Business and management in a global context
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Undergraduate study in Economics, Management, Finance and the Social Sciences

This is an extract from a subject guide for an undergraduate course offered as part of the University of London International Programmes in Economics, Management, Finance and the Social Sciences. Materials for these programmes are developed by academics at the London School of Economics and Political Science (LSE).

For more information, see: www.londoninternational.ac.uk
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This is one of a series of subject guides published by the University. We regret that due to pressure of work the author is unable to enter into any correspondence relating to, or arising from, the guide. If you have any comments on this subject guide, favourable or unfavourable, please use the form at the back of this guide.
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Introduction

1.1 Route map to the guide

The guide, and course, is structured in four parts. The first part provides an introduction to the global business environment and covers trends towards globalisation (Chapter 1), and the formal and informal institutions of countries. In particular we focus on international political, economic, legal, cultural and social diversity (Chapters 2 and 3). The subject guide provides activities that will help you to pick out the management challenges and implications, not least that of corporate social responsibility when operating on the global stage.

The second part gives an overview of why international trade takes place, why firms invest abroad (Chapter 4), the cross-border institutions that exist such as the IMF, World Bank and regional economic blocs (Chapter 5), and how the global financial system functions (Chapter 6).

These first two parts provide the context of international business while part three gives insight into how to analyse that context to arrive at competitive international strategies (Chapters 7 and 8), enter markets and evolve (Chapter 9) and develop marketing and R&D strategies (Chapter 10).

The fourth part focuses on major operational areas of an international business, namely designing the organisation (Chapter 11), global sourcing and supply chain management (Chapter 12), establishing global information systems (Chapter 13) and managing human resources (Chapter 14).

1.1.1 How to use this guide and hours of study

The advice normally given to International Programmes students is that if they are studying one course a year, they should allow at least six hours of study a week. This subject guide provides detailed chapters to save you time, since the number of books on this subject are too many to absorb in the time, while the articles in refereed journals tend to be overspecialised. There are also two essential texts. One by Peng and Meyer (2011) is very strong on international business, institutions and global context, while the other by Willcocks (2013) complements Peng and Meyer with its focus on business management. There is also some additional reading.

You should read each chapter of the subject guide once, then work through it methodically a second time, doing the activities as they appear. This will involve reading pages from the Essential reading texts and articles prescribed for the chapter, but might also involve looking at a case study provided in the textbook or on the virtual learning environment (VLE). There are many activities. Do not skip these! They are a key part of your learning. Where you are asked questions, write your answers down carefully and in detail so you can revise from them at a later point, before any examination.

1.2 Introduction to the subject area

If business was the same everywhere, we could all get on with providing products or services and, through gaining competitive advantage, make profits. However, despite the flattening effects of globalisation, international business demonstrates huge diversity and complexity. To understand business in a global context, and its threats and opportunities,
you need to consider the drivers and nature of globalisation, and the political, economic, social, technological and legal differences that various regions and countries exhibit. You also need to work within the frameworks of multilateral organisations and regional economic blocs.

As a manager faced with this complexity and diversity, you need to devise strategies that will work internationally, in different parts of the globe, plan entry strategies for new markets, and decide who you need to establish alliances with and how your strategy is to evolve. You then need to work at the detail of managing, specifically designing structure and organisation, devising sourcing and supply chain arrangements, establishing information systems that perform globally, and creating distinctive arrangements for managing international human resources.

As a student, you will find understanding and analysing international business and making managerial judgements to be full of fresh challenges, and you will also find that the study of this subject area not only provides insights, but also gives you the analytical equipment and knowledge to actually begin to perform in a business that operates globally.

### 1.3 The syllabus

**Part 1: Introduction to the global business environment**

*Perspectives on globalisation and international business* – trends and drivers of globalisation, foundations of global trade and finance, overview and framework for understanding the global economy, the development of the multinational enterprise (MNE), debates on the nature and impacts of globalisation, and the implications for managing international business.

*Political, economic and legal environments* – common and diverse; political, economic and legal; formal and informal institutions and how they contextualise and shape management practices and the conduct of business. This includes comparing national economies, regional integration, international organisations, and relationships between government and business. The chapter introduces the CAGE and Porter Diamond frameworks for analysing business management environments.

*Culture society, ethics and corporate social responsibility* – informal institutional influences of social, cultural, ethical and religious factors and how these play into globalisation, rendering a necessary focus on balancing global, regional and local factors when conducting business internationally. The chapter discusses differences and types of culture, and religion and the different types of ethics and attitudes towards corruption and corporate social responsibility to be found.

**Part 2: Business across borders: the foundations**

*International trade and investment – theory, patterns, growth of and rationale for foreign direct investment.*

*Global and regional integration and multilateral organisations* – the different levels of regional integration found across the globe, and the benefits and challenges of regional integration. It describes regional integration in Europe, the Americas, Asia and the Middle East and North Africa.

*The global financial system* – the international capital market, foreign exchange markets and related institutions.
Part 3: International business strategy

**Strategy and enterprise in international contexts** – introduction to international business management strategy. The PESTEL framework and Ghemawat’s culture, administration, geography, economy (CAGE) framework as a basis for analysing the international environment for a firm, types of strategy commonly pursued in international business, how such strategies evolve, Ghemawat’s aggregation, arbitrage and adaptation (AAA) framework as a basis for designing strategy for international contexts.

**Competitive strategy for international business** – concepts of corporate and business strategy, how firms compete through competitive positioning and resource-based approaches, dynamics of competition, the global, regional and local dimensions in strategy, Porter's five forces, value chain and generic strategies frameworks, resource-based and institution-based approaches to international competitiveness.

**Entry strategies, alliances and evolution** – foreign entry strategies, including where, when and how to enter international markets, the strategies to be pursued, the contextual factors that need to be taken into account, the role of strategic alliances in entering and positioning in international markets, how to organise operations given the choices made, evolving the global strategy, including growth by acquisition.

**Marketing and R&D strategy** – international marketing assessment, international consumers, developing marketing strategy, the 4 ‘P’s mix of place, price, product and promotion, and global branding, new product and market development, distribution and supply chain issues, R&D and sources of innovation including R&D offshoring.

Part 4: International business management

**Organisation of international business** – different types of organisational structure and how they relate to processes, institutions and culture, includes divisionalisation, matrix and hybrid structures, organisational change issues.

**Global sourcing of production and services** – global sourcing choices, make-or-buy, production and logistics concepts and developments, sourcing of business services, strategic sourcing issues of emerging locations and country attractiveness.

**Global information systems management** – business strategy and IS alignment, organising IS for international operations, sourcing choices and the role of offshoring and outsourcing business and IT services, the role of IT infrastructure and its management, retained capabilities, global implementation of IS projects.

**International dimensions of human resources management** – approaches to managing people, the main functions of the HR department, global pay and incentivisation practices, managing expatriates and multinational workforces, performance management.

1.4 Aims and objectives of this course

The aims and objectives of this course are to:

- give you a research-based grounding in the context of international business including globalising trends, formal and informal institutions, the political, economic, social, technological and legal issues and the resultant diversity of international business
• prepare you to be able to discuss cultural, ethical and social issues for international business and suggest policies of corporate social responsibility
• provide an introduction to and develop your ability to assess international trade and investment, multilateral organisations and regional integration and the global financial system
• prepare you to be able to discuss how firms develop international business, marketing and R&D strategies, enter markets and alliances, and operate and manage on the global stage
• give you insight through frameworks, studies and examples of how businesses manage organisational structure and architecture, sourcing and the supply chain, information systems and human resources, in different parts of the globe, globally, regionally and domestically
• give you insight into the contexts of international business and enable you to work within these contexts to make judgements on strategising and managing operations in the global economy.

1.5 Learning outcomes for the course

At the end of this course, and having completed the Essential reading and activities, you should be able to:

• demonstrate knowledge of, and the ability to assess, core institutions of international business and how firms manage on the global stage
• assess regional, cultural and institutional differences in how business is conducted globally
• apply core understandings, frameworks and management principles to specific business contexts
• formulate choices and decisions in international business strategy and operations
• operate as an informed employee in an international firm.

1.6 Overview of learning resources

1.6.1 Essential reading

For almost all chapters, the Essential reading consists of two texts:


Willcocks, L. Global business management foundations. (Stratford: Steve Brookes Publishing, 2013) [ISBN 978095641533]. Available to download in Kindle format from Amazon.co.uk, who provide a free Kindle app. Also available in hard copy from Lulu.com – see the VLE for details and link. This is an essential complementary text that is strong on strategy and management, and in areas not covered in so much depth by Peng and Meyer (2011), including information systems, global sourcing, international and business strategy, marketing and organisation. The book covers the syllabus and has been updated to late 2013.

You will find that all of the points covered in the subject guide chapters will be covered in either or, more often, both of these books. Reading further will give you more arguments, examples and detail that can enhance greatly your knowledge and understanding, as well as, more pragmatically, improving your examination answers.
Detailed reading references in this subject guide refer to the editions of the two set textbooks listed above. New editions of one or more of these textbooks – especially the Peng and Meyer (2011) book – may have been published by the time you study this course. You can read a more recent edition of any of the books; use the detailed chapter and section headings and the index to identify relevant readings. Also check the VLE regularly for updated guidance on readings and case studies.

There are also several Essential journal articles, listed below.

**Journal articles**


Kettinger, W., D. Marchand and J. Davis 'Designing enterprise IT architectures to optimise flexibility and standardisation in global business', *MISQ Executive* 9(2) June 2010, pp.95–113.


Willcocks, L. 'Take the outsourcing health check', *Professional Outsourcing Magazine* 7 2011, pp.6–12.

### 1.6.2 Further reading

Please note that as long as you read the Essential reading you are then free to read around the subject area in any text, paper or online resource. You will need to support your learning by reading as widely as possible and by thinking about how the principles apply in the real world. To help you read extensively you have free access to the VLE and University of London Online Library (see below).
Business and management in a global context is a fast moving subject to study. Therefore it is particularly important that you keep up with the most recent developments. You can do this by reading regularly such sources as *The Economist*, which has weekly news and regular, relevant special studies; *The Financial Times*, which provides daily world commentary and also has a backlog and regular regional and theme special issues; and *The Wall Street Journal*, which also provides detailed daily world commentary. The two daily newspapers have regional editions.

You should also identify more regionally based weekly business journals and magazines that will provide insightful articles and good illustrative examples of the events and practices you are studying in this course. Do not forget to keep detailed notes on what you find from such sources for revision purposes.

There are numerous books available on international business, far too many for you to be able to read. However, here are some of the most useful ones:


**Journals**

There are also many journals covering international business and management. Some will be too research based and advanced for your purposes. It is also best to focus on the more recent articles, written within the last three years. The main journals for additional articles on globalisation, business strategy and management are:


**Full list of Further reading**

For your ease of reference, here is a list of all the further reading for this course.

*AMA The Definition of Marketing. American Marketing Association, 2007. Available at: www.marketingpower.com/AboutAMA/Pages/DefinitionofMarketing.aspx*  


Fonstad, N. and M. Subramani *Building enterprise alignment: a case study*, *MISQ Executive* 8(1) 2009, pp.31–41.


Liu, R. et al. ‘Why are different services outsourced to different countries?’, *Journal of International Business* 42 2011, pp.558–71.


Ross, J. 'Creating a strategic IT architecture competence: learning in stages', *MISQ Executive* 2(1) 2003, pp.31–43.


### 1.6.3 Online study resources

In addition to the subject guide and the Essential reading, it is crucial that you take advantage of the study resources that are available online for this course, including the VLE and the Online Library.
You can access the VLE, the Online Library and your University of London email account via the Student Portal at: http://my.londoninternational.ac.uk

You should have received your login details for the Student Portal with your official offer, which was emailed to the address that you gave on your application form. You have probably already logged in to the Student Portal in order to register! As soon as you registered, you will automatically have been granted access to the VLE, Online Library and your fully functional University of London email account.

If you have forgotten these login details, please click on the ‘Forgotten your password’ link on the login page.

The VLE

The VLE, which complements this subject guide, has been designed to enhance your learning experience, providing additional support and a sense of community. It forms an important part of your study experience with the University of London and you should access it regularly.

The VLE provides a range of resources for EMFSS courses:

- **Electronic study materials**: All of the printed materials which you receive from the University of London are available to download, to give you flexibility in how and where you study.

- **Discussion forums**: An open space for you to discuss interests and seek support from your peers, working collaboratively to solve problems and discuss subject material. Some forums are moderated by an LSE academic.

- **Videos**: Recorded academic introductions to many subjects; interviews and debates with academics who have designed the courses and teach similar ones at LSE.

- **Recorded lectures**: For a few subjects, where appropriate, various teaching sessions of the course have been recorded and made available online via the VLE.

- **Audiovisual tutorials and solutions**: For some of the first year and larger later courses such as Introduction to Economics, Statistics, Mathematics and Principles of Banking and Accounting, audio-visual tutorials are available to help you work through key concepts and to show the standard expected in exams.

- **Self-testing activities**: Allowing you to test your own understanding of subject material.

- **Study skills**: Expert advice on getting started with your studies, preparing for examinations and developing your digital literacy skills.

Note: Students registered for Laws courses also receive access to the dedicated Laws VLE.

Some of these resources are available for certain courses only, but we are expanding our provision all the time and you should check the VLE regularly for updates.

**Making use of the Online Library**

The Online Library (http://onlinelibrary.london.ac.uk) contains a huge array of journal articles and other resources to help you read widely and extensively.
To access the majority of resources via the Online Library you will either need to use your University of London Student Portal login details, or you will be required to register and use an Athens login.

The easiest way to locate relevant content and journal articles in the Online Library is to use the Summon search engine.

If you are having trouble finding an article listed in a reading list, try removing any punctuation from the title, such as single quotation marks, question marks and colons.

For further advice, please use the online help pages (http://onlinelibrary.london.ac.uk/resources/summon) or contact the Online Library team: onlinelibrary@shl.london.ac.uk

1.7 Examination advice

Important: the information and advice given here are based on the examination structure used at the time this guide was written. Please note that subject guides may be used for several years. Because of this we strongly advise you to always check both the current Programme regulations for relevant information about the examination, and the VLE where you should be advised of any forthcoming changes. You should also carefully check the rubric/instructions on the paper you actually sit and follow those instructions.

1.7.1 Format of the examination

The examination is three hours long, and you are normally required to answer four questions from a choice of eight.

Remember, it is important to check the VLE for:

- up-to-date information on examination and assessment arrangements for this course
- where available, past examination papers and Examiners' commentaries for the course which give advice on how each question might best be answered.
Part 1: Introduction to the global business environment
Chapter 1: Perspectives on globalisation and international business

1.1 Introduction

Welcome to international management. Managing is essentially about getting work done through others. Historically, many have seen management as quite a ‘hands-off’ task, involving thinking, the scientific and systematic sifting of evidence, making decisions based on sufficient objective information, and then planning, controlling, coordinating and monitoring outcomes. All this is undoubtedly part of management. But from the 1970s, Mintzberg (2009) has demonstrated that managing is also, at the same time, an art involving vision and creative insights, a craft involving experience and practical learning and, ultimately, a practice aimed at getting effective results. In fact, study after study has supported Mintzberg’s views. It turns out that when you manage, typically you will experience unrelenting pace, brevity and variety of the activities you undertake and fragmentation and discontinuity in the job. You will need an orientation to action, will tend to favour informal and spoken forms of communication, and you will deal a lot with colleagues and associates, i.e. sideways as much as up and down the organisation’s hierarchy. And your soft skills in motivation, negotiation and persuasion will be as important as any formal control mechanisms you might have available.

In this course we explore management, but with the added complexity of moving management on to the world stage. Suddenly you will discover that what works in your own organisation, and in your own country, might not work as well, if at all, abroad. In this course you will learn about the factors that make managing internationally similar in many respects to managing in your home country, but very different in many other respects. In the first six chapters you will find out how the formal and informal institutions of the international community, regions and countries make the job of managing very much more sophisticated. In Chapters 7 to 10 you will learn how international managers deal with these contextual factors when they devise and implement strategies to compete, invest and operate in different regions and countries. And in Chapters 11 to 14 we will have a more detailed look at the international challenges facing managers responsible for devising organisational structure, global sourcing, information systems and human resources, and how they go about their tasks.

In this chapter we are going to start by looking at a major phenomenon that managers have to live with if operating internationally, that of globalisation. Globalisation can be defined as the shift towards a more integrated and interdependent world economy. In other words, the world is moving away from self-contained national economies, towards an interdependent, integrated global system. A major part of this is increased international trade and foreign direct investment. International trade occurs when a company exports goods or services to consumers in another country. Foreign direct investment (FDI) occurs when a company invests resources in business activities outside its home country. From a business perspective, you can think of globalisation in terms of the globalisation of markets and the globalisation of production. The globalisation of markets refers to the merging of historically distinct and separate national markets.
into one huge global marketplace. The globalisation of production refers to the sourcing of goods and services from locations around the globe to take advantage of national differences in the cost and quality of factors of production such as land, labour and capital.

What does all this mean for business? Have a look at Peng and Meyer (2011) Chapter 1 and the opening case concerning the Dell notebook and its global journey. Its components are sourced from over 30 countries around the world! What does all this mean for you and me? Consider my own day. I wake up in the United Kingdom in a bed made by Sweden's Ikea, get dressed in a shirt made in India and a pair of US Levis jeans that were produced in China. After putting on my Taiwanese-made trainers, and drinking an Italian-style cappuccino, I drive to work in my Japanese-made Honda that was manufactured in the UK. On the way to a client headquartered in the Netherlands, but with operations in the UK, I talked to my friend on a Nokia cell phone designed in Finland, about getting together later for Spanish-style tapas and Tiger beer from Singapore. As you can see, my day has already been filled with the effects of globalisation. But there are multiple other effects. As examples only, is my job safe? Are there new job prospects? Where is the next technological change going to come from? Is globalisation adversely affecting my environment?

This chapter introduces you to globalisation, the trends towards globalisation and its main drivers. We explore the major debates for and against globalisation, and whether companies wishing to operate internationally can work on the basis of the assumption that the world is flat, or something else. We look at the implications of globalisation for companies wanting to extend themselves further globally.

1.1.1 Aims of the chapter

The aims of this chapter are to:

• introduce the major attributes of globalisation the global economy
• identify the major trends and players in the global economy
• present the major debates around globalisation and its impacts, and the advantages and disadvantages from different stakeholder perspectives
• pinpoint the implications of globalisation for international and domestic businesses.

1.1.2 Learning outcomes

By the end of this chapter, and having completed the Essential reading and activities, you should be able to:

• define the major characteristics of globalisation
• assess the global economy and its broad trends
• explain the major trends in globalisation, and the major players in the globalisation process
• enter into the major globalisation debates and assess under what conditions and for whom globalisation can be considered an advantage or disadvantage
• describe the implications of globalisation for companies operating internationally.
1.1.3 Essential reading


1.1.4 Further reading


1.1.5 References cited


1.1.6 Synopsis of chapter content

Trends and drivers of globalisation, foundations of global trade and finance, overview and framework for understanding the global economy, the development of the multinational enterprise (MNE), debates on the nature and impacts of impacts of globalisation, and the implications for managing international business.

1.2 What is globalisation?

What is globalisation and what are the challenges it raises for business organisations worldwide? Some identify globalisation with the accelerated spread of communication and transportation technology. Others identify globalisation with the rising power of multinational enterprises (MNEs) and increased inequality in the world. Some experience it as increased competition for jobs, especially for low skilled workers. Others emphasise how globalisation is a force eliminating differences between distinctive cultures and identities, while still others argue this is exaggerated and the world is still defined by national boundaries, and others see the world moving rapidly towards a homogenous plain without national boundaries. Defining globalisation has big implications; how it is explained to the public influences how the idea is received.

Globalisation involves increasing amounts of cross-border trade, with traditional distances between nations lessening, due to advances in transportation and telecommunications technology. Globalisation does involve the rise of MNEs and has seen the globalising of markets and production, which has seen increased competition for jobs and between nations. Globalisation has also seen some erosion of differences among distinctive national cultures and identities, but, as we shall see below and in Chapter 7, the extent may be exaggerated. Companies that treat all markets the same invariably learn the limits of this approach.

Globalisation has also seen the development of international bodies to try to deal with all this increased interconnectedness. There are now
international governing bodies such as GATT (The General Agreement on Tariffs and Trade), which has been succeeded by the WTO (World Trade Organization), which hold the key to many economic decisions affecting the world and have power over nations akin to a political body or national government. These governing bodies symbolise the interconnectedness of the world just as the United Nations did after the end of the Second World War. The goal of the International Monetary Fund is to maintain order in the international monetary system. As we will see in later chapters, the World Bank promotes economic development by making loans to cash-strapped nations wishing to make significant infrastructure improvements like building dams or roads. These international organisations influence businesses and communities wishing to collaborate with other countries.

**Activity**


Decide for yourself:
1. What is a good definition of globalisation?
2. How would you define international business?

### 1.3 Trends towards globalisation

As Peng and Meyer (2011) Chapter 1 points out, globalisation is hardly new. People have been trading internationally for several thousands of years. However, the last 150 years have seen an intensification of globalisation, and what Jones (2004) depicts as two waves, arising in each case from a combination of long-term trends and pendulum swings.

**Activity**

Examine Figure 1.5 ‘Waves of globalisation’ in Peng and Meyer (2011) page 16. Also read Willcocks (2013) Section 1.3.

In the 1970s and 1980s globalisation as international trade was largely a matter for developed economies in the triad of North America, Western Europe and Japan. However, globalisation accelerated dramatically in the 1990s. Emerging economies joined much more in global trade, particularly the largest in terms of population, namely Brazil, Russia, India and China – the so-called BRIC countries. An emerging economy is one that has only recently established institutional frameworks that facilitate international trade and investment. Typically they have low- or middle-level incomes among their population and above average economic growth compared to other nations. In the 1990s world output grew by 23 per cent over the decade, global trade expanded by 80 per cent and the total flow of FDI increased fivefold.

Gross Domestic Product (GDP) is the sum of value added by resident companies, households and governments operating in an economy. In the first decade of the twenty-first century, world GDP cross-border trade and per capita GDP all grew to new, unprecedented levels. All this was before the 2008–09 global economic crisis with global output, trade and investment plummeting and unemployment rising. From mid-2009 there was renewed confidence after massive government intervention in developing economies, but economic recovery has been slow in developed economies, while some emerging economies have rebounded faster. Overall, the second wave shown in Peng and Meyer (2011) Figure 1.5 has become less steep from 2010–12 as globalisation has slowed down.
What has been driving globalisation? Two macro factors are important: first, the decline in trade and investment barriers since the Second World War, and second, technological change, specifically dramatic improvements in communication, information processing and transportation technologies. Hill (2010) suggests that four trends have been particularly important:

• **Changes in world output and world trade.** In the 1960s, the USA dominated the world economy and world trade picture. Today, this picture has changed. In 2008, the USA accounted for only about 20 per cent of world economic activity. Other developed countries saw their share of global economic activity decline over time as well. Developing nations saw the opposite trend – their share of world output is rising, and by 2020, it is expected that they will account for more than 60 per cent of world economic activity. Countries like China, Thailand and Indonesia have emerged as global economic players. Countries like the USA, the UK, Germany and Japan, which were among the first to industrialise, will continue to see their standings in world exports and world output slip, while developing nations like China, India, South Korea and Thailand see their economies and roles in global trade and investment increase.

• **Foreign direct investment.** In the 1960s, the USA accounted for over 66 per cent of worldwide foreign direct investment flows. Today, investments by developing nations are on the rise, while the stock, or total cumulative value, of foreign investments by rich industrial countries is falling. Developing nations like China have also become important destinations for foreign direct investment flows. The share of total stock of foreign direct investment by the world’s six most important sources – the USA, the UK, Japan, Germany, France, Netherlands and developing countries – has changed significantly from 1980 to 2007. In particular, the share of the USA has noticeably declined (from 38 per cent to 18 per cent), and the world's developing countries have increased from less than 1 per cent to 15 per cent. Increased growth in cross-border flows of foreign direct investment is very noticeable in the official figures, reaching an all-time high in 2007. One can also see the rising importance of developing nations as destinations for FDI. Chapter 4 deals with FDI in detail.

• **Types of companies.** The global economy has also shifted in terms of the types of companies that are involved. A multinational enterprise is any business that has productive activities in two or more countries. Since the 1960s, two important trends have emerged. First, an increase in the number of non-US multinationals. Multinational enterprises from France, Germany, Britain and Japan have become more important and there has been a notable decline in the role of US companies. Companies from developing countries such as China and South Korea have also emerged as important players. The second trend is the growth in the number of mini-multinationals. China’s Lenovo, for example, acquired IBM’s PC division in 2004, in an effort to become a global player in the PC industry, and moved its headquarters to the USA as part of its strategy. Traditionally, global markets have been the venue for large companies, but today, thanks to advances in technology like the internet, international sales can account for a significant share of revenues for small companies too.

• **Change in world order.** The collapse of Russian communism has brought about new opportunities in Eastern Europe, and China’s economic development and enormous population presents huge
opportunities for companies. Mexico and Latin America have also emerged both as new markets, and as production locations. And China and India, for example, are now home to a number of companies that either are or could become significant players in their global industries.

Activity
Read Peng and Meyer (2011) Chapter 1, pp.4–24 and think about the following questions.

1. What do Peng and Meyer mean when they refer to the 'institution-based' view and the 'resource-based' view?

2. What do you see as the significance of the global economic pyramid (see Peng and Meyer, 2011, Figure 1.6, p.19) for companies wanting to operate internationally?

1.4 The globalisation debates

What will the global economy look like in the twenty-first century? The world is moving towards a more global economic system but this interdependency creates new types of risk. Proponents of globalisation, such as Bhagwati (2007), focus on the benefits of globalisation. Supporters argue that globalisation means lower prices, more economic growth and more jobs. But critics worry that globalisation will cause job losses, damage the environment and create cultural imperialism. Four major areas of debate recur.

Jobs and income. Critics of globalisation worry that jobs are being lost to low-wage nations. They argue that falling trade barriers are allowing companies to move manufacturing jobs to countries where wage rates are low. Supporters, however, claim that free trade will prompt countries to specialise in what they can produce most efficiently, and to import everything else. They argue that the whole economy will be better off as a result. In other words, if you are in the USA and can buy an imported shirt that was made for cents in Honduras, you will have more money to spend on products the USA can produce efficiently like computers and software.

Labour policies and the environment. Critics fear that free trade encourages companies from advanced nations, where there are costly environmental standards, to move manufacturing facilities offshore to less developed countries with lax environmental and labour regulations. However, advocates of globalisation claim that environmental regulation and stricter labour standards go hand in hand with economic progress, so foreign direct investment actually encourages countries to raise their standards. Advocates of globalisation argue that by tying free trade agreements to the implementation of tougher environmental and labour laws, economic growth and globalisation can occur together with a decrease in environmental pollution.

Shifts in economic power. Critics of globalisation worry that economic power is shifting away from national governments and towards supranational organisations like the WTO (see Chapter 6) and the European Union (EU) (see Chapter 5). However, globalisation's supporters argue that the power of these organisations is limited to that granted by their members. They also point out that the organisations are designed to promote the collective interests of members and they will not gain support for policies that do not achieve this goal.

Wealth distribution. Critics worry that the gap between rich and poor is growing and that the benefits of globalisation have not been shared
equally. Supporters of globalisation concede the gap between rich and poor has got wider, but also contend that it has more to do with the policies countries have followed than with globalisation. For example, many countries have chosen to pursue totalitarian regimes, or have failed to contain population growth, and many countries have huge debts that are hindering economic growth.

1.4.1 Does distance still matter?

Yet another debate exists over the degree of globalisation, its impacts and its implications for international business. Friedman (2007) believes globalisation is accelerating and is flattening the world so that every nation will eventually be part of the global marketplace and production process. Dicken (2010) calls this a 'hyper-globalist' view. Friedman takes a technological stance on globalisation, believing it to be shaped considerably by technological advances, cheap computer access and the easy assimilation and transportation of knowledge over the internet. Before computer access was a worldwide phenomenon geographical distance played a big impact on how companies conducted business. Moreover, outsourcing would be harder as there would be no reliable, efficient way of collaborating with other departments in the same office or in a different country.

Friedman argues that 10 'flatteners' have shaped globalisation and caused increased homogeneity in the world. By calling the world 'flat' he does not mean literally flat, of course. He means that geography, differences and distance increasingly cease to matter as a result of the influence of these 10 'flatteners'. These 'flatteners' include the fall of the Berlin Wall representing economic liberalisation; the development of internet protocols, workflow and open source software; the increased use of outsourcing and offshoring; the development of global supply chains; the increased use of specialised companies to carry out internal functions; the development of search engines and, latterly, of wireless, digital, mobile, personal and virtual technologies. From this perspective, technological capacity and connectedness define the parameters of globalisation and this is only set to continue as the age of the personal technology relationship is gaining momentum, where people not content with established information-sharing bodies take matters into their own hands with blogs, review sites and the establishing of their own media channels.

Although for 'hyper-globalists' like Friedman globalisation means free cooperation and connection with nations all over the world, to Ghemawat (2001) and Dicken (2010) flattening creates a general misconception about the extent of globalisation. In his influential article 'Distance still matters', Ghemawat argues that companies consistently 'overestimate the attractiveness of foreign markets'. He argues that the true amount of trade and investment between countries is influenced largely by geographical and cultural differences. He cites that countries 5,000 miles apart only perform 20 per cent of the trade they would otherwise do if they were 1,000 miles apart, and furthermore trade is 10 times more likely to take place if a country was a former colony of another, which, Ghemawat argues, significantly lowers the cultural barriers to trade. Arguing against Friedman's flattening argument, Ghemawat elaborates that global communications and technologies have been argued to be 'shrinking the world, running it into a small and relatively homogenous place'. However, he points out that this is not only an incorrect assumption but a dangerous one.

The cultural difference between countries is still wide and complex, and although outsourcing and foreign direct investment have recently grown between nations, it is evident, as we shall see in Chapter 3, that cultural
differences still prove challenging. In support of Ghemawat’s argument, Dicken (2010) argues that quantitative and aggregative evidence suggests that the world economy was ‘more open and more integrated in the half century prior to the First World War than it is today’. Ghemawat also supports this empirically based analysis, stating that cultural differences in religious beliefs, language, social norms and behaviours have a huge impact in the risk involved in trading and the likelihood of succeeding. Therefore, according to these theorists, globalisation cannot be said to be flattening the world.

Dicken explains that part of the problem with defining globalisation is understanding that aggregative and quantitative analysis, though valid, are not the only story we should take on board when looking at the world economy today. The economy today, he goes on to suggest, constitutes a deep and complex integration that cannot be captured in the statistics of trade and foreign direct investment. Instead, globalisation is ‘a supercomplex series of multi-centric, multi-scalar, multi-temporal, multi-form and multi-causal processes’. This explanation, in contrast to Friedman’s linear model of technological progress, is more dynamic and circulatory in design.

In ‘Distance still matters’, Ghemawat complements this view by suggesting that companies often overestimate the ease with which their business can move abroad. The cultural, administrative and geographical distance between nations presents a fundamental challenge to companies facing the globalisation of the world economy today. As just one example, Coca-Cola had problems in the Peruvian market when they attempted to replace Inca Kola, the national beverage, with their own US-branded Cola. The Peruvian people held mass demonstrations against Coca-Cola until their Inca Kola was returned to the shelves. Being sensitive to national differences is not just a consideration; in international business it may well be an imperative to survival – something we explore in detail in Chapters 2, 3 and 7.

Activity


1. How ‘flat’ do you think the world is? Who is right?
2. If an Australian multinational retailer of men and women’s clothing chose to operate in your country, what difficulties do you think they would encounter?

1.5 What does globalisation mean for companies?

All this means that managing an international business, or any company that engages in international trade or investment, will be very different from managing a domestic business. In particular, companies operating internationally will find that countries and cultures differ – a subject we will explore in much more detail in Chapters 2 and 3. It will emerge from those chapters that the range of problems faced by managers is greater and more complex, not least because government intervention in markets creates limitations for companies, as do the ways in which the global trading system operates and the existence of international institutions as we shall discover in Chapters 4, 5 and 6. At the same time, companies can work with the forces for globalisation and improve their global performance. Such forces include:
• **Low barriers to trade and investment.** These mean that companies can see the world as their market, rather than a single country. Low trade and investment barriers also mean that companies can locate production facilities in the optimal location, wherever in the world that might be. Production and sales now take place in multiple markets, creating interdependency between countries for goods and services.

• **Technological change.** Major advances in communication, information processing and transportation technology have made what had been possibilities into tangible realities. The cost of global communication has fallen, for example, because advances in telecommunications and information processing help companies to coordinate and control global organisations at a fraction of what these costs might have been even a decade ago. The microprocessor that facilitates high-power, low-cost computing is perhaps the most important of these developments. Dell, for example, takes advantage of these innovations to control its globally dispersed production system. When a customer submits an order via the company’s website, it is immediately transmitted to the suppliers of the various components, wherever they are located in the world. Suppliers have real-time access to Dell’s order flows and can then adjust their production accordingly. Dell uses inexpensive airfreight to transport its products to meet demand as needed. The company maintains a customer service operation in India where English-speaking personnel handle calls from the USA. Indeed, the internet has made it possible for even small companies to play a role in the global economy. Yet, less than 20 years ago, this technology did not even exist. Growth in internet usage has gone from fewer than 1 million users in 1990 to more than 2 billion users in 2012.

• **Transportation improvements.** Improvements in transportation such as containerisation and the development of super freighters have also facilitated the growth of globalisation. The time it takes people and products to get from one place to another has shrunk, as has the cost. For example, Ecuador has been able to capitalise on falling transportation costs to become a global supplier of roses. As an experiment, surprise yourself and analyse where the goods you buy and use on a daily basis come from.

There is evidence that there have been huge global shifts in the ways in which we do business but that overall the strongest companies are international but are also, as we shall see in Chapter 7, strategically sensitive to localising their products or service when operating in different markets. For example, Google found this to be a winning combination in their expansion into China. Here, despite an initial backlash, Google pursued a local strategy for their Chinese market using a Chinese name for their search engine and customising their web page to fit the tastes of Chinese internet users, who tend to spend longer on a given page and read the left-hand side of the screen first. However, global linkages and interdependencies and working in foreign markets also mean global risks. As a symbol of the risks of globalisation for a company, Google also ran into subsequent problems with the Chinese government on a number of issues.
1.6 Key concepts

The key concepts in this chapter are:

- globalisation
- multinational enterprises (MNEs)
- foreign direct investment (FDI)
- World Trade Organization (WTO)
- International Monetary Fund (IMF)
- United Nations (UN)
- developed and emerging economies
- ‘the world is flat’
- globalisation trends
- globalisation debates
- distance still matters.

1.7 Reminder of your learning outcomes

Having completed this chapter, and the Essential reading and activities, you should be able to:

- define the major characteristics of globalisation
- assess the global economy and its broad trends
- explain the major trends in globalisation, and the major players in the globalisation process
- enter into the major globalisation debates and assess under what conditions and for whom globalisation can be considered an advantage or disadvantage
- describe the implications of globalisation for companies operating internationally.

1.8 Test your knowledge and understanding

Read Peng and Meyer (2011) Chapter 1, closing case ‘GE innovates at the base of the pyramid’.

1. What are the similarities and differences between traditional and reverse innovation?

2. Why is GE so interested in reverse innovation?

3. What are the main concerns that prevent western MNEs from aggressively investing in emerging economies? What are the costs of not doing so?

4. Why is a leading US multinational like GE afraid of emerging multinationals from emerging economies?

1.9 Sample examination questions

1. What is globalisation?

2. For an individual country, what are the likely advantages and drawbacks that come with globalisation?

3. How can an international business use globalisation trends to its advantage? What problems can globalisation trends create for an international business? Work with these arguments to establish competitive advantage internationally.
Chapter 2: Political, economic and legal environments

2.1 Introduction

You already know that the political, economic and legal systems of countries differ. But you may not know what these differences are, and how and why these differences are important to companies that do business in foreign markets. In practice, managers working abroad should have a thorough understanding of a country’s formal institutions before entering that country. In this chapter, we are going to explore these institutions and related systems, known collectively as the political economy of a country, and what they mean for businesses operating internationally. In doing so, we will introduce something called ‘an institution-based perspective’. As we shall see, political, economic and legal institutions establish the formal ‘rules of the game’ for operating in a particular country. The key functions of these institutions are to reduce uncertainty, reduce transaction costs and constrain opportunism. We will look at the equally, and sometimes more, important informal rules in Chapter 3.

In this chapter we will look at the varieties of political systems, ranging from totalitarianism through to different types of democracy. We will also examine systemic differences among economies, ranging from pure market economies and liberal market economies through to coordinated market economies. We will also explore the basic differences between legal systems. Finally, we will consider how these political, economic and legal institutions influence the economic development of a country and their implications for international business managers.

2.1.1 Aims of the chapter

The aims of this chapter are to:

• identify the nature of formal institutions in different countries, and the ways in which these reduce uncertainty
• introduce the major types of political, economic and legal systems, and point out the similarities and differences in these across countries
• develop knowledge of how these attributes and differences across countries impact and constrain how businesses operate internationally
• provide a platform for debating the role of national formal institutions in international business and how they can be managed.

2.1.2 Learning outcomes

By the end of this chapter, and having completed the Essential reading and activities, you should be able to:

• define the concept of institutions and delineate their key role in reducing uncertainty
• assess the basic differences among political systems and their influence on international business
• discuss the systemic differences among economies and the related challenges for international business
• describe the basic differences between legal systems in the world
• engage in and assess leading debates on political, economic and legal institutions and international business.

2.1.3 Essential reading


2.1.4 Further reading


2.1.5 References cited


2.1.6 Synopsis of chapter content

The institution-based view of international business; overview of political, economic and legal systems; how political economic and legal trends develop in different countries.

2.2 An institution-based view of international business

Peng and Meyer (2011) are great proponents of the institution-based view of international business. You can read more about this in Peng, Wang and Jiang (2008). They argue that, essentially, a country’s institutions establish the formal and informal rules for operating in that country. Companies operating internationally need to know these because these ‘rules’ differ between countries, and because they shape greatly what can be achieved and what is not possible in a country. Institutions can be formal or informal.

Look at Peng and Meyer (2011) Table 2.1, p.39. Here you will see that formal institutions consist of laws, regulations and rules. Informal institutions consist of norms, cultures and ethics. In this chapter we focus on the formal institutional framework – laws, regulations and rules – of a country that governs the behaviour of individuals and companies. In Peng and Meyer (2011) Table 2.1, the normative pillar refers to the norms, values, beliefs and actions of others that influence the behaviour of companies and individuals. The cognitive pillar refers to the taken-for-granted values and beliefs, which we will look at in Chapter 3.

What do institutions do? Essentially their key role is to reduce uncertainty by limiting the range of acceptable actions. Institutions have developed over time because the potential adverse consequences of uncertainty can be devastating. For example, if you were trying to do business in the Middle East in 2012, say in Egypt, Syria, Israel, Qatar, Libya, imagine the immense difficulties of just understanding the business context, let alone deciding what to do. Uncertainty increases transaction costs, a term made highly popular by Oliver Williamson (1985). Transaction costs are the costs associated with carrying out an economic transaction or, in short,
the costs of doing business – for example, search, negotiation, getting to contract, monitoring supplier performance. Transaction costs will increase if others behave opportunistically, defined by Williamson as ‘self-interest seeking with guile’. Institutional frameworks can reduce the potential for such opportunistic behaviour. This is important for international business, because if transaction costs become prohibitively high in a country, people may choose not to undertake trade in that country at all.

Institutions are evolving all the time, and international business managers need to keep up with these changes. For example, in the last decade and more, China, Poland, Russia and Vietnam have been moving from central planning to market competition, though each in different ways, and at different speeds. These are often called transition economies. Institutional transition can be defined as fundamental and comprehensive changes to the formal and informal rules of the game that affect organisations as players.

In summary, Peng and Meyer (2011) argue, convincingly, that, for international businesses, institutions matter. They suggest that at the heart of an institution-based view there are two core propositions. These are shown in Peng and Meyer (2011) Table 2.2 (p.41). Look at this table and read the examples of these propositions at work.

Activity

Now read Peng and Meyer (2011) Chapter 2, pp.36–41, noting the opening case on South Africa:

1. Imagine you are a company from your own country. What do you see as the main institutional – political, economic and legal – challenges of doing business in South Africa?
2. What are the sources of transaction costs in doing business with South Africa?
3. How important do you think informal institutions are in doing business in South Africa?

2.3 Political systems

A political system represents the rule of the game on how a country is governed politically. You can think of political systems as having two dimensions: first, the degree to which they emphasise collectivism as opposed to individualism, and second, the degree to which they are totalitarian or democratic.

Collectivism versus individualism

Collectivism refers to a system that stresses the primacy of collective goals over individual goals. In other words, in a collectivistic society, the needs of the society as a whole are generally viewed as being more important than individual freedoms. In modern times collectivism has been equated with socialism, and state ownership of the basic means of production, distribution and exchange. During the late 1970s, communism, with strong command economies, was a dominant force in the world. You might think of the former Soviet Union, for example, and its eastern European neighbours like Poland, Czechoslovakia and Hungary. Think also of China, Cambodia and Vietnam, and of Angola and Mozambique, Cuba and Nicaragua. By 2000, the world was a very different place than it had been in the 1970s. The Soviet Union, for example, had been replaced by 15 republics that were structured as democracies. China, though it still limited political freedom, was moving away from its strict communist
ideology. Today, only a few fringe states like Cuba and North Korea still practise a strong brand of communism. Social democracy, which believes in a mixed economy of central planning, state and private enterprises has also been fluctuating. For example, countries like the United Kingdom and France have placed less emphasis on state-ownership of the means of production and have seen moves towards privatisation (i.e. selling state-owned enterprises to the private sector).

Individualism has been championed by economists such as Adam Smith, Milton Friedman and Friedrich von Hayek. Individualism is based on two key concepts: first, that individual freedom and self-expression are guaranteed, and second, that people are allowed to pursue their own self-interest in order to achieve the best overall good for society. For international companies there is a debate about how important individualism and the related idea of free market economics are for creating a favourable business environment, and about who gains from applying these concepts in international trading environments.

**Totalitarianism**

You can think of totalitarianism and democracy as being at opposite ends of a political dimension with, at one end, totalitarianism, where one person or political party exercises absolute control over all spheres of life, and opposing political parties are forbidden; and at the other end democracy, a political system in which government is by the people, exercised either directly or through elected individuals. While we generally think of democracy as going hand-in-hand with individualism, and totalitarianism as being associated with collectivism, grey areas do exist. For example, China is not a western-style democracy, but has adopted free market policies that tend to be associated with individualism. The world has seen four major forms of totalitarianism:

- **Communist totalitarianism** advocates achieving socialism through totalitarian dictatorship. While this form of totalitarianism is declining worldwide, countries like Vietnam, Cuba and North Korea still follow the philosophy.

- **Theocratic totalitarianism** is where political power is monopolised by a party, group or individual that governs according to religious principles. This type of system exists in countries such as Saudi Arabia and Iran. Both countries are greatly influenced by the principles of Islam, and both countries restrict political and religious freedom.

- **Tribal totalitarianism** is where a political party that represents the interests of a particular tribe monopolises power. This type of system has occurred, for example, in some African nations like Zimbabwe and Tanzania.

- **Right-wing totalitarianism** may allow individual economic freedom, but individual political freedom is restricted to avoid forms of socialism. A nation's military often backs this type of system. This type of system has been declining, but existed in Germany and Italy during the 1930s and 1940s.

**Democracy**

A pure democracy is based on the belief that people should be directly involved in decision making. The most common form of democracy today, however, is representative democracy, where elected representatives vote on behalf of constituents.
Some of the reputed characteristics of democracies include freedom of expression, free media, regular elections, a fair court system and free access to state information. The political system is governed by institutions. The rules are usually laid down in a constitution, determining things such as how elections are organised, how votes are translated into representation in a parliament and how much power the elected officials and representatives have. There are notable variations in representation methods, including:

- **Proportional representation versus first-past-the-post.** Countries such as Germany and Denmark have systems whereby all votes are added up and seats are allocated to political parties in proportion to the number of votes they gained. Countries like India, the USA and the UK have a first-past-the-post system where each constituency elects one representative based on who in the election wins the most votes.

- **Direct versus indirect elections of government.** Some countries have direct elections for certain posts (e.g. citizens of France and the USA directly elect their presidents with executive power to appoint ministers). In most countries citizens elect representatives who then, on the citizens' behalf, elect and monitor government and ministers.

- **Representative versus direct democracy.** In most countries citizens elect representatives to act on their behalf.

- **Centralisation of power.** There are variations between countries in the degree of power held by central, regional and local governments. For example, in federated countries like Australia and the USA, states wield quite a lot of power. In the UK, central government has devolved quite a lot of functions to the Scottish, Welsh and Northern Irish assemblies.

Political systems matter for international business because they:

- set the rules and whose interests are served by the rules
- determine whether and how businesses can influence legislative processes through lobbying (mostly legal) or corruption (usually illegal)
- influence how frequently, and in what ways, the rules of the game for business change. This can be a major source of political risk since political changes may negatively affect domestic and foreign businesses.

**Activity**


1. Look at the In Focus 2.1 description of elections around the globe. How do elections and political processes work in your country?

2. How do elections and political processes work in a country with which your country trades a great deal?

### 2.4 Economic systems

An economic system refers to the rules by which a country is governed economically. Broadly, there are three types of economic system:

- **Market economy.** Here goods and services are privately owned and production quantities are determined by supply and demand. In a market economy, governments encourage free and fair competition
and discourage monopolies. Note that there have been very few pure market economies. In 2001, Hong Kong had the highest degree of economic freedom, but there was still some noticeable government intervention in the economy. However, the 2008–09 financial crisis and its aftermath saw increased government intervention in many countries across the world.

- **Command economy.** Here the goods and services that a country produces, the quantity in which they are produced and the price at which they are sold, are planned by the government. Businesses are state owned and the government allocates resources for the good of society as a whole. An example of a command economy was the former Soviet Union and, in 2013, North Korea.

- **Mixed economy.** Here elements of both a market economy and a command economy are present. Governments often take control of industries that are considered vital to national interest. Examples include France, the UK and Sweden.

- In the twenty-first century most countries are more or less market economies – they organise themselves by market forces but also have varying degrees of non-market coordination. The ‘varieties of capitalism’ view embodies this reality.

**Activity**

To understand the varieties of capitalism view, look at the diagram in Peng and Meyer (2011) Figure 2.1 (p.46) ‘Varieties of capitalism’.

The varieties of capitalism view (Hall and Soskice, 2001) suggests that, due to history, culture, resources and other factors, countries can vary enormously in how they combine market and non-market mechanisms to coordinate economic activity. Moreover, these economies will be constantly changing in the modern dynamic global environment. The view suggests two main types of economy (see Peng and Meyer (2011) Figure 2.1):

- **Coordinated market.** This operates through a system of coordinating by market signals together with a variety of other means, as, for example, in Italy, the Netherlands and Japan. Such economies may well have more employment protection and less ability to raise capital through the stock market. In Germany, for example, employees have representatives on corporate boards (unlike in the UK) and government is much more directly involved in vocational training. In Asia, many countries have embraced liberal market principles but also have a strong state providing direction and investment supporting the economic development path (e.g. South Korea, Singapore).

- **Liberal market.** This operates through a system of coordination primarily through market signals. Hall and Soskice (2001) suggest the UK, the USA, Canada and Australia were examples of this in 2000, though it is important not to understate the extent of government involvement in economic development even in these states.

**Activity**


1. Describe your own country’s economy. Is it a market, command or mixed economy?
2. What is the degree of coordination and liberalisation in your economy?
3. Has your country changed in terms of type of economy in the last 10 years? How?
4. Do you foresee further changes in the next five years?
2.5 Legal systems

A legal system represents the formal rules that regulate behaviour, along with the processes by which the laws of a country are enforced and through which redress for grievances is obtained. The importance for international managers is that a country’s laws regulate business practice, define the manner in which business transactions are to be executed and set down the rights and obligations of those involved in business transactions. The legal system impacts on the attractiveness of a country as a business investment or a potential target market (see Chapter 4). A country’s legal system is influenced by its political system. So, countries that are ‘collectivistic totalitarian’ states tend to restrict private enterprise, while ‘individualistic market’ economies support private enterprise and consumer rights.

Activity

Look at Peng and Meyer (2011) Table 2.4 (p.51).

There are three broad types of legal system shown in Peng and Meyer (2011) Table 2.4. Note, however, that many legal systems are influenced by multiple legal traditions:

- **Common law** is based on tradition, precedent and custom. Judges look at how previous cases have been treated to decide how to treat current cases. Then, as new precedents are made, laws can be amended if necessary. Common law is English in origin but has stretched to many English-influenced countries (in Africa, Asia, South Africa, and also Canada and the USA). It is based on statutes, customs and court decisions. Judges are arbiters and juries are decision makers. The implications for business are greater freedom to design contracts and codes of practice; detailed contracts are needed to fill in for gaps in the legal framework; more legal disputes involving much use of lawyers; a greater legal burden may favour the more powerful companies.

- **Civil law** is based on a detailed set of laws organised into codes. This type of system, which is practised in more than 80 countries including Germany, Japan and Russia, is less adversarial than common law because under civil law, judges only have the power to apply the existing law, not interpret the law. Here law is codified in books of law, and judges lead the proceedings including questioning and deciding. For businesses the implications tend to be relatively short contracts and codes of practice, and more consumer and employee protection available under the law. Businesses often complain about the bureaucracy of civil law, but civil law also often gives greater legal certainty.

- **Religious law** is based on religious teachings. Today, Islamic law is the most widely practised theocratic law system in the world and is practiced in countries including Iran, Libya, Saudi Arabia and Morocco. In practice, Islamic jurors and scholars are struggling to apply the foundations of Islamic law to the modern world, and many Muslim countries today are actually practising Islamic law combined with common law or civil law.

Why it is important for international companies to be familiar with the legal system in the countries in which they operate? One key reason is because each system approaches the enforcement of contracts in a
different way. So, suppose you come from a common law state, and you have signed an agreement with a company operating under a civil law system. Which law should apply? To deal with this type of scenario, about 70 countries have signed the United Nations Convention on Contracts for the International Sale of Goods (CIGS), which established a uniform set of rules governing certain aspects of the making and performance of everyday contracts between sellers and buyers who have their places of business in different nations.

### 2.5.1 Issues for international businesses

Legal systems are also important for dealing with several other essential issues for international businesses:

- **Property rights.** Property rights are the legal rights over the use to which a resource is put and over the use of any income that may be derived from that resource. In some countries, even though there are laws protecting property, the laws are not consistently enforced. Property rights can be violated through private actions and through public actions. Private violations like theft, piracy or blackmail are done by individuals. When public officials like politicians and bureaucrats violate property rights, they might use legal mechanisms such as levying excessive taxes, as in Venezuela in the 2000s, or requiring special expensive licences, or even simply taking assets into state control.

- **Intellectual property issues.** Intellectual property rights are rights associated with the ownership of intellectual property – which can include anything from computer software or a chemical formula for a new drug to a screenplay or a music score. Intellectual property can be protected in three ways:
  - A patent gives the inventor of a new product or process exclusive rights to manufacture, use or sell the invention.
  - A copyright is the exclusive right of authors, composers, playwrights, artists and publishers to publish and dispose of their work as they see fit.
  - A trademark is a design or name that may be officially registered, that allow merchants or manufacturers to designate or differentiate their products.

Protection of intellectual property rights varies by country. China and Thailand are currently among the world’s biggest violators of intellectual property rights. In Latin America, about 68 per cent of all software is pirated, and in China some studies estimate that 86 per cent of software is pirated. Nearly 200 countries have signed the Paris Convention for the Protection of Industrial Property to protect intellectual property rights, and are part of the World Property Organization, but enforcement of property regulations is still lax in many countries. What can you do if your intellectual property is stolen? You can lobby your government to take action. You can also file your own lawsuit. For example, Starbucks was successful in suing a Chinese company that opened stores that were almost replicas of the traditional Starbucks store.

- **Product safety and product liability.** Product safety laws set certain standards to which a product must adhere and product liability involves holding a company and its officers responsible when a product causes injury, death or damage. These vary greatly across countries. This often leads to an ethical dilemma for companies. What should a company do if the standards in a foreign market are lower
than the standards at home? Should they comply with home standards even if this puts them at a competitive disadvantage?

- **Corporate governance.** This involves the rules by which shareholders and other interested parties control corporate decision makers. Variations across countries are closely related to differences in economic and legal systems. Generally, common law systems have evolved in ways that provide strong protection for financial investors (i.e. shareholders). In civil law countries, for example Germany and Denmark, the law tends to offer less protection for shareholders and more rights to other stakeholders in the company – for example, non-managerial employees who tend to be represented on corporate supervisory boards.

**Activity**


1. Why in the NaturEner case (pp.49–50) does a Spanish company have problems doing business in North America?

2. Why do legal systems and international agreements have such a poor record against the violation of intellectual property rights (see In Focus 2.3, p.53)?

3. How would you describe the legal system of your own country?

### 2.6 Country development: political, economic and legal issues

The political, economic and legal environments of a country can have a significant impact on its economic development, and on its attractiveness as a potential investment location or target market. Economic development levels can be measured using gross national income per person, or GNI. But GNI measures can be misleading because they do not take into account cost of living differences. So, we adjust these numbers by purchasing power. Using purchasing power parity (PPP), we can adjust the numbers to reflect how far your money actually goes in a particular country. What does this mean for companies? Well, looking at a PPP-adjusted GNI for India in 2007, we would conclude that the average Indian could only consume about 6 per cent of the goods and services consumed by the average US citizen. Should US businesses have discounted India as a potential market then? No, because if we look a little deeper we would find that the country has an emerging middle class of about 100 million people that represents a tremendous opportunity for foreign companies.

Are there other ways to measure economic development? Sen (1999) argues that, rather than simply focusing on material output measures like GNI per capita, we should consider the capabilities and opportunities people enjoy when measuring economic development. Sen believes that economic progress includes things like removing impediments to freedom, such as tyranny, poverty and the neglect of public facilities, and a democratisation of political communities so that citizens have a voice in decision making. So, for example, Sen argues that providing basic healthcare and education is essential for economic growth. The UN has incorporated Sen’s ideas in its Human Development Index, or HDI, which measures the quality of life in different countries. HDI is based on life expectancy at birth, educational attainment and whether average incomes in a country are sufficient to meet the basic needs of life in that country.
Why do some countries succeed in economic development while others fail? Some argue that investment and technological progress explain capital accumulation, higher productivity and thus increasing economic success. Many policy makers and scholars argue that innovation and entrepreneurship are the engines of long-run economic growth, and that innovation and entrepreneurship require some form of market economy. In other words, new products and business processes can increase the productivity of labour and capital. Similarly, innovation and entrepreneurship probably require strong property rights. If the innovations by, say, Microsoft or Samsung were not given protection, there would have been little incentive for the companies to continue to develop new software and technological products.

Others argue that human capital is the key to prosperity, so developing counties must invest in higher education. Others relate success to market-friendly, macro-economic policies by government, including low inflation, stable exchange rates, low trade barriers and low government budget deficits. Peng and Meyer (2011) line up with the argument of North (2005) and see political, economic and legal institutions as the basic determinants of a country's national economic performance because these influence incentives and the costs of doing business:

- Institutions ensure that companies are able to make gains from trade.
- Lack of strong, formal market-supporting institutions force companies to trade on a much more informal basis, incurring political, legal and economic risks in conditions of instability and over-dependence on informal relationships.
- Emerging formal market-supporting institutions support foreign businesses moving into complicated long-distance trade with a country because they can see reasons for specialisation and growing in size, and making long-term commitments to international trade there.
- If property rights are protected, this will fuel innovation, entrepreneurship, more economic growth and increased inward investment.

**Activity**

Read Willcocks (2013) Chapter 2, Sections 2.1 to 2.7 and make additional notes on examples and points.

Read Peng and Meyer (2011) Chapter 2, pp.52–61 and think about the following questions.

1. Looking at the closing case on Russia, what would be your advice to the government on property right reforms?
2. If you were managing the funds of a Russian oligarch, where would you invest?
3. If you were the CEO of a major multinational retailer in your own country, or one like IKEA or Wal-Mart, would you look to set up your first major store in Russia? Give reasons for your answer.
2.7 **Key concepts**

The key concepts in this chapter are:

- institution-based view
- collectivism versus individualism
- market, command and mixed economies
- coordinated market
- liberal market
- types of totalitarianism
- proportional representation
- representative democracy
- civil law, common law and religious law.

2.8 **Reminder of your learning outcomes**

Having completed this chapter, and the Essential reading and activities, you should be able to:

- define the concept of institutions and delineate their key role in reducing uncertainty
- assess the basic differences among political systems and their influence on international business
- discuss the systemic differences among economies and the related challenges for international business
- describe the basic differences between legal systems in the world
- engage in and assess leading debates on political, economic and legal institutions and international business.

2.9 **Test your knowledge and understanding**

1. How do you think a country might make the shift from a centrally planned to a more market-based economy?

2. You are looking to sell goods to another country (pick one you know something about). What are the costs of doing business in this foreign market? Given the costs of doing business in a foreign market, is it worth it?

3. What do you think are the factors that explain the degree of development and success experienced by your own country over the last 10 years? What were the roles of political, economic and legal institutions?

2.10 **Sample examination questions**

1. a. What are the main political systems an international business faces when operating in another country?
   
   b. What are the main economic systems?
   
   c. What are the main legal systems?
   
   d. Describe the issues these differences can create for an international firm.
   
   e. How can these challenges be dealt with? Use examples and cases to illustrate your points.
Chapter 3: Informal institutions: cultural, social and ethical challenges

3.1 Introduction

If you ever visit a foreign country, you will probably notice some differences in how people dress, the food they eat or their choice of transportation. Perhaps a particular religion influences how society works, or a different language is spoken. All of these things are manifestations of culture. Just as you would adapt for differences when away from home, when doing business in foreign countries, companies need to adapt as well.

In this chapter we look at the informal institutions companies need to take into account when operating internationally. In particular we will focus on the differences between countries in culture, religion, language, ethics and approaches to corporate social responsibility. Culture is a system of values and norms that are shared among a group of people and that, when taken together, constitute a design for living. Values are abstract ideas about what a group believes is good, right and desirable, and norms are the social rules and guidelines that prescribe appropriate behaviour in particular situations. Long-standing cultural differences still influence how business is being done. Also, keep in mind that culture is dynamic, in other words it is always changing.

We will discover in this chapter that managers and companies unfamiliar with foreign languages and religious traditions may end up making mistakes that harm their business. We also explore different approaches to ethics in international business, and how variations on ethics across countries can create ethical dilemmas, as can a range of differences about dealing with such issues as the environment, labour, human rights and corruption. We also explore companies’ different corporate social responsibility (CSR) strategies, and whether CSR is vital to or a diversion from what international businesses need to be focusing on.

3.1.1 Aims of the chapter

The aims of this chapter are to:

• explain the concept of culture and provide means by which different cultures can be analysed and described
• identify the different type of language and religion across the globe, and their relevance to understanding cultures and behaviours
• pinpoint the importance of ethics in international business, and how what is considered ethical varies across countries, and religions
• introduce possible managerial responses to informal (and formal) institutions, with particular reference to corporate social responsibility activities.

3.1.2 Learning outcomes

By the end of this chapter, and having completed the Essential reading and activities, you should be able to:

• define what culture is and articulate two of its manifestations, namely language and religion
• discuss how cultures systematically differ from each other
• assess how language competences shape intercultural interactions
• explain how religions shape cultures
• describe the importance of ethics
• articulate corporate social responsibility challenges faced by companies operating in the global economy
• assess how institutions influence companies’ corporate social responsibility activities
• participate in leading debates about culture and social responsibility
• draw implications for management action.

3.1.3 Essential reading

3.1.4 Further reading

3.1.5 References cited

3.1.6 Synopsis of chapter content
Culture – definitions and role in international business; language differences and impacts; religion and ethics on the world stage; corporate social responsibility (CSR) in international business.

3.2 Cultures and international business
Informal institutions come from socially transmitted information and are part of the heritage that we call culture. They tell individuals in a society what behaviours are considered right and proper, and what would be unacceptable. Typically, cultures have no clearly defined origin, but have evolved over time. Those within a society tend to perceive their own culture as ‘natural, rational and morally right’. This self-centred mentality is known as ethnocentrism. Culture can be seen as the collective programming of the mind that develops over time which distinguishes the members of one group or category of people from another. Though we talk about the French culture and the Japanese culture, culture is not necessarily divided by national boundaries. Some countries like Switzerland even have multiple distinct cultures. Similarly, some cultures transcend national boundaries. For example, you might think of how the values promoted by Islam influence many countries.
Culture has been described as ‘the way things are done round here’ and also as the shared norms, values and assumptions of a group, organisation or society that translate into distinctive behaviours. The social rules that govern people’s actions towards one another are called norms, which you can think of as the routine conventions of everyday life like dress codes, social manners and accepted codes of conduct.

What determines culture? The values and norms of a culture evolve over time and are a function of a number of factors at work in a society including religion, political and economic philosophies, education, language and social structure. How can we understand differences in culture? Peng and Meyer (2011) distinguish between three approaches – the context approach, the cluster approach and the dimensions approach.

3.2.1 The context approach
Context is the underlying background upon which interaction takes place. In low-context cultures (such as in North American and western European countries), communication is usually taken at face value without much reliance on unspoken context. In other words, yes means yes. In contrast, in high-context cultures (such as Arab and Asian countries), communication relies a lot on the underlying, unspoken context, which is as important as the words used. For example, ‘yes’ does not necessarily mean ‘yes, I agree’, it might mean ‘yes, I hear you’. Failure to understand context and differences in interaction style can lead to misunderstandings in international business. According to this theory, Chinese, Korean, Japanese and Arab cultures are high context, while German, Canadian and Swiss, for example, are low context. This looks a bit simplistic, however. Critics point out that the context approach may exaggerate the lack of context in so-called ‘low context’ approaches, and that all cultures, national, business or otherwise, as products of history and tradition, have important unspoken aspects which are as important as the words used. Also the context approach only looks at one dimension, unlike the dimensions approach detailed below.

3.2.2 The cluster approach
A cluster in this case is a group of countries that share similar cultures. Peng and Meyer (2011) point to three theories of clusters (see Table 3.1, p.71). As can be seen, Ronen and Shenkar (1985) identify eight clusters, while the Globe study (House et al., 2004) proposes 10, of which five are similar to the Ronen and Shenkar study. Huntingdon (1996) proposes eight ‘civilisations’. The clusters are a useful way of looking at things, because we need to understand that in international business people will feel more comfortable doing business with countries and businesses from the same cluster. However, the approach tells us little about differences between countries within a cluster.

3.2.3 The dimensions approach
The most extensive studies exploring this have been done by Hofstede (1997). He and his colleagues identify five dimensions of culture: power distance, individualism versus collectivism, masculinity versus femininity, uncertainty avoidance and long-term orientation. These are well described in Peng and Meyer (2011) Chapter 3.

Note that Hofstede’s studies record only relative culture differences between countries. Look at Peng and Meyer (2011) Table 3.2, pp.73–74 to see these relative differences. Hofstede’s work has been criticised. While Hofstede’s original study gave us many important insights into cultural
differences, his study was flawed in that he made the assumption that there is a one-to-one relationship between culture and the nation-state. In addition, the research was culturally bound since it was conducted only by Europeans and North Americans, and the study may have been biased since it took place within a single company, IBM. It is important for you to read about and note the strengths and limitations of Hofstede’s work. Hofstede provides a good starting point for a cultural analysis that needs to be more fine-grained if it is to influence actual management practice.

What are the implications of all of this for managers? It is vital for international businesses to develop cross-cultural literacy. To be successful, you have to be able to conform and adapt to the value system and norms of the host country. One way you can gain knowledge of the local culture is to hire local citizens. Developing a cadre of cosmopolitan managers who have been exposed to different cultures can also be helpful. It is important to avoid being ethnocentric, believing that your ethnic group or culture is superior to that of others. A second reason for companies to be aware of cultural differences is the link between culture and competitive advantage. The value systems and norms of a country influence the costs of doing business, which of course then affect the competitive advantage of the company. A society’s class structure affects the relationship between management and labour, for example – look at Japan’s strong worker loyalty system, where lifetime employment guarantees affect the success of Japanese companies. Similarly, it has been suggested that a more individualistic culture promotes entrepreneurial activities as compared to a culture that emphasises collective behaviour. These differences provide companies with insight as to which countries are most likely to produce competitors, and which countries will be the best for investing or selling (see also Chapter 12 on the subject of location attractiveness).

Activity

Read Willcocks (2013) Chapters 1 and 3, in particular Sections 3.1 and 3.2, which have additional information on culture, points and cases.

1. Make notes on the criticisms of the context, cluster and dimensions approaches.
2. Make notes on the Trompenaars (1993) approach described in Section 3.2. Define the dimensions of the approach and criticisms of the approach.


1. Look at your own country and plot your own culture according to Hofstede’s five dimensions.
2. How useful is this for understanding behaviour at work in your country?
3. If you were doing business with a US company, what cultural differences would you need to take into account compared to doing business with a company from mainland China?

3.3 Languages

Language influences culture. It is how we communicate with each other both in the spoken and unspoken form and it is also how we perceive the world. Some countries have more than one language and distinct culture. Canada, for example, has both an English-speaking and a French-speaking area – both with their own cultures. Belgium is divided into Flemish and French speakers, and four different languages are spoken in Switzerland. Chinese is the mother tongue of the largest number of native speakers, though English is the most widely spoken language in the world.
Chapter 3: Informal institutions: cultural, social and ethical challenges

Activity

Look at Peng and Meyer (2011) Figure 3.2 (p.77).

Peng and Meyer (2011) Figure 3.2 show that Chinese is the single most spoken language in the world. 20 per cent of the global population speak Chinese, 6 per cent English, 5 per cent Hindi, 5 per cent Spanish, 4 per cent Arabic and 4 per cent Russian. However, 56 per cent of the global population still speak other languages, often in addition to these six major languages.

Many multinationals have adopted English as the official corporate language, to enable knowledge sharing and communication across borders, not least with customers, suppliers and fellow employees. But note that, even though English is the main global business language, using English as a language in a business meeting can still create problems. People from different cultures may understand the same words differently.

Why is unspoken language important? Think for a moment about how you stand when you are talking with another person. People in North America and western Europe usually stand about an arm's length away. But in Latin America, people tend to stand much closer together. Now, what happens in a business meeting between someone from Brazil and someone from Canada, for example? The Brazilian might try to stand at their customary distance causing the Canadian to take a step backwards because their personal space has been invaded. The Canadian may be annoyed at the Brazilian for standing so close, and the Brazilian may interpret their response as aloofness. The meeting is already off to a bad start. Similarly, consider the circle you might make with your thumb and forefinger. In the USA, you have signalled a positive response, but if you make the same gesture in Greece, you have just insulted someone.

Activity


1. What do you see as the value of being a multi-lingual employee? See the Kone Elevator case (In Focus 3.2) and In Focus 3.3.

2. You face a meeting with a business person from Mumbai in India. What would you see as the likely communication challenges? How would you deal with these?

3.4 Religion and ethics

Religion is another important determinant of culture, especially in countries where a single religion is dominant. Religion is the systems of shared beliefs and rituals that are concerned with the realm of the sacred. Religions with the greatest number of followers today are Christianity (1.7 billion), Islam (1 billion), Hinduism (750 million) and Buddhism (350 million). You might also include Confucianism with these. While not strictly a religion, Confucianism influences behaviour and shapes culture in many parts of Asia. Closely related to religion are ethical systems, or sets of moral principles or values that guide and shape behaviour. So, you might think of Christian ethics or Islamic ethics.

Most followers of Christianity live in Europe, the Americas or other countries settled by Europeans. Christians are divided into Roman Catholics, those who belong to the Orthodox church and Protestants. Muslims are found in more than 35 countries, particularly in the Middle East. Islam is an all-embracing way of life – prayers take place five times a day, women are expected to dress in a certain manner, and pork and
alcohol are forbidden. How does Islam affect business? The Koran, which is the sacred book for Islam like the Bible is for Christianity, supports free enterprises and legitimate profits, but advocates using profits in a righteous, socially beneficial manner. The central tenets of Hinduism, which is mainly based in India, are spiritual growth and development. Many Hindus believe that the way to achieve nirvana is through material and physical self-denial.

Hinduism creates interesting challenges for companies. For example, because the religion emphasises spiritual rather than individual achievement, the drive for entrepreneurial behaviour so common among Protestants, for example, is not present. So a devout Hindu may not see promotion or additional responsibilities as being desirable. Buddhism’s followers are located mainly in central and southeast Asia, China, Korea and Japan. Buddhism stresses spiritual achievement and the afterlife over involvement in this world. As with Hinduism, there is a lack of emphasis on entrepreneurial behaviour.

Confucianism is practised mainly in China and teaches the importance of attaining personal salvation through right action. Moral and ethical conduct is important, as is loyalty. What do the principles of Confucianism mean for business? The key principles of the ideology – loyalty, reciprocal obligations and honesty – could translate into making the costs of doing business lower.

A knowledge of religions is crucial even for non-religious managers. Religious beliefs and activities affect business through religious festivals, daily and weekly routines that vary across religions (e.g. prayer times, sacred days, fasts), and activities and objects with symbolic values. For example, in India cows are holy in Hindu religion and may not be disturbed or eaten. Some objects or practices are taboo or banned – for example, Muslims are not supposed to eat pork. Recall the international furore over the Danish newspaper which published cartoons involving the Muslim prophet Mohammed (see Peng and Meyer (2011) Chapter 3, p.66). Religious differences, more than any other differences, tend to raise emotions – and thus are challenging to handle for businesses. Showing respect for other religions and associated values will help you avoid conflict and create a basis for doing business. An individual’s religion may also help shape his/her attitude towards work and entrepreneurship.

### 3.4.1 Ethics

Ethics refers to the principles of right and wrong, standards and norms of conduct governing individual and company behaviour. Ethics are not only an important part of informal institutions but are also deeply reflected in formal laws and regulations. Business ethics are the accepted principles of right or wrong governing the conduct of business people. An ethical strategy is a course of action that does not violate these principles.

Managing ethics overseas is challenging because what is ethical in one country may be unethical elsewhere. How should you deal with ethical dilemmas that arise when operating internationally? The Friedman doctrine argues that the only responsibility of business is to increase profits. Friedman (1970) claimed that as long as the company stayed within the letter of the law, ethics did not enter the equation. So, in other words, he would argue that it is not the responsibility of a company to take on social expenditures beyond what is mandated by law, and what is required to run a business efficiently. What Hill (2010) calls the naïve immoralist approach argues that if a manager of a multinational company sees that companies from other countries are not following
ethical norms in a host country, that manager should ignore the norms as well. Peng and Meyer (2011) suggest three approaches.

- **Ethical relativism** follows the saying ‘When in Rome, do as the Romans do’.
- **Ethical imperialism** refers to the absolute belief that ‘There is only one set of ethics and we have it’.
- Companies often run into problems adopting either of these two approaches. Therefore Donaldson (1996) suggests a ‘middle of the road’ approach in international business by observing three principles when overseas – respect for human dignity and human rights, respect for local traditions, and respect for institutional context. In practice these principles may clash in specific circumstances, leaving the business manager to behave as diplomatically as he/she can in the prevailing situation.

Ethics provides a useful bridge between culture, language, religion and the subject of a major way forward – corporate social responsibility – which we will now look at.

**Activity**


1. In Focus 3.4 deals with the OECD anti-corruption convention. What does this do and what are the difficulties in implementing it?
2. What is cultural intelligence? What five types of cultural intelligence have been identified?
3. What do you see as the ethical rules of thumb for a company whose operations are impacted by the informal institutions of a foreign country?

**3.5 Corporate social responsibility in international business**

How can companies deal with the ethical dilemmas that arise when operating internationally? A major approach is corporate social responsibility (CSR), defined as the consideration of, and response to, issues beyond the narrow economic, technical and legal requirements of the company in order to accomplish social benefits along with the traditional economic gains the company seeks.

A stakeholder view of the company sees a business as responsible not just to its shareholders for its performance, but also to a much wider constituency. There are primary stakeholder groups on whom the company directly relies for its continuous survival and prosperity – managers, employees, customers, shareholders, governments. There are also secondary stakeholder groups who do not engage in transactions with the company, but who influence or are affected by the company, though they are not essential for its survival (e.g. Global Exchange in the Starbucks case). As a result of rising global concerns and the stakeholder view, companies increasingly develop CSR **triple bottom line strategies** that take into account their economic, social and environmental performance. One example of taking CSR action is Starbucks, an example which you can read about as the opening case in Peng and Meyer (2011) Chapter 10, pp.296–97. International businesses are faced with at least four major CSR concerns:

- The **environment** is currently a high profile topic, especially the irreversible damage that man-made pollution is causing. A key concern
is *sustainability*, defined as the ability to meet the needs of the present without compromising the ability of future generations to meet their needs. Because many countries are establishing strong environmental regulations to try to limit further damage, companies are having to adopt new, often costly measures to abide by the laws. For example, new regulations may be forcing your company to take costly steps to stay within the law. Should you shift your production to another country where the laws do not exist, or are only loosely enforced?

**Activity**

Look at Peng and Meyer (2011) Figure 3.3. It suggests reasons for and against a multinational enterprise (MNE) lowering its standards. Read also Willcocks (2013) Chapter 3, Section 3.5 on this subject.

1. Make notes on the pressures on MNEs to lower their standards on the environment.
2. Make notes on the pressures on MNEs to raise their standards on the environment.

- **Employment practices** frequently present ethical dilemmas. Suppose work conditions in a host country are inferior to those in the home country. Which standards should be applied – the home country standards or the host country standards? Nike found itself in the midst of a huge controversy in the mid-1990s when it was reported that the working conditions at some of its sub-contractors were poor. While neither the sub-contractor nor Nike were actually breaking the law, there was strong reason to suspect that workers were being exploited. Nike was forced by public pressure to establish a code of conduct for all of its sub-contractors, and implement a monitoring system to ensure that the code was followed. The pressure to lower conditions in foreign operations is particularly strong with ‘footloose plants’ that are labour intensive and can easily relocate when local regulations get tighter. Another problem area is where an MNE buys products or components from foreign companies. MNEs like Adidas (see Peng and Meyer, 2011, In Focus 10.4) sometimes introduce standards of engagement on their suppliers. These are written policies and standards for corporate conduct and ethics. But what happens if suppliers fail to meet standards or provide misleading evidence?

- **Human rights.** Human rights and freedoms are not respected in all countries. Think about the apartheid system that denied basic political rights to black people in South Africa, for example. Should companies do business in countries with repressive regimes? Some people argue that the presence of multinational companies actually helps bring change to these countries. Others, however, argue that some countries like Myanmar, which has one of the worst human rights records in the world, are so brutally repressive that no investment can be justified.

- **Corruption.** Is it necessary to be ethical when dealing with corrupt government or individuals? This is something companies have to consider. At what point does ‘gift giving’ become bribery, for example? From a government perspective, bribery is invariably not allowed. The Organization for Cooperation and Development (OECD) passed an anti-bribery measure in 1997, which obligates member states to make the bribery of foreign public officials a criminal offence. Despite laws like these, bribery continues to be a common practice for some companies. In fact, some economists believe that in certain cases speed payments, or payments made to speed up approval for business investments, can be justified, for example, if they enhance public
welfare by creating jobs. Others argue, however, that corruption can become ingrained as a way of doing business, and hard to stop if it is part of a country’s way of getting things done.

3.5.1 Institutions and CSR strategies

What are the moral obligations of companies operating internationally? You can guess that the formal and informal institutions operating in a country greatly influence the types of CSR strategies companies can adopt, and the levels of success experienced. In liberal market economies like the USA and the UK, companies have a high discretion over their activities. So far as they undertake CSR, it will be done as explicit corporate activities undertaken voluntarily as policies, programmes and strategies, with the extent of these activities dependent on the expectations of different stakeholders of the company. In more coordinated market economies, for example in Germany and Scandinavia, much more implicit CSR takes place, with CSR being part of the fabric of the legal, political, and social and cultural institutions, and indeed may not only be morally demanded but legally demanded, e.g. in Germany health care benefits must be paid for all those employed for more than 20 days a month. Note however that, among developed countries in particular, there has been some convergence towards more CSR regulation.

Do companies have a responsibility to take into account the social consequences of their actions when they make business decisions? Should companies always choose the path that has both good economic and good social consequences? You might answer yes – companies have a social responsibility simply because it is the right way to operate. Many people believe that companies need to give something back to the societies that have made their success possible. Some companies, however, do not share this view. Peng and Meyer (2011) Chapter 10 suggest companies adopt different responses to ethical challenges and give worked examples in the text which you will need to understand.

Activity

Refer to Peng and Meyer (2011) Chapter 3, Figure 3.4. Read also Willcocks (2013) Chapter 3, Section 3.6.

1. Describe the four strategies an international business can adopt on CSR.
2. Assess the advantages and disadvantages of each strategy.

Sometimes, it can very difficult for companies to decide how to behave in some situations. Managers will be influenced by their personal ethics and cultural perspective, which may or may not be appropriate in a given situation. However, there are several things that managers can do to be sure that ethical issues are considered when decisions are made:

- Companies can hire and promote people with well-grounded personal ethics.
- Companies can build an organisational culture that places a high value on ethical behaviour. To develop this, companies need to articulate values that place a strong emphasis on ethical behaviour. Some firms do this by establishing a formal code of ethics. Once a code has been developed, leaders need to emphasise it and act on it. Companies can encourage employees to adopt the code by offering incentives and rewards to those employees who behave in an ethical manner.
- Companies can make sure that leaders articulate the rhetoric of ethical behaviour and act in a manner consistent with that rhetoric.
• Managers can develop moral courage. Companies can strengthen the moral courage of employees by committing themselves not to retaliate against employees who exercise moral courage, say no to superiors or otherwise complain about unethical actions.
• Companies can put decision-making processes in place that require people to consider the ethical dimension of business decisions.

Activity
Read Willcocks (2013) Chapter 3, Sections 3.3 to 3.7 and make revision notes from the cases and points.
Read Peng and Meyer (2011) Chapter 10 and answer the following questions.
1. What is the case for and against MNEs adopting CSR policies on the environment? (see In Focus 10.2, the case of Dow chemical, and pp.301–04).
2. What CSR policies have Adidas adopted (see In Focus 10.4)? How can they be criticised?

3.6 Key concepts
The key concepts in this chapter are:
• culture
• context, cluster and dimension approaches to culture
• collectivism and individualism
• main types of religion
• ethics
• ethical dilemmas
• five corporate attitudes to ethics
• corporate social responsibility (CSR)
• reactive, defensive, accommodative and proactive strategies
• triple bottom line.

3.7 Reminder of your learning outcomes
Having completed this chapter, and the Essential reading and activities, you should be able to:
• define what culture is and articulate two of its manifestations, namely language and religion
• discuss how cultures systematically differ from each other
• assess how language competences shape intercultural interactions
• explain how religions shape cultures
• describe the importance of ethics
• articulate corporate social responsibility challenges faced by companies operating in the global economy
• assess how institutions influence companies' corporate social responsibility activities
• participate in leading debates about culture and social responsibility
• draw implications for management action.
3.8 Test your knowledge and understanding


1. If you were invited to a party in Saudi Arabia, how would you behave? What would you tell an Indian colleague who is a vegetarian?
2. Do you think it is necessary or appropriate to join in the drinking when being invited to a business party in China?
3. How would you treat your Saudi Arabian or Chinese colleagues at your own company official party?

Read Peng and Meyer (2011) Chapter 10, the closing case – on naming your school.

1. In your country, do you think universities should actively solicit donations from wealthy individuals and business? What about conflicts of interest?
2. What should businesses ask in exchange for handing over large amounts of cash to universities? Should shareholders support such donations? Why? Why not?
3. How should a university react when a donor's reputation is damaged due to activities unrelated to the university?

3.9 Sample examination questions

1. Define culture.
2. Describe and assess the context, cluster and dimensions approaches to international culture.
3. What challenges and risks do cultural issues present to an international business and how can these be managed?
Notes