WEEKLY OVERVIEW

WEEK 1: INTRODUCTION OF GLOBAL BUSINESS

GLOBALISATION

Globalisation is when there is a shift to a more integrated and interdependent world economy. It has impacts on governments, people and the economy.

Globalisation has several facets, including the globalisation of markets and globalisation of production.

The drivers of globalisation are the decline in trade barriers to the free flow of goods and services, and the technological change in communication, information processing and transportation technologies.

TWO MAIN COMPONENTS OF GLOBALISATION

Globalisation of Markets

- The globalisation of markets is the decline in trade barriers to sell in other countries besides home making the separate national markets one huge marketplace.
- Tastes and preferences of consumers in different nations are beginning to converge on some global form, creating a global market.
- By offering the same basically product worldwide, they help to create a global market.
- Examples are Coca Cola, Sony PlayStation and McDonald's.
- Technological innovations have also facilitated the globalisation of markets with low cost global communication networks such as the World Wide Web allowing firms to create electronic global marketplaces.
- Low-cost transportation has made it more economical to ship products around the world, thereby creating global markets. E.g. Due to lower shippings costs by air, roses grown in Ecuador can be cut and sold in New York two days later while they are still fresh. This has given Ecuador industry that didn't exist 20 years ago the chance to supply a global market for roses.

Globalisation of Production

- Many firms source goods and services from different locations around the globe to take advantage of national differences in cost and the quality factors of production. This allows firms to compete more effectively and efficiently against their rivals.
- As transportation costs associated with globalisation of production declined, dispersal of production to geographically separate locations became more economical. Due to technological innovations, the real costs of information processing and communication have fallen dramatically in the past two decades. This allows firms to create and manage a globally dispersed production system, further facilitating the globalisation of production.

Does globalisation of goods and production effect jobs and income?

- Critics argue that falling trade barriers allow firms to move manufacturing activities to countries where wage rates are much lower.
- When a country embraces free trade, there is always some dislocation – lost textile jobs at Harwood Industries, or lost call centre jobs at Dell – but the whole economy is better off as a result.
- According to this view, it makes little sense for the United States to produce textiles at home when they can be produced at a lower cost in Honduras or China. Importing textiles from China leads to lower prices for clothes in the U.S., which enables consumers to spend more of their money on other items. At the same time, increased income generated in China from textile exports increases income levels in that country, which helps the Chinese to purchase more products produced in the U.S., such as pharmaceuticals from Amgen, Boeing jets, Intel products and Microsoft software.

- The same argument can be made for support outsourcing of services to low-wage countries. By outsourcing its customer service call centres to India, Dell can reduce its cost-structure, and thereby its prices for U.S. consumers benefit from this development. As prices for PCs fall, Americans can spend more money on other goods and services. This also increases the income levels in India allows Indians to purchase more U.S. goods and services, which helps create jobs in the U.S.

Does globalisation affect the environment?

- Critics also argue that free trade encourages firms from advanced nations to move manufacturing facilities to less developed countries that lack adequate regulations to protect labour and the environment from abuse by the unscrupulous.
- They argue that tougher environmental regulations and stricter labour standards go hand in hand with economic progress. In general, as countries get richer, they enact tougher environmental and labour regulations.
- Because free trade enables developing countries to increase their economic growth rates and become richer, this should lead to tougher environmental and labour laws. In this view, critics of free trade have got it backwards.
- By creating wealth and incentives for enterprises to produce technological innovations, the free market system and free trade could make it easier for the world to cope with pollution and population growth. While pollution levels are rising in the world's poorer countries, they have been falling in developed countries.

QUESTIONS

1. How have changes in technology contributed to the globalization of markets and production? Would the globalization of production and markets have been possible without these technological changes?
    a. Technological changes have significantly contributed to the globalization of products and markets and accelerated the creation of a global village. Recent technological developments have brought the world closer together more quickly than at any time in the past.
    b. Developments in information processing and communication have decreased the costs of managing a global production system, and improvements in transportation have made the shipment of goods timelier and less costly than at any time in the past. International firms can locate facilities wherever it is most advantageous, coordinate the activities between facilities, and ship products to customers worldwide more cost effectively than at any time in the past.

2. "Ultimately, the study of international business is no different from the study of domestic business. Thus, there is no point in having a separate course on international business." Evaluate that statement.
    a. The truth is that if an international business attempts to utilize the same business techniques that were effectively domestically on the international scene, it is quite likely to fail. The annals of corporate business are lined with examples of that concept, from small companies struggling to make an impact to large multinationals like Procter and Gamble, who failed in Japan when they first introduced disposable diapers to that market. International business is different in many of the ways mentioned here: 1) countries differ, 2) the range of problems a manager faces is greater and more complex, 3 the limits imposed by governmental intervention and the global trading system complicate international business, and 4) international transactions require converting funds and being susceptible to exchange rate changes. A separate course on international business can provide an understanding of these difficulties, and how conducting international business requires consideration of issues not typically covered in other courses.

WEEK 2: GOING INTERNATIONAL I

Internationalism is when there is increased involvement in international operations such as inward and outward expansion.

- For example, an Australian company has outward expansion in the foreign market to export, license, FDI. The foreign company which may be an export will do inward expansion to Australia which will be an importer of stocks and supplies.

EXTERNAL VS. INTERNAL APPROACHES

- External approaches are when the firm does business without investing in owned assets and own human resources in target market.
  - E.g. domestically produced goods are exported to foreign markets through local agents or retailers.
- Internal approaches are when the business invests directly in assets and resources in the target market.
  - E.g. setting up a factory in a foreign market to produce goods.

ENTRY MODES

EXPORTING

Selling products produced in one country to the residents of another country.

- Indirect exporting is through an agent in the home country to the foreign country
- Direct exporting is selling to foreign market through own organisation.
- Intra-corporate transfer is when sales are made by business to an affiliated firm located in the host country.

Advantages:

- You can realise where your market and experience curve economies.

Disadvantages:

- There are high transport costs associated unless bulk. When transportation costs are added to production costs, it becomes unprofitable to ship some products over a large distance.
- There are trade barriers by countries and local companies are a challenge to beat.
- Motivation of local agents is a challenge.

LICENSING/FRANCHISING

Licensing is when you the licensor allow the licensee to use your technology or design for manufacturing.

- E.g. Xerox licensed its xerographic knowhow to Fuji

Franchising is when the franchisor allows the franchisee to adopt its entire business process or format.

- E.g. McDonald's franchises operating globally.

Advantages:

- Low financial risk and there is relatively low development costs.
- Quick cash flow and quick market access and the governments are less concerned.

Disadvantages:

- You can't control what the other firm is doing over quality.
- Could potentially lose know-how to potential competitor, your sharing the profit pie.
- Growth may be slower depending on franchisee's and licensee's intentions.
- Makes global coordination costlier than ownership.

Turnkey Project

- When a contractor sets up an operating plant for a foreign client and hands over the 'key' when the plant is fully operational.
- In a turnkey project , the contractor agrees to handle every detail of the project for a foreign client, including
- the training of operating personnel.
    - Common in industries such as chemical, petroleum refining, pharmaceutical where production technologies are expensive and complex.
- Advantages:
    - Know-how required to assemble and run a technological complex process, such as refining petrol and steel, is a valuable asset.
    - Way of earning great economic return from that asset.
    - Useful were FDI is limited by host-government regulations. For example, the governments of many oil-rich countries have set out to build their own petroleum refining industries, so they restrict FDI in their oil and refining sectors. But because many of these countries lack petroleum-refining technology, they gain it by entering into turnkey projects with foreign firms that have the technology.
    - Less risky than conventional FDI

- Disadvantages:
    - The firm that enters into a turnkey deal will have no long-term interest in the foreign country. This can be a disadvantage if that country subsequently proves to be a major market for the output of the process that has been exported.
    - The firm that enters into a turnkey project with a foreign enterprise may inadvertently create a competitor. If the firm's process technology is a source of competitive advantage, then selling this technology through a turnkey project is also selling competitive advantage to potential or actual competitors.

Strategic Alliance

- An agreement between potential or actual competitors
    - E.g. short-term collaboration on research, new product development, etc.
- Advantages are there is access to partners knowledge, sharing of risks and the foreign parent can deploy more resources across the national markets at once.
- Disadvantage: May be more difficult than international joint ventures.

Foreign Direct Investment (FDI)

Joint Ventures

- The establishment of a firm that is jointly owned by two or more independent firms. One or more firms are non-resident in the host market.
- Advantages: Quicker market access, government regulatory requirements, risk/cost sharing, access to partners knowledge and resources.
- Disadvantages: Limited or restricted control, disagreements and relationship difficulties, loss of flexibility and confidentiality.

Wholly Owned Subsidiary

- Firms establishes a subsidiary in a foreign market and owns 100% of the shares.
- This is business there is access to cheap labour, raw materials for manufacturing: facilitate purchase of inputs. Reducing transportation costs as the proximity to customers closes. A way to overcome export barriers.
- Methods include: acquisition of an existing firm in an foreign market or setting up a greenfield venture.
- Advantages: There is more control levels, greater access to customers and inputs, more favourably viewed by host countries' nationals and governments.
- Disadvantages: Most expensive method, required resource commitment, exposure to country risk factors, suitable for well-established business.

Greenfield Venture vs. Acquisition

A firm can establish a wholly owned subsidiary in a country by building a subsidiary from the ground up, the so-called greenfield strategy, or by acquiring an enterprise in the target market.

Greenfield

- The advantage of a greenfield venture in a foreign country is that it gives the firm a much greater ability to build the kind of subsidiary company that it wants.
- For example, it is much easier to build an organization culture from scratch than it is to change the culture of an acquired unit.

Acquisition

- The advantages of acquisitions are quick to execute, may enable a firm to pre-empt its global competitors, and involve buying a known revenue and profit stream.
- The disadvantages of acquisitions may fail when the acquiring firm overpays for the target, when the culture of the acquiring and acquired firms clash, when there is a high level of management attrition after the acquisition, and when there is a failure to integrate the operations of the acquiring and acquired firm.

New Trade Theory

The two key issues highlighted in this theory

1. Trade can increase the variety of goods available to consumers and decrease the average cost of these goods through economies of scale.
    a. Unit cost reductions associate with a large scale of outputs advantages.
    b. A country without trade would mean small market = small demand = lower production volume at higher costs – less variety and more expensive products for consumers.
    c. Trade means market expansion and economies of scale and specialisation meaning cheap products.

2. For industries where the global market may only support a limited number of firms, those with first mover advantage will create barriers to entry for other firms.
    a. The economic and strategic advantages that accrue to many entrants into an industry.
    b. Airbus was first to realise scale economies in the super – jumbo category and has dominated the global market for the export of very large aircraft.

<u>Question</u>

1. Licensing proprietary technology to foreign competitors is the best way to give up a firm's competitive advantage. Discuss.

The statement is basically correct - licensing proprietary technology to foreign competitors does significantly increase the risk of losing the technology. Therefore, licensing should generally be avoided in these situations. Yet licensing still may be a good choice in some instances.

- When a licensing arrangement can be structured in such a way as to reduce the risks of a firm's technological know-how being expropriated by licensees, then licensing may be appropriate.
- A further example is when a firm perceives its technological advantage as being only transitory, and it considers rapid imitation of its core technology by competitors to be likely. In such a case, the firm might want to license its technology as rapidly as possible to foreign firms in order to gain global acceptance for its technology before imitation occurs.

WEEK 3 – SOCIO-ECONOMIC ENVIRONMENT

ECONOMIC ENDOWMENTS

Include natural and created features. Influential to a firm's preliminary assessment of a potential target country.

1) *SIZE OF ECONOMY*

- Level of national income and production
- Population

2) *GEOGRAPHY*

- Natural resources and features that may affect level and patterns of market demand and production (e.g. climate, topography, distance, etc.)
- Physical location may be a help or hindrance

3) *PEOPLE*

- Population size, growth and distribution (e.g. age, gender, location) may indicate potential market size.
- Income, education and occupational distribution.
- Quality of human capital (e.g. educated and skill labour force) may make a country attractive for FDI.

4) *INFRASTRUCTURE AND INSTITUTIONS*

- Created infrastructure assets (e.g. transport, energy and communications systems) that facilitate businesses.
- Institutional components (e.g. financial laws, accounting standards, etc) that promote the functioning and effectiveness of the business sector.

5) *PRODUCTIVITY AND COMPETITIVENESS*

- Competitiveness: Quality of a nation or a business that allows it to maintain an economic advantage in the marketplace.
    - More competitive = More challenging
- Productivity: Ratio of output produced to the factors of production (labour and capital inputs) used.

ECONOMIC SYSTEMS

An economic system is the set of arrangements by which the society determines what should be produced, how it will be produced and how should the resulting personal income and claims to goods and services be distributed (and redistributed among households).

Market Economy

- This type of economy emphasises private ownership and free market activity.
- Firms use resources and produce products, while individuals own resources and consume products.
- Market is driven by supply and demand. Market economy is used by all major industrialised countries.
- Objectives are for competition, innovation and efficiency (capitalism).
- Problems: creates winners and losers; potential for socials and economic inequality; rising costs of living due to profit – seeking behaviour and user pay systems.

Command (Centrally Planned) Economy:

- This type of economy is one in which the allocative and distributive functions of the market are assumed by government. The government determines centrally what is to be produced, the levels of production, the employment of resources and the distribution of outputs.
- Characteristics: central planning (North Korea), state ownership where governments owns most, if not all, businesses. Objectives are to have social equality and fairness.
- Problems: Economic stagnation due to lack of competition. Same as one another, same wages, etc. Government generally not good at resources allocation (demand not met by supply).

Mixed Economy:

- This includes some elements of each:
    - Certain sectors of the economy are left to private ownership and free market mechanisms while other sectors have significant state ownership and government planning (e.g. state-owned banks, public utilities, etc.)
    - There must be no restrictions on either supply or demand.
    - No monopolistic sellers or buyers.
- Examples: Australia, NZ, GB, France, Sweden were mixed economies with significant state ownership but extensive privatisation since the 1980s has reduced the extent of state ownership of businesses in all these nations.

Levels of Economic Development

Less – Developed Countries

- Inadequate infrastructure
- Low literacy and Limited Technology
- Rural Based

Middle – Income Countries

- Developing infrastructure
- Improving Education
- Improving technology
- Diversified economy

Developed Countries

- Developed infrastructure
- High literacy
- Modern technology
- Industrialised, service economy

Economy Stability

1. Macroeconomic stability is when the economy grows without persistent and major fluctuations in the level of economy activity, inflation rates, unemployment and balance of payments imbalances.
2. Macroeconomic instability is when there is recession, high inflation rates, rising interest rates and volatile foreign exchange rates, among other indicators.

Governments have four stabilisation goals which are low inflation, low level of unemployment, positive economy growth, balance of international payments and receipts.

Analysing Economies

Size of economy (GNI)

- GNI is the gross national income.
- Total value of nation's income earned by nation's residents (no matter where the income is earned, in domestic or foreign market)

Income levels (GNI per capita)

- GNI per capita is the GNI divided by total population.
- High GNI per capita and GNI are more desirable than low GNI and GNI per capita in terms of market potential.

Balance of payments is a summary of payments to and from the country.

- Deficit (-): Payments to foreigners exceed receipts from foreigners.
- Surplus (+): receipts from foreigners exceed payments from foreigners.

GDP (Gross Domestic Product)

- Value of production and income earned with country boundaries no matter who owns the factors of production.
    - E.g. when Ford manufactures in U.S., they are counted in U.S GDP not Australia.
- When a country's GDP is high it means that the country is increasing the amount of production that is taking place in the economy and the citizens have a higher income and hence are spending more.

GDP per capita is the GDP divided by the total population.

Real GDP: economic output adjusted for the effects of inflation.

Purchasing Power Parity (PPP)

- Number of units of country's currency required to buy the same amount of goods and services in the domestic market.
- PPP considers cost of living differences between countries (allows a more direct comparison of living standards between countries.

Consumer Price Index (CPI)

- Measures inflation (increase in general price level over time)
- High inflation means depreciation of currency value.

Human Development Index (HDI)

- Composite index of health, education and income (GNI per capita)
- Countries ranked into 4 tiers of human development (low income $1,005 or less; lower middle income $1,006-$3,975; upper middle income $3,976-$12,275; and high income $12,276 or more)

Gini Index (or Gini Coefficient): A simple measure to gauge income inequality

- Value is between 0 to 1 (or in percentage 0 to 100) - the closer the value is to 1 (or 100), the greater the inequality, the closer to 0 means greater equality in income distribution
- E.g. Norway = 0.27 (27), South Africa = 0.63 (63)