration, and an intrusion of foreign values. Globalization has become a central theme in political, economic, and academic discourse. Recently, a major university sponsored a roundtable on the broader implications of globalization. The participants were an anti-globalization activist, a business executive, and a government trade official. Excerpts from the exchange provide diverse perspectives on globalization and international business.

Activist

"One problem with international business is that it often ignores human rights and basic labor standards. Low-wage factories abroad create substandard working conditions. The activities of multinational companies not only result in job losses here at home, but also in low wages and exploited workers around the world. Just think of the sweatshops in Asia that make imported clothing. Think of the autoworkers in Mexico who live in horrible conditions and make only a few dollars a day. Also consider the poverty caused worldwide by the recent global financial and economic crisis."

Business Executive

"Our country needs to participate in the global economy. Companies that export provide better-paying jobs, have more profits, pay higher taxes, and stimulate purchases from local suppliers. Foreign companies that invest here create new jobs, enhance local living standards, and pressure our firms to stay competitive in a challenging global marketplace. Exporters pay higher wages and provide better benefits than non-exporting firms do. Many companies need access to foreign markets because of the huge, upfront research and development costs they accumulate. One more pill is cheap; it's the cost of research to find a cure for AIDS that is prohibitive. Pharmaceutical firms can't do the necessary R&D unless they can amortize those costs over a huge, global marketplace. In the long run, uninterrupted international commerce is good."

Trade Official

"The current administration believes in the value of free trade. The government strongly supported NAFTA, and this has already had a positive effect on the economy through increasing exports to Mexico, creating jobs, and leading to improved investment opportunities. Countries are forging ahead with international trade ties.

Canada has completed a free trade agreement with Chile. Economic ties lead to cultural ties and more peaceful relations. Also, it's hard for our government to promote freedom and democracy around the world if we're not promoting free trade."

Activist

"We cannot overlook the detrimental effects of globalization on the natural environment. The more we trade internationally, the more irreparable harm will be done to the environment. International business means more environmentally damaging development. Companies internationalize so they can become more efficient. But if countries have weak environmental standards, then factories will be built with minimal environmental standards."

Business Executive

"If we trade internationally, then living standards will increase everywhere. As living standards rise, awareness of and care for the environment will also increase. International business is good for the world because it creates wealth. The more affluent the people, the more they will care about their environment and pass laws to protect it. We are also becoming more responsive to concerns over social responsibility and environmental degradation. We have shown that a good economy and a clean environment are not mutually exclusive. We can have it both ways: a clean planet and a better quality of life."

Trade Official

"I think part of the solution is to negotiate trade agreements that take environmental factors into account. International trade that disregards legitimate environmental concerns is counterproductive and defeats the political agendas of most governments around the world. It is clear that international trade must take environmental concerns into account."

Activist

"International trade interferes with the sovereignty of national governments. When Apple or Toyota are bigger than most countries in Africa, it is harder for governments to manage policies regarding taxes, monetary policy, social issues, and exchange rates. And who are we, trying to impose our own cultural standards on the world? When I travel in Asia or Latin America, I see McDonald's all over the place. They see Western powers exploiting globalization, harming the economic, cultural, and environmental interests of the rest of the world."

"Global corporations claim they spread modern technologies around the world. But technology is good only if you have access to it. In Africa, you have no on-ramp to the Internet. You need access to a computer, which is difficult or impossible in countries where people make only a few dollars a day. When you're paid such a low wage, how can you afford technology? How can you afford to see a doctor? Globalization is widening the gap between rich and poor. As inequality grows, people have less and less in common. Multinational companies exploit poor countries and expose their people to harmful competition. Infant industries in developing economies can't make it when they're confronted with the power of giant multinational firms."

Business Executive

"Companies increasingly recognize the importance of being good global citizens. Motorola has profited from its business in China, but it also contributes to developing educational systems in that country. There are more literate people, especially literate women, in China than ever before. Japanese MNEs invest in the communities where they do business. Companies are not all evil; they do a lot of good for the world, too. Bill Gates is doing more than any government to get people computers and connect them to the Internet. He has created the world's biggest fund to combat diseases of the poor. He and Warren Buffett are tackling many of these diseases. GlaxoSmithKline is working with the World Health Organization to find a cure for elephantiasis, a terrible disease that ravages people in Africa."

Trade Official

"Globalization is complex and it's hard to tease out the good and the bad. Globalization has made rapid progress. Global poverty has declined and social indicators are improving around the world. It's true that income disparities have increased over the past 50 years while international trade has integrated the world economy. But the world has experienced a generally rising tide in terms of living standards. People everywhere are better off than they were

50 years ago. There are some exceptions to this, especially during recessions, but it's better to live in a world where 25 percent of the people are affluent and 75 percent are poor than a world in which nearly 100 percent of the people are poor, as was the case throughout most of history. There is a strong role for government in all this. Countries benefit from trade, but governments are responsible for protecting citizens from the negative or unintended consequences that trade may bring."

Activist

"Governments have not done enough to regulate the excesses of capitalism. We saw this clearly in the recent global financial and economic crises."

The Outlook for Globalization

In recent years, nationalistic sentiment has triggered an "our country first" mentality and skepticism or outright hostility toward globalization. The election of Donald Trump as president of the United States gave way to anti-trade policies and efforts to reduce immigration. After taking office, the Trump administration began renegotiating the North American Free Trade Agreement (NAFTA) and withdrew from the Trans-Pacific Partnership (TPP). In 2016, the United Kingdom voted to withdraw from the European Union. "Brexit" voters were motivated by concerns about national sovereignty and increasing immigration into the United Kingdom. Elsewhere in Europe, nationalist political parties came to power, reflecting a popular backlash against open borders and unfettered globalization.

Labor unions, human rights activists, environmentalists, and religious groups are among those opposed to globalization. Recent events represent a step backward from long-standing forward movement on free trade and global commerce. Many experts view the backlash as a predictable, temporary pause in the evolution of globalization. They argue that large-scale transformations often progress in fits and starts—one step back for every two steps forward. However, no one knows for sure what the future holds. Is globalization receding, or is it here to stay?

AACSB: Written and Oral Communication, Ethical Understanding and Reasoning, Reflective Thinking, Diverse and Multicultural Work Environments

Case Questions

- 2-4.** Do you think globalization and MNE activity are creating problems for the world? What kinds of problems can you identify? What are the unintended consequences of international business?
- 2-5.** Summarize the arguments in favor of globalization that the business executive made. What is the role of technology in supporting company performance in a globalizing business environment?
- 2-6.** What are the roles of state and federal governments in dealing with globalization? What is government's role in protecting citizens from the potential negative effects of globalization? What kinds of government actions would you recommend?
- 2-7.** What is the role of education in (1) addressing the problems raised in the roundtable, (2) creating societies in which people can deal effectively with public policy issues, and (3) cultivating citizens who can compete effectively in the global marketplace?

- 2-8.** Do you believe globalization is receding or advancing? Defend your answer.

Sources: Jacques Bughin, Susan Lund, and James Manyika, "Harnessing the Power of Shifting Global Flows," *McKinsey Quarterly*, February 2015, pp. 1–13; "The Globalization Website," retrieved from Emory University Globalization website, www.sociology.emory.edu/globalization; J. Rennie Short, "Globalization and Its Discontents: Why There's a Backlash and How It Needs to Change," *The Conversation*, November 26, 2016, theconversation.com; K. Ahmed, "TPP: What Is It and Why Does It Matter?", BBC, January 23, 2017, www.bbc.com; L. Elliot, "Brexit Is a Rejection of Globalisation," *The Guardian*, June 26, 2016, www.theguardian.com; N. Saval, "Globalisation: The Rise and Fall of an Idea That Swept the World," *The Guardian*, July 14, 2017, www.theguardian.com; P. Goodman, "More Wealth, More Jobs, but Not for Everyone," *New York Times*, September 28, 2016, www.nytimes.com.

This case was written by Mourad Dakhli and 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

contagion 78
globalization of markets 64

value chain 64
World Trade Organization (WTO) 65

Summary

In this chapter, you learned about:

- **Market globalization as an organizing framework**

Globalization of markets refers to the gradual integration and growing interdependence of national economies. Early civilizations in the Mediterranean, Middle East, Asia, Africa, and Europe all contributed to the growth of cross-border trade. Today's international trade was triggered by world events and technological discoveries and has progressed in phases, particularly since the early 1800s. The current phase was stimulated particularly by the rise of IT, the Internet, digital platforms, and other advanced technologies. The World Trade Organization is a multilateral governing body empowered to regulate international trade and investment.

- **The driving forces of globalization**

Globalization is driven by several factors, including falling trade and investment barriers; market liberalization and adoption of free market economics in formerly closed economies; industrialization and economic development, especially among emerging markets; integration of world financial markets; and technological advances.

- **Technological advances and globalization**

Advances in technology, the most important of which have occurred in information technology, digitalization, communications, the Internet, manufacturing, and transportation, are particularly important in driving globalization. These systems help create an interconnected network of customers, suppliers, and intermediaries worldwide and have made the cost of international business affordable for all types of firms.

- **The dimensions of globalization**

Globalization can be modeled in terms of its driving forces, dimensions, societal consequences, and firm-level consequences. Globalization refers to the growing integration of the world economy from the international business activities of

countless firms. It represents a growing global interconnectedness of buyers, producers, suppliers, and governments and has fostered a new dynamism in the world economy, the emergence of regional economic integration blocs, growth of global investment and financial flows, the convergence of buyer lifestyles and needs, and the globalization of both production and services. At the business enterprise level, globalization amounts to reconfiguration of company value chains—the sequence of value-adding activities, including sourcing, manufacturing, marketing, and distribution—on a global scale.

- **Firm-level consequences of market globalization**

Globalization compels firms to organize their sourcing, manufacturing, marketing, and other value-adding activities on a global scale. Each value-adding activity can be performed in the home country or abroad. Firms choose where in the world they locate or configure key value-adding activities and internationalize value-chain activities to reduce the costs of R&D and production or gain closer access to customers.

- **Societal consequences of globalization**

There is much debate about globalization's benefits and harm. Globalization was a major factor in the recent global recession and financial crisis. Critics complain that globalization interferes with national sovereignty, the ability of a state to govern itself without external intervention. Globalization is associated with *offshoring*, the relocation of value-chain activities to foreign locations where they can be performed at less cost by subsidiaries or independent suppliers. Globalization tends to decrease poverty, but it may also widen the gap between the rich and the poor. Furthermore, unrestricted industrialization may harm the natural environment. Globalization is also associated with the loss of cultural values unique to each nation. Nevertheless, trade and investment can help address many needs of developing countries, especially those of Africa.

Test Your Comprehension

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

- 2-9.** What was the precursor to globalization, and why was it important?
- 2-10.** What important changes happened during the second phase of globalization?
- 2-11.** Summarize the six dimensions of globalization. Which of these do you think is the most visible manifestation of globalization?
- 2-12.** Describe the five driving forces of globalization.
- 2-13.** What is the role of the World Trade Organization?
- 2-14.** In what areas have technological advances had their greatest effect on facilitating world trade and investment?
- 2-15.** How can internationalization improve value adding opportunities for a business?
- 2-16.** What are the conditions under which contagion spreads from country to country?
- 2-17.** It is possible for an organization to add value through overseas operations?

Apply Your Understanding

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

- 2-18.** In 2017, the Singapore's Deputy Prime Minister Tharman Shanmugaratnam stated that the country was aiming to become a key part in the global value chain. The statement was made in the wake of the U.S. electronics firm Jabil announcing that they would be setting up a new manufacturing research and development facility in Singapore. For the minister, it showed that Singapore was well placed to provide all that was necessary to shorten value chains and enable products to be made much closer to the final marketplace. The net result was Jabil Blue Sky Singapore, which operates as an innovation and collaboration hub. How can a country secure a place in the global value chain? What are the advantages to a business in locating in such a country?
- 2-19.** Globalization provides numerous advantages to businesses and consumers around the world. At the same time, some critics believe globalization is harming various aspects of life and commerce.

In what ways is globalization good for firms and consumers? In what ways is globalization harmful to firms and consumers?

- 2-20.** *Ethical Dilemma:* Northern Energy, Inc. (Northern) is a large oil company with production and marketing operations worldwide. You are a recently hired manager at Northern's subsidiary in Nigeria, which provides jobs to hundreds of Nigerians and supports many local merchants and suppliers. Suppose Northern's drilling and refining practices have severely damaged the natural environment in Nigeria, polluting the air, land, and water. As a result, Northern has faced violent protests and much negative publicity in Nigeria. Develop suggestions for how Northern should address these issues. Keep in mind that top management is reluctant to invest significant new resources in Nigeria, given the firm's weakening business performance there.



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 Communications, Information Technology, Analytical Thinking, Diverse and Multicultural Work Environments, Application of Knowledge

- 2-21. The KOF Swiss Economic Institute prepares the annual *KOF Index of Globalization*, which ranks the most globalized countries (enter "KOF Index of Globalization" at globalEDGE™ or other search engine). The index uses three dimensions to measure globalization: *economic globalization*, *political globalization*, and *social globalization*. Visit the index, and explain what each dimension represents and why each is important for a nation to achieve a substantial presence in the global economy.
- 2-22. Production in the manufacturing and services sectors increasingly has been outsourced to lower-cost locations abroad. The globalEDGE™ website has various resources that detail the nature and location of jobs that have been transferred abroad. Some experts note that the resulting foreign investment and increased demand in lower-cost countries are causing wages to rise in those countries, eliminating cost advantages from offshoring and narrowing the income gap between advanced economies and low-cost countries. In other words, offshoring is helping to reduce poverty in less developed economies. Others believe that manufacturing jobs will be consistently moved to lower-cost countries, turning China, India, and other emerging markets into top platforms for innovation and production. What do you think? Find three articles about outsourcing at globalEDGE™ by doing a search using the keywords "global outsourcing" or "offshoring," and write a report on the most likely consequences of these trends for your country, its workers, and its consumers.
- 2-23. A key characteristic of globalization is the increasingly integrated world economy. MNEs and many nations have a stake in maintaining the globalization trend. If the trend were somehow reversed, participants in international business, such as exporters, likely would suffer big economic losses. In many ways, globalization's role in the world economy is critical. But just how big is the global economy? What is the extent of international trade relative to the size of the global economy? What is the proportion of international trade in the GDPs of each of the following countries: Australia, Canada, Sweden, United Kingdom, and the United States? Consult globalEDGE™ to address these questions.
- 2-24. Globalization refers to the reduction of barriers to trade and investment, which is facilitating the internationalization of countless firms. Globalization is quickening and affecting firms around the world. However, it's also associated with various issues and challenges that confront firms as they undertake international business. Among the major issues are conditions in individual economies, indebtedness of national governments; power shifts to emerging markets, country risk in the developing economies, and environmental harm caused by industrialization. Visit globalEDGE™, and enter the keyword "globalization." Explore the information and websites that emerge from your search. Write a report on the most important contemporary issues that firms are facing as they undertake international business.

Endnotes

1. This discussion is based on Lawrence Beer, *Tracing the Roots of Globalization and Business Principles* (New York: Business Expert Press, 2011).
2. The word *trade* comes from the Anglo-Saxon term *trata*, which means "to walk in the footsteps of others." Ancient trade routes were the foundation for a high level of cross-cultural exchange of ideas that led to the development of religion, science, economic activity, and government. The phrase "all roads lead to Rome" is not so much a metaphorical reference to Rome's dominance

of the world 2,000 years ago but to the fact that Rome's territorial colonies were constructed as commercial resource centers to serve the needs of the Roman Empire and increase its wealth. In an empire that stretched from England to Israel and from Germany to Africa, the Romans created more than 300,000 kilometers of roads. Roman roads were the lifeblood of the state that allowed trade to flourish. The Roman Empire was so concerned about the interruption of its shipping lanes for imported goods that it dispatched army legions to protect those lanes.

In the Middle Ages, the Knights Templar acted as guardians for pilgrims making the hazardous journey to pay homage to the birthplace of the Christian religion. In addition to protecting tourists, this warrior order created the first international banking system with the use of rudimentary traveler's checks, eliminating the need for travelers to carry valuables on their person.

In 1100, Genghis Khan not only united the Mongols but created an empire beyond the Chinese border that included Korea and Japan in the east, Mesopotamia (modern-day Iraq and Syria), Russia, Poland, and Hungary. He instituted common laws and regulations over his domain, most notably for the preservation of private property, to enhance and protect international trade.

Arab merchants traded in spices along land routes reaching from northern Arabia across modern-day Turkey, through Asia Minor, and finally reaching China. By concealing the origins of cinnamon, pepper, cloves, and nutmeg, traders gained a monopoly and controlled prices. Europeans came to believe that the spices came from Africa, when in fact they had merely changed hands in the region. Under the traditional trading system, spices, linen, silk, diamonds, pearls, and opium-based medicines reached Europe by indirect routes over land and sea. Representing one of the earliest systems of international distribution, the products passed through many hands on their long voyage. At every juncture, prices increased several fold. (This discussion is based on Lawrence Beer, 2011.)

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Part 2 | The Environment of International Business

Chapter 3

The Cultural Environment of International Business

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

- 3.1** Understand culture and cross-cultural risk.
- 3.2** Learn the dimensions of culture.
- 3.3** Describe the role of language and religion in culture.
- 3.4** Describe culture's effect in international business.
- 3.5** Learn models and explanations of culture.
- 3.6** Understand managerial implications of culture.

Hallyu and the Rising Influence of the Korean Global Culture

Culture matters in international business. Some of the ways it intersects with business are immediately evident; others are less so. Diasporas are often the first to spread the customs of their countries of origin, often shaping the cities they exist in to a degree that far surpasses the size of their communities. In more recent times, the proliferation of expats (short for “expatriates,” meaning professionals living far from home for reasons of work) clearly display the importance of culture in the business environment.

Other kinds of cultural impact go in a different direction. Sometimes, it is not the flows of populations bringing with them their nation’s products to their new home or its values to the job market; it is the country itself that manufactures iconic products or exports cultural products of worldwide appeal, thereby branding itself at a global level. If the United States is the most obvious example of this, there are recent ones to have attracted

the world’s attention. South Korea and the phenomenon named *hallyu* offer a textbook case in this sense.

While the country is certainly a powerhouse in terms of GDP and export performance (especially when its geographic and demographic composition are taken into account), the size of its expat community and long-term diaspora is smaller in comparison to other, more established overseas communities. A quick look at the number of Koreans overseas—7.4 million in 2017, according to the South Korean Ministry of Foreign Affairs—will show that they are considerably less numerous than, say, the Chinese (about 9 million in Thailand alone).

Yet one cannot on this count underestimate the growing appeal of Korean culture on groups of youth across the world, in other Asian countries but also as far away as Europe and the Americas. There is a growing literature, both in academia and in the press, that analyzes South Korea’s so-called “soft power,” a concept