INTERNATIONAL BUSINESS

FOURTH EDITION

Oded Shenkar, Yadong Luo and Tailan Chi

INTERNATIONAL BUSINESS

This fully revised and updated fourth edition of *International Business* offers an action-focused, practical approach to the topic, helping students understand the global business environment and its repercussions for executives. The book provides thorough coverage, delving into fundamental concepts and theory; the cultural, political, and economic environment; international business strategies; and even functional management areas.

More comprehensive than competing books, this new edition of *International Business* includes:

- A new chapter on the digitalization of the global economy and its implications for firm strategy and organizations.
- New examinations of the forces of de-globalization, implications of rising trade protectionism, challenges of geopolitical conflicts, and a friction framework for understanding the effects of cultural differences.
- Enriched and expanded discussions about potential reconfigurations of global value chains following the COVID-19 pandemic, changing perspectives on the role of the government with renewed attention to industrial policy, shifts in regional integration with the emergence of such new trade blocks as CPTPP and RCEP, and fresh insights on factors influencing a country's balance of payments.
- Strengthened, expanded global cases, examples, and "industry" and "country" mini-cases that give students practical insight into the ways companies actually behave within a competitive, global environment.

Also featuring a companion website with a test bank, PowerPoint slides, and instructor's manual, this book is ideal for students and instructors of any international business course at undergraduate or postgraduate level.

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"This book has an evocative blend of the 'big picture' of international business in the age of globalization, and all the key and more specific issues in IB today. These seasoned scholars' varied cases are not just great fun, but also provide great coverage, from the traditional IB topics to newer ones. The authors' practical vision is refreshing, eloquently written, and spot on!"

Mary Ann Von Glinow, *Knight Ridder Eminent Scholar Chair in International Management, Florida International University, USA; Former AIB and AOM President*

"Shenkar, Luo and Chi offer excellent, comprehensive coverage of international business in the new global environment. Written by three outstanding researchers, it is practically focused, firmly grounded in cutting edge research, and up-to-date with great student and instructor support."

Peter J. Buckley, *Professor and Director of Business Confucius Institute, University of Leeds, UK*

"For anyone who is interested in learning about international business, this is an excellent book that covers an amazing amount of information in each chapter. It is a basic book written by three experts in the field of IB. They address topics like foreign direct investment theories, country competitiveness, global marketing, managing global R&D, and international entrepreneurship that are important areas for the future. It is rare to find such explanations in one volume. Professors teaching a course on international business will find it an excellent resource for practical and conceptual material."

Marjorie A. Lyles, *Chancellor's Professor of Global Strategic Management, Indiana University, USA; Former AIB and SMS President*

4th edition

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To Miriam, Keshet, Joshua, and Rakefet; and to the memory of my parents, Bluma and Joshua—OS

To my family, Cuihua, Edward, and Rosalie—YL

To Susan, Alison, and Zoey; and to the memory of my parents, Biqing Chi and Ruobing Xu—TC

Contents

LIST OF EXHIBITS

1 International Business in an Age of Globalization

Do You Know?

1 What is globalization? Why is globalization important even to firms that do not have any international involvement at present? How does globalization affect the consumer and the employee?

2 What are the benefits of globalization, and what are its costs and risks, both real and perceived? Why has there been a backlash against globalization in recent years?

3 What do the terms "international business," "international transaction," "international trade," and "international investment" mean? Can you distinguish between the multinational enterprise (MNE) and the international firm?

4 What are the differences between international business and domestic business? What is the source of these differences?

5 Why do firms expand globally? What do they hope to gain and what hazards do they face? Does every firm seek identical goals or face the same obstacles and opportunities when expanding into international markets?

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OPENING CASE
THE COCA-COLA COMPANY

Atlanta-based Coca-Cola Company, a manufacturer, distributor, and marketer of non-alcoholic beverages, is one of the first examples that comes to mind when people think of a global company. With almost 500 beverage brands, and sales in more than 200 countries, few other companies can match Coca-Cola's worldwide presence or the visibility of its products, particularly its flagship Coke, which has become the symbol of a global product. Studies show that the brand enjoys the highest name recognition in the world. The Coca-Cola Company ranked 59th on the Fortune 500 list (up 11 slots from 2011), with roughly $46.54 billion in revenue and $8.57 billion in profit. The company, which first sold trademark-registered Coke in the United States in 1886, relied on international markets for 78 percent of its gallon volume in 2011. At 44.2 percent of the total, net operating revenue was highest for North America in the same year, followed by the Pacific with 11.7 percent, and 10.3 percent for Europe.

Coca-Cola normally sells concentrate, based on the recipe that Dr. John Pemberton invented over a hundred years ago and that has been kept secret ever since, to local bottlers that prepare the beverage and distribute it in their respective markets. However, in some countries it does not grant bottlers full manufacturing rights. Unlike its domestic contracts, its international agreements are limited in time, allowing for termination at the company's discretion, and marketing support, while common, is not provided in all markets. True to the now famous slogan, "think global, act local," the company preserves a coherent marketing theme, yet also adapts product taste and operations to local markets. The "think global, act local" slogan embodies what may be the central dilemma in international business: the need to maintain global strategic focus and leverage scale advantages, while allowing for adaptation to local circumstances in everything from product specifications to packaging and distribution. The company's most global function—advertising—avoids themes that would be controversial in local markets. This is in contrast to its rival Pepsi, which, for example, irked religious circles in Israel with ads showing monkeys as human ancestors. Both its secret concentrate recipe and its marketing know-how are considered key factors in its global success. In addition, the company also achieves cost savings by purchasing certain raw materials centrally in large quantities for its global operations and by siting bottling plants locally (thus reducing shipping costs), particularly in locations where labor and land costs are lower.

Coca-Cola's global success has ruffled some feathers. A few years ago, the European Commission rejected its bid to acquire a French beverage maker, pointing out that it already had a majority share in European Union (EU) markets. More recently, the Chinese Ministry of Commerce blocked its attempt to acquire a privately owned beverage company in China, also on anti-monopoly grounds. The company's argument that it has a tiny share of the total market—defined as all liquids consumed, including water—has fallen on deaf ears. Efforts to promote a global image did not prevent the company from being identified and labeled an American icon, making it a lightning rod for criticism and attacks by anti-US and anti-globalization activists. In 2001, Coca-Cola's facilities were bombed by Muslim rebels in India and by Maoist guerrillas in Nepal. In the years that followed, Coca-Cola has been the target of protests against US policies in Serbia, Europe, and the Arab world, among others.

Source: Coca Cola Annual Report 2011; *Fortune Magazine* 500 list 2012; media reports.

An Age of Globalization

"Globalization" has become one of the buzzwords of modern times. People see its manifestations all around them, from the Coke can in a small village store in Africa, to McDonald's golden arches in a Chinese city, to an article in the local newspaper about the outsourcing of software maintenance to India or the shifting of a call center to Canada. Opinions regarding the impact of globalization vary widely, ranging from praise for its association with rising living standards, to condemnation of its ill effects such as industrial pollution and rising income inequality. On the evening news you may hear praise for globalization from a farmer who has just concluded a contract for a large shipment of soybeans to China, only to see it followed by coverage of an anti-globalization demonstration outside a trade conference. So, what is globalization, and why does it generate such diverse and often emotional reactions?

In line with the diversity of opinion, globalization has been defined in numerous ways. In this book, we define **globalization** as the acceleration and extension of the interdependence of economic and business activities across national boundaries. Simply put, this means that a development on one side of the globe will have consequences on another. It is easy to see the impact within a particular industry, for instance, the automotive industry. US-based makers of auto parts such as Delphi and Visteon have been pushed to restructure by pressure from low-cost producers in Asia, Mexico, and Eastern Europe, who can make the same automotive components for less. Volkswagen has demanded concessions from its German workforce as a condition for keeping production local. Closer to home, the price you pay at the pump is partially determined by energy demand in other countries, with soaring consumption in China and India accounting for much of the doubling of oil prices between 2004 and 2006. This interdependence will not go away. So, both the ongoing process and outcome of globalization have profound implications for not only the economic policies of governments, but also for the strategies of firms around the world. The US National Intelligence Council notes in its 2020 Project Report that "certain aspects of globalization, such as the growing global connectedness, are not likely to go away," and that this will have far reaching consequences for the expansion of international business:

> Interdependence has widened the reach of multinational business, enabling smaller firms as well as large multinationals to market across borders and bringing heretofore non-traded services into the international arena.[1]

What Does Globalization Mean to You?

To the consumer, globalization means more choices, generally lower prices (but not always, as the example of gas prices shows), and an increasingly blurred national identity for products and services. Send a package from New York to London via DHL, and you have contributed to the revenue of the German Postal Service. Buy a Swedish Volvo, and you have increased the revenue of its Chinese owner, Geely Automobile Holdings Limited. Buy a Jaguar, and you have contributed to the bottom line of its Indian owner, Tata Motors. Buy a Dodge, and you have purchased a product of Italian-based Fiat. Buy a foreign brand, and you may find out that it is manufactured in the United States: Honda Civics in Ohio, Mercedes M class in Alabama, Nissan pickup trucks in Tennessee. If you prefer to buy Canadian, you can choose between a GM or a Ford vehicle manufactured in Canada; or you can settle for the Mercedes M class, made in the United States, but advertised in Canada as "made by a Canadian"—alluding to the manager of a US plant. If you are an Australian consumer who wants to buy a locally produced vehicle, you can select between three locally produced foreign brands: Holden (a GM brand whose design is influenced by its German subsidiary Opel), a Ford, or a Toyota. These Australian operations also export to other countries while facing more competition from imports as local tariffs are reduced.

Similar trends can be observed in the service sector. The mortgage on your US property might be underwritten by Swiss bank UBS, your life insurance by French insurer AXA. Your retirement funds might be invested in the stock of Swiss food giant Nestlé and Japanese electronics maker Sony, or managed by German-based Deutsche Bank. The advertisement enticing you to buy Cincinnati-based P&G's Pampers may have been conceived by the UK's Saatchi & Saatchi, but the graphic work may have been done in India. If you buy at your local Wal-Mart, chances are that much of the products on the shelves are made outside the country; Wal-Mart's imports from China, for instance, exceed those of the United Kingdom. Even the student sitting next to you may well be a foreign national, as might be the patient waiting next to you in the hospital clinic. You may take your next vacation in Mexico, rather than in Florida; just remember to take your Chinese-manufactured iPhone along for the ride.

In addition to offering a dizzying array of consumer products and services, globalization affects your career prospects. At times, it will also limit your opportunities, as when the transcription of medical records is outsourced to India; at other times, especially if you are better educated, globalization will greatly expand your career choices and opportunities. It is increasingly possible that you will join one of the many foreign firms in the United States upon graduation, or that you will be assigned to work in another country by a US-, local-, or a third-country foreign firm. If you are considering employment with a foreign firm, you may want to know whether the recruiting company tends to open its senior-most ranks to other than its own nationals. If in doubt, look for foreign names on the list of members of the board of directors, which provide a good indication of how open the company is to non-natives. Whether you work for a domestic or a foreign corporation, you will not only have to consider a foreign assignment, but will spend time negotiating, entertaining, coaching, and learning from foreign executives and employees. How well you perform these tasks will determine the rest of your career, as companies are increasingly on the lookout for individuals who can successfully operate globally.

Interim Summary

1. **Globalization is the accelerated interdependence of economic and business activities across national boundaries.**
2. **Globalization influences the availability and pricing of products and services around the world, while often blurring their source and identity.**
3. **Globalization affects your career opportunities and the skills you will need to be successful.**

The Face of Globalization

KOF Swiss Economic Institute publishes a Globalization Index on the extent of a country's integration with the rest of the world along three dimensions (economic, social, and political). Economic integration scores are based on a country's trade and foreign investment, discussed later in Chapters 2 and 3 of this book. Social integration scores are composed of such indicators as the number of Internet users, international travel and tourism, international telephone and mail traffic, and foreign population. Finally, political engagement scores are composed as a combination of membership in international organizations, participation in UN Security Council missions, the number of international treaties ratified, and the number of embassies in the country. In addition, the KOF index considers both de facto globalization (economic, social, and political exchanges with the rest of the world) and de jure globalization (regulations and institutions that affect the exchanges). Exhibit 1.1 shows the ratings of 60 countries according to their de facto globalization scores.

Exhibit 1.2 lists the 30 most globalized countries/territories of the world in 2018 according to the overall Globalization Index and on each of the three dimensions. Switzerland is in first place overall. The United States is in 23rd place, with its high levels of global integration along the social and political dimensions counterbalanced by its relatively low level of economic integration (typical of countries with large domestic markets), where the US does not even place in the top 50. Indeed one could argue that, in a global environment, being large is sometimes a liability in the sense that it allows firms to neglect international markets for too long. A well-known study of globalization was published in *Foreign Policy* magazine in 2005.[2] The study did not find a strong relation between globalization and the propensity to suffer terrorist attacks on one's soil, discounting speculation that opening up to the outside world invites security risks. However, the study did find a relation between globalization and public education spending, especially in the developing world. In other words, success in a global, knowledge-based economy depends on having an educated workforce. Elsewhere, a *New York Times* Op-Ed noted that countries that ranked high on the Globalization Index had higher economic and political stability (see Chapter 7), more flexible labor markets, better regulation, and less corruption (see Chapter 19).[3]

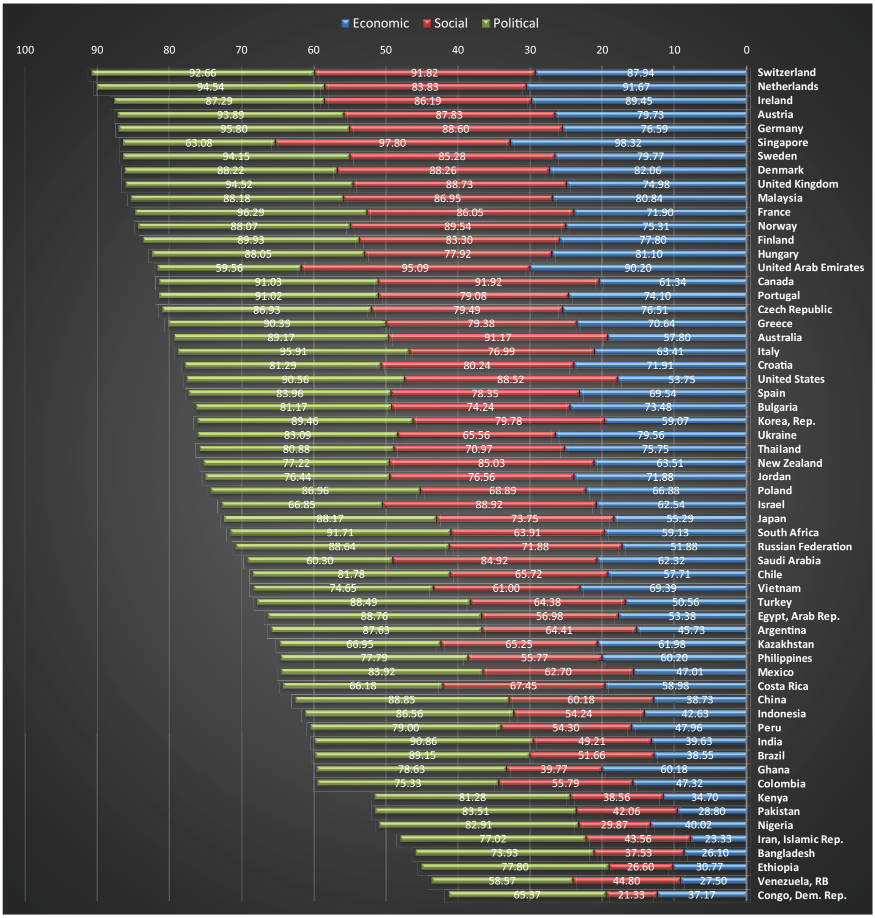

Exhibit 1.1

Globalization Scores of Selected Countries, 2018

Source: KOF Index of Globalization 2020. Gygli, Savina, Florian Haelg, Niklas Potrafke and Jan- Egbert Sturm (2019): The KOF Globalisation Index – Revisited, Review of International Organizations, 14(3), 543–574 https://doi.org/10.1007/s11558-019-09344-2. The methodology is based on Axel Dreher, "Does globalization affect growth? Evidence from a new Index of Globalization," *Applied Economics*, 38, 10, 2006, 1091–1110.

Who Benefits from Globalization?

One of the main arguments against globalization is that it confers benefits on rich nations at the expense of poor ones. Before we discuss this argument, let us take a look at the relationship between development level and globalization. It is evident from Exhibit 1.2 that some developed nations (e.g., Japan) obtain only moderate globalization scores, while some developing and emerging economies (e.g., the Czech Republic and Malaysia) obtain respectable scores. Still, the overall relationship is quite clear: The 12 nations that score highest on globalization are all developed economies, while the bottom half is occupied by developing and emerging economies. This does not mean that globalization brings no value

Exhibit 1.2 The World's Most Globalized Countries/Territories, 2018

Overall Rank	Countjry	Overall Score	Economic Rank	Country	Economic Score	Social Rank	Country	Social Score	Political Rank	Country	Political Score
1	Switzerland	91.19	1	Singapore	94.00	1	Luxembourg	91.91	1	Italy	98.26
2	Netherlands	90.71	2	Netherlands	88.66	2	Monaco	91.13	2	France	98.17
3	Belgium	90.59	3	Belgium	88.54	3	Norway	90.76	3	Germany	97.96
4	Sweden	89.93	4	Luxembourg	88.30	4	Switzerland	90.42	4	United Kingdom	97.90
5	United Kingdom	89.84	5	Hong Kong, China	88.21	5	United Kingdom	90.15	5	Spain	97.46
6	Austria	88.85	6	Ireland	87.97	6	Canada	89.81	6	Netherlands	97.33
7	Germany	88.60	7	Switzerland	86.79	7	Sweden	89.17	7	Sweden	97.26
8	Denmark	88.26	8	Malta	86.50	8	Ireland	88.50	8	Switzerland	96.37
9	Finland	87.70	9	Estonia	86.27	9	Singapore	88.42	9	Belgium	96.27
10	France	87.25	10	United Arab Emirates	85.95	10	Andorra	88.41	10	Austria	95.96
11	Norway	86.17	11	Denmark	84.46	11	Austria	87.72	11	Portugal	93.84
12	Spain	85.70	12	Cyprus	84.28	12	Australia	87.58	12	Finland	93.82
13	Czech Republic	85.60	13	Czech Republic	84.04	13	Liechtenstein	87.50	13	Denmark	93.77
14	Hungary	84.98	14	Sweden	83.35	14	Germany	87.37	14	United States	93.62
15	Portugal	84.72	15	Slovak Republic	83.07	15	New Zealand	86.89	15	Russian Federation	93.05
16	Canada	84.64	16	Finland	82.97	16	Belgium	86.84	16	India	92.96
17	Ireland	84.47	17	Austria	82.86	17	Denmark	86.55	17	Turkey	92.47
18	Estonia	83.77	18	Hungary	82.69	18	San Marino	86.49	18	Canada	92.41
19	Slovak Republic	83.72	19	Bahrain	82.54	19	Cyprus	86.45	19	Greece	91.95

continued

Exhibit 1.2 *continued*

Overall Rank	Countjry	Overall Score	Economic Rank	Country	Economic Score	Social Rank	Country	Social Score	Political Rank	Country	Political Score
20	Singapore	83.62	20	Mauritius	82.16	20	Finland	86.32	20	Hungary	91.85
21	Luxembourg	83.60	21	Latvia	82.08	21	Netherlands	86.15	21	Egypt, Arab Rep.	91.83
22	Italy	83.37	22	Georgia	82.02	22	Macao, China	86.13	22	Argentina	91.66
23	United States	82.41	23	United Kingdom	81.47	23	Iceland	86.12	23	Poland	91.61
24	Greece	82.38	24	Germany	80.49	24	Israel	85.85	24	Korea, Rep.	91.16
25	Australia	81.99	25	Portugal	80.17	25	Hong Kong, China	85.76	25	Romania	91.11
26	Malaysia	81.49	26	Lithuania	79.56	26	France	85.51	26	China	90.61
27	Croatia	81.42	27	France	78.06	27	United States	85.47	27	Norway	90.23
28	Lithuania	81.34	28	Montenegro	78.06	28	Lithuania	85.25	28	Australia	90.21
29	Poland	81.33	29	Bulgaria	77.82	29	Estonia	85.00	29	Czech Republic	90.16
30	Slovenia	81.14	30	Norway	77.53	30	Bahamas, The	84.93	30	Ukraine	89.24

Source: KOF Index of Globalization 2020. Gygli, Savina, Florian Haelg, Niklas Potrafke and Jan- Egbert Sturm (2019): The KOF Globalisation Index – Revisited, Review of International Organizations, 14(3), 543–574 https://doi.org/10.1007/s11558- 019-09344-2. The methodology is based on Axel Dreher, "Does globalization affect growth? Evidence from a new Index of Globalization," *Applied Economics*, 38, 10, 2006, 1091–1110.

to the developing world; on the contrary, integration into the global economy may well pave the route to economic growth and prosperity, as the case of China, one of the world's fastest growing economies, shows clearly. In contrast, countries that fail to integrate into the global economy face the prospect of falling further behind. Two related factors tend to limit the extent of benefit that poor countries can gain from globalization. One is the presence of serious deficiencies in domestic economic and politico-legal governance (e.g., civil conflict, macroeconomic mismanagement, lack of property rights protection, and corruption) that prevent the country from exploiting its advantages in international trade and that deter foreign investment. The other is the lack of trained personnel for effective participation in international economic institutions such as the International Monetary Fund, the World Trade Organization, and the World Bank.

The good news is that the share of developing countries in world merchandise trade is rising to its highest level in more than 50 years, and the trade growth of the 49 least developed countries (LDCs) exceeds the global average. It is also important to realize that many of the manifestations of globalization in wealthy nations end up helping poorer economies. For instance, when a Singaporean tourist is visiting Laos, he is in effect increasing the export sales of Laos by purchasing such services as hotel stays and tours. And while wages in developing country factories are low by developed nation standards, employees of foreign affiliates in developing economies are paid, on average, far more than those employed by domestic firms. While some local firms are unable to compete with large foreign corporations and exit the market, others take advantage of the learning opportunities associated with multinational presence and upgrade their capabilities, thus positioning themselves as future global players. If large multinational firms seem an exclusive club of rich nations, they are now joined by multinationals from developing economies. In 2000, for the first time ever, multinational firms from developing nations made it into the ranks of the top 100 global multinationals.[4] According to a more recent UN report from 2012, firms from Mexico, China, Brazil, and other developing nations continue to break into the top multinational ranks, with new contenders like China-based Lenovo growing rapidly.[5]

The Impact of Globalization

A common lamentation against globalization is that it deprives nations of their sovereignty. This will supposedly occur because of the growing power of international institutions such as the World Trade Organization (WTO) or the International Monetary Fund (IMF), whose officials are not elected by popular vote (see Chapter 8). Yet, while the WTO has assumed a conflict resolution role that was previously the domain of bilateral negotiations, its resolutions are based on consensus, meaning that the vote of the smallest nation counts as much as that of the largest. The most important decisions regarding international trade are still made by governments, and trade relations are governed by bilateral agreements negotiated and monitored by sovereign governments. And, while mega-multinational corporations abound, small firms remain viable players that have a role in the global economy. As you will see in Chapter 4, small firms in the United States and in many other countries have actually increased their share of national exports over the last decade.

Another complaint against globalization is that it comes at the expense of the environment. Environmentalists accuse firms of relocating their operations abroad solely for reasons