DKR26 - INTERNATIONAL BUSINESS MANAGEMENT

Unit – 1 : History of International business – Reasons for foreign entry – Patterns of International business – Types of FDI – Multinational Corporations – Market imperfection approach – approaches on firm bases and location specific advantages – Environmental factors – Economic, Financial, Political, legal, cultural, technological.

Unit – II : International business strategy – Internationalisation – Management Philosophies – Porter's Model – Prehalad and Doz's model – International Marketing Strategy – Introduction to product, price (INCOTERMS), Distribution, Promotion in international context.

Unit – III : Technology and MNC – Technological interdependence – strategy and innovation – technology accumulation – Home or Overseas R&D – Organsiational issues – Technological performance – Introduction to international finance – Exchange rate – changes, forecasting, risk – International cash management, taxation.

Unit - IV : International operation Strategy – Procurement – Subcontracting – Plant location decisions – plant design and interplant relationship – Staffing policies – Globalisation and HRM – International labour strategy – New directions in organizational structures – Performance evaluation.

Unit - V : International acquisitions – cultural, legal, political dimensions – conventional perspective of acquisition process – alternative perspective – acquisitions and business strategy – successful integration – Problems in acquisition integration – Approaches to integration – Future of multinational – international Co – operation – Determinants of competition – International managers for millennium.

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INTERNATIONALIZATION OF BUSINESS:

Meaning of International Business:

International business is a term used to collectively describe all commercial transactions (private and governmental, sales, investments, logistics, and transportation) that take place between two or more nations. Usually private companies undertake such transactions for profit; organizations undertake them for profit for political reasons. A multinational enterprise (MNE) is a company that has a worldwide approach to markets and production or one with operations in more than a country.

An MNE is often called multinational corporation (MNC) or transnational company (TCN). Well known MNCs include fast food companies such as McDonald's, and Yum Brands, vehicle manufacturers such as General Motors, Ford Motor Company and Toyota, consumer electronics companies like Samsung, LG and Sony, and energy companies such as Exxon Mobil, Shell and BP. Most of the largest corporations operate in multiple national markets.

The conduct of international operations depends on companies' objectives and the means with which they carry them out. The operations affect and are affected by the physical and societal factors and the competitive environment.

Internationalization of Business has benefited TCS, Asian paints, Wipro, Infosys. It may be understood as those business transactions that involve the crossing of national boundaries'. They include;

1. Product presence in different markets of the world.
2. Production bases across the globe.
3. Human resource to contain high diversity
4. Investment in international services like banking, advertising, tourism, retailing, and construction
5. Transactions involving intellectual properties such as copyrights, patents, trademarks and process technology

Why study international business?

1. Increasingly, companies are sourcing their human resource requirement globally, Sony corporation.
2. Most of the products we consume everyday are supplied to us by global businesses. We are sure of quality if the products bear such names as Nike, Toyota, Colgate, Gap T-shirt, and the like. To know these brands is to understand international business
3. Managing an international business is major complex than running a domestic business. Global business involves production of goods in facilities located in different countries with resources, human and physical sourced from all parts of the globe and marketing goods and services to users across the globe.
4. The major impact of international business in this area has been impet us on governments to open up their borders to international trade and investment, standardize their systems and procedures, and adopt internationally acceptable values and attitudes.
5. International business executives play a powerful role in determining the relative competitiveness of various countries in the global arena.

Advantages of international business:

- **Product Flexibility**

  If you have products that don't sell well in your local or regional market, you may find greater demand abroad. You don't have to dump unsold inventory at deep discounts. You can search for new markets where your products can sell for even higher prices than they did in your local market. Infact, you may find new products to sell abroad that you don't offer where you are based. You can offer amuch wider range of products whenyou market globally.

- **Less Competition**

  Company may have come to view competition as a local phenomenon. You can find international markets that have less competition and move quickly to capture market share. This can be particularly advantageous when you have access to high-quality versions of products that are superior to versions in other countries. Though your local competition may have access to the same quality as you have,

you will have little competition if you find an international market that has been buying an inferior product.

- **Protection from National Trends and Events**

  When you market to several countries, you are not as vulnerable to events in any one country. For example, if you sell soft drinks with high sugar content, you could discover that your home country frowns upon drinks that offer extracalories. You may be able to sell the same product in another country that has a much different attitude toward these drinks. In addition, a natural disaster in any one market can disrupt business, but you can compensate by focusing your sales efforts in another part of the world.

- **Learning New Methods**

  When you do business in another country, you learn new ways of doing things. You can apply this new knowledge to other markets. For example, according to the Cite Sales website, Unilever discovered a market for laundry detergent that would function in Europe's high – mineral – content or "hard" water. This product can now be marketed to parts of the U.S. that have similar water problems.

The economic benefits that greater openness to international trade bring are:

- Faster growth: economies that have in the past been open to foreign direct investments have developed at a much quicker pace than those economies closed to such investment e.g. communist Russia
- Cheaper imports: this is down to the simple fact that if we reduce the barriers imposed on imports (e.g. tariffs, quota, etc) then the imports will fall in price
- New technologies: by having an open economy we can bring in new technology as it happens rather than trying to develop it internally
- Spur of foreign competition:

  Foreign competition will encourage domestic producers to increase efficiency. Carbaugh (1998) states that global competitiveness is a bit like golf, you get better by playing against people who are better than you.
- Increase consumer income: multination will bring up average wage levels because if the multinationals were not there the domestic companies would pay less

- Increased investment opportunities: with globalization of companies can move capital to whatever country offers them ost attractive investment opportunity. This prevents capital being trapped in domestic economies earning poor returns.

REASONS FOR FOREIGN ENTRY

International markets provide various key advantages to the average corporation. By moving internationally, corporations have the ability to increase demand for their products, decrease the economic volatility from their home market, and develop new customers. In most cases foreign markets also allow companies to take advantage or larger margins and of less competition. The five Top reasons to enter International Markets are Population, High Demand, Growth Rate, the Informal Economy, and Small Business Hegemony.

1) Population: Emerging Markets (EM) represents the vast majority of the global economy that is composed of about 5.88 billion people who consume over $10 trillion US dollars a year. This would make the EM’s the second largest economy in the world, after the United States. What is even more important is that the emerging economies plan to invest an additional $29 trillion US dollars in the coming twenty years in infrastructure, and sector specific projects within business-to-business (b2b) and business-to-consumer (b2c) industries.

2) High Demand: Demand remains high for foreign products even when they are considered a luxury product within the emerging market. The main reasons are the Foreign Brand attractiveness and representation of financial and consumption power, the potential for inferior products within the domestic market, and/or product uniqueness. However, before entering the market an international feasibility study must be conducted to ensure a correct market entry strategy for the entering company.

3) Growth Rate: The Inflation adjusted GDP for Emerging Markets between 1998 to 2012 was 5.7% versus only 2.5% within the developed world. The Wealthy are increasing within Emerging Markets and Foreign Direct Investment (FDI) is still showing healthy signs of increasing. The number of Chinese households whose net worth was 1 million US dollars or more leaped by an astonishing 60% in 2010 to a total of 1.1 million Chinese households.

4) Informal Economy: the informal economy plays a key role within emerging markets. By some accounts over 60% of a countries economy lives in the informal economy, without bank accounts, cable, electricity or housing. Good examples of the informal economy are the Favelas of Brazil, or shantytowns of Lagos, Nigeria. They all have their own unique market conditions and informal economies. Companies can excel in this market space like the UAC

foods, whose Gala Sausage Roles are not sold in stores but rather distributed by an informal network of street vendors targeting commuters and pedestrians.

5) Small Business hegemony: The vast majority of the Emerging Market's population works within micro, small or medium sized businesses. Some 69% of the working population are employed by such business. Clients who want to enter new markets have the ability of joining forces with the local community via a Joint Ventures (JV) or an Alliance to increase their footprint and have domestic players develop the product or brand for you.

PATTERNS OF INTERNATIONAL BUSINESS

A number of patterns and trends are likely to be relevant to different types of international business activity.

International communication

- International travel
- International growth in leisure pursuits
- International growth in ageing populations
- International growth in currency transactions
- International growth in countertrade

Each of these patterns/trends are discussed below

International communication: There have been dramatic increases in various modes of international communication. For example, the time spent on international telephone calls has risen from 33 billion minutes in 1990 to over 120 billion minutes by the end of 2008. Internet usage is also rising exponentially, with the 2008 Human Development Report (UNDP, 2008) noting that the number of Internet hosts per 1000 people worldwide had risen from a mere 1.7 in 1990 to 136 in 2005/2006 with cellular mobile phone subscribers per 1000 people worldwide also rising from only 2 in 1990 to 341 in 2005/2006 (UNDP, 2008). Various studies have found a strong and positive correlation between the extent of telephone network and Internet usage.

International Travel: The number of international tourists has more than trebled from 260 million travelers a year in 1980 to over 800 million travelers a year in 2008. The growth of tourism is closely correlated with the growth of worldwide GDP and is an important source of income and employment for many developed and developing countries alike.

International growth in leisure pursuits: In 1980 some 80% of the time left over after necessities such as sleeping and eating were attended to, was used for earning a living. Today that percentage has fallen to below 40% over the average lifetime of an individual in the advanced industrialised economies and is projected to continue falling to around 25% over the next decade. This dramatic increase in leisure time availability in the higher-income advanced industrialised economies clearly has major implications for consumption patterns and therefore for the deployment of productive resources.

International growth in ageing populations: Between 1950 and 2008 the median age of the world's population rose by only 3 years, from 23.6 years in 1950 to 26.5 years in 2008. However, over the next 40 years, the UN projects the median age will rise dramatically to 37 years by 2050, with 17 advanced industrialised economies having a median age 50 years or above. This has major implications for international business in terms of productive locations (e.g. adequate supply of labour of working age) as well as the range of products likely to be in global demand.

International growth in currency transactions: The daily turnover in foreign exchange markets has dramatically increased from US$ 15 billion in the mid 1970s to over US$2400 billion in 2008. This has contributed to greater exchange volatility, on occasions putting server pressure on national economies and currencies

International growth in countertrade: When conventional means of payment for international means of payment for international transactions are difficult, costly or not available, then a range of barter (swap)-type transactions may be used instead. Whereas such 'countertrade' only accounted for 2% of the world trade in 1975, by 2008 over 20% of the world trade involved some elements of barter, with the former Soviet Union and the Eastern European economies particularly active in using countertrade.

TYPES OF FDI

Foreign direct investment (FDI) is an important factor in acquiring investments and grows the local market with foreign finances when local investment is unavailable. There are various formats of FDI and companies should do a good research before actually investing in a foreign country.

It has been proved that FDI can be a win-win situation for both the parties involved. The investor can gain cheaper access to products/services and the host country can get valuable investment unattainable locally.

There are various vehicles through which FDI can be acquired and there are some important questions the firms must answer before actually implementing a FDI strategy.

FDI – Definition

FDI, in its classic definition, is termed as a company of one nation putting up a physical investment into building a facility (factory) in another country. The direct investment made to create the buildings, machinery, and equipment is not in sync with making a portfolio investment, an indirect investment.

In recent years, due to fast growth and change in global investment patterns, the definition has been expanded to include all the acquisition activities outside the investing firm's home country. FDI, therefore, may take many forms, such as direct acquisition of a foreign firm, constructing a facility, or investing in a joint venture or making a strategic alliance with one of the local firms with an input of technology, licensing of intellectual property.

FDI and its Types

Strategically, FDI comes in three types −

- **Horizontal** − In case of horizontal FDI, the company does all the same activities abroad as at home. For example, Toyota assembles motor cars in Japan and the UK.
- **Vertical** − In vertical assignments, different types of activities are carried out abroad. In case of forward vertical FDI, the FDI brings the company nearer to a market (for example, Toyota buying a car distributorship in America). In case of backward Vertical FDI, the international integration goes back towards raw materials (for example, Toyota getting majority stake in a tyre manufacturer or a rubber plantation).
- **Conglomerate** − In this type of investment, the investment is made to acquire an unrelated business abroad. It is the most surprising form of FDI, as it requires overcoming two barriers simultaneously – one, entering a foreign country and two, working in a new industry.

FDI can take the form of **greenfield entry** or **takeover**.

- **Greenfield** entry refers to activities or assembling all the elements right from scratch as Honda did in the UK.

- **Foreign takeover** means acquiring an existing foreign company – as Tata's acquisition of Jaguar Land Rover. Foreign takeover is often called **mergers and acquisitions** (M&A) but internationally, mergers are absolutely small, which accounts for less than 1% of all foreign acquisitions.

This choice of entry in a market and its mode interacts with the ownership strategy. The choice of wholly owned subsidiaries against joint ventures gives a 2x2 matrix of choices – the options of which are −

- Greenfield wholly owned ventures,
- Greenfield joint ventures,
- Wholly owned takeovers, and
- Joint foreign acquisitions.

These choices offer foreign investors options to match their own interests, capabilities, and foreign conditions.

MULTINATIONAL CORPORATIONS:

The evolution of multinational corporations has its root in the origin of trade in and between various cultural communities across regions. Marked by the struggle of transacting across regions, trading has always been affected by the unequal and varied distribution of resources across geographies. It is this unequal distribution that has led traders to travel long distances and undergo unusual risks for the hope of gain.

The past few decades have witnessed the way global boundaries have shrunk, and communications and technology has bridged the gap. Advancements in technology have resulted in the development of new products, processes and forms of business that have changed the dynamics of economic environment the world over.

Economies started to change to accommodate these progressive developments. Organizations in order to capitalize on the growing opportunities globally started to change and expand. This gave rise to multinational corporations.

What are MNCs?

Multinational corporations are profit seeking enterprises having international power, capital, manpower, and resource-seeking practices. We can say that an organization that performs its business in two or more countries is a multinational company. These companies operate worldwide through their own branches and subsidiaries or through agents who represent them.

All the business activities are managed and controlled by the central head office of the organization, which is usually situated in the home country of the company.

The equity capital of the subsidiaries or branches in various countries is contributed by both the host company and the parent company. However, management and control of the branches is governed and controlled by the parent company.

As these organizations coordinate production and distribution on a global scale, they become enormous in size and wield enormous power, both economically and politically.

Multinational firms arise because

- Capital as a resource is mobile and can be used across geographies
- The growing global marketplace has created enormous consumerism
- The mutual cooperation among friendly nations and development of new technology has facilitated mass production.
- Inexpensive labour and skills are available in many countries
- Raw materials availability is spread across geographically.

Managers working in multinationals are required to understand and operate in multi-cultural international environment. As a result, they are required to constantly monitor the political, legal, socio-cultural, economic, and technological environments across international markets.

Types of Multinational Corporations

Some of the common forms of Multinational Companies are −

Franchise Operations

Under this form, a multinational corporation endows firms in foreign countries the legal right to use its business model and brand per the terms and conditions of franchise agreement, which can be reviewed and renewed periodically. The firms who get the right or license pay royalty or license fee to multinational corporations.

Branches and Subsidiaries

In this kind of a system, the multinational company opens its own braches in different countries, which operate under the direct control and supervision of the company’s head office. Sometimes, a multinational company may establish subsidiaries in foreign countries. These subsidiaries may be fully owned by the multinational (parent company) or partly owned, where the host countries own share capital. The subsidiaries follow the guidelines of the parent company.

Joint Venture

A multinational company establishes its company in a foreign country in partnership with the local firms or companies in the host company. The ownership and control of the business is shared by multinational and foreign company, where the governing policies are that of the multinational company and the day-to-day management is left to the local company.

MARKET IMPERFECTION APPROACH:

Market imperfections theory is a trade theory that arises from international markets where perfect competition doesn't exist. In other words, at least one of the assumptions for perfect competition is violated and out of this is comes what we call an imperfect market. We know that a perfect market isn't really attainable.

Market Imperfection theory states that there is no economy in the world which has a perfect market. Economists earlier have used the perfect market competition theory to explain different economic concepts. A perfect market has features which cannot exist in the real world such as :

1.) Each product is homogeneous.

2.) The taste and trend of the people is same or constant.

3.) Buyers and sellers are unlimited.

Basically, market imperfections theory states that the perfect market cannot exist and also demand and supply can never be equal.

Approaches on firm based and location specific advantages

With regard to horizontal FDI, it was argued that the market imperfections and location-specific advantages approaches might have the greatest explanatory power and therefore be most useful for business practice. This is not to belittle the explanations for horizontal FDI put forward by Vernon and Knickerbocker, since these theories also have value in explaining the pattern of FDI in the world economy. Still, both theories are weakened by their failure to explicitly consider the factors that drive the choice among exporting, licensing, and FDI. Finally, with regard to vertical FDI, it was argued that the strategic behavior and market imperfections approaches both have a certain amount of explanatory power.

1. Foreign direct investment occurs when a firm invests directly in facilities to produce a product in a foreign country. It also occurs when a firm buys an existing enterprise in a foreign country.
2. Horizontal FDI is FDI in the same industry abroad as a firm operates at home. Vertical FDI is FDI in an industry abroad that provides inputs into a firm's domestic operations.

3. Any theory seeking to explain FDI must explain why firms go to the trouble of acquiring or establishing operations abroad when the alternatives of exporting and licensing are available.
4. Several factors characterized FDI trends over the past 20 years; (1) there has been a rapid increase in the total volume of FDI undertaken; (2) there has been some decline in the *relative* importance of the United States as a source for FDI, while several other countries, most notably Japan, have increased their share of total FDI outflows; (3) an increasing share of FDI seems to be directed at the developing nations of Asia and Eastern Europe, while the United States has become a major recipient of FDI; and (4) there has been a notable increase in the amount of FDI undertaken by firms based in developing nations.
5. High transportation costs and/or tariffs imposed on imports help explain why many firms prefer horizontal FDI or licensing over exporting.
6. Impediments to the sale of know-how explain why firms prefer horizontal FDI to licensing. These impediments arise when: (*a*) a firm has valuable know-how that cannot be adequately protected by a licensing contract, (*b*) a firm needs tight control over a foreign entity to maximize its market share and earnings in that country, and (*c*) a firm's skills and know-how are not amenable to licensing.
7. Knickerbocker's theory suggests that much FDI is explained by imitative strategic behavior by rival firms in an oligopolistic industry. However, this theory does not address the issue of whether FDI is more efficient than exporting or licensing for expanding abroad.
8. Vernon's product life-cycle theory suggests that firms undertake FDI at particular stages in the life cycle of products they have pioneered. However, Vernon's theory does not address the issue of whether FDI is more efficient than exporting or licensing for expanding abroad.
9. Dunning has argued that location-specific advantages are of considerable importance in explaining the nature and direction of FDI. According to Dunning, firms undertake FDI to exploit resource endowments or assets that are location-specific.
10. Backward vertical FDI may be explained as an attempt to create barriers to entry by gaining control over the source of material inputs into the downstream stage of a production process. Forward vertical FDI may be seen as an attempt to circumvent entry barriers and gain access to a national market.

11. The market imperfections approach suggests that vertical FDI is a way of reducing a firm's exposure to the risks that arise from investments in specialized assets.
12. From a business perspective, the most useful theory is probably the market imperfections approach, because it identifies how the relative profit rates associated with horizontal FDI, exporting, and licensing vary with circumstances.

Vernon's Product Life Cycle Theory

Vernon argued that firms undertake FDI at particular stages in the lifecycle of a product they have pioneered. Vernon suggests that a product goes through three stages: it starts of as a new product, and then becomes a maturing product and finally a standardized product. Vernon's theory was based on the observation that for most of the twentieth century a large proportion of the world's new products had been developed by the U.S. firms and sold first in the U.S. market for example televisions, photocopiers, personal computers and so on. He argued that most new products were initially produced in the U.S.

An illustration is the photocopier which was first developed in the 1960's by **Xerox** in the United States and sold in the U.S. only. Initially, Xerox exported photocopiers mainly to Japan and advanced countries of Western Europe. As demand grew in those countries, Xerox entered into joint ventures and set up production in Japan (Fuji-Xerox) and Britain (Rank-Xerox). Once Xerox's patents on the photocopier expired, other foreign competitors entered the market such as Canon in Japan. As a result of this, U.S. exports declined and U.S. users began buying from mostly Japan due to lower costs.

Knickerbocker's theory of horizontal FDI

Knickerbocker's theory of horizontal FDI also known as Knickerbocker's theory of oligopolistic competition is based on the idea that FDI flows are a reflection of strategic rivalry between firms in the global market place. The action of one firm will lead to competitors immediately imitating the action. Knickerbocker insisted that this similar kind of imitative behaviour characterizes FDI For example, such imitative behaviours could be in the form of a price decrease by one firm with a view to improve its market position, others will decrease their prices accordingly in order not to allow the firm develop a competitive advantage at their expense. Example is with regard to FDI undertaken by Japanese firms in the 1980's when Honda invested in the U.S. and Europe, Toyota and Nissan responded by undertaking their own FDI into the U.S. and Europe as well in order not to be left behind.

ENVIRONMENTAL FACTORS WHICH AFFECT BUSINESS

In business analysis, the word 'environmental' can sometimes be used refer to all external factors that affect a business (just like in environmental analysis), from Political to Legal, and everything in between.A business does not operate in a vacuum. It has to act and react to what happens in the environment. These factors that happen outside the business are known as external environmental factors. These will affect the main internal functions of the business and possibly the objectives of the business and its strategies. From a business point of view, the major external environmental factor is likely to be political instability. Political instability may arise through frequent changes in the ruling political party or elite, and/or through frequent changes of policy by a stable ruling political party. If the political situation is one in which the environment surrounding the company is predictable, companies can develop and implement international business plans with some confidence. If the government changes direction frequently, medium and long-term planning becomes very difficult and companies will feel forced to adopt short-term, highly pragmatic approaches. Multinational companies should understand that the political background is different across the regions of the world. Many former centrally planned economies, for example, are still heavily protected by the government. In such a climate, it is more likely that proposals for a joint venture will be accepted. Each country has their own legal system and when a company internationalizes then it must keep within these legal systems. When it comes to developing marketing mix elements in foreign markets, the company's approach may have to be adapted. The legal environment must be assessed to determine whether it would affect the launch of a product into a new country. In many countries, government and regulations have a direct influence on product design. Law often imposes minimum or special product standards, which may necessitate the shape, kind, components or even the brand name of a product used. When Governments changes their rules and regulations, this could have an effect on a business. For instance, after the accounting scandals of the early twenty-first century, the United States Securities and Exchange Commission became more focused on corporate compliance and the government introduced the Sarbanes-Oxley compliance regulations of 2002. When a new party takes power, there is likely to be a measure of uncertainty whilst it settles into the job of running the country and the effect of new policies is awaited. Even if the same political party is in power for many years, there will be a variety of political and economic issues that will cause it to make changes in political and economic directions, and most governments pass laws which affect market opportunities from time to time. Stability, though, is not the only issue of interest to business. It is also concerned that governments take political and economic decisions that do not cause the economy to decline or become less profitable for companies.

Influence of external environment on organizations: Organizations have a challenge of dealing with the environment's dynamism and uncertainties, in order to be successful. Strategically, managers have to be aware and alert on how changes in the competitive environment are unfolding. The environment of organization is categorized into both internal and external. The external environment is classified into the macro-environment and the industry.

The factors in this environment look at the way in which future trends in the political, economic, social, technological, environment and legal environment might impinge on organization. The business environment of the firm consists of all external influences that impact a firm's decisions and performance. Continuous scanning of the whole range of external influence is desirable, though it is unlikely to be cost effective and may create information overload

Political Factors: The political dimension of the general environment affects business activity. The philosophy of the political parties in power influences business practices. The legal environment serves to define what organizations can and cannot do at a particular point in time. The political environment facing organizations is becoming more complex and affecting businesses more directly. It has become increasingly difficult for businesses to take action without encountering a law, regulation, or legal problem. A very brief listing of significant laws that affect business would include legislation in the areas of consumerism, employee relations, the environment, and competitive practices. Political factors include Stability of government, Social policies, Trade regulations, Tax policies and Entry mode regulations that influence and limit organisations and individuals in a given society. These refer to government policy such as the degree of intervention in the economy. Political decisions can impact on many vital areas for business such as the education of the workforce, the health of the nation and the quality of the infrastructure of the economy such as the road and rail system. The dimensions being evaluated include the government attitude to foreign markets, the stability and financial policies of a country and government bureaucracy.

Economic Factors: Economic factors refer to the character and direction of the economic system within which the firm operates. Economic factors include the balance of payments, the state of the business cycle, the distribution of income within the population, and governmental monetary and fiscal policies. This part of the analysis is concerned with overall prospects for the economy. Often the political factors spill over into economic factors; For example, tax is usually decided by politicians, based on a mixture of political and economic factors. Interest rates, in many countries

are decided by a central bank, but political factors may still be important. Other economic factors include exchange rates, inflation levels, income growth, debt and saving levels, which impact available money and consumer and business confidence. The current state of world stock markets is a typical example of the volatility of economic factors. Key measures of economic factors include: GDP/GNP, inflation, interest rates, exchange rates, fiscal and monetary policy, wage and price controls and unemployment figures.

Social Factors: Social-classes would be another aspect affecting the consumer behaviour. This refers to national status hierarchy by which groups and individuals are distinguished in terms of self-esteem and prestige. According to Economic survey of Delhi (2001) the urban population is over 93% with per-capita income of 9.1% which clearly demonstrates growth amongst social classes. Past purchase experiences can influence the store choice of consumers which are further affected by these Socio-economic factors such as income, geography, personality, age, among others. Moreover, elderly people are less price conscious in comparison to youngsters. This implies that aspects such-as convenience and familiarity of corner-shops will be of greater importance than savings made at supermarket. Socio-cultural components of the environment influence the ability of the firm to obtain resources, make its goods and services, and function within the society. Socio-cultural factors include anything within the context of society that has the potential to affect an organization. Population demographics, rising educational levels, norms and values, and attitudes toward social responsibility are examples of socio-cultural variables.

Technological Factors: Technology is an aspect of the environment a firm should consider in developing strategic plans. Changing technology may affect the demand for a firm's products and services and its production processes. Technological changes may create new opportunities for the firm, or threaten the survival of a product, firm, or industry. Technological innovation continues to move at an increasingly rapid rate. Technology can change the lifestyle and buying patterns of consumers. Recent developments in the field of microcomputers have dramatically expanded the potential customer base and created innumerable opportunities for businesses to engage in business via Internet. Whereas computers were traditionally used only by large organizations to handle data processing needs, personal computers are commonly used by smaller firms and individuals for uses not even imagined fifteen years ago. Technological developments are the fastest unfolding and per-reaching in extending or contracting opportunity of an established company, these include the discoveries of service, the related products development, the process improvement and the automation and data processing. Technological

changes can turn an organization into loose confederation of functional empires. Technology has become more important, because customers are changing as distribution systems in relation to technology and competition. Markets are changing faster than ever before. The explosive emergence of internet requires every business to be globally competitive even if it sells goods and services only within local or regional market as the distance barrier is eliminated for worldwide distinction. Technological changes is a powerful determinant of entry barriers, shifts the bargaining relationship between industry and its buyers and suppliers, alters the nature and basis of rivalry among existing competitor and creates new products or product uses that substitute for others; and broadens or shrinks industry barrier. In low technology organisation, focus is utilizing and expanding technology whereas in high technology organisation, technology is critical determining factor for future access and high technology turbulence requires cutting edge technology.

Environmental Factors: Environmental factors include the weather and climate change. Changes in temperature can impact on many industries including farming and banking industry. High population growth rate indicates an enormous increase in labour supply. Population with varied tastes, preferences, beliefs, temperaments etc. gives rise to differing demand pattern and calls for different marketing strategies. The projected size and distribution of the economic costs and benefits of environmental factors are of key interest to business leaders and policy makers. Many estimates of the aggregate net economic effects of climate change are now available. Such estimates are generally long-range projections and are therefore subject to large uncertainty. Nevertheless, there is a general consensus that climate change is very likely to reduce countries' annual GDP (gross domestic product) on an aggregate and NPV (net present value) basis. For increases in global average temperature of less than 1°C to 3°C, 21 some impacts are projected to produce marked benefits in some places and sectors and impose costs on others. With greater environmental awareness this external factor is becoming a significant issue for firms to consider. The growing desire to protect the environment is having an impact on many industries such as the travel and transportation industries. The general move towards more environmentally friendly products and processes is affecting demand patterns and creating business opportunities.

Legal Factors: These are related to the legal environment in which firms operate. In recent years in the UK there have been many significant legal changes that have affected firms' behaviour. The introduction of age discrimination and disability discrimination legislation, an increase in the minimum wage and greater requirements for firms to recycle are examples of relatively recent laws that affect an organisation's actions. The existence of bureaucratic systems and cultures is central in making the decision to invest globally. The nature of corruption, local values and

assumptions that are built into national ideologies are major variables in this field. A great concern is the extent to which there is a culture of law or a culture of personal patronage, where negotiations are done on a personal rather than a legal basis. The impact of international lending agencies such as the International Monetary Fund or the World Bank is also important in creating a legal culture that a business will have to take seriously. Legal forces are highly important as they cover many aspects of company policy. Government policy affects industry as a whole through regulatory bodies such as the Department of the Environment and the Department of Trade and Industry. These bodies develop policies on the trading, restrictions and standards within their particular field. The policies created can affect businesses in various ways; in how their products are produced, promoted and sold. Monetary and fiscal policies utilized by governments influence business operations. Monetary policies affect the size of the money supply and interest rates.

UNIT – 2

International business strategy – Internationalisation – Management Philosophies – Porter's Model – Prehalad and Doz's model – International Marketing Strategy – Introduction to product, price (INCOTERMS), Distribution, Promotion in international context.

INTERNATIONAL BUSINESS STRATEGY

Companies go international for a variety of reasons but the typical goal is company growth or expansion. When a company hires international employees or searches for new markets abroad, an international strategy can help diversify and expand a business.

Economic globalization is the process during which businesses rapidly expand their markets to include global clients. Such expansion is possible in part because technological breakthroughs throughout the 20th century rendered global communication easier. Air travel and email networks mean it is possible to manage a business from a remote location. Now businesses often have the option of going global, they assess a range of considerations before beginning such expansion. Overseas operations are often attractive to executives seeking to reduce their budgets in order to increase profit. For example, it is possible to cut business overhead costs in countries with relatively deflated currencies and lower costs of living. U.S.-based businesses can further reduce overhead by operating in countries that have free trade arrangements with the United States. It is often cheaper to employ a workforce in these countries since the cost of living is lower. When companies experience
financial crises, executives sometimes attempt to save what remains of the company by reformulating the budget and moving overseas.

Expanded markets entice many executives into going global. William Edwards of All Business explains that going global can reduce a company's reliance on local and national markets. That is, downturns in consumer demand at home are offset by upturns in consumer demand in international markets. Larger markets also mean the potential for greater profit, so companies go global to seek new business opportunities and even to expand the range of goods and services that they offer. Sometimes businesses expand to under-exploited regions to gain market dominance before an industry competitor expands into the region.

Change is an ever present facet of business development. Businesses transfer ownership, for example, and end up reformulating their entire business structures. Companies hire outside consultants to advise restructuring during financial crises. Sometimes the fact that businesses go global is the product of the inevitable ebb and flow of commerce. An overseas buyer may transfer operations to the home country. The majority of an industry's business may shift

overseas, making global expansion all the more desirable. Competition may develop in regions such that it is unwise for your company not to follow.

HOW DO FIRMS GO INTERNATIONAL? – ENTRY STRATEGIES

Foreign market entry strategies differ in degree of risk they present, the control and commitment of resources they require and the return on investment they promise. There are two major types of entry modes:

1) Non-equity mode, which includes export and contractual agreements,

2) Equity mode, which includes joint venture and wholly owned subsidiaries.

The market-entry technique that offers the lowest level of risk and the least market control is export and import. The highest risk, but also the highest market control and expected return on investment are connected with direct investments that can be made as an acquisition and Greenfield investments

Exporting and importing: The first and the most common strategy to be an international company is: import and export of goods, materials and services. Exporting is the process of selling goods or services produced in one country to other countries. There are two types of exporting: direct and indirect. Indirect export means that products are carried abroad by other agents and the firm doesn't have special activity connected with international market, because the sale abroad is treated like the domestic one. For these reasons it is difficult to say that it is an internationalization strategy. In the case of direct exporting, the firm becomes directly involved in marketing its products in foreign markets.

Licensing: Licensing is another way to enter a foreign market with a limited degree of risk. The international licensing firm gives the licensee patent rights, trademark rights, copyrights or know-how on products and processes. In return, the licensee will: produce the licensor's products, market these products in his assigned territory and pay the licensor fees and royalties usually related to the sales volume of the products. This type of agreement is generally welcomed by foreign public authorities because it brings technology into the country.

Franchising: Franchising is similar to licensing except that the franchising organisation tends to be more directly involved in the development and control of the marketing programme. The franchising system can be defined as a system in which semi-independent business owners (franchisees) pay fees and royalties to a parent company (franchiser) in return for the right to

become identified with its trademark, to sell its products or services, and often to use its business format and system.

Compared to licensing, franchising agreements tends to be longer and the franchisor offers a broader package of rights and resources which usually includes: equipments, managerial systems, operation manual, initial trainings, site approval and all the support necessary for the franchisee to run its business in the same way it is done by the franchisor. In addition to that, while a licensing agreement involves things such as intellectual property, trade secrets and others in franchising it is limited to trademarks and operating know-how of the business. Advantages of the international franchising mode are as follows:

− low political risk

− low cost

− allows simultaneous expansion into different regions of the world

− well selected partners bring financial investment as well as managerial capabilities to the operation.

There are also disadvantages of the international franchising mode:

− franchisees may turn into future competitors

− demand of franchisees may be scarce when starting to franchise a company, which can lead to making agreements with the wrong candidates

− a wrong franchisee may ruin the company's name and reputation in the market

− comparing to other modes such as exporting and even licensing, international franchising requires a greater financial investment to attract prospects and support and manage franchisees.

Joint Ventures: Foreign joint ventures have much in common with licensing. The major difference is that in joint ventures, the international firm has an equity position and a management voice in the foreign firm. A partnership between host- and home-country firms is formed, usually resulting in the creation of a third firm

This type of agreement gives the international firm better control over operations and also access to local market knowledge. The international firm has access to the network of relationships of the franchisee and is less exposed to the risk expropriation thanks to the partnership with the local firm.

This type of agreement is very popular in international management. Its popularity stems from the fact that it permits the avoidance of control problems of the other types of foreign market entry strategies. In addition, the presence of the local firm facilitates the integration of the international firm in a foreign environment.

Strategic alliances: A strategic alliance is a term used to describe a variety of cooperative agreements between different firms, such as shared research, formal joint ventures, or minority equity participation. The modern form of strategic alliances is becoming increasingly popular and has three distinguishing characteristics:
− they are usually between firms in high - industrialized nations
− the focus is often on creating new products and technologies rather than distributing existing ones − they are often only created for short term durations.
Technology exchange - this is a major objective for many strategic alliances. The reason for this is that technological innovations are based on interdisciplinary advances and it is difficult for a single firm to possess the necessary resources or capabilities to conduct its own effective R&D efforts. This is also supported by shorter product life cycles and the need for many companies to stay competitive through innovation.
The greatest disadvantage of strategic alliances is the risk of competitive collaboration - some strategic alliances involve firms that are in fierce competition outside the specific scope of the alliance. This creates the risk that one or both partners will try to use the alliance to create an advantage over the other.

Direct investments: In this arrangement, the international firm makes a direct investment in a production unit in a foreign market. It is the greatest commitment since there is a 100% ownership. There are two primary ways for direct investments: firms can make a direct acquisition in the host market or they can develop its own facilities from the ground up and this form is called Greenfield investment. Acquisition has become a popular mode of entering foreign markets mainly due to its quick access. Acquisition is lower risk than Greenfield investment because the outcomes of an acquisition can be estimated more easily and precisely. Greenfield investment is the establishment of a new wholly owned subsidiary. It is often complex and potentially costly, but it is able to full control to the firm and has the most potential to provide above average return. Greenfield investment is high risk due to the costs of establishing a new business in a new country. This entry strategy takes much time due to the need of establishing new operations, distribution networks, and the necessity to learn and implement appropriate marketing strategies to compete with rivals in a new market. Foreign market entry strategies are numerous and imply a varying degree of risk and of commitment from an international firm. In general, the implementation of an international development strategy is a process achieved in several steps. Indirect exporting is often used as the starting point; if the results are satisfactory, more committing agreements are made by associating local firms.

INTERNATIONALISATION

Porter's Five Forces model, named after Michael E. Porter, identifies and analyzes five competitive forces that shape every industry, and helps determine an industry's weaknesses and strengths. These forces are:

1. Competition in the industry;
2. Potential of new entrants into the industry;
3. Power of suppliers;
4. Power of customers;
5. Threat of substitute products.

Frequently used to identify an industry's structure to determine corporate strategy, Porter's model can be applied to any segment of the economy to search for profitability and attractiveness.

BREAKING DOWN 'Porter's 5 Forces'

Porter's Five Forces is a model of analysis that helps to explain why different industries are able to sustain different levels of profitability. This model was originally published in Porter's book, "Competitive Strategy: Techniques for Analyzing Industries and Competitors" in 1980. The model is widely used, worldwide, to analyze the industry structure of a company as well as its corporate strategy. Porter identified five undeniable forces that play a part in shaping every market and industry in the world. The forces are frequently used to measure competition intensity, attractiveness and profitability of an industry or market.

Competition in the Industry: The importance of this force is the number of competitors and their ability to threaten a company. The larger the number of competitors, along with the number of equivalent products and services they offer, dictates the power of a company. Suppliers and buyers seek out a company's competition if they are unable to receive a suitable deal.

Potential of New Entrants into an Industry: A company's power is also affected by the force of new entrants into its market. The less money and time it costs for a competitor to enter a company's market and be an effective competitor, the more a company's position may be significantly weakened.

Power of Suppliers: This force addresses how easily suppliers can drive up the price of goods and services. It is affected by the number of suppliers of key aspects of a good or service, how unique these aspects are and how much it would cost a company to switch from one supplier to

another. The fewer number of suppliers, and the more a company depends upon a supplier, the more power a supplier holds.

Power of Customers: This specifically deals with the ability customers have to drive prices down. It is affected by how many buyers, or customers, a company has, how significant each customer is and how much it would cost a customer to switch from one company to another. The smaller and more powerful a client base, the more power it holds.

Threat of Substitutes: Competitor substitutions that can be used in place of a company's products or services pose a threat. For example, if customers rely on a company to provide a tool or service that can be substituted with another tool or service or by performing the task manually, and this substitution is fairly easy and of low cost, a company's power can be weakened

PRAHALAD AND DOZ'Z MODEL:

Responsiveness Grid from Prahalad and Doz makes a suggestion for the international strategy of a firm. There are in total four strategies. The X-axis maps out the pressure on the firm for local responsiveness. The Y-axis maps the cost pressure on the firm.

Integration - Responsiveness Grid from Prahalad and Doz

The vertical axis represent a combination of pressure on integration and cost competiveness, with pressure on local responsiveness on the horizontal axis.

The more important it is for a firm to respond to local wishes the higher it is placed on the horizontal axis. For chemical manufacturers it is not very important to respond to local wishes, since chemicals are chemicals are no real adoptions can be made. High-end goods are often not

tailored to local wishes either. Think of a Rolls-Royce, they sell existing products to the local buyers at premium prices with no local adaptation. Firms who establish relative independent subsidiaries often find themselves adopting the product to local wishes and will be placed at the rights side of the horizontal axis.

INTERNATIONAL MARKETING STRATEGIES

No country or organization is sufficient unto itself. Organizations market goods and services that have no domestic demand in international markets and perhaps come back with products that have domestic demand. In some cases, industrial inputs such as labour, raw materials, capital and technology are imported from foreign lands to complement indigenous industrial inputs for efficiency and effectiveness. The importance of international marketing can never be overemphasized. In acknowledging this fact, Awoniyi (1999) states:

We are all affected by international marketing. We wake up in the morning with the help of Japanese alarm clock. At breakfast we eat Indomie or drink Maxwell or Colombian coffee and eat bread made of wheat from America. We glance at advertisement for French wine in the newspapers. Many of the goods and services we consume each day are imported. And over 70% of products made in this country (Nigeria) face direct foreign competition.

This analogy shows clearly that every individual, organization, even country is affected directly or indirectly by international marketing.

International Marketing Defined

Cateora et al define international marketing as "the performance of business activities that direct the flow of the company's goods and services to consumers or users in more than one nation". It is the performance of business activities including marketing research, product development and management, and marketing intelligence, across national boundaries with the view of satisfying human wants and needs and achieving company's predefined objectives."

Majaro stipulates that any company that endeavours to market its products in more than one country such a company is involved in international marketing. Basically, what differentiate international marketing from international trade are the operative words of 'sense', 'serve' and 'satisfy'. International marketing takes place when a company senses or identifies currently unfulfilled needs and wants, design appropriate product to fill the gap and satisfy the consumers at profit. International marketing is entrepreneurial. It is innovative and dynamic, hence requires deliberate, holistic, and concerted efforts and programmes to make it successful. International

trade is more or less individualistic in nature, may not be customer-centered, and may not require deliberate efforts in its operations.

Differences between Domestic and International Markets

In domestic market, there is homogeneity of currency, language and culture. There is little or no government interference; distance poses little or no barrier and marketing environment is not largely complex; whereas in international market, there are divergent cultures and languages, many currencies are involved, government interference to protect domestic markets and industries, distance barrier and business or marketing environment is largely complex, dynamic, and multi-dimensional; differences in legal systems, etc.

The Importance of International Marketing

The importance of international marketing can be looked at from two perspectives:

a. Its importance to the nation
b. Its importance to the organization

Its importance to the nation: In this case, international marketing derives its importance from international trade. Adam Smith made it clear when he stated that:

International trade carries out that surplus part of the produce of their land and labour for which there is no demand among them (exports) and brings back in return (imports for it something else for which there is a demand.

It gives a value to their superfluities by exchanging them for something else which may satisfy a part of their wants, and increase their enjoyment. Thus, international marketing makes available goods and services which are not or sufficiently produced in a given country, encourages even distribution of resources, goods and services. It increases the productive base and consumption level of a nation. The proceeds from international marketing contributes to the growth of both a nation's gross domestic and gross national products (GDP and GNP) which are sound indicators of economic growth. Adam Smith also pointed out that "international trade encourages the nationals to improve the productive power and to increase the real revenue and wealth of society."

International marketing encourages capital formulation and accumulation. It improves the living standard of the people; increase their per capita income through employment generation and entrepreneurial development. It is a sure means of revenue generation to the government through imposition and collection of taxes, levies and tariff. Umoren observes that for the

powerless third world countries, international marketing or trade appears to be seen as the only viable route to economic development, economic emancipation and politico-economic independence. Hence, international trade is seen to them as a source of earning foreign exchange to accomplish their developmental dreams.

It's Importance to the Organization: A firm that engages in international marketing benefits in the following areas;

i. Achieving economies of scale through large-scale production and reduced per unit cost of production.

ii. Prospects for high returns in foreign markets: certainly, a firm that markets internationally tend to generate more revenue and profit than a firm entangled with domestic market.

iii. Corporate Strategy to escape tough competition at home. A firm can liberate itself from harsh competition at home by venturing into international markets where opportunity abounds for it to explore.

iv Need to Prevent Stagnation and Vulnerability: Home market may not sufficiently provide for organization's growth especially where domestic markets is saturated.

v. Need to prolong the life of its products: A product that has reached its declining stage in India may begin its introductory stage in Srilanka depending on need, time and marketing programmes applied.

vi. National necessity: A firm can venture into international marketing because of the domestic country's foreign policy requirement. Nigeria sees Africa as centerpiece of her foreign policy, as such can direct all pharmaceutical companies, for instance, to take some of their products to other African states as a means of strengthening her foreign policy.

International Marketing Environment

International marketers operate within the ambits of a complex set of environments (controllable and uncontrollable), which can mar or make their aspirations. The uncontrollable environment includes economic, socio-cultural, politico-legal and technological factors, while the controllable factors are the 'popular' four Ps of marketing, in other words called the marketing mix.

The Economic Environment: Every country has unique economic factors that influence business decisions and activities. There are diverse prices for goods and services, diverse purchasing habits, difference in monetary and fiscal policies, position of GDP, interest rates, balance of payment business customs and practices, etc. For instance, investment seems to

concentrate more in countries with moderate tax regime than countries with harsh taxation. The economic system practiced in an economy also influences business decisions and international marketing. Countries that adopt free market system tends to be more liberal and easy to penetrate than ones that adopt centrally planned system. Penetration into centrally planned economies requires government direction, scrutiny and surveillance and in some cases government interference which may not augur well for the international marketer.

A countries position in GDP signifies her level of economic development, investment and consumption. Countries with high GDP growth rate are prone to high consumption level whereas countries with low GDP growth rate are prone to low consumption level and do not encourage investment. This explains why third world countries have low investment. Also, the financial climate that prevails in a country influences the international marketer's decision to a launch his offer in such a country. A stable financial climate (stable financial institutions, monetary policies, and encouraging interest rate) encourages business decisions while the reverse is the case for unstable and unhealthy financial climate.

Socio-Cultural Environment: This environment houses factors such as culture, social institutors, language, aesthetics, attitude and value, religion, etc which shape the behavioural pattern of a particular people. Culture has been defined by Vern Terpstra as the man-made part of our environment or the distinctive way of life of a people. Culture consists of material and non-material elements. Material elements of culture are those aspects of culture that can be seen, touched, tasted smelt and heard, e.g. products. Non-material aspects of culture cannot be seen, tasted, touched, smelt but could be heard e.g music; thus, non-material elements of culture are abstract in nature. Culture plays enormous role in determining and defining a market to venture into. An international marketer must be conversant with the people's total way of life before taking decision on what to produce, how to produce, for whom to produce and what should constitute price, promotional and distribution strategies. It is on this note that Umoren observes that there is need for greater sensitivity on the part of the international marketer to the cultural realities of his market. Cateora and Hass called it "Factual Knowledge" which provides the marketer with the knowledge and appreciation of symbols and other meaning of everyday things of life folded in the indigenous people. It determines the acceptance of a product. Close to a century, there has been a debate as to whether there is superior culture or inferior culture. In most responses, the answer has always been "no." However, the attitude of third world countries towards foreign made products has gone a long way to negate this response.

Social institution such as schools, churches, mosques, the press, government and its agencies, peers (age group, clubs, etc) and organizations also influence the behavioural pattern of the people. For instance, the level of education (i.e literacy level) influences the choice of advertising messages, mode of advertising, marketing strategies to be adopted and marketing institutions existing in a country.

Aesthetics is the beauty of the people expressed in their music, art and dance. Aesthetics and material culture are important in product type and design, quality, use, packaging, advertising design and effectiveness and total product presentation. Language showcases verbal and non-verbal expression to culture and it is indispensable to communication effectiveness in marketing. Language is found in product packaging, labeling and promotion.

Politico-Legal Environment: Another important aspect of the international marketing environment is the politico-legal factors. A country's political structure and practices as well as her legal framework have great influence on international marketer's decision to market his product there. There are diverse laws or legal systems guiding business activities in different countries. There are laws regulating business, which make procedures for business registration, ownership, structure and composition, size and type of business (sole proprietorship, partnership, joint stock, and cooperative businesses). In many countries, there are laws guiding business practices. An international marketer should be familiar with the laws guiding business activities in the country where he wants to penetrate.

Another subset of this environment is the political setting of a country. It is important to know the form of political system a country adopts before launching in their market. The following questions would guide the international marketer in his decision making process:

- *What is the political system of the country?*
- *What is the country's political structure?*
- *How stable is the government?*
- *Is the judicial system effective?*
- *What are the litigation procedures?*
- *Does the country respect international conventions?*

We must note that, international conventions include:

1. The Parish Convention
2. The Inter-American Convention
3. The Madrid Convention
4. The Lame Convention

Technological Environment: The level of technology prevalence in a country affects the level of production, innovation and assortment of goods and services that a marketer can market there. Today, firms are confronted with the challenge of using modern or improved techniques in production. Modern technique encourages mass production, innovation and greater returns on investment. For instance, the use of computers has replaced the use of thumb method that usually involved much paper work and mistakes. Thus, the use of computer is faster, reliable, accurate and gives up-to-date information about stocks.

Technology can also be found in the area of communication where different equipment and gadgets have been developed to ease and fasten communication. Today, we have the internet, fax, telephones, etc which guarantee effective communication. It should be the concern of an international marketer to identify the challenges and opportunities associated with technological advancement and use them to better his lots.

Problems in Marketing Internationally

The probable problems encountered by an international marketer are not different from the international marketing environment and they have been explained above. These problems are: divergent culture, divergent political/legal framework, geographical location, difference in currencies, inadequate communication devices, technology and competition.

DEGREE OF INVOLVEMENT IN INTERNATIONAL MARKETING

There are basically six ways through which a firm can involve in international marketing, namely: Casual involvement, Indirect export, direct export, foreign involvement without investment, foreign involvement with investment and multinational operations. This is shown in the diagram below:

Casual Involvement: The firm in this involvement does not actively or intentionally intend to internationalize as such it does not sense nor respond to the needs and wants of consumers in the international markets. This firm may fill a one-time order but does not consider or include it in its strategy thrust for long-term investment.

Indirect Export: In this case, the firm does not intend to go internationally but its products could be taken to international markets by resellers. These resellers are exporters, export merchants or export brokers who could be used by a firm to expand its sales base.

Direct Export: In this case, a firm can create export department which will take its product to the international markets or it can sell to international customers who invariably sell to the host consumers. According to Awoniyi in direct export, a firm begins to view international markets as a long term opportunity for sales and profits.

Foreign Involvement without Investment: This occurs where a firm intends to launch its product in a foreign market but does not wish to establish its production facilities in that country. By this, a firm can negotiate to license its production technology to a domestic investor who can establish the production facilities in that country.

Foreign Involvement with Investment: In this case, a firm finances the establishment of production facilities in the foreign land. This is affected when a firm realizes that the host country is juicy enough to guarantee sizeable returns on investment.

Multinational Operations: This operation is carried out by multinational corporations. They see the whole world as global village, hence make decisions within a global framework. Multinational corporations see the world as source of supply and a set of markets, as such, does not distinguish between national and international markets, e.g. of MNC is Unilever Plc.

Strategies for Entry

Entry strategy to adopt is one of the fundamental decision areas in international marketing. This decision requires the international marketer to consider factors such as cost, risk, and control. A rational marketer would always want his programmes to incur less operational cost, low degree of risk and exercise larger control.

The entry strategy adopted by an international marketer goes a long way to shape his programme, as such; holistic approach should be employed if he was to make reliable and rewarding decision. Osuagwu and Eniola identify factors necessary for entry strategy decision to include; the company's objectives and expectations of the volume of business to be generated, the size of the company and its financial resources, patterns of involvement in other foreign markets, the managerial culture and levels of international marketing expertise within the company, the nature and degree of competition within the market, the nature of the product and whether it has any distinct competitive advantage either in terms of its technology, patent production, or trademarks and the market's political infrastructure and whether any tariff or non-tariff barriers exist or are likely to be introduced. Other factors that need consideration according to them are; investment

needs of each market, the manpower requirements, levels of political and financial risk, the administrative needs, the marginal marketing cost, the degree of flexibility and control that is possible. All these and many more guide international marketer in his entry strategy decisions. *Below are the international market entry strategies available to a marketer.*

Exporting: This is the most popular strategy in developing countries and in countries where government takes active part in business ownership. This strategy involves direct and indirect exporting. In direct export, a firm sells its product to international customers. In this case, the firm is beginning to view international markets as goldmines, long-term opportunity for sales and profits (Awoniyi, 1999). Indirect export entails selling to domestic customers. These customers can be organizations or individuals who sell the products in the international markets. In indirect export, the firm has no intention of internationalizing and does not view international markets as opportunities for sales and profits, and does not include it in its long-term strategy thrust. Exporting strategy is best for companies with complementary products. Many firms adopt this strategy in order to earn foreign exchange, which aids in importation of required raw materials and other inputs.

Licensing and Franchising agreements: Licensing is a contract or agreement between an international firm and a firm in a host country in which the international firm grants a host country's firm the permission to use its patent, trademark, manufacturing process and technical assistance for a payment called royalty. This agreement gives the host country's firm a degree of freedom to produce and market its products. Coca-Cola (a USA Multinational Corporation) has granted license to many firms in the third world countries. Licensing is mostly applied to marketing of physical products.

Franchising on the other hand is mostly applied to service firms but retains all other characteristics of licensing. The franchisee honours specification on nature of operation directed by the franchiser. A good example is McDonald, which franchised its hamburger operation in many countries in Europe and Asia.

Piggyback Operations: Here an international marketer uses his own foreign distribution network to sell another company's products alongside his. It is mostly adopted when he realizes that the other product can complement and smoothen the sale of his own products. To an extent, this strategy is similar to exporting strategy. This strategy is beneficial to the marketer in that it guarantees greater economies of scale, expands product range and boost sales.

Contract Manufacturing and Management Contracting: An international marketer may decide to hand over manufacturing of a product to host country' firm(s) while retaining the marketing of the product. This is called contract manufacturing. It is usually adopted where local labour is efficient and cheap and there are stringent government restrictions on foreign manufactures. Management contracting entails a situation where a firm provides management skill and proficiency while domestic firms own the production facilities. This strategy is mostly seen in the service industries such as hotels and airlines. For example, Imo Concorde Hotel is managed by a foreign firm. There is relatively low risk associated with this strategy.

Assembly Operations: This is another strategy of entering into international market. This strategy involves product assembly and manufacturing in a host country. There are many factors which encourage the decision to adopt this strategy, namely, need to avoid tariff and non-tariff barriers, existence of cheap labour and other inputs, favourable tax rates, cheap capital, favourable business laws, unsaturated and less competitive market, etc.

Local assembly involves the manufacturing of component parts in a parent country and coupling them in the host country. Local assembly is expensive to operate as it involves multiple labour and operational costs especially in shipping, tariff, labour (domestic and abroad). Local manufacturing is cheaper especially where the host country provides good source of raw materials and labour. Peugeot and General Motors are using local assembly strategy in Nigeria.

Joint Ventures: Joint Ventures approach is another strategy of entering into international markets. It is very popular in developing countries. In Joint Ventures strategy, a foreign firm looks for local firm with which it can pool resources together to run a programme in the host country. It is a form of partnership in which a foreign firm enters into business with one or more domestic firms to achieve specific objectives. The problem with joint ventures is that of control and tendency for loss of investment. Control is shared between host firms and the foreign firm and there is the possibility of losing out especially where the alliance is with government or aggressive domestic partner owing to political, legal and economic trends in the host country. However, it allows for greater economies of scale in technology, production, marketing, and information generation.

Wholly-Owned Subsidiaries: A company may decide to wade into the international markets by building its (wholly-owned) subsidiaries there. This gives complete control over marketing, administrative and production decisions. Before, a firm adopts this strategy, there is need to

assess the potentiality and viability of the market and macro-environmental factors prevailing in the host country. There is high risk associated with this strategy particularly in the area of financial commitment and operation. It is mostly adopted by multinational corporations.

Multinational Operations: When a firm operates in more than one country and makes its production, marketing and administrative decisions within a global framework, it is called a multinational corporation. A multinational corporation views the world as a set of markets and sources of supply (Awoniyi, 1999). Its decisions (production, marketing and administrative) are centered on the entire world, hence it has no room for distinctive marketing programmes for different market segments.

Global Marketing: This strategy is related to multinational operations strategy. It is defined as "selling the same product, the same way, everywhere," The customers are seen the same way; thus the notion that they are similar and have same preferences and that developing standardized product and application of integrated marketing mix to all markets can guarantee customer and organization satisfaction. Coca-Cola is a good example of Multinational Corporation adopting global marketing. Others are General Motors, Exxon, IBM, Toyota Motor Co; etc.

Marketing Mix Decisions in International Marketing

The marketing mix is fundamental to marketing decisions. They shape all marketing activities and performance. The marketing mix as propounded by McCarthy is product, price, place and promotion. A lot have been said about these 4Ps, as such, decisions areas will be highlighted only.

Product: Decision areas include quality, packaging, features, labeling, sizes, brand name, servicing, product policies, design, uses and usage.

Price: Decision areas include price list, discount, payment period, credit terms and allowances, pricing policies, strategies and methods. Factors affecting price in international marketing are government legislation, competition, the buyer's level of disposable income, demand elasticity of the product, nature of the market, cost of production, pricing objective (pricing strategy and pricing policy).

Place (also called distribution): Decision areas cover channel of distribution, location and coverage, inventory, transportation, warehousing, etc.

Promotion: This covers advertising, personal selling, sales promotion, public relations and publicity.

Taking decisions on the marketing mix requires the international marketer to understand the market he intends to serve; the culture of the people, consumer behaviour and dispositions, taste and preferences, business customs, and laws guiding business activities in the host country.

Organizing for International Marketing

Organization for domestic marketing shares similarity with organizing for international marketing except in geographical expansiveness. Therefore, the reader is referred to marketing planning, organizing and control. This section will only serve as a remainder. There are six major organizational structures, namely:

1. Functional structure
2. Product groupings structure
3. Market or customer groupings structure
4. Geographical or territorial structure
5. Channel of distribution-base structure
6. Matrix approach: This combines functional structure with any of other organizational structures.

Other Areas of Consideration

Apart from the marketing mix, there are other important areas which an international marketer should prioritize in order to achieve his objective. These areas are summarized as the 12Cs of international marketing. They include:

Country: The marketer must be acquainted with the country where he intends to sell his product. He should know the country's policy to import, business customs, business laws, the country's marketing and business infrastructure.

Culture: Looks at the people's culture as expressed in their norms and values, language, behaviour, aesthetics, arts, music, technology, etc.

Concentration: Looks at geographical concentration of the people in the target country showing age distribution, income distribution, access to channels of distribution, access to decision makers, density of population, etc.

Communication: Available communication media, channel media, language, the choice of promotional media.

Channels of Distribution: Direct or Indirect marketing channel, distribution strategy to adopt, mode of transportation, etc.

Capacity: Capacity of the consumer to pay; capacity of customers or clients to reach contractual agreements.

Currency: The acceptability and stability of local currency; the use of hard currency.

Control and Coordination: Ability of the international marketer to exercise a degree of control over international marketing activities goes a long way to influence the success of his venture. There should be clarity and coordination of plans, policies, objectives and strategies; coordination of agencies and individuals involved in the chain of command and distribution channel; ensure effective communication, set and reach performance measurement criteria (standard).

Commitment: Commitment to quality and service.

Choices: The international marketer must consider the marketing mix choices available in the prospective or target markets and use them to satisfy the market at profit.

Contractual Obligations: This looks at payment terms and conditions, credit terms and period, warrantees, guarantees of delivery; stages of payments to be made by the customers, penalties for late delivery or failure to deliver; financial deposits (in hard currency) required as evidence of the marketers good faith.

Caveats: This has to do with the important aspect of the marketing environment which the international marketer should not ignore. The international marketer should pay attention to:

a. His company's reputation; the quality of its products, delivery on time, long term presence in the market.

b. Motivation of export salesmen.

c. Local risk

d. Political stability

e. Economic trends state of the economy

f. How business is done in the target country. (Morden; A. R., 1991).

Unit – 3

Technology and MNC – Technological interdependence – strategy and innovation – technology accumulation – Home or Overseas R&D – Organsiational issues – Technological performance – Introduction to international finance –Exchange rate – changes, forecasting, risk – International cash management, taxation.

TECHNOLOGY AND MNC

During the twentieth century different economic development models were conceived to overcome poverty, hunger, and underdevelopment and these have been applied around the world. At the end of the 1980s and early 1990s, global environmental concern started to enter debates on economic development as the Brundtland Commission (World Commission on Environment and Development, 1987) popularized the concept of sustainable development. Sustainable development defined by the Brundtland Commission as 'development that meets the needs of the present without compromising the ability of future generations to meet their own needs' is a broad concept that provides the basis for creating and applying the new development models. Among other important issues, technology transfer from the developed or first world, to the underdeveloped or third world, is essential for the successful implementation of these models. Agenda 21, one of the five documents generated at the United Nations Conference on Environment and Development (UNCED) held in Rio de Janeiro in 1992 recommends that countries should develop and implement policies to pursue technology transfer in order to achieve sustainable development. Capacity building, also considered within this document, is a key element for achieving sustainable development and can be used to facilitate access to new technologies, usually owned by multinational corporations.

TECHNOLOGY TRANSFER

Technology transfer is recognized as an important mechanism to help developing countries to overcome their lack of capacity for social and economic development and it is defined as 'the movement of the technology required for economic development from where it exists to where it is needed. Technology transfer can occur in both vertical and horizontal ways; vertical transfer takes place within the firm and horizontal transfer from one industry or country to another industry or country. It involves commercial and non-commercial transactions such as management, technology and technical operations and focuses our attention to broad aspects including:

a) the role of educational and research institutions

b) the interdisciplinary and interdependent nature of technology transfer, and

c) the variety and importance of stakeholders' involvement.

The main stakeholders in technology transfer include multinational corporations, government organizations and educational institutions.

Although there is a consensus that developing countries need the transfer of technology to improve their social, environmental and economic conditions, there has been a debate for many years regarding the level of technology that should be transferred to them. The debate revolves around 'appropriate technology' versus 'advanced technology.' The proponents of appropriate technology affirm that developing countries do not need most advanced technologies as epitomized in Schumacher's 'Small is Beautiful'. The argument is that the introduction of advanced technologies into poorer and less developed societies raises more problems than it can solve, they are very costly relative to the income of the local population, they require an educational and industrial infrastructure that takes decades to build and most importantly, they inhibit the growth of indigenous innovation capabilities.

The proponents of advanced technology affirm that developing countries can benefit from acquiring advanced technologies. They argue that (1) modern science and advanced technology are inextricably interrelated, (2) advanced technology is critical for economic growth, (3) advanced technologies can greatly accelerate the alleviation of poverty and underdevelopment, (4) advanced technology can enhance the overall institutional and organizational capacities for growth and change, and 5) advanced technologies are cleaner, healthier and more efficient. In the 2001 annual report entitled 'Human Development Report 2001: Making New Technologies Work for Human Development', the United Nations encourages the transfer of new technologies to developing countries in order to improve their economic and social systems to overcome poverty. It warns, however, about the risks of managing these new technologies.

Implementation of Technology Transfer

Almost all developing countries are importing technology of different kinds from different countries in different ways. The major channels for transferring technology include trade in products, trade in knowledge and technology, foreign direct investment, contractual agreements and international movement of people. Although direct investment is considered as one of the most important channels, trade in products and international and international movement of people has become an important channel as well. Multinational firms possess the abilities to undertake successful technology transfer in developing countries (United Nations

Industrial Development Organization, 1996). These abilities depend not just on their individual efforts, but also on the characteristics of the national system of innovation of host countries, which is defined as a network of public and private institutions located within national borders whose activities and interactions enable the generation, importation, assimilation, modification, diffusion and use of knowledge. In a national system of innovation, there is an interaction between six main subsystems: productive, scientific and technological, management, education and training, financial, and the administrative regulatory system. In most developing countries, national systems of innovation tend to be weak and unstructured.There are two scenarios for a technology transfer to take place: 1) there must be an absorptive capacity in the receiver country, and 2) technology transfer and capacity building are two events that have to occur at the same time.

CAPACITYBUILDING

There is no doubt that most developing countries lack capacity within their educational institutions to absorb the transfer of technology. Capacity building is a broad concept that includes individuals, organizations and societies that interact within an environment; it can be applied to different areas such as technology, science, leadership, education, community development and others. This article deals with building capacity in educational institutions for technology transfer. The United Nations Development Program (UNDP) defines capacity building as "the process by which individuals, organizations, institutions and societies develop abilities (individually or collectively) to perform functions, solve problems and set and achieve objectives (Management Development and Governance Division, 1997)." The International Petroleum Industry Environmental Conservation Association (IPIECA) provides a definition emphasizing the role of the private sector and defines capacity building as 'a process of constructive interaction between countries and the private sector designed to develop the capability and skills to achieve environmentally-sound forms of economic development through the use of modern technologies and management systems, a competitive workforce and appropriate laws and regulations' (International Petroleum Industry Environmental Conservation Association, 1995). Both definitions consider the development of skills and abilities as the main purpose of capacity building.

Barriers to Capacity Building

There are serious barriers to increasing the capacity of educational institutions in developing countries. These are: Resources and managerial barriers: Most developing country

educational institutions do not have the necessary resources and management skills to focus on research and development. Professors and teachers are not well paid and laboratories and research centers are not well equipped. Libraries do not have sufficient budgets required to keep up to date information on scientific developments. Professional orientation barriers: Educational organizations in developing countries are generally inadequately focused in terms of their research and professional orientations. Faculty members are often not well trained to conduct research and those who are, do not have access to current literature and/or do not have adequate resources to conduct their research. There is also a bureaucratic control and hierarchy that influence the organization that acts as a retardant in this development. Cultural barriers: the lack of a 'scientific culture' in developing countries is another barrier to capacity building. Most educational institutions are teaching-oriented and not oriented to applied research. Additionally, most of developing countries' national policies focus on health and education, giving little attention to enhancing capacity to produce, organize, and utilize scientific Knowledge and technology.

Capacity Building Implementation

Capacity building is concerned with creating or enhancing the ability of society to perform specific tasks and attain development objectives. To implement capacity building, it is important to understand the levels in which capacity building may occur: (United Nations Development Program, 1998): The system: This level would cover the entire country or society and all the subcomponents that are involved, including both formal and informal organizations within the defined system. The entity: This level is a formal organization, a private operation, or an informal organization. The individual: This level includes individuals both within entities involved in the management and delivery of an initiative, as well as those who are beneficiaries or are otherwise impacted by the initiative.

THE ROLE OF THE MNCs

It is widely recognized that economic growth of countries depends to some extent on the successful transfer of technology and MNCs are recognized as the key players for this to happen, because they control resources and technology and utilize efficient and sophisticated management systems. Corporations, through foreign direct investment (FDI), bring technology, management, know-how, and access to host country markets. FDI also affects employment creation, the environment, community development and human resources. However, their contribution in terms of technology transfer is often minimal and in some cases unnoticeable.

Based on the outcomes of field research, we can argue that there are many reasons for this, such as a) the misunderstanding of the term 'technology transfer'; b) the ineffective use of resources; c) the lack of capacity of developing countries to absorb new technologies, and d) the lack of communication with educational institutions in developing countries.

Some corporations operating in developing countries are bringing new technologies to improve their production (e.g. technologies to increase heavy oil production in South America). The question is: is this really transfer of technology? Is the country absorbing these new technologies? If the corporation is bringing new technologies to improve production in their local subsidiary, it may not be a transfer of technology. It is the use of new technology by the same corporation in a different location. But it does not necessarily follow that there is indeed technology transfer.

Corporations engaged in technology transfer sometimes do not effectively use their resources. Some examples presented in the report "The oil industry experience: technology cooperation and capacity building" (IPIECA, 1995) show that the transfer of technology could be more effective if educational institutions were involved.

Another important reason for not having an effective transfer of technologies from MNCs to developing countries it the lack of capacity in their educational institutions to absorb, transform and innovate with the new technologies. Finally, there is a lack of communication between educational institutions in developing countries and corporations. Few corporations are considering educational institutions in developing countries as key partners for technology transfer. There is the opportunity for corporations to improve the capacity of educational institutions in developing countries. By doing so, they will contribute to their host country in a more effective way. Examples include Placer Dome in Chile where the company was able to improve the capacity of the local university and both parties benefited from it. The corporation saved money by using the university laboratories for sample analysis and by hiring local graduates and the university increased their level of education by teaching new technologies used by the corporation such as underground water monitoring. This example was part of a field study conducted between 2000 and 2002 in Andean Latin American countries.

MODEL FOR BUILDING CAPACITY IN EDUCATIONAL INSTITUTIONS

The key role of academic institutions in development is widely accepted because they are centers for acquiring and innovating in knowledge. However, their role becomes less effective if there is not a common ground between what educational institutions deliver and what the country's needs are. For instance, some universities in poor regions of Latin American countries do not offer

programs needed in the region such as resource development and management courses (e.g. water management, land management, agriculture, and farming). It was found that the weight of constraining factors for building capacity varies across countries. As a consequence potential intervention strategies will vary from country to country. The participation of both the governmental and private sectors in the formulation process is essential because of the need for dialogue and consensus for capacity development.

There are many ways to build capacity in educational institutions in developing countries. Based on our field research in Latin America and literature review we identified six different strategies for improving the capacity of educational institutions: direct involvement, partnership, involving a third partner, network of partners, creating a cluster. Based on the concepts and current strategies/approaches for technology transfer and capacity building, we propose a model that requires the engagement and commitment of multinational corporations, host countries and educational institutions if transfer of technology is going to happen. No one of the three stakeholders can make successful technology transfer happen without the active domain-based collaboration of the others. This model, represented by Figure 2, includes four main steps for host governments, with the help of MNCs operating in their countries to follow:
Step 1: Stabilize the economic, social, political and legal conditions in the host country (the system). Having a stable environment will encourage MNCs to invest. Countries like Chile and Colombia in Latin American have proven to be stable in the long term in terms of economic and political conditions. Also, they have established the necessary legal framework to protect foreign investments. The opposite exists in Bolivia and Ecuador where political and economic instability has caused many firms to leave these two countries. The more stable a country is in terms of economic, social, political and legal conditions, the more likely that foreign direct investment will happen.

Step 2: Strengthen government entities' capability to negotiate with MNCs. Most developing countries do not have well qualified people to negotiate with MNCs mainly due to the low salaries paid by government. However, we suggest that government entities should have well educated professionals to negotiate the contracts with MNCs. In addition to technical and economic considerations, social development and environmental issues should be key components during the negotiation process.

Step 3: Create a national system of innovation (NSI). Developing countries' lack of a NSI that can improve their capabilities to absorb knowledge and innovate from technology transfer. A NSI is comprised of educational institutions, private firms, government entities, NGOs and communities, all working with a common goal. Educational institutions are the key players and should be able to engage other stakeholders in the process of building and improving, their capacity to absorb and innovate knowledge.

Step 4: Develop strategies for absorbing, assimilating, and innovating imported technologies. Strategies to absorb and assimilate new technologies and innovate should consider short, medium and long term plans.

COMPETITIVE ADVANTAGE

Firms obviously need to consider the benefits to them from helping developing countries to build their capacity; Armand Hammer, an American industrialist and philanthropist, bought Occidental Petroleum Company in 1956 when the company was near bankruptcy, and turned it into a billion dollar conglomerate. He made his fortune supporting the Soviet Union to fight against starvation in the 1920s, 1930s and 1940s. Because of his concerns for solving critical social issues in Russia he was granted commercial concessions and the support of Soviet leader Vladimir Lenin (Wikipedia, 2007). The lesson for managers is that when doing business internationally, especially in developing countries, it should not just be about focusing on the core business of the firm (that is the economic oriented focus), but also on focusing on the environment and social aspects of the host country which could represent better opportunities for the firm in the long term. During the cold war era, Armand Hammer was the only American who could do business in the Soviet Union. Similarly, firms operating in developing countries have many opportunities yet to explore that could lead them to gain competitive advantage.

Also valuable to the firm is the process of adaptation to local markets that could challenge the companies' mindset or their dominant business model. For example, energy companies headquartered in the developed North may have their assumptions challenged with respect to renewable energy technologies such as wind energy when faced with regions in developing countries where there is no established electricity grid structure. When these companies enter into another country they will have an advantage over other developed country companies because they have already had their dominant business model challenged and have adapted. Multinational corporations gain competitive advantage by developing knowledge-based capabilities which may

be strategically shared with partners in emerging economies. In addition companies who have their business model challenged in one country and learned to adapt are better positioned to innovatively seize new opportunities not only in other emerging economies but also in their home economies.

TECHNOLOGICAL INTERDEPENDENCE

Technological interdependence is the degree to which different parts of the organization must exchange information and materials in order to perform their required activities. There are three major types of technological interdependence:

Pooled interdependence

The type that involves the least interdependence is known as a pooled interdependence, in which units operate independently but their individual efforts are important to the success of the organization as whole. For example, if the local branch of the bank performs poorly and loses customers, its problems will have negative effect on the health of the bank as a whole.

Sequential interdependence

With sequential interdependence, one unit must complete its work before the next unit in the sequence can begin work. For example, a strike over a local issue at one plant of General Motors frequently causes workers at other plants to be laid off temporarily.

Reciprocal interdependence

The most complex situation is reciprocal interdependence, in which one unit's outputs become inputs to other unit and vice versa. When an airplane lands, the flight crew turns the plane over to the maintenance crew. After refueling the plane, and performing other necessary activities, the maintenance crew releases the plane back to the flight crew so that the plane can continue its journey. Reciprocal interdependence is likely to require greater efforts at horizontal coordination than do the other two types of technological interdependence.

Thus managers need to give some thought to technological interdependence, when developing organization structure.

STRATEGY AND INNOVATION

Despite massive investments of management time and money, innovation remains a frustrating pursuit in many companies. Innovation initiatives frequently fail, and successful

innovators have a hard time sustaining their performance—as Polaroid, Nokia, Sun Microsystems, Yahoo, Hewlett-Packard, and countless others have found. Why is it so hard to build and maintain the capacity to innovate? The reasons go much deeper than the commonly cited cause: a failure to execute. The problem with innovation improvement efforts is rooted in the lack of an *innovation strategy.*

A strategy is nothing more than a commitment to a set of coherent, mutually reinforcing policies or behaviors aimed at achieving a specific competitive goal. Good strategies promote alignment among diverse groups within an organization, clarify objectives and priorities, and help focus efforts around them. Companies regularly define their overall business strategy (their scope and positioning) and specify how various functions—such as marketing, operations, finance, and R&D—will support it. But during my more than two decades studying and consulting for companies in a broad range of industries, I have found that firms rarely articulate strategies to align their innovation efforts with their business strategies.

Without an innovation strategy, innovation improvement efforts can easily become a grab bag of much-touted best practices: dividing R&D into decentralized autonomous teams, spawning internal entrepreneurial ventures, setting up corporate venture-capital arms, pursuing external alliances, embracing open innovation and crowdsourcing, collaborating with customers, and implementing rapid prototyping, to name just a few. There is nothing wrong with any of those practices per se. The problem is that an organization's capacity for innovation stems from an *innovation system:* a coherent set of interdependent processes and structures that dictates how the company searches for novel problems and solutions, synthesizes ideas into a business concept and product designs, and selects which projects get funded. Individual best practices involve trade-offs. And adopting a specific practice generally requires a host of complementary changes to the rest of the organization's innovation system. A company without an innovation strategy won't be able to make trade-off decisions and choose all the elements of the innovation system.

Aping someone else's system is not the answer. There is no one system that fits all companies equally well or works under all circumstances. There is nothing wrong, of course, with learning from others, but it is a mistake to believe that what works for, say, Apple (today's favorite innovator) is going to work for your organization. An explicit innovation strategy helps you design a system to match your specific competitive needs.

Finally, without an innovation strategy, different parts of an organization can easily wind up pursuing conflicting priorities—even if there's a clear business strategy. Sales representatives hear daily about the pressing needs of the biggest customers. Marketing may see opportunities to leverage the brand through complementary products or to expand market share through new

distribution channels. Business unit heads are focused on their target markets and their particular P&L pressures. R&D scientists and engineers tend to see opportunities in new technologies. Diverse perspectives are critical to successful innovation. But without a strategy to integrate and align those perspectives around common priorities, the power of diversity is blunted or, worse, becomes self-defeating.

A good example of how a tight connection between business strategy and innovation can drive long-term innovation leadership is found in Corning, a leading manufacturer of specialty components used in electronic displays, telecommunications systems, environmental products, and life sciences instruments. (Disclosure: I have consulted for Corning, but the information in this article comes from

Corning's Breakthrough Innovations

During its more than 160 years, Corning has leveraged its expertise in glass and materials science to produce a long list of highly successful products, including the following.

1800s

1879 Glass envelope for Thomas Edison's lightbulbs

1900s

1912 Glass for railroad lanterns that could withstand extreme temperature changes

1915 Heat-resistant Pyrex glass for cookware and laboratory equipment

1926 Ribbon machine for the mass production of lightbulbs

1932 High-purity fused silica—the foundation of other Corning innovations, such as telescope mirrors and optical fiber

1934 Silicones, a class of materials that are a cross between glass and plastic

1947 Process for mass-producing television picture tubes

1952 Heat- and break-resistant glass-ceramic material used in Corning Ware cookware and missile nose cones

1964 Fusion overflow process for producing flat glass

1970 Low-loss optical fiber used in telecommunications networks

1972 Cellular ceramic substrates used in automotive catalytic converters and today's diesel engines

1982 Active matrix liquid crystal display (LCD) glass for high-quality flat-panel displays

2000s

2007 Gorilla Glass—thin, lightweight glass with exceptional damage resistance for smartphones, tablets, and other consumer electronics

2012 Ultraslim, flexible, lightweight glass for consumer electronics and architectural and design applications

SOURCE CORNING; GARY P. PISANO
FROM "YOU NEED AN INNOVATION STRATEGY," JUNE 2015

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the 2008 HBS case study "Corning: 156 Years of Innovation," by H. Kent Bowen and Courtney Purrington.) Over its more than 160 years Corning has repeatedly transformed its business and grown new markets through breakthrough innovations. When judged against current best practices, Corning's approach seems out of date. The company is one of the few with a centralized R&D laboratory (Sullivan Park, in rural upstate New York). It invests a lot in basic research, a practice that many companies gave up long ago. And it invests heavily in manufacturing technology and plants and continues to maintain a significant manufacturing footprint in the United States, bucking the trend of wholesale outsourcing and offshoring of production.

Yet when viewed through a strategic lens, Corning's approach to innovation makes perfect sense. The company's business strategy focuses on selling "keystone components" that significantly improve the performance of customers' complex system products. Executing this strategy requires Corning to be at the leading edge of glass and materials science so that it can solve exceptionally challenging problems for customers and discover new applications for its technologies. That requires heavy

investments in long-term research. By centralizing R&D, Corning ensures that researchers from the diverse disciplinary backgrounds underlying its core technologies can collaborate. Sullivan Park has become a repository of accumulated expertise in the application of materials science to industrial problems. Because novel materials often require complementary process innovations, heavy investments in manufacturing and technology are a must. And by keeping a domestic manufacturing footprint, the company is able to smooth the transfer of new technologies from R&D to manufacturing and scale up production.

Corning's strategy is not for everyone. Long-term investments in research are risky: The telecommunications bust in the late 1990s devastated Corning's optical fiber business. But Corning shows the importance of a clearly articulated innovation strategy—one that's closely linked to a company's business strategy and core value proposition. Without such a strategy, most initiatives aimed at boosting a firm's capacity to innovate are doomed to fail.

The Innovation Landscape Map

When creating an innovation strategy, companies have a choice about how much to focus on technological innovation and how much to invest in business model innovation. This matrix, which considers how a potential innovation fits with a company's existing business model and technical capabilities, can assist with that decision.

	LEVERAGES **EXISTING** TECHNICAL COMPETENCES	REQUIRES **NEW** TECHNICAL COMPETENCES
REQUIRES **NEW** BUSINESS MODEL	**DISRUPTIVE** • Open source software FOR SOFTWARE COMPANIES • Video on demand FOR DVD RENTAL SERVICES • Ride-sharing services FOR TAXI AND LIMO COMPANIES	**ARCHITECTURAL** • Personalized medicine FOR PHARMACEUTICAL COMPANIES • Digital imaging FOR POLAROID AND KODAK • Internet search FOR NEWSPAPERS
LEVERAGES **EXISTING** BUSINESS MODEL	**ROUTINE** • A next-generation 3 series FOR BMW • A new index fund FOR VANGUARD • A new 3-D animated film FOR PIXAR	**RADICAL** • Biotechnology FOR PHARMACEUTICAL COMPANIES • Jet engines FOR AIRCRAFT MANUFACTURERS • Fiber-optic cable FOR TELECOMMUNICATIONS COMPANIES

SOURCE CORNING; GARY P. PISANO
FROM "YOU NEED AN INNOVATION STRATEGY," JUNE 2015

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Connecting Innovation to Strategy

About 10 years ago Bristol-Myers Squibb (BMS), as part of a broad strategic repositioning, decided to emphasize cancer as a key part of its pharmaceutical business. Recognizing that biotechnology-derived drugs such as monoclonal antibodies were likely to be a fruitful approach to combating cancer, BMS decided to shift its repertoire of technological capabilities from its traditional organic-chemistry base toward biotechnology. The new business strategy (emphasizing the cancer market) required a new innovation strategy (shifting technological capabilities toward biologics). (I have consulted for BMS, but the information in this example comes from public sources.)

Like the creation of any good strategy, the process of developing an innovation strategy should start with a clear understanding and articulation of specific objectives related to helping the company achieve a sustainable competitive advantage. This requires going beyond all-too-common generalities, such as “We must innovate to grow,” “We innovate to create value,” or “We need to innovate to stay ahead of competitors.” Those are not strategies. They provide no sense of the types of innovation that might matter (and those that won’t). Rather, a robust innovation strategy should answer the following questions:

How will innovation create value for potential customers?

Unless innovation induces potential customers to pay more, saves them money, or provides some larger societal benefit like improved health or cleaner water, it is not creating value. Of course, innovation can create value in many ways. It might make a product perform better or make it easier or more convenient to use, more reliable, more durable, cheaper, and so on. Choosing what kind of value your innovation will create and then sticking to that is critical, because the capabilities required for each are quite different and take time to accumulate. For instance, Bell Labs created many diverse breakthrough innovations over a half century: the telephone exchange switcher, the photovoltaic cell, the transistor, satellite communications, the laser, mobile telephony, and the operating system Unix, to name just a few. But research at Bell Labs was guided by the strategy of improving and developing the capabilities and reliability of the phone network. The solid-state research program—which ultimately led to the invention of the transistor—was motivated by the need to lay the scientific foundation for developing newer, more reliable components for the communications system. Research on satellite communications was motivated in part by the limited bandwidth and the reliability risks of undersea cables. Apple consistently focuses its innovation efforts on making its products easier to use than competitors’ and providing a seamless experience across its expanding family of devices and services. Hence

its emphasis on integrated hardware-software development, proprietary operating systems, and design makes total sense.

How will the company capture a share of the value its innovations generate?

Value-creating innovations attract imitators as quickly as they attract customers. Rarely is intellectual property alone sufficient to block these rivals. Consider how many tablet computers appeared after the success of Apple's iPad. As imitators enter the market, they create price pressures that can reduce the value that the original innovator captures. Moreover, if the suppliers, distributors, and other companies required to deliver an innovation are dominant enough, they may have sufficient bargaining power to capture most of the value from an innovation. Think about how most personal computer manufacturers were largely at the mercy of Intel and Microsoft.

Companies must think through what complementary assets, capabilities, products, or services could prevent customers from defecting to rivals and keep their own position in the ecosystem strong. Apple designs complementarities between its devices and services so that an iPhone owner finds it attractive to use an iPad rather than a rival's tablet. And by controlling the operating system, Apple makes itself an indispensable player in the digital ecosystem. Corning's customer-partnering strategy helps defend the company's innovations against imitators: Once the keystone components are designed into a customer's system, the customer will incur switching costs if it defects to another supplier.

One of the best ways to preserve bargaining power in an ecosystem and blunt imitators is to continue to invest in innovation. I recently visited a furniture company in northern Italy that supplies several of the largest retailers in the world from its factories in its home region. Depending on a few global retailers for distribution is risky from a value-capture perspective. Because these megaretailers have access to dozens of other suppliers around the world, many of them in low-cost countries, and because furniture designs are not easily protected through patents, there is no guarantee of continued business. The company has managed to thrive, however, by investing both in new designs, which help it win business early in the product life cycle, and in sophisticated process technologies, which allow it to defend against rivals from low-cost countries as products mature.

What types of innovations will allow the company to create and capture value, and what resources should each type receive?

Certainly, technological innovation is a huge creator of economic value and a driver of competitive advantage. But some important innovations may have little to do with new

technology. In the past couple of decades, we have seen a plethora of companies (Netflix, Amazon, LinkedIn, Uber) master the art of business model innovation. Thus, in thinking about innovation opportunities, companies have a choice about how much of their efforts to focus on technological innovation and how much to invest in business model innovation.

A helpful way to think about this is depicted in the exhibit “The Innovation Landscape Map.” The map, based on my research and that of scholars such as William Abernathy, Kim Clark, Clayton Christensen, Rebecca Henderson, and Michael Tushman, characterizes innovation along two dimensions: the degree to which it involves a change in technology and the degree to which it involves a change in business model. Although each dimension exists on a continuum, together they suggest four quadrants, or categories, of innovation.

Routine innovation builds on a company’s existing technological competences and fits with its existing business model—and hence its customer base. An example is Intel’s launching ever-more-powerful microprocessors, which has allowed the company to maintain high margins and has fueled growth for decades. Other examples include new versions of Microsoft Windows and the Apple iPhone.

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Disruptive innovation, a category named by my Harvard Business School colleague Clay Christensen, requires a new business model but not necessarily a technological breakthrough. For that reason, it also challenges, or disrupts, the business models of other companies. For example, Google’s Android operating system for mobile devices potentially disrupts companies like Apple and Microsoft, not because of any large technical difference but because of its business model: Android is given away free; the operating systems of Apple and Microsoft are not.

Radical innovation is the polar opposite of disruptive innovation. The challenge here is purely technological. The emergence of genetic engineering and biotechnology in the 1970s and 1980s as an approach to drug discovery is an example. Established pharmaceutical companies with decades of experience in chemically synthesized drugs faced a major hurdle in building competences in molecular biology. But drugs derived from biotechnology were a good fit with the companies’ business models, which called for heavy investment in R&D, funded by a few high-margin products.

Architectural innovation combines technological and business model disruptions. An example is digital photography. For companies such as Kodak and Polaroid, entering the digital world meant mastering completely new competences in solid-state electronics, camera design, software, and display technology. It also meant finding a way to earn profits from cameras rather than from “disposables” (film, paper, processing chemicals, and services). As one might imagine, architectural innovations are the most challenging for incumbents to pursue.

A company’s innovation strategy should specify how the different types of innovation fit into the business strategy and the resources that should be allocated to each. In much of the writing on innovation today, radical, disruptive, and architectural innovations are viewed as the keys to growth, and routine innovation is denigrated as myopic at best and suicidal at worst. That line of thinking is simplistic.

In fact, the vast majority of profits are created through routine innovation. Since Intel launched its last major disruptive innovation (the i386 chip), in 1985, it has earned more than $200 billion in operating income, most of which has come from next-generation microprocessors. Microsoft is often criticized for milking its existing technologies rather than introducing true disruptions. But this strategy has generated $303 billion in operating income since the introduction of Windows NT, in 1993 (and $258 billion since the introduction of the Xbox, in 2001). Apple’s last major breakthrough (as of this writing), the iPad, was launched in 2010. Since then Apple has launched a steady stream of upgrades to its core platforms (Mac, iPhone, and iPad), generating an eye-popping $190 billion in operating income.

The point here is not that companies should focus solely on routine innovation. Rather, it is that there is not one preferred type. In fact, as the examples above suggest, different kinds of innovation can become complements, rather than substitutes, over time. Intel, Microsoft, and Apple would not have had the opportunity to garner massive profits from routine innovations had they not laid the foundations with various breakthroughs. Conversely, a company that introduces a disruptive innovation and cannot follow up with a stream of improvements will not hold new entrants at bay for long.

Executives often ask me, “What proportion of resources should be directed to each type of innovation?” Unfortunately, there is no magic formula. As with any strategic question, the answer will be company specific and contingent on factors such as the rate of technological change, the magnitude of the technological opportunity, the intensity of competition, the rate of growth in core markets, the degree to which customer needs are being met, and the company’s strengths. Businesses in markets where the core technology is evolving rapidly (like pharmaceuticals, media, and communications) will have to be much more keenly oriented toward

radical technological innovation—both its opportunities and its threats. A company whose core business is maturing may have to seek opportunities through business model innovations and radical technological breakthroughs. But a company whose platforms are growing rapidly would certainly want to focus most of its resources on building and extending them.

In thinking strategically about the four types of innovation, then, the question is one of balance and mix. Google is certainly experiencing rapid growth through routine innovations in its advertising business, but it is also exploring opportunities for radical and architectural innovations, such as a driverless car, at its Google X facility. Apple is not resting on its iPhone laurels as it explores wearable devices and payment systems. And while incumbent automobile companies still make the vast majority of their revenue and profits from traditional fuel-powered vehicles, most have introduced alternative-energy vehicles (hybrid and all-electric) and have serious R&D efforts in advanced alternatives like hydrogen-fuel-cell motors.

Overcoming the Prevailing Winds

I liken routine innovation to a sports team's home-field advantage: It's where companies play to their strengths. Without an explicit strategy indicating otherwise, a number of organizational forces will tend to drive innovation toward the home field.

Some years ago I worked with a contact lens company whose leaders decided that it needed to focus less on routine innovations, such as adding color tints and modifying lens design, and be more aggressive in pursuing new materials that could dramatically improve visual acuity and comfort. After a few years, however, little progress had been made. A review of the R&D portfolio at a senior management meeting revealed that most of the company's R&D expenditures were going to incremental refinements of existing products (demanded by marketing to stave off mounting short-term losses in share) and to process improvements (demanded by manufacturing to reduce costs, which was, in turn, demanded by finance to preserve margins as prices fell). Even worse, when R&D finally created a high-performing lens based on a new material, manufacturing could not produce it consistently at high volume, because it had not invested in the requisite capabilities. Despite a strategic intent to venture into new territory, the company was trapped on its home field.

The root of the problem was that business units and functions had continued to make resource allocation decisions, and each favored the projects it saw as the most pressing. Only after senior management created explicit targets for different types of innovations—and allocated a specific percentage of resources to radical innovation projects—did the firm begin to make progress in developing new offerings

TECHNOLOGY ACCUMULATION

"MNC in manufacturing emerged historically and became successful through the generation and cultivation of innovative ownership advantages. The accumulation of technology and innovation gives the cumulative competitive advantage, whether the innovation is in products or processes and whether it cumulates in the same products/ process or is diversified."

Successful Innovators tend to invest in several countries. As they do so their investments generates spillover effects to industry. The centers then become the location of several innovating companies and this generates external economies of agglomeration. There are cumulative effects at the macro and micro level. The accumulation of technology leads to higher productivity and therefore high growth in income per capita. This generates high levels of demand, thus attracting new levels of investment. While we have leader firms in innovation, we cannot equally talk of leader countries.

Innovations are almost always located in the home country of the parent, an usually close to the site of corporate technology headquarters. International investment lead by technology leaders by a means in which they increase their share of world markets and world production.

2.2 Technological accumulation and firms' internationalisation

The theoretical core of the approach The technological accumulation approach towards firms' internationalisation builds upon the dynamic and evolutionary perspective of the capability based view of the firm described above. In addition, to the existing theory it provides a link between the growth of the firm and the changing international location of production. Cantwell (1989) sets out to explain why – within a given industry – some firms become more successful at international activities compared with rival firms. Thus, he is not concerned with a theoretical explanation of the existence but the growth of the multinational firm. The technological accumulation approach addresses the question of why it is that technology is developed in international networks, rather than a series of separately owned plants. It is a theory of international production and changing technology of production rather than exchange (Cantwell 1989). Capital and technological accumulation Cantwell (1989) traces back the theoretical roots of his analysis to the approach of the classical school of political economy (most notably Adam Smith, David Ricardo and Karl Marx). According to them, the mainspring of a capitalist economy is the process of capital accumulation. Cantwell (1989) holds that in the case of expansion of manufacturing industry, which has been central to capitalist development since the time of industrial revolution, capital accumulation has been bound up with technological accumulation. Cantwell (1989) refers to the term 'technological accumulation' as originally

coined by Pavitt (1987). It encapsulates the idea that the development of technology within the firm is a cumulative process. That is, the creation of new technology within is to be understood as a gradual process of continual adjustment and refinement as new productive methods are tested and adapted in the light of experience. In any firm there is a continual interaction between the creation of technology and its use in production. For this reason a group of firms in a given industry are likely to have similar lines of technological development, yet the technological path of each is to some degree unique and differentiated. Cantwell (1989) argues that the notion of technological accumulation is consistent with the ideas of Rosenberg (1976, 1982), Usher (1929) and the earlier work of Marx on technological change through systemic adaptation. Similarly, he draws parallels to the work of Atkinson and Stiglitz (1969), Nelson and Winter (1977, 1982) and Stiglitz (1987) on 'localised' technological change in the context of previous technological evolution and learning experience of the firm. 19 Cantwell (1989) reverts to the classical terminology in speaking of technological accumulation and capital accumulation, rather than simply innovation and investment to emphasise that they both continues and interlinked processes, and not just a series of discrete actions. Cantwell (1989) considers technology to be both embodied in new items of capital equipment, and disembodied in improvements in the way it is used. Hence, technology is defined with reference to the production process as a whole, and encompasses productivity improvements that are due to both scientific and organisational factors. This entails a broad definition of technological innovation to cover everything in the production process itself that over time raises productivity. Thus, it does not include productivity growth that is due to changes in the scale of output or the size of the plant, using a given technology at a point in time. The gradual accumulation of technology generates dynamic rather than static economies of scale, associated with the changing conditions in production. Technology of this definition encompasses organisational capacity, managerial skills, as well as R&D, but excludes the advertising part of marketing. The accumulation of technology involves the gradual building of largely intangible assets, and is reflected in the skills of the workforce and the design of capital equipment. Cantwell and Fai (1999) hold that while on the surface innovation is commonly observed through the market phenomena of the emergence of new products and differentiation of existing products, the underlying capacity to change what markets receive is provided by the corporate capability to create and refine to a viable point new products and processes, which rests on the cumulative generation of technological competence in firms. Learning in production creates the capability base of firms that is better captured by diverse fields of technological expertise of a company than it is by the firm's product area (ibid). Within this perspective, the accumulation of technology and innovation gives cumulative advantage, whether the innovation

is in products or processes and whether it accumulates in the same product/processes or is diversified (Cantwell and Piscitello 2000). The acquisition of new skills, and the generation of new technological capacity, partially embodied in new plant and equipment is a condition for every firm in an oligopolistic industry to maintain or increase profits (Cantwell 1989, 1995, 2000). Technological accumulation and firm location For Cantwell and Piscitello (2000) in the capability based view of the firm the major issue is not so much how the firm exploits a given capability, but rather how it establishes a spatially and 20 sectorally diffuse system for the creation of new competence (Cantwell and Piscitello 2000). They argue that the firm is able to benefit from the dynamic economies of scope that derive from the technological complementarities between related fields of activity, and the complementarities between related paths of innovations or corporate learning in spatially distinct settings (ibid). In the technological accumulation approach 'the use of technology in new environments feeds back into fresh adaptation and new innovation depending on the state of local scientific and technological capability' (Cantwell 1989, p. 9). When production is located in an area that itself is a centre for innovation in the industry concerned, the firm may gain access to research facilities which allow it to extend technology creation in untried directions (ibid). International expansion of production brings gains to the MNE as experience from adapting its technology under new conditions feeds back into the technological development path of the MNE as a whole. Given a sufficient level of technological strength, firms are keen to produce in locations from which there major international rivals emanated which offers them access to complementary innovation (Cantwell 2000). The notion that the geographical dispersion of technological development enhances innovation in the network of the MNE as a whole is founded on the belief that innovation is location specific as well as firm specific (Cantwell 1989, 1995). Internal economies of scale in innovation activity can be achieved across the multinational corporation due to the transfer of knowledge and innovation from affiliate to affiliate and from location to location rather than just one country. Cantwell (1989, 1995) argues that successful innovators tend to invest in innovation activities in several sub-national centres across countries. As they do so, their investment generates spillover effects to the location and the industry, thus encouraging more investment and innovation activities by other firms. Each innovating firm brings external benefits to the locality in which it invests. Conversely, investors benefit from a favourable technological environment that develops in the locality. Agglomeration economies are generated and they further strengthen the location and the ownership specific advantages of firms operating within them (Cantwell and Iammarino 1998, 2001, 2003). Thus, locational advantages are considered as endogenously created by the innovation and location strategies of firms combined with spillover effects of their

activities (Cantwell 1989, 1995). What emerges is a complex 'dynamic interaction of the ownership advantage of groups of firms and the locational advantages of the sites in which they produce' (Cantwell 1989, p. 207).

Home or overseas R&D

To enhance their competitiveness, multinational enterprises (MNEs) rely on multiple geographical sources of knowledge by tapping into host location-specific, and benefit from them through reverse knowledge transfer from foreign subsidiaries to the parent. Traditionally, foreign R&D investments in those countries have been a means to adapt products or processes to local markets with little or no contribution to the knowledge home-base. Recent trends suggest a more strategic role of some EM (Emerging Markets) in attracting R&D investments as a result of the emergence of talent pools and adequate expertise as well as of the technological upgrading in mature technologies of these countries. This new trend of R&D internationalisation from DM (Domestic Markets) to EM poses a number of challenges to international business (IB) research and calls for an analysis of the opportunities EM may offer to or the threat they may represent for DM location advantages (LAs). IB scholars converge on the idea that both home and host environments contribute to the firm's international competitiveness as this is strictly connected to the institutional set-up and spatially-bounded knowledge-flows of the external. In particular, Rugman and Verbeke's (1993) double diamond model explains MNE's international competitiveness as a direct result of both home and host LAs.

LAs are the benefits associated with the localisation of certain activities in particular countries or regions. Extant IB research converges on the idea that home LAs are a major source of international competitiveness. Drawing on the OLI paradigm (Dunning 1977), Rugman and Verbeke's (1993) double diamond model proposes that foreign input markets for valuable resources and/or foreign output markets for delivery of end products do contribute to international competitiveness. The double diamond model moves from the critique to Porter's (1990) diamond model and traditional theories of MNEs which contend that international competitiveness is solely grounded in the home country (Vernon 1966; Hymer 1990). This view was primarily motivated by the dominating FDI pattern whereby non-location-bound advantages were created in the home country and subsequently transferred to host country subsidiaries serving as a base for MNE's international competitiveness. However, in the last decades the significance of localised accumulated specialised resource pools and positive externalities for firm competitiveness has drawn attention to location-bound assets. These are assets that benefit a company only in a particular location (or set of locations) as they "cannot easily be transferred as

an intermediate good and require significance adaptation in order to be used in other locations". To account for this, the double diamond model explains international competitiveness in terms of both home and host location-bound assets. The implicit view of the MNE underlying this argument is that of an inter-organization network including both headquarters and different subsidiaries which are embedded in an external network of customers, suppliers, regulators and competitors with which they must. In this multi-hub 'integrated network' each unit contributes to the creation of new knowledge by relying on the knowledge available in its external environment. In particular, headquarters embeddedness at home enables to build the home base of the MNE international competitiveness by drawing on the home country location-bound assets. Foreign subsidiaries embeddedness in host locations enables the entire network to benefit from host country location-bound assets since the subsidiary assimilates and applies new external knowledge, and then transfers it within the MNE network.

With respect to R&D internationalisation, it has been argued that foreign R&D investments are motivated by the need to build upon and extend the extant core competences of the MNE or to access complementary assets that are lacking at home. The implications of this reasoning are that both host and home locations of R&D activity can potentially enhance international competitiveness as in the double diamond framework. A number of studies have indeed documented that the MNE home location is an important source of valuable intangible assets and capabilities that can be exploited to prosper globally. Empirical evidence focusing on sub-national locations shows that there is a link between the technological capacities of the home region and the innovativeness of the MNEs that have their headquarters in the region. Similarly, evidence is available on the contribution of foreign R&D units to the creation of new technological competences at home through the leveraging of host-location specific knowledge assets. By means of reverse knowledge transfer foreign subsidiaries are able to transfer host country valuable knowledge to the parent company and, as a result, transform location-bound knowledge assets into ownership advantages for the whole MNE. The differentiated MNE network acts indeed as a link between home and host location being able to absorb and transfer location-bound knowledge assets from one location to another. In particular, host location-bound knowledge assets are increasingly transferred from the overseas units back to the headquarters embedded in the home environment where these assets then spill over affecting home location-bound knowledge assets.

ORGANISATIONAL ISSUES AND TECHNOLOGICAL PERFORMANCE

Political, economic, and environmental issues are increasingly becoming the remit of international business leaders as much as governments.While the global marketplace becomes more interconnected and accessible, the risks involved in doing business abroad are not to be taken lightly.

Expanding business overseas means reaching new clients or customers and potentially boosting profits. Despite all the uncertainty of 2017 and the challenges that have yet to reveal themselves, there are some guidelines for conducting business on a global scale that you should always consider before leaping into new international operations. Following are the advice on how to tackle the 11 biggest challenges for international business:

1. International company structure
2. Foreign laws and regulations
3. International accounting
4. Cost calculation and global pricing strategy
5. Universal payment methods
6. Currency rates
7. Choosing the right global shipment methods
8. Communication difficulties and cultural differences
9. Political risks
10. Supply chain complexity and risks of labor exploitation
11. Worldwide environmental issues

- **International company structure**

If your aim is to be competitive globally, you must have a team in place that's up for the challenge. One fundamental consideration is the structure of your organization and the location of your teams.For instance, will your company be run from one central headquarters? Or will you have offices and representatives "on the ground" in key markets abroad? If so, how will these teams be organized, what autonomy will they have, and how will they coordinate working across time zones? If not, will you consider hiring local market experts who understand the culture of your target markets, but will work centrally?

Coca-Cola offers one example of effective multinational business structure. The company is organized into continental groups, each overseen by a President. The central Presidents manage Presidents of smaller, country-based or regional subdivisions. Despite its diverse global presence, the Coca-Cola brand and product is controlled centrally and consistent around the world.

While Coca-Cola is a vast international brand, the structure of your business and the number, nationality, and level of expertise of your team will vary depending on your industry, product, and the size of your business.

- **Foreign laws and regulations**

Along with getting your company structure in place, gaining a comprehensive understanding of the local laws and regulationsgoverning your target markets is key. From tax implications through to trading laws, navigating legal requirements is a central function for any successful international business. Eligibility to trade is a significant consideration, as are potential tariffs and the legal costs associated with entering new markets.

- Airbnb ran into trouble in 2014, with a crackdown on advertised rental properties falling outside local housing and tourism regulations. The company was forced to pay a €30,000 fine for a breach of local tourism laws in Barcelona.
- It's important to note that employment and labor requirements also differ by country. For instance, European countries stipulate that a minimum of 14-weeks maternity leave be offered to employees, while on the other hand, there is no such requirement for U.S. employers. With the complexity involved in foreign trade and employment laws, investing in knowledgeable and experienced corporate counsel can prove invaluable.
- Beyond abiding by official laws, engaging in international business often requires following other unwritten cultural guidelines. This can prove especially challenging in emerging markets with ill-defined regulations or potential corruption. In response, companies doing business in the United States must abide by the Foreign Corrupt Practices Act, which aims at eliminating bribery and unethical practices in international business. A good rule of thumb is to beware of engaging in any questionable activities, which might be legal but could have future reputational repercussions.
- **International accounting**

Of the main legal areas to consider when it comes to doing international business, tax compliance is perhaps the most crucial. Accounting can present a challenge to multinational businesses who may be liable for corporation tax abroad. Different tax systems, rates, and compliance requirements can make the accounting function of a multinational organization significantly challenging.

Accounting strategy is key to maximizing revenue, and the location where your business is registered can impact your tax liability. Mitigating the risk of multiple layers of taxation makes good business sense for any organization trading abroad. Being aware of tax treaties between

countries where your business is trading will help to ensure you're not paying double taxes unnecessarily.

A focus on tax efficiency is often the aim of international accounting efforts. In the European Union, companies may benefit from the Common Consolidated Corporate Tax Base proposal, whereby companies with operations around the EU can limit tax liability to one corporate center. Tax consolidation is a feature of several multinationals' decision to be headquartered in Dublin, as Ireland is known for its "business-friendly" corporate tax policy. Well-known companies with operational headquarters in the Republic of Ireland include Google, Facebook, and Intel.

- **Cost calculation and global pricing strategy**

Setting the price for your products and services can present challenges when doing business overseas and should be another major consideration of your strategy. You must consider costs to remain competitive, while still ensuring profit. Researching the prices of direct, local-market competitors can give you a benchmark, however, it remains essential to ensure the math still works in your favor. For instance, the cost of production and shipping, labor, marketing, and distribution, as well as your margin, must be a taken into account for your business to be viable.

Pricing can also come down to how you choose to position your brand — should the cost of your product reflect luxury status? Or will low prices help you to penetrate a new market? Swedish furniture giant Ikea, known in Europe for its low-cost value, struggled initially in China due to local competitor costs of labor and production being much cheaper. By relocating production for the Chinese market and using more locally sourced materials, the company was able to successfully cut prices to better reflect its brand and boost sales among target consumers.

Wherever you're looking to launch your product or service, here are four useful strategies to help you find the right price:

- **Universal payment methods**

The proliferation of international e-commerce websites has made selling goods overseas easier and more affordable for businesses and consumers. However, payment methods that are commonly accepted in your home market might be unavailable abroad. Determining acceptable payment methods and ensuring secure processing must be a central consideration for businesses who seeks to trade internationally.

Accepting well-known global payment methods through companies like Worldpay, as well as accepting local payment methods, such as JCB in Asia or Yandex Money in Russia, can be a good option for large international businesses. Accepting wire transfers, PayPal payments, and Bitcoin, are other possibilities, with Bitcoin users benefiting from no bank or credit card transaction fees. Despite the risk of fluctuating value, the lack of fees is one of the reasons

a number of online companies, including WordPress, the Apple App Store, Expedia, and a number of Etsy sellers accept Bitcoin.

- **Currency rates**

While price setting and payment methods are major considerations, currency rate fluctuation is one of the most challenging international business problems to navigate. Monitoring exchange rates must therefore be a central part of the strategy for all international businesses. However, global economic volatility can make forecasting profit especially difficult, particularly when rates fluctuate at unpredictable levels.

Major fluctuations can seriously impact the balance of business expenses and profit. For instance, if your company is paying suppliers and production costs in U.S. dollars, but selling in markets with a weaker or more unpredictable currency, your company could end up with a much smaller margin — or even a loss. One way to protect yourself against large fluctuations in currency is to pay suppliers and production costs in the same currency as the one you're selling in. This may mean switching to more local production where possible in order to better balance your outgoings and sales revenue.

Another option for mitigating the risk of unpredictable currency rates can be setting up a forward contract and agreeing a price in advance for future sales. Of course, this potentially means missing out on greater profit should rates shift in your favor. However, it can protect your sales from the risk presented by unstable currency.

Learn more about six key factors that can influence currency exchange rates:

- **Choosing the right global shipment methods**

The potential of online sales presents a huge international business opportunity for retailers in the 21st century, but finding reliable, fast, and cost-effective shipment and distribution methods can be a difficult balance in some markets. Depending on the volume and destination of your shipments, will you send by land, sea, air, or a combination? Your choice of shipping method can be a major influence on your revenue and may be a limiting factor to the products you can viably sell overseas.

Other considerations to address according to your company's products and your target markets include customs fees, the need and cost of storage, and local methods of distribution. There are also country-specific regulations and shipping requirements to take into account. For a quick check of costs and compliance, UPS International has created an online tool called TradeAbility to help businesses and individuals manage the movement of good overseas.

- **Communication difficulties and cultural differences**

Good communication is at the heart of effective international business strategy. However, communicating across cultures can be a very real challenge. Effective communication with colleagues, clients, and customers abroad is essential for success in international business. And it's often more than just a language barrier you need to think about — nonverbal communication can make or break business deals too. Do your research and know how different cultural values and norms — such as shaking hands — can and should influence the way you communicate in a professional context. Being aware of acceptable business etiquette abroad, and how things like religious and cultural traditions can influence this, will help you to better navigate potential communication problems in international business.

Discover the subtle nuances of body language for different countries and nationalities you may be doing business with: cultural differences can also influence market demand for your product or service. The need your business may address at home may already be met or not exist at all overseas. Local market insight is key, and there are a number of successful brandswhose business models simply weren't viable in overseas markets. For instance, American coffee company Starbucks seriously struggled in Australia, where the demand for local, independent cafes and coffee shops vastly outweighed the appeal of the corporate giant.

Small practical considerations can also be easily overlooked, such as creating quality translations of product and marketing materials, and even ensuring your brand name works well abroad. A number of well-known companies have had to consider adapting the names of their brand or product when launching in a foreign market. The Chevrolet Nova is perhaps the most commonly cited example, where "no va" literally translates to "no go" in Spanish—not the best product name for a car. Although slumping sales figures in Latin America have proven to be an urban legend, the story of the "no go" car serves as a useful reminder of the importance of preparing well before launching your business in a new market.

- **Political risks**

An obvious risk for international business is political uncertainty and instability. Countries and emerging markets that may offer considerable opportunities for expanding global businesses may also pose challenges, which more established markets do not. Before considering expansion into a new or unknown market, a risk assessment of the economic and political landscape is critical.

Issues such as ill-defined or unstable policies and corrupt practices can be hugely problematic in emerging markets. Changes in governments can bring changes in policy, regulations, and interest rates that can prove damaging to foreign business and investment.

A growing trend towards economic nationalism also makes the current global political landscape potentially hostile towards international businesses. For instance, companies like Facebook are banned in China, partially in preference for national social networks and also due to government regulation over internet content. Monitoring political developments and planning accordingly can mitigate political risks of doing business abroad.

- **Supply chain complexity and risks of labor exploitation**

When it comes to sourcing products and services from overseas, managing suppliers and supply chains can also be a tricky process. Unfortunately, the length and complexity of supply chains increases the chance of working with suppliers who have unethical — and even illegal — business practices. Of growing concern is the risk in international business of forced labor and worker exploitation.

In October 2015, the UK passed the Modern Slavery Act in response to this often-hidden human rights violation. Recent research led by a partnership between Hult International Business School and the Ethical Trading Initiative revealed that an astonishing 77% of businesses believe that modern slavery exists at some point in their supply chains.

To raise awareness and help local and international businesses respond more effectively to this issue, their published research report presents case studies of businesses who have implemented practices at the leading edge of the fight against modern slavery.

- **Worldwide environmental issues**

As the environmental risks and effects of climate change are becoming better understood, sustainability is high on the agenda of many major global corporations. Recent international legislations and proposals, such as the UN's Sustainable Development Goals, have put environmental issues at the forefront of international business development. The Ashridge Centre for Business and Sustainability at Hult researches innovative ways that organizations can develop and implement more environmentally sustainable business models.

On a practical level, if you're considering expanding your business overseas, it's important to be aware of the country-specific environmental regulations and issues associated with your industry. Some key considerations include how your production methods might impact the local environment through waste and pollution.Beyond a legal or ethical incentive to be more eco-friendly, establishing environmentally conscious business practices can attract new, forward-thinking consumers to your company. With a number of brands such as Dell, Renault, and MUD

Jeans leading a shift towards the circular economy, there is an opportunity and demand for changing production methods and consumer behavior to establish a more sustainable future for the environment and society as a whole.

INTERNATIONAL FINANCE

Global economy – A Historical perspective

The process of globalization is not a new phenomenon. Some communication and trade took place among distant civilizations even in ancient times. In spite of occasional interruptions, the degree of economic globalization among different societies, around the world has generally been rising. More than a century ago, Marx and Engels rightly sensed the unprecedented efficiency of the industrial capitalism and predicted that capitalism would sweep through the entire world. Eventually capitalism spread to nearly the entire world, in a complex and sometimes fierce process. (Brookings Papers on Economic Activity, 1995). Indeed, during the past half century, the pace of economic globalization has been particularly rapid. With the exception of human migration, global economic integration today is greater than it ever has been and is likely to deepen further It was the instrument of colonial expansion rather than the economic reforms through which the global capitalism came into existent. Western European powers with their superior industrial and military powers expanded their kingdom around the world. By the 1870s, the industrial revolution and colonial expansion led to establish, a global market. Improvements in the technological progress in transportation and communication sectors, changing tastes and preferences of individuals and societies and public policies have significantly influenced the character and pace of economic globalization. Global economic system started functioning with the development of long distance communication system. Monetary standards, based on gold and silver, provided the vital support for the stability and spread of economic globalization. First World War, Great Depression of the 1930s and political upheaval created unprecedented crises to global economy. The free trade regimes of 19th century were replaced by highly protected trade, state planning, authoritarianism and limited market based economy. At the end of the Second World War, the international economic system was in a state of collapse. International markets for trade in goods, services, and financial assets were essentially nonexistent. However, there was a silver lining in the midst of black cloud. It gave an opportunity for a completely new beginning for the world economy. The new beginning started in the formation of International Monetary Fund for world level monetary standard. It also led in the establishment of various other international institutions like the International Bank for Reconstruction and Development, General Agreement on Trade and Tariff etc. Those institutions

have contributed in the integration of world economy. After the World War II, most national governments began to lower their entry barriers, to make them more permeable for world trade. The multilateral negotiations under the auspices of the General Agreement on Trade and Tariffs (GATT) stand out as the most prominent examples of reduction of barriers for trade in goods. The years between 1970 and 1990 have witnessed the most remarkable institutional harmonization and economic integration among nations in the world history. The decade of 1980, witnessed the integration of the communist world with the world economy as capitalism spread to their economies. The decade of 1980s also witnessed the practice of open economy macroeconomic policies by many developing countries. Several Latin American and Asian Countries had implemented financial reform policies or eliminated Government control of domestic interest rates, credit allocation and exchange rate etc. Countries like Korea, Malaysia, Chile, Argentina, Uruguya, Japan, Hong Kong, India and China have liberalized their economies. They have undertaken many policy decisions to reform their financial markets. One of the primary aims of financial reforms programme of these countries has been to integration of the various segments of financial markets. The decade of 1990s is generally considered as the decade of re-unification of global economy. The world reached its climax in the process of integration of developed and developing worlds. Disintegration of the Soviet Union, the emergence of market-oriented economies in Asia, the creation of a single European market, formation of new era of trade liberalization through World Trade Organization etc., are few events of 1990s which led to global financial and economic integration. Development of IT-based communication system and services have significantly contributed in the further expansion of global financial system.

Financial Globalization-The Missing Link

If there is any arena of economic activity that has become extremely global in recent decades, it is finance. The world of finance has changed markedly over the past 40 years or so. During the early part of 1970s world economy witnessed scarcity of international liquidity primarily due to gold linked fixed monetary standard. There was also a growing realization that for achieving sustained growth with stability, it would be necessary to have open trade, liberalized external capital movements and a relatively flexible domestic monetary policy. Industrialized countries and emerging market economies took steps to liberalize capital account and allow capital to move across the globe.

Simultaneously, efforts were made to remove distortions in the domestic financial sector through financial sector reform measures. With the technological improvements in electronic payments, world economy became increasingly integrated in terms of trade, investment and financial flows among countries over the past decades. There are primarily three traceable

aspects of the growth of financial markets, which have led to financial globalization. These are: (i) Significant expansion and deepening of the existing markets, (ii) Emergence of new financial markets like derivatives (iii) Development of secondary markets for many instruments. A number of developing countries, especially in Asia, that moved early on to the path of economic liberalization had experienced large capital inflows. Large capital inflows, however, carried with it risk of financial sector vulnerability. The world economy had witnessed many financial crises. The experiences helped in for setting regulatory and supervisory framework, in proper place, to ensure the safety and stability of financial systems. The costs of financial crisis falling on the sovereign governments, the notion of financial stability has come to occupy a centre-stage in public policy along with the requirement of ensuring that the efficiency of financial sector is high. The sub-prime crisis, which engulfed the world economy, has called for establishing a new international financial architecture. According to the IMF's Global Financial Stability Report (GFSR), the widening and deepening fallout from the U.S. subprime mortgage crisis would have profound implications on financial system. Financial markets remain considerably stressed because of a combination of weakening balance sheets of financial institutions, continued process of deleveraging, free fall in asset prices and difficult macroeconomic environment in the wake of debilitating global growth. The global financial system has proved to be woefully inadequate, particularly in view of the manifest structural deficiencies in meeting the regulatory requirements of the present-day international financial system of the Bretton Woods architecture. The extraordinarily synchronized nature of the sub-prime crisis makes it necessary to launch the creation of a "Global Monitoring Authority" to promote global supervision of cross-border investment, trade and banking with the fast-growing economies. Even in this era of sweeping globalization, the free play of unfettered market mechanism is fraught with great danger. The market on its own is not enough. Accordingly, the governments must play an important role in shaping the economic policies and the broader frame of reference.

Experiences from India:

India's link with international trade is as old as the Indian civilization. Prior to colonial rule, India was known as the hub of manufacturing goods and artifacts. During the colonial rule India was converted to a raw materials suppliers to rest of the World. On the eve of independence in 1947, foreign trade of India was typical of a colonial and agricultural economy. Trade relations were mainly confined to Britain and other commonwealth countries. Exports consisted chiefly of raw materials and plantation crops while imports composed of light consumer goods and other manufactures. Over the last 60 years, India's foreign trade has undergone a complete change in terms of composition and direction. The exports cover a wide range of traditional and non-

traditional items while imports consist mainly of capital goods, petroleum products, raw materials, and chemicals to meet the ever-increasing needs of a developing and diversifying economy. 1.3 Experiences from India For about 40 years (1950-90), foreign trade of India suffered from strict bureaucratic and discretionary controls. Similarly, foreign exchange transactions were tightly controlled by the government and the Reserve Bank of India. From 1947 till mid-1990s, India, with some exceptions, always faced deficit in its balance of payments, i.e. imports always exceeded exports. This was characteristic of a developing country struggling for reconstruction and modernisation of its economy. Imports galloped because of increasing requirements of capital goods, defence equipment, petroleum products, and raw materials. Exports remained relatively sluggish owing to lack of exportable surplus, competition in the international market, inflation at home, and increasing protectionist policies of the developed countries. Beginning mid-1991, the government of India introduced a series of reforms to liberalize and globalize the Indian economy. Reforms in the external sector of India were intended to integrate the Indian economy with the world economy. India's approach to openness has been cautious, contingent on achieving certain preconditions to ensure an orderly process of liberalization and ensuring macroeconomic stability. This approach has been vindicated in recent years with the growing incidence of financial crises elsewhere in the world. All the same, the policy regime in India in regard to liberalization of the foreign sector has witnessed very significant change. Over the years issues related to trade policy, export strategy, tariff policy, current account dynamics, exchange rate management, foreign exchange reserves, capital account liberalization, external debt and aid, foreign investments and WTO have been the center of discussion under the International Trade and Finance.

Openness of Indian Economy

Openness of an economy relates to its cross-border movements of goods, services and factors of production. The basic indicators of openness is the Trade -GDP ratio, which has been increasing and staying above 15 per cent which a good indicator of an open economy. The sharp increase in the inflows of foreign private capital into India in the 1990s has increased the cross-border financial integration. Another way to measure degree of financial openness is to gauge the co-movements of indices in the domestic stock market and international stock market. The ongoing process of reforms in trade, industry and finance, India's openness to crossborder trade and private capital has increased considerably since 1993-94 indicating thereby the progressive integration of domestic financial markets with the international financial markets. Table 1.1 indicates the FDI and Foreign Portfolio Investment in US$. In India, the very short-term interest rate is the inter-bank call money rate, which is an overnight rate. It is highly volatile in nature and

significantly affected by the development of foreign exchange market, which, in turn, is influenced by the international financial developments. The significant correlation between call money rates and 'three month' and 'six month' forward premia is an encouraging sign of openness of Indian Economy

INTERNATIONAL FINANCIAL TRANSACTIONS

Prior to First World War, growth in world trade was quite smooth. Gold based monetary standard provided stability to world trade. However, the collapse of gold standard, great depression of 1930s and subsequent events created a high tariff international trade regime which affected the world trade. With the establishment of IMF and GATT world trade started gaining the lost pace again. The General Agreement on Tariffs and Trade (GATT), was established after World War II in the wake of other new multilateral institutions dedicated to international economic cooperation. Seven rounds of negotiations occurred under the GATT for reducing tariffs, anti-dumping and nontariff trade barriers. The eighth GATT round — known as the Uruguay Round was the biggest negotiating mandate on trade ever agreed. The talks were going to extend the trading system into several new areas, notably trade in services and intellectual property, and to reform trade in the sensitive sectors of agriculture and textiles. The Final Act concluding the Uruguay Round and officially establishing the WTO regime was signed during the April 1994. The agreements fall into a structure with six main parts: • The Agreement Establishing the WTO • Goods and investment — the Multilateral Agreements on Trade in Goods including the GATT 1994 and the Trade Related Investment Measures • Services — the General Agreement on Trade in Services • Intellectual property — the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) • Dispute settlement (DSU) • Reviews of governments' trade policies (TPRM) The WTO agreements deal with agriculture, textiles and clothing, banking, telecommunications, government purchases, industrial standards and product safety, food sanitation regulations, intellectual property, and much more. The fundamental principle of post-WTO international trade is the foundation of the multilateral trading system. The economic case for an open trading system based on multilaterally agreed rules is simple enough and rests largely on commercial common sense. But it is also supported by evidence. Tariffs on industrial products have fallen steeply and now average less than 5% in industrial countries and 25% in developing countries. During the first 25 years after the war, world economic growth averaged about 5% per year, a high rate that was partly the result of lower trade barriers.

During the last four decades of the world economic liberalization, the World trade has not been smooth. At the same time, it is not confined to developed/industrialized countries. World economic activities were affected by international liquidity crisis, credit crunch, high crude oil prices, galloping inflation, severe drought and other natural calamities. World trade is generally affected the international business cycles. The characteristic of international business cycle has been changed a lot since 1980s. Prior of 1980s, 70% of the world output was confined to advanced economies and hence the international business cycles were affected by the performance of these economies At present, the share of the advanced economies in World output came down to 55% on purchasing power parity basis. Hence, international business cycles are no longer control by these advanced economies; rather it is the emerging market economies which are playing the leading roles in the world output and trade. In 2007, as the slowdown in economic activity in the USA and other advanced economies began, the hope was that emerging and developing economies, with their domestic economic size and strength, would help in keeping the international business cycles upward. As per the WTO forecast, the collapse in global demand brought on by the biggest economic downturn in decades will drive exports down by about 9% in volume terms in 2009, the biggest such contraction since the Second World War. Economic contraction has led to steep export declines which already posted in the early months of 2009 by major economies makes for an unusually bleak 2009 trade assessment, as per the annual assessment of global trade by the WTO. Signs of the sharp deterioration in trade were evident in the latter part of 2008 as demand sagged and production slowed. Although world trade grew by 2% in volume terms for the whole of 2008 it tapered off in the last six months and was well down on the 6% volume increase posted in 2007. The global economy is in a severe recession inflicted by a massive financial crisis and an acute loss of confidence. Wide-ranging and often unorthodox policy responses have made some progress in stabilizing financial markets but have not yet restored confidence nor arrested negative feedback between weakening activity and intense financial strains. While the rate of contraction is expected to moderate from the second quarter onward, global activity is projected to decline by 1.3 percent in 2009 as a whole before rising modestly during the course of 2010. This turnaround depends on financial authorities acting decisively to restore financial stability and fiscal and monetary policies in the world's major economies providing sustained strong support for aggregate demand.

Exchange rates, changes, forecasting, risk

Economists and investors always tend to forecast the future exchange rates so that they can depend on the predictions to derive monetary value. There are different models that are used to find out the future exchange rate of a currency.

However, as is the case with predictions, almost all of these models are full of complexities and none of these can claim to be 100% effective in deriving the exact future exchange rate.

Exchange Rate Forecasts are derived by the computation of value of vis-à-vis other foreign currencies for a definite time period. There are numerous theories to predict exchange rates, but all of them have their own limitations.

Exchange Rate Forecast: Approaches

The two most commonly used methods for forecasting exchange rates are −

- **Fundamental Approach** − This is a forecasting technique that utilizes elementary data related to a country, such as GDP, inflation rates, productivity, balance of trade, and unemployment rate. The principle is that the 'true worth' of a currency will eventually be realized at some point of time. This approach is suitable for long-term investments.
- **Technical Approach** − In this approach, the investor sentiment determines the changes in the exchange rate. It makes predictions by making a chart of the patterns. In addition, positioning surveys, moving-average trend-seeking trade rules, and Forex dealers' customer-flow data are used in this approach.

Exchange Rate Forecast: Models

Some important exchange rate forecast models are discussed below.

Purchasing Power Parity Model

The purchasing power parity (PPP) forecasting approach is based on the Law of One Price. It states that same goods in different countries should have identical prices. For example, this law argues that a chalk in Australia will have the same price as a chalk of equal dimensions in the U.S. (considering the exchange rate and excluding transaction and shipping costs). That is, there will be no arbitrage opportunity to buy cheap in one country and sell at a profit in another.

Depending on the principle, the PPP approach predicts that the exchange rate will adjust by offsetting the price changes occurring due to inflation. For example, say the prices in the U.S. are predicted to go up by 4% over the next year and the prices in Australia are going to rise by only 2%. Then, the inflation differential between America and Australia is: $4\% - 2\% = 2\%$

According to this assumption, the prices in the U.S. will rise faster in relation to prices in Australia. Therefore, the PPP approach would predict that the U.S. dollar will depreciate by about 2% to balance the prices in these two countries. So, in case the exchange rate was 90 cents U.S. per one Australian dollar, the PPP would forecast an exchange rate of −

$(1 + 0.02) \times$ (US \$0.90 per AUS \$1) = US \$0.918 per AUS \$1

So, it would now take 91.8 cents U.S. to buy one Australian dollar.

Relative Economic Strength Model

The relative economic strength model determines the direction of exchange rates by taking into consideration the strength of economic growth in different countries. The idea behind this approach is that a strong economic growth will attract more investments from foreign investors. To purchase these investments in a particular country, the investor will buy the country's currency – increasing the demand and price (appreciation) of the currency of that particular country.

Another factor bringing investors to a country is its interest rates. High interest rates will attract more investors, and the demand for that currency will increase, which would let the currency to appreciate.

Conversely, low interest rates will do the opposite and investors will shy away from investment in a particular country. The investors may even borrow that country's low-priced currency to fund other investments. This was the case when the Japanese yen interest rates were extremely low. This is commonly called carry-trade strategy.

The relative economic strength approach does not exactly forecast the future exchange rate like the PPP approach. It just tells whether a currency is going to appreciate or depreciate.

Econometric Models

It is a method that is used to forecast exchange rates by gathering all relevant factors that may affect a certain currency. It connects all these factors to forecast the exchange rate. The factors are normally from economic theory, but any variable can be added to it if required.

For example, say, a forecaster for a Canadian company has researched factors he thinks would affect the USD/CAD exchange rate. From his research and analysis, he found that the most influential factors are: the interest rate differential (INT), the GDP growth rate differences (GDP), and the income growth rate (IGR) differences.

The econometric model he comes up with is −

USD/CAD (1 year) = z + a(INT) + b(GDP) + c(IGR)

Now, using this model, the variables mentioned, i.e., INT, GDP, and IGR can be used to generate a forecast. The coefficients used (a, b, and c) will affect the exchange rate and will determine its direction (positive or negative).

Time Series Model

The time series model is completely technical and does not include any economic theory. The popular time series approach is known as the autoregressive moving average (ARMA) process.

The rationale is that the past behavior and price patterns can affect the future price behavior and patterns. The data used in this approach is just the time series of data to use the selected parameters to create a workable model.

To conclude, forecasting the exchange rate is an ardent task and that is why many companies and investors just tend to hedge the currency risk. Still, some people believe in forecasting exchange rates and try to find the factors that affect currency-rate movements. For them, the approaches mentioned above are a good point to start with.

Exchange rate fluctuations affect not only multinationals and large corporations, but also small and medium-sized enterprises. Therefore, understanding and managing exchange rate risk is an important subject for business owners and investors.

There are various kinds of exposure and related techniques for measuring the exposure. Of all the exposures, economic exposure is the most important one and it can be calculated statistically.

Companies resort to various strategies to contain economic exposure.

Types of Exposure

Companies are exposed to three types of risk caused by currency volatility −

- **Transaction exposure** − Exchange rate fluctuations have an effect on a company's obligations to make or receive payments denominated in foreign currency in future. Transaction exposure arises from this effect and it is short-term to medium-term in nature.
- **Translation exposure** − Currency fluctuations have an effect on a company's consolidated financial statements, particularly when it has foreign subsidiaries. Translation exposure arises due to this effect. It is medium-term to long-term in nature.
- **Economic (or operating) exposure** − Economic exposure arises due to the effect of unpredicted currency rate fluctuations on the company's future cash flows and market value. Unanticipated exchange rate fluctuations can have a huge effect on a company's competitive position.

Note that economic exposure is impossible to predict, while transaction and translation exposure can be estimated.

Economic Exposure – An Example

Consider a big U.S. multinational with operations in numerous countries around the world. The company's biggest export markets are Europe and Japan, which together offer 40% of the company's annual revenues.

The company's management had factored in an average slump of 3% for the dollar against the Euro and Japanese Yen for the running and the next two years. The management expected that the Dollar will be bearish due to the recurring U.S. budget deadlock, and growing fiscal and current account deficits, which they expected would affect the exchange rate.

However, the rapidly improving U.S. economy has triggered speculation that the Fed will tighten monetary policy very soon. The Dollar is rallying, and in the last few months, it has gained about 5% against the Euro and the Yen. The outlook suggests further gains, as the monetary policy in Japan is stimulative and the European economy is coming out of recession.

The U.S. company is now facing not just transaction exposure (as its large export sales) and translation exposure (as it has subsidiaries worldwide), but also economic exposure. The Dollar was expected to decline about 3% annually against the Euro and the Yen, but it has already gained 5% versus these currencies, which is a variance of 8 percentage points at hand. This will have a negative effect on sales and cash flows. The investors have already taken into account the currency fluctuations and the stock of the company fell 7%.

Calculating Economic Exposure

Foreign asset or overseas cash flow value fluctuates with the exchange rate changes. We know from statistics that a regression analysis of the asset value (P) versus the spot exchange rate (S) will offer the following regression equation −

$$P = a + (b \times S) + e$$

Where, **a** is the regression constant, **b** is the regression coefficient, and **e** is a random error term with a mean of zero. Here, **b** is a measure of economic exposure, and it measures the sensitivity of an asset's dollar value to the exchange rate.

The regression coefficient is the ratio of the covariance between the asset value and the exchange rate, to the variance of the spot rate. It is expressed as −

$$b = Cov(P,S) / Var(S)$$

Economic Exposure – Numerical Example

A U.S. company (let us call it **USX**) has a 10% stake in a European company – say **EuroStar**. USX is concerned about a decline in the Euro, and as it wants to maximize the Dollar value of EuroStar. It would like to estimate its economic exposure.

USX thinks the probabilities of a stronger and/or weaker Euro is equal, i.e., 50–50. In the strong-Euro scenario, the Euro will be at 1.50 against the Dollar, which would have a negative impact on EuroStar (due to export loss). Then, EuroStar will have a market value of EUR 800 million, valuing USX's 10% stake at EUR 80 million (or $120 million).

In the weak-Euro scenario, currency will be at 1.25; EuroStar would have a market value of EUR 1.2 billion, valuing USX's 10% stake will be equal to $150 million.

If **P** represents the value of USX's 10% stake in EuroStar in Dollar terms, and **S** represents the Euro spot rate, then the covariance of **P** and **S** is −

Cov (P,S) = –1.875

Var (S) = 0.015625

Therefore, b = –1.875 ÷ (0.015625) = – EUR 120 million

USX's economic exposure is a negative EUR 120 million, which is equivalent to saying that the value of its stake in EuroStar decreases as the Euro gets stronger, and increases as the Euro weakens.

Determining Economic Exposure

The economic exposure is usually determined by two factors −

- Whether the markets where the company inputs and sells its products are competitive or monopolistic? Economic exposure is more when either a firm's input costs or goods' prices are related to currency fluctuations. If both costs and prices are relative or secluded to currency fluctuations, the effects are cancelled by each other and it reduces the economic exposure.
- Whether a firm can adjust to markets, its product mix, and the source of inputs in a reply to currency fluctuations? Flexibility would mean lesser operating exposure, while sternness would mean a greater operating exposure.

Managing Economic Exposure

The economic exposure risks can be removed through operational strategies or currency risk mitigation strategies.

Operational strategies

- **Diversifying production facilities and markets for products** − Diversification mitigates the risk related with production facilities or sales being concentrated in one or two markets. However, the drawback is the company may lose economies of scale.
- **Sourcing flexibility** − Having sourcing flexibilities for key inputs makes strategic sense, as exchange rate moves may make inputs too expensive from one region.

- **Diversifying financing** − Having different capital markets gives a company the flexibility to raise capital in the market with the cheapest cost.

Currency risk mitigation strategies

The most common strategies are −

- **Matching currency flows** − Here, foreign currency inflows and outflows are matched. For example, if a U.S. company having inflows in Euros is looking to raise debt, it must borrow in Euros.
- **Currency risk-sharing agreements** − It is a sales or purchase contract of two parties where they agree to share the currency fluctuation risk. Price adjustment is made in this, so that the base price of the transaction is adjusted.
- **Back-to-back loans** − Also called as credit swap, in this arrangement, two companies of two nations borrow each other's currency for a defined period. The back-to-back loan stays as both an asset and a liability on their balance sheets.
- **Currency swaps** − It is similar to a back-to-back loan, but it does not appear on the balance sheet. Here, two firms borrow in the markets and currencies so that each can have the best rates, and then they swap the proceeds.

INTERNATIONAL CASH MANAGEMENT, TAXATION:

Cash is one of the principal forces behind the success or failure of any company. Due to the state of the current global economy, it is becoming increasingly difficult for companies to achieve both their short and long-term financing needs. The long-term objective for many of today's companies is to expand and compete on the global stage, and as companies begin to shift to the global arena, it's more important than ever to evaluate and adopt sound cash management practices.

Companies must look beyond the traditional practices of:

- Debt service
- Collection of receivables
- Disbursements to vendors
- Forecasting

While these practices are instrumental to sound cash management, when operating internationally, it's important to evaluate and implement new polices not traditionally used in domestic cash management. Implementing some of the topics discussed below can be the vehicle to giving your company the extra edge.

Centralized Cash Management – Alleviating the Challenges of Cross-Border Transactions

Managing cash across borders with numerous bank accounts and currencies can often be a challenging undertaking for most companies. A means to alleviating some of the challenges is implementing a centralized cash management system. Centralized cash management systems offer more efficiently handled cash and produce a greater rate of return on cash investments. Under a centralized system, each subsidiary only worries and forecasts cash demands for their own subsidiary. The parent company then controls and distributes cash around the organization to meet required working capital needs, or maximize investment returns.

Cash savings are produced in several ways. For example, if the parent company determines, based on forecasting needs, that Subsidiary A will have a $100,000 short fall of cash this month, but Subsidiary B will have a $125,000 surplus, they can move cash from one subsidiary to the other. As a result, Subsidiary A does not need to obtain financing from an outside financial institution.

In addition, cash can be pooled from multiple locations to help maximize the rate of return on an investment. If the organization has excess cash not being used for operations, the company can consolidate cash into one account, receiving the most advantageous interest rate and earning a higher rate of return due to a larger balance and maximum interest rate.

Last, companies that operate with multiple currencies can maintain separate accounts of foreign currencies and distribute them to subsidiaries when in demand, reducing periodic translation costs.

Using a Netting Policy to Reduce Clerical and Transaction Costs

By putting into practice a centralized cash management system or working directly with subsidiaries and other companies, a netting policy can be implemented to assist in reducing clerical and transaction costs. The objective of a netting policy is to accumulate two or more companies' transactions, whether it is collections or payments, for an extended period of time and aggregate transactions into batches.

Accumulating the balances over a period of time will succeed in reducing the quantity of transactions that occurs between companies. Instead of collecting or paying on multiple transactions a month, a single aggregated transaction can occur. The reduction to the number of transactions will yield several benefits:The overall administrative and banking charges will be reduced, as decreased number of transactions will free up company resources and reduce cash transfer fees

For international transactions, costs typically associated with translation expense will be reduced. In addition, it can also act as hedge against currency losses connected with translation, and reduce normal banking fees

Netting can improve control over a company's cash position with fewer transactions, companies will find it easier to monitor and predict cash inflows and outflows.

Restriction of Funds – Getting the Money In and Out

Many countries such as Brazil and China have strong currency control measures. Many foreign governments mandate that profits generated within their borders be reinvestment into the local economy to help stimulate economic growth or recovery. Understanding these controls is important to effectively managing your cash and providing the needed capital to keep your business strong.

Some countries, such as China, restrict money entering or exiting the country. Generally, only the approved paid-in capital can be remitted to certain bank accounts in China, and only reasonable amounts are allowed to be converted to the local currency RMB. However, often time's companies that are importing and exporting out of China will be allowed to pay and receive funds in CNY. Furthermore, select companies are now permitted to open non-resident CNY accounts. Due to the constant state of flux in currency regulations and restrictions, it's imperative that you talk to an experienced professional before implementing any new policies.

Intercompany Transfers – A Tool to Manage Cash and Earnings

In addition to the policies discussed above, there are further tools an international parent subsidiary relationship can use to help manage cash and earnings. The most familiar method is through intercompany agreements for services or products. Although establishing intercompany arrangements can be an effective means of cash management and tax planning, many government agencies are aggressively examining companies' records, and have become diligent in ensuring that companies are observing the set forth regulations. Penalties can be harsh for companies that do not comply with the international transfer pricing regulations; therefore, it is important a proper analysis of transferring pricing is performed before being implemented.

Transfer pricing, put simply, is moving goods and services across borders to related companies. Transactions must be performed at an arm's-length, meaning that prices would be the same for any other company on the open market. Transfer pricing can be an effective tool to:

- Help shift income between tax jurisdictions
- Lower taxes paid
- Be used as a way to counter blocked funds, as discussed above

Before setting up the intercompany transactions, a services tax and other withholding tax should be considered. For example, the service providers may subject to a 5% service tax if the clients are in China, even the services are provided in the United States.

Another approach of intercompany relationships is using leading and lagging. Under this approach, subsidiaries can either pay for supplies from the parent company in advance, known as leading, or the parent can lend supplies to its subsidiaries and not require payment straight away, known as lagging. Leading and lagging can help free up additional cash to service debt or fund other operational requirements.

Operating abroad can very different from doing so domestically, as foreign governments and banking systems are very different from our own.

TAX TREATIES

Double taxation arises where two or more countries tax the same income or cash remittance. For instance, if a US-based company has a branch overseas, it is possible that the profits of the branch will be taxed both by the overseas authorities and (as part of the company's overall profit) by the US Inland Revenue Service. Tax treaties (also known as double taxation treaties) are agreements between two countries that set out the taxation rights of each country in respect of tax charged in the other. They are designed to facilitate international trade by avoiding double taxation.

When setting up new operations or planning the routing of income within an international group, it is important to consider which tax jurisdictions are involved. For example, if a cash manager was considering routing dividends from the US via a French holding company to a Swiss parent, then both the tax treaty between France and the US, and the treaty between France and Switzerland, would have to be taken into account.

In order to benefit from a treaty's rules, a company will usually have to seek prior approval from the tax authorities before making any remittances, so the cash manager must work closely with the tax team ahead of moving funds.

PERMANENT ESTABLISHMENT

In most countries, income tax is only levied once a permanent establishment exists and, typically, tax treaties permit a certain level of activity in a foreign country before a permanent establishment is created. For example, a company may be running the sales operations from their home country, but warehousing goods and advertising in a foreign country. Normally, this would not create a permanent establishment.

But in some countries, merely holding a bank account can create a permanent establishment (for example, in Thailand) and the company can be taxed accordingly, so care must be taken whenever operating in a new country.

CONTROLLED FOREIGN COMPANIES (CFCS)

Usually, the profits of a subsidiary are only taxed at the parent level when they are distributed (for example, when dividends are paid) and so setting up a foreign company in a favourable tax location is a popular technique for avoiding domestic taxation.

But where a company has established an overseas subsidiary controlled by the parent purely in order to take advantage of favourable tax rates, most countries now have CFC rules that allow them to tax income immediately on recognition (ie tax is levied on the parent as soon as it is earned, before any distribution).

For example, a company that is resident outside the UK, but controlled from the UK, will be subject to UK CFC anti-avoidance tax rules.

Companies with genuine operations and substance in a foreign country should not be caught by such rules, but care should be taken when deciding the location and structure of special-purpose vehicles, including shared service centres or treasury companies, as they are frequently subject to close scrutiny by the tax authorities.

Interest income or income from intercompany lending activities may be subject to tax immediately on being earned if CFC rules are triggered. Even the location of the cash pool may invoke CFC rules.

THIN CAPITALISATION (THIN CAP)

When a company sets up a subsidiary, there is a choice between debt and equity funding in varying proportions. Where a foreign subsidiary is taxpaying, loading the subsidiary with interest-bearing debt can reduce the level of tax payable because interest on that debt is generally tax-deductible, even if the debt is inter-company.

In order to avoid this loss of tax income, tax authorities try to ensure that companies do not receive excessive levels of debt funding from other group companies through the introduction of thin cap rules (such as a minimum debt/equity ratio). Thin cap rules state that any debt above predetermined levels is treated as equity and the interest payment is treated as a dividend and taxed accordingly.

Care should be taken when implementing liquidity structures as these may trigger thin cap rules. For example, cash concentration structures where cash is physically pooled create inter-company loans that may be included as debt. In some jurisdictions, tax authorities may even

regard a subsidiary with a debit balance in a notional cash pool as in effect 'borrowing' from the group for the purposes of calculating thin cap ratios.

TRANSFER PRICING

Where two companies that are connected (for example, from the same group) trade with each other, the price at which goods or services are traded is referred to as the transfer price. By adjusting the transfer price, it is possible to make one company more profitable and the other less so. This has major implications for the amount of tax collected on the profits of each company, as transfer pricing can shift earnings from a high-tax jurisdiction to a low-tax one.

As a result, most countries have transfer pricing rules that require the connected companies to trade on the same terms as if with third parties (ie 'arm's length' or market price basis). In some jurisdictions, tax rules for transfer pricing now include domestic transactions as well as cross-border ones.

A central treasury operation or an in-house bank will attract particular attention from tax authorities in respect of transfer pricing.Therefore, treasurers must ensure that:

- All inter-company loans carry a market rate of interest and are documented and signed;
- Commercial FX rates are used when transacting between group companies;
- Spreads are agreed for taking deposits or buying or selling currencies; and
- Fees for services such as netting, re-invoicing or providing a parental guarantee to secure lower funding costs must be fully documented and recharged among those members of the group that benefit from them (this also applies to other services provided to group companies and may be recharged under 'management service agreements').

Companies should always maintain documentation of trading relationships and provide evidence that the terms are at market rates. Sources of daily rates, such as Reuters, Bloomberg or *The Wall Street Journal*, are examples of independent sources that might be used to corroborate the rates applied.

WITHHOLDING TAXES (WHT)

Where a company makes cross-border payments, typically of interest, dividends or royalties, it may have to withhold an amount from the payment and pay this to the domestic tax authority. WHTs are taxes on the recipient rather than the payer, and are levied as a means of collecting tax that would otherwise be payable on the income in the hands of the recipient. Each territory has its own rules on WHT; it is the rules that apply in the territory of the payer, not the recipient, that are relevant.

From the treasury perspective, the major areas where WHTs can be an issue are:

- Dividends and royalty payments;

- Bank interest and gross-up clauses – financial markets work on the basis that interest is paid and received gross, ie without any tax deduction; all interest rates are quoted on this basis. If WHT is payable, most banks and other investors will require interest to be 'grossed up'. The lender receives the equivalent gross amount even after deduction of WHT. A gross-up clause preserves the investor's return, but places an additional potential cost on the borrower;
- Deemed bank interest applied by the corporate treasury as part of a cash pooling structure;
- Interest on intercompany loans including those created as a result of a cash pooling structure; and
- Payments considered 'in lieu of interest', such as arrangement fees.

STAMP DUTIES

- Stamp duty is a form of tax that is levied on documents (or transfers of some types of property). Traditionally, a physical stamp (a tax stamp) must be attached to, or impressed upon, the document to denote that stamp duty has been paid before the document becomes legally effective, hence its name.
- In certain countries, the execution of financial documents such as loan agreements (even for intercompany lending) may require stamp duties.
- Stamp duties can generally be avoided by not executing documents in those jurisdictions that levy them. But the tax can still become due if the document is 'repatriated' for legal or other reasons, so such documents may have to be stored as well as signed offshore.

Unit 4

International operation Strategy – Procurement – Subcontracting – Plant location decisions – plant design and interplant relationship – Staffing policies – Globalisation and HRM – International labour strategy – New directions in organizational structures – Performance evaluation.

A firm that has operations in more than one country is known as a multinational corporation (MNC)**.**The largest MNCs are major players within the international arena. Walmart's annual worldwide sales, for example, are larger than the dollar value of the entire economies of Austria, Norway, and Saudi Arabia. Although Walmart tends to be viewed as an American retailer, the firm earns more than one-quarter of its revenues outside the United States. Walmart owns significant numbers of stores, as of mid-2014, in Mexico (2,207), Brazil (556), Japan (437), the United Kingdom (577), Canada (390), Chile (386), Argentina (105), and China (400). Walmart also participates in joint ventures in China (328 stores) and India (5). Even more modestly sized MNCs are still very powerful. If Kia were a country, its current sales level of approximately $42 billion (in 2012) would place it in the top 75 among the more than 180 nations in the world (Wal-Mart Stores Inc., 2014).

Multinationals such as Kia and Walmart have chosen an international strategy to guide their efforts across various countries. There are three main international strategies available: (1) multidomestic, (2) global, and (3) transnational. Each strategy involves a different approach to trying to build efficiency across nations while remaining responsive to variations in customer preferences and market conditions.

Multidomestic Strategy

A firm using a **multidomestic strategy** sacrifices efficiency in favor of emphasizing responsiveness to local requirements within each of its markets. Rather than trying to force all of its American-made shows on viewers around the globe, MTV customizes the programming that is shown on its channels within dozens of countries, including New Zealand, Portugal, Pakistan, and India.

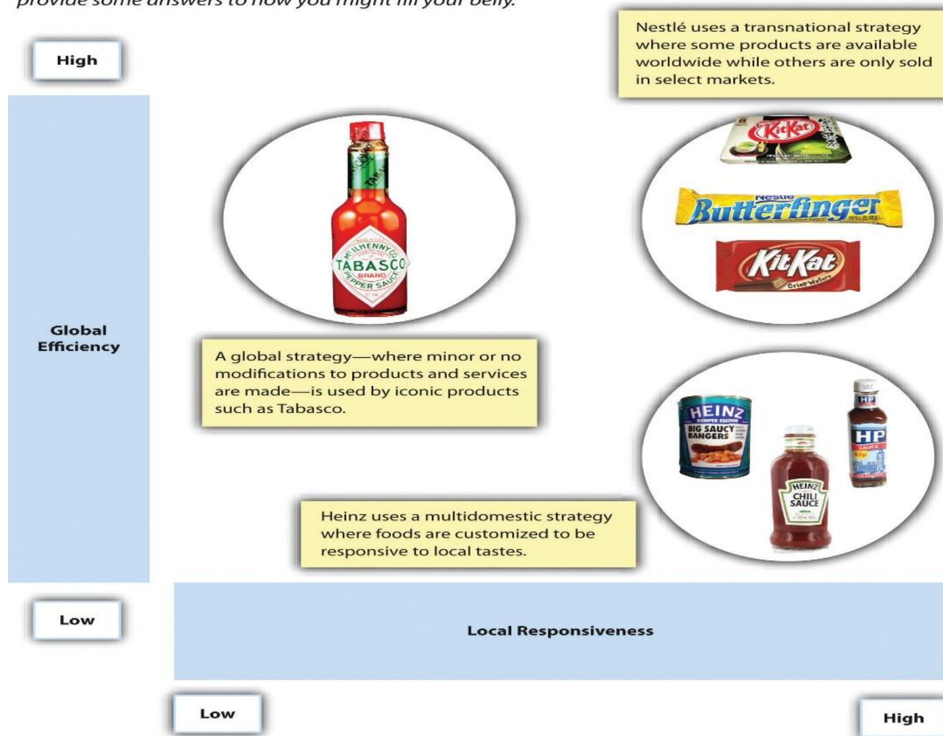

Figure: International Strategy

Similarly, food company H. J. Heinz adapts its products to match local preferences. Because some Indians will not eat garlic and onion, for example, Heinz offers them a version of its signature ketchup that does not include these two ingredients.

Figure: Baked beans flavored with curry? This H. J. Heinz product is very popular in the United Kingdom.

Global Strategy

A firm using a global strategy sacrifices responsiveness to local requirements within each of its markets in favor of emphasizing efficiency. This strategy is the complete opposite of a multidomestic strategy. Some minor modifications to products and services may be made in various markets, but a global strategy stresses the need to gain economies of scale by offering essentially the same products or services in each market.
Microsoft, for example, offers the same software programs around the world but adjusts the programs to match local languages. Similarly, consumer goods maker Procter & Gamble attempts to gain efficiency by creating global brands whenever possible. Global strategies also can be very effective for firms whose product or service is largely hidden from the customer's view, such as silicon chip maker Intel. For such firms, variance in local preferences is not very important.

Transnational Strategy

A firm using a transnational strategyseeks a middle ground between a multidomestic strategy and a global strategy. Such a firm tries to balance the desire for efficiency with the need to adjust to local preferences within various countries. For example, large fast-food chains such as McDonald's and KFC rely on the same brand names and the same core menu items around the world. These firms make some concessions to local tastes too. In France, for example, wine can be purchased at McDonald's. This approach makes sense for McDonald's because wine is a central element of French diets.

PROCUREMENT

The act of obtaining or buying goods and services. The process includes preparation and processing of a demand as well as the end receipt and approval of payment. It often involves

(1) Purchase planning,

(2) Standards determination,

(3) Specifications development,

(4) Supplier research and selection,

(5) Value analysis,

(6) Financing,

(7) Price negotiation,

(8) Making the purchase,

(9) supply contract administration,

(10) Inventory control and stores, and

(11) Disposals and other related functions.

The process of procurement is often part of a company's strategy because the ability to purchase certain materials will determine if operations will continue.

SIGNIFICANCE OF PROCUREMENT

Many decisions taken by departments have a procurement implication that can impact on the overall cost of carrying out the decision. Here cost includes the total cost of the good or service and not simply the price that is paid.

In the private sector, procurement is viewed as a strategic function working to improve the organisation's profitability. Procurement is seen as helping to streamline processes, reduce raw material prices and costs, and identifying better sources of supply. In essence, helping to reduce the 'bottom line'. Indeed, in many organisations the importance of procurement is recognised by having their head of procurement placed at an Executive Board level.

In the public sector, the concept of a 'bottom line' is less well defined - there are no shareholders' dividends to be paid out or publicly declared profit (or loss) announcements. There is however a need to maximise the output, in terms of teaching and research, within the available funds. These funds come, substantially, from public funding in the form of grants, student fees etc. We are the sector's shareholders as tax payers, students and/or staff. This, therefore, places an inherent requirement that the funds provided are managed in a manner that is accountable and demonstrates both probity and value for money.

At higher levels of expenditure, this need for openness, transparency and non-discriminatory action is required by legislation. The European Procurement legislation, implemented in the UK, means that all requirements for supplies/services (>£172,000 approximately) and works (> £4.3 million approximately) are advertised and tendered in accordance with published rules.

Within an institution, its expenditure is made up of two distinct elements - pay (salaries and wages) and non-pay (all other expenditure). Procurement is concerned with the management of a significant proportion of the non-pay expenditure and ensuring that the best possible value for money is obtained when committing this expenditure. Non-pay spend includes the day-to-day running costs of the institution as well as its capital expenditure. This expenditure can be further divided into that which is used to obtain goods and services from suppliers and other expenditure

such as payments made to other educational establishments or to HM Revenue and Customs. The procurement function is concerned with obtaining the required goods and services from appropriate suppliers to enable the institution to meet its strategic objectives in an economic, efficient and effective manner.

Research has shown that within an institution, its non-pay expenditure is usually between 30 - 40% of its total expenditure

PLANT LOCATION

Location of an industry is an important management decision. It is a two-step decision: first, choice of general area or region and second, the choice of site within the area selected. Location decision is based on the organisations long-term strategies such as technological, mar-keting, resource availability and financial strategies.

The objective of plant location decision-making is to minimise the sum of all costs affected by location.

Plant location is important because of the following:

(i) Location influences plant layout facilities needed.

(ii) Location influences capital investment and operating costs.

Location decisions are strategic, long-term and non-repetitive in nature. Without sound and careful location planning in the beginning itself, the new facilities may create continuous operating problems in future. Location decision also affects the efficiency, effectiveness, produc-tivity and profitability.

The location decision should be taken very carefully, as any mistake may cause poor location, which could be a constant source of higher cost, higher investment, difficult marketing and transportation, dissatisfied and frustrated employees and consumers, frequent interruptions of production, abnormal wastages, delays and substandard quality etc.

Therefore, it should be based upon a careful consideration of all factors that are essentially needed in efficient running of a particular industry. The necessary factors in the selection of plant location vary among industries and with changing technical and economic conditions.

Site selection is not an easy problem because if the selection is not proper then all money spent on factory building, machinery and their installation etc., will go as waste and the owner has to suffer a great loss. Therefore, while selecting a site, owner must consider technical, commercial, financial aspects which may provide maximum advantages.

It is sometimes pos-sible that all the requirements and features of ideal site may not be available at one particular location but then it will be advantageous to find out suitable site with combinations of all essential requirements of the particular industry to be established as explained in following paras.

LOCATIONAL ECONOMICS:

The selection of the location for an industrial plant is a long time commitment. A new enterprise may be suffered throughout its life due to unfavourable location. Once a plant has been built, the expense and disruption of activities necessary to move it to a more favourable location is quite impracticable. Therefore, the search for plant site justifies very careful consid-eration.

For evaluation of economical location following factors should be considered:

1. Raw material procurement.

2. Proximity of market.

3. Availability of labour, their training and compensation.

4. Availability of power.

5. Availability of finance.

6. Miscellaneous considerations like donations, subsidies, taxes and non-interference by government or local bodies, war and political effects and other facilities or bottle necks.

PLANT DESIGN

We can define layout as, ‘The physical location of the various departments/units of a facility within the premises of the facility.’ The departments must be located based on some consideration. The common considerations are –

1. Logical sequence of processing operation

2. Direction of material flow and material handling

3. Aesthetic considerations

4. Government regulations

5. Special requirements The entrance and exit gates are usually critical in the layout planning of facilities

OBJECTIVES OF A PLANT LAYOUT

Plant layout is the method to plan and arrange materials and facilities so that a steady flow of production is ensured at minimum cost. A good plant layout always results in comfort and satisfaction of workmen and this automatically increases the production. A bad plant layout leads to accidents and unnecessary problems. A good plant layout is designed to achieve the following objectives:

1. Economic handling of materials and finished goods
2. Fast and efficient quality production
3. Enhanced utilization of available space
4. Flexibility in change of plant design and possibility of expansion at a later date
5. Improvement in work condition leading to higher productivity
6. Unidirectional/systematic flow of production operation
7. Reduction in waiting time
8. Reduction in manufacturing cost

ADVANTAGES OF A GOOD PLANT LAYOUT

A good plant layout results in better production and lower costs. The advantages of a good plant layout are as follows:

1. Well-organized workspace: A good plant layout means well-organized workspace with adequate facilities provided for the machines as well as for the workmen. Proper arrangement of machineries and tools eliminates congestion. The materials required are stored in their appropriate places so there is no confusion. Workmen are also distributed to their respective departments and there is no confusion in work.

2. Better working conditions: A good plant layout results in labour satisfaction due to improved and clean working conditions. It has been well-documented that motivation level increases when lighting and other aesthetics are improved. Safety of workmen is another important factor. A good plant layout ensures that the machine are properly placed, with adequate space in between so that there is no congestion and no danger of the workmen getting injured. This provides safety to the workmen and creates a good environment for work

3. Minimization of material handling costs: A good plant layout minimizes material handling costs. The machinery and equipment are placed in such a manner that there is no difficulty in transferring materials between workstations. The provision of adequate material handling systems will ensure that there is minimal labour cost, labour fatigue, etc., and labour can be utilized in productive jobs.

4. Minimization in damage and spoilage of material: In a good plant layout, materials are handled properly which results in good quality of production. There is minimum damage and spoilage of materials. Minimizing waste also leads to increase in profits for a company.

5. Flexibility in changing production conditions: A good layout provides adequate space for future expansions, laying additional workstations, etc. The advantage is that in future if the market conditions change, the firm can easily put up new machinery, etc. without having to dismantle the existing ones and with minimum hindrance to the daily schedule or work.

STAFFING POLICY & HRM ISSUES IN INTERNATIONAL BUSINESS

Human resource management in international business presents issues that are different from those in domestic or local business. The nature and characteristics of international business are more complicated than domestic or local business. As such, it is necessary to account for different types of human resource management issues in international business. HR managers must also choose the right staffing policy approach based on the needs of the organization. Effectively addressing the various types of human resource management issues and deciding on the most suitable staffing policy approach leads to success in HRM in international business.

TYPES OF STAFFING POLICY APPROACHES IN INTERNATIONAL HRM

In international human resource management, the types of staffing policy approaches are as follows:

- Ethnocentric staffing
- Polycentric staffing
- Geocentric staffing

The ethnocentric policy approach to staffing designates home country nationals as top ranking employees in global operations. For instance, executive positions are given to Americans in an office of an American company located in Indonesia. The main benefit of this staffing policy approach is that it allows the organization to ensure that the people in the top positions are experienced in the business of the firm. This is especially the case where the host country does not have enough qualified workers for staffing top positions in the organization. The ethnocentric staffing policy approach is also used to ensure that the culture of the entire organization is unified rather than diversified. However, the problem with the ethnocentric policy approach is that it

does not fully support the transfer of local knowledge to the company. Also, this staffing policy approach could block locals from promotion in the organization.

The polycentric policy approach to staffing assigns home country workers to top positions in the central offices or headquarters, and overseas local workers to other positions. The main advantage of this policy approach is that it facilitates organizational learning on local markets. This staffing policy approach also provides better opportunities for locals to improve their careers through promotion. However, this promotion is limited to key positions in the local operations, and does not include central or corporate top positions. This staffing policy approach is disadvantageous because it could create knowledge and performance gaps between overseas managers and managers in the home country.

The geocentric policy approach to staffing assigns job positions to any person best suited for the position, regardless of the employee's background, culture or country of origin. The main advantage of this staffing policy approach is that it is highly flexible. It can increase the firm's cultural knowledge about the different markets and countries. However, a disadvantage of this staffing policy approach is that it could be difficult to apply. Immigration policies, costs of worker relocation and diversity management create pressure on HR management.

GLOBALIZATION ON HRM

Globalization symbolizes free flow of technology and human resources across national boundaries presenting an ever-changing and competitive business environment. Globalization is a process that is drawing people together from all nations of the world into a single community linked by the vast network of communication technologies. This aspect of globalization has also affected the HRM in the business world of today. HR managers today not need to rely in a small limited market to find the right employees needed to meet the global challenge, but today they can recruit the employees from around the world. The future success of any organizations relies on the ability to manage a diverse body of talent that can bring innovative ideas, perspectives and views to their work. Thus, a HR manager needs to be mindful and may employ a 'Think Global, Act Local' approach in most circumstances. Many local HR managers have to undergo cultural-based Human Resource Management training to further their abilities to motivate a group of professional that are highly qualified but culturally diverse. . Furthermore, the HR professional must assure the local professionals that these foreign talents are not a threat to their career advancement. In many ways, the effectiveness of workplace diversity management is dependent on the skilful balancing act of the HR manager.

Global HRM refers to Human Resource Management practices that deal with managing a diversity of workforce from all around the world.

THE IMPACT OF GLOBALIZATION ON HRM IS AS FOLLOWS:

Managing Cultural Diversity: Managing different employees from different cultures in the same organisation is a complex activity. Employees from each country think differently, perceptions are different towards work culture, the languages change, vocabulary differs and even non verbal communications are quite different from each region. This makes the task of the human resource department challenging due to globalization.

Managing Expatriates: Preparing the home country employees to work in a different country is a herculean task. The beliefs, value system, culture, attitude are diverse in nature. Recruiting, retaining and motivating expatriates have a major impact on the business. Understanding expatriate's need is a prime concern for the human resource team.

Difference in The Employment Laws: The employment laws or the labour laws differ from one country to another. The understanding of not only the monetary benefits becomes essential but also the non monetary benefits such as leaves, flexi timings are important to be included in the human resource policy.

Managing Outsourcing of employees: Outsourced employees to manage business are the big impact of globalization. Managing the BPO, KPO employees working with a different culture, different language, working in completely opposite shifts is a new shift in the area of human resources. Managing the expectation of these employees is a challenge for today's HR and this challenge is a result of globalization.

Managing virtual employees: Majority of the information technology based organisations have employees working "on-site" at a client's location which is completely new to them. The virtual employees have to be managed, retained and motivated in a different way unlike the "off-shore" employees. This practice of managing the virtual employees is a result of organisations going global.

Corporate Social Responsibility: Corporate houses actively participating in the practice of doing for the betterment of the society has emerged from the western countries. It is one of the ways make the presence felt in the host countries. Employees are encouraged to participate in such activities which help to reduce stress working with MNC's.

Coping with flexible working hours: The practice of flexible working hours has emerged as one of the retention initiative of workforce specially women employees who can maintain the work life balance. This practice of flexible working hours is result of working beyond normal time zones. Organisations which have a global presence need the attention of employees at various time zones which is not possible for all employees doing a continuous shift. Hence this practice emerged from globalization and has a positive impact on the HRM practice.

Evolution of more part-time and temporary work (especially among women, the elderly and students): The concept of part time employment, contract jobs have emerged from the practice of MNC's since hundred percent of workforce on permanent payroll is quite a expensive matter to these organisations. Majority of large MNC's in the information technology sector has their employees under contract employment.

Coping up with emerging technologies & quality measures: Every employee in today's leading organisation is being trained with the latest technologies especially with the ERP concept like SAP or Peoplesoft. This step has been taken by MNC's to equip the employees with latest technology enabling the employees to cope up with the changing technology. Certifications like Six Sigma are availed to employees to manage the business on an international platform.

Changing perspective from subordinates to business partners: The shift has been observed in today's MNC that culture of subordinates is getting extinct. Employees have been treated as business partners' i.e every employee is responsible towards the growth of the organisation and considered as a partner in the company. This impact is the result of globalization.

International Human Resource Management: Performing the HRM functions across the globe for the organisation.

International human resource management is all about the world wide management of human resources – Process of sourcing, allocating, and effectively utilising their skill, knowledge, ideas, plan and perspective in responding to TQM.

The process of procuring, allocating and effectively utilizing human resources in an international business is called International Human Resource Management or IHRM. International Human Resource Management is the process of sourcing, allocating and effectively utilizing human resources in a multinational organization.

Purpose of IHRM: To enable the firm /, the multinational corporations (MNCs), to be a successful globally

Dimensions of IHRM:

According to P.V. Morgan: IHRM is the interplay among 3 dimensions:

HR Activities

Types of employees

Types of Countries

1) Broad activities of IHRM – procurement, allocation and utilization of human resources cover all the six activities of domestics HRM i.e, HR planning, Employees Hiring, Training and Development, Remuneration, Performance Management and Industrial Relations.

2) The three national or country categories involved in IHRM activities are:

The host country where subsidiary may be located

The home country where the company has its head quarters and

Other countries that may be sources of labour or finance.

NEW DIRECTIONS IN ORGANISATION STRUCTURE

An organizational structure defines how activities such as task allocation, coordination and supervision are directed toward the achievement of organizational aims.Organizations need to be efficient, flexible, innovative and caring in order to achieve a sustainable competitive advantage.

Types of Organisational Structures

(i) Line organisational structure.

(ii) Staff or functional authority organisational structure.

(iii) Line and staff organisational structure.

(iv) Committee organisational structure.

(v) Divisional organisational structure.

(vi) Project organisational structure.

(vii) Matrix organisational structure and

(viii) Hybrid organisational structure.

Types of Organisations:

Multinational Corporation (MNC) : MNC is an organisation which operates in more than one country

Transnational Corporation (TNC): TNC is an organisation, that produces, markets, invests and operates across the world

Home Country/Parent Country: HC/PC is the one where the headquarters of an MNC or TNC is located.

Host Country: Host country is the one where the subsidiary/branch of an MNC/TNC is located

The three types of employees of an international business are – Parent Country Nationals (PCNs) , Host Country Nationals (HCNs) and Third Country Nationals (TCNs). For example, IBM which employs Australian citizens in its Australian operations, after sends US citizens to Asia Pacific countries on assignment, and may send some of its Singaporean employees to its Japanese operations.

TYPES OF EMPLOYEES

Expatriates/ Guest Employees: (All Types of foreigners.) Expatriate is an employee working and living in a foreign country where he/she is a non citizen.

Inpatriates: Inpatriates are those Host Country Nationals transferred to head quarters of MNC

Home Country Nationals/ Parent Country Nationals: (PCN) are employees of an MNC/TNC who are citizens of the home country/parent country of the MNC/TNC

Host Country Nationals (HCN): Employees of an MNC/TNC's subsidiary/ branch who are the citizens of the country where the subsidiary/branch of the MNC/TNC is located.

Third Country Nationals (TCN) : These are employees of an MNC/TNC or their subsidiary/ Branch and are the citizens of those countries other than the MNC/TNC's home country and or host country.

PERFORMANCE EVALUATION

The second evaluation challenge is that networks are unique organizations that contrast to a large degree with the corporate, governmental or civil society organizational structures of their members. To paraphrase systems thinker Russell

The organizational chart on the left is common for government, business or civil society organizations...typically the organizational forms of the members of a network. The network's own organizational chart, however, is quite different, similar to what is presented on the right. The difference between a network and other organizational forms is more than the structure of relationships of power, money, information, co-operation and activities. The nature of those relationships is also unique in two important ways.

DEMOCRACY:

It is a necessity because network members are voluntary autonomous organizations. Hierarchical management and command and control simply do not work well with these social actors. Success depends on equity in the relations and exercise of power within the network. Leadership must stimulate and strengthen the active participation of all members and effective work in alliances. Democratic management and participation are the keys to empowerment, ownership and concerted, common action in a network.

Therefore, members' participation in decision-making is the best guarantee that the decision will be implemented. Echoing the folks at the Canadian International Development Research Centre's Evaluation Unit, the willingness of the members of a network to monitor and interpret success (along with planning, implementing and adjusting activities) constitutes ownership in a network.i

Another unique difference of a network compared to other organizational forms is the great diversity amongst its members, of course within a unity of purpose. Part of the genius of this organizational form is that its members share common values and a collective purpose but have different visions and strategies on how to achieve change. The organizational challenge is to enable each one of these heterogeneous actors to make a creative and constructive contribution. The evaluation task is to assess how well the actors are interacting and understand the fruits of their co-operation.

Because networks are such unique organizational forms that demand empowerment of the enormously diverse actors within it, the task of evaluation is also unique. Essentially, it is all about participation. As Madeline Church and colleagues at the Development Planning Unit, University College London say:

"Evaluation in the network context needs to pay attention to how the network: fosters participation by its members, adds value to the work of its participants and

NETWORK STAKEHOLDERS EXPECT PROJECT-TYPE EVALUATIONS

The third challenge of evaluating the performance of networks is that stakeholders demand accountability and results seen from a program or project perspective. Stakeholders want to see quick progress and clear results for money and time invested in the network project. Consequently, donors especially exert project-minded, cost-benefit pressure. The familiar project planning, monitoring and evaluation approach runs along the linear, These are valid, understandable questions but they are problematic for two reasons. First, when a network carries on projects, typically managed by the secretariat, that mode of evaluation may be appropriate. When, however, the evaluation focus is the operation of the network as a whole, project or program evaluation methodologies do not work. Why? Well, for three reasons that flow from the two challenges presented above.

Networks are in the category of organizational forms that Michael Quinn Patton calls "non-linear, dynamic social change agents".iiiThey make interventions based more on values than hypotheses. Their activities take place in complex situations without predetermined, predictable,

or controllable results. Even the “right” inputs-activities-outputs equation is often uncertain, because what works and does not work only emerges as the interactions of the network unfold.

In a network’s activities and results—and we are talking fundamentally about fluid relationships amongst members and significant social change—cause and effect is rarely known and frequently not knowable, and then usually in retrospect.

The time horizon of a network is long-term and especially uncertain. The farther out the time horizon, the more uncertainty increases. Opportunities and risks proliferate, and with more time, these variations magnify uncertainty.

That is, sometimes the environment in which international networks operate is so volatile that project evaluation may not work even for short-term Secretariat projects. The project evaluation approach is even less appropriate for a program of projects or for the network as a whole.

NETWORK EVALUATION REQUIRES HYBRID, INNOVATIVE APPROACHES

The fourth and last challenge I see for network evaluation is the other side of the coin: How can networks demonstrate results if standard evaluation methods are inappropriate? The short answer is that networks must innovate and create hybrid approaches that meet their special needs and circumstances. That, however, requires just as much professional rigor as it does vigor.

Thus, a basic criterion is that evaluation in an international network must conform to professional standards. These four evaluation standards originally developed by the American Evaluation Associationiv are now being adapted around the world. Of course, a network may want to modify these or affirm others. An evaluation must meet standards of

Utility - Serve the information needs of intended users.

Feasibility - Ensure that an evaluation will be realistic and achievable in the light of the questions it seeks to answer and the available resources, be politically sensitive and sensible, and cost effective.

Propriety - Make sure that evaluation is conducted legally, ethically, and with due regard for the welfare of those involved, as well as those affected by its results.

Accuracy - Utilize evidence generated through appropriate and solid research methods and quantitative and qualitative analytical tools. For example, information should be triangulated—derived from three or more sources

Unit V

International acquisitions – cultural, legal , political dimensions – conventional perspective of acquisition process – alternative perspective – acquisitions and business strategy – successful integration – Problems in acquisition integration – Approaches to integration – Future of multinational – international Co – operation – Determinants of competition – International managers for millennium.

International Restructuring: Acquisitions

An international acquisition of a business is similar to other international projects: it requires an initial outlay and is expected to generate cashflows whose present value will exceed the initial cash outlay. Global consolidation and market share are two possible motivations for international restructuring and acquisition. Some U.S. multinational firms that have acquired internationally during the recent years are Ford Motor Company, Dow Chemical Company and Rockwell International.

As against establishing a new subsidiary, international acquisitions have some distinct advantages: they take less time, and can benefit from customer relations that have already been established. These incremental benefits have to be traded off against the incremental costs of such acquisitions. International acquisitions usually generate quicker and larger cash flows but also require a larger initial outlay. International acquisitions also require aligning the parent's management style with that of the acquired firm.

The volume of foreign acquisitions of U.S. firms has increased continuously since 1993. European firms have been the most likely targets due to more uniform regulations across countries in the European Union, the rapid change towards privatization in Eastern Europe, and the emergence of a single currency in the Eurozone.

Valuation of a foreign target

The multinational parent would only consider investing in a target if the foreign target's value can be estimated as positive, i.e., only if the estimated PV of the cashflows it would ultimately receive from the target over time exceeds the intitial outlay necessary to purchase the target. Thus, capital budgeting analysis can be used to determine whether a firm should be acquired. The PV of cashlfows would be made up of the PV of cashflow to be generated by the target for

the acquiring firm as well as the PV of the salvage value of the target, which is the expected selling price of the target at a point in the future.

The capital budgeting analysis of a foreign target must account for the relevant exchange rate values. For example, the dollar initial outlay needed by the US firm is determined by the acquisition price in foreign currency units and the spot exchange rate for the foreign currency in HC / FC units. The dollar amounts of cashflows to the US firm is determined by the foreign currency cashflows remitted to the US per year and the spot exchange rate from year to year. Similarly, the dollar amount of salvage value to the US firm is determined by the salvage value in FC units and the spot rate at the time when it is converted into dollars.

Of course, this simple valuation model ignores any withholding taxes or blocked-fund restrictions imposed by the host government and any income taxes imposed by the US government. These aspects that we have studied earlier need to be incorporated to refine this valuation model of a foreign target for the real world.

Expected Cashflows of Foreign Target

Several factors need to be taken into account that reflect conditions in the country of the foreign target as well as conditions for the target itself. These factors may be broadly classified into:

a) Target-specific factors
b) Country-specific factors

a) Target-specific factors

i. Target's previous cashflows: Since the foreign target has already been in business, it is sometimes easier to estimate its future cashflows than cashflows generated from a new subsidiary. Previous cashflows have to be used as a basis for projecting future cashflows together with future exchange rates.

ii. Managerial capability: On acquiring a foreign target, the acquiring multinational has several choices available for managing the business. Allow the target to be managed as it was before the acquisition, downsize the target firm after acquiring the business, or maintain the existing employees of the target but restructure the operations so that labor efficiency is better than before. The alternative chosen will affect the estimated cashflows generated by the target.

b) Country-specific factors

i. Economic conditions: primarily determine market demand in the target market. If the target market for the acquired firm's products is in a different country, economic conditions are less relevant.

ii. Political conditions: the more favorable they are, the less likely the target's cash-flows are variable. Country or political risk will be dealt with when we move on to that topic in a separate session.

iii. Industry conditions: essential characteristics of the industry to which your acquired business belongs are positive growth and limited competition. Industry conditions may decide the country.

iv. Currency conditions: ideally, the target is located in a weak currency country so costs are low, where the currency is expected to strengthen as the target starts to remit profits to the parent.

v. Market conditions: may result in substantial swings in the stock price of the acquired firm and thus affect the price paid for the target, especially in emerging markets.

vi. Corporate taxes: in assessing the value of a foreign target, an MNC must estimate the expected after-tax cashflows that it will ultimately receive in the form of remitted funds to the parent.

Most MNCs that consider acquiring a specific target will use a quite similar process for valuing the target. Nevertheless, their valuations will differ because of differences in the way the MNCs estimate the key determinants of a target's valuation, such as cashflows to be generated by the target, exchange rate effects on funds remitted to the MNC's parent, and the required rate of return when investing in the target. It is possible that depending on the treatment the valuation differs between different acquirers.

Vertical integration is a competitive strategy by which a company takes complete control over one or more stages in the production or distribution of a product.

A company opts for vertical integration to ensure full control over the supply of the raw materials to manufacture its products. It may also employ vertical integration to take over the reins of distribution of its products.

A classic example is that of the Carnegie Steel Company, which not only bought iron mines to ensure the supply of the raw material but also took over railroads to strengthen the distribution of the final product. The strategy helped Carnegie produce cheaper steel, and empowered it in the marketplace.
he political environment in international business consists of a set of political factors and government activities in a foreign market that can either facilitate or hinder a business' ability to conduct business activities in the foreign market. There is often a high degree of uncertainty when conducting business in a foreign country, and this risk is often referred to as political risk or sovereign risk.

Common Political Factors
Let's look at some common political factors that influence the international business landscape. The type of economic system a country builds is a political choice. Foreign countries often will have different economic systems from your domestic market, and adjustments often need to be made to take these differences into account.

For example, a country may operate in a market economy where private individuals own most of the property and operate most of the businesses. A market economy is usually the best economic environment for a foreign business because of the protection of private property and contract rights.

Some countries lean more towards a socialist economy where many industries and businesses are owned by the state. Operating businesses in this environment will be more difficult, but products can still be produced and sold as people still pick their jobs and earn money.

A few countries operate under a communistic economic system where the state pretty much controls all aspects of the economy. Conducting business in this environment ranges from difficult to impossible.

Of course, the reality is that all economies are mixed economies that take parts from two or more of the 'pure' economic systems. For example, you can conduct business in communist China in Hong Kong and other special areas where a market economy is allowed to operate.

Businesses also must often contend with different governmental systems. Examples include democracies, authoritarian governments, and monarchies. Some governments are easier to work with than others. Democracies, for example, are answerable to their citizens and the rule of law.

Authoritarian regimes are usually answerable to no one, including the law. It is less risky to conduct business in democracies and constitutional monarchies, a monarchy with a constitution that protects the public and subjects the monarch to the rule of law, than in countries with authoritarian regimes.

The next major factor is trade agreements. Countries often enter into trade agreements to help facilitate trade between them. If your country has entered into a trade agreement with another country, conducting business in that country will usually be easier and less risky because the trade agreement will provide some predictability and protection. One great advantage, for example, is that your products will be subjected to fewer trade barriers that serve as obstacles to exporting your products into the country.

Horizontal integration

Horizontal integration is another competitive strategy that companies use. An academic definition is that horizontal integration is the acquisition of business activities that are at the same level of the value chain in similar or different industries.

In simpler terms, horizontal integration is the acquisition of a related business: a fast-food restaurant chain merging with a similar business in another country to gain a foothold in foreign markets.

Enterprise business integration is much more than any one approach or collection of approaches to integration concerns. Applying the most appropriate approach or solution demands a systematic way of looking at integration opportunities and responses.

There are many integration issues an enterprise faces today. Most of us can relate to the few that are listed below:

Data is scattered among a number of databases, data warehouses and datamarts.
Rewrite of applications is costly and time consuming.
Changes in strategy and direction of the enterprise come at an increasing pace.
Changes are enterprise wide and not limited to a single product, operating unit or location.
Management is faced with multiple choices of investment in integration.
Integration options are increasingly expensive with large investments needed in infrastructure, processes, applications, and data management.

Bi–Directional Integration

There is an orderly way we can look at the integration landscape to help sort out the approaches and solutions. Integration has been addressed from two directions in the enterprise often eachunaware of the other. One direction is driven by the business strategy and strategy execution such as a merger, acquisition, consolidation, expansion etc. The other is driven by operational needsand is technology driven such as data access, application interfaces, process renovation and others. Not coordinating the two directions can be costly for an enterprise in terms of time and money.
It is like a rail track starting at each end of a country and not meeting in the middle.

We call the business driven/technology driven pairing a ‘bi-directional’ view of business integration. It takes into account the two major directions of integration and attempts toorganize them into a simple framework with a set of layers to help determine the situation and approach most appropriate for your enterprise. The diagram below shows the layers of integration andthe two directions. We have observed five basic layers going from purely technology oriented to purely business oriented. Both of these are going on at the same time in the enterprise. The motivesfor each direction are different:

Business Driven – Outward focused as a response to the business environment. This is usually a business need looking for an enablement technology.
Technology Driven – Inward focused as a response to operational pressures. Often a solution looking for a business justification.
The business oriented top layer may have very little to do with technology. This level is featured by strategic business actions such as merger, acquisition, consolidation etc. It is the result ofthe response an enterprise makes to the forces in the economy, market, industry and government.

This approach is effectiveness driven, that is, it answers the question ‘are we delivering theright products to the marketplace?’ Integrating a business is not the same as integrating technologies but some of the principles are common to all layers of integration.

The Layers of Integration

Business Integration – The key effort here is the restructuring of the enterprise from a business perspective. The use of technology is of secondary consideration.

The concern is about integrating processes, locations, and product lines, infrastructure, intellectual property, markets, and production and delivery operations, catalogues and so on. These are all‘pure’ business things and only impact IT when there is a need for integration of infrastructure such as used in the delivery of financial data. The techniques used involve enterpriseanalysis and do not involve IT based methodologies.

Partner Integration – This layer addresses linkage to enterprise partners including suppliers, customers, investors, analysts, interested parties, potentialcustomers and employees. While it may seem strange that an employee would be considered a partner it is reality that employees have both an internal and external view of their enterpriseparticularly when it involves remote access such as for sales or technical support. Architecture and requirements are critical to this layer with an understanding of the goals and objectives of thestakeholders. IT enablement begins to take on importance at this layer as the means of delivering data, knowledge and information. At this layer, IT methodologies are blended with enterpriseanalysis approaches to get a linkage between the business view and the technology enablement.

Content Integration – Content integration pulls together intellectual property from many sources and displays the results to interested parties. In some cases they
are power users inside the enterprise and in other cases they are external users that are looking for support information such as catalogues, product sheets, maintenance data, parts and replacementinformation, service manuals, operations manuals and other bounded knowledge domains. New types of requirements articulation and tools are needed here. Methods to identify the knowledgerequirements (e.g. essential knowledge identification) are needed with the capability to convert them to delivered functionality for users.

Application Integration – The intent of application integration is to provide access to functionality across multiple applications or processing data across severalapplications. There are a number of integration strategies for applications depending on the scope and reach of the

requirements. The concepts of scope and reach are importantto integration. If the scope includes only two applications then pair-wise integration is used. If the scope is three or more applications then a strategy of logic, data and functionality
Encapsulation come into play. If the scope of the integration is within a small area of the enterprise such as a single operating unit or location, then there is high likelihood of success. If the
scope is across many operating units then other factors will impact the effort such as company politics, conflicting business objectives, competitive technology strategies, executive incentives and
many more that have little to do with integration. Reach is a very different idea. It relates to the architecture of the enterprise, both business and IT architectures. If the impact of the
integration effort changes the business or IT architecture dramatically then the reach risk is very high and there is a likelihood of failure. If the reach risk is low, that is, the architecture
will not change much, then the likelihood of success is high. Clearly an alignment approach is needed to determine if the scope and reach will place the enterprise at risk in its integration efforts.

Data Integration – This is the core integration approach in many enterprises today. Managing data well and achieving data integration go together. The need to manage
data carefully varies among types of enterprises. Data purveyors (firms that sell data about consumer purchases, how many people watching television programs, who sees which kind of movies and so
on) have a very high need for quality metadata, efficient data management, and consistent quality of data. Hence they do considerable data cleanup, completion and management. Manufacturing firms)

FUNCTIONS OF THE INTERNATIONAL MANAGER

Global competition has forced businesses to change how they manage at home and abroad. The increasing rate of change, technological advances, shorter product life cycles, and high-speed communications are all factors that contribute to these changes. The new management approach focuses on establishing a new communication system that features a high level of employee involvement. Organizational structures must also be flexible enough to change with changing market conditions. Ongoing staff development programs and design-control procedures, which are understandable and acceptable, are outcomes from this new approach. Management values

are changing, and managers must now have a vision and be able to communicate the vision to everyone in the firm.

Although the international manager performs the same basic functions as the domestic manager, he must adjust to more variables and environments. Therefore, each of the five basic management functions must change when operating in a foreign market.

Planning

The first stage of international planning is to decide how to do business globally: whether to export, to enter into licensing agreements or joint ventures, or to operate as a multinational corporation with facilities in a foreign country.

To develop forecasts, goals, and plans for international activities, the manager must monitor environments very closely. Key factors include political instability, currency instability, competition from governments, pressures from governments, patent and trademark protection, and intense competition.

Organizing

International firms should be sure that their plans fit the culture of the host country. Typically, U.S. firms feel that long-term plans should be three to five years in length; but in some cultures, this time period is too short. Many countries must plan with the assistance of governmental agencies. And working through bureaucratic structures, policies, and procedures is often time-consuming.

International businesses must be organized so that they can adapt to cultural and environmental differences. No longer can organizations just put “carbon copies” or clones of themselves in foreign countries. An international firm must be organized so that it can be responsive to foreign customers, employees, and suppliers. An entire firm may even be organized as one giant worldwide company that has several divisions. Above all, the new organization must establish a very open communication system where problems, ideas, and grievances can quickly be heard and addressed at all levels of management. Without this, employees will not get involved, and their insights and ideas are crucial to the success of the business.

As an organization extends its operations internationally, it needs to adapt its structure. When the organization increases its international focus, it goes through the following three phases of structural change:

Pre-international stage. Companies with a product or service that incorporates the latest technology, is unique, or is superior may consider themselves ready for the international arena. The first strategy used to introduce a product to a foreign market is to find a way to export the product. At this phase, the firm adds an export manager as part of the marketing department and finds foreign partners.

International division stage. Pressure may mount through the enforcement of host country laws, trade restrictions, and competition, placing a company at a cost disadvantage. When a company decides to defend and expand its foreign market position by establishing marketing or production operations in one or more host countries, it establishes a separate international division. In turn, foreign operations begin, and a vice president, reporting directly to the president or CEO, oversees the operations.

Global structure stage. A company is ready to move away from an international division phase when it meets the following criteria:

The international market is as important to the company as the domestic market.

Senior officials in the company possess both foreign and domestic experience.

International sales represent 25 to 35 percent of total sales.

The technology used in the domestic division has far outstripped that of the international division.

As foreign operations become more important to the bottom line, decision making becomes more centralized at corporate headquarters. A functional product group, geographic approach, or a combination of these approaches should be adopted. The firm unifies international activities with worldwide decisions at world headquarters.

Staffing

Because obtaining a good staff is so critical to the success of any business, the hiring and development of employees must be done very carefully. Management must be familiar with the country's national labor laws. Next, it must decide how many managers and personnel to hire from the local labor force and whether to transfer home-based personnel.

For example, U.S. firms are better off hiring local talent and using only a few key expatriates in most cases, because the costs of assigning U.S.–based employees to positions overseas can be quite expensive. Simply, expatriates (people who live and work in another country) are expensive propositions even when things go well. Adding up all the extras—higher pay, airfare for family members, moving expenses, housing allowances, education benefits for the kids, company car, taxes, and home leave—means that the first year abroad often costs the multinational company many times the expatriate's base salary. The total bill for an average overseas stay of four years

can easily top $1 million per expatriate. In any case, managers need to closely examine how to select and prepare expatriates.

Directing

Cultural differences make the directing function more difficult for the international manager. Employee attitudes toward work and problem solving differ by country. Language barriers also create communication difficulties. To minimize problems arising from cultural differences, organizations are training managers in cross-cultural management. Cross-cultural management trains managers to interact with several cultures and to value diversity.

In addition, the style of leadership that is acceptable to employees varies from nation to nation. In countries like France and Germany, informal relations with employees are discouraged. In Sweden and Japan, however, informal relations with employees are strongly encouraged, and a very participative leadership style is used. Incentive systems also vary tremendously. The type of incentives used in the U.S. may not work in Europe or Japan, where stable employment and benefits are more important than bonuses.

Controlling

Geographic dispersion and distance, language barriers, and legal restrictions complicate the controlling function. Meetings, reporting, and inspections are typically part of the international control system.

Controlling poses special challenges if a company engages in multinational business because of the far-flung scope of operations and the differing influences of diverse environments. Controlling operations is nonetheless a crucial function for multinational managers. In many countries, bonuses, pensions, holidays, and vacation days are legally mandated and considered by many employees as rights. Particularly powerful unions exist in many parts of the world, and their demands restrict managers' freedom to operate.