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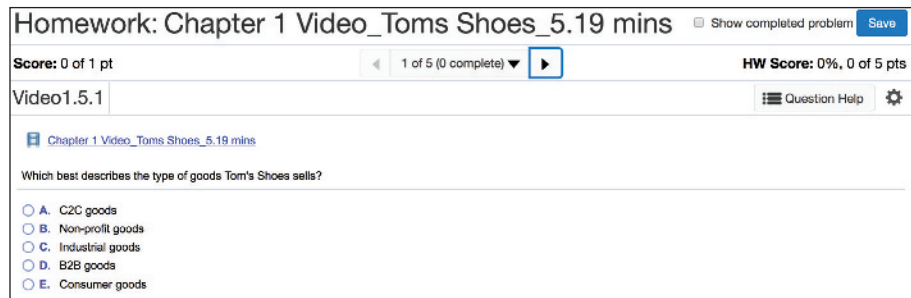
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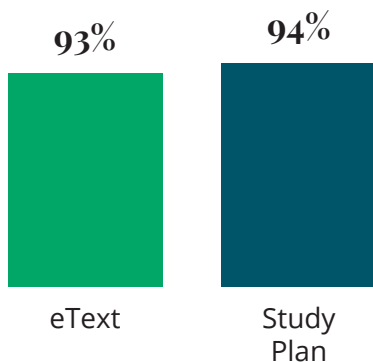
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International Business

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International Business

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Dedicated to...

This book is dedicated to all those who feel passionate about cross-border business, our readers around the world. I trust that this edition will inspire and help you discover the magic of international business. Since any journey is much more rewarding when you are accompanied by others, I also dedicate this edition to my students of four decades whom I had the opportunity to mentor over the years.

S. Tamer Cavusgil
Atlanta, Georgia

This book is dedicated to my wife, Mari, for her intellect, patience, and adventurous spirit; to Bill and Audrey, and to Hiroshi and Hisako, for being great parents and role models; and to the many students I have had the good fortune to influence over the years.

Gary Knight
Salem, Oregon

This book is dedicated to my parents, Richard and Marie Riesenberger, for their example, many sacrifices, and love. To my wife and best friend, Pat, for her enthusiasm and loving support. To my daughters, Chris and Jen, of whom I am so very proud and thankful. To Byron, Ann-Marie and Terry, who enrich my life. To my amazing grandchildren, Ryan, Paige, Ethan, and Emma—the future of the New Realities.

John R. Riesenberger
Scottsdale, Arizona

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Preface

New to This Edition

Our aim is to keep the text fully up-to-date and at a reasonable length. Thus, we have dropped some items and added new ones. From Chapter 1, we dropped the Opening Case on Facebook. From Chapter 4, we dropped the Closing Case on Bribery and Corruption at Siemens. From Chapter 4, we dropped the Closing Case on Bribery and Corruption at Siemens. From Chapter 5, we dropped the Closing Case on Hyundai and the Global Auto Industry. From Chapter 6, we dropped the Opening Case on Risks in Russia's Political and Legal Systems. From Chapter 9, we dropped the Closing Case on Financial Contagion and the Global Financial Crisis. From Chapter 17, we dropped the Opening Case on International Human Resource Management at Johnson & Johnson.

To replace the above dropped items and maintain currency, we have created new or greatly revised opening and closing cases in the fifth edition of Cavusgil, Knight, and Riesenberger (CKR 5e) as follows:

Chapter 1: A new Opening Case on *Instagram: A Global Phenomenon*

Chapter 2: A heavily revised Opening Case on *Spotify and the Rise of Born Global Firms*

Chapter 4: A new Closing Case on the recent *Scandal at Volkswagen*

Chapter 5: A new Closing Case on *Unilever's Comparative and Competitive Advantages*

Chapter 6: A new Opening Case on *Odebrecht and Risks in Brazil's Political and Legal Systems*

Chapter 7: A heavily revised Closing Case on *Government Intervention at Airbus and Boeing*

Chapter 8: A heavily revised Closing Case on *Tata Group: India's Top Global Challenger*

Chapter 9: A new Closing Case on *Tesco, the European Debt Crisis, and Brexit*

Chapter 15: A heavily revised Closing Case on *Subway and the Challenges of Franchising in China*

Chapter 16: A heavily revised Opening Case on *Michael Kors: The Global Affordable Luxury Market*

Chapter 17: A new Opening Case on *International Human Resource Management at Google*

In addition, for our feature *You Can Do It: Recent Grad in IB*, we have added new biographies of young graduates with careers in international business. In Chapter 1, we added *Mary Lyles*, who works in global sourcing for Starbucks; and in Chapter 15, we added *Juanita Velez*, who works in international social media at Delta Air Lines.

In various chapters, we also added several new exhibits and significant new material on such contemporary topics as preparing for international travel, the rise of digital technologies, the trade and GDP growth relationship, the meaning of colors worldwide, workplace harassment, Brexit and the UK, populism, national governance, blockchain and cryptocurrencies, carbon taxes, cross-national project management, the Global Connectedness Index, global sourcing for smartphones, reshoring and nearshoring, the best global companies to work for, and women in international business, among numerous others.

Solving Teaching and Learning Challenges

Today's students—often called Generation Z, Post Millennials, or the iGen—have grown up in a constantly connected world. To address the unique wants, needs and learning style of Generation Z students, we have designed CKR 5e to emphasize the following features:

- **Visual learning.** CKR 5e emphasizes interactive media and videos as well as exhibits, maps, and other visual learning aids. The MyLab Management provides access to a wide variety of additional visual resources.
- **Relevant knowledge and job-related skills.** CKR 5e includes more relevant examples and activities, concise foundational course content, Intangible Soft Skills, and Tangible Process Skills that prepare Generation Z students for the work world.

- **Contemporary issues that matter to Generation Z.** CKR 5e emphasizes the new international business environment, in-depth coverage of contemporary international business topics such as emerging markets, developing economies, growth of the service sector, risks in international business, digital technologies, women in international business, and other important trends.
- **Meaningful content.** CKR 5e provides substantial content on ethics, corporate social responsibility, and sustainability in international business.
- **Digital platform.** Generation Z learners prefer content that they can read or access digitally at a time and place of their choosing. Digital learning enhances engagement, self-pacing, and the ability to customize content to individual needs. Digital platforms help ensure timely, up-to-date content and the ability to collaborate with peers. In these and other ways, CKR 5e provides such digital options. To improve Generation Z students results, we recommend pairing the text content with MyLab Management, which is the teaching and learning platform that empowers you to reach every student. By combining trusted author content with digital tools and a flexible platform, MyLab personalizes the learning experience and will help your students learn and retain key course concepts while developing skills that future employers are seeking in their candidates. From Mini Sims to Personal Inventory Assessments, MyLab Management helps you teach your course, your way. Learn more at www.pearson.com/mylab/management.

Some of the main features of the textbook and MyLab are as follows:

HIGHLY ACCESSIBLE WRITING AND EXPLANATIONS THAT ENGAGE STUDENTS. Opening and closing cases appeal to students, featuring firms and subjects such as Apple, IKEA, Harley-Davidson, H&M, Instagram, born global firms, social media in China, and the global movie industry. The content stimulates student desire to learn more about international business.

Constantly fluctuating exchange rates require international managers to keep in mind three facts:

- The prices the firm charges can be quoted in the firm’s currency or in the currency of each foreign customer.
- Because several months can pass between placement and delivery of an order, fluctuations in the exchange rate during that time can cost or earn the firm money.
- The firm and its customers can use the exchange rate as it stands on the date of each transaction, or they can agree to use a specific exchange rate.

MORE EXERCISES AND ACTIVITIES THAT ENABLE STUDENTS TO ACQUIRE CRITICAL THINKING AND PROBLEM-SOLVING SKILLS. CKR 5e contains 174 exhibits (about three times more than leading competitors). Students like exhibits because they help clarify complex material and facilitate reading the chapters.

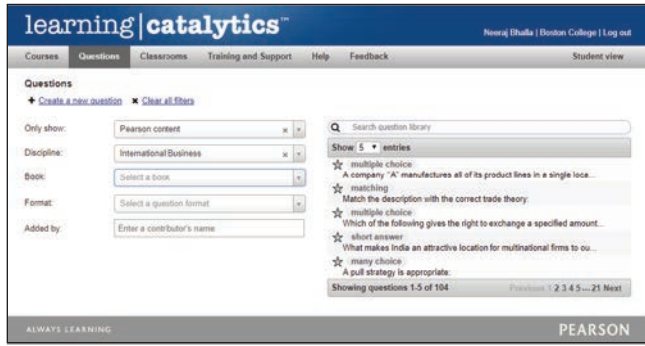
TANGIBLE PROCESS TOOLS. They are designed to simulate real-world decision making that will help increase effectiveness in the workplace.

GROUP PROJECT ON INTERNATIONAL CORPORATE SOCIAL RESPONSIBILITY. CKR 5e contains a comprehensive activity in which students debate corporate social responsibility (CSR) in international business. In this extended exercise, located in the *Instructor’s Manual*, students debate the merits and consequences of CSR as executives, consumers, or activists.

YOU CAN DO IT—RECENT GRAD IN IB BIOGRAPHIES. CKR 5e offers eleven biographies of actual university graduates who have embarked on fascinating careers in international business. These biographies include comments concerning the specific intangible soft skills that have helped them be successful in work.

You Can Do It	RECENT GRAD IN IB
	<p>TERRANCE ROGERS</p> <p>Terrance’s Majors: Finance and international business</p> <p>Objectives: Exploration, international perspective, self-awareness, career growth, and learning about foreign markets</p> <p>Internships during college: Deutsche Bank</p> <p>Jobs held since graduating:</p> <ul style="list-style-type: none"> • Business analyst at Deutsche Bank, New York • Management associate at Deutsche Bank, New York • Executive management rotation at Deutsche Bank, New York • Executive management associate at Deutsche Bank, London and New York

LEARNING CATALYTICS™. With this tool, you'll hear from every student when it matters most. You pose a variety of questions that help students recall ideas, apply concepts, and develop critical-thinking skills. Your students respond using their own smartphones, tablets, or laptops.



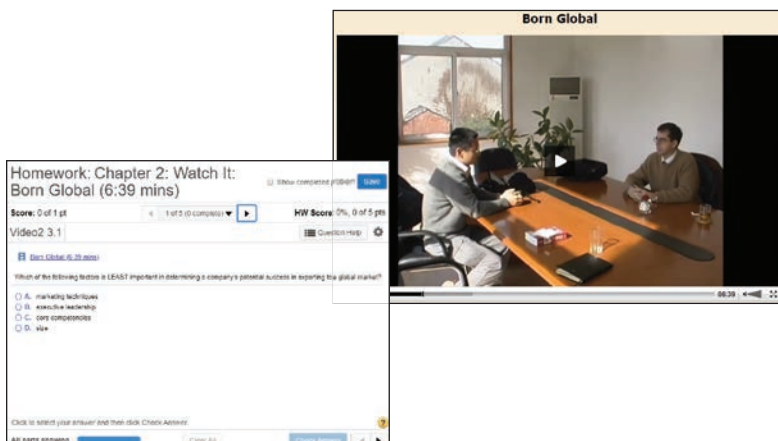
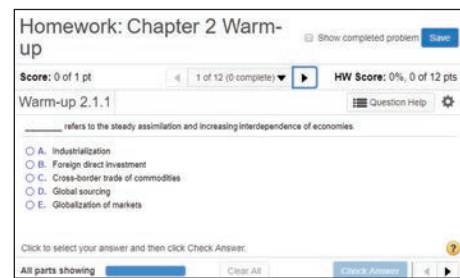
NEW MINI SIMS. Mini Sims put students in professional roles and give them the opportunity to apply course concepts and develop decision-making skills through real-world business challenges.

The simulations use each student's decisions to create various scenario paths that help them understand the impact their decisions can have on an organization.

These branching Mini Sims strengthen a student's ability to think critically, help students understand the impact of their decisions, engage students in active learning, and provide students with immediate feedback on their decisions.

Each decision point remediates to the Learning Objective in the eText.

CHAPTER WARM-UP. These questions help you hold your students accountable for learning key concepts in each chapter before coming to class.



VIDEOS EXERCISES. Engaging Videos explore a variety of business topics related to the theory students are learning in class.

Exercise Quizzes assess students' comprehension of the concepts in each video.



Developing Employability Skills

The Association to Advance Collegiate Schools of Business (AACSB) International increasingly advocates a more skills-oriented, practical approach in business books, which this text provides, rather than a theory-based approach.

For students to succeed in a rapidly changing job market, they should be aware of their career options and how to develop various critical skills. In this book and MyLab Management, we focus on developing these skills.

The CKR 5e Career Preparation Kit™ incorporates CKR Tangible Process Tools™ as well as CKR Intangible Soft Skills™, which constitute guidelines of the Association to Advance Collegiate Schools of Business (AACSB). CKR Intangible Soft Skills focus on the skills employers have identified as needed for employability and success in the marketplace today. The CKR Tangible Process Tools will help students increase their effectiveness in the workplace.

The Employability Skills Table below provides students with a guide to features that support the development of skills employers are looking for in today’s business graduates, helping students to see from the start of class the relevance of the course to their career goals. This table identifies which features and end-of-chapter materials will help students to develop these skills.

Employability Skills Table			
Skills	Sections in the text and MyLab covering these skills		
Written and oral communication	Global Edge Internet Exercises - End of chapter box element	Test Your Comprehension - Chapter End exercises	EOC Writing Assignment - MyLab Management
Critical thinking and problem solving	Chapter Opening and Chapter Closing Cases	Apply Your Understanding - short, essay-style questions at the end of the chapter	New Mini Sims - MyLab Management
Teamwork and collaboration	Chapter Opening and Chapter Closing Cases	Apply Your Understanding - short, essay-style questions at the end of the chapter	
Leadership	Chapter 11, “Strategy and Organization in the International Firm”		
Creativity	Apply Your Understanding	Chapter Opening and Chapter Closing Cases	
Ethics	Chapter 4, “Ethics, Corporate Social Responsibility, Sustainability, and Governance in International Business”	Chapter 4 Watch It Video Exercises - MyLab Management	
Information technology skills	Global Edge Internet Exercises - End of chapter box element		

OPENING CASE. Each chapter begins with a brief case study that illustrates chapter topics and asks key questions about real-world companies and situations covered in the case.

CLOSING CASE. Every chapter closes with an extensive case study that addresses the learning objectives highlighted in the chapter. The cases help students build managerial skills by applying chapter material to a situation faced by real-world managers. Questions accompany the case for assignment as homework. Class discussion helps students sharpen their analytical and decision-making skills.

TEST YOUR COMPREHENSION. A list of 6 to 12 short questions assesses student learning of chapter learning objectives and other chapter concepts.

APPLY YOUR UNDERSTANDING. An additional collection of three short, essay-style questions aims to have students apply chapter material to real-world international business practice.

CLOSING CASE Internationalization at Harley-Davidson

Considered an American icon by many, Harley-Davidson (Harley) is a U.S. motorcycle manufacturer founded in 1903 and offers 32 models through a network of about 1,500 dealers. Its global motorcycle revenue was about \$6 billion in 2017, continuing a three-year downward trend. Total sales have been relatively flat since 2012, with U.S. sales declining and international sales rising. Harley earns about two-thirds of its total sales in the United States, where it also manufactures almost all its bikes to support its brand image and quality control. The firm is embarked on a course to build the next generation of Harley riders globally; international markets are crucial to the firm's survival and growth. The CEO recently announced a bold goal to grow international sales to 50 percent of annual volume by 2027.

Harley is the only U.S.-based global motorcycle manufacturer and makes four distinctive groups of models:

- **Standard:** Practical bikes used for low-cost commuting
- **Performance:** Sleek, sport-style racing bikes built for speed and easy handling
- **Custom:** Stylized bikes customized to customer tastes
- **Touring:** Long-distance, large-capacity, comfort bikes that typically include cruise control, stereos, and luggage racks

quality management and empowered its production workers. Management increased marketing efforts, improved the dealer network, and undertook various cross-branding ventures. By the mid-1990s, management had repositioned Harley more strongly in the performance motorcycle market. The enhancements paid off in sharp improvements in company image and sales. However, the volume of Harley motorcycle shipments peaked in 2006. Shipments flattened or declined during the global financial crisis and ensuing recession and still had not recovered by 2018.

International Expansion

Harley management resolved that future success would come from expansion into foreign markets. The firm had established a distribution network and local subsidiary in Japan, and by 2016, it was selling more than 16,000 motorcycles annually. It continued to sell heavyweight motorcycles in Japan at a price of more than \$20,000, substantially more than Honda's standard lightweight model. Harley's foreign saw a sustained growth.

Harley also made inroads in Europe, a vast marketplace and home to dozens of countries with diverse needs and tastes. In Europe, performance bikes are the top seller by far, accounting for more than one-third of Harley sales, followed by touring, standard



INTERNET EXERCISES

Access globalEDGE™ at www.globalEDGE.msu.edu

AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Information Technology, Application of Knowledge, Diverse and Multicultural Work Environments, Written and Oral Communication, Analytical Thinking and Reflective Thinking

Knowledge Portal

globalEDGE™ is a leading knowledge portal for professionals in international business. It is a gateway to specialized knowledge on countries, international business transactions, culture, and firm practice. globalEDGE™ was developed at Michigan State University under the direction of Professor S. Tamer Cavusgil. Consult the globalEDGE™ portal to complete the Internet exercises at the end of each chapter.

1-20. You can gain valuable insights into international business by examining how countries compare to each other. Various research groups and international agencies systematically examine economic, political, and other features of nations. Visit globalEDGE™ Tools and Data, scroll down, and click Interactive Rankings. Select Countries. You will find dozens of criteria ranking countries based on GDP per capita; Education—literacy rate; People—population total; People—population density; Health—mortality rate; Energy—electricity production; Infrastructure—mobile cellular subscriptions; Infrastructure—roads, total network; Trade and Investment—foreign direct investment net inflows; and many other factors. Choose the ranking criteria that interest you most, and then examine the following three countries: Germany, India, and South Africa. Based on your analysis, explain why they rank where they do. Do

their relative positions make sense to you? Does each country seem like a good place to do business? Why or why not? **Hint:** Evaluate countries on a per-capita basis by dividing each criterion by the country's population.

1-21. In this chapter, we reviewed the four major risks that firms face in international business: cross-cultural risk, country risk, currency risk, and commercial risk. Identify one or more countries that interest you, and then visit globalEDGE™ and research the countries to uncover examples of each of the four types of risks. For example, China is characterized by various cultural differences and a national government that tends to intervene in business. Research by entering the country name in the search engine. Visit Global Insights and Market Potential Index. Illustrate each risk with examples.

1-22. You have recently been hired by a smaller firm that is beginning to expand internationally. When first starting out, most firms choose exporting as their main foreign market entry strategy. However, no one in your firm knows how to conduct exporting. Therefore, your boss has given you an assignment: Prepare a presentation for your coworkers on how to engage in exporting. Using globalEDGE™, find and review Guide to Exporting, which you can use to create your presentation.

GLOBALEDGE INTERNET EXERCISES. GlobalEDGE™ (<https://globaledge.msu.edu>) was developed by CKR author S. Tamer Cavusgil and is the leading knowledge portal for professionals in international business. It provides a gateway to specialized knowledge on countries, cross-border ventures, culture, and company practice. Each chapter provides several globalEDGE exercises as the basis for student assignments and projects.

CKR TANGIBLE PROCESS TOOLS™. These practical exercises familiarize students with key managerial challenges and decision making that professionals typically encounter in international business. By completing CKR Tangible Process Tools™ exercises, students can acquire real-world skills that will help them perform better in their careers.

CKR Tangible Process Tools™

What is a CKR Tangible Process Tool Exercise?

CKR Tangible Process Tools consist of practical exercises and work processes designed to familiarize you with key managerial challenges and decisions that professionals typically encounter in international business. Completing CKR Tangible Process Tool exercises in this text enables you to acquire practical, real-world work processes that will improve employability and success in the workplace. Each exercise presents a managerial challenge in a real-world scenario, the skills you will acquire in solving the exercise, and a methodology and the resources to use in solving it. The second half of the exercise is provided at the Pearson MyLab Management website (www.pearson.com/mylab/management).

AACSB TAGGING. This book and MyLab Management support AACSB international accreditation. In every chapter, after each section of questions, specific AACSB tagging is provided to help instructors identify which AACSB Intangible Soft Skills that activity supports. AACSB tagging is also part of all questions in the Test Item File that accompanies the book.

Instructor Teaching Resources

At the Instructor Resource Center, www.pearsonhighered.com, instructors can easily register to gain access to a variety of instructor resources available with this text in downloadable format. If assistance is needed, our dedicated technical support team is ready to help with the media supplements that accompany this text. Visit <https://support.pearson.com/getsupport> for answers to frequently asked questions and toll-free user support phone numbers.

Supplements available to instructors at www.pearsonhighered.com/irc	Features of the Supplement
Instructor’s Resource Manual authored by Marta Szabo White, S. Tamer Cavusgil, Gary Knight, and John Riesenberger	<ul style="list-style-type: none"> • Chapter-by-chapter summaries • Examples and activities not in the main book • Teaching outlines • Teaching tips, including openers to help launch lectures • Solutions to all questions and problems in the book
Test Bank authored by John Capela	1,600 multiple-choice, true/false, short-answer, and essay questions with the following annotations: <ul style="list-style-type: none"> • Difficulty level (1 for straight recall, 2 for some analysis, 3 for complex analysis) • Type (multiple-choice, true/false, short-answer, essay) • Learning objective • AACSB learning standard (Written and Oral Communication, Ethical Understanding and Reasoning, Analytical Thinking, Information Technology, Interpersonal Relations and Teamwork, Diverse and Multicultural Work Environments, Reflective Thinking, and/or Application of Knowledge)
TestGen® Computerized Test Bank	TestGen allows instructors to: <ul style="list-style-type: none"> • Customize, save, and generate classroom tests • Edit, add, or delete questions from the Test Item Files • Analyze test results • Organize a database of tests and student results
PowerPoints Presentations authored by S. Tamer Cavusgil, Gary Knight, and John Riesenberger	<ul style="list-style-type: none"> • Cover all concepts, explanations, and major examples in each chapter • Include all exhibits in the textbook • Meet accessibility standards for students with disabilities. Features include, but not limited to: <ul style="list-style-type: none"> <input type="checkbox"/> Keyboard and Screen Reader access <input type="checkbox"/> Alternative text for images <input type="checkbox"/> High color contrast between background and foreground colors
Image Library	<ul style="list-style-type: none"> • A collection of photos and other images for use in enhancing PowerPoints and other teaching materials related to CKR 5e

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John is an accomplished author, consultant, and international executive with senior executive positions in major pharmaceutical firms, biotechnology firms, and pharmaceutical agencies. John’s international business career spans more than three decades in the global pharmaceutical industry. He has conducted business transactions in 22 countries.

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He worked for 30 years with Pharmacia & Upjohn and The Upjohn Company as a senior international executive. His experience covered a diverse range of divisional, geographic, and functional accountabilities. His most recent position was as vice president of Global Business Management. He also served as corporate vice president and chief commercialization officer for a biotechnology firm and as the executive vice president of a pharmaceutical science agency.

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Chapter

1

Introduction: What Is International Business?

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

- 1.1 Describe the key concepts in international business.
- 1.2 Understand how international business differs from domestic business.
- 1.3 Identify major participants in international business.
- 1.4 Describe why firms internationalize.
- 1.5 Appreciate why you should study international business.
- 1.6 Learn the CKR Intangible Soft Skills™ and the CKR Tangible Process Tools™ to improve your employability and success in the workplace.

Instagram: A Global Phenomenon

Globalization refers to ongoing economic integration and growing interdependency of countries worldwide. It implies rising economic, political, and personal interconnectedness among countries, companies, and consumers. Widespread adoption of smartphone apps like Facebook and Instagram exemplifies globalization and converging lifestyles around the world. The number of smartphone users worldwide has reached 3 billion, about 40 percent of world population. Smartphone ownership is common in the advanced economies—especially in Australia, Europe, and North America—where 65 percent of residents own such devices. The phones are increasingly popular in emerging markets—countries such as Chile, China, Poland, and Russia—where the ownership rate is more than 50 percent. Developing economies—countries such as Bangladesh, Nigeria, Pakistan, and Ukraine—have low

smartphone penetration rates, mainly due to lower incomes and underdeveloped infrastructure.

Founded in 2010, Instagram is a photo- and video-sharing network that smartphone owners use to share photos and short videos with others. The site has more than 700 million active monthly users, the majority of whom are women, and most are under age 35. Instagram was acquired by Facebook in 2012 for about US\$1 billion.

Available in 33 languages, Instagram has a dual identity—a for-profit business *and* a vehicle for our personal lives. Instagram is the sixth most popular social media platform worldwide, after Facebook, Twitter, LinkedIn, YouTube, and Google+. Instagram emphasizes sharing photographs and enjoys a very enthusiastic following from visually oriented social media users. The app is popular worldwide, especially in countries like Russia,



Source: Dmytro Kosmenko/123rf

Brazil, Turkey, the United Kingdom, Poland, and the United States.

Instagram is a truly global platform—more than 80 percent of users are outside the United States, where the app is based. Management has used foreign direct investment to establish offices around the world. The most photographed countries among Instagram users are Italy, Japan, Indonesia, Kuwait, Thailand, and France. Tourist destinations such as Rome, Kyoto, Dubai, Paris, and the Grand Canyon are popular subjects. Pizza is the most Instagrammed food, followed by sushi.

The Instagram platform allows people to take and share high-quality photographs using low-resolution phones, which appeals to users in less-developed economies. Users in such countries often cannot afford sophisticated phones or access fast cellular networks that allow conveniently downloading the Instagram app. Many lack enough phone storage to easily download the

app. To get around these problems, Instagram launched an expanded web version that allows users to skip the app's wait time, data costs, and storage needs while still providing basic functionality.

Retailers and other companies leverage Instagram to market their products and services at low cost. Instagram first launched advertising, along with its photo feed, to subscribers in Australia, Canada, and the United Kingdom in 2014. Most of the world's top brands—for example, Apple, BMW, and Sony—have established Instagram pages, and many actively share photos or videos every week. Today, Instagram earns more than \$5 billion in annual advertising revenue worldwide.

German sportswear company Puma contracts with Instagrammers who have many followers to capture photos that showcase the firm's products. The Danish brewing company Carlsberg launched a marketing strategy called "Happy Hour" that offers half-priced beers in

exchange for Instagram posts. In Japan, Instagram's most popular influencer is a dog, Marutaro, who promotes pet food, real estate, and other ventures through the app. Sports teams use Instagram to promote themselves in Brazil. The Instagram phenomenon illustrates how converging lifestyles, communications technology, and imaginative entrepreneurship are facilitating the emergence of global enterprises.

AACSB and CKR Intangible Soft Skills to improve employability and success in the workplace: Written and Oral Communication, Reflective Thinking and Application of Knowledge

Questions

- 1-1.** What advantages does Instagram obtain from doing business in international markets?
- 1-2.** What attributes of Instagram have allowed it to gain rapid acceptance in countries around the world?
- 1-3.** How do companies use Instagram to market their products and services?

SOURCES: B. Ahmadinejad and H. Asli, "E-business through Social Media: A Quantitative Survey (Case Study: Instagram)," *International Journal of Management, Accounting and Economics*, 4, No. 1 (2017), www.ijmae.com; S. Aslam, "Instagram by the Numbers: Stats, Demographics & Fun Facts," *Omnicores*, August 10, 2017, www.omnicoreagency.com; J. Constone, "Instagram Launches Mobile Web Sharing to Pursue Global Growth," *Techcrunch*, May 8, 2017, <https://techcrunch.com>; E. Hamburger, "Instagram Shoots for Global Expansion with Big Android Update," *The Verge*, March 11, 2014, www.theverge.com; E. Hancock, "The 23 Most Instagrammed Countries of All Time," *Business Insider*, December 1, 2016; J. Hempel and A. Nyantakyi, "Instagram Is Ready to Take Its Shot," *Fortune International (Europe)*, July 21, 2014, pp. 72–77; S. Joseph, "Carlsberg Offers Drinkers Half-Priced Beers in Exchange for Instagram Posts," *Marketing Week*, March 17, 2014, www.marketingweek.com; Newzoo, "Top 50 Countries by Smartphone Users and Penetration," April 2017, <http://newzoo.com>; M. Swant, "This Instagram Timeline Shows the App's Rapid Growth to 600 Million," *Adweek*, December 15, 2016, www.adweek.com.

International business

Performance of trade and investment activities by firms across national borders.

As revealed in the opening case, international business touches our daily experiences. **International business** refers to firms' performance of trade and investment activities across national borders. Because it emphasizes crossing national boundaries, we also refer to international business as *cross-border business*. Firms organize, source, manufacture, market, and conduct other value-adding activities on an international scale. They seek foreign customers and engage in collaborative relationships with foreign business partners. Although international business is performed mainly by individual firms, governments and international agencies also conduct international business activities.¹ Firms and nations exchange many

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- *Written and oral communication*
- *Ethical understanding and reasoning*
- *Information technology*
- *Analytical thinking*
- *Diverse and multicultural work environments*
- *Reflective thinking*
- *Application of knowledge*
- *Interpersonal relations and teamwork*

Each chapter of CKR has been specifically designed to integrate and advance your learning of these intangible soft skills. End-of-chapter exercises—Test Your Comprehension, Apply Your Understanding, and globalEDGE Internet Exercises—help you develop these critical skills.

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Understanding and applying these tools will help you increase your effectiveness in the workplace. “Tangible Process Tools” appear at the end of selected chapters and consist of process tools that will enable you to address real-world challenges often encountered by managers in the workplace. Some of the tools consist of helpful checklists. Others will present a real-world management scenario, methodology, and the resources to solve it. Please visit the Pearson MyLab Management at www.pearson.com/mylab/management to access the “CKR: Travel Abroad Preparation Checklist™,” which will assist you in gathering necessary documents, as well as tools and aids for health care, telecommunications, funds, customs, and other requirements for visiting different countries.

For a more detailed treatment of this topic, visit the Pearson MyLab Management website (www.pearson.com/mylab/management).

physical and intellectual assets, including products, services, capital, technology, know-how, and labor. In this book, we are mainly concerned with the international business activities of the individual firm.

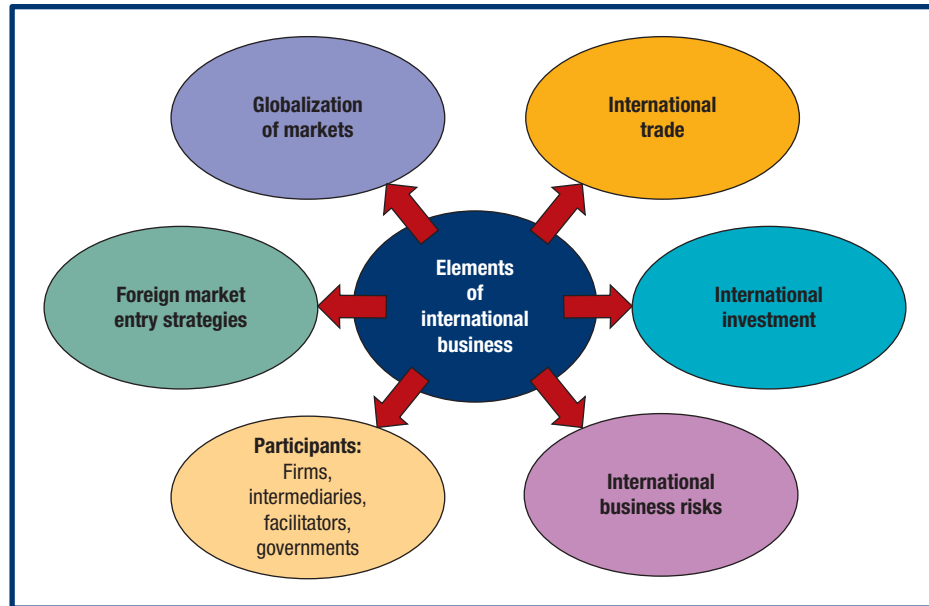
International business is characterized by six major dimensions, as shown in Exhibit 1.1. Firms' growing international activities give rise to the globalization of markets. As they venture abroad, firms undertake international trade and investment activities. In doing so, they encounter various types of risks and challenges that occur to a lesser degree, or not at all, in the home country. Participants in international business are diverse and include firms, distribution channel intermediaries, and facilitators. When they expand abroad, firms employ such international market entry strategies as exporting and direct investment. We explore each of the six dimensions in detail in this chapter.

Although trading across borders has been around for centuries, contemporary international business has gained much momentum and complexity over the past few decades. Firms seek international market opportunities more than ever before. Like Instagram, international business affects the everyday lives of people worldwide. Daily activities such as shopping, listening to music, watching a movie, or surfing the Internet involve interactions and transactions that connect you to the global economy. Internationalization of business gives you access to products and services from around the world. It profoundly affects your quality of life and economic well-being.

Online platforms such as Amazon, Alibaba, Facebook, and Instagram are all expressions of ongoing economic integration and growing interdependency of countries worldwide, known as the **globalization of markets**. Globalization is a macro-trend of intense economic interconnectedness among the nations of the world. A parallel trend is the ongoing internationalization of countless firms and dramatic growth in the volume and variety of cross-border transactions in

Globalization of markets

Ongoing economic integration and growing interdependency of countries worldwide.

EXHIBIT 1.1**Elements of International Business****Internationalization**

The tendency of *companies* to deepen their international business activities systematically.

goods, services, and capital flows. **Internationalization** refers to the tendency of companies to deepen their international business activities systematically. It has led to widespread diffusion of products, technology, and knowledge worldwide.

Globalization both compels and facilitates firms to expand abroad. Simultaneously, company internationalization has become easier than ever before. A few decades ago, international business was largely the domain of large, multinational firms. Recent developments have created a more level playing field that allows all types of firms to benefit from active participation in international business. In this book, you will read about the international activities of smaller firms and those of large, multinational enterprises. You will learn about companies in the services sector that are internationalizing in such industries as banking, engineering, insurance, and retailing.

The globalization of markets is evident in several related trends.

- *Unprecedented growth of international trade.* In 1960, cross-border trade was modest—about \$300 billion per year. Today, it accounts for a substantial proportion of the world economy, with world exports alone amounting to some \$16 trillion annually—that is, \$16,000,000,000,000!
- *Trade between nations, accompanied by substantial flows of capital, technology, data, and communications.* In 2004, total cross-border bandwidth in digital data transfer and communications was practically zero. Today, total cross-border bandwidth flows now exceed 400,000 gigabits per second. Virtually every type of international transaction now includes a digital component.
- *Development of highly sophisticated global financial systems and mechanisms* that facilitate the cross-border flow of products, money, technology, and knowledge.
- *Greater collaboration among nations* through multilateral agencies such as the World Trade Organization (WTO, www.wto.org) and the International Monetary Fund (IMF, www.imf.org).

Source: McKinsey Global Institute, *Digital Globalization: The New Era of Global Flows* (2016), www.mckinsey.com; UNCTAD, *World Investment Report*, New York: United Nations (2017), www.unctad.org; World Trade Organization, *World Trade Report*, Geneva: World Trade Organization (2017), www.wto.org.

What Are the Key Concepts in International Business?

International trade describes the exchange of products (merchandise) and services (intangibles) across national borders. Exchange can occur through **exporting**, the sale of products or services to customers located abroad from a base in the home country or a third country. Exchange also can take the form of **importing or global sourcing**—the procurement of products or services from suppliers located abroad for consumption in the home country or a third country. While exporting represents the outbound flow of products and services, importing is an inbound activity. Both finished products and intermediate goods (for example, raw materials and components) can be imported and exported.

International investment refers to the transfer of assets to another country or the acquisition of assets in that country. Economists refer to such assets as *factors of production*; they include capital, technology, managerial talent, and manufacturing infrastructure. Trade implies that products and services cross national borders. By contrast, investment implies that the firm itself crosses borders to secure ownership of assets located abroad.

The two essential types of cross-border investment are international portfolio investment and foreign direct investment. **International portfolio investment** refers to the passive ownership of foreign securities such as stocks and bonds to gain financial returns. It does not entail active management or control over these assets. The foreign investor has a relatively short-term interest in the ownership of these assets.

Foreign direct investment (FDI) is an internationalization strategy in which the firm establishes a physical presence abroad through acquisition of productive assets such as land, plant, equipment, capital, and technology. It is a foreign-market entry strategy that gives investors partial or full ownership of a productive enterprise typically dedicated to manufacturing, marketing, or management activities. Investing such resources abroad is generally for the long term and involves extensive planning.

The Nature of International Trade

Overall, export growth has outpaced the growth of domestic production during the past few decades, illustrating the fast pace of globalization. Exhibit 1.2 contrasts the growth of total world exports with the growth of total world *gross domestic product (GDP)* since 1980. GDP is defined as the total value of products and services produced in a country in the course of a year. As reflected in the exhibit, world trade declined in 2009 due to the global recession, following a 27-year boom. Trade revived and returned to normal levels by 2012. Trade was a key factor in reducing the impact of the global recession.² What is remarkable is that throughout most of the

1.1 Describe the key concepts in international business.

International trade

Exchange of products and services across national borders, typically through exporting and importing.

Exporting

Sale of products or services to customers located abroad from a base in the home country or a third country.

Importing or global sourcing

Procurement of products or services from suppliers located abroad for consumption in the home country or a third country.

International investment

The transfer of assets to another country or the acquisition of assets in that country.

International portfolio investment

Passive ownership of foreign securities such as stocks and bonds to generate financial returns.

Foreign direct investment (FDI)

An internationalization strategy in which the firm establishes a physical presence abroad through acquisition of productive assets such as capital, technology, labor, land, plant, and equipment.

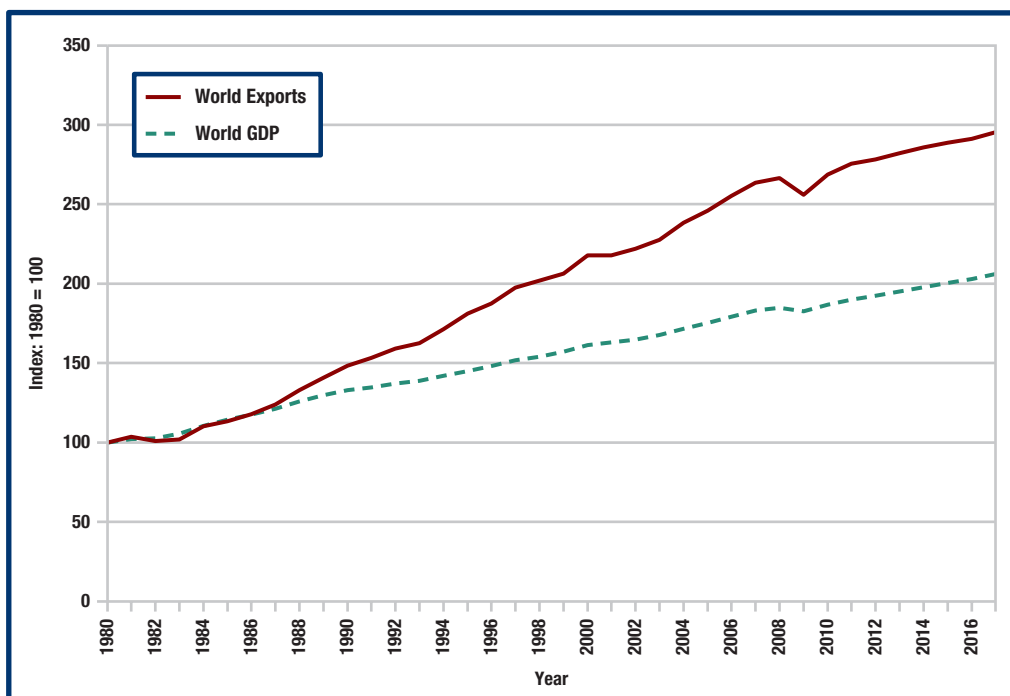


EXHIBIT 1.2

Comparing the Growth Rates of World GDP and World Exports

Source: Based on data from the International Monetary Fund, *World Economic Outlook Database October 2017*, www.imf.org.

past few decades, average annual growth rate in world exports has surpassed that of world GDP by a factor of almost two (5.3 versus 2.8 percent).

Three factors have been especially notable in explaining why trade growth has long outpaced GDP growth. First is the rise of emerging markets during the past three decades. These rapidly developing economies are home to swiftly growing middle-class households possessing substantial disposable income. Second, advanced (or developed) economies such as the United States and the European Union are sourcing many of the products they consume from such low-cost manufacturing locations as China, India, and Mexico. Third, advances in information and transportation technologies, decline of trade barriers, and liberalization of markets all have contributed to rapid growth of trade among nations.

Exhibit 1.3 identifies leading nations in exports of merchandise (and not services). Panel (a) shows the total annual value of merchandise exports and imports in billions of U.S. dollars. Panel (b) shows the annual value of products traded as a percentage of each nation's GDP. Total merchandise trade (exports plus imports) of the countries in panel (a) is nearly \$18,000 billion and accounts for about half of world merchandise trade. To get a better sense of the structure of international trade, Exhibit 1.4 presents the world's top trading countries. It reveals that China, the United States, Germany, and Japan are the world's leading international traders. China and the United States are close competitors in total trade, but trade accounts for about 31 percent of China's GDP as opposed to 19 percent for the United States. Merchandise trade is a much larger component of economic activity in countries such as the Netherlands (126 percent) and South Korea (69 percent). These percentages suggest that some countries depend very heavily on international trade relative to the value of all goods and services they produce domestically.

In some cases, countries' total trade surpasses 100 percent of the nation's GDP. How can this be? The answer is that countries such as Singapore, Hong Kong, and the Netherlands are known as *entrepôt* economies. *Entrepôt* is from the French for "intermediate depot." Such countries import a large volume of products, some of which they process into higher value-added products and some of which they simply re-export to other destinations. They often arise in locations that enjoy especially advantageous access to larger, adjacent markets. For example, Singapore is a major *entrepôt* for Southeast Asia, e.g., for transshipping petroleum products that it receives from the Middle East. Hong Kong is an *entrepôt* for China. The Netherlands is an *entrepôt* for the greater European Union.

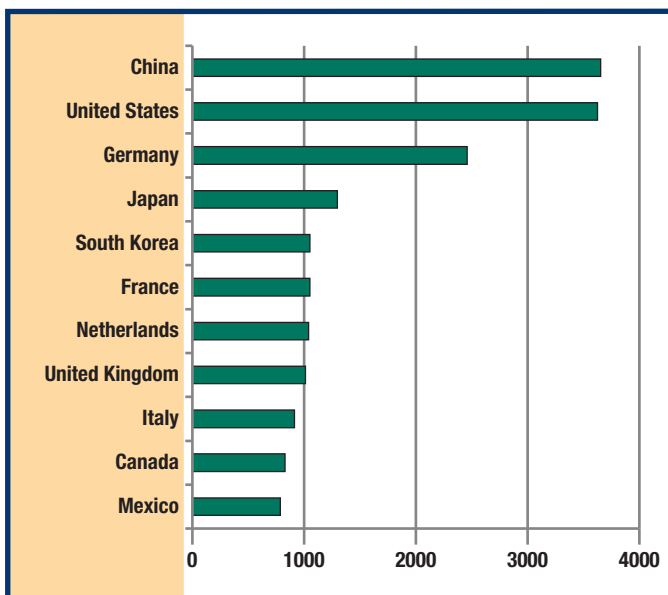
EXHIBIT 1.3

Leading Countries in International Merchandise Trade

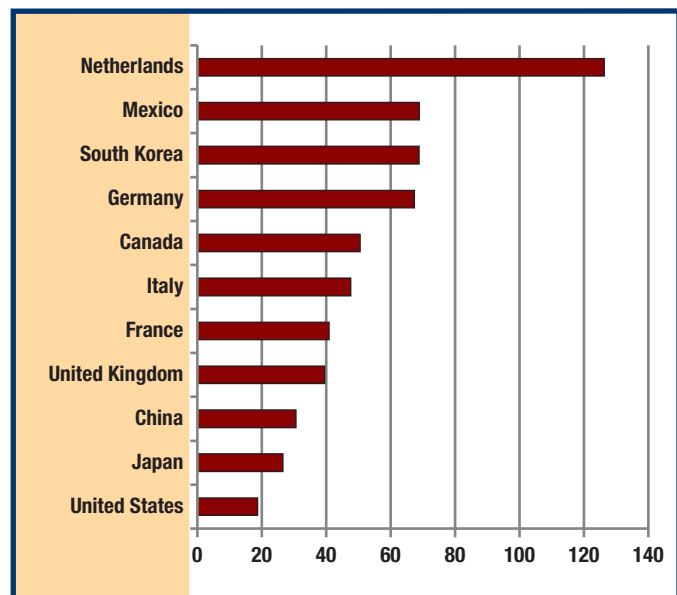
Sources: Based on data from the World Bank, *World Development Indicators*, Washington, DC: World Bank (2017), www.worldbank.org; World Trade Organization, *Statistics Database*, Geneva: World Trade Organization (2017), www.wto.org; UNCTAD, *World Investment Report*, New York: United Nations (2017), www.unctad.org.

The Nature of International Investment

Of the two types of investment flows—portfolio investment and foreign direct investment—we are concerned primarily with foreign direct investment (FDI) in this text because it is the ultimate form of internationalization and encompasses the widest range of international business



(a) Total annual value of products trade (exports + imports) in billions of U.S. dollars



(b) Total annual value of products trade (exports + imports) as a percentage of nation's GDP

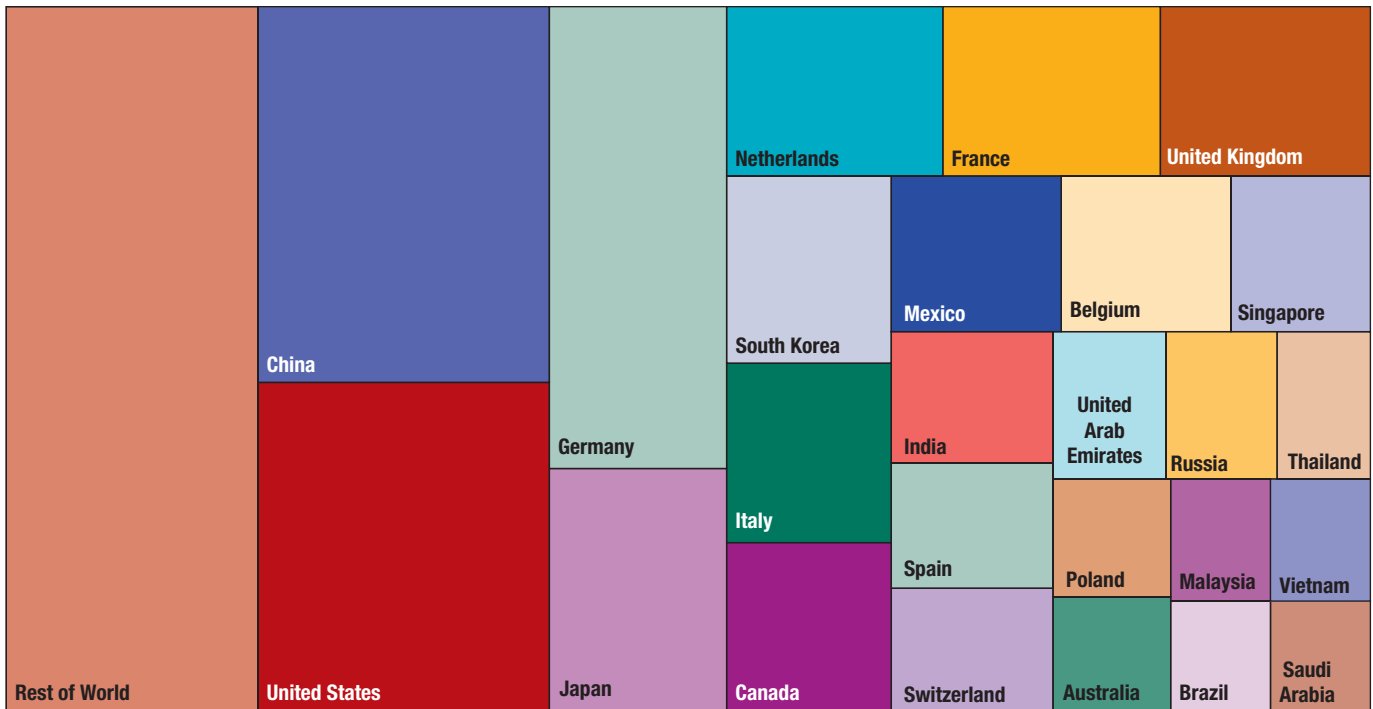


EXHIBIT 1.4

The Top 25 Countries in International Merchandise Trade

Sources: Based on data from the World Bank, *World Development Indicators*, Washington, DC: World Bank (2017), www.worldbank.org; World Trade Organization, *Statistics Database*, Geneva: World Trade Organization (2017), www.wto.org; UNCTAD, *World Investment Report*, New York: United Nations (2017), www.unctad.org.

Note: The exhibit reflects the value of each country's combined exports and imports as a percentage of total world trade.

involvement. FDI is the foreign entry strategy practiced by the most internationally active firms. Companies usually undertake FDI for the long term and retain partial or complete ownership of the assets they acquire. In the process, the firm establishes a new legal business entity in the host country, subject to the regulations of the host government.

FDI is especially common among large, resourceful companies with substantial international operations. For example, many European and U.S. firms have invested in China, India, and Brazil to establish plants to manufacture or assemble products, taking advantage of low-cost labor or natural resources in these countries. At the same time, companies from these rapidly developing economies have begun to invest in Western markets. In 2012, for example, the Haier Group from China acquired New Zealand's appliance manufacturing company Fisher & Paykel. Then, in 2016, Haier purchased General Electric's appliance division for \$5.4 billion.³

Exhibit 1.5 illustrates the dramatic growth of FDI since the 1980s. The exhibit reveals that the dollar volume of FDI has grown immensely since the 1980s, especially in developed (advanced) economies such as Japan, Europe, and North America. FDI inflows to the developing economies began to surpass those to the advanced economies in about 2010. FDI inflows were interrupted in 2001 as investors panicked following the September 11 terrorist attacks in the United States. The inflows were interrupted again in 2008 by the global recession but then rose sharply in subsequent years. These dips underscore the importance of maintaining stability in the world economy. Despite these setbacks, the overall trend remains strong and growing over time. Particularly significant is the growth of FDI into developing economies, much of which results from their need for modern industrial infrastructure. It reflects the importance of developing economies and emerging markets as target markets and sourcing bases.

Services as Well as Products

Historically, international trade and investment were mainly the domain of companies that make and sell products—tangible merchandise such as clothing, computers, and motor vehicles. Today, firms that produce *services* (intangibles) are key international business players as well. Services are deeds, performances, or efforts performed directly by people working in banks, consulting firms, hotels, construction companies, retailers, and countless other firms in the services sector. International trade in services accounts for about one-quarter of all international trade and is growing rapidly.